

Company Name: Paypal Holdings Inc
 Company Ticker: PYPL US
 Date: 2017-07-26
 Event Description: Q2 2017 Earnings Call

Market Cap: 70,665.58
 Current PX: 58.79
 YTD Change(\$): +19.32
 YTD Change(%): +48.949

Bloomberg Estimates - EPS
 Current Quarter: 0.422
 Current Year: 1.795
 Bloomberg Estimates - Sales
 Current Quarter: 3137.114
 Current Year: 12741.325

Q2 2017 Earnings Call

Company Participants

- Gabrielle Scheibe Rabinovitch
- Daniel H. Schulman
- John D. Rainey
- William J. Ready

Other Participants

- Daniel Perlin
- Lisa Dejong Ellis
- Ashwin Shirvaikar
- Tien-Tsin Huang
- Paul Condra
- Darrin Peller
- Bryan C. Keane

MANAGEMENT DISCUSSION SECTION

Gabrielle Scheibe Rabinovitch

GAAP and Non-GAAP Financial Measures

We will discuss some non-GAAP measures in talking about our company's performance

In discussing certain historical y-over-y comparisons, we have chosen to present non-GAAP pro forma measures because we believe that these measures provide investors a consistent basis for reviewing the company's performance across different periods

You can find a reconciliation of these non-GAAP measures to the most directly comparable GAAP measures in the presentation accompanying this conference call

Please note that as reflected in the reconciliation of GAAP net income and non-GAAP net income in the press release included in our 8-K filed earlier this afternoon, GAAP diluted net income per share for the six months ended June 30, 2016 was \$0.56

Daniel H. Schulman

Business Highlights

Revenue and Non-GAAP EPS

- I'm pleased to say that PayPal delivered another strong quarter of financial results, achieving new milestones for the company on multiple fronts

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- PayPal generated \$3.136B in revenue, the first time we've exceeded \$3B in a single quarter and representing 20% FX-neutral growth, nearly a 110-basis-point acceleration from Q1 and 70BPS from a year ago
- We exceeded our guidance and delivered \$0.46 of non-GAAP earnings per diluted share, up 27% y-over-y
- Our non-GAAP operating margin grew by 110BPS y-over-y to 21%
 - We generated \$747mm in FCF, up 51% from a year ago

Customer Metrics

- Perhaps more importantly, we had strong performance across our customer metrics
- We gained 6.5mm net new active accounts, the largest organic quarterly gain in the past three years and up over 80% from a year ago
- We ended the quarter with 210mm active accounts, including 17mm merchant accounts, growing our base by 12% y-over-y

Net New Active Additions

- Given our H1 results, we now anticipate our net new active additions will exceed 25mm for 2017
- Engagement once again increased, growing 10% y-over-y
- Our customers now transact 32.3 times per year, up from 29.4 times a year ago, and 31.7 times last quarter
- Our growing base and increasing customer engagement enabled us to pass another milestone as we processed \$106B in payment volume, exceeding \$100B in quarterly TPV for the first time
- TPV grew at a currency neutral rate of 26% y-over-y, accelerating 75BPS from last quarter

Volume Growth

- Our volume growth was driven by our leadership in mobile
- In the quarter, 34% of the payments on our platform were made on a mobile device
- PayPal processed approximately \$36B in mobile payment volume in Q2, up 50% y-over-y
 - This growth is largely driven by the exceptional and differentiated consumer experiences we enabled on mobile devices
- One Touch adoption continued to expand in the quarter with over 60mm consumer accounts opted in
- Merchant accounts accepting One Touch now number just over 5.5mm, growing by 500,000 in the quarter
- Venmo users sent and received \$8B in Q2, representing a 103% increase from this time last year as we continue to achieve increasing network effects in the Millennial market

Initiatives

- Based on the strong trends we are seeing across the business, we are once again raising guidance for revenue and EPS for the full year
- John will share more details about our results and guidance during his remarks

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- Our performance is driven by the cumulative effect of multiple initiatives
- We have fundamentally re-tooled our technology and infrastructure, leading to significant improvements in availability and developer productivity
 - We have meaningfully improved our core experiences and expanded our suite of products

Digital Payment

- Our overall scale is accelerating due to the network effects of our two-sided platform
- There is clearly a macro secular shift towards digital payments
- And our customer choice results continue to exceed our expectations
- We have completed the rollout of Choice across our on-boarding, servicing, and checkout experiences in the United States and over 13mm customers have opted into Choice
- With the data from millions of customers over multiple quarters, we are beginning to see clear trends resulting from our Choice initiative
- Choice has both simplified and clarified our customer experiences, which has meaningfully reduced the volume of calls into our customer service centers

OpEx Savings

- Despite our transaction volume increasing by more than 20%, our net call volumes into our global operations are down y-over-y
- The results of Choice, along with numerous other product improvements, will deliver significant OpEx savings over the course of our three-year planning horizon
- More importantly, customers who have opted into Choice had meaningful increases in overall satisfaction

Funding Cost

- As a result, Choice is driving a significant reduction in churn and a meaningful lift in overall engagement
- And consistent with last quarter, the impact on our funding cost continues to remain well within our expectations
- Based on the success of Choice in the U.S., we're pleased to be expanding this rollout into Australia, Canada, the U.K., and Japan later this year

