Second Quarter 2022 Analyst Call | August 2, 2022

CORPORATE PARTICIPANTS

Dan Schulman, *Chief Executive Officer and President*

Gabrielle Rabinovitch, *Interim Chief Financial Officer, Senior Vice President of Corporate Finance and Investor Relations*

CONFERENCE CALL PARTICIPANTS

Josh Beck, *KeyBanc*

Colin Sebastian, *William R. Baird*

James Faucette, *Morgan Stanley*

Bob Napoli, *William Blair*

Ken Suchoski, *Autonomous Research*

Jamie Friedman, *Susquehanna*

Jeff Cantwell, *Wells Fargo*

Ashwin Shirvaikar, *Citi*

PRESENTATION

Operator

I would like to welcome everyone to the Sell-Side Analyst Call for PayPal's Second Quarter 2022 Earnings.

Thank you. I would now like to turn the conference over to Dan Schulman. Please go ahead.

Dan Schulman

Thanks so much. Hi, everybody. Welcome. We are looking forward to getting all of your questions, no real limit to them, so just fire away. That's all the opening remarks I really need to say, except again, congratulations, Gabz on your expanded role. We're all really excited about that and thank you for everything you did in the interim. Okay with that, let's open it up for questions.

Operator

Our first question will come from the line of Josh Beck with KeyBanc. Please go ahead.

Josh Beck

Yes, thank you for taking the question. I think one of the important points investors are looking for, and certainly applies to [market] share gains, is when I look at the FX-neutral excluding eBay growth in the first half and the monthly detail, it certainly seems to be intact. Behind that, are there major items you would point to? Is it moving higher in the funnel? Is it some well-funded competitors have less funding? What would you point to as we try to kind of communicate the share gain momentum that you do seem to have?

Dan Schulman

Yes, Josh, I'll start off and then maybe Gabz can add into it.

Markets never move in V's. They move more gradually than that. It's a combination of a number of things that have been underway for quite some time.

First of all, I think buy-now-pay-later has gained a tremendous amount of momentum for us. We are in more merchants than any other player out there. We have more upstream presentment than any other buy-now-pay-later player and that adds to flexibility and more share.

Second, we are clearly seeing a flight to quality in the market. I think retailers got a little bit spooked by some of the announcements where people are pulling back, retrenching, wondering if they're going to be able to raise money, seeing valuations crash. We've had more sales wins than we've seen in quite some time and a number of them are quite large, especially on the Braintree side. That's going to make a difference going forward, because Braintree integrations, that's the best possible integration for both PayPal and Venmo in terms of a native in-app experience. You're not seeing people buying placement anymore in the market. People were using venture [capital] dollars to buy placement. We were never going to chase that, and it's just not out there anymore, you're not seeing people offering parts of their companies for placement.

Then, I talked about little things, but it's not really a little thing. Taking off five seconds of latency in checkout, when every second matters, really makes a difference. Our reliability now is pretty close to five 9's [statement on up-time of our checkout processing] across the board which is outstanding. Our authorization rates are going up as well. Little things we're doing right now are improving conversion. Our conversion went up by 0.3 or 0.4 of a basis point last quarter.

All those things together add up to share gain. The ones I'm most excited about are the in-line checkout and native checkouts, so you don't need to [access a] pop out [to check out]. That SDK API [Software Developer Kit that enables native in-line checkout on mobile devices] that we're putting out, if that hits, that could be a pretty big thing in the future. Not today, but going forward, that could make a big difference.

Josh Beck

Okay, very helpful, and then maybe just the follow-up. You obviously covered it pretty well in the call, about the success that you're having with Venmo monetization. As we look out to next year and beyond, I'm just curious how meaningful the shifts in the different monetization buckets may be, as we think about some of the new partners that you have. Obviously, you gave some really impressive stats on the

commerce transaction front. But, just curious, as we think about the next phase of Venmo monetization, if it will be quite a bit different, maybe, than what you're seeing take place this year.

Dan Schulman

Yes and Venmo is going to grow more and more on the commerce side. The way that I think about it, PayPal started off many, many moons ago as a P2P business and then started monetizing merchant payments. Venmo started off as a P2P business. It's got a ton of advantages that PayPal didn't have those many, many years ago. Pay with Venmo I think will be the dominant way we will monetize Venmo going forward. That's why we look at these commerce stats religiously and we are pushing to make sure that every integration of Pay with Venmo is seamless. When we tried to do this several years ago, it was a clunky experience. That's why I've come back to the teams. It's not about getting experiences out there, it's about getting beautiful experiences out there and doing less but doing it in a beautiful manner. The commerce stuff is what I'm quite focused on. There will be other things in the wallet people will be able to do, but commerce will be the main growth driver of it going forward.

