Company Name: Mastercard Inc
Company Ticker: MA US
Date: 2017-01-31
Event Description: Q4 2016 Earnings Call

Market Cap: 115,858.70
Current PX: 106.33
YTD Change($): +3.08
YTD Change(%): +2.983

Bloomberg Estimates - EPS
Current Quarter: 0.962
Current Year: 4.264
Bloomberg Estimates - Sales
Current Quarter: 2685.304
Current Year: 11883.594

Q4 2016 Earnings Call

Company Participants

- Warren Kneeshaw
- Ajay Banga
- Martina Hund-Mejean

Other Participants

- Bryan C. Keane
- James Schneider
- Donald Fandetti
- Jason Alan Kupferberg
- Tien-Tsin Huang
- Sanjay Sakhrani
- Andrew Jeffrey
- James Friedman
- David J. Koning
- James E. Faucette
- Lisa D. Ellis
- George Mihalos
- Christopher Brendler
- Darrin Peller

MANAGEMENT DISCUSSION SECTION

Warren Kneeshaw

GAAP and Non-GAAP Financial Measures

GDV and Purchase Volume Growth Rates

- Both the release and the slide deck include reconciliations of non-GAAP measures to their GAAP equivalents
- As a reminder, as we initiated last quarter, we've also added the table the end of both documents which provide additional information about the impact of Article 8 of the EU's recent payment regulation on our GDV and purchase volume growth rates
- Our comments on the call will be on the basis of rates adjusted for these impacts

Switched Transactions

- In addition, we are introducing a new name for what we previously referred to as processed transactions
- Going forward, we will now refer to these as switched transactions
- Our methodology for calculating this metric has not changed

- We are simply changing the name to more explicitly align with the information provided, that is transaction counts that Mastercard has authorized, cleared or settled or in other words switched
  - This is distinct from transaction where we provided value-added processing services, such as issuer or acquiring solutions which extend our capabilities beyond switching
  - There is no change to our nomenclature for transaction processing fees as these include switching fees, connectivity fees as well as other processing fees

Ajay Banga

Business Highlights

Opening Remarks

- And this is Warren's First Call and as you noticed in his First Call he's made the first change of changing nomenclature from processed to switch
- So welcome to the place
- Our business continues to perform well
- We're very pleased to have delivered a strong result for the year driven by solid execution of our strategy
- For the quarter, our net revenue growth was 10%, EPS growth 7% or 31% EPS when you normalize for taxes
- And what those numbers mean for the full year of 2016 is we saw net revenue growth of 13% and EPS growth of 11%, or 19% when normalized for taxes

Global Economic Condition

- We continue to see bright spots as well as some areas of concern in the global economy in the US. Post-election optimism remains relatively high
- Consumer confidence, unemployment, wages all seem to be holding steady
- It’s still too early to tell what impact any new policy proposals might have on the US or other economies
- But like all of you, we’re expecting to see initiatives around taxation, regulation, infrastructure spending and trade
  - And in fact, on regulation, you’ve all seen the recent executive order talking about taking out two regulations for every one proposed

Europe

- Turning to Europe, the economic recovery is persistent in many markets throughout the prior year, throughout 2016, led by Germany
- And the prospects for this coming year of 2017 seem encouraging as economic sentiment and unemployment continue to improve
- The UK appears to be stable

- We're seeing continued growth in travel to the country as a result of the weaker pound, and it's going to take a few years obviously to work through the specifics of how Brexit is implemented
  - So, we remain watchful of the implications of that on the UK and broadly on the EU

Asia, Australia and Brazil

- In Asia, we remain cautious, largely as a result of the prolonged slowdown in China
- In India, the government has recently implemented a plan to address its parallel economy and to help drive the shift from cash to electronic forms of payment
- Given the heavy reliance on cash in that economy, this is expected to soften consumer spending in the short term, but could well fuel economic growth and modernize the payment system in the long term
- In Australia, both consumer and business confidence remain weak
- While Brazil's economy appears to be emerging slowly from a deep recession
  - The road to recovery for Brazil is expected to be long, as there is still political uncertainty

Strategy

- So with that as the backdrop, what are we doing is to continue to focus on executing our strategy and growing our business
- We're seeing double digit volume and transaction growth across most of our markets
- We're continuing to win deals by leveraging our service offerings

Legal

- On the legal front, we received positive news yesterday regarding the judgment on our case for ten retailers in the United Kingdom representing approximately 40% of our existing damages exposure
- We're delighted that the UK court found that Mastercard's interchange fees do not restrict competition, and actually are necessary for the functioning of the payment system

Planned Acquisition of VocaLink

- So finally, on the legal side, still let me provide you with a brief update about our planned acquisition of VocaLink
- We've been working with the UK competition regulator to secure approval of the transaction, and we're really pleased as they have accepted in principle our proposed solution to address their one concern regarding the LINK ATM scheme
- And we're now looking forward to working with the regulator for final approval of that solution
- We expect to close the transaction sometime in the spring of 2017

2016 Performance

- So now, let's move on to a few highlights from 2016 and some of our recent business activity

- Overall, 2016 was a year that had its economic and regulatory challenges, but I think we've navigated those successfully while putting significant points on the board as a result of our investments in digital, in safety and security, in data analytics, loyalty and processing