Landmark Partnership Agreements

- Choice will also help to expand PayPal's presence in our customers' lives
- These opportunities are driven by the landmark partnership agreements we've announced with technology companies, financial networks, wireless carriers and financial institutions around the world
- In Q2, we continue to make excellent progress with our partnerships
 - We continue to expand our relationship with Visa, extending our partnership into Europe
- As most of you will recall, last quarter we announced an agreement with Visa that covered the Asia-Pacific region

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Visa

- Consequently, we now work around the globe with Visa
- And as part of our network agreements announced last year with Visa and Mastercard, we recently announced a new service that is designed to allow PayPal and Venmo users in the U.S. to instantly transfer money to their bank accounts via eligible debit cards linked to their PayPal account
- Finding faster and more convenient ways for our customers to get funds into and out of their PayPal accounts is a key part of our overall value proposition

New Strategic Relationship

- Throughout the quarter, we saw our relationships with issuers grow increasingly collaborative and productive
- For example, we are pleased to see leading issuers, including Wells Fargo and HSBC, actively marketing PayPal to their customer base, encouraging their clients to link their cards into PayPal accounts
- We also announced new strategic relationships with JPMorgan Chase and, as of today, Bank of America, to utilize their token services and enable their customers to easily integrate their cards into PayPal and seamlessly create a new PayPal account from their properties

Citi and Chase

- Furthermore, as part of our expanded relationship with Citi and Chase, we will make Citi ThankYou Reward Points and Chase Ultimate Reward Points available in our PayPal Wallet to be used as a funding source for consumers shopping at our 17mm merchants

Global Platform

- As I said on last quarter's call, it's hard to overstate the difference in the relationships we now have with companies across multiple sectors who many once viewed as potential competitors
- We are confident these partnerships would drive enhanced value to our mutual customers
- The accelerating and extensive scale of our two-sided global platform which allows consumers and merchants to transact instantly in new contexts, cross-operating systems, technologies and platforms, creates a strong foundation and it's very attractive to multiple partners

Open Technology Platform

- Our open technology platform has enabled expanded partnerships with Google, Apple, Facebook, and Samsung over the past few months
- These agreements benefit both PayPal and our partners by creating innovative consumer-focused experiences that connect their combined billions of consumers to new buying experiences enabled by PayPal's powerful platform

Google

- In April, Google announced an extension of our partnership to make it easy for consumers to use PayPal as a payment method in Android Pay wherever it is accepted, in store, in app, and online

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- In addition, Android Pay users on Google's Chrome mobile web will be able to seamlessly pay as the millions of online merchants that accept PayPal simply by using their PayPal account and fingerprint authentication
- Just like the deployment of One Touch, this great new checkout experience will be available to millions of PayPal merchants without requiring any integration work from the merchant, further extending the value we bring to our merchant customers

F8

- Also in the quarter, Facebook announced additional commerce experiences with PayPal that will be available within its Messenger platform
- At F8, Facebook shared that over one million joint PayPal and Facebook customers have already enabled our payments experience within Facebook Messenger
- Earlier this month, PayPal and Apple announced an extension of our iTunes integration, which means customers can now buy games, music, movies, and in-app purchases with PayPal on their iPhones and iPads, in the Apple App Store, iBooks, Apple Music, and iTunes stores in 12 countries, including the U.S., Australia, and parts of Europe
- We anticipate that this integration will expand to more countries around the world in the coming months
 - This complements our existing integration into Siri and Apple iMessage and marks a growing relationship with Apple

Strategic Partnership with Samsung

- Finally, we announced a strategic partnership with Samsung
- Users of Samsung Pay in the U.S. will be able to use PayPal to pay for purchases in stores using Samsung Pay's mag-stripe emulation technology, which is used at the vast majority of merchants that accept cards
- The totality of these partnerships reinforces the fact that we're becoming an underlying open payments platform and wallet for many of the leading technology platform, OEM, and wireless carriers around the world

Venmo

- We continue to make good progress in rolling out Venmo as a payment option for PayPal merchants
- As we shared last quarter, we are now introducing the ability for U.S. PayPal merchants to accept Venmo as a mobile payment option
- Venmo users are now able to use Venmo at an expanded number of PayPal merchants, such as lululemon and Forever 21, and I'm quite encouraged by the early results
- We expect that the ability to pay with Venmo will be widely deployed across millions of our PayPal merchants by the end of this year, and I look forward to sharing more details in the coming quarters

Sales Growth

- The ability to deliver new consumers and enhanced sales growth to merchants of all sizes is a key benefit of PayPal, especially as the world becomes more global and increasingly digital
- As of today, this includes bringing the power and reach of the PayPal platform to the expansive and rapidly growing Chinese consumer market

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- We are very pleased to announce that PayPal has signed a strategic partnership agreement with Baidu, the leading Chinese-language Internet search provider with approximately 700mm users
- This partnership allows Chinese consumers to pay with their Baidu wallet and PayPal at our merchants outside of China

China

- Beginning later this year, this partnership will provide Chinese consumers more ways to discover and buy from PayPal merchants in the U.S. and will eventually expand PayPal's entire global merchant base outside of China
- We expect this partnership to drive significant demand and additional cross-border trade over the PayPal platform

Acquisition of TIO Network

- In addition to helping our merchant customers, maximize their opportunities in the age of digital commerce, another key part of our strategy is helping under-served consumers join and thrive in the digital economy
- This vision drove our recent acquisition of TIO Networks, which adds bill pay functionality to our two-sided platform, offering consumers the ability to access a digital network and benefit from the convenience and speed of digital bill payments
- Last week, we announced that we have closed our acquisition of TIO Networks, and I'd like to take this opportunity to welcome Hamed and the TIO team to the PayPal family

