



PayPal Holdings, Inc.

Third Quarter 2020 Analyst Call

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C O R P O R A T E P A R T I C I P A N T S

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C O N F E R E N C E C A L L P A R T I C I P A N T S

Colin Sebastian, *Baird*

Craig Maurer, *Autonomous Research*

Joseph Vafi, *Canaccord*

Sanjay Sakhrani, *Keefe, Bruyette & Woods, Inc.*

George Mihalos, *Cowen and Co.*

Ashwin Shirvaikar, *Citigroup*

Bob Napoli, *William Blair*

Timothy Chiodo, *Credit Suisse*

Josh Beck, *KeyBanc Capital Markets*

Jamie Friedman, *Susquehanna International Group*

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P R E S E N T A T I O N

Operator

Good afternoon, ladies and gentlemen, and thank you for joining PayPal's Quarter Three Analyst Call.

If you would like to ask a question, press star, one on your telephone keypad. To withdraw a question, press the pound key.

It's now my pleasure to turn the conference over to [PayPal's] Chief Financial Officer, John Rainey. Mr. Rainey, I hand it to you.

John Rainey

Thank you, Holly, and thanks, everyone, for joining us this afternoon. We're looking forward to fielding the questions that you have. As usual, I'm here with my Investor Relations team. And Holly, I'll just kick it back over to for Q&A.

Operator

Thank you. Once again, to ask a question, press star, one.

And our first question is going to come from the line of Colin Sebastian with Baird.

Colin Sebastian

Great. Good afternoon. How are you doing, John?

John Rainey

Hey, Colin.

Colin Sebastian

So, I just want to come back to the commentary on 2021 since that's seems to where a lot of the questions are. I think you've said in the past that you expect to be able to grow margins even through the eBay transition. I just wanted to clarify if that view's changed at all given the pace of that migration as well as the additional spending initiatives. And then any sort of help factoring in the headwind from credit next year?

John Rainey

Sure. Well, it's still a little early, which is why we didn't provide the guidance, but longer term we've got a lot of conviction in the margin profile of our business. Credit is a notable call-out though, because that's a very high margin product for us, and we would expect to see depressed levels around credit through next year, and so that certainly is a headwind. eBay, we obviously noted, but offsetting some of that is the huge tailwinds we see in our business around what's happening with just core PayPal checkout right now. And as we covered on the call, there are a number of other new products that we're launching next year, which will be accretive to the bottom line.

So, there's a number of puts and takes. Next year was always going to be the more challenging year from a growth perspective, but it's probably premature at this point to make any comments around the directionality of our margins next year.

Colin Sebastian

Okay, that's helpful. And maybe a quick follow-up. I think it was Dan who called out the October trend. I guess there were a day or two that were the highest level of volume that you've seen, I think. Was that a result of earlier start to holiday shopping, or any specific event that you can call out there? Thank you.

John Rainey

Well, that's a great question. And that point is one that we're keenly following. Meaning, how much of the shopping season will be pulled forward. But the holidays are always sort of a more challenging time to forecast and I think over the last few years you just see more and more come online, which is to our benefit, but it's more difficult to forecast. And so, in this period, where people are shopping online already, it's reasonable to assume some sales could be pulled forward, though we've not been able to pinpoint that in our business. I think, Colin, it stands to reason like you and I certainly don't want to go stand in line and be metered in and out of a store in a pandemic sort of metered environment at a Best Buy during the holiday season.

So I would expect there to be just sort of intuitively more online shopping this season, but the curve of that or how much of that is pulled forward, it's really hard to tell right now. So we've been closely watching and listening to what retailers are saying. And if I can generalize, I would say most retailers right now are saying they haven't seen a lot of that and we certainly haven't seen much in our business that we can specifically call out.

Colin Sebastian

Okay, thank you.

John Rainey

You bet.

Operator

And our next question will come from the line of Dan Perlin with RBC Capital Markets.

Dan Perlin

Thanks. Hey, good evening.

John Rainey

Hey, Dan.

