



Third Quarter 2021 Analyst Call | November 8, 2021

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

John Rainey, *Chief Financial Officer, and Executive Vice President, Global Customer Operations*

Erica Gessert, *Senior Vice President, Finance and Analytics*

Gabrielle Rabinovitch, *Senior Vice President of Corporate Finance and Investor Relations*

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

Sanjay Sakhrani, *KBW*

Ramsey El-Assal, *Barclays*

Jamie Friedman, *Susquehanna*

Robert Napoli, *William Blair*

Timothy Chiodo, *Credit Suisse*

Chris Brendler, *D.A. Davidson*

George Mihalos, *Cowen & Co.*

Josh Beck, *KeyBanc Capital Markets, Inc.*

John Davis, *Raymond James*

Paul Golding, *Macquarie Capital*

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

Operator

Good evening, my name is Carl and I'll be your conference operator today. At this time, I would like to welcome to PayPal's Q3 2021 Analyst Call.

Without further ado, I would like to welcome your host for today's call, Mr. John Rainey, CFO of PayPal.

Sir, the floor is yours.

John Rainey

Thank you, Carl, and thanks everyone for joining us today.

As usual, I am accompanied by Gabrielle and the rest of the Investor Relations team, as well as Erica Gessert, who is another Senior Vice President of Finance here at PayPal.

We look forward to your questions, and, Carl, I'll just turn it back over to you for the first question.

Operator

Thank you, sir.

Our first question comes from the line of Sanjay Sakhrani from KBW. Your line is open.

Sanjay Sakhrani

Thanks.

I had some clarifying questions from the call if you don't mind. John, you mentioned the adjusted growth rates ex eBay this year and next, but if we were to just think about that 18% [revenue growth] you're landing on now for 2022 versus the 20% medium term revenue growth, is the difference between that eBay or supply chain or both? As far as the assumptions you're using, are you using sort of a similar supply chain-constrained backdrop as today, or worse? Then for eBay, do you assume you retain that 50% of branded volumes you expected? I'm just curious on those numbers. Thanks.

John Rainey

Sure, Sanjay. It's good to speak with you.

Let me talk a little bit about supply chain and the assumption there, and then I'll move into eBay, if that's okay. Look, there are probably people that are far more equipped to prognosticate on the effect of what's happening around labor market shortages and logistic issues around supply chain than me, but our basic assumption is that things don't necessarily get worse, but any moderation of that happens slowly over time.

We also, as you think about next year relative to our growth this year, we have the added impact of stimulus measures this year, which we're lapping, and certainly we saw some benefit of that, most pronounced in the first half of the year.

Those are a couple underlying assumptions that go into the model for next year, but I think getting to eBay—I mentioned on the call that if you look at our business ex eBay, the [revenue] growth we expect in 2022 is 22%. I think that really speaks to how the overall business is doing, particularly as the economy is reopening, and as our reliance on eBay is much less going forward.

If you think about that in the context of the medium-term revenue guidance of 20% that we provided [at our Investor Day in February 2021], we're kind of excited to be so early on with many of our initiatives and have that kind of growth. There's going to be a few issues that relate to tougher comps that lead us right now to that high teens percentage point on revenue growth, but again, some of these are exogenous factors. Not as if the last year and a half has been easy to forecast, but they make it more challenging as well, but those are temporary in nature, and certainly we don't expect that to have any long-term impact on our business.

Sanjay Sakhrani

Appreciate that.

Just one quick follow-up, one on the Amazon win. Congratulations on that, by the way. When we think about the economic impact of that deal, is it more about the ability to improve engagement, or do you think it could be decently transaction margin accretive over the next several years?

John Rainey

Well, I don't want to speak to the direct economics of any deal that we do. It is fair to say, and you know this Sanjay, you've followed our business for a long time, with size, comes pricing power. We enjoy that in our business, and certainly some of our merchants that are larger are going to have more favorable pricing than others. You can make an assumption there about sort of relative economics to the rest of our business, but I think primarily for us, to your other point, ubiquity of acceptance is really important for us, whether that's online with merchant acceptance, or even in the offline world. Those are things that we're really trying to emphasize, and so quite excited that we now have placement at what is the largest ecommerce player, at least in the United States, if not the world.

