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Bloomberg Transcript

Company Name: Mastercard Inc
Company Ticker: MA US
Date: 2018-02-01
Event Description: Q4 2017 Earnings Call

Market Cap: 183,074.70
Current PX: 172.93
YTD Change($): +21.57
YTD Change(%): +14.251

Bloomberg Estimates - EPS
Current Quarter: 1.256
Current Year: 5.772
Bloomberg Estimates - Sales
Current Quarter: 3178.192
Current Year: 14211.059

Q4 2017 Earnings Call

Company Participants

- Warren Kneeshaw
- Ajay Banga
- Martina Hund-Mejean

Other Participants

- James Schneider
- Donald Fandetti
- Darrin Peller
- David Mark Togut
- Andrew Jeffrey
- Jason Kupferberg
- Bryan C. Keane
- Craig Jared Maurer
- Tien-Tsin Huang

MANAGEMENT DISCUSSION SECTION

Warren Kneeshaw

Financial Measures

Our comments today regarding our financial results will be on a currency-neutral basis and exclude special items unless otherwise noted

Both the release and the slide deck include reconciliations of non-GAAP measures to their GAAP equivalents

Ajay Banga

Business Performance Review

So our business continues to perform well

We are very pleased to have delivered strong results again this quarter

I think they're driven by our continued focus on the execution of our strategy that we laid out for you, in fact, as recently as the Investor Day in September

Earnings Overview

- For the quarter, we delivered net revenue growth of 18% and EPS growth of 30% excluding special items, which are primarily related to the U.S. tax reform and our Venezuela operations
  - On that same basis, net revenue growth for the year was 15% and EPS growth of 21%

Global Business Environment

- Now the major economies around the world generally improved in 2017, and we expect to see a relatively steady environment again this year, although with some pockets of instability
- In the U.S., consumer confidence has been healthy, unemployment relays remains low, and holiday retail sales were solid, although y-over-y quarterly growth was slightly lower in Q4 than in the previous quarter, according to our SpendingPulse estimates
- In Europe, the economy has been relatively stable
- Germany and France are driving some mild growth
- Retail sales growth in the UK, however, slowed in Q4, again, according to SpendingPulse
    - And about the UK, we remain concerned about the potential impacts of Brexit over the medium and longer term
- Latin America, now there is a region that has been recovering from its economic recession
- And while Brazil and Mexico both have presidential elections coming up, and of course, Mexico has the added uncertainty of NAFTA renegotiations, we are cautiously optimistic that economic growth in that region in 2018 will be similar to 2017
- The political and economic crisis in Venezuela continues to worsen, and Martina is going to discuss that in some detail when she comes on to her section
- Now in Asia, we see an improvement in consumer and business sentiment in Australia, and the ASEAN countries continue to be bright spots
- So overall, although we know that the world is not without geopolitical and trade-related risks, absent any major impacts from these, we expect 2018 to be similar to 2017 from an economic standpoint

Global Business Drivers

And with that as the backdrop, we're focused on continuing to execute our strategy that's allowing to grow share across all of our product lines in 2017, and let me give you a few examples of how we are doing this

US

- So in the U.S., you heard this morning probably that we have just announced that we have now gotten the combined Bass Pro Shops and Cabela's, co-brands
    - They've chosen Mastercard for their consumer credit co-brand book
- It's one of the largest retail co-brands in the market
- You probably know that we have been the network for the Bass Pro Shops co-brand, and we're going to convert the Cabela's portfolio to Mastercard later this year

KeyBank

- We also renewed our exclusive agreement with KeyBank for their consumer and commercial credit and debit portfolios this quarter

- Now, KeyBank actually is a great example of a customer who uses various Mastercard services
    - They use artificial intelligence authentication tools, our loyalty platform processing services, so that's a nice wide spread of services

Bank of America

- Another example is Bank of America
- As we told you in September, we had won their Mastercard Cash 1-2-3 consumer credit cards
- We'll be launching those exclusively by the end of Q1
- They leverage many of our capabilities, including fraud products, advisors, and then also one of our largest labs as a service customer
    - And that's where we innovate together with our customers, using design thinking to rapidly co-create targeted solutions for their business opportunities

