

Square, Inc.

Cash App Virtually Unstoppable; Virtual Software Tour Takeaways

Summary

We recently hosted Nikhil Dixit, SQ's IR Director, and several Cash App Business Leads including Alex Anderson (Finance & Strategy), Ben Shen (Consumer Banking Product), and Alex Bentley (Go-to-Market) as part of our 2nd Annual Mizuho Virtual Software Tour.

The discussion focused solely on the vast growth opportunities available for Cash App. We remain upbeat about Cash App's TAM, ARPU potential, user growth prospects, and revenue sustainability. Our key takeaways are below.

Key Points

1. Cash App's ARPU May Double. Cash App's ARPU has seen stellar growth rising from nothing to \$45 over 4-5 years. How high could it go? For the 50% of monetized users, the ARPU is as high as \$90. We estimate that rapid product adoption, 1-2 new launches per year, and ARPU at \$80+ by 2023 may potentially drive Cash App's medium-term CAGR to 60%+ (Ex. 1).

2. Cash App's TAM May Double. We believe that SQ's \$60bn Cash App TAM may understate the long-term opportunity. Incremental opportunities include tapping of new demographics like the 100mn US millennials, and introducing products like small loans (*see our consumer survey showing 10%+ GP upside*), insurance, investing, and wealth management.

3. Effective Network Strategy Is Key Success Factor. Management highlighted three main success drivers for the Cash App including: (1) Beneficial demographics: Cash App customers tend to have less access to banking services. This drives strong market fit, adoption, and leads to higher engagement and retention; (2) Smart brand investment including viral marketing on social media; (3) A targeted paid marketing campaign for the first time.

4. Unit Economics More Favorable than Banks & Neobanks. Offering banking services is a significant long-term opportunity for the Cash App. The lower cost of acquisition vs. traditional banks and some popular neobanks is a key competitive advantage. For example, SQ does not need to recoup acquisition costs by offering mortgages like banks do, and its viral P2P aspect lowers the cost of acquisition vs. neobanks.

5. Worried About Revenue Sustainability? New Products Are Scaling Rapidly. Investors often worry about sustainability of Cash App's revenue streams. Yet scaling of new products like Cash Card are following similar trajectories of the successful Instant Deposit product. All this bodes well for substantiality of revenue growth.

Rating	Buy
Previous Rating	No Change
Price (9/23)	\$149.59
Price Target	\$225.00
Previous Price Target	No Change

Key Data

Symbol	SQ (NYSE)
52-Week Range	\$170.61 - \$32.33
Market Cap (\$mm)	\$66,348
Shares Outstanding (mm)	371.3
Float	368.0
Average Daily Volume	12,855,226
Dividend/Yield	\$0.00/0.0%

Fiscal Year-End: Dec 31

	2019A	2020E		2021E	
		Prior	Curr	Prior	Curr
Revenue (\$mm)					
1Q	—	—	—	—	—
2Q	—	—	—	—	—
3Q	—	—	—	—	—
4Q	—	—	—	—	—
Yr	2,276A	—	2,921E	—	4,582E
EBITDA (\$mm)					
1Q	—	—	—	—	—
2Q	—	—	—	—	—
3Q	—	—	—	—	—
4Q	—	—	—	—	—
Yr	417A	—	286E	—	779E



Dan Dolev
Managing Director
+1 646 949 9599
Dan.Dolev@mizuhogroup.com

Ryan Coyne
Associate
+1 212 205 7975
Ryan.Coyne@mizuhogroup.com

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Exhibit 1: Hypothetically, Higher ARPU Means Better CAGR for the Cash App

Cash App Ecosystem Hypothetical CAGR at \$80+ ARPU							
Unit Economics Analysis	2015	2016	2017	2018	2019	2020E	2023E
Gross Profit Est. (\$mns)		5	47	195	458	928	4,113
Monthly Actives (mns)	1	2	5	11	20	27	60
Incremental Monthly Actives per Year		2	3	6	9	8	11
Gross Profit Per Active		3	9	18	23	34	68
ARPU							82
Incremental Gross Profit per Active, per Year		3	7	8	6	11	11
Cash App Ecosystem Gross Profit						928	4,113
2020 - 2023 CAGR Potential							64%