Sanjay Sakhrani

Absolutely. Congrats.

Operator

Our next question comes from the line of Ramsey El-Assal from Barclays.

Please ask your question

Ramsey El-Assal

Hi, guys, and thank you for taking my question this evening.

John, could you help us parse out the OVAS line, sort of what percentage of the outperformance in the quarter there came from those non-recurring factors? The PPP [Paycheck Protection Program] loan forgiveness, I think, was one of them. Then how should we think about that impacting the next quarter, or whether that's just finished this quarter? And how should we think about kind of forecasting that line going forward?

John Rainey

Yes, Ramsey, it's a great question, particularly because the quarter unfolded a little bit differently than what we had indicated with respect to OVAS on the last time we had this call.

We were expecting some of those growth rates to moderate a little bit, but as background, we partner with WebBank on the servicing and origination of the PPP loans, but it's on their balance sheet. So, we actually—for the origination of that loan and the servicing of that loan, we receive a fee. We have to, by accounting standards, amortize that over the expected life or duration of that agreement.

What happened in the quarter—two things, actually—one is that WebBank elected to sell some of those loans. The other is that we processed more forgiveness applications than what we had expected. Those two things combined resulted in an acceleration of the revenue recognition, because effectively that origination and the [associated] servicing obligations have terminated. We recognized more revenue than what you would assume, sort of on a normal basis.

As you think about—getting to your question of what that means for the fourth quarter, we should expect that to moderate much more. I don't have the numbers in front of me in terms of what we were thinking our growth rates would be, but yes, I can remember the last quarter, when we were talking about this—I think we had roughly 50% growth in OVAS last quarter, and our expectation was that that would be pretty much cut in half for the back half of the year.

Now, as it happened, we saw a 50% growth again, but I think assuming something, sort of half of that, for the fourth quarter is probably a good operating assumption.

Ramsey El-Assal

That's super helpful. Thank you so much.

John Rainey

You bet.

Operator

Your next question comes from the line of Jamie Friedman of Susquehanna.

Your line is open.

Jamie Friedman

Hey, John and team. Thanks for doing this call.

I'll just ask a couple at the same time, just to get them out there. I wanted to ask about the deceleration in cross-border TPV—that's Slide 16, John. Is there any call out there why that may have decelerated? I know Q2 was a great one, but that's the first one.

Then, how should we be sizing the volumes for the PayPal button on eBay for the next few years? Are you going to continue to break that out separately, or is that water under the bridge? Thank you.

John Rainey

You bet.

I'm going to take that in reverse order, because I realize that Sanjay asked that, and I didn't get to that part of the answer as well. Our expectation is that we will retain a similar share of checkout to what we enjoy today, which is roughly 50%. You may expect that to decline a little bit over time, but we've witnessed with other merchants, where we've gone down this path, that we retain a very high share of checkout. That's our general expectation going forward.

I did call out the change in [eBay] take rate on the call, going from 4.00% to 2.43% in the quarter. While we retain that share of checkout, it comes at a lower take rate. We do expect that, though, to generally continue.

With respect to cross-border activity, actually, eBay has a lot to do with that as well. We had 17% FX neutral growth, but if you were to look at that excluding eBay, it was 20%. So, we—stronger than what the headline number was but still maybe not as strong as other parts of our business, but cross-border, that was actually quite a difficult comp. If you go back to last year, and you think about how that unfolded with COVID, specifically, Europe was impacted at that point in time, and they went into kind of another lockdown, if I can call it that, and so we saw heightened cross-border commerce in EMEA.

Also, I guess one other thing to add as it relates to the APAC region, that's a region that we're seeing more of an impact from some of the supply chain shortages. Those factors really contributed to what we saw in the quarter around cross-border.

Jamie Friedman

Got it. Thanks for that.

John Rainey

You bet.

Operator

The next question comes from the line of Bob Napoli of William Blair.

Please ask your question.

