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Visa, Inc. (V)

Q2 2014 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to Visa Inc.'s fiscal Q2 2014 earnings conference call. All participants are in a listen-only mode until the question-and-answer session. Today's conference is being recorded. If you have any objections, you may disconnect at this time.

I would now like to turn the conference over to your host, Mr. Jack Carsky, Head of Global Investor Relations. Mr. Carsky, you may begin.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

Thank you, Adrienne. Good afternoon, everyone, and welcome to Visa, Inc.'s fiscal second quarter 2014 earnings conference call. With us today are Charlie Scharf, Visa's Chief Executive Officer, and Byron Pollitt, Visa's Chief Financial Officer.

This call is currently being webcast over the Internet. It can be accessed on the Investor Relations section of our website at www.investor.visa.com. A replay of the webcast will also be archived on our site for 30 days. A PowerPoint deck containing financial and statistical highlights of today's commentary was posted to our website prior to this call.

Let me also remind you that this presentation may include forward-looking statements. These statements aren't guarantees of future performance, and our actual results could materially differ as a result of a variety of factors. Additional information concerning those factors is available in our most recent reports on Forms 10-K and 10-Q, which you can find on the SEC's website and the Investor Relations section of our website.

For historical non-GAAP or pro forma related financial information disclosed on this call, the related GAAP measures and other information required by Regulation G of the SEC are available in the financial and statistical summary accompanying today's press release. This release can also be accessed through the IR section of our website.

And with that, I'll now turn the call over to Byron.

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

Thanks, Jack. Let me begin with my usual callouts and observations.

First, turning to revenue, as expected and previewed on our call last quarter, revenue growth moderated during the quarter, growing 9% year over year on a constant dollar basis or 7% nominally, which includes the expected two percentage points of FX headwind we had been guiding to since the beginning of the fiscal year. As a reminder, the current Q2 is lapping 15% revenue growth in the prior-year quarter, which benefited from a number of favorable one-time adjustments.

Looking ahead to Q3, we expect nominal revenue growth to be in the mid-single digits, which could be a couple of percentage points below Q2's growth rate. As signaled on last quarter call, a softer Q3 growth rate was also anticipated given continued FX headwinds of two percentage points, a 17% revenue comp in the prior-year

quarter, also driven in part by one-time events, and a moderation in cross-border spend, which we view as short term.

After two softer quarters, in fiscal Q4 we expect to see constant dollar revenue growth more reflective of the secular shift as well as the e-commerce and mobile trends that have driven and will continue to drive attractive growth for years to come. As a footnote to fiscal Q4, we expect very little impact from Chase card conversions, particularly given our quarter lag in reporting of service fees. This event will have more impact in fiscal year 2015.

Our guidance for client incentives remains unchanged. Despite delivering first half client incentives as a percent of gross revenues of 15.8%, we expect incentives to be second half weighted and finish the year within the current guidance of 16.5% to 17.5%. On a full fiscal year basis, we now expect our guidance of low double-digit constant dollar net revenue growth to be in the 10% to 11% range, with a negative two percentage point impact from FX.

Now let's turn to payment volume and transaction growth. On a constant dollar basis, global payment volume growth was 12%, unchanged from Q1. U.S. payment growth for Q2 was 8%, also unchanged from Q1. With a boost from Easter timing and better weather, U.S. payment volume growth for the first 21 days of April rose to 12%.

The deceleration in cross-border growth seems to be bottoming out. Q2 constant dollar growth was 8%, four percentage points down from Q1. But the first 21 days of April registered 7% growth, nearly flat to Q2. Cross-border weakness is pronounced in Latin America, as in Brazil, Argentina, Venezuela, the Canada to U.S. corridor, and Russia. Visa processed transaction growth was a healthy 11% in Q2 and rose to 14% for the first 21 days in April. Taken together, we are seeing a sustained economic recovery but no signs yet of acceleration.

A word on Russia and Ukraine; we have clearly seen a drop-off in cross-border volume, and sanctions are expected to have some impact on volume. Our guidance assumes several pennies of EPS impact for the fiscal year. We are fully engaged with all parties involved and will continue to adjust our outlook as the situation clarifies over time.

Next callout relates to our effective tax rate for the period. At 22% for the quarter, our rate was positively influenced by the recognition of tax benefits under IRS Section 199, which allows for the deduction of a portion of the income related to U.S. domestically produced computer software. As a reminder, successfully employing strategies to manage our tax rate lower has been a consistent component of our earnings guidance since we went public in 2008 and will continue to be in the future.

The total benefit to the quarter was \$218 million, \$184 million of which represented prior years and \$17 million of benefit for each of the first two fiscal quarters. We expect an additional \$30 million to \$35 million of benefit over the remaining two fiscal quarters and a continuing benefit in future years. Accordingly, we are adding to our guidance for fiscal 2014 a full-year tax rate approaching 30%. Please note, this rate was contemplated in our full-year EPS guidance for fiscal 2014.