US

- This last quarter, we continued our momentum in the US, pleased to have renewed a number of deals, including SunTrust Bank for their credit, debit and commercial business, which, by the way, includes Labs as a service to help drive their innovation agenda, as well as the First National Bank of Omaha, one of the largest private banks in the US, for their credit and commercial portfolios
- In addition, we've given you several examples in the past as to how we've been extending our capabilities beyond switching into processing, back to Warren's clarification, enabling us to drive more deals and touch more transactions
- This quarter, we've renewed agreements with USAA for debit card processing services and with Jack Henry & Associates to provide processing solutions for credit, debit and commercial to their more than 10,000 clients
- Outside of the U.S., we're continuing to make significant progress as well

Europe, Latin America, Mexico and Brazil

- In Europe – I'm just giving you a few examples by the way – in Europe, we signed Amazon for their credit co-brand business in the UK; renewed our debit agreement with ABN AMRO, one of the largest banks in the Netherlands
- In Latin America, we signed a new deal with Caixa in Brazil for credit and debit, which also includes Advisor services
- Additionally, we renewed agreements with Bancolombia for credit and debit with a focus on affluent, as well as with Santander in Mexico for credit, debit and commercial, and a flip of their commercial business in Brazil, while in Asia we renewed our agreement with The Commonwealth Bank of Australia, the largest bank in that country

China

- Finally, while discussing these, let me touch on the domestic opportunity for China
- We continue to speak with the regulators there to better understand the entry requirements, and to clarify our options on how best to approach that market
- In the meanwhile, what we're doing is focusing on driving single branded card issuance
- We're pleased to add Bank of China this quarter, bringing the total number of programs for single branded card issuance launched in 2016 to 44, with more than 10 banks
  - All of these are aimed at driving cross-border spend with the country's growing affluent segment

Digital

- So let me move on to digital, and we've often said that this is a marathon, not a sprint
- But I believe we are executing well against our strategy, and have made some good progress in 2016; and starting as Masterpass, where we continued our focus on driving both user adoption and acceptance

Digital by Default Strategy

- We've talked to you about our Digital by Default strategy, which basically enables issuers to auto-enroll cardholders through their online banking app, and helps to drive scale, but at the same time keeps the issuer at the center of their consumer relationship
- We're pleased to have achieved our stated goal of enabling 80mm accounts by the end of 2016
- The service is now being rolled out globally with several banks, including Bank of America, Capital One, Citi, Nordea, and The Commonwealth Bank of Australia

Masterpass Markets

- With a healthy pipeline to build on this momentum in 2017, we've also added five new Masterpass markets in 2016, bringing the total to 34
- Last year, Masterpass became the first digital payment service to work across all devices and channels, which helped drive acceptance and enabled consumers to shop online, in-store, or in app using a bank-branded offering from the issuer of their choice

Partnerships

- So from an acceptance standpoint, we've added roughly 80,000 new merchants, bringing the total to about 340,000 for online and in-app purchases, as well as more than 6mm locations in about 80 countries that allow contactless payments
- This quarter, we're pleased to announce partnerships with Dunkin' Donuts, Walgreens, Gulf Oil, Wyndham Hotels, and so on
- Last quarter, we highlighted our agreement with the Ecobank Group to roll out Masterpass QR
  - That's a mobile person-to-merchant service across 33 African countries
  - This quarter, we're building on that momentum
- We've partnered with SnapScan, a mobile QR-based payment solution backed by Standard Bank in South Africa, as well as the Government of India and RBL Bank to add a combined 40,000 merchants who will now be able to accept secure digital payments quickly and without the expense of a traditional POS terminal

Mastercard Send

- So let me move on to Mastercard Send
- This past year, we highlighted our partnership with Green Dot and Uber, Stripe and Lyft as well as Allstate, and how they are using the platform to make convenient and secure payments to drivers, delivery people, and claimants, among others
- This quarter, we added Wells Fargo Bank, who will leverage Mastercard Send for their treasury and merchant services customers

Digital

- So let's keep going a little bit with the partnerships in digital

- This past year, we helped Apple Pay, Android Pay, Samsung Pay and Microsoft Wallet to expand to several new countries
- We've added Spain, Ireland, Poland, Russia, and Hong Kong, bringing the total to 17 markets around the globe where consumers can use one or more of these services
- We've also enabled several of them to allow their consumers to shop online, in-app, and check out using their same MDES tokenized login credentials at the hundreds of thousands of merchants around the world where Masterpass is accepted
  - And by doing that, obviously, this also benefited our merchant partners, as they did not have to do any additional development work to support these services

Artificial Intelligence

- Finally, as part of the innovation agenda, we've been looking at ways to combine digital payments with artificial intelligence to create better and more personalized experiences for consumers
- And to give you an example, this past year we launched an AI bot platform, which simulates a human interaction and enables consumers to buy products via messaging platforms like Facebook Messenger and check out using Masterpass
  - So, building on that theme of AI, we've also launched Decision Intelligence, one of our safety and security products which uses machine learning to score transactions based on an individualized risk profile in order to reduce false declines, while at the same time mitigating potential fraud

Services

- That brings me to services
- And remember, our focus on services is in delivering capabilities that connect right back to our core business, providing great value and competitive differentiation to our clients while giving us an incremental revenue stream
- I think we've made significant progress in this area in the prior year

Safety and Security

- Still, let me quickly run through a few examples, starting with safety and security, which has been a key area of focus for us this past year
- We continued the rollout of our leading biometric authentication product, Identity Check, fondly known as selfie pay, to 16 markets around the world, in addition to the launch of Decision Intelligence, which I just mentioned

