Square, Inc. (SQ)

$104.22 (As of 06/22/20)

Price Target (6-12 Months): **$110.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 11/25/19) Prior Recommendation: Outperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:D
	Value: F | Growth: B | Momentum: F	

Summary

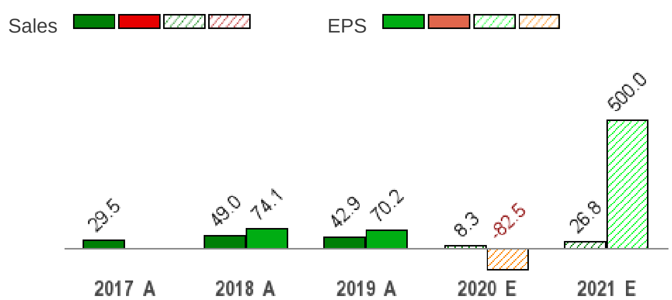
Square is gaining on growing gross payments volume. Its seller ecosystem, which helps in strengthening relationship with sellers, is contributing well to the payment volume growth. Further, robust Square Terminal, Instant Deposits, Cash Card, Square Register and Square Capital are major positives. Also, solid adoption of Cash App in the bitcoin space remains a tailwind. Strong momentum across peer-to-peer volumes, Cash Card spend, Cash Card orders, direct deposit transacting active customers and bitcoin volumes are likely to aid Square. The stock has outperformed its industry on a year-to-date basis. However, rising product development expenses and costs related to Cash Card issuances are risks. Further, accumulating reserves for transaction and loan losses owing to the expected impact from coronavirus pandemic on losses in future are overhangs.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$106.36 - $32.33**
20 Day Average Volume (sh)	**11,930,644**
Market Cap	**$45.8 B**
YTD Price Change	**66.6%**
Beta	**2.67**
Dividend / Div Yld	**$0.00 / 0.0%**
Industry	**Internet - Software**
Zacks Industry Rank	**Top 16% (40 out of 253)**
Last EPS Surprise	**-115.4%**
Last Sales Surprise	**5.8%**
EPS F1 Est- 4 week change	**-18.4%**
Expected Report Date	**08/06/2020**
Earnings ESP	**44.1%**
P/E TTM	**155.6**
P/E F1	**744.4**
PEG F1	**18.8**
P/S TTM	**8.9**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	1,513 E	1,523 E	1,631 E	1,734 E	6,473 E
2020	1,381 A	1,111 E	1,229 E	1,385 E	5,106 E
2019	959 A	1,174 A	1,266 A	1,313 A	4,714 A

EPS Estimates

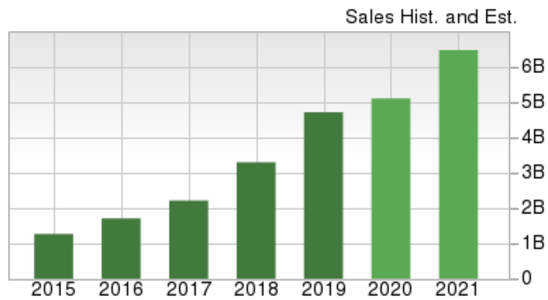
	Q1	Q2	Q3	Q4	Annual*
2021	$0.18 E	$0.20 E	$0.25 E	$0.29 E	$0.84 E
2020	-$0.02 A	-$0.11 E	$0.07 E	$0.15 E	$0.14 E
2019	$0.11 A	$0.21 A	$0.25 A	$0.23 A	$0.80 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 06/22/2020. The reports text is as of 06/23/2020.

Overview

Headquartered in San Francisco, CA, Square, Inc. was incorporated in 2015. The company offers financial and marketing services through its comprehensive commerce ecosystem that helps sellers to start, run and grow their businesses.



We combine sophisticated software with affordable hardware to provide sellers powerful payment and point-of-sale solutions. The company provides payment and point-of-sale (POS) services, which include hardware and software to accept payments, streamline operations and analyze business information.

Square's payments and POS services include In-Person Payments, Online Payments, Square Cash, Square Register, Square Analytics, Square Appointments and Square App Marketplace. The company's financial services include Square Capital and Square Payroll.

Square reported total revenues of $4.7 billion in 2019. The company earns revenues from transactions, subscription and services, hardware and bitcoin.