Gabrielle Rabinovitch

I'd also point out the card strategies for Venmo are important, as well. The debit and credit cards continue to grow their volumes and those are really important for habituation. They reinforce all the in-wallet spend with offline spend, as well.

Dan Schulman

Yes, I totally agree with that. If you look at Cash App, their big growth is off of their debit card. We have a lot of room in our debit card and credit card to grow too.

Josh Beck

Super helpful. Thanks, Dan and Gabz.

Dan Schulman

You bet. It's a pleasure.

Operator

Our next question will come from Colin Sebastian with Baird. Please go ahead.

Colin Sebastian

Thank you and good afternoon guys. I think these are both follow-ups. I guess Dan, this question's come up a little bit with investors. I wonder if you could expand a little in terms of the operational changes or balance of the expense savings that you're committed to today and next year with upping investments in areas like product and engineering where the headcount isn't exactly one of the lowest cost areas of investment. How much is your commitment to increasing investments in R&D and technology versus lowering the overall expense structure and expanding margins? Then, I have one follow-up.

Dan Schulman

I think the way you should think about it is we have a lot of engineers. They were not all focused on the right things. Our highest impact highest conviction growth opportunities, we're putting a lot of investment behind. At the same time there's a huge amount of opportunity. The numbers we put out there, we're very confident and we think there's more room beyond that. We see a lot of opportunity for productivity.

When you have engineers, first they need to be focused on the right things and we now know exactly where we want to be focused. Second, when you have duplication of platforms that makes things inefficient. As we are now starting to bring those platforms together, we can be much more productive. Our development environment is getting better and better. We could probably do the amount of work we need with less than more once we start to put all the productivity out there.

As Gabz mentioned, a lot of the cost savings we're doing right now are leveraging our scale and driving down unit costs. And that has nothing to do with headcount but everything to do with scale. A lot of people said, "Well, you've got the scale. What can you do with it?" We are leveraging it through our cost structure right now.

We have a lot of room to be even more efficient and productive. The whole team knows that, we're focused on it. The number one issue that we have is gain share, grow and invest. It is as simple as that and we will put the investments in places that we need, but we're going to be focused on it. I think we have a pretty clear game plan right now. We're seeing the impact of it in the market, the whole company is rallying behind it. We are bringing in really seasoned people who are operationally focused, who are no-nonsense, understand exactly what needs to get done. Like when we brought in Archie Deskus (Chief Information Officer) from Intel a couple quarters ago to run our tech platforms, she's making a huge difference. It's just a pleasure to watch her in action. One of the major things we love about Blake Jorgensen (Chief Financial Officer) is he is very operationally oriented as well. You can be sure the new Chief Product Officer that we bring in will be from a tech background, will understand scale, will understand beautiful consumer experiences at scale, and be operationally oriented as well. So, quite excited about the team that is assembling here. It's kind of the next generation. We're managing all the moving pieces. I think we've been working it for quite some time and it's beginning to show up finally.

Gabrielle Rabinovitch

Colin, just one more thing I'd add. I know the cost savings numbers sound big. They certainly are big and we're excited about the opportunity to deliver against them as well as to do more. When you think about the non-transaction related opex growth in our business over the past few years, in 2020 we grew 17% and in 2021 we grew 20%. You're talking about a tremendous amount of increased costs that we invested into. What we're doing right now is really just scaling more efficiently with what we have and making the right decision to ramp prioritization. We're not going to sacrifice any of our key priorities, but we're really looking to do things as efficiently as we can to grow more profitably.

Colin Sebastian

That's great. That's very helpful and I think that's crystal clear. Dan, by the way, covering EA [Electronic Arts] for years, Blake is definitely operationally focused, so it sounds like a great hire there.

Dan Schulman

Yes.

Colin Sebastian

Then I guess secondly, and lastly, if you look at Amazon and Shopify and PayPal, adding up GMV, I mean that's a significant portion of e-commerce GMV in markets where you guys overlap and so the announcement [] I know you partner with Shopify already, but the expansion of that relationship seems pretty interesting. Is this French opportunity, is that something that has potential to expand across more of Shopify's merchant base over the near or medium term?