Europe

- In Europe, we were pleased to announce that later this year we will be launching the new Virgin Atlantic consumer credit card, and that is issued by Virgin Money in the UK
- We continue to make progress with European banks
- We signed a number of new deals with large issuers in France this quarter, including moving market share with the flip of Crédit Mutuel's debit business

ING Bank

- In addition, we are shifting share to us in credit and debit from local competitors with ING Bank
- In Italy, as one example, ING is also launching new prepaid issuance with Mastercard, and they're leveraging added benefits such as Mastercard Instalments, which gives consumers financial flexibility to split their payments over monthly installments
- Now, the interesting aspect beyond this is that ING's implementation is entirely managed by our APIs
    - And of course, it gives their customers an easy way to convert purchases to installments through their mobile banking app

Latin America

- We have also been getting debit in other regions, such as in Latin America, where we signed a new deal with Davivienda in Colombia, emphasizing cross-border and digital capabilities
- We launched a new co-brand debit program with Amazon in Mexico

Middle East

- In the Middle East, a flip of Doha Bank's debit portfolio is giving us portfolio exclusivity in one of the most affluent markets globally
- In China and India, we're making progress

- We signed new deals in China this quarter with customers such as ICBC, China Industrial Bank, the Agricultural Bank of China
- In India, the government has finally published new merchant discount rates, and we think that's going to spur merchant acceptance and continued transaction growth over the next few years
- And we're making progress with VocaLink
  - Since the acquisition in May, we have launched real-time payments with The Clearing House in the U.S
- We have further scaled the person-to-merchant Pay by Bank app, and we went live with an image-based clearing system with a check and credit clearing company in the UK
- In Q4, we expanded our analytics capabilities at VocaLink
- We have successfully launched a corporate fraud alert product, with RBS as our first customer
  - They're using analysis of corporate payment history and machine learning to help protect companies with their clients against various types of corporate fraud, with voice redirection being an example
- On the infrastructure side, we are participating in a number of RFPs around the globe, and we believe these will position us well in the real-time payments space over time
- And in parallel, we're developing apps and value-added services that can be deployed across this infrastructure

Digital Business

- So a few comments on the digital space, we have expanded the rollout of tokenization, which as you know, is the foundational technology for secure digital payments
- We've added 500 new issuers and 21 markets over the course of 2017
- And we now have a total of 1,200 issuers in 46 markets
- For the year, we saw tokenized transaction growth of over 500%
  - Now, that's from a small base, but it reflects this momentum that I'm speaking to
- And last year, we continued to see how important the seamless digital purchasing experience is to our merchant partners, as we grew Masterpass acceptance with Dunkin' Donuts, Walgreens, Verizon Wireless, and many others

Partnership Addition

- And this quarter we're pleased to add several more partners, including in the grocery category, such as BJ's and Giant Eagle in the U.S
- With McDonald's, we're going beyond a simple implementation and helping them develop a food delivery app with exclusive Masterpass acceptance in multiple markets across Latin America

U.S. Tax Reform Update

Now let me wrap up by saying a few things about U.S. tax reform

We see this as a very positive development for the country, particularly in the near term, and businesses will have an increased capacity to invest and many consumers will have more disposable income

What we are thinking in – of taking of opportunity – take the opportunity is to make several focused investments that build on our longstanding commitment to strengthen our business, support our people, and make a positive contribution to the communities where we operate, while of course continuing to provide strong capital returns to our shareholders