Dan Perlin

There's been a ton of questions, obviously, on 2021, so let me just ask it this way. When you look at the cohorts, so the 70 million or so net new actives that you're expecting to have by end of year and you look at those engagement statistics and try and again to kind of maybe weed out what might be some anomalistic behavior from some of those users, are you finding that the velocity of their transactions are greater than kind of legacy? And then secondarily, do you think that that pool of net new actives are—are these new products really purposely built for those types of consumers?

John Rainey

Yes. So, the short answer is yes, we're seeing more engaged cohorts than previous cohorts. But let me give some context to that. In a typical net new active, there's a maturation curve where someone may come to us through a first transaction and it may take sometimes several months for that second transaction and typically it's over a year before they reach an engagement level that is commensurate with our more engaged customers. And one of the things or two of the things that we're seeing right now that have been pretty consistent trends over the last six months are the daily active users, which we're up

32% in the third quarter, which is much higher than what we've seen previously. And then the 10 day adoption rates, which still is a double-digit percentage increase from what they were before. And again, a 10 day adoption rate, as we define it, is when it's a cohort of customers that uses us four times in a 10 day period. And so, that level of engagement is up double-digit percentages versus prior cohorts.

So two good leading indicators about the engagement level of these customers. Offsetting that, and in a year where you've got 70 million-ish net new actives, you've obviously got to be very concerned about the churn dynamics of those in the following years. So, that's one of the things that our analytic team is doing a lot of work to really try to help influence their behavior and keep them engaged with not only offers but new product opportunities and things like that. And again, as we add additional functionality to the wallet and you see things like the network effect among users, I think that all bodes well for us, but those are some of the competing dynamics as we think about the next year there.

Dan Perlin

Okay. And just a brief follow-up, and it was somewhat addressed in the call, but you have—you obviously have a huge product set that's getting rolled out next year. It sounds like from what Dan said at the end of the call there that the trajectory of expenses are probably going to fall heavier in the first half of the year relative to the second half given most of that's going to be completed. I'm just trying to make sure I understand kind of the cadence a little bit of this expense. Fourth quarter was heavier than what we had anticipated, and so I just want to make sure as we calibrate our models we're not just going to be way off base. Thank you.

John Rainey

Yes. I'm glad you asked the question because I don't think that's exactly what he implied on the call. As I am—we're in the throes of a budget process right now and the last thing that happens in the budget process is the quarterization of all those expenses and revenue efforts. So it's a little early, but I don't think there's anything that I would call out necessarily that is going to create a different expense trajectory for one quarter or the next, with the exception that we're going to see a little bit of a tail of this \$300 million that we earmarked bleed into the first half of the year.

So, maybe the first quarter's affected a little bit more and then we'll just have to gauge what that level of investment is going forward depending upon the benefit that we're pulling through related to these efforts. We're pretty rigorous and disciplined in the way that we approach this and it's not just, you know, us throwing buckets of money at initiatives. So we've got a constant feedback loop on the effectiveness or the efficacy of that spend, and so that could help influence how things go through the year as well.

Dan Perlin

Okay. Thank you very much.

John Rainey

Mm-hmm.

Operator

Thank you. Our next question will come from the line of Craig Maurer of Autonomous Research

Craig Maurer

Yes. Hi. Thanks for taking the question. John, I hope you're well.

John Rainey

(Multiple speakers) you're well as well.

Craig Maurer

Yes, getting by. Wanted to ask about how we should think about OVAS next year, what are the puts and takes? And secondarily, how aggressively did Paymentus volume come on in the third quarter? Thanks.

John Rainey

Sure. Well, Craig, you surprised me. I thought surely, given your quote in the Wall Street Journal this morning, that you'd be asking some questions about the sustainability of P2P trends or something. But no, it was a good article. With OVAS, we'll see a benefit again from Honey next year as that continues to grow, and really pleased with the progress of that product and the capabilities that we can offer there. Credit is going to be a drag still. And honestly, like I would say, if there's something that someone's missing about our financial modeling, it's probably that, that you probably know as well as anyone, Craig, sort of the dynamics of that. So that's going to continue to be something that is a headwind for the year.