Dan Schulman

Our relationship with Shopify I think continues to get closer. We both see a number of strengths that each of us have and we both want to figure out how we can do more and more together to serve our mutual customers. So, yes, that partnership which was already strong is clearly getting stronger.

Colin Sebastian

Okay, thank you.

Dan Schulman

On the Amazon side we're excited about Pay with Venmo. On all of these things you start off in one place and then you see how things evolve from there. But clearly some things like getting out of the eBay contract was painful in a lot of ways. Most of that is in the rear-view mirror right now and you're seeing that, but it also opened up quite a number of doors to us as well that we'll take advantage of.

Colin Sebastian

Sounds good. Thank you, Dan.

Dan Schulman

Yes, you bet.

Operator

Our next question will come from James Faucette with Morgan Stanley. Please go ahead.

Dan Schulman

Hey, James.

James Faucette

Hey, good afternoon, Dan, Gabrielle. My thanks and congratulations as well as everybody else's.

I wanted to just hit on a couple of quick things around assumptions and details. First, I think, Dan, you quoted some different numbers for forecast e-commerce growth this year. Can you give us a sense of what you're baselining on for the year, overall, just so we have some sense of how you're thinking about your business relative to the e-commerce growth, especially since, as we all can appreciate, e-commerce growth right now is probably the hardest thing to forecast?

Dan Schulman

It really is. I'll let Gabz get into some of the details of it. I think it's an uncertain macro-economic and geopolitical environment that we're in and nobody's got a crystal ball. We thought hard about where [] we want to anchor our guidance and we anchored it to the low end of our [prior] FX-neutral range because we thought that was the most prudent thing to do.

You could see through our revenue growth over the next several months that it's not this major step-up. We're [preliminarily] at 14% plus [revenue growth] in July and our guidance is for 14% growth [in Q3-22] if you normalize for the PPP revenue recognized in Q3-21 [PayPal's Q3'22 revenue outlook is for +12%

FXN revenue growth; in Q3-21, revenue growth had a ~1.5pt benefit from revenue related to the Paycheck Protection Program] and then 14% or so in the fourth quarter.

In there we're assuming inflation remains high, there's strong dollar pressure on FX, the risk of a recession in Europe remains quite elevated. We don't see improvements in supply chain or really big improvements coming out of China right now. When we look at different cross-border flows we don't see improvements, we're not thinking that that comes back. We saw the low-end consumer pullback on spending probably before most others did given the scale of our platform. That spending still remains depressed. At the high end, high-end consumers with credit cards, etc., still robust spend. I think the big bet is what happens in the middle there. We're assuming it stays about the same as where it is. We're not assuming anything massive for back-to-school, we're still looking at basically what we saw last year. You talk to some people, they think that maybe back-to-school will be better. But we're being conservative on that as well and then we'll see how the holidays play out.

I think there's a lot in the macro and geopolitical to be appropriately conservative about and that really informs kind of our opinions and why our view is that e-commerce will accelerate in the back half. But when you look at the full year you're more in the 8% range [independent forecasts for how fast U.S. e-commerce may grow in 2022], probably. We'll probably take share as we have demonstrated to do. We'll grow faster, significantly faster. We've got some one-time things that are unique to PayPal. We're lapping eBay, we have these series of Braintree wins that are pretty significant in the pipeline, and our revenue initiatives that are pretty focused are beginning to bite as well in the market. By the way one thing we don't talk about is higher interest rates, in general, that's beneficial for us.

Gabz, anything else you'd put in?

Gabrielle Rabinovitch

No, I think you covered it well. James, you're right, e-commerce growth has been more sluggish than we expected. At the start of the year we thought it would be around 10%, it was lower in the first quarter, even lower in the second quarter as Dan commented. Excluding travel, we think U.S. e-commerce growth was slightly negative. With travel probably something closer to flat. We were low single digits in Q2 [growth of U.S. PayPal Branded Checkout], so we showed some good market share growth. At the same time there are lots of estimates out there. We're watching all of them trying to triangulate and we're going to kind of pace it. I think overall through the back half of the year as well as next year and years forward, we would expect to continue to be able to grow faster than the overall rate and that's what we're really looking to do.