Business Investments

- And so I'm going to lay out a couple of steps we're going to take
- The first one is we will make additional investments in our Center for Inclusive Growth, which we launched back in 2014 as a way to focus our data expertise, technology and philanthropic investments to support inclusive growth
- You know that we believe that enables more people to become financially empowered
- It's therefore good for our business as well
- Over the next several years, we plan to invest an additional $0.5B to fuel their philanthropic contributions into the community, and among our initial efforts will be training programs for U.S. workers to help create the workforce for tomorrow
  - Now these additional investments in this center go beyond the impacts we already delivered through other existing initiatives across the company as well as the Mastercard Foundation, which you will recall is one of the world's largest private philanthropic funds, and of course, our public-private partnerships with governments which today are in over 60 countries
- We've got 1,300 programs, and that's taken us more than two-thirds of the way to our goal of bringing 500mm more people into the financial system

U.S. Tax Reform Benefits

- Our second area of focus with this opportunity around the U.S. tax reform is our employees and their retirement planning
- And while we've always been an active and generous contributor to our employee benefits, we're going to take this opportunity to enhance our employer match to 10% for defined contribution retirement plans
  - Now this will be an opportunity for the majority of our employees, including those across the United States, to benefit from this change

Investments

- And finally, we will absolutely accelerate investments, both on an organic and inorganic basis, in areas that are aligned with our business strategy, digital infrastructure, Fast ACH, data analytics, those places
- Now, just to put this in context, yes, we will be making all these additional investments, but the majority of the tax savings will be used to invest in the growth of our business and also to return excess capital to our shareholders

Martina Hund-Mejean

Financial Results

As you can see in the highlights on page 3, we have delivered another strong quarter

Foreign exchange was a tailwind of about 2.5 ppt [percentage points] to net revenue and 3 ppt to net income, primarily due to the strengthening of the euro

I will now highlight the numbers on a currency-neutral basis excluding the impact of special items, which I will explain in more detail on the next slide

Earnings Highlights

- Net revenue grew 18%, driven by solid momentum in our core business and includes a 3 ppt benefit from acquisitions
- Operating expenses increased by 15% and includes an 8 ppt impact from acquisitions, primarily for VocaLink
- Operating income grew by 20% while net income was up 25%, resulting from our strong underlying performance and a lower tax rate
- EPS was $1.14, up by 30% y-over-y, with share repurchases contributing $0.03 per share
- During the quarter, we repurchased about $1B worth of stock and an additional $287mm through January 30, 2018

Impact of U.S. Tax Reform

- So let me turn to page 4, and here I'm going to touch on the special items we have taken this quarter
- The U.S. tax reform resulted in three impacts to the tax line in our P&L in Q4
- This is our best estimate based on our current interpretation of the new tax laws and could still change during 2018:
- The first item is $629mm charge related to deemed repatriation on accumulated foreign earnings and is payable over eight years
- The second item is related to the revaluation of our deferred tax assets and liabilities at the new corporate tax rate of 21%
  - Since we are in a net deferred tax asset position, we have recorded $157mm charge this quarter
- Finally, we have an $87mm impact due to the loss of certain foreign tax credits and a change in policy regarding foreign earnings
- The total of all tax impacts related to the U.S. tax reform bill was $873mm, or $0.82 per share
- In addition, the economic and political conditions in Venezuela continued to deteriorate
  - And therefore, similar to what other companies have already done, we have decided to exclude the financial results of those operations from our consolidated financial statements for future periods
  - This has resulted in a pre-tax charge of $167mm or $108mm after-tax
- However, we will continue to provide switching and other services in the country
- As a result of these special items, we have combined after-tax impact of $981mm or $0.92 per share this quarter

Operational Business Performance

So let me now continue to explain our underlying business performance for the quarter

Here on page 5, you can see the operational metrics for Q4

GDV Growth

- Worldwide gross dollar volume, or GDV growth, was 13% on a local currency basis, and that's up 2 ppt from last quarter
- We saw solid double-digit growth in all regions outside of the U.S
- U.S. GDV grew 9%, up 3 ppt from last quarter, and was made up of credit and debit growth of 10% and 8% respectively
- Outside of the U.S., volume growth was 15%
  - That's up 2 ppt from last quarter, led by Europe and Asia
- And cross-border volume grew at a healthy 17% on a local currency basis, with strong double-digit growth across all regions, again, led by the U.S. and Europe