Last callout, we remain bullish on our future growth prospects and fully committed to returning access cash to our shareholders. To this end, we repurchased a total of 5.1 million shares during the quarter at an average price per share of \$217 and change, resulting in a total cost of \$1.1 billion. This leaves an outstanding open-to-buy of \$3 billion at the end of March. And as always, we will take advantage of market movements to effectively repurchase at attractive rates.

Now let me dive a little deeper into the numbers. As noted earlier, global payment volume growth for the March quarter in constant dollars was 12%. The U.S. grew 8% and international grew 16%. Drilling down further for the March quarter, U.S. credit growth was 11%, slightly higher than the 10% in Q1. Through April 21, credit improved

to 14% growth. U.S. debit was 7% in Q2, flat compared to Q1. And through April 21, debit also improved, rising to 11% growth.

As mentioned earlier, global cross-border volume delivered an 8% constant dollar growth rate in the March quarter, down from 12% in the December quarter. The U.S. grew 7% and international grew 8%. Through April 21, cross-border volume on a constant dollar basis grew 7%, with the U.S. growing 8% and international registering 7% growth.

Transactions processed over Visa's network totaled 15.4 billion in the fiscal second quarter, an 11% increase over the prior-year period. The U.S. grew 7% while international delivered 23% growth. Through April 21, processed transaction growth rose to 14%.

Now turning to the income statement, net operating revenue in the quarter was \$3.2 billion, a 7% increase year over year, driven primarily by growth in both domestic and international transactions and, as mentioned earlier, negatively impacted by a two percentage point foreign currency headwind.

Moving to the individual revenue line items, service revenue was \$1.5 billion, up 7% over the prior year, and was driven by moderating global payment volume growth. The difference between the 7% reported revenue growth and the 12% growth in constant dollar payment volume is largely due to three percentage points of negative FX. Visa service fees are disproportionately impacted by foreign exchange translation compared to other revenue lines.

Data processing revenue was \$1.2 billion, up 7% over the prior year's quarter, based on solid growth rates in Visa processed transactions both in the U.S. and internationally. The difference between 7% revenue growth and 11% transaction growth in the period was due to one-time FANF accrual reversals in the prior year in combination with the influence of the fixed fee component associated with the FANF pricing structure that does not grow with transactions. International transaction revenue was up 5% to \$871 million, reflecting some moderation of growth across the globe that first impacted us at the outset of calendar year 2014.

Total operating expenses for the quarter were \$1.1 billion, up 2% from the prior year. Certain expenses have been rephased to the Q3 and Q4 fiscal quarters. And as signaled last quarter, we continue to expect elevated marketing investments in Q3 and Q4 relative to Q1, tied to the 2014 FIFA World Cup event.

Operating margin, 65% for the second quarter, ahead of our annual guidance of low 60s% but consistent with our expectations for higher expenses in the fiscal third and fourth quarters. That said, we now expect our full-year operating margin to be in the low to mid-60s%.

Capital expenditures were \$97 million in the quarter. At the end of the March quarter, we had 629 million shares of Class A common stock outstanding on an as-converted basis. The weighted average number of fully diluted shares outstanding for the quarter totaled 634 million.

Finally, given our year-to-date results and our outlook for the balance of the year, let me recap our full-year guidance: constant dollar net revenue growth 10% to 11%, with two percentage points of negative FX impact; client incentives in the 16.5% to 17.5% range; operating margin in the low to mid-60s%; tax rate approaching 30%; EPS growth of mid to high teens; free cash flow of about \$5 billion.

And with that, I'll turn the call over to Charlie.

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Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

Thanks a lot, Byron, and good afternoon, everyone.

Let me start with a couple of comments about the quarter and reiterate some of the things that Byron had said. First of all, probably most importantly to us as we look at our results underlying what we see, the business drivers for the most part remained steady from last quarter. Specifically, U.S. spending levels grew consistent with that of the prior quarter, not accelerating or decelerating, but still reasonably strong. And as Byron had mentioned, April is off to a strong start, which is certainly encouraging for us.

Non-U.S. domestic spending grew at consistent levels as well, and non-U.S. cross-border spending was weaker. And as Byron mentioned, it's from very specific corridors which we can certainly talk more about.

Revenue growth came in where we expected. And as we mentioned, it was impacted by the strong U.S. dollar and these non-recurring comps from the prior year. And we expect these effects to be slightly more pronounced in the third quarter. And looking even beyond the third quarter, we would expect in the fourth quarter to see revenue growth more reflective of the strong payment volumes that continue to underpin our quarterly results.

Let me move now for a second and just describe what we see in Russia. As I'm sure you all know, the U.S. government imposed economic sanctions a few weeks ago, which has forced us to take action. We are complying with U.S. law, as you would expect, which means that two affected banks cannot issue or acquire transactions for Visa. These banks represent less than 1% of our volume in Russia. And you would expect that we would continue to comply with U.S. law as the sanction situation evolves. As of now, all Visa systems are processing normally. We continue to serve all of our other clients in Russia today.