James Faucette

Got it, and then just a quick follow-up on capital allocation. You highlighted that with the new authorization, you've got outstanding [share buyback] authorizations of $17.8 billion. I'm wondering if you can just give us some sense over what time period that's intended to be spread and how does this impact your expected use of capital for buybacks versus M&A and other options?

Gabrielle Rabinovitch

As a starting point the most important use of capital for us is investing in our business, so organic investment always incredibly critical. Since separation we've generated approximately $25 billion of free cash flow. We've been very balanced about that allocation between share repurchase and M&A. At the same time given the dislocation in our stock price and the conviction we have in our business, we think it's an appropriate time to be more opportunistic with our share repurchase activity, so that's what you've seen us do. At the end of last year you started to see more aggressive repurchases. Certainly through the first half of this year you've seen more aggressive repurchases and what you'll wind up seeing is for 2022

call it 75% to 80% of our free cash flow will be returned to shareholders in the form of share repurchase. That means about $2 billion more of repurchase in-year, around $1.8 billion that we expect to do.

As it relates to longer term we have that medium-term capital allocation guidance out there that was for 35% to 40% of free cash flow returned in the form of share repurchase. This year we're doing twice that. As you heard Dan mention on the call we are expecting to do an Investor Day early next year. We also put in the press release that we're doing a full review of all capital allocation priorities and all alternatives, so I'd expect that we'd come back to you at our Investor Day and give you an update on the medium term outlook. But for right now through the end of the year, expect to see more aggressive repurchase [activity].

Dan Schulman

To build on Gabz's remarks we have somewhere between $15 billion and $16 billion of cash, cash-like and investments on our balance sheet along with the free cash flow that we have. So we have room for M&A. We are always looking in the market. Probably more than ever people are reaching out, with all of the dislocation in the market. We're seeing valuations in the private side come down quite substantially. So, there may be opportunity. If there is an opportunity down the middle of the fairway, something really aligned with our skills and capabilities, we're not ruling out M&A. We have the firepower to go and do that. But we've a lot to execute against and don't want to be distracted. But if the right opportunity comes along that can accelerate us in the right place we wouldn't hesitate to do that.

James Faucette

Great thanks, Dan. Thanks, Gabrielle.

Dan Schulman

James, one last thing I'd say on that. There are rumors around this Pinterest thing. I just want to put an end to those rumors. There is no substance to that whatsoever. When people are talking about M&A, I'm not sure where those come from, but that speculation is unwarranted.

James Faucette

Appreciate that, thanks a lot.

Dan Schulman

Okay.

Operator

Our next question will come from Bob Napoli with William Blair. Please go ahead.

Bob Napoli

Thank you, Dan. I think the fact that Bill Ready's running Pinterest and he was at PayPal and then you have Elliott in both companies, might have sparked some of that, and I appreciate your clarification.

Dan Schulman

Yes.

Bob Napoli

Thank you. On the credit business I think on the call you talked a little bit more about growth of credit, you had 9% growth in the quarter. That's pretty healthy growth. Is credit going to become a bigger part of the PayPal story, are we going to see credit cards or other credit products become a bigger part of the story over the next few years?

Dan Schulman

I think the way we're thinking about credit is really how a consumer can utilize PayPal both online and offline. It's really a bigger part of our offline strategy. We want those cards to be fully integrated into our app. For instance you could have our 3/2 card, which is 3% cash back on all PayPal purchases, 2% everything else, but you could tap that card at a retailer and then come back into the app and then decide to buy-now-pay-later off of it. The card is the interface at the point-of-sale but the actual management of that transaction happens within the app. You can load your rewards and everything and tap your card and get those automatically as part of the transaction. That's really where we're going with the credit and debit side of the business. It'll always be a smaller part of our business. It's predominantly the way that we'll get into new [offline] mediums until the mobile phone becomes a much bigger part of the offline world. It's a very effective way for us to go in. It's something that our consumers understand and it takes full advantage of the app that we have.

Bob Napoli

Thank you and then just a follow-up. I appreciate the Investor Day early next year. But the long-term growth of the business and your focus on customer engagement, can you give some color on how we should think about, with the super-app, should we think about PayPal's growth as being more from transactions per account than account growth? Should we expect account growth kind of low-single-digits and double-digit transaction growth per account, is that the right way to think about that and just any update on the super-app strategy if you would?