Data Analytics

- On the data analytics front, since the acquisition of APT, we've integrated the sales and product organizations at APT with Advisors to drive significant benefits
- We've added more than 60 organizations who have subscribed to the APT platform in recurring subscription-based contracts
- So in addition to McDonald's, which we mentioned in the past, we got JCPenney and Duracell in the US, Asahi Breweries in Japan, Thomas Cook in the UK.
  - In fact, there were 28 deals in total that were additive to APT's business as usual efforts

- So with assets like these, we not only deliver great insight, we're actually building even stronger relationships with our merchant partners as well

Martina Hund-Mejean

Financial Highlights

Net Revenues

- Starting on page 3, you will see we have delivered another strong quarter
- Overall, the results were in line with our expectations
- However, as reported net revenues were impacted by the stronger US dollar vs. our assumptions when we talked last to you in November
- The figures on this chart exclude the impact of a special item
- So, here are a few highlights
- Unless otherwise stated, the growth numbers I call out will be on a currency neutral basis
- Net revenue growth was 10% and operating expenses declined by 1%
  - This resulted in strong operating income growth of 23%

EPS, Share Repurchases, Tax Rate and Cash Flow

- EPS was $0.86, up 7% y-over-y, driven primarily by our strong operating performance
- Share repurchases contributed $0.03 per share
- As a reminder, the tax rate was much lower in the year-ago quarter, primarily due to discrete tax benefits in 2015
- And when you normalize for that in both periods, Ajay already told you that the EPS growth was 31% for the quarter
- Lastly, cash flow from operations was $1B

Operational Metrics

GDV Growth and Purchase Volumes

- So, let me turn to page 4, where you can see the operational metrics for Q4
- Worldwide gross dollar volume, or GDV growth, was 9% on a local currency basis, down 2 PPT from last quarter, primarily driven by the rolloff of one agreement in the US and lower cash volume in India
- As a result of the government's initiative in India that Ajay already mentioned, ATM cash withdrawals in the short term have declined more than the growth that we saw in purchase volumes
- However, purchase volumes in India was up significantly, 75% y-over-y, and over time, these volumes are expected to continue to ramp as acceptance grows
- US GDV grew 3%, made up of credit and debit growth of 4% and 1%, respectively

- And outside of the US, volume growth was 11%
- Cross-border volume grew 13% on a local currency basis, up 1 PPT from the 12% we saw in Q3

Switched Transactions

- Turning to page 5
- Switched transactions grew 17% globally to $15.2B with double digit growth in all regions other than the US.
- Globally, there are 2.3B MasterCard and Maestro branded cards issued

Revenue Growth, Rebates and Incentives

- Let me turn to page 6 for highlights on a few of the revenue line items, again described on a currency-neutral basis unless otherwise noted
- Net revenue growth was 10%, driven by an increase in switched transactions, domestic and cross-border volume, as well as utilization of our services offerings
- Rebates and incentives grew 21%, reflecting higher volumes and increased incentives for new and renewed deals

Domestic Assessments, Cross-Border Volume Fees and Other Revenue

- Looking quickly at the individual line items for revenue
- Domestic assessments grew 7%, while worldwide GDV grew 9%, the difference being primarily due to unfavorable mix
- Cross-border volume fees grew 10% while cross-border volume grew 13%
- The 3 PPT gap is mostly due to higher intra-Europe growth
- Transaction processing fees grew 17%, in line with the 17% growth we saw in switched transactions
- And finally, other revenue grew 20%, driven primarily by Advisors and our safety and securities services

Expenses

- On page 7, you can see that expenses remained generally steady in each subcategory
- Excluding the special item, total operating expenses declined 1% on a currency-neutral basis with ongoing cost management activities offsetting our continued investments in strategic initiatives

Switched Volume

- So I'm going to turn now to slide 8 and let's discuss what we have seen in January through January 28, where most of our drivers are slightly better when compared to Q4
- The numbers through January 28 are as follows
- Starting with switched volume, we saw global growth of 10%
  - That's similar to the 10% growth we saw in Q4, with double digit growth in each region outside the US.

- In the US, switched volume grew 3%, down less than 1 PPT from Q4, with higher growth in credit programs, but lower growth in debit programs
- Gas had slightly less than a 1 PPT positive impact to our January growth
- Switched volume outside the US grew 18%, up 1 PPT from Q4, with higher growth in each region

Switched Transactions Growth

- Globally, switched transactions growth was 19 %, up 2 PPT from what we saw in Q4, primarily due to growth in India, Brazil, Venezuela and Russia
- Switched transaction growth outside the US was up 3 PPT, while the US growth was similar to Q4
- With respect to cross-border, volumes grew 14% globally, slightly higher than Q4

Performance Objectives

- Turning to our performance objectives for 2016 to 2018, we continue to expect to grow net revenue CAGR at a low double digit rate, deliver an operating margin of at least 50% in each year, and drive an EPS CAGR in the mid teens
- As a reminder, these objectives are on a currency-neutral basis, exclude special items and M&A, and are normalized for tax
- We are off to a solid start in 2016 as we delivered net revenue growth of 13%, exceeded our minimum operating margin target and grew EPS by 19% using normalized tax rates for 2015 and 2016
- As is our historical practice, we will update you on our longer-term expectations at our Annual Investor Community Meeting

