MoffettNathanson
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OPERATOR: This is Conference #101918Moffett

OPERATOR: Good day, ladies and gentlemen, and welcome to the PayPal Earnings investor call. All lines have been placed on a listen-only mode and the floor will be open for questions and comments following the presentation.

If you should require assistance throughout the conference, please press star zero on your telephone keypad to reach a live operator. At this time, it is my pleasure to turn the floor over to your host, Lisa Ellis. Ma'am, the floor is yours.

LISA ELLIS: Terrific. Thank you. And thanks, everyone, for joining us. And thanks to, John Rainey, the CFO of PayPal for doing this virtual fireside chat after PayPal reported their earnings yesterday evening. John, thanks for joining us.

JOHN RAINEY: It's my pleasure, Lisa, thank you for hosting it.

ELLIS: Of course. And thanks to everyone on the phone. I know many of you sent in questions. We have curated that list and have it ready to go. We have John all warmed up to power through the list.

If, of course, any of your questions that you had sent in don't get answered on the call, please follow-up with me or with the I.R. team of PayPal and we will, of course, get back to you because we had, probably, many more questions that came in than we'll be able to get through in the next 45 minutes.

So John, why don't we just dive in? Last night, you laid out your 2019 framework. What are the major headwinds and tailwinds from your perspective that are assumed in that 2019 framework, including the impact of acquisitions, Synchrony, Venmo, et cetera?

RAINEY: Sure. So let me start with the headwinds. As we've called out many times, we'll still be lapping the sale of our U.S. consumer credit receivables portfolio for the first two quarters of the year. And so that'll have a similar impact on revenue growth, about three and a half percentage points next year on the full year basis, seven percent in each of those quarters roughly. And so that represents a headwind.

And then as we integrate the four acquisitions that we've made thus far this year, that'll represent about 8 to 10 cents of dilution. And so, we'll need to overcome both of those headwinds.

One the tailwinds side, obviously from a revenue perspective we'll have the benefit related to the acquisitions, which we said was about a point and a half of revenue yesterday. We'll continue to see operating leverage in the business. Continue to make really good progress there, demonstrating the sustainability to grow our platform at a very low marginal cost.

And I think we could -- we'll talk about maybe later some of the cost metrics in the most recent quarter. But I think that's very representative of what we're able to do going forward.

And then, there's a ton of initiatives that we have as we integrate partnerships and we look to expand with other partners that are not yet announced. And there's a lot of stuff in the pipeline that we're excited about. We'll continue to move forward with that and look at expanding our footprint internationally as well.

The last thing I would say is that the merchant lending part of our business, keep in mind that in the most recent quarter we had the results from Swift, which a year ago we did not have. And so, we see good growth there but that'll continue to go into 2019, although not at the same rate of growth that we saw in the most recent quarter because of the comparability issue there.

ELLIS: Got it. OK. And how -- just double clicking a little bit, how should we think about the 2019 margin outlook? Do you see the inorganic impacts of the headwinds being offset by core operating leverage and what are the cost line-item drivers of that?

RAINEY: Sure. So if you were to take our guidance of 17 percent revenue growth with 20 percent EPS growth that would imply roughly, I think 50 basis points of margin expansion -- if my math's correct. I'm doing this on the fly.

But we continue to believe that there's great opportunities to continue to expand margin. And that's what we said and gave our guidance over the next five years at investor day.

But we believe that each year we can expand margins, obviously from one year to the next there'll be certain pressures on that like we see in 2019 with integrating those acquisitions. Some will be more dilutive than others.

I think importantly for us, when we look at the composite of those four acquisitions, they'll be accretive to our earnings in 2020. Incrementally, there'll be a new set of acquisitions that we have to integrate that year. But certainly, the margins in our business want to go up. It's just the scalability of our platform, that's just the pure math of it.

But we're not going to drive just for that, because we've got such a precious growth opportunity in front of us we're going to continue to invest for growth, both organically and inorganically.

