

Robinhood Markets

1Q23E: MAU inflection, reverse sorting and positive overall financial results

Reiterate Rating: UNDERPERFORM | PO: 8.00 USD | Price: 9.07 USD

HOOD reported overall positive results

Robinhood Markets (HOOD) reported in-line adj. EPS (-\$0.57 actual vs. -\$0.62 BofA and -\$0.56 consensus) that included a one-time \$485M charge from the cancellation of founder awards as well as a larger than expected increase in NIR (+\$41M q/q actual vs. +\$20M guidance) driven by strong securities lending revenue. HOOD also reported lower than expected SBC (\$598 actual vs. \$615-645 guidance). Key points of interest that were discussed on the call included a return in growth in MAUs (first time in 6 quarters), "reverse-sorting" as clients flooded HOOD with deposits in its Gold-tier cash sweep program, strong growth in NIR, and the success of current product launches (Cash Card) as well as excitement around upcoming ones (launch of 24 hour stocking trading 5 days a week and the eventual planned launch of futures trading).

Raising EPS and PO

We increased our 2Q23/2024/2025 EPS estimates to \$0.02/\$0.21/\$0.55 from \$0.00/\$0.18/\$0.51 driven by a slightly lower expense forecast (given \$30M improved guidance) and robust NIR growth (strong securities lending and cash sweep trends). Our price objective of \$8 (\$8.10 prior) is derived from a price to revenue method. We continue to apply a 3x multiple on 2025 revenues before discounting back one year.

Reiterate Underperform but positive quarter a good sign

We reiterate our Underperform rating on HOOD as we believe the Covid-related tailwind reversal (bear market, back to work, stimulus reduction...) continue to impact HOOD's growth/retail engagement but we are monitoring for signs of stabilization and find this quarter promising. Following multiple expense cuts and an emphasis on expense discipline, we have HOOD generating a positive adj. EBITDA going forward and positive adj. EPS as soon as next quarter. Other downside risk factors include regulatory risks surrounding PFOF (~50% of revenues) and market expansion. Risks to our Underperform rating include a rapid return of retail engagement and additional product launches / market expansion.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025
EPS	(7.49)	(1.17)	(0.55)	0.21	NA
GAAP EPS	(7.49)	(1.17)	(0.55)	0.21	NA
EPS Change (YoY)	NM	84.4%	53.0%	NM	NA
Consensus EPS (Bloomberg)			(0.66)	(0.06)	0.04
DPS	0	0	0	0	NA
Valuation (Dec)					
P/E	NM	NM	NM	43.2x	NA
GAAP P/E	NM	NM	NM	43.2x	NA
Dividend Yield	0%	0%	0%	0%	NA

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11 May 2023

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	8.10	8.00
2023E Rev (m)	1,871.9	1,868.2
2024E Rev (m)	2,203.1	2,176.5
2023E EPS	-0.64	-0.55
2024E EPS	0.18	0.21

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Stock Data

Price	9.07 USD
Price Objective	8.00 USD
Date Established	11-May-2023
Investment Opinion	C-3-9
52-Week Range	6.81 USD -12.76 USD
Mkt Val / Shares Out (mn)	7,034 USD / 775.5
Average Daily Value	59.93 USD
BofA Ticker / Exchange	HOOD / NAS
Bloomberg / Reuters	HOOD US / HOOD.OQ
ROE (2023E)	0%
ESGMeter™	NLA

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Glossary:

SBC = share-based comp
NIR = net interest revenue
NIM = net interest margin
MAU = monthly active user

iQprofileSM Robinhood Markets

Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025
Net Revenues	1,813	1,358	1,868	2,177	NA
Compensation & Benefits	(1,371)	(925)	(1,140)	(672)	NA
% of Net Revenue	75.6%	68.1%	61.0%	30.9%	NA
Non-Compensation Expenses	(2,084)	(1,444)	(1,228)	(1,323)	NA
Net Income to Ordinary Shareholders	(3,688)	(1,028)	(501)	181	NA

Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025
Total Assets	19,769	23,337	26,156	26,887	NA
Deposits	NA	NA	NA	NA	NA
Long Term Debt	0	0	0	0	NA
Total Equity	7,293	6,956	7,556	7,757	NA

Sector Metrics (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025
DARTs	0	0	0	0	NA
Net Interest Margin	NA	NA	NA	NA	NA
Interest Earning Assets	17,097	17,520	20,942	21,890	NA
Net New Assets	27	18	19	19	NA
Growth	19.9%	19.9%	19.9%	19.9%	NA
Total Client Assets	98	62	97	122	NA