Switched Transactions

- Turning to page 6, here you see switched transactions continued to show strong growth at 17% globally, with U.S. growth up sequentially
- Similar to the last few quarters, we saw healthy double-digit growth in all regions outside of the U.S
- Globally, there are 2.4B Mastercard and Maestro branded cards issued

Revenue Contributors

- Now let's turn to page 7 for highlights on a few of the revenue line items, again described on a currency-neutral basis unless otherwise noted
- As I already mentioned, net revenue increased by 18%, including approximately a 3 ppt benefit from acquisitions, and was driven by strong transaction and volume growth as well as growth in services
- Rebates and incentives grew 23%, reflecting higher volume and incentives for new and renewed deals
- Let me quickly go through the individual revenue line items
- As we've commented on throughout the year, the difference between fees charged and volumes and the domestic assessment and cross-border categories were mainly due to pricing, which was essentially offset in rebates and incentives as well as some mix
  - This continues to be the case this quarter
- The domestic assessment grew 19% while worldwide GDV grew 13%
- Cross-border volume fees grew 19% while cross-border volume was up 17%
- Transaction processing fees grew 22%, primarily driven by the 17% growth in switched transactions as well as revenues from our various services offerings
- And finally, other revenues grew 15%
- As a reminder, most of the VocaLink revenues show up in this line
- Advisors and safety and security revenues were also up

  - These items more than offset the 4 ppt impact from the changes we made to our loyalty business in Asia that I've called out previously

OpEx

- Moving on to page 8, here you can see that total operating expenses increased 15% excluding special items on a currency-neutral basis, and that was higher than our expectations due to foreign exchange hedging losses
- Similar to last quarter, this includes an 8 ppt impact from acquisitions, primarily from VocaLink, including the impact of purchase accounting and integration-related costs
  - The remainder was due to our continued investment in geographic expansion and digital capabilities

Global Switched Volumes

- I am going to move on to slide 9, and here we're going to discuss what we have seen so far on the drivers for January, and the numbers are through the 28th of January
- Starting with switched volume, global growth is at 14%, up 2 ppt from what we saw in Q4, with healthy growth in all regions
- In the U.S., our switched volume grew 10%, up 2 ppt, with higher growth in both credit and debit programs
- And switched volume outside the U.S. grew 18%, up 2 ppt too, driven by higher growth in Europe, with slower growth in APMEA, as we lapped difficult year-ago comps related to the de-monetization effort in India
- Globally, switched transaction growth was 16%, down 1 ppt from what we saw in Q4
  - This decrease is the result of the exclusion of Venezuelan transactions, as we will no longer be recognizing the related revenue in 2018
- Ex-Venezuela, our growth was similar to Q4

Cross-Border Volumes

- With respect to cross-border volumes, our volumes grew 22%, up 5 ppt, with double-digit growth in all regions
- So let me explain this a little bit more
- About 3 ppt of this was driven by higher growth in Europe, resulting from both increased intra and inter-Europe travel, as well is holidays extending further into January this year in certain markets
- APMEA also contributed about 1 ppt to this growth
  - The remaining 1 ppt was driven by cardholders funding accounts at cryptocurrency exchanges, which was then used to purchase these digital currencies
- You should note that these accounts can be funded from a number of sources such as bank accounts, wire transfers, et cetera
- With the recent interest in and the price volatility of cryptocurrencies, we have seen an increase in this activity
  - Just to be clear, we do not switch or settle cryptocurrency transactions over our network
- Our plans do not assume this type of activity will continue, as we have no line of sight as to how cardholders will view cryptocurrencies in the future, and given that we've already seen some declines in our recent weekly trends

2018 Outlook

So now I'm going to turn to our thoughts about 2018 on slide 10

Let me start by talking about the numbers on the same basis as we always have; that is, before the impact of the new revenue recognition rules on a currency-neutral basis and excluding acquisitions and special items

- On this basis, our business fundamentals remain strong, and we continue to grow through the combination of new and renewed agreements and our expanded set of service offerings