ELLIS: And specifically when it comes to eBay and Synchrony, I know -- and, I guess, kind of continuing with the rollout of Choice -- those three discrete items all had, kind of, specific costs associated with them. Can you give us a sense of how much of the OpEx base is going to come off as a result of those three areas?

RAINEY: Sure. So let me take each of those individually.

Synchrony, we are continuing to serve that business in a transition agreement. And that'll happen for two more quarters. After that, we'll completely transition that to them, the servicing aspect of that.

And so, we do retain a reasonable number of employees for that today. And so, we'll see a cost reduction related to that in the second quarter next year. So that's the first piece and that's built into our guidance.

On Choice, I presume you're asking about the impact of that on transaction expense. And with the line of sight that we have into the movements here, both the puts and the takes on what's happening with transaction expense, I'd expect it to stay in the same range that you've seen this year.

Roughly, take maybe a little wider range, 95 to 100 basis points, so it's a good way to think about our business over the next six to eight quarters which we have a pretty good line of sight into. And not to suggest that it should change appreciably after that, just the margin of error in forecasting goes up.

And then with eBay, eBay will I think be more of a gradual transition. Each quarter it seems that our volume on that -- with our eBay business, kind of comes down about -- we look at about 200 to 300 basis points a year is what we're seeing. So that kind of works its way through our system through things like customer contacts.

So an example would be if you think about an eBay transaction. Oftentimes, you're taking an unknown buyer and an unknown seller and putting them together. That is the most complex transaction from a risk perspective. And so, we tend to bear more costs related to that.

And many times, because of the risk decision that we make, it results in a contact to our customer service center. So you'll continue to see more of a gradual decline on those versus what is maybe more of a step function change like what we're talking about with Synchrony.

ELLIS: OK, let's switch gears over to growth and some of the TPV metrics. So in the quarter if we took your FX neutral TPV growth rate and then subtract out P2P as well as eBay, it looks like that core underlying TPV decelerated quarter-to-quarter.

How should we – realizing that there's some TIO contribution to that, how should we think about where that kind of core TPV volume growth should bottom out and potentially reaccelerate?

RAINEY: Sure, so it does look like that from a reported perspective, but the entirety of the deceleration in TPV is related to TIO and foreign currency. And so, if you actually subtract that out, it's actually an acceleration from the previous quarter.

We get asked a lot of questions about TPV because we don't tend to guide on that as much as we do other items, but as we look at sort of the what's going on in our business, we still continue to expect TPV to grow in that mid 20 percent range like we have over the last several years.

ELLIS: Got it, OK. And then in the U.S. after the success over the last couple of years, you're now hitting penetration levels where it seems like we'll see slowing growth unless you continue to accelerate transactions per user.

I guess could you just update us on how important of a priority and what is the path to getting that transactions per user up from the current three times a month levels to more like three times a week or higher?

RAINEY: Sure, sure. So you're right in that if you look at our penetration of digital users in the U.S. or really core markets for that matter that you could apply the same to like a U.K. and Australia, Germany, even Canada.

We're about a third penetrated into those markets. And so, the opportunity there not to say that we don't believe we can get more penetrated, but certainly as you look out over the next three to five years, there'll be an emphasis on increasing that level of engagement.

And you're seeing that already sort of – pockets of that already. So one example I would point to is Venmo where we talked about the level of month-over-month growth in Venmo, and in particular we cited Uber and Uber Eats.

And what we're seeing on pay with Venmo and even Venmo debit cards is a use case where people are using these in things like restaurants and grocery stores, which are every day use cases, which historically has not really been what PayPal has been used for. It's been more for that more infrequent, online transaction.

So I think as we sort of expand our ubiquity and provide our customers an opportunity to shop with us or shop using us, in many different ways we'll continue to see that engagement improve over time.

And I'm very encouraged just by our most recent numbers. As we see like in the most recent quarter, we had almost a 10 percent. A nine percent increase in the transactions per active, and that's in a quarter where we added the largest number of net new actives than we ever have in our history. So I think part of it is just the relevance of PayPal is becoming more pronounced.