Dan Schulman

Yes. It's a good question because they actually are linked. We have something like 430 million active accounts out there. Our focus is driving incremental engagement from those accounts. If you take your TPA [Transactions per Active Account] up a little bit versus adds, [an expected] 10 million NNAs [(net new actives) for 2022], it's not even close in terms of the value that you can generate from taking your TPA up. The interesting thing is when you take your TPA up and you take engagement up and you drive ARPA [Average Revenue per Active Account], you reduce churn. Our top of the funnel is not the issue. We have strong organic activations, we have strong reactivations that go on. It's just when you're at 430 million active accounts, churn is a big part of the bottom of the funnel. When we say we're focusing on engagement, it is because we have so much opportunity. We're not a subscription business, we're a transaction business. By definition, that is going to help our NNAs grow. They are integrally linked together. The more successful we are in driving engagement, the faster our NNAs will grow. But we are focused on high-quality NNAs coming in.

One of the things that we're beginning to see, our June '22 cohort versus June of '21, the first month value of those are double. That's because we're focusing on the right set of high-value accounts coming in. Our CLV [Customer Lifetime Value] for active accounts is up 15% from pre-pandemic right now. The things we're doing with digital wallets and focusing on these high-value cohorts coming in, they really will drive the economics of this business. I believe that digital wallets, call them what you will, but a combination of financial services, payments and commerce, 70% of consumers want an integrated app and 80% of our consumer base would highly consider starting their shopping journey with PayPal. We can take advantage of a lot of the trust we've built up over time to really create a quite meaningful ecosystem within our digital wallets.

Bob Napoli

Thank you and congratulations, Gabrielle. Just a quick numbers question. Have we ever gotten sizing on Braintree recently? Is there anything you could tell us on the sizing?

Gabrielle Rabinovitch

We haven't given Braintree sizing recently. We've really never given it. We have discussed the growth in the Braintree platform. We provided that last quarter Braintree grew TPV [Total Payment Volume] 61% year-over-year. In Q2 of this year Braintree grew TPV 44%. I think it's important to recognize the 44% deceleration was on very strong growth in Q2 of last year. When you look at the three-year CAGR between Q1 and Q2, it's actually relatively consistent, it was about 50%. But we've not provided the standalone Braintree full stack volumes.

Bob Napoli

Thank you.

Operator

Our next question will come from Ken Suchoski with Autonomous Research. Please go ahead.

Ken Suchoski

Hey, good evening, everyone, and thanks for taking the question. Congrats to all of you on the new roles over there, very exciting.

I wanted to ask about the cost savings initiatives. Could you just talk about what percentage of the $900 million in cost savings are already in the 2Q numbers, what are you assuming for the 3Q run rate versus 4Q, and I guess what portion of that $900 million and $1.3 billion do you expect to reinvest versus flow-through to the bottom line, just because we're getting a few questions there?

Gabrielle Rabinovitch

The [non-GAAP] EPS guide that we provided contemplates the benefits from the $900 million, as well as the reinvestment in certain areas and in our high-conviction growth areas. We haven't disaggregated the amount of the $900 million that we're reinvesting, but it's all contemplated by the [non-GAAP] EPS guide that we provided, which is a raise at the midpoint of $0.05.

Dan Schulman

Also you see the [non-GAAP] operating margin improvement kick-in in the fourth quarter. So you see more of those costs coming in and then you also see in the fourth quarter that [non-GAAP] EPS likely turns positive for the first time year-over-year as well. Then obviously with at least $1.3 billion of cost savings run rate, you see some of it was more back-end loaded than front-end loaded.

Ken Suchoski

Okay. Then, as my follow-up, I wanted to ask about the transaction expense savings that make up part of that $900 million. Could you just remind us where those are coming from? I thought I heard some comments that it's from scale, so perhaps better network fees or more rebates, but then I also heard a comment about resurfacing the most relevant funding instruments when appropriate. So, if you could just clarify where those savings are coming from that would be great. Thanks a lot.

Gabrielle Rabinovitch

They're really coming from the network ecosystem and how we work across the payments ecosystem and our ability, given the scale we have, to negotiate better rates overall. So it's across a number of different partners. It really is separate from this idea of surfacing what our customers are selecting, right? That is really about customer experience. I think our network of partners are very supportive of this idea that we want to show our customers the funding instruments that they want to use whether it's credit, debit, stored balance. It is not about steering in any way. It really is about surfacing what our customers want to use when they want to use it, with the right merchants and the right context, with the benefits that we see on the transaction expense side really being about continuing to benefit from the scale that we have.