Innovative Mobile Checkout

- Three years ago, we set off to transform PayPal
- Our goal was to create an open platform for digital commerce that delivered innovative mobile checkout experiences that blurred the lines between physical, online, and mobile shopping
- We set off to create an integrated suite of services, experiences, and APIs that could extend the power of our two-sided ecosystem to our merchants with little and often no integration work required
 - That vision has grown increasingly important to our merchants in today's rapidly evolving retail landscape

Leadership Team

- Our execution in support of that vision is yielding strong results and extending our leadership position
- Our efforts to place our customers front and center in everything we do is driving both scale and engagement on our platform, and has opened the door to strategic and productive partnerships that have extended the PayPal experience from multiple contexts in existing and new geographies
- But we know we are still in the early stages of our transformation, and we are just scratching the surface of the opportunities in front of us
 - We are fully committed to delivering improved core experiences and additional innovative and comprehensive solutions for our customers
- Helping our consumers and merchants to navigate the rapidly evolving and expanding digital payments landscape

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John D. Rainey

Financial Highlights

Revenue

- I also wanted to thank all of PayPal's customers and our employees worldwide for making this another great quarter
- As Dan discussed, we achieved several notable milestones in Q2 including, for the first time, processing more than \$100B of TPV and generating more than \$3B of revenue in a quarter
 - In addition, we saw accelerating growth in customer accounts, revenues, operating income, EPS, and FCF

Operating Income

- Our second quarter financial and operating results demonstrate the momentum in our business and builds on the strength of our recent performance
- Relative to our expectations going into the quarter, our revenue and operating income outperformed
- On the top line, we attribute acceleration in our core to strong account and engagement growth, enhanced user experiences that make setting preferences and choosing funding instruments intuitive, cross-border initiatives as well as increased functionality that allows our customers to use our products in additional context

Headwind

- In addition, though, foreign exchange rates continued to be a headwind in comparison to last year, they provided a benefit relative to our plans going into the quarter
- On the expense side, non-volume related expenses grew only 4.5%, approximately 25% of the rate of revenue growth
- Our team did an outstanding job managing cost, resulting in cost performance slightly better than our expectations
- At the same time, we continued to fully fund our key growth initiatives
 - This level of expense growth demonstrates our ability to scale with minimal incremental costs

Non-GAAP Operating Income

- Before I discuss the financial results in detail, here are some highlights for the quarter
- Revenue was \$3.14B, growing 18% on a spot basis and 20% on a currency neutral basis
- Non-GAAP operating income grew 25% to \$659mm and non-GAAP EPS grew 27% to \$0.46
- We generated \$921mm of operating cash flow, and FCF grew 51% to \$747mm

Payment Volume

- For Q2, our total payment volume was \$106B, up 26% on a currency neutral basis, consisting of U.S. payment volume growth of 27%, and the international volume growth of 25%

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- Our merchant services volume grew 30% on a currency neutral basis to \$91B.
- Merchant services represented approximately 86% of our total volume in the quarter
- Volume associated with eBay represented approximately 14% of the total, compared to 15% in Q1 2017 and 17% in Q2 2016

Venmo

- P2P continues to be a meaningful contributor to TPV, representing approximately 21% of total payment volume
- In the quarter, active accounts grew 12%, and we ended Q2 with 210mm active accounts
- Active account growth was driven by strength in our core PayPal business as well as growth in Venmo
- The number of payment transactions per active account on a trailing 12-month basis reached 32.3 with 6.8B transactions occurring on our payment platform over that period
- In Q2, transactions grew 23% to \$1.8B
- Revenue grew 18% on a spot basis in Q2 and was the result of an 18% increase in both transaction revenue and revenue from other value-added services
- The revenue growth in Q2 represents an acceleration of more than 100BPS vs Q1

Transaction Revenue Growth

- Transaction revenue growth was primarily driven by our core PayPal and Braintree businesses, and revenue from other value-added services was predominantly driven by credit
- For Q2, our transaction take-rate was 2.58%, a decline of 11BPS from Q2 2016, and our total take rate was 2.95%, down 13BPS y-over-y
- Approximately 75% of the decrease in both transaction and total take-rate was related to the increase in our P2P volume

Transaction Expense

- Increased stability in our transaction take-rate in Q2 is indicative of the balanced growth and the strength we are seeing across our platform as well as our ability to monetize experiences where we demonstrate a compelling value proposition for our customers
- Volume-based expenses were up 29% y-over-y
- Transaction expense was \$1.06B, up 31% y-over-y, driven primarily by increased funding costs across our core PayPal platform
- As Dan mentioned in his remarks, the increased transaction expenses we have seen from Choice have been well within our expectations
- Further, we continue to see benefits on both the top line as well as cost improvements from lower customer call volumes and servicing costs, validating our initial expectations
 - We are pleased to roll out these experiences to additional geographies in Europe and Asia

Consumer and Merchant Credit Products

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- Transaction loss in the quarter was \$185mm, or 17BPS of TPV compared to 18BPS of TPV in Q2 2016
- Loan losses across our consumer and merchant credit products were \$123mm, representing 26% growth, in line with the growth of our receivables portfolio
- Our consumer credit portfolio continues to perform in line with our expectations

Net Charge-Off Rate

- The net charge-off rate was 6.9% in Q2
- We ended the quarter with an aggregate gross receivables balance, including both principal and interest, of \$6.1B in our consumer and merchant loan portfolios and a total reserve of \$380mm