One last thing I'd like to say on this before we move to the next question, but the Amex example I think – or the Amex relationship that we announced is a really good example of how we can increase engagement.

When you think about the opportunity going forward where an Amex cardholder in the Amex mobile app can now pay a friend or a peer through Venmo or PayPal. That helps with that every day use case.

Moreover when that very same customer has the opportunity to redeem their loyalty points or membership rewards points at many of the merchants that we have around the world, again, helps with that level of engagement where we're just – we've got so much greater opportunity than we have in the past.

ELLIS: Got it, and then looking beyond the core markets – U.S., U.K., Australia, Canada – as you mentioned, in many other markets you face sort of a chicken or egg issue where there's perhaps a local wallet player or you don't necessarily have the P2P footprint or the incubator of eBay.

So how do you – what's PayPal's strategy to overcome this issue in those markets and do you envision getting to a level where you are outside the U.S. subscriber growth or net new active growth is kind of comparable or higher than that in the U.S.?

RAINEY: That's a great question, and I would generally agree with the point that you're making there in that I do think as we look forward over the next several years, a lot of our net new active growth is going to come through these international markets that we don't define as core today.

India is a great example. This is an organic growth opportunity versus inorganic, but when we look at the uptick in our net new actives in the most recent quarter and we compare that to a year ago, one of the key differentiators is India.

India is a place where we're adding a lot of net new actives. So I think just as a general rule we would expect a lot of the net new active growth to come in some of these underpenetrated international markets.

To the first part of your question about the chicken and egg problem, it's – I can't be dismissive of that. That's the challenge that everyone that's trying to compete with us has, right? It's very, very difficult to organically develop that two-sided network and we compete with many other prominent players in these other markets.

And so, rather than focusing on kind of an organic strategy, this is where I believe we can use our balance sheet and our cash generation as an asset and a competitive weapon if you will where we can go out and be a natural consolidator in some of these areas.

Buy some companies or make investments in companies and partner with them so that we can penetrate those international markets that are faster growing in terms of digital commerce and what we see in our core markets and still have a nice share of that market.

ELLIS: Well, speaking of partnerships, let's talk for a moment about the Walmart announcement that you made. Give us a sense for where this is going. Is Walmart just the first of many of these partnerships that you envision striking with retailers centered around the underbanked and unbanked?

RAINEY: Sure. Well, we're exceptionally pleased with the announcement we made around Walmart, and it is kind of a first step in this next chapter for PayPal. A lot of focus was on where are we going to get additional growth when eBay announced they were embarking on their own payments experience.

This is an example of that, and hopefully we can build upon that not only with Walmart but with many other large players in this space as well. But very important for us to the point of your question, this is an example where our mission around financial inclusion really comes to life.

As you are well aware, there are many people, in the billions, depending upon what metric you look at, that are underrepresented in terms of what they have access to financially. And the partnership with Walmart effectively provides on ramps and off ramps for this demographic that doesn’t have access to the digital economy.

And so you can now upload cash into a PayPal account or withdraw cash from a PayPal account at a Walmart brick and mortar facility. And this effectively will give access to many people that today may not have a credit card or a debit card or for that matter, even a bank account, to go out and shop and enjoy digital commerce like everybody else does.

ELLIS: And can you give us a sense for how the partnerships that you’ve signed so far, so things like in addition to the Walmart one, of course the American Express one and then the Google one you announced earlier or the Baidu partnership. How do you think about how that flows into your core volume growth or other metrics?

RAINEY: Sure. It's more of a sort of a linear trajectory, if you will, but the series of step function changes. But this is really what gave us the conviction, post the eBay announcement earlier this year to give the guidance that we gave over the next three to five years because we’re in discussions with these players all the time and we recognize their interest and their appetite for partnering with us.

And I think if you look at the most recent quarter, the 9.1 million net new actives. I mean, a big part of that is the ease of use that it gives to PayPal today that didn’t two or three years ago. And so it's difficult to say like, I'll make up a number here, but 25 percent of the net new actives came from this partnership.