I guess, adding to that, if we say in a lower interest rate environment, then we're going to see the interest income on customer balances be more akin to the level that we saw in the third quarter this year. So that could also be a drag. I'm looking at Gabrielle and Akila. Anything that I'm missing there on that?

Gabrielle Rabinovitch

Yes. The contra revenue adjustment to OVAS that we had in Q1 and Q2 as a result of CECL and the changed macro outlook will not be recurring most likely if we're more in steady state. So that's a little bit of an offset to some of that credit impact.

John Rainey

That's a really good point, and we're at a reserve ratio, coverage ratio right now that is 24%, and if we were to see the economy rebound, testing and vaccines be readily available potentially, that sort of relaxes some of the pressure around credit. So you could even see some of that reserve reverse over the next year, potentially, so that's something to consider as well.

With respect to payment, as to the second part of your question, we're 100% ramped on that now. In terms of through the quarter—and I guess what you're getting to is did we really have a run rate effect in the quarter. Close to it. Probably 80% is the way that I'd say that without having the math in front of me. So pretty close to it.

Craig Maurer

Okay. And if you could dimensionalize how much that dragged on take rate would just be helpful because I think that was a hard thing for us to model.

John Rainey

On bill pay, Paymentus?

Craig Maurer

Yes, bill pay.

John Rainey

So, let's take the 24 basis point decline in total take rate. I would say that's probably kind of four equal parts of P2P, hedge, credit, and then mix in our business which includes Paymentus.

Craig Maurer

Okay. Thank you. I'll let you move on. Thanks.

Operator

Thank you. Our next question will come from the line of Joseph Vafi with Canaccord.

Joseph Vafi

Hi, good afternoon, John. Thanks for taking the call.

John Rainey

Hey Joe.

Joseph Vafi

Just a couple of questions. Yes. Hey. Just looking out beyond maybe this year and early next year and into the future there's a couple of things that I think are probably pretty interesting for your model. Number one is kind of personal banking initiatives and you alluded to it on the call with more direct deposit and other things and kind of expanding the customer usage cases just kind of beyond e-commerce. And then secondly, just maybe a little more drill-down on what potentially transaction margins could look like on crypto-based transactions if you can do those away from the VISA and MasterCard card networks. Thanks a lot.

John Rainey

Sure. So, with respect to personal banking, we very much want to partner with others in the ecosystem here and take our complementary capabilities with issuers and really try to go after the addressable market that way. So, we are in no way looking to replace one's checking account or personal bank with PayPal or Venmo. We think that we can provide capabilities that are very much complementary to that. That said, there are many capabilities that are complementary to that. And we've talked about subscription services and bill pay, but crypto is actually another one, right.

And it gets to the second part of your question, where I'm glad you asked because the accounting—well, first of all, on crypto, we're basically providing that as a free service. We monetize that only on any spread between what it costs us to acquire the currency versus what the consumer purchases and if there happens to be a transaction involved there. So, when someone uses that to shop at a merchant there's no additional fee related to that, to the consumer or the merchant. And the accounting on that is such that it won't be recognized in our TPV—but for buy, sell, hold, I'm just getting corrected here, yes, at a merchant—when shopped it will, but the buy, sell, hold of the acquisition of the crypto itself is not included in our TPV. We will account for that on a net basis - meaning that we won't gross it up for what the

consumer is purchasing it for. So, we'll only have the transaction fee for any spread related to the buy and the sell of that hitting our books.

So at this point it's probably a relatively small financial impact to us. I think the play here though really goes to the first part of your question, which is, just having more utility in the wallet and as this is maybe some type of currency that we see more of in the future, we want to be at the forefront of this and make sure that both our consumers and our merchants have access to this.

Akila Moorthy

So on the purchase with a merchant where crypto is being used in that use case, Joe, we will essentially have a take rate with the merchant. Again, not an incremental take rate, but the take rate that the merchant is charged typically and that's how it will flow through our books in that use case.