Transaction-based revenues (65.4% of total revenues in 2019) include transaction fees that sellers pay for managed payment solutions and services.

Subscription and services-based revenues (21.9%) include fees that sellers pay for a range of paid services-based products including Square Appointments, Gift Cards, Customer Engagement, Employee Management, Payroll, Instant Deposit, and other subscription and services-based products offered through Square Marketplace. A significant portion of the revenues comes from Square Capital that provides loans to pre-qualified sellers and Caviar, Square's food ordering service.

Hardware revenues (1.8%) are generated from sales of contactless readers, chip card readers and third-party peripherals which include cash drawers, receipt printers and barcode scanners. Square's hardware portfolio is comprised of Square Stand, Magstripe reader, Square Register and Square Terminal, and chip readers.

Bitcoin revenues (10.9%) are derived from total sales of bitcoin to customers. Cash App users can buy and sell bitcoins.

Geographically, the United States contributed almost 94.9% of revenues, while the rest came from International markets.

The company had approximately 3,835 employees worldwide as of Dec 31, 2019.

Reasons To Buy:

Square's comprehensive commerce ecosystem, accelerated business growth and entry into bitcoin space remain major positives.

- Square differentiates itself by offering a **comprehensive commerce ecosystem** enabling sellers to combine software, hardware and payments services from several vendors. The company's managed payment solutions allow sellers to accept payment through a range of media such as magnetic stripe (a swipe), Near Field Communication (NFC), EMV (Europay, MasterCard, and Visa), online through Square Invoices, Square Virtual Terminal, or the seller's website. Square's powerful point-of-sale software and services help sellers manage locations, orders, inventory, employees, and payroll. It helps sellers grow their sales with customers; and gain access to business loans. The Square Capital service offers loans to sellers on the basis of their payment processing history. Caviar, the company's food ordering service, helps restaurants gain access to new customers and enhance sales without additional overhead. A technology focused approach has enabled the company to develop products and services that are unified, fast, self-serve, and reliable and we expect this to continue in the coming years. We believe the company's strong efforts toward expansion of its payment solutions portfolio will continue to drive its top-line growth and aid momentum in the growing market for online payment solutions.

- Square's rate of **growth has been impressive** since it started operations eight years back. The company serves millions of sellers across various industries such as food, retail and services, and geographies including the U.S., Japan, Australia and Canada. It processed $106.2 billion of Gross Payment Volume (GPV) in 2019. The company has been doing well with larger and midmarket sellers. In first-quarter 2020, larger sellers contributed 52% to total GPV. The company's robust product portfolio is the key catalyst behind its improving GPV. The newly launched Square Reader SDK is a major positive. Additionally, API Platforms, Build with Square, Virtual Terminal, Instant Deposit and especially Square for Restaurants will continue to drive the GPV growth further.

- The company is deeply focused on integration and automation. On the integration front, Square aims to make its services more cohesive. It focuses on integration with the customer directory to give sellers an advanced client base. It also helps to build customer profiles and provides purchasing history directly from the point of sale. On the automation front, Square is trying to make its services more self-serve. It focuses on machine learning to automate internal as well as customer-facing experiences.

- Square's **entry into bitcoin market** with CashApp product, is contributing well to the company's quarterly results. Further, Square's expanding global presence will continue to benefit its top-line growth. The intoduction of CashApp and Instant Deposit in U.K. bodes well for the company's market position and it will continue to generate revenues.

- Square has a strong balance sheet. As of Mar 31, 2020, the company's net cash amounted to $723.3 million compared with $600.7 million as of Dec 31, 2019. Further, debt-to-total capital was 49.3% as of Mar 31, 2020 which increased from 35.4% as of Dec 31, 2019. However, given the strong liquidity position this is not a concern. Additionally, Square entered into a new revolving credit agreement with certain lenders in May 2020, which now provides a $500 million senior unsecured revolving credit facility maturing in May 2023.

Reasons To Sell:

- Growth will continue to depend on the company's ability to differentiate. Square is **vulnerable to intense competition and changing technology, industry standards and seller and buyer needs**. Competition is tough as the likes of PayPal are encroaching on its turf. Also, increasing competition from Shopify remains a headwind. These call for frequent changes in product and service offerings, which in turn require heavy investments, putting pressure on its earning capacity.