If you just go back to call it 2016 which is when we announced our first set of network agreements, the volume on our platform today is multiples greater which is just recognition of the fact that we're a very, very scaled business. Even relative to pre-pandemic I think our TPV is 2x what it was. We're continuing to represent a very important distribution channel for all of our partners and we want to be sure that we're benefiting from it.

Ken Suchoski

Great. Thank you so much.

Dan Schulman

You bet.

Operator

Our next question will come from Jamie Friedman with Susquehanna. Please go ahead.

Jamie Friedman

Hi. Let me echo the congratulations. Gabz, in your prepared remarks, you talked about the credit externalization strategies. I was just wondering, could you elaborate on that a little? How should we deal with provisions and reserves with that as a prospective event?

Gabrielle Rabinovitch

Yes, absolutely. We haven't done an externalization of credit in a meaningful way in several years and obviously through the pandemic the profile of our credit business changed, the actual overall balances changed. Now we're getting to the point again with our originations and the growth of our buy-now-pay-later business, that credit is becoming a bigger piece of our overall balance sheet mix. Even more importantly, it's taking up more of our free cash flow. As we think about how to allocate free cash flow to the best and highest returning areas of the business, that has led us to do a full assessment of potential externalization. We'll continue to provide details as we move through the year. But, our goal with any externalization is deconsolidation; meaning off our balance sheet, provisions come off, not funding it with our own cash. To the extent that we we're able to externalize part of our book, there would be an impact on our provisions and we would take it out. We haven't provided more detail yet on which pieces of the book we're looking at, but we'll do that as appropriate. We look forward to continuing to keep you guys up to speed on how we're thinking about it. We think this is our first step and then I think you could expect to see us continue to look to externalization over the coming years with different parts of the portfolio.

Jamie Friedman

Okay, makes sense. If I could pivot over to OVAS [Other Value Added Services], and I apologize if I'm messing this up, but my recollection is that previously you had contemplated maybe mid-single-digit growth for OVAS for the year. Is that right and does that still hold?

Gabrielle Rabinovitch

Yes, you're right. We started the year out with low- to mid-single digit growth expectations for OVAS. We moved that up after Q1 to mid-single digit growth. Now based upon the 21% growth in Q2 I would expect to see slightly stronger growth on other value-added services revenue. I'd expect it to be high-single digit growth to potentially low-double digit growth. We did talk about that in the third quarter we are lapping some revenue recognition from last year from PPP, that does put pressure on our other value-added services revenue growth in the third quarter. I would not expect to see the same strong trajectory as you saw in the first half of the year in part because of that. That said, we're also seeing strong interest income on customer stored balances so that's supporting us as well. So yes, our expectation for OVAS have come up a bit since we last came to you. In part that's just the strength in the credit business overall, the strength of the Synchrony [U.S. consumer credit] book, and so we're pleased with that and we're expecting a little more in-year.

Jamie Friedman

If I could just ask a quick question. The Q4 margin expansion comments, that is a sequential comment right, that's not year-over-year?

Gabrielle Rabinovitch

At the high end of the guide it is a year-over-year expanded [non-GAAP] operating margin comment. I believe at the high end of the guide for the year, [non-GAAP] operating margin would be about 20.5%, and that contemplates year-on-year improvement in the fourth quarter.

Jamie Friedman

Got it. Okay, thank you.

Dan Schulman

Yes.

Operator

Our next question will come from Jeff Cantwell with Wells Fargo. Please go ahead.

Jeff Cantwell

Okay, thanks so much. There's some great questions being asked, and even better answers, so thanks for doing all this. Hope you're doing well, Dan and Gabrielle. Appreciate getting on.

Dan Schulman

Thank you, Jeff.

Jeff Cantwell

And at this point in time, it might just be the three of us, because everyone else has had a long day, so.

Dan Schulman

That would be fine.

Jeff Cantwell

Dan, I wanted to ask you. There's some big moves that you're making, and there's many of us who were kind of listening to this and we've been watching you run your Company for years now, right? There was a question earlier about M&A and I was kind of thinking that through a little bit and thinking about all the acquisitions you've made, like Hyperwallet and Honey, and so forth. Maybe this is like an introspective question. Did things turn out the way you expected? What worked out well and what maybe are you able to say like, "Hey, maybe this didn't work out as well as I was expecting." Can you give us a little bit of insight into where you stand today, and then I have a follow-up, as well, but I've always wanted to ask you that one?