I think it all kind of bleeds together by not only the partnerships that we’ve announced but also the improvements we’ve made in the product and the ease of moving money or uploading a financial instrument into the PayPal wallet, all this works together and really puts us on a completely different trajectory than we were just a few years ago.

ELLIS: And can you give us a sense for sort of rate and pace of the drumbeat here? I mean, we’ve now had two big ones in the last couple of weeks, should we be expecting a number more announcements, sort of between now and the end of the year?

RAINEY: Well, I certainly don’t want to preannounce anything...

ELLIS: You're welcome...

RAINEY: ...but we are by no means, done, and I would apply that to both partnerships as well as acquisitions. There's a huge opportunity out here for us and you're seeing the receptiveness of companies like Walmart to partner with us or American Express, because of what we can do together.

And that's the fundamental change, Lisa, is that it has happened over the last couple of years is, by turning what were formally competitors into people that are partners and want to grow their platform with us, there's a much greater opportunity to capture this enormous addressable market.

And the same exists with acquisitions. We're not going to hit pause here. We've got a good balance sheet and we're pretty unique in the amount of cash generation that we have for a company that's growing at our rate. And so we can put that to use and use it as an asset as we compete in this space.

ELLIS: OK, well now the moment everyone's been waiting for, I will finally ask you about Venmo and Venmo monetization.

But I'll start off with maybe the one I've gotten the most frequently is, look, on one hand, your commentary around the timeframe of Venmo monetization has been relatively cautious, measuring that in years, not imminently, and yet last night, Dan referred to being at a tipping point when it comes to Venmo monetization. So can you just help kind of reconcile those statements or give us -- yes, I'll leave it there.

RAINEY: Well, I'm always going to be cautious, that's my nature. And certainly, I don't think we want a CFO that's getting out over their skis on some of this stuff. But I guess just to level set, Venmo loses money today.

If you look at -- if you were to assemble a full P&L of Venmo, it's not profit-making today. And what Dan alluded to in terms of an inflection point is the confluence of several things coming together where we're just seeing before our own eyes, sort of the expectations that we had before.

And an example of that would be in September, we had $1 billion, $1 billion of volume on the Venmo platform that participated in instant cash withdrawal. And so we recently announced a price change there of charging 1 percent for that.

So you can do the math and see what that would mean on an annual basis, right? So that's one aspect. And that it, to be clear, of the monetization alternatives today, that is one that we are realizing the most of, its through the instant cash.

But Pay with Venmo is something that we're seeing really good growth with and the numbers that we quoted yesterday in terms of -- an excess of 300 percent growth on Uber and UberEats, you see these use cases coming to life.

And that really came about, and one of the reasons Uber was so eager to do that is, we could see in the social feed on Venmo what people were spending money on, and we shared that with

Uber, and they're like, gosh, we want to have this is a payment option. And again, the use case being restaurants and grocery stores, things like that, it just gets us pretty excited about Venmo.

And then lastly, the card. And the card is, again, we've seen tremendous demand for that. And a lot has been made of offline strategies and what happens in terms of tap and pay or things like that. I think that is slower to play out in terms of offline moving into digital commerce.

And so we've got a great alternative with a Venmo debit card where many of the experiences that the Venmo customer base shares are in the offline world, and this gives them the vehicle to actually use that, use Venmo, and we get to monetize it as well.

And so I'm not going to be so bold as to put a time frame around when this becomes profit making versus the position that it's in today, but I would say this is pretty consistent with the way that we thought about this all along. We're just really excited to see these things coming to life, all these experiences at the same point in time.

ELLIS: OK, and so as we look out, say, over the next four quarters, will the primary monetization vehicle for Venmo continue to be the instant transfer-related revenues or do you think you're seeing enough trajectory, realizing its coming off a very small base in terms of the Pay with Venmo that will be a component as well?

RAINEY: Well, so as we think about the buckets of profit or benefit that we receive today from Venmo, sort of with instant transfer being first, and then second being debit and pay with Venmo.

