

## **Block, Inc. Third Quarter 2022 Earnings Call - Prepared Remarks**

### **Nikhil Dixit, Head of Investor Relations**

Hi, everyone. Thanks for joining our third quarter 2022 earnings call. We have Jack and Amrita with us today.

We will begin this call with some short remarks before opening the call directly to your questions. During Q&A, we will take questions from our customers in addition to questions from conference call participants.

We would also like to remind everyone that we will be making forward-looking statements on this call. All statements other than statements of historical fact could be deemed to be forward-looking. Actual results could differ materially from those contemplated by our forward-looking statements. Reported results should not be considered as an indication of future performance.

Please take a look at our filings with the SEC for a discussion of the factors that could cause our results to differ. Also, note that the forward-looking statements on this call are based on information available to us as of today's date. We disclaim any obligation to update any forward-looking statements, except as required by law.

During this call, we will provide preliminary estimates of gross profit growth performance for the month of October. These represent our current estimates for October performance as we have not yet finalized our financial statements for the month of October, and our monthly results are not subject to interim review by our auditors. As a result, actual October results may differ from these estimates. Moreover, this financial information has been prepared solely on the basis of currently available information by, and is the responsibility of, management. This preliminary financial information has not been reviewed or audited by our independent public accounting firm. This preliminary financial information is not a comprehensive statement of our financial results for October or the fourth quarter.

Also, we will discuss certain non-GAAP financial measures during this call. Reconciliations to the most directly comparable GAAP financial measures are provided in the Shareholder Letter, Investor Day materials, and Investor Presentation on our Investor Relations website. These non-GAAP measures are not intended to be a substitute for our GAAP results.

Finally, this call in its entirety is being audio webcast on our Investor Relations website. An audio replay of this call and the transcript for Jack and Amrita's opening remarks will be available on our website shortly.

With that, I would like to turn it over to Jack.

## **Jack Dorsey, Block Head**

Thank you all for joining us.

As we've discussed before, we are building multiple ecosystems to serve different audiences. Square for sellers, Cash App for consumers, TIDAL for musicians, and TBD for developers. What makes Block unique is our ability to connect all of these together. We've made a lot of progress on each, and I'll share some highlights from Square and Cash App before Amrita's remarks and your questions.

We'll start with Square. We realize there are some significant challenges all businesses are facing today, and so giving sellers simple and intuitive tools that remove complexity from running their businesses is critical. We're focused on three priorities to achieve this: enabling omnichannel capabilities, growing upmarket, and expanding internationally.

Core to our strategy is building integrated solutions that give larger sellers a cohesive view of their operations, so that they can easily manage every aspect of running a business. Our developer platform extends our software capabilities by allowing integrations with hundreds of third-party products built by developers and partners using our open platform. We enable customized solutions for sellers with more complex needs and provide a single platform for developers to take payments from Square across mobile, in-person, and web.

We're also continuing to build out our vertical point of sale solutions that serve our largest verticals of food & drink, retail, and services, with Square for Restaurants, Square for Retail, and Square Appointments. Together, gross profit from these solutions grew 45% year over year, much faster than Square overall in the quarter.

In Q3, we also expanded the payment methods we support. In the U.S., we launched Apple's Tap to Pay on iPhone, giving Square sellers a simple way to accept contactless payments with no hardware needed, and customers a convenient way to pay. In Japan, sellers can now accept PayPay QR code payments, the most popular QR code wallet in the country.

And now Cash App. As we shared during our Investor Day earlier this year, we are focused on building seven development pillars to drive Cash App's business. I'll touch on progress we made this quarter in Financial Services and Commerce.

Within Financial Services, we want to strengthen our relationships with customers through a full suite of banking products. This starts with customers being able to easily fund their Cash App accounts. Overtime we've expanded the ways customers can do this, whether through direct deposit, paper money, check deposits, or bank transfers.

Cash App Card and direct deposit are two of our most important banking products and we're focused on growing usage of both. Cash App Card is usually our first financial services product that customers try, and often their introduction to banking with Cash App. As of September,

there were nearly 18 million actives using Cash App Card, making up more than 35% of our monthly actives and bringing in half of all inflows across our platform.

In Q3, we made it easier to bank with us. Customers can now receive an account and routing number instantly when ordering a Cash App Card. This reduces friction for those who need banking services and has driven meaningful growth in direct deposit customers.

As we continue to deepen the connections between our ecosystems and undertake the complex integration of Afterpay, one of the long-term opportunities we are most excited for is in Commerce.

In Q3 we completed the rollout of our first iteration of the new Discover tab, making it seamless for customers to search for people and businesses and find offers, including instant discounts from merchants who accept Cash App Pay. Cash App Pay lets customers checkout through a simple QR code payment whether online or in-person. After testing Cash App Pay at Square sellers over the past year, we're beginning to broaden Cash App Pay acceptance outside of the Square ecosystem, starting with select Afterpay merchants.

We're still early in our journey to transform Cash App into a commerce destination that bridges our seller and consumer ecosystems. We believe it will take some time to achieve this vision, and doing so will bring us back to our original mission to help sellers make more sales.