Sources: Company reports, MSUSA estimates

Exhibit 2: SQ Financial Model

Square (SQ) - Selected Annual Financial Information					
\$mns, except per share data	FY 2019	FY 2020E	FY 2021E	FY 2022E	FY 2023E
Adjusted Net Revenue (Est.)	2,276	2,921	4,582	5,989	7,515
% Growth		28%	57%	31%	25%
Gross Profit	1,898	2,505	3,980	5,210	6,551
% Growth		32%	59%	31%	26%
Adjusted EBITDA	417	286	779	1,198	1,879
Adjusted EBITDA margin	18.3%	9.8%	17.0%	20.0%	25.0%
Adjusted Earnings	387	238	642	982	1,564
Adjusted EPS	\$0.80	\$0.47	\$1.26	\$1.95	\$3.13
Free Cash Flow	403	(85)	544	867	1,428
Free Cash Flow Conversion	104%	n/m	85%	88%	91%

Sources: Company reports, MSUSA estimates

Price Target Calculation and Key Risks

SQ is best positioned to benefit from SMB dislocation, in our view. Superior unit economics for its Cash App could help drive 4x growth in GP. We believe that SQ's margins are understated (40%+ steady state) as it seeks to maximize its terminal value. We believe all this merits a mid-teens sales multiple. Our \$225 PT is based on ~15x our 2023 sales forecast.

Downside risks include: (1) inability to further evolve sustainable revenue streams for the Cash App, (2) key end markets seeing post-COVID structural decline, and (3) inability to innovate on par with other disruptors in the industry.

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Investment Risks and Valuation Methods can be located in the following section of this research report - Price Target Calculation and Key Risks.

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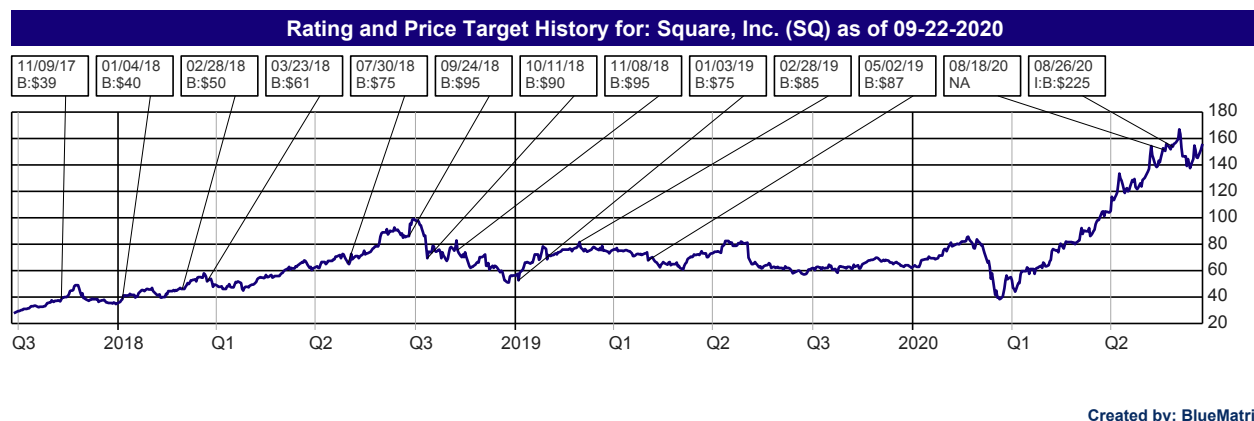
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(As of September 23)	% of coverage	IB service past 12 mo
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Hold (Neutral)	37.14%	50.77%
Sell (Underperform)	2.29%	75.00%

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