

SQUARE (SQ)

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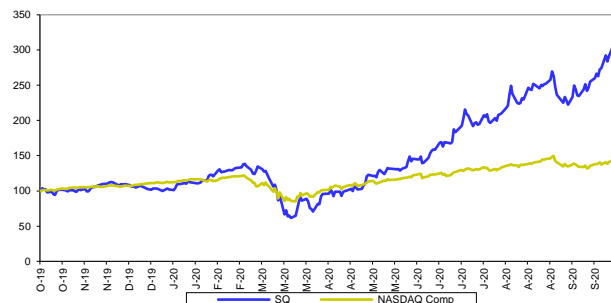
Rating: **BUY** | Price Target: **\$212.0** | Horizon: 6 Months | October 2020

Price	\$212	52wk High	\$191	Market Cap	\$82,620 M	EPS	\$0.18
Upside	14%	52wk Low	\$33	Shares Out.	327 M	Industry	Transaction Processor

COMPANY OVERVIEW

SQ is a transaction processor that operates two lines of businesses:

- Seller:** SMB transaction processing, merchant SaaS and PoS hardware 1.95% market share in processing vs Stripe 3.5%, PayPal 10% by processing volume
- Cash App:** P2P transfers, direct deposit, Bitcoin/stock investing, targeting underbanked population. Cash App has 15% of market share by MAU vs Venmo at 29%



Multiple Valuation

2020E Adj Sales (M)	\$ 6,803.8	2020E Rev Growth	68.9%
Target Multiple	16x	Implied Price	\$ 212
Current Multiple	16x	Upside	14%

INVESTMENT THESIS

SQ has significant upside potential driven by rapid penetration of the underbanked segment post-pandemic and steep growth in customer lifetime value (CLV) through the launch of payday lending products

INVESTMENT SUMMARY

Substantial Income Upside Driven by Rapid Penetration of Underbanked TAM and Efficient Acquisition Strategy

- Rapid penetration:** Near doubling of existing user base from 30M to 47M as early majority segment of customer adopts services at +18% QoQ to increase Square's penetration of 53M smartphone savvy unbanked adults from 10% to 60% by 2021
- Efficient acquisition strategy:** Compression of CAC to \$20 driven by earned media and Cash Friday Twitter giveaway, reducing break even < 1 year

Counter-market View:

- Attach rate:** Early cohort study by management indicates attach rate of 23% compared to 19% implied by market, suggesting that market underestimate rate from customers acquired via stimulus deposits
- Revenue per user:** Square's superior revenue per user at \$10.83, driven by higher utilization of fee-generating product, compared to Venmo's \$1.88 implies that market's usage of Venmo's revenue per user to forecast Square's revenue is inaccurate

Payday Lending Rollout to Further Leapfrog CLV Through High Fees with Minimal Impact on Risk

- Leapfrog CLV:** Payday lending, piloted in Q3 '20 with expected launch in 2020, will boost annual revenue per customer to \$77 from \$33
- Minimal risk:** Payday lending expected to generate net loss of only 12% portfolio value annually compared to income of 65% effective APR portfolio value as high fees of 5% and high recovery rate of 69% offsets the default rate of 40%

Counter-market View:

- Launch awareness:** News on payday lending only circulating in the tech circle away from analysts

KEY METRICS

	2018	2019	2020E	2021E	2022E	2023E	CAGR
Seller business	\$2,720	\$3,440	\$3,424	\$4,213	\$5,124	\$6,108	
Cash app (ex-Bitcoin)	\$264	\$589	\$1,882	\$3,652	\$4,839	\$5,928	
Bitcoin	\$167	\$516	\$2,678	\$3,102	\$3,257	\$3,420	
Revenue (ex-Caviar)	\$3,150	\$4,545	\$7,984	\$10,967	\$13,220	\$15,456	
YoY Growth	64.0%	44.3%	75.6%	37.4%	20.5%	16.9%	
Revenue (ex-C, ex Bitcoin)	\$2,983	\$4,029	\$6,804	\$10,969	\$13,221	\$15,457	
YoY Growth	34.7%	35.0%	68.9%	61.2%	20.5%	16.9%	
GAAP revenue	\$3,298	\$4,714	\$7,984	\$10,967	\$13,220	\$15,456	24.6%
YoY Growth	49.0%	42.9%	69.4%	37.4%	20.5%	16.9%	

RISKS

Banks/Neo Banks Move Down Market to Compete

Superior CAC, high NPS, market leadership safeguards expansion plans and existing customers.

Unsuccessful Rollout of Payday Lending

Parallel projects such as payroll processing will continue to drive CLV and revenue per customer.