Dan Schulman

When I first came to PayPal eight years ago now, it was a nascent company. I think most people thought it was a dinosaur and most people were writing off that PayPal at the time had a very antiquated tech stack, a lot of competitors moving in, and I think most people thought we would be commoditized and start to shrink. When I look back to then to now across almost every metric, whether it be our active accounts, our TPA, our revenues, our profitability, you've seen three to four times growth on all of that.

I did not expect that the leap forward in e-commerce would come back to historical rates, like so many of us on the call and so many in the industry, and we've adjusted on that. I think it's taken some time to go and do that, but I think you're seeing real concrete examples of us making that turn now. I think the team has been working extraordinarily hard to go and do that.

We're bringing in new talent into the team, which is something that always is invigorating and refreshing. From Blake Jorgensen (CFO) coming in, to Archie Deskus (CIO) coming in, to a new CPO coming in. I'm quite excited and they'll build on what those others who have left have done and take us to a whole different mode. Every one of the people that I personally interviewed, 14 people before we selected Blake to give you an idea of how extensive process was, they're all extremely operationally focused, extremely excited about the mission and the values of PayPal, as am I.

In general when you talk about the M&A piece, many of the parts of that have become critical parts of our app. Honey is the engine behind PayPal shopping. Happy Returns will be the engine in our post-purchase process within our app. Hyperwallet, it is the perfect complement to Braintree, where you have pay-in and pay-out and how we satisfy marketplaces where you have a pay-in from a customer and a pay-out to a gig economy worker. You look at things like Zettle, that was slower than we expected, because we got caught up in the U.K. CMA exam and then went right into the pandemic where nobody was shopping in-store, but that's a big part of our PayPal Commerce Platform, omnichannel platform.

So not everything has worked out as we expected by far and away, it never does. But in general, as I look back and look at the forest for the trees, and sometimes our nose is right up against the trees, I'm pleased with the distance we've come. I would call us a good company and we still have work to do to become a great company. That is what we are focused on and hopefully we'll be able to execute on that.

Jeff Cantwell

Thanks so much, that was great. Just kind of thinking that through a little bit, right? By the way, this is going to sound like pandering to all the other analysts, but in my book some of your best moments were during the pandemic, Dan. I just want you to know that.

Dan Schulman

Thank you. I appreciate it.

Jeff Cantwell

But the other side is about the go-forward, right? I sit here thinking to myself, your cost cuts, what does that mean for Xoom or for Hyperwallet? I think about a lot of the assets that you've built over time and what does that mean for Honey. So, I guess, how do we get more comfort about that there will be more leverage, right, and positive leverage on the revenue side from those assets, given how much you've invested in them, but also with what you're saying on the cost side going forward.

Dan Schulman

Well, that's exactly the places we're investing. I said we had three things that we're doing. First is to focus on strengthening our value proposition to ensure that we take share. That's our number one priority and we are investing heavily in those areas to go and make that happen. Second, we are reducing our cost structure because we can and because we're focused. We built our cost structure up during the pandemic, we have plenty of room to do that. We have scale to leverage with our suppliers as well. The third is to always revitalize, reinvigorate the organization with new talent, with new structures, so that you make all the right trade-offs, bring in the very best talent to run the Company. Honey is a key part of the digital wallet. Hyperwallet is a key part of the Braintree platform on the pay-in and pay-out. Happy Returns is a key part of the post-purchase part of the app that we're doing. If it's part of the app, both Venmo and PayPal, part of the Braintree platform or unbranded, or part of checkout, we are investing heavily in that because it is making a real different in the marketplace.

Jeff Cantwell

Okay, sounds great. Congrats, and thanks, Dan.

Dan Schulman

You bet. Thank you for the question. May we have room for one more question?

Operator

Our final question will come from the line of Ashwin Shirvaikar with Citi. Please go ahead.

Ashwin Shirvaikar

Hi, Dan. Hi, Gabrielle. How are you? Sorry, I kind of put myself on mute, finally, after two years. Now, I have to get off mute.

Dan Schulman

It's good to hear from you.

Ashwin Shirvaikar

Gabrielle, congratulations, very well deserved.