We expect the global economic environment to be similar to what we saw last year, with a few areas to monitor as Ajay mentioned

Revenue

- With this backdrop, we expect to deliver strong organic growth again this year, with net revenue growing towards the high end of the low double-digit range
  - This is in line with our recent trajectory, though we will be absorbing a slight headwind as a result of the de-consolidation of our Venezuelan entity

OpEx

- On the expense front, we continue to invest in key long-term growth areas such as digital, security solutions, and geographic expansion, in addition to the incremental employee and technology investments Ajay just highlighted
- Overall, we expect operating expenses will grow at a mid-single-digit rate y-over-y, reflecting our ongoing cost management efforts
- So as you can see, we are well positioned to deliver strong operating performance again in 2018, slightly ahead of where we had previously expected

Acquisitions and New Revenue Recognition

- Turning to slide 11, now let me add to those growth numbers the impact of acquisitions, the new revenue recognition rules, and the investment in the Center for Inclusive Growth that Ajay talked about
- All of these items are very important when you try to model our results for 2018, so please bear with me as we're going through this
- So let me walk down the chart
- First, with respect to acquisitions, we estimate that having the acquisitions for a full year in 2018 rather than just a partial year in 2017 will contribute about 0.5 ppt to revenue growth and approximately 2 ppt to OpEx growth for the year
- Second, the new revenue recognition rules will contribute approximately 2.5 ppt or $300mm to revenue growth, and 4 ppt or $200mm to expense growth, based on our current estimates
- These amounts are driven by two factors:
  - First, we have recently determined that certain market development programs will now flow through the P&L on a gross basis, resulting in about $200mm in increased revenues and offsetting expenses
  - The remaining $100mm relates to a change in the timing of when particular deal incentives are recognized

- These amounts, which are also detailed in the appendix, are estimated based on our current and assumed commitments and are thus subject to change
- We will be disclosing the impact of the new revenue recognition rules on a quarterly basis throughout 2018, so you will be able to follow the effects each quarter
    - You can have fun with that one
- Just as a reminder, the new rules have no impact on the underlying economics of the business
- And finally, we will be expanding our Center for Inclusive Growth
    - The initial contribution will be $100mm to a new not-for-profit entity to enable a variety of workforce training, financial inclusion, and digital infrastructure initiatives, which will add another 2 ppt to operating expense growth for the year
    - We expect to take this charge in Q1

Gross Net Revenue and OpEx

- So overall, with these adjustments, we estimate 2018 y-over-y gross net revenue will grow at a mid-teens rate, and operating expenses will grow low double digits, both on a currency-neutral basis and excluding special items
- I have a few other items for you to consider for 2018
- We expect operating expense growth in Q1 to be $250mm higher than what our annual growth rate of low double digit would imply due to: the timing of the market development programs, which I just referred to as part of the new revenue recognition rules; the impact of the acquisitions, which occurred after Q1 last year; and the charge for the Center for Inclusive Growth

FX and Tax Rate

- When modeling as-reported numbers, foreign exchange is expected to be a 1 to 2 ppt benefit to the top line and about a 2 ppt benefit to net income for the year based on our planned exchange rates
- And finally, we expect a tax rate of approximately 20% in 2018, primarily due to the impact of the tax reform here in the U.S

Long-Term Performance Objectives

So turning to slide 12, I would like to move to our long-term performance objectives for the 2016 to 2018 period

As a reminder, these objectives are on a currency-neutral basis

They do exclude acquisitions and special items and are normalized for tax

- They do, however, incorporate the impact of the U.S. tax reform in 2018

Revenue

- For revenue, given our expectations for 2018 that I just discussed, including the new revenue recognition rules, we now believe that net revenue will grow in the low teens on a three-year CAGR basis

Operating Margin and EPS

- We remain committed to a minimum annual operating margin of at least 50%
  - And we now expect EPS CAGR over the three-year period to be in the mid-20s, up from the approximately 20% we last commented on
  - This reflects our continued strong business performance and expanse management initiatives as well as a 4 ppt benefit from lower taxes in 2018
- The new revenue recognition rules to be implemented in 2018 are expected to have a minimal impact on the three-year EPS CAGR