Other Operating Expenses

- Other operating expenses increased 4.5% to \$1.1B, representing 35% of total revenue, an improvement of 465BPS of operating leverage vs. the same quarter last year
- Both general and administrative and product development costs were flat y-over-y, and experienced their lowest rates of growth since separation
- Sales and marketing expenses grew 10% as we invested to support our brand strategies and Choice experiences
- For Q2 in a row, other operating expenses increased only \$0.10 for every incremental dollar of revenue, demonstrating the scalability of our platform
- Strong revenue and cost performance resulted in 25% growth in non-GAAP operating income to \$659mm

Non-GAAP Operating Margin

- Non-GAAP operating margin expanded 110BPS to 21% compared to Q2 2016
- GAAP operating income grew 16% in Q2 to \$430mm, resulting in a GAAP operating margin of 13.7%
- Both GAAP and non-GAAP EPS grew 27% in Q2 to \$0.34 and \$0.46, respectively

Cash, Cash Equivalents and Short-Term Investments

- We ended Q2 with cash, cash equivalents and short-term investments of \$6.4B
- We generated \$921mm of operating cash flow in the quarter, and CapExs were \$174mm, or 6% of revenue
 - This resulted in \$747mm of FCF in the quarter as we generated \$0.24 of FCF for every dollar of revenue

YTD

- Capital return is a fundamental component of our overall capital allocation strategy
- YTD, we have returned more than \$600mm to shareholders in the form of stock repurchases
- We now have approximately \$400mm remaining on our original \$2B authorization
- As announced on our last earnings call, our board has also approved an additional \$5B buyback authorization

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- In addition to focusing on enhanced capital allocation strategies, we are also committed to optimizing our capital structure

Credit Products

- As we've shared over the past few quarters, we're exploring alternatives to run our consumer credit business in a less capital-intensive manner
- We are encouraged by the discussions with potential partners
- And based on the progress we are making, the timing and structure of these alternatives are in line with our expectations
 - While we continue to assess more efficient ways to manage balance sheet exposure to consumer credit, we're also assessing strategies that will support the growth of merchant credit products

Working Capital

- We continue to introduce and expand financial services and tools to help small and midsize business customers start and grow their businesses
- Since 2013, PayPal working capital has provided in excess of \$3B in funding to more than 115,000 merchants
- PayPal working capital is a strategic offering to PayPal which drives merchant sales growth, increases processing volume, and reduces merchant churn rate
- We will continue to invest in our working capital business to provide innovative financial products to small and medium-size businesses

Guidance

Revenue

- I would now like to discuss our updated guidance for the full year 2017 as well as the guidance for Q3
- For the full year, we are raising our revenue guidance and now expect revenue between \$12.775B and \$12.875B, representing currency-neutral growth of 19% to 20%
- At current exchange rates for the full year, we expect currency translation to impact revenue by approximately 100BPS, resulting in spot growth of 18% to 19%

Non-Volume Related Expenses

- For H1 2017, non-volume related expenses have grown only 4.5%
- We are pleased with this performance, and it's indicative of the type of cost discipline with which we can operate going forward
 - This level of growth for our non-volume-related expenses is sustainable given the manner in which we are scaling our business and the changes we have made to our organizational structure
- At the same time, this very measured approach to expense growth gives us the flexibility to be opportunistic and make investments to drive our business going forward

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YTD Performance

- Given our YTD performance and our operating plans for the remainder of the year, we expect that our full-year non-GAAP operating margins will expand relative to 2016
- We are also raising our full-year EPS outlook by \$0.05 at the high-end and now expect non-GAAP EPS to be in the range of \$1.80 to \$1.84
- Further, we are increasing our FCF outlook and now expect to generate in excess of \$2.9B in 2017

Acquisition of TIO Networks

- As Dan mentioned, we recently closed our acquisition of TIO Networks and have included an expected impact of \$25mm in revenue for the remainder of the year in our full-year outlook with a negligible impact to our earnings
- At the high-end of the ranges we are providing today, our current full-year guidance represents an increase of \$225mm in revenue and \$0.10 increase in non-GAAP EPS relative to the initial full year 2017 guidance that we provided in January
- For Q3, we expect revenue to be between \$3.14B and \$3.19B and we expect non-GAAP EPS to be between \$0.42 and \$0.44

Net New Active Accounts

- I want to close with a few observations on the quarter and our full year outlook
- We saw accelerating growth across net new actives, TPV, and revenue in the quarter
- Net new active accounts grew by 80% and, on a currency-neutral basis, TPV grew 26%, and revenue increased 20%
- Our merchant services growth has been consistently in the 30% range and demonstrates we are continuing to grow our market share
- And while growing our top line, we expect to maintain disciplined expense growth, which allowed us to deliver more than 100BPS of non-GAAP operating margin expansion in the quarter
 - This performance gives us great conviction in our ability to deliver on our commitments for the year

QUESTION AND ANSWER SECTION

<Q - Daniel Perlin>: I had a question around the payment transactions per active account. I know they were up 10% and that's still a very strong number. It was down a little bit relative to the last quarter. I think it was up 12% and over the last six quarters prior to that it was up on average 13%. So I would've thought, given Choice and all of the kind of reduced friction that you guys have had, that you might actually see that number accelerating as opposed to decelerating in its growth. Is there any callouts in the quarter we should know about?