Robert Napoli

Thank you, and good afternoon. Thanks.

John, so I'll throw my two questions out there as well.

Just to be clear on earnings for next year, EPS, you said you expected like a 10-point headwind from provisions and tax rate, so you're ~\$4.60 for this year, are you looking at a 10% earnings growth rate for next year?

Then my second question was just you're investing quite a bit in buy now, pay later [BNPL], the acquisition of Paidy. Just your confidence on the unit economics, what types of margins do you expect to have on buy now, pay later and returns, your confidence in the credit quality? I mean, your loans were up a good amount this quarter, I think mostly from short term buy now, pay later. Just the overall confidence, what you expect from economics on buy now, pay later? I mean, it's early days in the growth of that industry, if you would, and you're certainly leaning forward into it.

John Rainey

Sure. I'll start, and if any of my colleagues want to jump in, they can.

Let me tackle [non-GAAP] EPS first, Bob. We're not guiding at this point to 2022, and in part because there's uncertainty, but in part because we're actually not finished with our internal plan, and so that's just the reality of it at this juncture of the year, but yes, as noted, we've released \$300 million of credit reserves this year, which presents a real headwind for us next year. It's a tailwind in 2021, but it's a headwind next year.

Then our tax rate, if you just take the most recent quarter, was 7.0% versus 11.6% last year; but even that was sort of artificially low, and so we expect—setting aside anything that's being discussed in terms of legislation around tax rate and potential increases, just the core tax rates in our business should go up. We've benefitted from a couple of audit settlements and one-time things this year, which really have us having an artificially low tax rate.

Those two combined are just mathematically about 10 [percentage] points of [non-GAAP EPS] headwind for us next year.

Then we also, we've got to decide—sharpen the pencil on how much we invest. As I noted on the call, we think that that is hugely important right now. All those factors will influence where we come out on EPS, but also, let me be very clear. We are not backing off of our medium-term guidance of [non-GAAP] EPS growth that we laid out on Investor Day at all. We have a ton of conviction around that, but again, we don't want to be hamstrung or handcuffed to not be able to invest because we're trying to achieve some certain margin performance or EPS performance in one quarter or the next. That hopefully addresses the EPS part of the question.

On buy now, pay later, so there are a couple aspects to that; one is credit quality, the second is margin performance. Credit quality is probably one of the areas that we are most excited about with what

we're seeing on buy now, pay later. Those skew heavily towards debit funding, and we've got great history on our customer base that is electing to use that. The underwriting of those customers comes at a very low risk, and so I think across the board what we've seen on buy now, pay later, our installment pay product, is that the risk performance or the risk losses around that have been much better than what we originally expected, but let me remind everyone about how we monetize that, and that'll get to your question on the margin performance.

We actually don't charge for that to our merchants or our consumers. The way that we elect to monetize that is by increased engagement, or increased transactions, or more TPV. This is one of the things that, again, looking at this early on, we're most excited about, because as we look at those customers that are using buy now, pay later, they have over a 20% increase in engagement, or transactions, or TPV, however you want to look at that. That is precisely the type of performance that we hope for, and in fact, better than what we had hoped for.

Again, we're about a year into this, and still expanding this, as we noted with Italy and Spain, into certain regions, but really pleased about this. Clearly, there is demand among the consumer segment that this product appeals to, so it's a great complement to our existing portfolio of credit products.

Erica Gessert

Hey John, this is Erica.

Can I just add on BNPL—so, to John's point, the BNPL unit economics are basically our branded business economics, because this is just another way to pay in our wallet, but it's that value proposition, and actually the relative pricing of those transactions as compared to our competitors in this area, that has enabled us, for example, to raise our U.S. headline price over the last quarter.

John Rainey

Right.

Erica Gessert

It's really the inclusion of this value proposition that's actually enabling us to raise prices where it's appropriate. Now we lowered our unbranded pricing at the same time, but we see this as an enabler of future unit economics.

Robert Napoli

Great. Thank you. Appreciate it.

Operator

Your next question comes from the line of Timothy Chiodo from Credit Suisse.

Your line is open.

