Marqeta 2Q21 Earnings Call Introductory Remarks

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Operator

Good afternoon, ladies and gentlemen. Thank you for standing by. Welcome to the Marqeta Second Quarter 2021 Earnings Conference Call. At this time, lines have been placed on mute to prevent any background noise. After the speakers' remarks, we will open the lines for your questions. As a reminder, this conference call is being recorded. I'd now like to turn the call over to Stacey Finerman, Vice President of Investor Relations to begin.

Stacey Finerman

Thanks, Operator. Before we begin, I would like to remind everyone that today's call may contain forward-looking statements. These forward-looking statements are subject to numerous risks and uncertainties, including those set forth in our filings with the SEC which are available on our Investor Relations website, including our prospectus dated June 8, 2021, and our subsequent periodic filings with the SEC, such as our quarterly report on Form 10-Q for the quarter ended June 30, 2021. Actual results may differ materially from any forward-looking statements we make today. These forward-looking statements speak only as of the time of this call and the Company does not assume any obligation or intent to update them, except as required by law. In addition, today's call may include non-GAAP financial measures. These measures should be considered as a supplement to, and not a substitute for, GAAP financial measures. Reconciliations to the most directly comparable GAAP measures can be found in today's earnings press release, which is available on our Investor Relations website. Hosting today's call are

Jason Gardner, Marqeta's Founder and CEO, and Tripp Faix, Marqeta's Chief Financial Officer. With that, I'd like to turn the call over to Jason to begin.

Jason Gardner

Thanks, Stacey. Thank you everyone for joining us for Marqeta's first earnings call as a public company. It's great to be connecting with you all. We had a very successful IPO, we raised a lot of capital, and we are off to a great start! Tripp and I are excited to share Marqeta's second-quarter results as well as an overview of our business.

I am going to point to a few financial items about which Tripp will provide additional detail. Next, I will talk about three key themes for the quarter. And, lastly, for those on the call that are less familiar with us, I will provide some focus about Marqeta. With that, let's begin.

Our second-quarter results demonstrate our strong product-market fit and execution in this rapidly evolving digital payments environment: $27 billion in Total Processing Volume, or TPV, a 76% increase compared to the same quarter of 2020. $122 million in net revenue, a 76% increase compared to the same quarter of 2020

There are three key themes that I want to highlight from the second quarter. First, we continue to land winners. Google chose Marqeta to power the launch of a digital card for its Google Pay balance users, allowing them to instantly use their balance through a virtual card tokenized in Google Pay.

Second, we continue to expand and grow rapidly with our current customers. We expanded our relationship with Square. During the quarter Square announced the launch of Square Banking Services and we are proud to power the Square Checking product.

And third, we continue to retain our customers by building long-term relationships where our interests are mutually aligned. During the quarter, we extended our agreement with Affirm until 2024. This is a confirmation of the enduring value of our platform and our very strong partnership.

Again, Tripp will provide more details on our second-quarter performance in a few minutes, but since this is our first earnings call, I'd like to spend some time providing you a brief overview of Marqeta, the industry tailwinds driving our growth, and a few of our strategic initiatives.

Marqeta created modern card issuing, and modern card issuing is at the heart of today's digital economy. When you think of the cards in your wallet, these do very little and have seen little innovation in decades. Now imagine a card that can take any form factor you want it to, solve significant payment problems at scale, and disrupt entire industries: from authorizing transactions based on dozens of dynamic criteria to allow you to pay in installments, to creating a brand-new consumer or commercial experience. These cards can be physical, virtual, or tokenized into mobile wallets. They can be credit, debit or prepaid, all built by developers in days using cutting-edge tools instead of months. This is Modern Card Issuing. When you order food using DoorDash or groceries using Instacart, modern card issuing works in the background as money moves from the app to the delivery driver's card. When you buy a big screen TV and pay for it in installments using Affirm or Klarna, modern card issuing helps move money to the payment card used to seamlessly pay the merchant.

Some of the most disruptive companies of the last decade, such as Square, Instacart, Uber and Klarna use Marqeta technology at the heart of their products. We are the first modern card issuing platform, built from the ground up by developers for developers: in the cloud, with open APIs, and best in class developer tools. We believe we are the first to market with multiple issuing and processing innovations, including the first open APIs for building bespoke payment card solutions, Just-In-Time or JIT Funding, and Tokenization as a Service. These innovations put the control of designing great payments experiences in the hands of our customers, to enable them to launch unique card products in a fraction of the time that they could on legacy platforms.

We believe that Marqeta is now the ‘de facto’ Modern Card Issuing Platform and that our continuous innovation further cements and expands our market-leading position. We are deeply integrated with our customers in three ways: technical, experience and partnership. Marqeta’s technology underpins our customer’s core business or supports a core business. Our people are their trusted partners, as our solutions drive their key processes. Our deep experience serving the most innovative commerce disruptors, technology giants and financial institutions brings valuable issuing expertise to build and scale innovative programs. Additionally, we partner with our customers for long term success. Our usage-based business model provides a win/win for both our customers and for Marqeta: as their businesses thrive on our platform, our net revenue grows. Moreover, our customers are incentivized to bring new volume and launch new card programs on our platform as they benefit from volume-based discounts via tiered pricing. As a result, we have long-term contracts that promote and maintain alignment. Customer success is at the core of everything we do and “connect the customer” is a core company value. We build technologies for people who serve people. The strength and durability of our customer relationships are evidenced by our second quarter year-over-year net revenue growth of 76%.