Square is vulnerable to intense competition and changing technology, industry standards and seller and buyer needs.

- The nature of its business makes Square vulnerable to **foreign exchange risk**. Apart from the U.S., the company operates in Canada, Australia and Japan and derives a significant part of its sales and earnings from there. Thus, appreciation or depreciation of the U.S. dollar versus foreign currencies could impact the company's results.

- Moreover, the company is trading at premium in terms of Price/Book (P/B). Square currently has a trailing 12-month P/B ratio of 22.99. This level compares unfavorably with what the industry witnessed in the last year. Additionally, the ratio is nearing the high end of the valuation range in this period. Consequently, the valuation looks slightly stretched from P/B perspective.

Last Earnings Report

Square Reports Loss in Q1

Quarter Ending	03/2020
Report Date	May 06, 2020
Sales Surprise	5.84%
EPS Surprise	-115.38%
Quarterly EPS	-0.02
Annual EPS (TTM)	0.67

Square reported first-quarter 2020 adjusted loss of 2 cents per share, which compares unfavorably with the Zacks Consensus Estimate of earnings of 13 cents per share. Notably, the company reported earnings of 11 cents and 23 cents in the year-ago quarter and prior quarter, respectively.

Accumulating reserves for transaction and loan losses owing to the expected impact from coronavirus pandemic on losses in future resulted in loss during the reported quarter.

Net revenues of $1.38 billion surpassed the Zacks Consensus Estimate by 5.8%. Further, the figure came ahead of the revised guided range of $1.30-$1.34 billion. The top line also improved 44% from the year-ago quarter and 5.1% sequentially.

The top line was driven by Seller ecosystem that contributed $853 million to net revenues, up 16% year over year. Further, robust performance of Cash App, which generated $528 million of net revenues, up 197% year over year, was a major positive. Furthermore, strengthening momentum across Bitcoin and strong adoption of Cash Card contributed to the results.

Additionally, continued acceleration in gross payment volume (GPV) aided the results.

Notably, the company completed the divestiture of Caviar to DoorDash at the end of October 2019. Caviar had been underperforming and consequently its sale remains a major positive.

Excluding Caviar, net revenues would have exhibited growth of 51% on a year-over-year basis.

Square has refrained from providing guidance for the ongoing quarter and the full year 2020. This can be attributed to the uncertainties related to COVID-19, which are expected to act as headwinds during the second quarter.

The company has put a temporary stop on subscription billings and waived subscription fees on software for sellers. This is likely to hurt subscription revenues in the second quarter.

Nevertheless, growing adoption of contactless payment mode remains positive. Further, seller GPV from card-not-present transactions is expected to gain steam.

Additionally, growing momentum across peer-to-peer volumes, Cash Card spend, Cash Card orders, direct deposit transacting active customers and bitcoin volumes are likely to sustain revenues generated by Cash App.

Gross Payment Volume

GPV in the first quarter amounted to $25.7 billion missing the Zacks Consensus Estimate of $26.7 billion. Notably, the figure improved 14% year over year on the back of the company's continued momentum across the larger sellers.

Square defines larger sellers as those that make more than $125,000 of annualized GPV and mid-market sellers as those with annualized revenues of more than $500,000.

GPV from larger sellers contributed 52% to total GPV. This can be attributed to Square's robust product portfolio and comprehensive ecosystem that aided it in attracting new sellers to its platform while retaining the existing ones.

Notably, the company witnessed 29% year-over-year growth in GPV during the January 2020 to February 2020 time period. However, the growth started slowing down since mid-March due to the rapidly spreading COVID-19 that impacted the seller business negatively.

Seller GPV declined 49% on a year-over-year basis in the last week of the first quarter.

Nevertheless, strong performance of Square Online Store owing to coronavirus-induced growing transition rate of sellers to online commerce from in-person sales mode drove GPV growth. Further, solid GPV generated from eGift Cards remained a positive.

Top-Line Details

Transaction (54.9% of net revenues): The company generated transaction revenues of $758.1 million, up 15.4% year over year. Strong payment volume contribution from existing and new sellers during the first two months of the reported quarter drove the category's top line. The company witnessed softness in transaction revenues during last two weeks of the first quarter owing to coronavirus pandemic.