Gabrielle Rabinovitch

The cost of funds will essentially be very similar to sort of stored balance. The difference being that we will be paying a fee back to Paxos on essentially the currency conversion from the crypto back to fiat currency. But overall, from a transaction margin standpoint, the unit economics are good because essentially it's sort of stored balance funds with a slight fee attached for the conversion.

Joseph Vafi

Great. So it sounds like you would welcome the more crypto-based transaction volume for purchases relative to where your transaction margins are today.

Gabrielle Rabinovitch

Well, look, I mean, the way we think about is today crypto is really sort of an asset for diversification and people are not using it in a transactional way necessarily. That said, we think it's important to remove some of the boundaries there and the friction around people's concerns around volatility. So what we've done is create an experience for merchants and consumers that eliminate some of the risks around settlement or volatility and makes it potentially be used in a more ubiquitous way as a transactional currency, but I still think there's going to have to be consumer adoption around that given the way people use crypto today relative to what this experience contemplates.

Joseph Vafi

That's great. Thanks everyone for the answers. Much appreciated.

John Rainey

You bet.

Operator

Thank you. Our next question will come from the line of Sanjay Sakhrani with KBW.

Sanjay Sakhrani

Thanks. Had a quick follow-up question on the eBay headwind, and then one on the credit costs. As far as the eBay headwind, just want to follow-up on the question asked on the call. That 3.5 percentage point

headwind, does that continue through the third quarter and then abate or can that accelerate or remain the same for sometime?

John Rainey

Well, Sanjay, the 3.5 point headwind is related to the fourth quarter.

Sanjay Sakhrani

Mm-hmm. Would it continue into next year or?

John Rainey

Yes. Yes, and a lot of that depends upon the rate of adoption throughout the year. But eBay has noted, I think, that they've migrated 344,000 merchants already. I think it's fair to assume that eBay's focus is going to be on merchants with greater volume versus lesser volume initially. So, it's not probably correct to just assume that if you take their entire merchant base that that percentage is the same as the volume. The volume is probably more outsized than that.

But yes, that'll be a headwind throughout next year.

Sanjay Sakhrani

I guess what I'm thinking about the rest of the pool of volume that's left, how much of it do you expect to retain, if any?

John Rainey

So, eBay can—they can move everyone if they want through their managed payments experience, if that's what they like to do, even forcing it upon people that don't want it. We're not in control of that. What we're focused on is our share of checkout in that managed payments experience. And as I noted on the call, it's north of 50%. Actually, 59%, 60% in the entities that they've already migrated. So, that's actually in excess of what our initial expectations were. So, this is, I would say, tracking more or less on par with what we talked about in January of 2018 when we talked about this.

And so, it certainly presents a headwind to next year but nothing that we think is so significant that we can't get through it.

Sanjay Sakhrani

Okay. And just to clarify the OVAS or just sort of the credit cost impacts. I know Gabrielle you mentioned the CECL impact and such. When you're talking about the pressure that's not being contemplated and the outpaced impact of credit, do you mean just assuming the macro outlook remains the same? So on the new growth you have to apply high reserve factors against them, or something else? I'm just trying to make sure I understand how to think about that line and the growth of that line in 2021.

John Rainey

Yes. So, credit, seriously, has been a cash inflow for us this year because of the contraction in the book. And so, typically, within OVAS, it's one of the areas that grows in the past sometimes faster than the rest of the business, and if we assume the macro outlook remains pretty constant to what it is today, there's

going to be continual management of that book and so we're not going to see growth in credit like we have in the past. So, that's going to put a headwind to both revenue growth as well as margin.

Sanjay Sakhrani

Okay. Got it. So you're assuming you're going to shrink and that's why it's going to be a headwind for revenues.

John Rainey

Well, shrink to not grow and specifically not grow at a rate commensurate with the rest of our business.

Sanjay Sakhrani

Got it. All right. thank you.

John Rainey

Yes.

Operator

And our next question will come from the line of George Mihalos with Cowen.

George Mihalos

Hey guys. Thanks for taking my question and thanks again for doing this.

John Rainey

Hey, George.