<A - Daniel H. Schulman>: Dan, it's Dan. Nice to hear you and thanks for the question. So I'm quite pleased with our progress on engagement. It is up 10% despite really what is an accelerating pace right now, which is kind of a high-class problem to have. We are seeing tremendous adoption across merchants and consumers into the PayPal franchise. As I mentioned, we think we'll exceed 25mm net new actives for the year.

In the past couple of years, we've taken our active user engagement almost seven transactions per user across the whole base. And if you look under the covers, which we've done here quite a bit, the news is even better, because the majority of our user engagement right now is coming from the core PayPal Wallet.

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And in many places, before it was coming from the growth of Braintree and core PayPal, but now it is being driven the majority from our PayPal core wallet, and that is a great news story for us. And if you look at our product growth and our core PayPal franchise over the last several quarters, we've taken multi-year trends that have been drifting slightly down in terms of their growth rate y-over-y, and we have bent those curves across pretty much every single one of our core products, and they are now up and accelerating.

So that is a piece of really good news that you probably wouldn't see from the number in and of itself, and I kind of feel like we're just at the beginning of this. We have One Touch that is driving engagement – that's driving increased engagement and it's accelerating across the base. Choice is still new, but Choice engagement, when somebody opts into Choice, that engagement is up quite substantially. And I am really pleased with what we are seeing from Choice. As I mentioned, about 13mm plus customers that are in Choice now, that will grow and that will impact engagement.

We're obviously just beginning the journey to move into new context. Now we now have basically major agreements with pretty much every major issuer, we've got agreements from the financial networks to utilize their tokens and they'll start to move us, move more into an in-store environment as we go into next year. That will also drive engagement.

You've got pay with Venmo. Right now, there are no engagement with Venmo, there's P2P, but we don't count that in our engagement total so you'll see that drive up. TIO just came on. Our new partnerships with Facebook and Google are going to start to kick in. That's really not in our guidance right now. Those things are going to start to accelerate and drive our future growth as we look into 2018, 2019, 2020.

So we still have a goal to have a consumer use PayPal two times a week. That is our goal. Not to drive it once a week, but to drive to two times a week. And I feel like with all the initiatives we have right now and the trending that we're seeing that over our medium to long term, that's within our reach. So feeling pretty good about where we are in the engagement side.

<Q - Daniel Perlin>: Yeah. That's fantastic. Can I just ask one other quick one? You mentioned all these strategic partnerships and they are plentiful. I'm wondering how you're viewing that from a trend perspective to bring down your customer acquisition cost as we think about the future. Thanks.

<A - Daniel H. Schulman>: Yeah. You violated the first cardinal rule of one question per – but it's okay. You got away with it and I admire that.

<Q - Daniel Perlin>: I'm increasing my engagement.

<A - Daniel H. Schulman>: Exactly. I see that. So, listen, one of the things that I mentioned in my opening remarks is we're beginning to see a tremendously collaborative relationship with issuers right now. We're seeing, I mentioned, two that are marketing to their base to actively encourage them to link their cards into our PayPal account. And that's happening because we're going to drive growth for them.

As John mentioned in his remarks, our [ph] MS (40:18) TPV – our TPV growth outside of eBay is growing at 30%. And we are the perfect digital distribution channel for financial institutions, especially now that we've implemented Choice and consumer will opt on how they want to pay and where they want to pay on that. And so, I think this acceleration of our net new actives is coming at a lower cost to us. So it's really kind of serve a one-two punch that's positive for us now especially as we look forward.

<Q - Lisa Dejong Ellis>: I had a question about in-store and your in-store strategy in light of the partnerships that you've signed. Can you kind of give an overall view of in which of these instances, like in Android Pay vs. Samsung Pay vs. using the network tokens in your own wallet, you are able to generate revenues for PayPal or envision that over time vs. where it's just a strategy of driving more user engagement at the POS even though it's not revenue generating?

<A - William J. Ready>: Hi, Lisa. It's Bill. So great question and you're exactly right that as you parse out the parts there are places where we earn revenue, there are places where you think about it as engagement opportunity. And so the places where somebody's paying in-store and they're using their PayPal balance, those are places where we would make revenue on those transactions. And places where we are enabling the use of an issuer's card directly and we're

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providing a pass-through token, we wouldn't earn revenue on those but we also don't have costs on those, and so we get great consumer engagement but without costs on those transactions per se.

Also importantly, in addition to what we're doing with partners like Samsung Pay and Android Pay to drive into the store, we're working with those same partners, particularly like Android Pay for example, where it's not just in-store but that blends into in-app purchasing and online purchasing, and there's a lot of blurring of the lines of online and in-store with things like buy online pickup in store where these cross-channel experiences are really getting to consumers using a mobile device, but really engaging with the retailer and the store. You see us really, really delivering on those types of experiences as well.

So we have a broad strategy that can both help the retailer engage across multiple fronts, drive engagement with the consumer, and we have several of those that we monetize directly and some of those that are going to be a pass-through, which would not generate revenue for us but would also not generate cost for us. So we have many of those, like buy online pickup in store, paying with your balance, where we do generate revenue on those things.

And by the way, this is consistent with PayPal history, where we have historically had products such as P2P that were free that we then monetize in other forms and so this is a strategy that we have employed previously and so we feel really good about where we are on that.

<A - John D. Rainey>: And just to add to that, Lisa, first of all, nice to hear your voice, hope you're doing well. And we spent a lot of time, as we've started to transition the company from being really single-product type of company to being a platform company that offers a suite of services to both merchants and to consumers.

