Better Buy: Square, Inc. (SQ) vs. PayPal (PYPL)

Which of these digital payment leaders is the best buy now?

Joe Tenebruso (TMFGuardian)
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Investors who can identify the businesses best positioned to profit from powerful long-term trends stand to make a fortune. The challenge, however, lies in choosing which trends will endure and which companies will capitalize on them.

One trend on investors radar's in digital payments, and it seems it's here to stay -- credit and debit card payment volumes will grow to $55 trillion by 2025, according to the Nilson Report, and the companies that can compete and win in this huge and rapidly growing market will no doubt deliver handsome profits to their investors. In fact, digital payment leaders **Square** (NYSE:SQ) and **PayPal** (NASDAQ:PYPL) are doing just that, and both have rewarded their shareholders with hefty gains in recent years.

But which of these stocks is the better buy today? Let's find out.

IMAGE SOURCE: GETTY IMAGES.

Financial strength

Let's first take a look at some key financial metrics to see how Square and PayPal stack up.

Metric	Square	PayPal
Revenue	$2.42 billion	$13.80 billion
Operating income	($61 million)	$2.48 billion
Net income	($72 million)	$1.92 billion
Operating cash flow	$136 million	$1.43 billion
Free cash flow	$107 million	$734 million
Cash and investments	$1.15 billion	$7.79 billion
Debt	$363 million	$0

DATA SOURCES: MORNINGSTAR, COMPANY FILINGS.

PayPal and Square are simply in different leagues when it comes to financial strength. PayPal's revenue, profits, and cash flow dwarf those of its smaller rival. And with nearly $8 billion in cash reserves, PayPal has 10 times the net cash as Square. Thus, PayPal clearly has the edge here.

Advantage: PayPal

Growth

PayPal may be the more financially powerful business, but Square is growing much more rapidly.

Looking forward, PayPal is projected to increase its revenue by a respectable 17.6% in 2018 and nearly 16% in 2019, driven by the strong growth of mobile commerce. Square's sales, meanwhile, are expected to increase by an incredible 49% this year and 34% next year fueled by its cross-selling initiatives and international expansion.

Moreover, Wall Street estimates that Square's earnings per share will rise more than 50% annually over the next five years, while PayPal is expected to grow its EPS by less than 20% annually over this same time.

So, in terms of both recent past and expected future growth, Square has a decided edge.

Advantage: Square

Valuation

Lastly, let's take a look at some valuation metrics.

The price-to-sales ratio -- which can be calculated by dividing the company's market capitalization by its revenue -- can be helpful when evaluating growth stocks, including those that are not yet consistently profitable, such as Square.

A businesses' forward price-to-earnings ratio -- which can be determined by dividing its stock price by the amount of earnings per share that analysts expect the company to generate in the next year -- helps to give us an idea of how much investors are willing to pay today for a company's projected future profitability.

And the price-to-earnings-to-growth (PEG) ratio -- which can be calculated by dividing a stock's price-to-earnings ratio by its expected earnings growth rate -- helps to add perspective by factoring in a company's growth prospects. In this case, I'm using analysts' five-year projected EPS growth rates, as it correlates most closely to my long-term investment time horizon.

Metric	Square	PayPal
P/S	11.30	7.59
Forward P/E	85.36	31.28
PEG	2.76	1.91

DATA SOURCE: YAHOO! FINANCE.

Square's stock is significantly more expensive than that of PayPal in terms of price-to-sales and price-to-earnings. This is to be somewhat expected, because Square's revenue and earnings are projected to grow at much faster rates than that of PayPal. Yet even when we account for Square's higher forecasted EPS growth -- as we do with the PEG ratio -- PayPal's shares are still far cheaper.

Thus, PayPal is the better bargain.

Advantage: PayPal

The better buy is...

Square and PayPal are two great ways to profit from the trend toward a cashless society. But while Square offers investors turbocharged growth, PayPal's stronger financial position and more attractively priced shares make it the better buy today.

PayPal Holdings is not on our top "Buy" list, but these 10 stocks are

sting geniuses David and Tom Gardner just released their best stocks to buy now -- and
ıld pay to listen. Especially when you consider their average stock pick is up 353% vs. a
81% for the S&P 500.

just shared what they think are the **ten best stocks** for investors to buy right now to
ıbers inside their service *Motley Fool Stock Advisor*… and PayPal Holdings wasn't one
em! That's right -- they think these 10 stocks are even better buys.

See the 10 stocks

Advisor returns as of June 4, 2018

*enebruso has no position in any of the stocks mentioned. The Motley Fool owns shares of and
ımends PayPal Holdings and Square. The Motley Fool has a disclosure policy.*

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Joe honed his investing skills as an analyst for Stock Advisor, Fool One, Supernova, Million Dollar Portfolio, and Income Investor. He battle-tested his investment philosophy and strategies as portfolio manager of Tier 1, a market-crushing Motley Fool real-money portfolio that delivered 24.58% annualized returns during its existence. Now, Joe's mission is to pass on what he's learned -- and what he continues to learn -- as a contributing writer to Fool.com.

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Technology and Telecom

STOCKS

PayPal Holdings
NASDAQ:PYPL
$87.07 $-0.40 (-0.46%)

Square
NYSE:SQ
$71.58 $1.17 (1.66%)