Due to U.S. sanctions, the Russian Duma is working on modifications to the current national payments system law. President Putin has directed the Duma to pass a series of changes, which could pass as early as tomorrow. The proposed modifications are evolving, but as we understand them, could include the following. First of all, all domestic data processing would need to be onshore. Second, most domestic transaction data would need to remain domiciled within Russia. Third, a payment network must provide continuity of services, in compliance with Russian law. Fourth, the creation of a settlement center 100% owned by the central bank of Russia; fifth, a collateral requirement for foreign payment systems; and lastly, the ability to impose fines on foreign payment system providers.

Keep in mind this is all still fluid. And while none of this is certainly helpful for Visa if passed, parts might even cause us to rethink our domestic processing opportunity in Russia. But we're hopeful that there are still opportunities for Visa to participate in the growing electronic payments business in Russia. We will not understand the impact on our business and potential future until the laws and regulations are completed, but we remain committed to finding ways to provide our services as long as the U.S. government and Russian government allow.

On the legal and regulatory front, not a lot to talk about this quarter; as I'm sure you know, in late March the U.S. Court of Appeals for the DC Court ruled that the Federal Reserve acted properly in its interpretation of Dodd Frank, a result which we're obviously pleased with.

A quick update on payment security and specifically industry collaboration; last quarter I spoke at length about the need for the industry defined broadly to work together to create payment standards and improve security. We believe there is an opportunity for this collaboration to occur and are encouraged. We and MasterCard have

formed a cross-industry working group to accelerate this joint collaboration. The purpose is to work with a broad group of participants in the payments landscape, not just to move forward to more secure technologies in the short term, but to think in the long term as well.

This includes driving EMV adoption. But it looks to create a clear roadmap for the future of payment security, inclusive of both physical, POS, as well as card-not-present transactions. The group will have representation of banks of all sizes, credit unions, acquirers, retailers, point-of-sale manufacturers, and industry trade groups. We also look forward to broad network participation so we can be as effective as possible.

On EMV specifically, First Data's STAR network, FIS's NYCE network, Discover Financial Services' PULSE network, and other regional network providers have agreed to participate in the common debit solution that Visa introduced last year. The collaboration between Visa and our partners will help enable the deployment of debit EMV solutions. This is again an example of industry players working together to move payment security forward.

Let me talk for a second about tokenization. The standards, services, and technologies we're working on will play an important role not just in security, but in enabling and securing new payments experiences in the online, mobile, and face-to-face channels. We're making progress on our work towards getting it into the marketplace. The token standard that we, MasterCard, and American Express jointly wrote and sponsored has been adopted by EMVCo, the industry standards body and is currently in a comment period across the other card networks, banks, and security industry groups.

We will be rolling out our token services, capable of associating a limited-use Visa token with an underlying card credential and are working with issuers, processors, and acquirers to introduce the first wave of token programs. You will see applications deployed within the next 12 months, and these tokens will play a role in our offerings but also those of select strategic partner engagements, ranging from remote, online, or mobile purchases to proximity mobile interactions.

We have also talked a great deal about our merchant efforts. We recently reorganized the company to strengthen the outreach to our merchant partners. We are lucky to have hired Ramón Martín, a well respected industry expert in payments with a great deal of merchant knowledge. As an example, he has a history as a member of the Board of Directors of the National Retail Federation. We're excited that he'll lead our efforts relative to our merchant strategy and help deliver customized products and services and look forward to discussing more specifics in the future.

Let me now just turn for a second and just talk about small business merchants. We have made changes to our FANF structure, our Fixed Acquirer Network Fee, including modifications that are designed to lower or in some cases eliminate FANF on volume from small merchants with less than \$15,000 in annual gross Visa sales. Most importantly, we believe these changes could serve to expand Visa acceptance among very small businesses. While eliminating the fees for smaller retailers, we're also making other adjustments to FANF to improve the alignment of these fees, regardless of whether a merchant connects to Visa through an acquirer, a processor, a payment facilitator, or other party.

We've also talked on these calls about rules in the past and our efforts to simplify our operating regulations. On October 1, we will be eliminating close to half of our operating rules. This includes reducing the complexity of our dispute resolution processes. And while we're making substantial changes now, we continue to get client feedback and will continue to introduce more changes beyond.

I want to talk for a second about Japan. I have spoken about two things here in the past, both the opportunity within Japan, but also the importance of growing our processing business globally. Just a reminder that although

Japan is the third largest economy in the world by GDP, the number of payment cards in the market and usage is still very low, only 14% of PCE and just 8% on Visa products.

Earlier this month, we acquired 100% ownership of GP Net, a joint venture that we had founded with seven leading Japanese issuers back in 1995. As a result of having total control, we now control our domestic transaction processing activities. It will allow us to further integrate our processing and product solutions to merchants, acquirers, and issuers, something that we're very excited about.