2017 Outlook

Foreign Exchange

- Now turning to 2017, we expect the global economic outlook to be similar to what we saw last year, and we expect foreign exchange to remain a headwind to our business
- However, our underlying business fundamentals remain strong with a number of factors driving revenue, including growth in our core business driven by a mix of new deals, renewed agreements and the expansion of our differentiated service offerings

Net Revenue Growth, Rebates and Incentives

- We expect net revenue to grow at a low double digit rate on a currency-neutral basis, consistent with our three-year performance objective
- And when you model on an as-reported basis adjusting for the FX impact of all currencies, we estimate there would be a headwind of a little more than 2 PPT to net revenue growth and 3 PPT to the bottom line given the current strength in the dollar relative to the euro and the British pound, in particular
- Our plans assume continued strengthening of the US dollar to about $1.05 to the euro

- From a sensitivity standpoint, $0.01 change in the value of the US dollar relative to the euro is expected to have just $30mm annual impact to revenue, considering both transactional and translational foreign exchange effects
- We expect net revenue growth in H1 to be lower than H2, due to higher incentives for new and renewed agreements and the rolloff of one agreement
- So for 2017, let me call out several things that you should also consider
- For rebates and incentives on an as-reported basis, we currently expect to see about the same 20% growth that we saw in 2016, reflecting the impact of volume growth and deal activity

Expenses

- And on expenses, let me just give you a couple of comments there
- In 2017, we're continuing to invest in key long-term growth areas, such as digital, including Masterpass and MDES, safety and security and investing in geographic expansion
- Through our ongoing cost management efforts, we expect y-over-y operating expenses to grow in the high single digit range on a currency-neutral basis, and we expect foreign exchange will have about a 1 PPT benefit to as-reported operating expenses for the year
- Also of note, we're accelerating our advertising and marketing spend into H1 to support the rollout of Masterpass
  - In particular, first quarter A&M spend will be up by about $40mm vs. the year ago, quarter

Interest Expense and Tax Rate

  - In the other income and expense line, interest expense related to the additional debt we issued in November adds approximately $15mm to our normal underlying run rate of roughly $25mm per quarter
  - Finally, you should assume a tax rate of 28% to 29%

QUESTION AND ANSWER SECTION

<Q - Bryan C. Keane>: Just wanted to talk about rebates and incentives. It looks like it's going to be up 20% again for the second year in a row, so it seems like we have a more consistent pattern. Can you just talk a little bit about that line item vs. incentives and renewals at pricing, because we always get a lot of questions about the growth there? Thanks.

<A - Martina Hund-Mejean>: Sure, Bryan, and good morning. Really, no change from 2016. As you know, back in late 2014 and early 2015, we actually had renewed a couple of agreements that were for a very long term. One was 10 years and one was actually 20 years. And at that point in time, you actually saw the rebates and incentive growth coming up a little bit more because a number of the items that we had in the incentive line had to be amortized in the early part of the agreement – of the term of the agreement, rather than in the later part of the agreement. At that point in time, I said that that will be with us for a number of years, and 2017 happens to be still a year where we're seeing that. In addition, when you put the volume growth that we are actually expecting for the year, when you put all of that together, that will drive the 20% – roughly 20% growth in rebates, incentives vs. 2016.

<Q - James Schneider>: I was wondering if you could maybe talk a little bit about the impact of any potential pricing actions you've already taken that are going to impact the 2017 revenue guidance and anything that you might be contemplating that's going to roll in and affect the full year?

<A - Martina Hund-Mejean>: Jim, actually there's fairly little impact from pricing actions in our 2017 numbers. As you know, we really look at pricing from a long-term perspective. It has to be strategic. We are doing that every year, depending where the market environments are; but for 2017, there's relatively little comprehended.

<Q - Donald Fandetti>: Ajay, your guidance for 2017 still has pretty attractive low double digits net revenue growth. As we look around the world and we see a lot more direct out of bank account type payments from Alipay, and you see what's going in the U.S., are you still as constructive on a secular growth opportunity as you have been?

<A - Ajay Banga>: Yes, I absolutely am. Remember that in the retail business alone, the consumer to retail payments, 85% of the world's retail payments are still cash and check. So, there's a lot of opportunity there, first; second, there's the whole commercial space that's got a great deal of opportunity that we've been assiduously building on; third, we've got our services revenue; and fourth, we've actually beginning to participate in the direct to bank account payments once the VocaLink acquisition is complete. So, to me, we're building the right portfolio to take on the opportunities that this secular growth represents over the next decade, not just one or two years.

<Q - Jason Alan Kupferberg>: So just thinking about the three-year performance objectives, and we're still talking about the mid teens kind of EPS growth in constant currency. I mean, you did 19% on this as adjusted basis in 2016, so I guess there's some implied deceleration in 2017 and 2018, unless the guidance proves to be a little bit conservative. So, can you just remind us what would potentially drive that. Is it just kind of expense timing or other factors?

<A - Martina Hund-Mejean>: Look, Jason, we're only one year into our three-year performance period, so at this point in time we're not yet refreshing our performance objectives. And typically, as you know, we're doing that in September at our Investor Meeting; so, we believe it's too early. You see that we are thinking that we are going to put really good points on the board for 2017, and I don't think you should be reading into anything for 2018.