There will be a gradual shift where eventually those will shift. And ultimately we would expect Pay with Venmo of those to be, presumably by a large margin, the largest of all of those in terms of the benefit that we've received.

I don't want to put a time frame on it in terms of when that inflection point will happen. Again with Pay with Venmo this is something that we've talked about being measured in the roll out. We recognize it's a great opportunity. And we want to get the experience just right.

ELLIS: All right. Sure I could keep asking questions all day about that. But I'll move on to the far less glamorous topics like take rates and transaction costs. Can you talk a little bit about on the take rate side, just the underlying trend in take rates once we strip out both the P2P impacts as well as your hedging gains impacts?

RAINEY: Yes, it's pretty consistent. So, maybe said another way if we were to quote this on kind of a same store sales basis it's pretty flat, and that, it's just that a couple basis points each quarter of decline.

But almost the entirety of our decline in take rates over the last several quarters generally has been either free P2P or in the most recent quarter the impact from the sale to Synchrony has an impact as well.

And then hedges tend to vacillate positive or negative from one quarter to the next. And then if you just take what's left, it's really the mix of our business. With maybe certain parts like Braintree growing faster than others.

And that element results in a couple basis points of decline from one quarter to the next. If you just – if were to take just merchant X, that is maybe a small to medium sized merchant. We're not seeing really any pressure there on take rate. It's – those have been pretty flat.

That said we do recognize that there's a lot of competition here. And there will be pressure in certain entities where that may come down over time. But at the same point in time we're providing more and more opportunities to monetize different services to merchants.

And as we move towards more segmented pricing you can imagine merchants that might be willing to pay for enhanced services like risk as a service or other complementary aspects that we add to the platform. And so I kind of expect, sort of more of the same with take rate.

I don't necessarily think we're going to see something dramatically different over the next few years. I think P2P will continue – or free P2P will continue to put pressure on that. As we begin to monetize Venmo that'll help buoy that, that number a little bit.

But then changes in mix and other things like that will add a few basis points of decline. But certainly there's not an expectation that we're going to see a dramatic shift going forward from what we've seen in the past several quarters.

ELLIS: And how sensitive are the take rates to FX dynamics? Like meaning impacting cross border volumes.

RAINEY: Sure, well maybe not focusing so much on take rate but just volumes in general. But they are sensitive – you know and you can see that in our results in the most recent quarter. And I'll give you a couple numbers to kind of point to. So our international revenue growth in the quarter was 15 percent. And that was a seven point decline from a year ago.

All right, U.S. revenue growth was 13 or 14 percent, 13 percent. Now to be clear that was, that had the impact of asset light in it. So if we were to adjust for that, to really look at what's really happening in the U.S. that would be 25 percent. So let me reframe those numbers. You've got 15 percent growth internationally, 25 percent in the U.S.

And a big part of that is what's happening around the currency environment. You know we often talk about the translation effect to earnings from movements in currency. But there's an effect on consumer buying patterns as well. And the example I provided yesterday I think is a really good one.

Australia is a fantastic market for us. We have very high penetration there. But the Australian dollar depreciated seven percent against the U.S. dollar in the quarter. And we – and so when we look at Australia sent volumes, they were – they declined notably because in part of the U.S. dollar being much more expensive.

And so there are always pockets or regions around the world where we see the effect of that. And so when we look at corridors in the recent quarter that affected that international growth of the getting to 15 percent, they were strongly correlated to where there was a weakness in that currency relative to the dollar.

Now importantly that goes both ways, right? And one of the things that we want to do is make sure that we have a, let's call it a natural hedge to our portfolio. So that -- and I think you see that with the U.S. revenue growth in the most recent quarter.

And we want to continue that going forward so that we're not susceptible to any shock because we've got a huge imbalance in terms of our footprint around the world.

ELLIS: OK, and how about on the transaction expense side? Transaction expenses had up ticked last quarter. They down ticked down again. You've got these kind of countervailing trends of likely continued increases in credit card mix in the U.S. post choice.