George Mihalos

Wanted to start off, based on the commentary from Dan on the trends that you see more recently with TPV, John, it is safe to say as you look through the month of October and your performance there that TPV growth was sort of tracking at the higher end of your fourth quarter guide and you're sort of in the mid 30s as opposed to the low 30s?

John Rainey

I would say it's pretty much on track with our guide. We've been very encouraged by some of the days that we've seen that, as we noted, were at all-time high levels. But overall I would say it's consistent with our guide.

George Mihalos

Okay. And just a quick follow-up. I know it's been asked a couple of different ways, but maybe just to sort of ask it a bit bluntly. The transaction margin, and obviously, the improvements that you've seen there over the last two quarters, should we be thinking that this rate of overall transaction margin is sustainable as we look into '21? And I know you talked about some of these puts going against you but you also have a lot of these new products that seem to be accretive to the margin.

John Rainey

Transaction margin will largely track with what's happening with the overall trends in our business. So, as we've seen more volume come from the branded checkout experience that carries a lower transaction expense and those tend to be higher margin. If you look at some of the areas, like the travel and event verticals where maybe we do more of the unbranded processing, they've obviously put a significant headwind into our revenue growth, but they also come at a lower margin.

So, to the extent that that persists, then yes I would expect transaction margin to continue to be at this level. To the extent that we see travel and events rebound, that's going to put a little bit of pressure there. But the question I think everyone has is, okay, well, if the core branded experiences still remain at an elevated level going forward, well, then that's going to bode well for us on transaction margin. And then to your point, when we add things like Venmo monetization going forward, that's going to be—that's something that is bringing that down right now, which will start being accretive to that.

So a number of dynamics influencing that. And maybe I didn't specifically answer your question, but tried to provide some color on the puts and takes there.

George Mihalos

Great. Thank you.

John Rainey

You bet, George.

Operator

Thank you. And our next question will come from the line of Ashwin Shirvaikar with Citi.

John Rainey

Hey, Ashwin.

Ashwin Shirvaikar

Hey, John. How are you?

John Rainey

Good. I hope you're doing well.

Ashwin Shirvaikar

Yes, thanks. So, my first question was on BNPL. Do you expect maybe a higher rate of losses that should settle out later as you figure out the type of user that has a tendency to use BNPL? And then, eventually will you take this off of the balance sheet?

John Rainey

Two very good questions. First, we don't expect a high rate of losses, and that's typically what one would assume when you launch a new credit product. For example, when we launched the international consumer product, we saw a higher rate of losses there initially, but fortunately, because of some of our risk capabilities we're not seeing that in BNPL, nor do we expect to. So, very pleased about that.

And just to add a finer point around the monetization of that. That's very much a product targeted for share of checkout, because as Dan noted, there's no incremental fee on the merchants related to that product, which is the normal take rate, while others are charging for that. But, clearly, this is an area of credit where a lot of people are participating and we believe we've got a better value proposition there. And then when you get to the fact that it's effectively free, we think that we'll see the benefits there through a higher share of checkout.

With respect to the second part of your question, which was...

Akila Moorthy

Externalization

John Rainey

Oh yes, yes. So, right now, we don't have any plans to externalize that. One of the interesting things about this, Ashwin, is that because of the duration of the receivables it's actually much less capital intensive for the amount of revenue that it brings in, in contrast to some of our other consumer-oriented products. And so, we don't have anything in the works right now to put that off balance sheet. But that said, our mantra around this remains the same. We will continue to be very thoughtful around how we use credit in our business, where it's not too capital intensive or it doesn't become such a large part of our portfolio of products that it introduces volatility to our earnings that is not desirable.

Ashwin Shirvaikar

Got it. And then the other question was, in terms of just thinking of eBay and the 3.5 points of headwind, could you kind of bring that down to sort of what the margin impact is and considering eBay's push in these faster rate of merchant attrition, if you will? Does your tactical objective here change in terms of how you service eBay?