Timothy Chiodo

Great, thanks. Hi, everybody.

Two quick ones. One is around Amazon, which you may or may not be able to help us with, which I totally respect. The second one is more around modelling, but on the Amazon Venmo one, are you able to give us any context around how the button might be placed, whether it's on product pages, at checkout pages, if it will always be there, or sometimes be there? I realize some of this might be part of a test and you'll see how it goes, but if you have any initial indications, we'd greatly appreciate it.

John Rainey

I totally appreciate the question, Tim, but as you suspected, there's limited things that I can say about that at this point. Look, we're still trying to kind of work through that with Amazon, and so it's just a little bit premature to give any color on that right now.

Timothy Chiodo

Okay, no problem at all. We'll stay tuned.

John Rainey

Yes.

Timothy Chiodo

The modelling one then, maybe you could—I think you gave the volume contributions from Paidy, but in terms of the Q4 revenue guide and the initial topline outlook for 2022, could you just give us some context of how much Paidy revenue might be included in that number, and then if there's anything at all, even a minor assumption associated with Amazon Venmo?

Gabrielle Rabinovitch

You know, it's really, it's well below 1% in terms of contribution to revenue.

John Rainey

Yes, so not that material, Tim.

Timothy Chiodo

And then is Venmo included in the outlook?

John Rainey

Venmo with Amazon? Is that what you're referring to?

Timothy Chiodo

Yes, exactly.

John Rainey

We do have a basic assumption around both the rollout and the magnitude of Venmo with Amazon but not something we can disclose.

Paidy is what Gabrielle was referring to that is less than 1%.

Timothy Chiodo

Right, yes. Totally follow you.

Paidy, less than 1%, included in the guide. Amazon Venmo TBD on sizing, but I'm sorry, I just want to clarify, is some assumption included in the outlook for next year?

John Rainey

Yes, that's correct. We do have an assumption in that, yes.

Timothy Chiodo

Alright, perfect. Very, very helpful. Thank you so much.

John Rainey

Okay. You bet, Tim.

Operator

Your next question comes from the line of Ashwin Shirvaikar from Citi.

Please ask your question.

Ashwin Shirvaikar

Thanks. Hey, John, team.

John Rainey

Hey, Ashwin.

Ashwin Shirvaikar

Hey.

I wanted to clarify first, did you explicitly say the tax rate for next year should be in that 17%, 18% ballpark? Is that what you're implying?

John Rainey

We did not say, and we'll give that guidance when we give our full-year EPS guidance. As I noted, there's still some uncertainty right there. Who knows what and when anything will be passed from a legislative perspective? So, we're kind of sitting tight on that one for now, Ashwin, but fair to say that we definitely expect it to be in a zip code north of what we had in the third quarter.

Ashwin Shirvaikar

Higher than third quarter of this year?

John Rainey

Yes, yes. I mean, we were at 7% in the third quarter this year.

Ashwin Shirvaikar

[] I'm trying to also reconcile sort of this year and next year outlook, and I know it's not a formal outlook for next year, but with the five year, right? The starting point, obviously, is important. The reason today's guide down doesn't affect it is because—it doesn't affect the five year is because it basically takes you down to what your outlook was back in February, which is 17% [FXN].

John Rainey

That's correct. Yes.

So, we are right on track with the numbers that we laid out at our Investor Day, when we gave that medium term outlook, because at that point in time, the guide [for 2021] was approximately what we gave on our fourth quarter call, which was roughly the 50 million net new actives and \$25.5 billion of revenue. We feel really good about that, and of course at that point in time, we did not necessarily have an explicit assumption around things like Amazon and things like that, so we're quite optimistic as we look over the next few years.

We've got some exogenous factors and kind of one-time headwinds as we roll off of eBay, but if you look at our core business aside from that, you can do the math and see that our growth rates have been so much higher on our merchant services business, so we feel pretty good about that.

Ashwin Shirvaikar

Got it, got it.

Then I appreciate the lapping comment. I appreciate what you said about the \$300 million of credit reserves, but isn't it also true that on the other side you will not have the eBay impact, especially in the back half of next year? Credit was not really a factor in the first half of this year, right? As the economy improves, presumably, you will be cranking up PayPal credit?

