

# Hyperion Asset Management

## Company Profile

## PayPal Holdings Inc

### **Main Business Activities**

PayPal Holdings Inc (PayPal) was founded in 1999 and in just over 20 years has grown to become the world's leading digital and mobile payments company, facilitating transactions across numerous platforms in both the online and offline world. PayPal has a network of 416 million active accounts which include 33 million merchants. The company operates in 205 countries and facilitates payments in over 100 currencies.

PayPal's core digital payments business was initially developed to securely enable online transacting and e-commerce. Historically, a barrier to e-Commerce was that the consumer did not know or trust the merchant they were purchasing from. PayPal concealed the customer's sensitive account information from the merchant and most importantly provided peace of mind. Since then the business has expanded through both organic innovation and acquisition. Core business lines today include:

- Braintree – a leading global payment gateway that powers transactions for large platforms including Airbnb and Uber;
- PayPal Credit & PayPal working capital loans – Consumer credit and small business lending;
- Venmo a Peer-to-Peer (P2P) payment platform that has over 80 million annual active users;
- Xoom – International remittance;
- Honey – an online merchant and consumer platform offering e-commerce discounts and rewards;
- Paydiant and partnerships with issuers – Integration of in-store merchant reward programs;
- iZettle – Physical card readers and POS software; and
- PayPal Pay-in-4 – Buy now, pay later offering consumers to pay products off in installments.

Over time PayPal intends to become a financial services super app. The company's digital wallet functionality will increase meaningfully and is expected to include new payments, commerce, and financial products and services over the coming years.

PayPal has also made several investments in large marketplaces in order to defend their position as the leading and first choice payment provider. These include MercadoLibre (\$750 million) and Uber (\$500 million).

### **Key Value Proposition to Customers**

The key value proposition to users is security, speed, convenience, and over the longer term will be the ability to access a range of financial services in one place. For merchants it is scale of network, high checkout conversion rates, and ease of integration.

The consumer specific value proposition includes:

- Security - rather than sending payment credentials to a merchant a consumer may not have an existing relationship with or trust, they can make the payment via their PayPal account. Payments are covered by PayPal's buyer protection program which provides refunds for fraud;
- Speed - credit/debit card details are saved on PayPal which removes the need to re-enter details at time of purchase, only a username/password is required to transact.
- Innovation - like OneTouch reduce friction even more (biometric authentication);
- Convenience – A digital wallet where consumers can use a variety of funding sources to complete a transactions at over 33 million merchants. PayPal has a strategic focus on expanding 'merchant ubiquity'. Venmo is a popular P2P platform, enabling users to send funds to the friends in an easy and engaging way. Today Venmo has more than 80 million users; and
- Broader financial services offering - PayPal is expanding the functionality of both its traditional and Venmo App with early examples being cryptocurrencies and a Buy-Now-Pay-Later (BNPL) offering. PayPal has also stated it will incorporate features such as direct-deposit, cheque cashing, budgeting and savings tools etc. over time.

The merchant specific value proposition includes:

- Unrivalled scale - PayPal has 383 million potential customers merchants can access;
- Checkout conversion - OneTouch has taken the average checkout time from two minutes (with a regular PayPal account) to 11 seconds. PayPal's conversion rates are markedly higher than other digital wallets and payments overall. Furthermore, higher conversion rates dramatically increases sales for merchants;

- Ease of integration - PayPal and Braintree can be integrated into a merchant's digital checkout with minimal friction; and
- Merchant protection program - Protects merchants from financial loss resulting from fraud and counterparty non-performance. PayPal's program is generally broader than similar protections provided by competitors, and as a result, merchants may incur lower losses for chargebacks and other claims than when using competitor solutions.

Finally, PayPal is innovating rapidly to grow the number of potential use cases, reduce transaction friction and increase checkout conversion, further enhancing the value proposition to both consumers and merchants.

### ***Sustainable Competitive Advantages and Outlook***

PayPal's first-mover advantage and resulting two-sided digital network combined, with industry-leading conversion rates at checkout and constant product innovation, result in an extremely strong and sustainable competitive advantage. The margin by which PayPal's network leads any other digital payment alternative makes it the obvious choice for merchants to have in their checkout. Given the company's dominance it is essentially irrational for a merchant to not accept PayPal at checkout even at a premium to alternatives.

Over time growing merchant and consumer adoption strengthens the network effect. As the world continually shifts to online and mobile first merchants are essentially forced to upgrade their checkout functionality. Given PayPal's brand and reputation as well as scale it is almost always the case they are front of mind.

Additionally, the competitive landscape has improved meaningfully following PayPal's decision to open up their platform and partner with other payment providers such as Mastercard and Visa, Facebook, Google and Android Pay, Vodafone, as well as issuing banks and payment processors. We expect PayPal will continue to play a dominant role in the global payments industry for the foreseeable future.

### ***Overall Company Growth Options***

Long-term organic growth will be fuelled by the ongoing digitisation of cash as well as the structural shift to e-commerce and mobile commerce from brick-and-mortar retail. Many merchants will have to upgrade their existing online presence and digital checkout to be mobile-first which will be to the benefit of PayPal and its product suite. Currently around 60% of retail research is undertaken on mobile however only 10% to 15% of transactions are completed through the medium.

PayPal has defined an overall total addressable market opportunity of greater than \$110 trillion spread across online retail, Peer-to-Peer and remittances, in person services, business-to-consumer (B2C), in-store retail, digital services, emerging market payments, government payments, asset trading, as well as business-to-business (B2B) and other non-cash payments. We believe the company is extremely well positioned to capture these opportunities given it is the dominant two-sided consumer and merchant digital network with market-leading conversion rates, strong brand and reputation, and a constantly improving product suite.

PayPal has now also outlined they will expand both the Venmo and PayPal wallet functionality with the long-term goal of becoming a financial services super-application. Early examples of product expansion have been enabling cryptocurrency in-wallet as well as rolling out a buy now, pay later offering. Longer-term plans include offering savings and budgeting functionality, additional payment tools, and commerce focused products and services.

Lastly, management are targeting 750 million annual active users by 2025 and have an aspirational 1 billion daily active users (DAU) target over the long term. PayPal believe the COVID-19 pandemic accelerated the shift to online and digital payments by three to five years and as result saw a significant acceleration in user acquisition. The company has now stated they expect elevated user additions to continue into the medium term, with the business and broader digital payments industry having experienced a step-change in both growth and adoption.

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