I guess the first question is with regards to the growth of credit, especially given macro concerns that seem to be creeping up. I know the growth of credit helps engagement, but could you comment on what your assumptions are with regards to usage increasing because of that as well as risk management by product as you look at pay later versus PayPal credit versus products like credit card. I understand a lot of pay later that is heavily debit funded, but is still a loan, so I'll put it there.

Gabrielle Rabinovitch

Yes, absolutely. We think about credit as a percentage of assets on our balance sheet. We think about the percentage of free cash flow that gets allocated to fund credit. We think about credit in terms of the amount credit contributes to our overall income statement both the revenue as well as the earnings. We look at credit across a number of different dynamics and of course we're always paying very close attention to our charge-off rates, our loss rates, and the overall performance of the book. Across all of those metrics our credit business is actually incredibly healthy today. When we look at the size of our credit business overall relative to the size it was in 2017 or prior actually, the overall kind of percentage of assets represented by credit today is quite low. Not as low as it was during the pandemic because we got really low then. But 7% of total assets. So we feel very good about the overall size of the book.

I think it's really important to know that the single largest area of growth in the book that we've seen over the past two years is coming from short duration global pay later. That is actually quite easy to flex depending on the environment that we're in. So, very different from the consumer revolve [revolving credit] book that we used to run where you're talking about a credit line for people that extends multiple years, the duration's quite long, and once you extend that credit line there's really nothing you can do to pull it back because of consumer credit rules and protections. In the case of the pay later portfolio, we're really talking about risk decisioning on every single transaction. If we want to contract that book quickly, we actually can flex it really easily. So we feel good about that.

The funding on that portfolio is something that we continue to pay very close attention to. Today overall, we're still seeing debit funding a very meaningful part of that overall book as well as bank funding. So call it 10% of the overall global pay later portfolio is funded with credit, so you're talking about feeling really good about how it's funded and about the loss rate overall. Charge-offs I think this quarter across our total portfolio is about 4% maybe 4.2%, so again we're talking about very low loss rates in that context and the coverage ratio came down a point sequentially.

I'd say thinking long term about our credit business, that's part of why we started to talk today about externalizing more of the book. We'll continue to come back to you with how we're thinking about that and how we're thinking about externalization into the future. The key part for us on credit is what it does for the platform, how it continues to help to grow and accelerate our business and reinforce our relevance at checkout for our merchants and our consumers. It's not because we particularly have an interest in having credit on our balance sheet relative to partnering. You've seen us partner with Synchrony pretty extensively. We partner with others as well to help fund our credit business and you can expect to continue to see us do that. I think overall we feel very good about where we are right now. We feel like even in an evolving credit cycle given where we're seeing growth which is this real short-term product, we do have the ability to calibrate that pretty well.

Ashwin Shirvaikar

Got it, thank you for that. One clarification I had was you mentioned the 50 basis points of [non-GAAP] margin improvement for next year, right, off of this year's whole year outcome. How should we think of the

FY'23 benefit of $1.3 billion as we sort of think of what's the baseline for this year off of which that benefit is counted?

Gabrielle Rabinovitch

It's a little early to give guidance for 2023, so we're not going to get ahead of ourselves. It's August 2 we've got a big piece of the year ahead. Frankly, a lot of how we think about margin will also be dependent on how we think about top line growth next year. It's a little early without having seen back-to-school, the very important holiday season, how the consumer environment continues to evolve as we move through the back half to kind of give full guide. But what we did say was that we're targeting at least 50 basis points of [non-GAAP] operating margin expansion next year and obviously we'll look to do more. As you heard today we've already identified the $900 million of savings in 2022. We're reinvesting some of that in high-conviction areas and we're letting some of that flow through which is part of why you saw us raise [non-GAAP] EPS. Next year we already identified the $1.3 billion and part of that is the annualization of some of the savings we have this year as well as additional savings we expect to realize. I think we want to get through more of the back half before we give a more detailed guide about sort all those parts and pieces, and so obviously we'll do that. To the extent that we're having an Investor Day early next year, we'll obviously dig a little deeper into some of those areas, as well.

Ashwin Shirvaikar

Okay, got it. Cool. Thanks.

Dan Schulman

Thank you.

Thanks, everybody, for joining the call, we really appreciate it, and keep those questions coming. Thanks a lot. Bye-bye.

Operator

This will conclude today's conference. Thank you for your participation. You may now disconnect.