But at the same time P2P and also international growth with the lower interchange rates help that number. So where are you like netting out on that kind of trend line on transaction expenses?

RAINEY: Again Lisa, I think this is an area that should be pretty steady from here. We don't expect an appreciable change. You know we see certainly with P2P, Venmo things like that there's a strong likelihood that someone is funding that transaction with ACH or balance, or a debit card.

All very low cost funding instruments. Take a Venmo user, they begin to shop in the store and if they have a larger purchase, we certainly see just like our behavior, you might use a credit card for that. You might want to earn points on that transaction.

And so when we look at the presentation and all the balance there that still sort of nets out in the range that we see today. So I would expect that, that high 90's basis point number to continue to for the foreseeable future.

ELLIS: OK, and then moving down the income statement. Can you hold non transaction OPEX in this mid single digit range over the next three to five years?

RAINEY: Yes, yes very clearly. You know the – and when we say mid single digits to be clear, I don't really think of that as let's say three to six or seven percent. It's more kind of the five to eight percent range.

Now that's, to be clear, on an organic basis. Acquisitions will always put pressure on that, but as I'm thinking about how to manage the expenses of the company, business as usual, on an organic basis, that's where that expense for us should be.

Another way to think about it, and you – and I know all of you have heard me talk about this a lot, but I'm very focused on the incremental profitability of our growth. And so, I talked about the incremental opex or non-transactional related expenses for every dollar that we bring in.

And in the most recent quarter, on an organic basis, that was 10 cents. So for that (ph) – I mean for every incremental dollar of growth that we brought in, from a revenue perspective, those non-transactional related expenses went up a dime – 10 cents.

The right way to think about our company, going forward, is that should be in the 10 to 15 cent range. And at that level, we're not starving the business of investments, and – but we still demonstrate that we can scale it a little more to a cost.

If we get below that, or let's just say that we get to the 2 to 3 percent expense rate of growth, I actually think that's too low for us, because there are too many opportunities that we have to invest for growth.

And at that point, we'll probably make a suboptimal decision to manage to a cost number. And so, the natural rate of growth for us, that still shows cost discipline, is in that mid to high single-digit range that I talked about.

ELLIS: OK. And then the last balance sheet-related question; there's been an uptick in the loan growth coming off the Swift acquisition, in terms of your merchant working capital loans. So how should we be thinking about the expansion of the loan growth on your – on your balance sheet over time, going forward?

RAINEY: Sure. So let me start by saying that, if we're looking at year-over-year growth numbers, we're looking at a quarter this year, where we didn't have the acquisition of Swift. And so, the year-over-year growth numbers will not be this large.?.

And maybe another way to state that, is if you look at the absolute amount of other value-added services revenue that we had in the third quarter, we expect the fourth quarter to look pretty similar to that, just on an absolute number perspective.

But Swift, as well as international consumer credit, continue to be good growth opportunities for us that are also pretty high margin. That said, I certainly want to allay any concerns that people may have about, they just – they just sold this U.S. consumer credit business, Synchrony.

Now they're getting right back into the same situations they were in before, where maybe they're too dependent upon credit. That's not going to be the case. As we demonstrated with Synchrony, we can complete a transaction, to make sure we that we do this in a asset-light way.

And so, you'll see, when we release our Q next week, that the total amount of credit balance outstanding, on the merchant side, is about a billion and a half. And if you add the international consumer credit, that's another $500 million getting you to $2 billion.

We’re not going to let that get appreciably higher than that, without looking at other ways to offload some of that risk and the capital intensiveness of that. So we’ll continue to do asset-light transactions, going forward.

ELLIS: OK. Switching gears over to the eBay transition; a couple of quick ones here, to help to dimensionalize this impact. Let’s start with, actually, the primary impact to your earnings and top-line from the eBay roll-off will be in 2020 and 2021.

What are you assuming in your medium-term guidance around that eBay roll-off impact, and what are the offsets to it?