Performance Metrics (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025
Operating Margin	-90.6%	-74.4%	-26.7%	8.3%	NA
Net Profit Margin	-203.4%	-75.7%	-26.6%	8.5%	NA
Comp Expense/Revenue	75.6%	68.1%	61.0%	30.9%	NA
Non-Comp Expense / Revenue	114.9%	106.3%	65.7%	60.8%	NA
Net Revenue Growth	89.1%	-25.1%	37.6%	16.5%	NA

Company Sector

Asset Management

Company Description

HOOD is an online broker that pioneered commission-free trading and targets underserved "unbrokered" retail investors that are less wealthy and younger than the clients of other wealth managers. HOOD undercut much of its established competition by generating fees through order routing client trades to market-makers instead of charging commissions.

Investment Rationale

While the benefits from the perfect storm created by the pandemic continue to reverse and at the same time its main revenue driver (PFOF) is being investigated by the SEC, MAU's have shown signs of stabilization and net interest revenue is becoming a larger driver of revenue. We look for continued signs of reversing trends and maintain our Underperform rating.

Quarterly Earnings Estimates

	2022	2023
Q1	-0.45A	-0.57A
Q2	-0.34A	0.02E
Q3	-0.20A	-0.01E
Q4	-0.19A	0E

Additional information

MAUs grow for first time in 6 quarters

HOOD's MAUs increased to 11.8M (vs. 11.4M q/q) signaling a possibility that a floor in retail engagement has been reached. The broker grew accounts at a staggering pace through 2020 on the back of Covid tailwinds reaching a peak in 1H21 during the meme-stock and GameStop short-squeeze period, trends which have since reversed driving 6 quarters of declining MAUs. While battling declining active users and a tough market backdrop, HOOD has launched a multitude of new products (options trading cash accounts, advanced charting, Robinhood Retirement, non-custodial wallet, etc.) while continuing to clean up their cost base in tandem in preparation for a re-acceleration in user-activity which we think could be on the near-horizon. Despite the termination of their Ziglu deal and plans to offer brokerage services in the UK with a "crypto-first" approach, we are waiting for more updates surrounding their ambitious goal to expand internationally (and how they plan to monetize international clients) by the end of 2023 which should further open their TAM.

Competitive cash sweep rate causes "reverse-sorting"

Given HOOD's competitive cash sweep rates (Gold = 4.65% / Non-Gold = 1.50%), the broker has been experiencing "reverse-sorting" as yield seeking clients have flooded the broker with new deposits (Gold cash sweep balances +\$3.2B q/q). This is in contrast with most of its broker peers who have opted to keep their cash sweep rates low to protect their NIM at the expense of elevated levels of client cash sorting while some brokers were forced into this strategy having gone too far out on the yield curve in their asset portfolios during the long period of record low interest rates. We consider this a winning strategy for HOOD allowing them to convert more clients into its Gold membership that helps to create customer-stickiness and promote the further use of other services such as the Robinhood Cash Card and increase user-activity. It's important to note, despite the high cash sweep rate, HOOD was still able to earn a net interest margin of 1.20% on avg cash sweep balances proving it can still generate positive economics from sweep cash despite its high sweep rate available to clients.



Price objective basis & risk

Robinhood Markets (HOOD)

Our price objective (PO) of \$8 for Robinhood is derived from a market cap to revenue method: We apply a 3x multiple to forecasted 2025 revenues to obtain a valuation which we then discount back one year to obtain our PO. We also no longer include excess cash as we are including net interest revenue generation from that cash and wish to avoid double counting.

Upside risks to our PO are: expansion of cryptocurrency offering, entrance into international markets, and new product launches.

Downside risks to our PO are: US regulatory risks regarding payment for order flow, continued reversal of pandemic related tailwinds, and decelerating growth potential given its high market share within its addressable market.