John Rainey

No, I wouldn't say so. eBay tends to be a higher margin part of our business historically, as they've enjoyed in the range of a 4% average take rate, and so there's an outsized earnings impact related to that decline in revenue. We saw some of that in the most recent quarter and look, we're still expanding margins. So, the impact will be [relatively] contained to 2021 and hopefully when all is said and done it's not aiming at something that I think is really relevant to our overall financial performance. I guess said differently, Ashwin, we believe that we can manage the margin impact of that just fine with what's happening with the rest of our business.

So, it's really going to be the impact on revenue growth that is the only thing that's really, I think, significant to call out.

Ashwin Shirvaikar

Got it. Okay, thanks.

John Rainey

Yes.

Operator

Thank you. Our next question will come from the line of Bob Napoli with William Blair.

Bob Napoli

Hi. Thank you. Good afternoon.

John Rainey

Hey Bob.

Bob Napoli

John, I guess, probably an impossible question to answer, but that e-commerce has gained massive market share this year relative to historical trends and as you think about next year and you're looking to next year, as you start lapping the massive, do you think—what are your thoughts, do you think that e-commerce market share gives up some of the gains before it starts growing again? Or what are the thoughts on the trajectory of e-commerce, say, a year from today we have a vaccine and the world starts to get back to normal?

John Rainey

You're right, Bob, that's an impossible question to answer. I'll share my thoughts with you on this. I think we've seen a permanent step-up in e-commerce. I notice it from my own personal behavior in my household and it's validated by the numerous studies that we do on consumers weekly saying that—and we've all seen figures that 50% of people suggest they're going to continue to shop online. You've got the CEO of Kroger saying that their customers are telling them that they'll continue to shop, buy groceries online. And just one vertical after the next. Will things come down from the peak when the entire world was locked down in a shelter in place? Certainly, because people will have mobility and they've got the latitude to buy in whatever channel that they want.

So I'm not suggesting that we're going to see the peak levels sustainable, but I absolutely believe that we've seen a step-up change in e-commerce penetration relative to what we saw prior to the pandemic. And again, we actually want to put some gasoline on the fire here. This is why we're investing. This is why we're doing QR code, why we want to give contactless options for our customers, because we think that we could help shape some of these trends because it's—and I've joked about it earlier in the call, but the quote that Craig Maurer had in the Journal today was basically essentially saying he sees no reason why once someone uses a digital product to pay somebody else why they'd never go back to cash. And I agree with that. And actually history would tell us that that's largely true. So, I do think that we're seeing sustainable trends here.

Bob Napoli

Thanks. And then just a follow-up. I mean, there's been huge growth in money transfer, digital money transfer. I wondered how Xoom was doing. And then, how do we track your physical retail progress? What are the thoughts and what you might give us to be able to track the progress on physical retail?

John Rainey

Sure. Well, Xoom is doing exceptionally well, and I think that that would stand to reason given the environment that we're in. We don't call out the volume metrics related to that. Look, it's still a pretty small part of our overall volume in our business.

In terms of tracking the retail metrics, we're early on here, and we will provide some indications around how we're doing, the success of that. But this is not something that we're going to be able to measure success in the next quarter or two or three, for that matter. This is going to be a long slog. If it were easy, it would have already been done, and we just think that this is an opportune moment in history where there is a real demand among both merchants and consumers to have contactless options. But when appropriate and when material, we will provide some indication of how we're doing.

Bob Napoli

Thank you.

John Rainey

You bet.

Operator

And our next question will come from the line of Timothy Chiodo with Credit Suisse.

Timothy Chiodo

Thank you. Okay. I want to ask about—you made the comment on the call that at the February investor day you'll be raising the medium term guide. So a clarifier there. What would be the base year that the guide would be based off of?

John Rainey

Well, it'll...

Timothy Chiodo

Would it be 2020 or 2021, I guess, is the question.

John Rainey

You know, I haven't really thought about that, but we'll make it very clear what it is when we do that. I presume it'll be 2020. But I think our comments, Tim, really is just our bullishness around the business and it kind of speaks to the answer I just provided to Bob. We do believe that there's some sustainable tailwinds given what's happening now. We'll also be lapping eBay—or not lapping, but sort of not as reliant on eBay's volume going forward, which will have a higher growth rate for us.