We're also very focused on the debit opportunity in Japan. While debit is still considered in its infancy stage, there is a meaningful opportunity for growth, given the large deposit base which exists in the banks from which to grow the debit business. As an example, this quarter we launched Visa Debit with Bank of Tokyo-Mitsubishi, one of the three megabanks. Again, it's just one example of how we're working collaboratively with the banks to target a very meaningful opportunity.

So to conclude, let me just make a couple of comments looking ahead. First of all, I continue to remain very excited about the opportunity that we have to continue growing the business. While the strengthening U.S. dollar and difficult comps from the prior year have affected our reported revenue and will again next quarter, the underlying revenue growth of the business is strong. It will accelerate as the economic recovery accelerates as well. And most importantly, the long-term secular trends and our competitive position remain as strong as ever. And I'm constantly reminded that there is more cash to disintermediate today than when the company went public in 2008.

And with that, Byron and I are glad to take your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question is from Sanjay Sakhrani from KBW. Sir, your line is open.

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

Q

Thank you. I guess I just wanted some more context around some of the comments Byron had about the volumes. Byron, you talked about cross-border weakness being temporary and seeing some firmness in the decline. Could you just talk about what gives you comfort that we could rebound from here, or at least flatten out?

And then second, you guys talked about sustained economic growth and non-accelerating growth. Is that simply just by observing the absolute volume statistics, or is there something else you're seeing underneath the covers that leads you to believe it's more sustained versus accelerating? Thank you.

Byron H. Pollitt
Chief Financial Officer, Visa, Inc.

A

So let me start with cross-border. We haven't seen single-digit cross-border growth rates since I would say 2009. That was five years ago. And given the underlying secular trends in our business, none of those are diminished. None of those are going away. As Charlie said, there's more cash to disintermediate today, note, outside the U.S. in particular than there was when we went public. So from our standpoint, we looked at cross-border. The fundamentals are still in place. It recovered nicely from 2009. So we expect to see the same; hard to predict when and it may be a little early to call given the April results. But given the four percentage point drop we saw between

the two quarters and given the fundamentals underpinning this secular shift, our view is we could be reaching a bottoming out. And in any event, looking forward we would expect this to move north.

In terms of the broader economic question of sustained recovery, this is very much anchored in the volume trends we're seeing, recognizing that there is modest if not weak job creation in the U.S. At some point that will begin to accelerate, but we are adding jobs, so the underlying fundamentals that should inform and drive spend are in place. They're just in first gear. And so that's our take on the environment. Charlie, would you like to add?

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

The only thing that I'm going to add, back to the first part of the question on cross-border, as Byron and I both pointed out, the corridors that were seeing the weakness are very, very specific places. So for instance, when you look at U.S. cardholders traveling abroad, that volume – those growth rates are actually flat quarter to quarter, which is obviously a good sign for U.S. and the help of the U.S. consumer; again, very, very specific places and not at all across every single geography, which would give us more cause for concern.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

A

Next question.

Sanjay Sakhrani

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Can I ask one more follow-up, if you don't mind? Embedded in your guidance is what assumption around cross-border growth for the rest of the year?

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

No acceleration.

Sanjay Sakhrani

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay, great. Thank you.

Operator: Our next question is from Tien-tsin Huang from JPMorgan Chase. Your line is open.

Tien-tsin Huang

Analyst, JPMorgan Securities LLC

Q

Great, thanks. Just to clarify, is the revenue revision at the high end of the revenue outlook, is that really just explained by cross-border, or is there something else? I just wanted to clarify.

And then just maybe on the Russia front, did you disclose how much it represents in terms of revenue today? And I'm curious as a bigger picture question, sorry to build on this. But does this Russia situation build this case that maybe more countries are going to consider creating their own domestic schemes like the ones that Putin is talking about? Thanks.

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

I'll tell you what, Tien-tsin, could you re-ask your first question? I didn't actually understand it.

Tien-tsin Huang

Analyst, JPMorgan Securities LLC

Q

Yes, sorry, I'm rambling a little bit, Byron. The first question in a simple way, is the revenue revision in terms of your outlook – I think you said it was 10% to 13% before. Now we're looking at 10% to 11%, if I heard that correctly. Is the difference there just cross-border, or is there something else?

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

It's heavily driven by cross-border. We would also add that U.S. debit downshifted more than we had anticipated when we constructed the original range. And so I'd say those are the two primaries.

Tien-tsin Huang

Analyst, JPMorgan Securities LLC

Q

Understood, and then on the Russia stuff?

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

On the Russia, let me answer the first part of the question, which is the revenue part, and then I'll turn it back over to Charlie for the second part. When we said that there were several pennies of impact, you may attribute 100% of that to revenue, and we didn't put any expense offset against that. So it would be the revenue equivalent in this fiscal year heavily weighted – I'm just looking – 90% weighted to fiscal quarters three and four.