John Rainey

That's right. If I make sure I understand your question correctly—as we begin to grow credit more next year, we're going to have to begin reserving with those new originations. That creates an expense for us relative to the benefit that we've had this year as we've released the reserve that we built when there were concerns around the credit cycle in 2020. The release of that reserve was a tailwind this year, and then as we grow credit, it'll be a headwind next year.

eBay, certainly the back half of next year will be a much more normalized comparison, year-over-year, but the first two quarters of this year, was kind of when eBay really sort of ramped up their transition away. We still do have some year-over-year headwind as I noted in my comments. It's about 200 basis points on a revenue perspective if you think about the impact of eBay on our business next year versus the impact this year.

Ashwin Shirvaikar

Got it, okay. Thank you.

John Rainey

Yes, you bet.

Operator

Your next question comes from the line of Chris Brendler of D.A. Davidson.

Please ask your question.

Chris Brendler

Hi. Thanks, and good afternoon. Thanks for taking my question. Hi John, how are you?

John Rainey

Hey, I'm doing well, Chris. How are you doing?

Chris Brendler

I'm just great, thanks.

I'd love to get some color if you can on the pricing in the U.S. that went through in this quarter, just from effectiveness and any merchant pushback. Are you happy with the roll out? Is there any pricing planned for international in 2022? If it is, is that already included in your guide? Thanks.

John Rainey

Sure. Every year, we do include some assumptions around pricing. I don't want to be specific as to what that is right now. We have a protocol we have to follow on the announcement of that, but we do have some assumption around some pricing increases next year as well. I'll just kind of generalize with that.

Backing up to this, the U.S. pricing increase that we implemented in August—you know, Chris, unless I'm sort of forgetting some price increase in the past, I might even go so far as to say this is one of our most successful. I'm judging that by the receptiveness of merchants, or said differently, sort of the lack of blowback. Keep in mind that I have customer service that reports to me. When they're upset with something, they let us know, they give us a call. Generally, from the feedback that we've received, people understand it.

I think it really goes to the point that Erica Gessert made just a second ago. When you think about the value-added opportunities that we have—as an example, providing installment pay products for free, it's pretty reasonable to assume that we can price to this point. That is the thesis around our pricing, is we want to price to the value that we create.

This has been a really successful pricing increase, but I'm going to take this opportunity, Chris, to address a different point, but somewhat related. If you go back to our last earnings call, we provided a slide in the investor update that talked about a bridge from what our revenue expectations were at that point in time to the end of the year, and there were a number of items that were in that graph. Pricing was one, some of our initiatives was another one, and there were a few more. All of those have really tracked pretty much according to plan. We've been quite pleased with those.

The delta with where we are today is really the starting point as we exited the quarter, this most recent quarter, at a lower rate than what we had anticipated. So, this was really a little bit of that September malaise that I think we saw, like with low consumer confidence numbers, softer back to school shopping, and we just exited the quarter at a lower exit rate than what we had anticipated.

Chris Brendler

That's very helpful. Thanks.

Just one quick follow-up, that chart from last quarter was really helpful. The PayPal initiatives part of that, put in a second box in there, that green box, Venmo, BNPL, fair to say said that's tracking ahead, or at least in line? Because I think it feels like the new initiatives are getting traction. You maybe can't see it in your '22 guide yet, but I do feel like there's been a successful redesign of the app, and I love the Venmo credit card myself. Any color there? Oh, and also crypto?

John Rainey

First of all, we appreciate your business. Don't want to miss the opportunity to say that.

I would say, overall, it's tracking mostly in line. There are a few that are slightly ahead, but I'm hesitant to overstate the impact of any initiative when we've launched it very early on. I like these things to marinate a little bit, and us to see the experience versus making sort of a knee-jerk reaction or

judgement based upon a few weeks or a month or two of data. So, I would say everything is pretty much in line.

Chris Brendler

Great. Thanks so much.