So, very excited about what the future holds and I think there are strong indications that the business will be performing at a higher growth rate level than what it was in our previous meeting in terms of guidance.

Timothy Chiodo

Okay, great. Thank you. Yes, and you kind of hit at what I was getting at. When I was saying if it was off the 2020 base and it would be higher and incorporating the headwinds in 2021, which is very different than starting in 2021 with kind of those headwinds behind you. So—okay, thank you.

John Rainey

But, Tim, to be clear, I don't want to be overly precise here or prescriptive on this. We're really speaking to the overall trends in our business over a multiyear period and we're really excited about what that bodes.

Timothy Chiodo

Okay. All right. Point taken. I follow you. On the eBay headwinds, this is a little bit of a minor one, but when we think about the headwind in Q4, how much of that can we think about as the volume that's gone - and I apologize if you hit on this earlier - versus the repricing of some of the remaining volume, so the retained checkout but perhaps under the new agreement?

John Rainey

It's both. It's both the repricing on the branded piece as well as the mix in terms of those moving to their integrated payments experience.

Timothy Chiodo

Okay.

John Rainey

So not enough to call out one being outsized more than the other necessarily.

Timothy Chiodo

Okay. All right. Very helpful. Thanks a lot for taking my question.

John Rainey

You bet.

Operator

Our next question will come from the line of Josh Beck with KeyBanc.

Josh Beck

Thanks, John, and team for this. Appreciate it as always.

John Rainey

Hey, Josh.

Josh Beck

Hey, John. So, the BNPL came up and there seems to be a lot of optimism around, obviously not this quarter, but where that can go over the next couple of years. So would like to hear what's behind that? And then strategically, obviously, some of those companies charge a premium for that take rate. It seems like you're going with more of the standard pricing. So do you see this bringing in volume maybe from someone else's credit card? Just would like to hear how you think about the business case.

John Rainey

Sure. So let me give you a little bit of a lay of this landscape competitively. We get asked a lot of questions about other payment marks and whether we—how we compete on share of checkout with those payment marks, and consistently we've said and we still see that we compete very well with them. We don't see any appreciable shift in share of checkout when a new payment mark, and whatever name you want to give it, is inserted.

Where we have seen some changes in cases is when these buy now, pay later options are offered, we see our share of checkout be affected. And so that really informs our strategy on this to where we want to provide that same offering so we don't jeopardize any of that share of checkout, or, moreover, given the strong consumer demand among certain demographics for this payment option, we actually see more payment, more share of checkout, more payment volume. And so, we believe the best strategy is to go in and offer basically a free offering for this, where the only monetization is just the take rate model that we have with that merchant that was in place beforehand in probably most cases and there's no incremental fee that all the others are charging to have this additional product.

And so, early indications have been really—everything's been really well received around that and I think your comments around this I think are very much consistent with our thoughts. This is something we're pretty excited about. This is not just the next product that any company has thrown out there. This has the potential to be pretty meaningful for us.

Gabrielle Rabinovitch

Yes. Just I think the other piece too is that we're really bringing a very innovative solution to a long tail of merchants that wouldn't be on the road map for a lot of these other sort of single product buy now pay later programs because there's a sales process involved. And so, essentially very seamlessly we're bringing this solution to our long tail of merchants and providing the ability to compete for the same sales on the same basis with those consumers.

Josh Beck

Okay. That's all really helpful context. Thank you both. And then just quickly a follow-up on Tim's last question there around how much of it is repricing versus volume. So, as we think about next year and as we think about the path, should we assume that the biggest variable is really going to be the volume and kind of the merchant piece that, John, you talked about earlier, or as we go through the year maybe does one of those factors take over? Just any context you can share on just the path and the trajectory there.

John Rainey

I appreciate the question, Josh, though we have not called those out in terms of the materiality of each of those, and so I can't do it here. They both have an impact and both will be noted in whatever we say the impact will be next year, but we haven't called them out separately.

Josh Beck

Okay. Okay, makes sense. Thank you both again.

John Rainey

You bet.