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

And the only thing I would just add on that point and then going to your last point, Tien-tsin, is remember, we don't know exactly what our position will be in the marketplace. So the issues that exist really today relate to domestic processing within Russia. We still think, by the way, that there are meaningful reasons why the Russian government should want ourselves and the other established networks to participate there, and so we're not assuming that it's in the best interest of them for us not to want to be there. And away from the domestic business, obviously a very big part of our opportunity there is cross-border, which as you know is extremely hard to build a cross-border brand and processing assets in a short period of time. So again, we really are still trying to understand ourselves exactly how this could play itself out, but still are hopeful that we still have a meaningful opportunity to continue to participate in the growing electronic payments business in Russia.

And then more broadly on the last part of your question on national payment systems, certainly the activities within Russia get people thinking about what it means for them. I'm not sure how many parts of the world are actually contemplating the types of activities that Russia has taken upon themselves to bring about the sanctions, which certainly should factor into people's minds. But as you know, there are national payment schemes in different parts of the world that we compete with. And we firmly believe that what we have to offer goes well beyond what a national payment scheme can offer in terms of the capabilities of our network, our global acceptance, our ability to be accepted across all channels, fraud screening. We could go on and on with the list.

And so we're used to competing, and as long as there is the opportunity to compete, then we feel okay about the prospects. But certainly it's an issue.

Tien-tsin Huang

Analyst, JPMorgan Securities LLC

Makes sense, thank you.

Q

Operator: Our next question is from Bryan Keane of Deutsche Bank. Your line is open

Bryan C. Keane

Analyst, Deutsche Bank Securities, Inc.

Hi, guys, just a couple questions. One, just the downshift in U.S. debit and then obviously the lower cross-border volume, is any of that impacted by a share shift or share loss, or do you think that's all economically driven?

And then secondly, just a clarification on Russia, is the couple pennies that you're talking about in earnings hit, is that 100% of Russia going away, or is that just the piece you think is going away due to the written proposal or the legislation that Charlie highlighted? Thanks.

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

On U.S. debit, it is, and we expect it to continue to be a pretty competitive space without full access to all the other debit spend just yet. Hard to know whether there's any shift going on, but we think that there has been a downshift in debit spend. We saw some of it occur right after the Target breach. And so this is one where we'll just have to see it play out. We're very encouraged by the spike post-Easter. So I think we'll stay with this question over the next couple of quarters and get better informed.

Cross-border, we don't think so in terms of share shift. When you revert back to very specific corridors, very specific countries that have regulatory and tax events, namely in Brazil and Argentina, manipulation of exchange rates by the Venezuelan government, those things are going to impact everybody. And so we don't think there's a sense of share shift there. This is just something much more fundamental to cross-border travel and it should impact all.

With regards to Russia, a portion of the downshift in revenue growth is very clearly cross-border. In the quarter leading up to the Crimea crisis, we began to see a downshift in Russian travel, but it was a modest deceleration. It then dropped quite a bit further after the Crimea crisis unfolded. This is the level of travel that – this country generates a level of cross-border travel that if things "return back to normal," whatever that is in the future, we could easily see a rebound in Russian cross-border. We've got some placeholders in for sanction effects that could be ongoing. But honestly, as Charlie said, it's way too early to call this. This situation is very much fluid at the moment, and we'll keep you updated as we progress. Charlie, do you want to add?

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

No, I think that's fine.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

Next question.

A

A

Operator: Our next question is from Glenn Fodor from Autonomous Research. Your line is open.

Glenn T. Fodor
Analyst, Autonomous Research US LP

Q

Hi, thanks for taking my question. I appreciate all the color on a confusing situation like Russia. But, Charlie, turning to an issuer that you know very well, during the quarter Chase gave a little more color on what they're doing with ChaseNet. So now we have the largest wallet initiative out there among the large issuers. So just thinking about it, if this initiative takes hold and is successful for them and other large issuers start considering the same strategy, what do you think it means for your efforts with V.me? I'm sure this issue comes up in your discussions with large issuers. Can you shed some light on how they reconcile the thoughts between their own initiatives on wallets and V.me? Thanks.

Charles W. Scharf
Chief Executive Officer & Director, Visa, Inc.

A

Sure. Listen, I can't speak for every issuer or certainly I cannot speak for Chase as well. But I can tell you from our point of view is we are fairly agnostic as to whether it's our wallet or someone else's wallet as long as our cards are appropriately represented on a fair and level playing field. And in the case of Chase, whether it's our cards or whether it runs over VisaNet or their version of VisaNet, again, we view those as our transactions. So to the extent that other issuers choose to want to go build their own wallets, we'll be supportive of that, but that doesn't stop us from continuing to build our wallet capabilities, which I don't like to use the word 'wallet'. I like to use the word 'digital acceptance' as a way to think about what we're trying to build, so that every bank out there can serve its customers properly in digital commerce with digital acceptance. So I hope that answers your question.

John R. Carsky
Head of Global Investor Relations, Visa, Inc.

A

Next question.