And what we've found and we've done a ton of detailed research and analytics on this, is when we add an incremental service to a consumer, or even to a merchant, we see their lifestyle value basically double. And so if a consumer adds P2P, we see they engage more, their use of PayPal goes up, the churn goes way down, and it is a gigantic benefit for our flywheel and for our economics. And so the more products and services and experiences and more engagement we can have with the consumer and the merchant, the better the LTV is for us. And that comes through as Bill said, historically, as we've seen that with P2P and others.

We also have started in-store with trials – with Vodafone as we've rolled that and we've seen as people have used Vodafone and PayPal in-store, they use PayPal more in app and online, because the distinctions between those things are blurring, especially with mobile. And so, our ability to engage with consumers and drive that engagement is a good thing both for consumers, for merchants, and for the economics of PayPal.

<Q - Ashwin Shirvaikar>: My question is with regards to the rise in active accounts and the reacceleration of that as that has gone from 10% to 11% to 12%. Is that a straightforward relationship with consumer choice? Is it possible to potentially estimate? Is there sort of an untapped number of inactive accounts people who downloaded PayPal, but didn't use it, that can give us some idea of the potential to continue increasing these accounts?

<A - Daniel H. Schulman>: I'll start, and then maybe Bill can supplement. So I would say kind of as I mentioned in my remarks, there is no one single thing driving the growth of those net new actives, and as I mentioned, I said I think we'll do in excess of 25mm net new actives. That would imply that we're going to do another, on average, 6mm or so in the third and fourth quarter. So we see a continued strength in net new actives. That's coming as a result, and I don't want to say this, but I will, of the great work that Bill and his product and engineering teams have done, great work that Tomer Barel and the risk teams have done around improving our core experiences.

And as I mentioned, we are bending multi-year curves now and we are seeing now really nice y-over-y growth in our core experiences. Availability – just things like availability, is up. That matters a lot. Latency is down, that matters a lot. We've got a new mobile app there, we've got One Touch, we have Choice coming in. Choice is driving both a reduction in churn, which helps net new actives, obviously, but it's also driving additional new adds because the onboarding process is so much more streamlined. And then you also have partners that are now actively marketing PayPal because together we're sort of allies in advancing digital payments and tapping into that growth.

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And so, I think there is a number of things, and we also, obviously, with 210mm people now on the platform, we've got maybe at a tipping point on these network effects right now where there are so many merchants on the platform, so many consumers on the platform that it's a must-have for people, especially as they move into mobile checkout experiences. I think what Bill and the risk teams have done in things like One Touch have really been an unparalleled kind of a mobile checkout experience. Almost two times the conversion of the industry average. And so, I look at a number of things that we've done over the course of the last several years and they're beginning to take hold in the market and are really driving our results. And, Bill, would you add to that?

<A - William J. Ready>: I think you captured it really well just doing the points there. We have multiple new places that customers are coming in, but as Dan described, we have, across nearly every major product area, revamped those products over the last few years. And so we're seeing not only do each of those products tend to get more net new actives for us coming in, we're driving increased engagement across each of those. As people come in through those, they become more engaged on those products. And there's additional product that they can engage with, that also deepens our relationship with those customers, really leading us to more of their daily lives.

So, just as Dan said, it is across multiple fronts, and quite noteworthy that it's across our core experiences as well and we're deepening that engagement.

<A - Daniel H. Schulman>: Yeah. If I just – I just have one last thing and then we'll be done with your question, Ashwin. I wouldn't underestimate what could happen with Baidu, I mean, we are now tapping into that Chinese consumer marketplace. And that is going to open up a whole new market for consumers to come onto the PayPal platform, interact with our PayPal merchants outside of China and drive what we think could be substantial cross-border traffic. And I talked about this, it's not just Baidu, it's Baidu and PayPal. So it's almost a little like we've done with Android Pay, it's a co-branded experience, they sign-up to be a PayPal account from there. So there are a lot of things that we're working on, a lot of things we still want to implement, but feel good about the current trend right now.

<Q - Tien-Tsin Huang>: Good results and momentum. I want to ask about the – maybe the partner pipeline. Just any big partnerships out there still to sign and – in 2017? And maybe I'll ask about the acquisition pipeline as well and your appetite to do deals.

<A - Daniel H. Schulman>: Yes. So we've done, I think, 24 major partnerships in the last 18 months. And you've seen this last quarter, it started to accelerate, actually. And it's accelerating because I think people are beginning to understand the assets that we bring to our partners. We obviously bring a lot of scale to partners, and when you talk to different platforms, whether it be Baidu or Google or Samsung, the ability to tap into 17mm merchants we have, that long tail of merchants, that's a very difficult asset for others to replicate, and it's accelerating in its growth.

Now, if you look at other partnerships, you can add potential for pretty significant additional growth for them, whether that's driven by mobile or what we can do on One Touch or TPV, that's accelerating. And as you know, we also control the value prop end to end. There are very few players who do that there. There are some players that control a piece of it, but very few players own it, including risk, customer service, brand, reputation, and we own all of that and parts of the value proposition. And we've also changed our model quite a bit. We are an open platform and a suite of services, both branded and unbranded, that's operating system and device and technology agnostic.