RAINEY: Yes. So we have not been explicit with the exact assumptions on that, and there’s a range of outcomes. But based upon our experience, which we have hard facts on this, in terms of when we transitioned – or I should say when other marketplaces have transitioned to payments, that, one, takes a long time, and two, we retained a sizable portion of the payment volume because of customers’ preference for using PayPal.

And so, our medium-term guidance assumes that we’ll maintain some share of payments, and as you know, we have an extended agreement with eBay, post-the operating agreement which protects that.

At the same point in time, we believe a lot of that volume is going to be backfilled with other agreements, for example, like what we have done with Walmart, or could do with Walmart and other large companies and marketplaces.

And so, there’s, I think, a tremendous opportunity for us to go out and partner with others in this space, to backfill a lot of that volume. And as we’ve demonstrated, and I think it’s important to note that this is not based on speculation, we’ve been doing this. We’ve been transitioning off of eBay, each quarter, for the last several years.

And we continue to show that we can expand margins. And so, whether this happens in a perfect linear fashion – of course it won’t. There’ll be bigger deals that are now implemented, but when look forward five, six years from now, we believe that we can produce the type of financial results that we talked about when we gave our medium-term guidance.

ELLIS: And can you – are there examples of where PayPal is operating as like the – in the full merchant of record role with other large retailers in marketplaces, sort of analogous to what you do with eBay? Or was that just a very unique situation? And then as you look forward, do you now anticipate that you’ll do more like that?

RAINEY: Yes. So there are not other examples; that was pretty unique situation. And it’s not to say that being MOR, or merchant of record, is the endgame here. It’s really the partnership with these fast-growing marketplaces – that are growing much faster than, in this case, eBay.

Whether that is merchant of record or not is actually kind of less important to us. You can have good economics, being merchant of record, or you can have good economics if you're not merchant of record.

That really comes down to how that partner wants to handle the payment experience. And that's something that I think we're very adept at, and we've shown that we bring a lot of value to bear, when we do provide that. But others want to be more involved with that and control more parts of that payment experience.

Some of the conversations that we've had with other companies, they'd rather turn that over to us. So it's one of the main things that you negotiate when you do an agreement like this, and not to say we're all that shaked out, but that, I want to address the fact that that is not the endgame, is to be merchant of record.

ELLIS: OK. And in the eBay situation, can you dimensionalize for us what the – what – at least roughly speaking, what you expect on the change in take rate, as you transition away from being merchant of record and then the offsets on the cost side, because clearly you're bearing a bunch of additional cost as well?

RAINEY: Yes. I'm only willing to say, Lisa, that the agreement that we have with eBay today was obviously not an arm's-length transaction between two individual companies in the marketplace. It was part of the transition agreement that we contemplated over the five year period after the spinoff.

When we move to the next chapter after that operating agreement expires, the take rate that we will enjoy will be more emblematic of a marketplace transaction of an arm's-length transaction that is out there today, reflecting the type of volumes that eBay has on their platform.

In terms of the cost, I alluded to this, so I talked about this earlier, but we bear a lot of cost around customer service, around the risk parts of our business to support that business.

And so, between those two areas declining as well as just the additional growth that we expect through this period of time and our ability to scale at a low marginal cost, I believe that we can still expand operating margins through that transition.

ELLIS: All right, I'm going to power through a couple more here before we run out of time. I'm going to jump to Braintree. You included a page in your presentation last night on Braintree for the first time.

So, I guess the question is what motivated your inclusion of these metrics around Braintree? And then also, just can you comment on the growth rate of Braintree transactions and sort of the competitive dynamic in that space.

RAINEY: Sure. So, we always try to provide the investor community the information to make them – give them the ability to make informed decisions about PayPal.

And as you can appreciate, like there's a lot behind any numbers, but I think there was some misplaced concern in the market around the overall size of Braintree relative to some of the other competitors in this space who were talking about the size of our business.

And so, we wanted to demonstrate that on an apples to apples basis, when you include things like gateway transactions the size of Braintree. Not to say that we'll do this every quarter, but I thought that was important just given some of the recent competitive announcements in this space and new companies doing IPOs and things like that.