Ajay Banga

Closing Remarks

We're pleased with 2017 financial results

We think it's all driven by strong operating performance and execution of our strategy

Overall economic trends are positive

And as we said a couple of times on this call, we're going to monitor some risks and uncertainty that Martina and I have spoken to

- But overall, we expect 2018 growth to be similar to 2017

Meanwhile, we expect tax reform to benefit the U.S. economy and have a positive impact on our company

- We see this as an opportune time to further invest in our employees and communities and continue to strengthen our business's strategic investments in those key growth areas while continuing to return excess capital back to our shareholders

And so thank you for your continued support of all of us and our company and thank you very much for joining us on the call today

QUESTION AND ANSWER SECTION

<Q - James Schneider>: I was wondering if you could maybe start out on the healthy trends you've seen across the globe, but particularly in international debit, which I think accelerated, as you mentioned quite a bit. There was a particular pickup in Europe. Can you maybe talk about how much of that is market share, how much of that is the improving economy? And maybe you can talk about the impact going forward on your yields, given it seems like there was a substantial decrease again in the number of Maestro cards as you convert those to standard debit.

<A - Martina Hund-Mejean>: Let me just take this for a minute. In Europe, where we've seen really good drivers in Italy and Germany and France, a number of these countries, and those are good economic environments. I called out that the holidays in January lasted a little longer in some of these countries. In terms of where we added market share was really in the Nordics. So we actually have flipped a deal in Sweden. That is coming in over this year, and that will actually benefit these numbers.

From a Maestro point of view, yes, you're absolutely right. We have been talking about that in a number of countries. We're actually flipping our Maestro portfolios into debit MasterCard portfolios. We are very well on our way in many of those countries, and what we are actually seeing is when we do these flips that on the new debit Mastercards we see about 2x the volume we used to see on the Maestro cards. So we are not just seeing cross-border volume, but we are also seeing local volume. And that will continue to benefit, and it will improve our yield over time.

You have actually been seeing that our yields have been improving over the last many years, both on the core business, where you're seeing it predominantly because of the addition of processing that were coming in. By the way, we are now processing about 54% of the transactions that are done on Mastercard vs. when you just look two years ago, it was just shy of 50%; and secondly, of course, the healthy cross-border trends. When look at our total yield, that is where obviously our growing services offerings are really benefiting us, and that's why you're seeing very healthy yields across the whole country.

<Q - Donald Fandetti>: The cross-border number, even if you strip out cryptocurrency, was noticeably better. And I know the dollar has been generally weakening. Do you expect as you think about guidance for 2018 and just look out, have we stepped up into a structurally higher cross-border rate? And then lastly, can you talk about volume into the U.S. cross-border?

<A - Martina Hund-Mejean>: Don, I'm so glad you're asking this question because of course when you see for the first four weeks in the year a 22% cross-border number, you're asking exactly the right question, in my opinion. What we always say is four quarters do not make a year. In fact, the guidance...

<A - Ajay Banga>: Four weeks. Four weeks don't make a year.

<A - Martina Hund-Mejean>: Four weeks don't make a year.

<A - Ajay Banga>: Four quarters do. [indiscernible] (33:43)

<A - Martina Hund-Mejean>: Yes, four quarters do. You're absolutely right, Ajay, as usual, so four weeks don't make a year. But in particular, all of the guidance that we're giving you for the top line of 2018, we are not planning on those kind of cross-border growth numbers. We are planning much more to what we have been seeing over the last couple of years. And even with the weaker dollar, I don't think that trend will change much. So I don't think it's prudent to be planning on this kind of number, and I would like to point you back to the guidance that we had from a new revenue point of view.

<Q - Donald Fandetti>: Okay, and then the volume into the U.S.?

<A - Martina Hund-Mejean>: Volume into the U.S., we actually do see mid-single-digit volume into the U.S. What we do see is volume outbound of the U.S. is picking up.