Operator

Your next question comes from the line of George Mihalos of Cowen.

Please ask your question.

George Mihalos

Hey, guys. Thanks again for doing this. Appreciate all the color and your time.

John Rainey

You bet, George. Good to speak with you.

George Mihalos

Likewise, John, likewise.

First question I guess from me is the KPIs for the quarter generally came in in line, just slightly ahead of what we were looking for. The one sort of delta was the average transaction size. That seemed to decline a little bit, sequentially, and I think the last couple of quarters were sort of up double digit. It looks like it was up sort of low singles. Just curious what might be driving that, and how should we be thinking about that as we go into fourth quarter, and then into '22 as well?

John Rainey

You're right. We have been seeing sort of a ratchet up or a tick up in average transaction size, which has really been the result of eBay's declining business as, keep in mind, that there's a lot of people buying little trinkets and Cabbage Patch dolls or whatever that come in less than that mid 60 average price point, and so that's created some inflation there over the last few quarters. I actually don't know off the top of my head what might be driving this right now.

Gabrielle? Erica?

Erica Gessert

I would just say that overall, during the pandemic and the quarters of lockdown, we definitely saw bigger basket sizes, right? That was really because people were just—they were ordering more things for delivery to their home. I think there's a little bit there, and I would also just point back to the kind of overall, just kind of September malaise, as John articulated it. I think we did see September to be very light across the board, and things are picking up a little bit now, but I really think it's those factors.

John Rainey

Yes. That's a good point, Erica.

Likely, George, there's a little bit of the reopening effect in that, as well.

Erica Gessert

Yes.

Gabrielle Rabinovitch

Yes, I think Uber also contributes through Braintree, with the average ride size on Uber being lower than our historical average \$60. So, as we saw some more normalization on the Braintree business, I think that also has a mix effect.

John Rainey

Yes.

George Mihalos

Okay, that's super helpful.

Then, just as a quick follow-up, a little bit on OVAS. Forgive me if I missed it, but the PPP forgiveness contribution, what exactly was that in 3Q? Then I'm curious, John, to the extent, and you can maybe update us a little bit, as to what the revenue contribution is from Honey and iZettle right now. How big is that now within that OVAS line?

Again, thanks, guys.

Gabrielle Rabinovitch

Yes, so we're not disaggregating the component directly from the acceleration of WebBank sale of the PPP loans. We are providing a disclosure in our [10-Q], which will be available tomorrow [November 9], but we can tell you the number. So, I think that the number ran to about \$90 million of benefit overall from PPP, but that was normal PPP plus the benefit from this acceleration, but we haven't disaggregated the total amount. I think it was an important driver, though, of the OVAS revenue for us in the quarter.

John Rainey

The other part of your question, George, was with respect to Honey and Zettle, that's not something we disclose separately but continue to see really encouraging progress with both those, particularly with Zettle launching in the U.S. and beginning to ramp up there. We're excited about the results, but Honey, is—we're building those experiences into the new PayPal digital wallet around commerce, and just quite pleased with what that platform is adding to old PayPal, overall.

George Mihalos

Great. Thanks, guys.

John Rainey

Yes.

Operator

Josh Beck, from KeyBanc, you are next.

Your line is open.

Josh Beck

Thank you, John, and team for the time, as usual.

John Rainey

You bet, Josh.

Josh Beck

Yes, and congrats on the Amazon announcement. I had always backed them out of my TAM [total addressable market] calculation for you all, so I will have to update that.

So, I'm curious, what do you think got them over the hump? Obviously, Venmo's been a success for years and years, so I'm curious maybe, what was the external change that made this happen, if there's anything you can share there? I know it's sensitive.

Then, secondarily, just wanted to ask about social. Obviously, that's been a rising influence, other companies, Shopify and others have spoken to this. I'm just curious, kind of like you've achieved with Amazon and some of these other partnerships, do you feel like you'll have a similar opportunity, shots on goal, to have a similar type of market share in social as you do in traditional?

Kind of a loaded question there, but that's all of it.