Operator: Our next question is from Dan Perlin of RBC Capital Markets. Your line is open.

Daniel R. Perlin
Analyst, RBC Capital Markets LLC

Q

Thanks. So just quickly, I thought I heard you say, Charlie, that you're dropping as of October 1, you're eliminating – you said 50% of your operating rules. Is that...

Charles W. Scharf
Chief Executive Officer & Director, Visa, Inc.

A

That's correct.

Daniel R. Perlin
Analyst, RBC Capital Markets LLC

Q

Okay. And so what I was trying to get at I guess in that question is what is it that I guess you're hoping to achieve by simplifying that? I know it's a big part of your strategy that you've highlighted in the past, but I'm wondering. Is that hope that it's going to come with incremental volumes and the retailers are looking to this and you've also

adjusted the FANF fee for small merchants? So I'm just trying to understand from a bigger perspective. What is it that you're hoping to gain by changing half of your operating rules because it's a pretty significant change?

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

Sure. Listen, I think all of these things that you pointed out in addition to the operating regs go towards the point of – I think most people would tell you, whether you're an issuer or a merchant or an acquirer, people would say that historically that we were probably pretty difficult to deal with. We operate in a very competitive world today. People have choices, both established choices and have the opportunity to think of other ways to process payments. And we want people to enjoy doing business with us and to think that we treat them openly, fairly, and clearly. And our operating regs, which I've got the version – they're sitting on my desk, it's actually 1,538 pages pre-our changes. And so imagine trying to be – you're an issuer or an acquirer, and you've got to live by those.

And so simplification, redundancy, helping people understand what it means to do business with us as well as going out, and what we've been doing is asking, again, issuers, acquirers, merchants, what don't you like and what doesn't make sense? A big part of the feedback that we received was on charge-backs and the processes that we have put in place, the reporting requirements, documentation, and things like that. So we're very committed to continuing to support the integrity of our brand, the integrity of the payment system security, and things that go towards the quality of our network. But we have to be at the kind of place that people say I understand the rules. I understand what it means to do business with you, and you don't have a bunch of things buried on page 1,427 that they didn't understand. That in combination with these other things, again, I think just is – if I was on the other side trying to figure out who I would want to do business with is the way I'd want to be treated, and that's the way we're approaching it.

Daniel R. Perlin

Analyst, RBC Capital Markets LLC

Q

Got it, thank you.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

A

Next question?

Operator: Our next question is from James Friedman of SIG. Your line is open.

James E. Friedman

Analyst, Susquehanna International Group, LLP (SIG)

Q

Hi, I wanted to ask you about NACHA and the prospects for acceleration in ACH. Either Charlie or Byron, if you could help us think about the competitive dynamics in the instance that ACH were to be accelerated, how if at all might it impact your business?

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

Sure. So I guess I'd start with this, which is the differences between what the established payment networks have and what ACH is, the differences are huge. It's not just the frequency of settlement. It's the underlying ease of use. It's the ability to integrate within your systems. It's the data that we have collected and then enable both issuers, acquirers and merchants, to use it in a way which is good for risk purposes, scorings that we've developed. We

have a whole series of capabilities that again we've all developed over 10, 20, 30, 40 years that really is not easily replicable.

Our view is that certainly the issuers understand the benefits of working with that in this ecosystem. They control the customer relationships. And so we're very confident in the position that we have and the ability to differentiate our services versus what ACH can do. And I think if you look at some of the big players that use ACH and actually track through ACH and see how does it actually impact the customer experience, it's a terrible experience for the customer as opposed to a network like ours. And in the environment that we live in today and the way banks are viewing the importance of their customer relationships, it's just another differentiator that we have. So we love the position that we have relative to ACH.

James E. Friedman

Analyst, Susquehanna International Group, LLP (SIG)

Thank you.

Q

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

Next question.

A

Operator: Our next question is from Don Fandetti of Citigroup. Your line is open.

Donald Fandetti

Analyst, Citigroup Global Markets Inc. (Broker)

Yes, Byron, just given the slowdown in cross-border, I was wondering if you could talk a little bit about the relative revenue yield. My understanding is that in the U.S., the yield is pretty high compared to domestic. Is there a difference between let's say LatAm and Asia? Can you talk a little bit about that?

Q

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

There are differences and there are different practices with regards to yields across the globe. We typically don't get into that level of detail. To be a little helpful in this arena, to the extent that there is strong growth by U.S. cardholders, it's a strong, consistent yield from an area of the world that is particularly well positioned to grow cross-border because of the strength of the U.S. dollar. You'll note that when we referenced the cross-border weakness before, we called out a specific corridor. It was Canada to the U.S. The U.S.-to-Canada corridor is doing just fine. And as Charlie said, the outbound travel by U.S. cardholders has remained quite strong. And so I will leave the color at that.

A

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

Next question.

A

Operator: Our next question comes from David Hochstim of Buckingham Research. Your line is open.