Subscription and services (21.4% of revenues): The company generated $296.2 million revenues from this category, surging 34.9% from the year-ago quarter. This improvement can be attributed to the strong performance by Cash App, which contributed $222 million to the category's top line. Further, solid momentum across seller subscription and services products remained positive. Additionally, Square Capital, which facilitated 75,000 loans worth $548 million, up 8% from the year-ago quarter, contributed to the results. However, performance of Square Capital was also impacted by COVID-19.

Hardware (1.5% of revenues): Square generated revenues of $20.7 million from this business, up 13.5% year over year. The category's top line was primarily driven by robust Square Terminal. However, COVID-19 hurt the hardware unit sales.

Bitcoin (22.2% of revenues): The company generated revenues of $306.1 million from this category, up a whopping 367.1% on a year-over-year basis. Square continued to benefit in the bitcoin space driven by growing adoption of Cash App. Notably, without bitcoin revenues, Cash App revenues would have come in at $222 million. The company witnessed growth in the transacting active bitcoin customer base owing to fall in bitcoin prices.

Operating Details

Per management, gross profit grew 36% from the year-ago quarter to $538.5 million. As a percentage of net revenues, the figure came in 38.9%, contracting 240 basis points (bps) year over year. While Transaction, Subscription and services and Bitcoin generated profit, Hardware category reported loss during the reported quarter.

Further, coronavirus pandemic remained a woe.

Adjusted EBITDA as a percentage of net revenues was 0.7%, contracting from 6.4% in the year-ago quarter.

Operating expenses came in $628.8 million, surging 50.1% from prior-year quarter.

Product development expenses were $194.9 million, up 26% year over year, primarily owing to growing engineering, data science and design personnel costs.

General and administrative expenses were $129.5 million, up 27% from prior-year quarter. This can primarily be attributed to finance, legal and support personnel costs.

Further, sales and marketing costs were $194.5 million, up 45% year over year, due to increase in Cash App peer-to-peer payment transfer and Cash Card issuances.

Balance Sheet

As of Mar 31, 2020, cash and cash equivalents balance was $1.96 billion, up from $1.05 billion as of Dec 31, 2019.

Short-term investments were $521.8 million in the reported quarter, down from $492.5 million in the previous quarter.

Long-term debt was $1.8 million, increasing from $938.8 million in previous quarter.

Recent News

On **Jun 15, 2020**, Square revealed Square Capital is gaining strong traction among the small businesses on the back of Paycheck Protection Program (PPP). Notably, Square Capital has facilitated PPP loans worth more than $820 million as of Jun 10 since Apr 29.

On **Mar 18, 2020**, Square received conditional approval to operate a bank from the Federal Deposit Insurance Corporation (FDIC) Board. Following this approval, the company is aiming to launch Square Financial Services as a bank by 2021. Square Financial Services will be headquartered in Salt Lake City, UT and operate as a direct subsidiary of Square.

Valuation

Square shares are up 68.7% in the year-to-date period and 45.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are up 49.2% and 10.7% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are up 32.3% and 23.4%, respectively.

The S&P 500 index is down 3.1% in the year-to-date period but up 5.8% in the past year.

The stock is currently trading at 7.95X forward 12-month sales, which compares to 8.58X for the Zacks sub-industry, 3.91X for the Zacks sector and 3.5X for the S&P 500 index.

Over the past three years, the stock has traded as high as 10.2X and as low as 2.66X, with a 3-year median of 5.97X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $110 price target reflects 8.39X forward 12-month sales.

The table below shows summary valuation data for SQ

Valuation Multiples - SQ

		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	7.95	8.58	3.91	3.5
	3-Year High	10.2	8.58	3.91	3.5
	3-Year Low	2.66	4.87	2.62	2.76
	3-Year Median	5.97	5.73	3.21	3.16
P/B TTM	Current	25.29	10.07	5.76	4.26
	3-Year High	37.25	10.07	5.76	4.56
	3-Year Low	9.61	4.27	3.59	3.03
	3-Year Median	22.79	6.38	4.6	3.93
EV/Sales TTM	Current	8.83	9.95	4.44	3.05
	3-Year High	14.79	9.95	4.44	3.46
	3-Year Low	3.39	4.54	3.05	2.24
	3-Year Median	7.54	6.35	3.81	3.01