Finally, we know a lot's changed in our business over the last year, including with the acquisition of Afterpay, and we recognize that understanding our business today may seem complex, especially in a changing macro environment. We're working to distill how we invest and operate into a clearer and more cohesive framework to help you better understand our business in 2023 and the longer-term. Amrita will be addressing some of our current thinking for 2023 today in her remarks but we plan to do so more comprehensively in our fourth quarter call in February.

With that, here's Amrita.

**Amrita Ahuja, Chief Financial Officer**

Thanks Jack. There are three topics I'd like to cover today.

First, an overview of our third quarter results. Second, trends we've seen across our business in October. And third, our discipline around expenses.

In the third quarter, we delivered strong growth across our ecosystems with gross profit of \$1.57 billion, up 38% year over year and 46% on a three-year CAGR basis. Gross profit includes a \$19 million impact from the amortization of acquired technology assets primarily related to Afterpay, and excluding these non-cash expenses, gross profit was \$1.59 billion.

We delivered strong profitability during the quarter, with Adjusted EBITDA of \$327 million.

In the third quarter, our BNPL platform, which we acquired through the acquisition of Afterpay, contributed \$150 million of gross profit split across Square and Cash App; and excluding this, gross profit for the quarter was \$1.42 billion, up 25% on a year-over-year basis and 42% on a three-year CAGR basis.

Cash App generated \$774 million of gross profit in the third quarter, an increase of 51% year over year, and 84% on a three-year CAGR basis. Excluding our BNPL platform, Cash App gross profit was \$700 million, up 37% year-over-year and 78% on a three-year CAGR basis.

This quarter, overall inflows into Cash App totaled \$52 billion, for growth of 19% year over year, and represented our highest quarterly inflows into Cash App. Let's look into the drivers using our inflows framework, across actives, inflows per active, and monetization rate:

First, our network reached 49 million transacting actives in September, up 20% on a year over year basis, with daily and weekly actives growing even faster. With Cash App's Community pillar, we remain focused on enhancing the viral growth of peer-to-peer with complementary marketing programs that target new audiences.

Second, inflows per active averaged \$1,046 in the third quarter, which was relatively consistent with the first and second quarters, and was also stable on a year over year basis. Inflows per active have been driven by continued product adoption, with Cash App Card and direct deposit as Jack mentioned, and by expanding our inflow channels.

We believe driving inflows per active starts with customers' ability to easily fund their Cash App accounts through a variety of channels. Together, direct deposit and paper money deposits have made up a growing share of overall inflows, reaching 14% of inflows in the third quarter, up from 9% a year ago.

In September, customers received more than \$2 billion in direct deposits into their Cash App accounts, driven by strong growth in direct deposit actives and direct deposit inflows per active compared to the prior year.

Paper money deposits crossed nearly \$3.5 billion in cumulative deposits through September, only a year since launch.

Square generated \$783 million of gross profit in the third quarter, an increase of 29% both year over year and on a three-year CAGR basis. Excluding \$75 million of gross profit from our BNPL platform, Square gross profit was \$708 million, up 17% year-over-year and 25% on a three-year CAGR basis.

Square GPV grew 20% year over year in the quarter, or 22% on a constant currency basis with a 2 point headwind to growth from foreign exchange rates.

Looking at our cohort economics, we continued to see healthy retention trends across our existing seller base. In the third quarter, we achieved positive GPV and gross profit retention for our Square business.

Looking into the drivers of Square's third quarter performance. First, we continued to drive growth with larger sellers. Gross profit from mid-market sellers was up 22% year over year, and 39% on a three-year CAGR basis. Our developer tools have helped us serve the needs of larger, more complex sellers, allowing us to grow upmarket. During the third quarter, nearly 50% of mid-market GPV was generated by sellers connected to our open developer platform.

Second, we've continued to expand globally. In the third quarter, GPV from our markets outside the U.S. grew 40% year over year, or 55% on a constant currency basis, as foreign exchange was a significant drag on our year over year growth across all international markets. Looking at volume trends by market in the quarter, growth in Australia and Canada remained strong while we saw a macro-related slowdown in the UK.

Now to provide an update on our BNPL platform, which we acquired through the Afterpay acquisition. In the third quarter, GMV for our BNPL platform was \$5.4 billion, up 10% year over year, or 60% on a three-year CAGR basis.

For overall growth trends, we've experienced an impact from spend shifts from online to in person, competitive dynamics, as well as foreign currency, which slowed year over year GMV growth by five points in the third quarter.

As we integrate Afterpay, our teams are focused on bridging commerce across Cash App and Square, and are making steady progress towards our longer-term vision.

On a GAAP basis, revenue for our BNPL platform was up 6% year over year, growing slower than GMV given mix shifts to enterprise sellers and newer markets. Gross profit was down 3% year over year, impacted by \$12 million in amortization of intangibles within cost of sales. Without this impact, gross profit growth would have been more in-line with revenue growth.