<Q - Tien-Tsin Huang>: I want to put you on the spot and ask for your thoughts on how some of Trump's initiatives might impact Mastercard's business, like cross-border activity or thoughts on deregulation and Durbin and whatnot. Thanks.

<A - Ajay Banga>: Who allowed you to ask that question, Tien-Tsin?

<Q - Tien-Tsin Huang>: I don't know, figured just for giggles and fun. Everything looked clean, so let's ask you a tough one.

<A - Ajay Banga>: It's nice to hear from you. So, I think that it's early days to talk in great depth about what all could happen, but I'll tell you my views that are on the positive side of this, and then you can see, obviously, through the news that there are people who are concerned as well about the negative side of it. The positive side of it to me, his regulatory announcement, the fact that he seems genuinely concerned about the manner in which regulations enacted are creating millstones for business, both small and large, to grow in the U.S. I think that's pretty clear, and he is definitely committed to helping make it easier for businesses to open, operate and run profitably in the system.

Now, what that means specifically for a company like ours, or for merchants or for banks who are in our ecosystem, I don't yet know, because you'll only get to know that over a period of time. My general belief is that, certainly, it'll help both of the other parties, the merchants and the banks, in the ecosystem in different ways. They'll end up winning on some and losing on some. I just don't know which ones will go where.

I do know that in an environment which talks about regulation being something you need to watch carefully so that you enact the right kind of regulation, but you don't stifle innovation and growth, that could lead to definitely a constructive view. That's kind of where I'm coming from. I don't yet know, specifically, how it will impact our company or those in our immediate ecosystem.

I do believe that in the space of infrastructure, there will be some form of investment or the other funded in some form or the other into infrastructure, both physical and digital, in our country. I believe that will only increase the velocity of money in the country. That will be helpful for a company like ours, both in retail and commercial payments. So, I look forward actually to that, both as a direct impact on our company, but also, frankly, traveling the way I do and the way most of you do, the infrastructure in our country could do with the benefit of a sustained investment program, both in physical and digital. So, I think that's important.

The aspects of taxes, there's all kinds of discussions floating around about what kind of tax rate. I'm talking corporate taxes right now. What kind of corporate tax rates could come to if it comes down from the current level that we're paying, which as Martina told you, 28%, 29%. If it comes down to anything below that, you should expect us as a company to benefit from it directly to the bottom line. There's rumors that it will go to 20% or 25%. You can put your own probability factor on which one. I think there's lots of things to be worked out about how you pay for that reduction in taxes and what impact that has, border taxes, adjustments of import and export circumstances. All of these have implications for us as a company.

Mostly we are a net exporter of service rather than a net importer of service as a company, because of the fact that so much of our back office and our technology and our product development has historically been developed in the United States with US IP. We do have a lot overseas. We do have stuff in Asia. We do have stuff in Dublin and Europe, but net, I think you will find us to be a net exporter rather than a net importer. So I guess on all of those aspects on taxes to regulatory to infrastructure, I can find ourselves finding this to be net positive for our company over the next four to five years.

<Q - Tien-Tsin Huang>: Great. I appreciate that.

<A - Ajay Banga>: The aspects of trade, Tien-Tsin, as you know, my normal approach to trade is that I continue to believe that the United States is way too large a marketplace for companies and businesses to feel that they shouldn't be involved with having on-soil presence and on-soil activity and frequent travel in and out by business executives alike. So, I consider the US to be too attractive for that to change dramatically. I do believe like everybody else that in the corporate world, there are a lot of us have built our business on the freer flow of cross-border trade, data and people. If that were to change over time, that would be a problem, but I don't believe that that's what the administration wants to do. They want to grow the economy. The economy is not going to grow without the right inputs in the right places. It may change specifics of the way trade gets enacted, but I continue to be relatively bullish on where this economy could go over the next four to five years.

<Q - Sanjay Sakhrani>: Ajay, I want to talk about the European market. I think I heard you say you guys won the Amazon co-brand relationship. But just maybe you could talk broadly about the competitive environment with Visa in that market in a broader way, as well as PSD2 and then lapping the interchange changes, as well. Thanks.

<A - Ajay Banga>: Sure. So, the interchange changes have already gone, and as you know, some time back, and so have all the other rules that went with it, including the co-badging. And that's why there's an Article 8 and Article 7 implications. They're all baked into our earnings calls for the last two, three quarters. First of all, I actually am beginning to see an expansion in acceptance, for sure, across the EU, probably facilitated by the lower interchange rates that merchant who earlier were reluctant to accept electronic payments are now willing to do so. That's for sure. That's a good thing.

There is obviously an impact on bank P&Ls caused by the lower interchange rates. Every bank, as you know, is working on other ways to find ways to get to their P&L again. That includes fees. It includes services. It includes alternative products. It includes an emphasis on commercial in some cases. There's a whole series of actions that banks in different countries across Europe have been taking to try and find a way to put some energy back into their P&L.

My sense on the other aspects, PSD2, as you know, it's still two or three years away from fully being implemented. 2018 is when it starts hitting the road. But there's a lot of energy and a lot of passion going into preparing for it. I actually believe that VocaLink could play a very instrumental role for banks in the EU to help them actually find a way to navigate through PSD2 and to maintain scheme-like look and feel to the ability to create payments in a way that they can manage through their customer relationships and their chargebacks and their fraud management and the like. So, I believe that to be an essential part of our strategy for Europe.