As of 06/22/2020

Industry Analysis **Zacks Industry Rank:** Top 16% (40 out of 253)

Top Peers

Company (Ticker)	Rec	Rank
Automatic Data Processing, Inc. **(ADP)**	Neutral	3
Alphabet Inc. **(GOOGL)**	Neutral	3
MoneyGram International Inc. **(MGI)**	Neutral	5
PayPal Holdings, Inc. **(PYPL)**	Neutral	3
Shopify Inc. **(SHOP)**	Neutral	3
Wix.com Ltd. **(WIX)**	Neutral	3
The Western Union Company **(WU)**	Neutral	3
Intuit Inc. **(INTU)**	Underperform	5

Industry Comparison Industry: Internet - Software

Industry Peers

	SQ	X Industry	S&P 500	INTU	PYPL	SHOP
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	5	3	3
VGM Score	D	-	-	B	C	F
Market Cap	45.79 B	730.33 M	21.83 B	76.70 B	199.88 B	106.10 B
# of Analysts	12	5	14	8	15	24
Dividend Yield	0.00%	0.00%	1.93%	0.72%	0.00%	0.00%
Value Score	F	-	-	F	D	F
Cash/Price	0.06	0.10	0.07	0.05	0.05	0.02
EV/EBITDA	95.55	-0.58	12.63	34.31	50.55	-1,726.51
PEG Ratio	19.04	3.68	2.90	3.06	3.44	52.18
Price/Book (P/B)	25.29	6.11	3.01	16.18	12.47	34.88
Price/Cash Flow (P/CF)	280.33	25.07	11.47	45.04	52.29	NA
P/E (F1)	755.50	59.85	21.30	40.53	51.20	1,772.69
Price/Sales (P/S)	8.92	4.52	2.29	11.19	10.95	61.41
Earnings Yield	0.13%	0.30%	4.42%	2.47%	1.96%	0.06%
Debt/Equity	1.17	0.14	0.77	0.01	0.50	0.04
Cash Flow ($/share)	0.37	-0.00	7.01	6.53	3.26	-0.60
Growth Score	B	-	-	B	B	F
Hist. EPS Growth (3-5 yrs)	NA%	16.26%	10.84%	23.70%	20.03%	NA
Proj. EPS Growth (F1/F0)	-82.71%	-4.04%	-10.80%	7.50%	7.27%	70.14%
Curr. Cash Flow Growth	130.71%	2.99%	5.46%	18.22%	30.28%	85.89%
Hist. Cash Flow Growth (3-5 yrs)	26.09%	17.49%	8.55%	9.68%	18.18%	NA
Current Ratio	2.19	1.48	1.29	1.79	1.39	9.45
Debt/Capital	53.86%	21.01%	45.14%	1.00%	33.23%	4.15%
Net Margin	5.99%	-16.33%	10.53%	19.50%	10.27%	-7.65%
Return on Equity	0.44%	-14.72%	16.06%	32.03%	16.06%	-2.56%
Sales/Assets	1.07	0.61	0.55	1.02	0.36	0.55
Proj. Sales Growth (F1/F0)	8.33%	5.47%	-2.66%	9.14%	12.62%	36.85%
Momentum Score	F	-	-	A	C	F
Daily Price Chg	6.37%	0.90%	0.09%	2.72%	3.59%	2.70%
1 Week Price Chg	12.98%	4.67%	0.92%	2.01%	5.86%	18.64%
4 Week Price Chg	27.89%	9.36%	5.61%	2.26%	12.86%	9.65%
12 Week Price Chg	89.49%	34.70%	16.49%	23.55%	75.47%	110.24%
52 Week Price Chg	43.34%	0.00%	-6.63%	12.11%	46.15%	190.16%
20 Day Average Volume	11,930,644	716,798	2,841,862	1,369,021	7,721,157	2,969,448
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.88%	0.00%
(F1) EPS Est 4 week change	-18.36%	0.00%	0.00%	0.00%	-0.31%	0.18%
(F1) EPS Est 12 week change	-2,165.84%	-0.19%	-13.25%	-5.23%	-8.97%	23.62%
(Q1) EPS Est Mthly Chg	-11.35%	0.00%	0.00%	0.00%	0.27%	-0.09%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	B
Momentum Score	F
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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