We’ve managed to support massive innovation for these customers at a huge scale. Our platform operates at 99.995% uptime, while volume through the Marqeta platform has increased 30x in the last 4 years. We operate in 36 countries and growing. We believe the opportunity within payments and Modern Card Issuing is tremendous. There's a $74 trillion global money movement market, of which $30 trillion is global card issuing. The Marqeta platform processed $60 billion last year, which is a small fraction of the total card issuing opportunity. With the accelerating shift to digital payments, the market continues to expand, and we believe Marqeta has the modern technology, deep experience and momentum to capture a growing share of this market. We believe this TAM is a vast ocean of opportunity ahead of us as everything moves to digital electronic transactions -- changing the entire landscape of how the world is moving money in the future.

Marqeta is well-positioned to capture this large-scale opportunity in three ways. First, the shift to digital payments is accelerating. More and more transactions are moving online and when they are in-person, people around the world are increasingly choosing not to pay with cash. They are choosing to pay by card, or with contactless payments. This has only accelerated during the pandemic.

Second, payments are not only becoming more digital, they are also integrated more frequently into consumer and business applications. Think about the last time you used online food delivery, a messaging app, or a digital marketplace. Payments is deeply embedded as a part of the experience. Software companies are continually partnering with payments companies to provide simple, scalable, and configurable payment services to meet their end users' needs.

Third, consumers' trust in new payment technology is growing. Consumers are increasingly more confident about the use of online shopping and digital payments for safety and convenience. While the pandemic may have encouraged the use of services such as Instacart or contactless payments as a matter of safety, once consumers experience these conveniences, we believe they are unlikely to change back. Because of these three tailwinds as well as our eleven-plus years of experience, we are confident in our ability to further expand our leadership position in Modern Card Issuing.

The work we have achieved to date and our goal to be a generational business going forward is dependent on creating an atmosphere where our people can do the best work of their lives. To do this we have recently added two new leaders to the executive team in Darren Mowry, our new Chief Revenue Officer, and Randy Kern, our new Chief Technology Officer.

Both Darren and Randy have tremendous hands-on experience in scaling large enterprise businesses. Darren comes to Marqeta from leading AWS throughout EMEA, a business unparalleled for the innovations it has powered at scale and the same laser focus on customer success as Marqeta. Randy has spent almost three decades in engineering, almost all of it at Microsoft and Salesforce, building the technical infrastructure to support huge high-availability businesses. We’re excited to see their impacts on the company, and I have a strong belief that these are the right people to have on our executive team as we focus on capturing the huge market opportunity in front of us.

This quarter marks the first step in our life as a public company. We believe we are barely scratching the surface when it comes to modern money movement. We are excited about the opportunity in front of us and we look forward to a successful track record. With that, I'd like to turn it over to Tripp Faix, Marqeta’s Chief Financial Officer to discuss our second-quarter financial results

Tripp Faix

Thanks, Jason. Good afternoon, everyone. I am excited to talk to you today about our strong Q2 financial results and provide guidance for Q3.

Given that this is our first earnings call as a public company, I will talk briefly about our business model and some of the key points of our story.

We are a usage-based business, a transaction-based business, an interchange-based business.

We believe that Total Processing Volume or TPV, which increased 76% compared to Q2 of 2020, is a key indicator of the market adoption of our Platform, growth of our business, our ability to scale with our customers, and our customers' continued usage of the Platform.

TPV drives a majority of our revenue as we earn interchange fees from card transactions. We share those interchange fees with our customers so that our customers' interests are aligned with those of Marqeta's. Our customers are incentivized to bring new volume and launch new card programs on our Platform as they benefit from volume-based discounts via tiered pricing. This results in long-term contracts that promote and maintain our alignment. The amount we generate after our revenue share with our customers is recorded in our Net Revenue line item on our Income Statement. We also generate revenue from other sources: processing fees, monthly platform access fees, ATM fees, card fulfillment fees, and tokenization.

Costs of revenue consist of Card Network fees, Issuing Bank fees, card fulfillment costs and a contra-line item of network incentives. When looking at costs, it is important to know that through our strategic partnerships with the Card Networks, we receive incentives that are earned based on achieving certain volume milestones over the year.

Again, these network incentives are recorded as contra- cost of revenue, and therefore reduce our costs of revenue. Incentives can be earned in the quarter or on an annual basis. For certain incentive arrangements with an annual measurement period, the one-year period may not align with our fiscal year. This can result in variation in our cost of revenue between quarters. Finally, netting our cost of network fees, issuing bank fees, card fulfillment costs and our contra-cost of revenue network incentives gets us to Marqeta’s Gross Profit line item.

With that, I wanted to turn to our results for the three-month period ended June 30, 2021, and then discuss some of our Non-GAAP results.