And so – and very importantly, we're a neutral third-party platform. So we don't compete with any of our merchants or our partners, we're allies in advancing digital payments. So I think our positioning is really good within the entire ecosystem to continue to partner. There are a number of other partnerships that are on the horizon and I think the more we partner, the more people see that the benefit of doing that can be quite substantial. So, I think we announced enough partnerships right now, so we'll save some for the next announcement. But I think we're really well positioned on that front.

On the M&A front, because you got your two questions in there in a very subtle way, but on the M&A front, look, we have a very strong balance sheet. John mentioned, we have \$6.4B of cash equivalents on our balance sheet. We're generating – now our guidance is over \$2.9B of FCF for the year. So that's a competitive advantage for us. There's no

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question about it, and we're very active in looking at a range of opportunities around the world, both big and small. But, look, those opportunities need to tie in to our vision and our mission. They've got to accelerate our progress either against a key vertical or a geographic expansion.

We'll do tuck-in acquisitions from a tech or a functional capability like a TIO type of thing, but we look at this through the lens of do we build, do we partner, or do we buy? And the amount of work that Tomer and Bill have done on their respective platforms whether it's risk capabilities or our full infrastructure. I mentioned the increased developer productivity. We can put out a ton of releases, now we've got something like 30,000 releases in a quarter. I mean, it's amazing the velocity of new functionality and innovation that Bill and his team are putting out into the marketplace. And so what we used to have to buy at one-time because it used to take us months to make a change on our website because we had such a monolithic infrastructure, now there's a rapid velocity of very innovative services coming in.

The second thing is, we can partner now in ways that we never could partner before. Choice has enabled that. We have a new philosophy about cooperating with people. It's created an environment that's gone from a very competitive one to one that's much more cooperative. We have a ton of complementary resources that we can use with partners, and now many times where we used to think we'd have to buy something, we can now partner on a commercial relationship to go and do that.

And then, obviously, if we can't do any of that, we'll look at buy and we do that in a very disciplined manner. We've got a certain amount of scale and capabilities. And so, you can expect us to continue to be acquisitive, but in a disciplined fashion and within the context of what I just mentioned.

<Q - Paul Condra>: I guess, Bill, I just wondered if you can give a little bit more detail on Venmo, kind of what you're seeing as you roll that out in terms of the way consumers are using it. Are they potentially using a credit card? And then any merchant feedback, and just anything, any surprises or anything unexpected just to kind of help us understand where you're focus is as you're scaling that product out.

<A - William J. Ready>: Sure. As we talk about, in prior calls, we spent quite a long time really making sure that we had dialed in the customer experience so that Venmo would not just be another pay button but that the uniqueness of Venmo it's really gets to great mobile payments as well as the social engagement, and we'd have that dialed in as we took that from person-to-person payments into merchant payments.

We have been working through that for a year plus, and so we're really now in the place of taking those prior learnings which we've got to feeling really great about, and we're opening that up to the PayPal merchant base. So the really interesting thing that is happening right now is that we're saying for our Venmo users, we are lighting up PayPal merchant, allowing Venmo users to pay a PayPal merchant notably without PayPal merchants having to do any work, just like we rolled out PayPal One Touch, just like we rolled out Android Pay. And so, you're seeing us leverage that very unique distribution capability to PayPal merchants again to go deliver Venmo consumers to those PayPal merchants.

And so, we're in the midst of a ramp with that, but we're feeling really good about that. We not only had previously proven out that consumers on Venmo really wanted to use Venmo for more things beyond P2P, we have a number of merchants where we see really, really positive results in terms of how Venmo stacks up next to other payment alternatives, and those merchants we feel great about those things. We're now really focused on how we take that from where we are now with a handful of merchants to go take that to millions of PayPal merchants. And we started that journey already, as Dan mentioned previously.

We've started to introduce that. We have merchants like lululemon and Forever 21 that are now there. We have thousands of PayPal merchants now where you can use Venmo to pay and we expect we'll progress that towards the millions of PayPal merchants over the coming quarters. So we're feeling really good about those things. But the – would consumers want to do this, what was the interaction model, would they like it? Those are things that we've really spent that prior year testing out. So now we're in the mode of just thoughtfully scaling that and we're feeling really good about how that's going so far.

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<Q - Darrin Peller>: Just following up on this acceleration in partnerships, Dan, especially around the mega tech companies, such as Apple and Google, this past quarter. Can you touch on these partnerships in a little more detail? But more just – does this underscore any type of deeper meaning around the positioning in the payments ecosystem by any of these companies, just given there's always been a lot of questions over the competitive threats from some of these names vs. PayPal. Are they now more partnerships?

And then, John, just to sneak one quick financial one in. Pricing opportunities, I know that was a key driver potentially in the quarter. Is it still a driver? Or it's supposed to be a – it could be a driver in the year. How much more of that to go is there? How much of an impact in the quarter? And just maybe comment on that a little further. And again, thanks again, guys.

<A - John D. Rainey>: Sure. Darrin, I'll start and then kick it over to Dan. As we've talked a little bit about this year, pricing is an opportunity for us. We did announce a couple of corridors where we made price increases, and part of that is reflected both in our financial results for the quarter as well as our improved guidance for the year. I will say that we're very focused on really identifying where customers derive value enhancement as part of their experience and then pricing to that vs. just sort of arbitrarily going out and raising prices for something where there's no incremental value that's perceived by the customer. And so, we had some targeted initiatives that we've done, and that's reflected in our results as well as our guidance for the year.