David S. Hochstim

Analyst, The Buckingham Research Group, Inc.

Q

Thanks, I wonder. Could you just give us an update on what's happening with CyberSource? There's a little bit of a deceleration in volume growth and V.me signings too?

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

Okay, I'll take the CyberSource. So there has been some deceleration in the growth of CyberSource. We can attribute that specifically to two large customers or clients that we lost in fiscal year 2013, and we're starting to see the impacts of that in 2014. That said, we are very bullish on CyberSource. We recognize the issue. We are investing significant sums to upgrade and add to the features of our CyberSource platform, both for large enterprise businesses as well as for small businesses. We are actively adding people to this business, so our enthusiasm remains robust. I will caution that it will take several quarters before we can get this turned around, but we remain very bullish and very confident on the outlook of CyberSource's future with Visa.

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

And let me take V.me. So as I think I've talked to on the prior year's call, we have learned an awful lot since our initial rollout of V.me, and we have altered our approach to really take away all the functionality other than what I described before as meaningful digital acceptance. And so we're getting really excellent feedback from merchants and issuers alike. We've actually rolled out the first phase of the new platform a few months ago, and we've begun launching it with those merchants. It's incredibly simple. It's just hugely more simple for them to actually integrate it into their checkout experience, literally days as opposed to months.

And the new integrations that we have include lululemon, AutoZone, Petco, and the Wine Enthusiast. But probably more exciting, those are terrific names, but we've also executed term sheets, or master service agreements, with an additional 38 large merchants, which represent almost \$60 billion in addressable volume. Twenty-three of those merchants are actually in the Internet Retailer Top 100. So we're continuing to press forward. We have a much better solution in the market, and it's resonating.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

A

Next question.

Operator: Our next question is from Craig Maurer of CLSA. Your line is open.

Craig J. Maurer

Analyst, CLSA Americas LLC

Q

Hi, thanks, a couple things. Regarding – just I want to clarify. So your EPS guidance fully contemplates the tax benefit you received in the quarter. Please clarify that. And secondly, regarding Russia, should we see the changes to law that you discussed earlier specifically related to basically trapping data and transaction flow and whatnot within Russia, is your current network structure capable of doing that as of tomorrow? Because if I remember correctly, you guys were in a hub-and-spoke network where your data flows back through the States. Thanks.

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

Let me take the tax and EPS question first. The direct answer to your question is yes. The tax benefit that we recorded this quarter was contemplated in our full-year guidance.

That said, let me just provide a bit of perspective. When we give guidance as we did at the beginning of the fiscal year, so this was back in October, our style is to offer guidance without caveat and without excuse. And so when we give guidance, it is naturally broader and has to take into a number of unknowns. And you make educated judgments on how the year would unfold: the rate of economic recovery, unknown; cross-border impacts given a stronger U.S. dollar and currency movements, unknown; cross-border impacts due to global tensions, unknown.

The thing about taxes is that as we get into a lower – the range where we're currently operating on taxes, this becomes more initiative-driven as opposed to where you're operating throughout the country – throughout the world. And so these initiatives, as this one, often take several years to research, prepare before recording. And so the timing of these is often outside of our immediate control and therefore unknown with regards to when we can actually take them. And so all of these things are contemplated; we did contemplate including tax. We also began the year with a range of revenue that was low double digits constant dollar, which was 10% to 13%. Had we delivered in the 12% to 13% constant dollar as opposed to what we're now seeing given other impacts in other areas of 10% to 11%, then we would have been at the upper end – certainly at the upper end of our guidance, if not a little above, because more than one factor is playing out in our favor to a greater degree than we might have contemplated in the beginning. So that's the context. Charlie, Russia?

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

So I guess I'm the Russian expert here. On the question, again, I just want to reiterate and be clear that the law is still evolving. As it gets read, it does evolve and there are changes that occur from day to day. And then once the law is actually passed, there do have to be regulations to coincide with those laws before they get implemented. So there are some things in the law which they would be relatively quick implementation. There are other things which I think some of the dates go out until 2016.

To answer your specific question, today we do not have the ability in a very quick way to deploy a separate version of VisaNet in a specific country. Having said that, we do have instances where we can start to move parts of it, whether authorization is much easier for us to do than entire clearing and settlement. And it's certainly something that we're capable of building, even though it might take a little bit of time.

But also remember, and I think this is critical because you've got very much – we're caught between the politics of the United States and the politics of Russia. But if you just get down to reality for a second, we have 100 million cards in Russia today. We have 100 million cards there. And it's not in anyone's best interest, inclusive of the Russians, to make those cards not available to their own citizens. And so that's why we are hopeful that as this situation unfolds that people understand things like that. And to the extent that they believe it's important to build a national payment system, it can be done in a way where there's the appropriate transition and we have the ability to figure out whether it makes sense to compete in that marketplace. But it would be unlikely that, unless there are some draconian things that are passed, that it wouldn't evolve in a way like that.