On the Visa, Visa European competitive environment, honestly, it's still very early days. They've just about closed. As you know, they're going through their own adjustments across the world on catering for that acquisition. We're in the marketplace, looking at what anything happens in the market on either pricing, in which case we may have some opportunity, or on volume growth and share growth, which we continue to pursue and we're continuing to win some deals in Europe. So, it's kind of early days. We're in the game. We're looking at everything. We'll see how it goes.

<A - Martina Hund-Mejean>: Yeah, so let me just add something. As you know, economic growth in Europe is generally much lower than what we're seeing here in the United States, though when you actually look at our numbers, in terms of we are producing high double digit growth, both in volume and in transactions in Europe, right. I mean close to 20% for each of those numbers. There are really two factors that fuel that growth. One is secular trend. A lot of parts in Europe outside of the UK are still using a lot of cash. And secondly, the market share gains that Ajay was referring to that Javier, our President, and his team have been able to gain over many, many years, we don't really expect to see much changes to that. We think that we continue to grow in that way, going forward for a number of years to come.

<Q - Andrew Jeffrey>: Martina, I think you mentioned that, at least quarter to date in the US, you're seeing faster relative credit growth, volume growth. Can you just speak to whether or not you think that's cyclical or if there's a change in consumer behavior or if it's simply transitory?

<A - Martina Hund-Mejean>: Andrew, I think it would be hard in four weeks to be really figuring out what is going on. In there we saw a little bit of a decline in Q4, now we're seeing a little bit of a snap back. So, I can't really point that to a consumer story or to another story. I think it's just a typical trend at this point in time.

<Q - James Friedman>: I wanted to ask again about the now famous commentary and slide from the September 7 Investment Community Meeting, the one about services, Martina. In that one you disclosed services as a percentage of total revenue and the margin trajectory. I know, Ajay, you called out some of the trends that you're seeing on the security side. But what is your forward expectation on services? Do you think the future growth will parallel that that we've seen in the recent past?

<A - Ajay Banga>: So, I continue to believe that the entire services space, remember, there's a set of different businesses inside it. So, there's safety and security, there's Advisors in the consulting business. There's the information services and data analytical space. There's the space of loyalty and rewards and there's processing, which actually allows us to get a role to play in many of the other services we want to be participating in.

They've all got different growth rates and trajectories. Safety and security happens to be one of the fastest growing, along with information and data analytics. That's because one, they're intertwined, but two, that's a very important topic right now for consumers, merchants and banks. And I believe we have cutting-edge products that are differentiated and are capable of helping institutions across the world plug in and help them manage potential fraud while work on declines, and so help them really maximize their P&L in attractive ways when they're looking for revenue. So, I continue to believe those two will be very attractive growth areas over the next five to ten years.

Our processing grows when we win deals, but processing, and when we get into more footprints, processing tends to be a very local business. It has some global transferability, but is it tends to be quite local. And therefore, it tends to have also a different margin profile than safety and security and information analytics because local means you've got to build locally and that creates its own expense profile. We also tend to make more money out of the transactions we see rather than in the processing business itself. So, it tends to be a input into deal winning rather than part of the revenue cycle as much as the others.

The loyalty business is actually very interesting. We started with a relatively good platform in MasterCard Rewards. We've added to it over the years with merchant funded rewards by buying into Truaxis in California and buying into Pinpoint in Australia. We're actually getting some nice wins in that space and we continue to believe that the loyalty and rewards space will be a good growth area and a good sticky area with our customers.

So, do I see this as being a relatively attractive growth area, a faster percentage of growth than our core business? Probably, because it's off a smaller base as well. Do I see this changing dramatically over the next couple of years? No, but beyond that, we'll see. This is a live area. We're investing in it both organically and inorganically, so it's kind of a live growing segment for us.

<A - Martina Hund-Mejean>: Jamie, interesting that you're referring to the now famous charts. I think I have not heard that term that way. But just to leverage off Ajay's comments, we have really not changed our story on this. We are very encouraged in what we have seen in the rest part of the year since September. You know it's about 25% of our total revenues. That has not changed in a material manner. You know that exuding acquisitions, the growth was roughly 14% for those kinds of services. We believe that these services can continue to deliver great growth. And as we're scaling those services, we will be able to expand some of the margins on those services. Again, that was on the chart. So, story hasn't changed and we believe that in 2017 some of the thoughts that I've put down for you does include exactly that kind of growth trajectory. By the way, I have to correct one number. I said 14% organic growth. It's 18% organic growth that we actually saw when we talked in September.

<Q - David J. Koning>: I guess transaction and other both grew about 20%, those two segments last year. And you kind of answered that other will continue to grow pretty fast, but then assessments and cross-border both grew more like 8% to 11%. Is that sort of mix that those two faster growth segments will continue to be transaction other and then assessments and cross-border continue to be a little on the slower side of your total company growth?

<A - Martina Hund-Mejean>: Yeah, I think that is a trend that we have been seeing now a number of times. And there's a number of things happening. First of all, when you look outside of the United States, we have been growing in a number of countries such as India and Brazil and Russia, et cetera, where you're typically seeing lower volume coming per transaction, but more transactions. And then in the United States, as you might remember from last year, which also helped us in Q4, we saw more PIN transactions because of the number of deals that we have been doing. Again, that adds to the transactions. You don't really see that showing up in as big of a mover, needle mover on the volume side.