<A - Daniel H. Schulman>: Yeah. And, hey, Darrin. So I'll start off and then I'll turn it over to Bill. But I think there's a real difference now with the partnerships that you've mentioned, major tech platform companies. I think, and none of them really wanted to go into payments as an end to itself. It was a means to an end that they had. And so, it might be more engagement on their platform, and that engagement could lead to key metrics that they want to drive, it could be advertising, it could be other things.

And when we made the shift to being an open-payments platform as opposed to just being a button as a checkout experience, and really opened our platform up through pretty sophisticated technological upgrades, through open APIs, with the partnerships we have, with tokenization, and that kind of thing, we were then able to become really in many ways an underlying payment OS for those tech platforms that enabled them to create the experiences that they wanted to drive for their end-user. And so, that partnership is fundamentally different right now. It has evolved greatly over the last several years. I'll ask Bill to add color to that. But it's a very different conversation that we have now than we used to have.

<A - William J. Ready>: Yeah. I would just add to that that, absolutely, payments was a means to an end, as Dan described, and what we have demonstrated is that, through unique two-sided platform that we have and our ability to connect consumers and merchants around the world and do so in a single touch, makes us very unique in being able to light up those experiences for those partners.

And so, not only did we make the strategic shift to say we want to be a more open platform to enable those things and improve our experiences so that we could do things like One Touch to drive industry-leading conversion levels to connect to those experiences, I think as mobile has matured and players have been able to see different alternatives in the ecosystem and see what consumers have affinity to, what drives better conversion rates, I think we are demonstrating consistently that the uniqueness of our two-sided platform, our ability to connect consumers and merchants lets us drive connection between consumers and merchants of all types, or consumers and tech ecosystems, in ways that others can't, or whatever their aspirations are, whether that's selling more apps or selling more devices or driving engagement with their experiences, we're generally able to connect users to them and those experiences in a lower friction way than anybody else out there. And that's why you've seen us really start to play a central role there. And I think as more and more of these interesting new experiences proliferate, every time that happens, I think PayPal is now positioned as a place where, of course, people would want to look first given what we've demonstrated we can do on those things.

<Q - Bryan C. Keane>: Just wanted to ask, lots of new partnerships. The Chase deal in particular caught my eye. Thinking about the ability for PayPal to process through ChaseNet. Doesn't that materially lower your funding costs with Chase cards going forward? And then just as a strategic bigger picture, maybe Dan, with all these partnerships, are

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we about to launch a big in-store campaign or opportunity? Or is it going to be more of a trial and error process?
 Thanks so much.

<A - Daniel H. Schulman>: Do you want me to go? Yeah. So I'll start off with that. Obviously we've worked closely with JPMorgan Chase over the last couple of years, actually, as we've talked about the potential for how we might work together. And I'm really pleased with where we came out in this partnership. We both see a lot of value in it. You have two very strong companies lending what are really impressive assets to create great consumer experiences, including, as you mentioned, processing through ChaseNet, which obviously does give the potential, we're not talking about any deal terms one way or another, but potential for lower costs on that. So I'm really pleased with the comprehensive nature of the partnership that we have with Chase. It took us time to work through all of the details of it. But I think both of us feel really good about it, and really good about what we can drive coming out of that.

<A - William J. Ready>: Yeah, and I would just add to that, again, without commenting on the deal terms for any one specific deal, the closer working relationship that we now have with the broader financial ecosystem, as you look through a broad lens of how you think about costs, whether that's customer acquisition costs, or risk and fraud losses, or all of these kind of things. We, as one of the largest drivers of digital transactions for banks and issuers and that being a place that is one of the largest drivers of growth for banks and insurers, the opportunity for us to collaborate across a number of fronts across the ecosystem is quite meaningful, we believe. And we see that across these partnerships that it's not just about what the cost of processing a transaction, but how can we think about delivering better digital experiences to customers, that has positive impact on customer engagement on customer acquisition costs, and how you think about the lifetime value of a customer, risk, all these things. The opportunity to collaborate with the ecosystem has many, many potential positives across a number of those things, and that is something we feel really encouraged by in the conversations that we have and the relationships we're building.

<A - Daniel H. Schulman>: I think you just think about things like Reward Points. Discover, Chase, Citi have all decided that utilizing Rewards Points within the PayPal platform to utilize those for purchases at our 17mm merchants. I'd say that is a real significant differentiation for those particular financial institutions and their customers who are using their instruments, but also for PayPal, because you now can utilize those Reward Points in a split transaction. You have X number of Reward Points but maybe couldn't do that full transaction. You can now split that, you can use those Reward Points to purchase 40% of what you're going to go do, and then the other 60% can be done through whatever funding instrument you select as a consumer. That's a lower-cost funding mechanism as well for us.

So there are all sorts of things within these relationships that we have that drive enhanced value for our regional customers that, if you parse through them, it's really quite significant and differentiated from where we were, certainly a year or so ago. Now the in-store stuff, we obviously now have the ability to use industry tokens from Visa, Mastercard, and others, and now we're working with each of the FIs to utilize their tokens for their particular instruments. And so, you'll start to see that just naturally began to roll out. There really isn't much of a trial and error per se on this.

We will have the ability for a PayPal customer or if they're opted into one of the bank services that's provided tokens, we'll use the network tokens with that, and you'll simply be able to use that instrument seamlessly across where actually it's accepted. On an Android phone, for instance, across an in-app experience, an online experience, or an in-store experience without us having to do bespoke customization of software at the point-of-sale terminal. And so that would just be a natural rollout utilizing existing POS technology.

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