Total net revenue increased by 76% to $122 million in Q2 of 2021 from $69 million in Q2 of 2020. This was a strong result that exceeded our expectations. The increase was primarily driven by the 76% growth in TPV. Our revenue share payments increased 78% from the second quarter of 2020. As a reminder, revenue share payments are incentives to customers to increase processing volumes on our platform. As a result, net interchange fees increased 68% to $95 million. Processing and other fees, increased 121% to $23 million in the quarter primarily due to higher ATM processing volume along with monthly fees and tokenization as a service.

Let me delve into our TPV for the quarter, which was $27 billion, an increase of 76% compared to the second quarter of 2020. This increase reflects outperformance from both our Digital Banking and buy-now-pay-later or BNPL customers, mitigated by tougher comparables from our on-demand delivery customers. First, in our Digital Banking vertical, it is important to note that in addition to the strong adoption of these products, we also benefited from the tax season filing deadline shifting further into Q2 from April 15th to May 17th. We believe the effect of that filing delay resulted in more spend shifting into the second quarter as people received refunds later. Second, our BNPL customers experienced 350% growth in net revenue compared to the same quarter of 2020, demonstrating both the growth enabled via product-market fit on our Platform and the adoption of this method of payment worldwide. Third, the quarter also represented the first time we encountered tough comparables in on-demand delivery as a result of the pandemic. Although growth for this vertical was down compared to previous quarters, absolute volume levels remained high. This is a testament to the enduring nature of changing consumer behaviors, strength of on-demand delivery services, and secular tailwinds in our industry.

Gross profit increased by 70% year over year to $47 million compared to $28 million from the second quarter of 2020. Gross margin decreased slightly from 40% in the second quarter of 2020, to 38% in the second quarter of 2021, primarily due to card network fee growth which was driven by the 76% increase in TPV and a 77% increase in the number of transactions offset by lower growth in our issuing bank fees.

I wanted to spend a little time on gross margin. Firstly, we remain committed to our long-term gross margin target of between 40% and 45%. We had a higher gross margin in Q1 2021 due to an annual recurring incentive payment from the networks. This lowered our Costs of Revenue and increased our Gross Margin by a few points. In Q2, we had higher network fee growth. Network fees can vary significantly by merchant, MCC code, transaction type, card-present or not, and the like. While we will not be providing specific gross margin guidance going forward because we are a usage-based business and our margins can vary quarter-to-quarter, we do not expect 38% gross margin as a run rate going forward and are very comfortable with our long-term target for gross margin between 40% and 45%.

Overall, our GAAP net loss was $69 million driven by our continued investment in people and technology and included $56 million in share-based compensation, of which $23 million was recorded for restricted stock units upon the consummation of our IPO. In addition, we recorded stock-based compensation of $5.8M for secondary stock sales which should be considered non-recurring.

On a non-GAAP basis, Adjusted EBITDA for the quarter was negative $10.6 million compared to a loss of $3.0 million in the comparable quarter of 2020. The growth was largely driven by compensation-related costs to invest back into the business to support future growth. As a note, we do view Adjusted EBITDA as a useful measure of our operating profitability.

We ended the quarter with over $1.7 billion in available liquidity in cash and marketable securities. Approximately $1.3 billion of that liquidity was the result of the capital we raised in our initial public offering. As Jason mentioned in his opening remarks, we are just scratching the surface of a large addressable market. Therefore, we believe that the best way to capitalize on that opportunity is to invest in our products, our technology, and our people.

I'll now move onto guidance. As we mentioned in our press release, we are providing the following guidance for the third quarter of '21 based upon our current assumptions.

Net revenue for the quarter is expected to be in a range of $114 million - $119 million, At the midpoint, this would represent growth of 38% on a year over year basis. Our range for Adjusted EBITDA is negative $16 million - negative $13 million.

Q2 was a strong quarter that exceeded our expectations. Q3 guidance reflects ongoing strength from our Digital Banking and BNPL verticals. We believe Q2 net revenue included a one-time benefit from the delayed tax season as I explained earlier; if we normalize Q2 for this one-time benefit, our guidance for Q3 2021 net revenue would have represented a sequential increase quarter over quarter. The midpoint of our Q3 net revenue guidance is 38% YoY growth as we will be one year removed from the Q3 stimulus of 2020. We remain very pleased with the growth we are seeing from both our largest customers and from our emerging customers, both in the near term and our forecast for the long run. In addition, our Adjusted EBITDA guidance takes into account increased headcount investment as we look to add additional talent primarily in our product and technology teams.

While we are not giving guidance for Q4, we did want to provide additional color. Historically, we have seen a positive bump in Q4 driven by increased consumer spending which has traditionally manifested itself in our Digital Banking and BNPL verticals - given the Q4 holiday season. In past years, we have also seen an increase in our Expense Management vertical due to travel - however, we remain thoughtful and prudent as we all grappling with the changing dynamics of the COVID pandemic.

In summary, we had a very strong Q2 overall and are very optimistic about the quarters ahead, our customers and the opportunity ahead of us in Modern Card Issuing. I would now like to turn the call over to the operator to open up the line for Q&A. Operator?