<A - Ajay Banga>: And those PIN transactions go up and down, as we've told you a few times. There's months and quarters when they are growing faster. That tends to be a more, it's almost a weekly and daily issue that we deal with. But, if you're talking about generally long-term trends, you should expect that the two will grow faster than the other two. The fact is that even at 8% or 10%, core payment transaction growth of 8% or 10% is attractive. That reflects the secular change as well as all the day-to-day activities that Martina just referred to.

<Q - James E. Faucette>: Wanted to ask a question, maybe for Ajay and Martina combined, around the opportunity to support some of the other new payment schemes that are emerging in different countries around the world, including RuPay, et cetera. I know you've talked a little bit in the past about the opportunity to provide services to some of these new payment schemes. Can you just expound on that, as to how you think about that opportunity set and how important those new partnerships could be to continuing to drive services growth? Thank you very much.

<A - Ajay Banga>: Well, there have been for years in the industry these alternative payment schemes to the global networks. In fact, I used to say that our competition is not just the global networks. And of course, it's not just cash that we've been talking about for a while, but it's also these local payment schemes country by country. Europe had a number of them. Mexico has them. Canada had them. Australia has them. Russia now has it post the sanctions in the Crimean circumstances. India has launched RuPay and UID. China's always had one, called China UnionPay, which kind of most people know lots about.

And so, in every marketplace there have been these schemes. These schemes are either owned by the local banks or by governments in some cases, so CUP is owned by the Chinese government, whereas a lot of the other schemes are owned by local bank associations. Cartes Bancaires in France, for example, is owned by the French banks.

They play different roles. They play roles where they will look at all the debit transactions locally. Others, like CUP, all domestic transactions are mandated to go through them, and so on. So, there's a whole range of these. What we've been trying to do is to go back into marketplaces that we believe that the existence of these schemes is, one, either creating an imbalance in the market or holding back growth, and attempt to either work with the government or the banks to find ways to either partner with those schemes or find ways to change the laws around those schemes so that you can have a more open marketplace, which should benefit merchants and should benefit banks and should benefit consumers. And we've had different degrees of success over the years. The European Union, as you know, through its directives over the years in PSD and – what is it called, the other one? The European Special?

<A - Martina Hund-Mejean>: SEPA.

<A - Ajay Banga>: SEPA. I get mixed up between SEPA and [ph] SIPA (51:07); but, SEPA. Those have created opening up of these schemes for people like us to be able to play. I continue to believe that the model will be a mix of all of those. The one you're specifically getting at is more like the Russian model, where there is a domestic payment scheme generated and created, and we have helped them put their technology together and connect with them and provide services that are value added from safety, security, cross-border approvals, transaction management to information and data, which are provided by our better capable systems than they have of their own.

And the fact that we see global transactions and they tend to see localized transactions adds a long-term value differentiator between what we can provide and what a local scheme can provide. It's the same with the RuPays of the world or others. We're always looking for ways to cooperate with them, in some cases successfully, in others not so.

I'm sorry it's not a clear answer because this is not a clear space. It's a space that evolves and breathes and lives every day and week depending on the circumstances of a marketplace. And you should just know that our country managers on the ground have this as one of the major objectives in their evaluations, and the decisions in how they get paid.

<Q - Lisa D. Ellis>: In keeping with the theme of putting Ajay on the hot seat this morning, do you mind commenting on how you see Mastercard's relationship with Alipay and Ant Financial evolving, like friend, foe, frenemy, both in the context of China, India and expanding elsewhere in the world?

<A - Ajay Banga>: Well, in China right now there's nothing to say because we are still waiting for clarity on how we could be partners domestically in China. Having said that, we have had a relationship with Alipay and Alibaba for the last couple of years on helping them think through how to use our technology to figure out different aspects of their own service, including the detection of fraud products on their website. Some of that relationship has worked well. Some of it, it depends on the energy on both sides of the partnership to implement that.

I consider different forms of payment to all be competitive, but also conducive to the bigger challenge of fighting the 85% that is still cash and check in retail payments; and that's always been my stance and I haven't changed. So, I've had the same view of PayPal. I have the same view of Alipay. I have the same view of all of these, that I think there's enough place in this market for all of us to play, and there's enough, let's say, challenges in the marketplace for all of us to put our shoulders to it. We've come at it differently. We'll win some deals; we'll lose some deals. But I kind of believe there's enough secular growth opportunity in this space for a lot of us to flourish.

<Q - George Mihalos>: Martina, just had a quick question on the guidance as we look at 2017. Obviously in 2016, from a revenue perspective, you outperformed, 13% constant currency top line growth. As we look at 2017, it seems you're implying 11%-ish. Can you just maybe bucket for us what are some of the headwinds, 2016 going into 2017, outside of, obviously, the USAA de-conversion? Thank you.

<A - Martina Hund-Mejean>: Yeah, look. It's a number of things that are impacting 2017 or that are driving growth for 2017, as I did say low double digits. You can come to your own conclusion in terms of the specific number. But the combination of one of the agreements, USAA rolling off, as well as quite a few agreements actually rolling on, as well as the growth in our services offerings are all making up the numbers. Also, what I said in my script, so that you guys are all having the right kind of modeling down is we said that the growth rate will be lower in H1 than H2, and that is obviously impacted in terms of how agreements roll off and roll on.