So, that was the purpose of that. On the growth rate, I don't want to be apologetic about this, because it's still growing at a very handsome rate, but it is sort of a law of large numbers. So, as eBay gets bigger, the growth rates will decline over time.

ELLIS: OK, and…

RAINEY: I'm sorry, Braintree, not eBay…

ELLIS: Braintree, yes. Yes – no, I know. OK. Quick one on the competitive landscape, Apple Pay has been releasing some data points. Amazon Pay has as well. We've got the joint button with Visa MasterCard, etcetera. Are you seeing any impact of any of those alternative buttons in the U.S. in particular?

RAINEY: Not -- nothing to call out. I mean, certainly we have a lot of insights in to things like Apple Pay because in many cases we're doing all of the processing for some of these companies that offer Apple Pay as an option. There are independent objective metrics out there that are not PayPal numbers that support our positioning head to head with many of these other payment options.

And I think even eBay put out some numbers around the percentage of their transactions that are Apple Pay. And that's even when PayPal is not an option to pay. And so, we can go head to head with the competitors, we really like our positioning. And the IPSOS study that just came out that we alluded – we talked about yesterday were, 54 percent of customers are willing to buy online when PayPal is an option.

That's a pretty profound number. And I think it really demonstrates our value proposition. With Amazon, look, another great competitor, a great company, but it just shows the difficultly of getting real traction in this space when I think they've got – I can't remember the number, 3 or 4 percent penetration in the top 500 retailers compared to our 81 percent penetration.

And so, I'm not being dismissive of the potential competition here in any way. But it just – with a two sided platform at the scale that we have, it's – that's pretty difficult to replicate. And what we're going to try to focus on is just continue to enhance that value proposition both for our consumers as well as for our merchants.

ELLIS: All right. And we're going to end on a question just on M&A. You mentioned earlier on the call that you're not slowing down either on the partnership front or on the acquisition front. Just in closing, can you give us a sense for what are the areas that you're looking at on the acquisition front in particular?

RAINEY: Sure. I'd put it in to a couple categories. One is where we can continue to build out assets of our platform to really be – provide all the solutions that merchants are wanting today.

And so, the examples of the recent acquisitions of Hyperwallet, Simility, iZettle all fit in to that category. And we want to be that platform that is one stop shopping for our merchants to give them everything that they need. And even in an omnichannel experience.

And so, acquisitions like iZettle, Hyperwallet, those really fit in to that category. On the other side is like when we look at the growth opportunities around the world, some of those are better achieved inorganically versus going out and trying to grow organically from the grassroots effort type of initiative.

And so, there's a fair amount of white space around the globe that we think there's some attractive opportunities there. So, that's why I say we'll continue to be aggressive. I – we are really a unique company, and that there are – there are obviously tons of companies that have our growth rate. But there are very few companies that have our growth rate and our cash generation.

And so, when you combine that cash generation with the balance sheets that we have, we believe that we're an actual consolidator in this space. And we're going to continue to try to expand the advantage that we have today for our leadership position.

ELLIS: Terrific, thank you. John, did you have any closing comments before I wrap it up?

RAINEY: No, I really appreciate you taking the time to facilitate this call this morning. And I appreciate the investors that are listening in. We're excited about the third quarter and launching off in to 2019. And it's – a lot of good things to come from PayPal.

ELLIS: Wonderful, thank you. And many, many thanks to John and the PayPal team doing these calls after a very hectic quarter end, is really going above and beyond. On behalf of everyone joining, I'll certainly thank you and thanks to everyone joining this morning.

If I did not manage to get to your questions, I apologize. Definitely follow-up with me or Gabrielle and Akila, and we will – we will get those resolved. All right, thanks, everyone. And have a great weekend. And operator, we can close the call.

OPERATOR: Thank you. This concludes today's conference call. We thank you for your participation. You may disconnect your lines at this time. And have a great day.

END