John Rainey

With respect to Amazon, it's not one thing that necessarily contributed to this. It's a multitude of things, and keep in mind that we've been in discussions with Amazon for a number of years. In fact, there are parts of our business that—we were actually already doing business with them on some of our payout services internationally, and then they actually [team up] with Paidy today.

So, I think it's the culmination of a lot of these different things, where we just began to develop that and prove that relationship over time, but I think, we can't ignore the fact that Venmo just has a lot of caché among the Millennial demographic. That is perhaps the most coveted demographic of spenders that

exist today. I think that that is an addition or an improvement to the service that they provide, but it's also the same thing for us as it gives our users yet another large merchant to use their cash or whatever their funding instrument is for Venmo, so quite excited about that.

On social, look, I recognize there's a question within a question there, probably a multitude, but that's something where we've been working for a long period of time, whether it's kind of some of the experiences that we're powering with Instagram and Facebook around contextual commerce, and certainly have explored that with others, and we certainly—I think that is where the puck is going, as people say. We enjoy a great platform today that is, I think, the very definition of social payments in Venmo. This is kind of a natural extension of that, and we'll continue to explore opportunities around that.

That all plays into the strategy that we've had with the acquisition of Honey, and what we can do with some of their capabilities, and so I think this is an important aspect of the future of payments, and it's something that we want to continue to invest in.

Josh Beck

Very helpful. Thanks, John, and the team.

John Rainey

You bet.

Operator

Your next question comes from the line of John Davis of Raymond James.

Please ask your question.

John Davis

Hey. Good afternoon, guys.

John Rainey

Hey, John.

John Davis

John, I really just want to start on the net new actives. As we look out, not just to 2022, but beyond, obviously your mid-term guide assumes some acceleration beyond the 55 million or 52 million NNAs ex Paidy this year. Just, maybe what is the assumption at a high level—not looking for specific numbers here—around gross ads versus the improvement in churn? Obviously, I would assume this year would have the highest churn, just given all the new ads last year, but maybe just talk a little bit about how churn plays into that and kind of what we can expect from net new actives going forward, not just in '22, but beyond.

John Rainey

Sure.

John, I'll start at a higher level, and then Erica is more of the expert here, so I'm going to defer to her on some of this. I think a good assumption is that with each passing year, we should begin to see more and more of a benefit from churn. Appreciate, as we're over 400 million users today, or accounts today, there's a significant amount of churn each year.

Our focus really, historically, has been much more top of funnel, but bottom of the funnel becomes much more important as we look forward, which is why we're so focused on these experiences where it's increased engagement opportunities, because that, by definition, is reducing churn. As we add each incremental product, whether it's a savings account or the ability to buy, hold and sell crypto in the U.K., or buy now, pay later in Europe, whatever it is, all of these things are additional opportunities for people to engage with us, and hence, see less churn.

Erica, do you want to add anything else?

Erica Gessert

No. I think you covered the crux of it, John. I would just say for absolutely each and every year, particularly as we go to kind of 2023 and beyond, we certainly expect products like the digital wallet and others to improve that engagement, and so churn rates to start to decline as well.

I think that the top of the funnel is still important to us. We've been very pleased with the ongoing strength in core markets of our top of the funnel acquisition, and it continues to be very, very strong.

We also do expect to get new sources of acquisition from investments, like in Japan and in China and other places like that. That's going to be a few years out, so not next year, or even the year after, but I think that's out there in our outlook as well.

John Davis

Okay.

So, surmise it to say that your outlook doesn't necessarily assume that top of funnel gets significantly bigger. It's kind of, maybe I guess a little bit bigger, but improvement in churn is definitely a big driver. Is that fair to say?

Erica Gessert

Yes.

John Rainey

That's correct, yes.

John Davis

Okay. Then just, a quick follow-up. I appreciate the comments on the margin headwinds from the reserve releases next year, but just going forward, any reason to assume that you wouldn't see some modest amount of operating leverage and kind of improving margins on a year-over-year basis, kind of ex-ing out one-time items, kind of like the reserve releases this year?