Analyst Certification

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US - Brokers, Asset Managers, & Exchanges Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
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	Ares Management Corp	ARES	ARES US	Craig Siegenthaler, CFA
	BlackRock, Inc.	BLK	BLK US	Craig Siegenthaler, CFA
	Blackstone	BX	BX US	Craig Siegenthaler, CFA
	Blue Owl Capital	OWL	OWL US	Craig Siegenthaler, CFA
	Interactive Brokers	IBKR	IBKR US	Craig Siegenthaler, CFA
	Intercontinental Exchange	ICE	ICE US	Craig Siegenthaler, CFA
	KKR & Co. Inc.	KKR	KKR US	Craig Siegenthaler, CFA
	TPG Inc	TPG	TPG US	Craig Siegenthaler, CFA
	Tradeweb Markets Inc.	TW	TW US	Craig Siegenthaler, CFA
	Victory Capital Holdings, Inc.	VCTR	VCTR US	Craig Siegenthaler, CFA
NEUTRAL				
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	Invesco	IVZ	IVZ US	Craig Siegenthaler, CFA
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	Robinhood Markets	HOOD	HOOD US	Craig Siegenthaler, CFA
	T. Rowe Price	TROW	TROW US	Craig Siegenthaler, CFA
	The Carlyle Group	CG	CG US	Craig Siegenthaler, CFA
RSTR				
	Focus Financial Partners	FOCS	FOCS US	Craig Siegenthaler, CFA

IQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity
Operating Margin
Earnings Growth
Free Cash Flow

Quality of Earnings

Cash Realization Ratio
Asset Replacement Ratio
Tax Rate
Net Debt-To-Equity Ratio
Interest Cover

Valuation Toolkit

Price / Earnings Ratio
Price / Book Value
Dividend Yield
Free Cash Flow Yield
Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income
Operating Profit
Expected 5 Year CAGR From Latest Actual
Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations
Capex
Tax Charge
Net Debt = Total Debt – Cash & Equivalents
EBIT

Numerator

Current Share Price
Current Share Price
Annualised Declared Cash Dividend
Cash Flow From Operations – Total Capex
EV = Current Share Price × Current Shares + Minority Equity + Net Debt +
Other LT Liabilities
Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Amortization
Shareholders' Equity
Sales
N/A
N/A

Denominator

Net Income
Depreciation
Pre-Tax Income
Total Equity
Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)
Shareholders' Equity / Current Basic Shares
Current Share Price
Market Cap = Current Share Price × Current Basic Shares
Sales

Basic EBIT + Depreciation + Amortization

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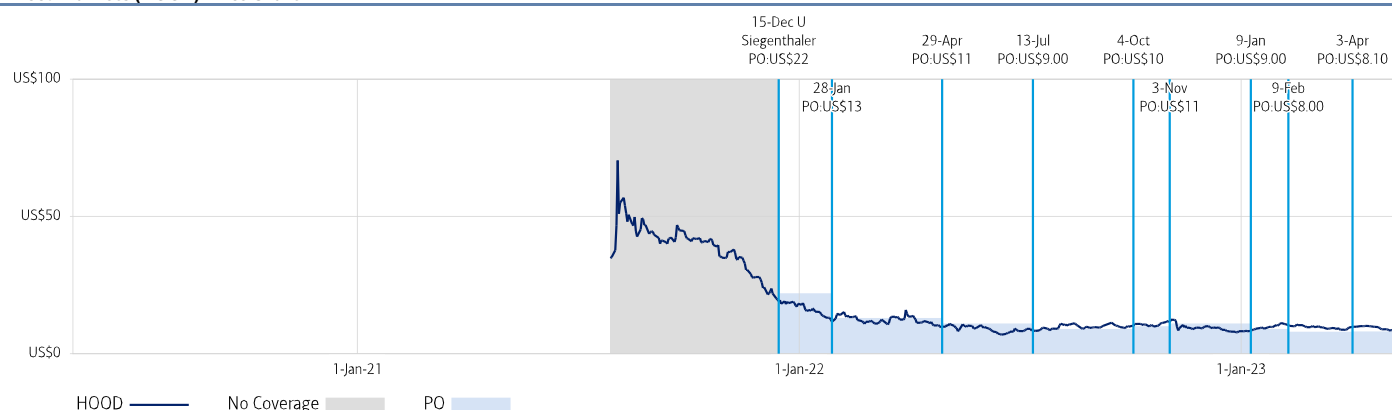
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Robinhood Markets (HOOD) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Financial Services Group (as of 31 Mar 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	152	52.41%	Buy	92	60.53%
Hold	73	25.17%	Hold	44	60.27%
Sell	65	22.41%	Sell	41	63.08%

Equity Investment Rating Distribution: Global Group (as of 31 Mar 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1869	53.01%	Buy	1030	55.11%
Hold	827	23.45%	Hold	476	57.56%
Sell	830	23.54%	Sell	389	46.87%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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