Operator

Thank you. Our next question will come from the line of Jamie Friedman with Susquehanna.

Jamie Friedman

Hi. Thanks guys for doing this call.

John Rainey

Hello, Jamie.

Jamie Friedman

Hi. A couple of questions. So, clearly, great job with the transaction expense at 82 basis points. Record low. I was wondering though, did you see a similar mix shift to debit [cards] that the networks were calling out, which was up debit, down some on credit, and is that relevant to the transaction expense improvement?

John Rainey

So, without being specific in terms of the materiality, we did see a shift to debit. So that certainly has an impact on our numbers as well. And we called that out in the second quarter as well that it was perhaps maybe a little more intuitive in the second quarter as there were a lot of stimulus checks being delivered at that point in time going directly to people's bank accounts. But we have seen a persistent higher level of debit relative to what we've seen historically. And perhaps, some of that is also just consumer behavior.

Jamie Friedman

Got it. Thank you. And then John, also in your prepared remarks in the previous call or maybe in one of your answers you had referred to credit as a headwind next year. I just want to make sure I understood, is that apropos of your prior answer, meaning, as a funding mix or are you talking about credit as it impacts OVAS?

John Rainey

As it impacts OVAS. And by extension, our overall revenue growth and earnings.

Jamie Friedman

Yes.

John Rainey

And look, I don't want to emphasize that too much. Credit's still a pretty small part of our business, but I'm simply trying to provide a couple of the things that are moving year-on-year or are the performance is

different than what we've seen historically. And people have noted that eBay, I think we called that out for sometime is going to have an impact, but credit, our expectation right now, given the macro environment, is that will continue to be a drag on our revenue growth and earnings.

Jamie Friedman

Got it. Thank you for the perspective.

John Rainey

You bet.

Operator

Thank you. And our last question for the day will come from the line of Brett Huff with Stephens, Incorporated.

Brett Huff

Good evening, John, Gabrielle, and Akila. I hope you're all doing well.

John Rainey

Same to you, Brett.

Brett Huff

Two quick questions, all about bigger picture because a lot of the detail was already covered tonight, so thanks for all that. Number one is, Venmo card, heavy focus on QR codes. Understand the Chinese and Asian success with QR code and ubiquity there. Could you talk about that versus tap-to-pay and contactless, etc., and kind of how you're choosing one or the other or straddling? And then the follow-up is, anything on pricing on just the plain vanilla stuff you guys are offering, or is e-com so in demand that you're able to raise pricing, hold pricing better, just any change with that? And thanks in advance.

John Rainey

You bet. So, first on QR code, Brett, our goal is to allow our customers to pay in whatever form they want. And so we don't want to be overly prescriptive on forcing them into a QR code experience. It just so happens though that I think that is the quickest and easiest to launch and we've seen that success in China, as you called out, and perhaps the interoperability aspects of that are much greater than some of the others. And so, that's where our focus has been initially, but longer term you should really hear us talk more about contactless payments versus QR code, because we want to provide whatever capability it is for our customers in terms of their preference.

In terms of pricing, I'll start with kind of the same-store sales pricing is basically still constant, flat. We've not seen any change there. The changes in our take rate are really related to the four items that I called out earlier on this call. But we do continue to get more sophisticated with how we price, and as we look at the various products that we provide out there, there are a number of different ways to price around that.

So, every year we've earmarked certain benefits in our annual plan related to pricing changes. And pricing also goes both ways. We also look at, as I mentioned earlier, with the buy now pay later. I mean, this is one where we're electing to give something away for free because we think there's a greater

opportunity in share of wallet. And so, that certainly cuts both ways, but there are a number of pricing changes that we've got, both implementing right now, as well as in our plans for next year.

So, thank you for the question, Brett. And Holly, I see that we are right at the end of our time. So, I want to thank everyone for their question or questions, and I'm sure that we'll be following up with many of you over the coming days.

So until then, I hope everyone remains healthy and stays well. Take care.

Operator

Once again, we'd like to thank you for participating in PayPal's Quarter Three Analyst call. You may now disconnect.