John Rainey

We should continue to see operating leverage. It's not been as evident recently, as we've invested heavily into our business. You've got the noise that's present with eBay, but we manage our business to really realize that operating leverage. That's one of the great things about our business is being able to scale at a very low marginal cost.

Like as a BAU, or business as usual perspective, you're going to see that operating leverage. The only thing that's going to take away from that is if we electively decide to invest a lot more from one period to the next, which we will only do because we think that that presents a growth or a profitable opportunity for us that is too precious not to invest into.

John Davis

Okay. Very helpful. Thanks.

Operator

Our last question comes from the line of Paul Golding of Macquarie Capital.

Please ask your question.

Paul Golding

Thanks so much for taking my question.

John, I had a question around QR. I know as part of the guide you were sharing that there could be some mix shift as far as lack of confidence in delivery, moving volume to in person, so that's where I think of your deployment of QR. Anything you can share on merchant deployment? I know you talked about a few of the winds, but anything with TPV relative to other initiatives? Any clarity there? Thanks.

John Rainey

To be very clear, Paul—and first, thank you for the question.

There's no lack of confidence around the opportunity in QR code. That said, we've noted for multiple quarters now that this is not an easy lift. This is something that will take some time. We are being very patient here, but it's also one of those areas that we're investing in. We continue to make progress, good progress each quarter with more and more merchants that are accepting that, and not only that, but improving the experiences as we learn from this.

As you roll out what is effectively kind of a new product for us, you learn things like latency at the time of purchase, and how to improve upon that, and the importance of educating the customer base at the merchant. All of those are adding to improvements as we roll this out, but the takeaway for me, like the thing that I look at that I am so encouraged by, is the TPV lifts, or the engagement lift. Not only have we seen that lift that we expected, and we noted in the last quarter that it was roughly a [19]% engagement lift, it's actually accelerated.

We're at close to 20%, now, which actually just emboldens us to want to do more in the space because it is absolutely validating what our initial expectations were and then some, but you're changing consumer behavior, which is a long, slow process, and so we've got metered expectations around the impact of this overall on our business, and this is something that success will be measured in years, not the next few quarters, but really encouraged by that TPV lift that we're seeing among the customers that are using QR codes.

Paul Golding

Yes. Just to clarify, I was referencing Dan's comment around the consumer being concerned with delivery of products and buying them online, and so maybe more mix shift going to store, not delivery on QR. It seems like you're having a lot of success there.

John Rainey

Yeah. Nothing more to add there.

Paul Golding

Okay.

John Rainey

The holiday season is always sort of a difficult one to forecast, and I think what he was noting is that this is even more so, with concerns around supply chain. So, if you can go to the store and you actually see it right there versus maybe needing to wait to have that shipped, it could have some impact on our business, but I wouldn't emphasize that point too much. I think that's kind of a footnote to the bigger discussion.

Erica Gessert

Yes. I think Dan was just referencing the fact that I think we're probably just thinking that the holiday season, especially as you approach kind of Christmas and those holidays, it's just a little bit more uncertain than in other years because of that.

John Rainey

Yes.

Sorry I misunderstood your question initially.

Paul Golding

Oh, no worries.

In the same vein though, on deals for the new app, are you hearing anything from your merchants that there's some limitation on what they're able to post through you from a supply constraint perspective? Is there upside if things loosen up a little bit from that?

John Rainey

No. We don't really—we're not going to hear things that are more SKU or product-related around supply concerns as it relates to experiences that we build out. We certainly do see that I think the SMB segment is probably hit the hardest with these issues. If you've got 1,000 widgets to sell to a merchant that goes into a product that they're making, it's going to go to a Target or Walmart before it goes to Betty's Cupcakes. So, I just think that they're probably disproportionately hit, and that affects our business, and we're seeing that to an extent, but nothing from a product experience that I would call out.

Paul Golding

Great. Thank you so much.

John Rainey

You bet.

Well, I want to thank everyone for joining the call today and appreciate all the questions. We'll certainly be following up with many of you in the coming weeks and days.

Thank you very much, and everyone have a great rest of the evening.

Operator

Thank you again for participating.

This concludes today's conference call.

You may now disconnect.