<Q - Christopher Brendler>: Can we just talk a little bit more on the ground level of what's happening in India? Where do you stand from an issuing relationship with the major banks? Are you sort of spurring the adoption of alternative payments through terminalization and helping merchant acquirers get terminals out into the market? And I think you noted in the prepared remarks a very substantial increase in volume. I know it's off a low base. Maybe try to size that market for us a little bit over the next couple years would be great. Thank you.

<A - Ajay Banga>: Sure. So, India has only 1.4mm terminals actually at the point of sale, and it tends to be a very cash dominated market. I'd say 95%-plus of the transactions in retail are cash. When the demonetization happened, the two biggest currency notes were taken out of circulation, the INR 500 and the INR 1,000 notes constituted 86% of the currency notes in circulation. That's the shock that is referred to as what could lower consumer spending for a couple of quarters. We saw that because restrictions in cash withdrawal from banks and from ATMs were instituted as the government tried to catch up with the demand for cash. With the new notes, they were printing, those notes had to be put into the market. The ATMs had to be redesigned. Their hoppers had to be redone. Or you can just imagine the level of work in a country where the largest public sector bank has 18,000 branches, and is spread across a relatively large country. So, that's what caused some of the dislocation.

Now, 1.4mm merchant terminals. Their point of sale payments can take this, but behavior habits that used those terminals very infrequently. The 75% increase in purchase volume you're seeing is because people began to use their cards more frequently at those very same point of sales terminals. What's going on now is a concerted move to increase the number of point of sales terminals, double plus over the next I'd say three to six months. That work is being done by the acquirers, the banks, the networks, us, Visa, others, but also by the government actively pushing that logic.

Second, there's a great deal of partnership with merchant organizations on the ground. The Confederation of All India Traders estimates that there's as many as 60mm casual and regular merchants in India. Even if you were to go from 1.4mm terminals to 5mm acceptance points in the next two years, we're talking 5mm out 60mm. So, there's a long way to go before we get to a ubiquitous terminal acceptance model.

There's a lot of work going on on cheaper terminals. QR codes is an example of almost zero cost for terminals for a merchant. We are actively rolling them out. You heard that in my prepared remarks with the Government of India and with RBL and others of that type. We're working actively with issuers, acquirers and the government in short on this topic, but don't expect this to change in a quarter or a month. It is a long fight, and I think the Prime Minister is to be credited for his willingness to take it on, because in the medium to long term, this could be transformative for the way India's economy operates in the recognizable formal economy, as compared to the informal economy, where it's denied taxation and denied credit and denied insurance. I think he's really trying to do something pretty brave here.

<Q - Darrin Peller>: Can you just touch on the, first of all, the cross-border volume trends and just bigger picture, what you're seeing regarding sort of the headwinds and tailwinds globally? I know you started touching on that before and saying that maybe there were some elements that might be a little bit slower on the volume side. But I guess I also just want to understand. The cross-border revenue growth rate during the quarter on a constant-currency basis was I think 10% vs. volume of 13%. So, is anything going on on pricing or anything else you could explain around that? We'd appreciate it. Thanks.

<A - Martina Hund-Mejean>: So first of all, Darrin, on your last question, the difference, the 3 PPT difference was really the relative higher intra-Europe growth, which you know comes at a lower yield vs. the inter-regional growth, which typically comes at a higher yield. That's all that's going on. We've seen that going for quite a few quarters, eight quarters or nine quarters. So, there's really nothing else in there. It's really nothing.

<A - Ajay Banga>: That's Europeans traveling within Europe. That's basically what's going on.

<Q - Darrin Peller>: Got you.

<A - Ajay Banga>: Europeans are staying closer to home.

<A - Martina Hund-Mejean>: Right. From an overall cross-border trend point of view, what we have been seeing lately in Q4 was that actually more Chinese, Hong Kongnese, Japanese have been traveling in Asia-Pacific. As well in Latin America, we are starting to see Brazil coming back a little bit more. However, some of that was offset by what's going on in Middle East, Africa, in particular those economies that are hurting because of the low oil price, right. So, you have a particular impact in Nigeria and Qatar and Kuwait, and Saudi Arabia based on that. But when you take all of this together, we are still seeing a very significant cross-border volume growth. And you saw that in the first four weeks of the year that has been going up a little bit more, mostly predominantly to Latin America, so that is the Brazil phenomena. That country is obviously working itself out of a very deep recession and we're seeing some good signs there.

<A - Ajay Banga>: The UK is interesting. Inbound into the UK is up substantially. Outbound from the UK is negative. Not just down, negative, substantially. That's because of what happened to the pound vs. other currencies. So, it's kind of a mixed bag across the range.

Ajay Banga

Closing Remarks

I'll leave you with a couple of closing thoughts

We had a strong year in 2016

Our financial performance was driven by the growth for our core business and our ability to continue to differentiate ourselves with services

That led to significant business wins this year

As I just said in some of the Q&A, the secular growth opportunity in our business remains very strong. India is just a great recent example of this

The actions taken there has the potential to be transformative

We will continue to invest for that future

We're going to shape the payments landscape through innovation and expand into new payment flows, hence the interest in VocaLink and other such efforts, to ensure that we are well positioned for success for many more years to come

Obviously, in terms of what this means for 2017, we're going to remain focused on growing our business by driving the shift from cash to electronic payment, by building new service offerings, by advancing our digital strategy, and hopefully closing in the spring on our acquisition of VocaLink

All this while Martina ensures that we all very carefully manage our expenses