<Q - Darrin Peller>: I just want to touch on when you look at your guidance for 13% revenue growth at the – or 15% including the accounting changes, just vs. the 18% run rate, just make sure we have the right variables that would cause the deceleration being I guess Venezuela, M&A grow-over, lower pricing, anything else we're missing there, just lower pricing benefits?

<A - Martina Hund-Mejean>: Yeah, so...

<Q - Darrin Peller>: And then just quickly, Martina, when you look at the tax investments, I just wanted to squeeze in, what will be the steady state of investment beyond 2018? Some of this just feels that it could be one-time. Or should we expect that to continue? Thanks, guys.

<A - Martina Hund-Mejean>: Yes, okay. On the first question, first of all, you need to take into account the 0.5 ppt on Venezuela. That's the impact on revenue. And then in particular, you also need to take into account the acquisitions that you called out. We had eight months of acquisitions built into 2017 numbers, and so you only get the lapping effect from the four months. So when you actually look at the total results of 2017, we are basically saying that 2018 is just going to be slightly better, in part because, of course, what we're expecting in the United States, even though we are very watchful on a number of more potential risk countries around the world, right? Middle East /Africa is a risk country. We are watching very carefully Brazil. We are watching very carefully Mexico, as well as the impact, potential impact from a Brexit point of view. So overall, while the U.S. is a little better, we're actually believing that the economic environment in 2018 will be very similar to 2017. So our business baked in just slightly better than 2017 on the net revenue side. That's where we are.

<Q - Darrin Peller>: Okay, and on the tax savings? Yes.

<A - Martina Hund-Mejean>: Yes, on the tax impact just your second question. So what we're doing, in terms of the Center for Inclusive Growth, as Ajay said, we're planning over several years to put $0.5B into that center. The first chunk is going to go in, in Q1 with $100mm, and then we're going to see how we're going to lay it out for the next several of years. So you are going to have to expect that we are going to continue to do some contributions in that, not in 2018, but likely 2019-2020, et cetera.

The employee benefits, that is a permanent adjustment, of course. That's not just a one-time thing. We really want to make sure that our employees are focused on making sure that they are well situated from a pension benefit point of view. So this is going to go in this year, sometime this year. We haven't given a date yet, and that's going to continue. The other investments are also in our baseline. And I would suggest to you that both organically as well as inorganically, we're going to continue to look at that and make more investments.

<Q - Darrin Peller>: Okay.

<A - Ajay Banga>: Particularly in those areas that we're talking about, from digital and technology and data and Fast ACH, the kind of things we talked about in September. We're very focused on the strategy.

<Q - David Mark Togut>: Europe continues to accelerate nicely, and clearly a lot of that's due to some solid market share gains. But I'm wondering, Ajay, if you could comment on the merchant acceptance footprint in Europe for electronic payments, especially post-interchange caps a couple of years ago.

And then my follow-up is on PSD2 and any update you could give us on bringing VocaLink's capability to the European continent in advance of PSD2.

<A - Ajay Banga>: The first part, the merchant acceptance, there is growth across the European region on merchant acceptance from large outlets that earlier used to prefer to take either local payment systems only or cash. And that changes that, all the way to small ones. What you do see really changing also is a reduction in suppression. So even if the outlet said we accept – in actual fact, when you showed up for a small ticket charge or a low-value payment that would encourage you to lay off the idea of producing electronic payment, I think all that has changed quite dramatically. It's helpful. It's part of the secular change in the way cash is used in the European economy.

I wouldn't declare victory on that right now because I think a year or two in Europe is a relatively small time in a set of complicated countries with lots of local dynamics vis-à-vis local schemes, local players and the like. So I would tell you keep your eye on that space, and we'll keep working with the acquiring community. We are talking about a full five-year transition in a continent like Europe. It's a good sign. It's helpful. It's a nice tailwind, but I'm not running with it to the bank yet. That's going to be the first part. Your second question was about – did I know what the second question was?

<A - Martina Hund-Mejean>: PSD2.