Craig J. Maurer

Analyst, CLSA Americas LLC

Q

Just on that point, because I think this is important looking out concerning the NSA concerns and whatnot, if they did go ahead and make those changes, have you contemplated the length of time it would take to restructure your network to comply because this could apply in the future to how China opens up? And we know that your biggest competitor is already there with the technology in place. So if it was a short window given, a conversion could theoretically be done away from you.

Charles W. Scharf

Chief Executive Officer & Director, Visa, Inc.

A

Okay, so two different things. Number one is absolutely we've done an awful lot of work, and you can assume that we're preparing for everything that we should prepare to. The second is I would just caution you to make the statement that others can comply.

Craig J. Maurer

Analyst, CLSA Americas LLC

Q

Okay, thank you.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

A

Next question.

Operator: Our next question is from David Togut of Evercore. Your line is open.

David M. Togut

Analyst, Evercore Partners (Securities)

Q

Thank you very much. Can you give us an update on the size of the commercial card as a percentage of total volumes and give us also a sense of the growth rate and whether that has been affected at all by the issues you brought forward today?

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

On the first part of your question, no. Investor Relations could give you an update on that afterwards. Let me just quickly look. Commercial payment volume growth, we can give you a perspective from the U.S. Since the beginning of the calendar year, it has been low double-digit growth – very high single to low double-digit growth consistently, January, February, March, with an uptick in April.

David M. Togut

Analyst, Evercore Partners (Securities)

Q

Thank you.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

A

Next question.

Operator: Our next question is from Darrin Peller of Barclays. Your line is open

Darrin D. Peller

Analyst, Barclays Capital, Inc.

Q

Thanks. I just want to shift gears to margins for a minute. Personnel expense came in below our estimates, and you also raised your outlook for margins to the mid-60s% versus low 60s% previously. First, is there anything new that's driving the change versus your initial expectation? And can we expect that to really continue off of a new base being mid-60s% now into future years?

And then just a quick housekeeping question, Byron. I know that you showed metrics into April 21. Most of them looked like they were expanding or accelerating. Just what impact did Easter actually have, given the timing in April this year versus last year? I don't know if you said that on the call before. Thanks.

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

We didn't. What I said on the call beginning with the April results is that it's very clear. I've been in a form of retail for 18 years before coming to Visa. The Easter impact is absolutely a phenomenon that exists. Typically, you look at the run rate going in, the run rate going out. You compare it to the prior year. We're several weeks away from being able to do that metric. But the lift, part of the lift is certainly due to Easter. It's also sensible that part of the lift could well be a return to more normal weather. It's very hard to isolate specific weather impacts. But we have done a lot of work around those states in the U.S., for example, that had much more severe weather than normal versus those that didn't. The growth rates, there's a clear delta in the growth rates, some of it but not all of it mitigated by e-commerce. So as we get back to more normal periods post-Easter, post-weather, I think we'll see a more normalized growth rate and one that may very well have some pent-up demand fueling it.

With regards to expenses, at some point, predictably, as we continue to invest aggressively in extending our network, the reach of our network, like a CyberSource, that investment will come with margins that are not attractive – not that we wouldn't invest, but they're not going to be in the 60s%. We've not reached that inflection point yet, and so that's why you saw us on the margin move up from low 60s% to low to mid-60s%.

And with regards to personnel, if you think about it, when we went public in 2008, we had 4,000-plus employees. Today, we have 10,000. And so in the span of a little over five years, we have more than doubled our employee base. We go in surges. We digest. We optimize. We go forward. We will continue to invest in talent, which is a key driver of our success. And we would expect growth off of the personnel base that you see today, despite the more than doubling of our personnel over the past five years.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

A

Adrienne, as this point, we have time for one more question.

Operator: Okay. Our final question is from Jennifer Dugan of Sterne, Agee. Your line is open

Jennifer C. Dugan

Analyst, Sterne, Agee & Leach, Inc.

Q

Thank you. Most of my questions have been answered, but I was wondering. Could you give us a little bit more color on the expected fiscal 2015 revenue impact from the Chase conversion that's going to happen towards the end of the year?

Byron H. Pollitt

Chief Financial Officer, Visa, Inc.

A

At this point, we do expect it to have an impact. It should not be – it's a valued and important addition to our business. I think to the extent that we wouldn't give color on that specifically, but we do expect it to start showing up in the first fiscal quarter. And I'll just remind the group, some of the conversions are taking place today and will pick up pace, or is expected to pick up pace as the year unfolds. But to the extent that that revenue shows up

in service fees, we book our service fees on a one quarter lag. So any conversions that take place say in the fourth fiscal quarter, the service fees won't show up until the first fiscal quarter of fiscal 2015.

John R. Carsky

Head of Global Investor Relations, Visa, Inc.

And with that, we'd like to thank everybody for joining us today. If anybody has follow-up questions, feel free to call Investor Relations. Have a nice evening.

Operator: Thank you for your participation. This concludes today's conference. And you may disconnect at this time.

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