Losses on consumer receivables were 0.96% of GMV during the third quarter, an improvement quarter over quarter compared to 1.02% in the second quarter, and an improvement year over year -- driven by mix shifts as well as enhancements to our risk models and processes during the first half of the year. We continued to see healthy consumer repayment behavior with more than 95% of installments paid on time.

As we enter into 2023, we intend on simplifying many of these disclosures. We don't intend on speaking to our BNPL performance separately once we anniversary the acquisition of Afterpay, and we'll also shift our focus away from three-year CAGRs and towards year over year growth rates as we lap the onset of the pandemic three years ago.

Next, an update on recent trends. On both a year-over-year and three-year CAGR basis, October total gross profit growth is estimated to be relatively consistent with the third quarter.

In October, we estimate overall company gross profit growth of 37% on a year-over-year basis including our BNPL platform, or 24% excluding our BNPL platform.

We expect fourth quarter gross profit growth to remain relatively consistent with third quarter growth rates on both a year over year and three-year CAGR basis at the total company level.

Now let's dig into some of the dynamics by ecosystem.

For Cash App, we expect the year over year gross profit growth rate to improve in the fourth quarter compared to the third quarter. We saw this play out in October, where we estimate Cash App gross profit growth excluding our BNPL platform improved on a year over year basis compared to 37% in the third quarter.

On a three-year CAGR basis, we expect to see a slight decrease in Cash App's gross profit growth in the fourth quarter relative to the third quarter as we lap the launch of Tabs in 2019.

Cash App's gross profit growth in October was driven by growth in actives and monetization rate, while inflows per active was relatively consistent on a year-over-year basis.

Cash App Card continued to have strong momentum on actives and spend per active, which both increased on a year-over year basis.

For Square, we expect the year-over-year growth rate for gross profit excluding our BNPL platform to moderate in the fourth quarter compared to the third quarter, given we are now lapping \$59 million of non-recurring PPP gross profit recognized in the fourth quarter of 2021.

Excluding PPP and our BNPL platform, we expect year over year gross profit growth for Square in the fourth quarter to be relatively consistent with the third quarter, which had a 19% year over year growth rate with the same exclusions.

On a three-year CAGR basis, we expect gross profit growth excluding our BNPL platform to decrease slightly in the fourth quarter relative to the third quarter.

Looking at recent volume trends, we estimate Square GPV in October was up 16% year over year, compared to 20% growth in the third quarter, and on a constant currency basis, 19% year over year as compared to 22% in the third quarter.

Trends on a three-year CAGR basis were more stable, as we estimate GPV grew by 21% in October, compared to 22% in the third quarter.

By region, growth in the U.S. remained relatively stable through October. However, we have seen a meaningful slowdown in year over year GPV growth in our international markets, primarily driven by foreign exchange rates and to a lesser extent, the ongoing macro-related slowdown in the UK. In October, we estimate that international GPV was up 23% year over year, or 44% on a constant currency basis.

Moving to our planned investments for the fourth quarter of 2022. While our business trends have remained stable through October, we have been increasingly focused on our spend amidst an uncertain macro environment.

We plan to reduce our investments for the full-year 2022 by an additional \$140 million, which brings the total pullback on our planned non-GAAP operating expenses on the year to \$590 million, or approximately 25% of our expected step-up entering the year.

For the fourth quarter, we expect to increase non-GAAP operating expenses by \$206 million compared to the third quarter.

Looking ahead to 2023. We are still in the process of finalizing our plans for next year and, while we aren't quite ready to share specifics, we wanted to give you a sense of how we are thinking about next year.

Over the past several years, we've significantly grown our business and our expense base. Looking to 2023, we're focused on operating more efficiently, and we expect to slow our pace of expense growth meaningfully compared to prior years.

Based on our preliminary plans, our outlook includes a slowdown across several areas of our discretionary expenses, a continuation of the discipline you've seen from us in recent quarters. In particular, two areas to underscore:

First, hiring. Headcount makes up the largest driver of our expense base. In 2023, we expect to significantly moderate our pace of hiring compared to recent years, which will benefit our financial results on a lag with greater leverage on headcount costs expected in the back half of 2023 and into 2024.

Second, sales and marketing. In 2023, we intend on pulling back on lower-ROI, more experimental areas including brand and awareness spend across both our Square and Cash App ecosystems, and continue investing in channels with more proven ROIs.

Outside of these, one-third of our non-GAAP operating expenses include variable expenses which have historically grown more in-line with overall gross profit -- including transaction and loan losses, peer-to-peer costs, Cash App Card issuance costs, and expenses related to data and our platform infrastructure.

We continue to see a compelling opportunity for long-term growth, and we are prepared to be dynamic with our spend as we see the macro environment play out, both investing more where we see returns, and pulling back with lower or uncertain returns as we have done in the past.

We'll look to share more on our approach for the coming year in our fourth quarter earnings call in February.

To conclude, as we enter an uncertain macro environment, our agility means we can track our business trends in real-time across a diverse set of products and customers, and make strategic decisions quickly to support our customers and adapt to the changes we observe.

With that, we'll open it up to your questions.