<A - Ajay Banga>: PSD2, favorite topic. So we're coming up to the timeframe of when all this starts to go live in so many ways in different aspects of implementation in Europe. We have been working both internally as well as with the help of our largest clients, as well as in conversations with regulators about the implications of PSD2 and the things we can do around PSD2 with these European merchants and European banks and the new European entities that will get created as a part of PSD2, the PSPs and the various acronyms that are being created in PSD2.

Your question was around VocaLink and PSD2. So to get VocaLink onto the ground in different European countries beyond the software status, which is what it is today in the Nordics and some other markets around the world, will require us to actually participate in the RFP process of different ACH systems being opened up in Europe. We are participating – you heard me in my opening comments. We are participating in those RFPs. These take a year or two to get resolved and settled. After they get settled, it will take a while to get invested and implemented, but we are very active in all of those.

And one of the reasons why I think you will see us using some of the tax reform money in a sensible way in our business is to keep on focusing on the opportunity with Fast ACH thanks to VocaLink's capabilities in Europe but also outside of Europe, even in the United States and other markets. Not just infrastructure, but it could be in the applications, it could be in the scheme rules, and it could, of course, be a different aspect of the range of things we could do with Fast ACH.

<Q - Andrew Jeffrey>: Ajay, a big-picture strategic question for you, especially in the wake last night of a pretty meaningful shift in the PayPal-eBay relationship. One of the things that PayPal has asserted is its value prop to large marketplaces, especially next-gen marketplaces. And I see Mastercard building a pretty comprehensive value proposition of its own. And I just wonder how you think about the so-called commodity nature of Visa/Mastercard vs. the value-add of a provider like PayPal and whether or not the lines perhaps are beginning to blur a bit in terms of go-to-market value proposition.

<A - Ajay Banga>: So I think in the whole E&M commerce space, there's so much going on, Andrew, in that whole space. And I think if you go back in time when essentially Visa and Mastercard in those spaces and other brands like us, Eurocard, football card co-brands, we got into a position where we became part of a dropdown on a merchant's checkout site. In a dropdown, you've got one brand or the other and you enter a lot of details and you enter a lot of addresses, and that created its own friction and its own lack of branding at the checkout point, even though the consumer was aware of the brand because they were looking at their card and entering the data. I think that's moving, and PayPal is one way of that movement, but our own efforts with branded checkout points is moving, and we will continue to do that.

I think PayPal itself, its relationship with eBay, I want to look at the IPO time as something for Dan [Schulman] to answer, but I'm pretty certain that all of you thought about one day that relationship will come up for reassessment. Then, it's come up for reassessment, and eBay has chosen what it wants to do. I think Dan has done some interesting work of building out his partnerships in the meanwhile. Chase consolidated its own position today with their second and third leg of the stool. And I think we are a key beneficiary of that because, as you know, we've got a great partnership with PayPal, which includes all their co-branded cards and their corporate cards and all the understanding about how their wallet is used, including the visibility of the brand and the non-steering towards ACH and the data flow and basically the pass-through angle, competitive stage angle, blah, blah.

So my general net take of all this is this is still a wide-open field. It's going to be years before you can figure out who is playing what game here. All I'm trying to do with our company and all of us are doing is we want to be very much a part of that game. So we will keep investing in tokenization and secure checkout. We're going to keep investing in an enhanced consumer experience in digital. You'll find us doing all kinds of things with banks, with merchants in that space. We're going to keep investing in allowing the developer community to access our capabilities in digital and core payments, so the simplest form of APIs and SDKs, so we can get embedded in more and more locations. We're going to keep investing in creating good R&D with our labs and making sure that they are capable of working with our clients with labs. And the service you heard me talk about that with specific reference to Bank of America, but frankly, it applies to many other clients as well. So we've got a whole series of strategies in digital to make us not be anywhere other than at the forefront of what's going on here with simple, transparent standards and standards that are important because they enable merchants and banks to connect one-time, not multiple times.

So you'll see us over this period of years to come, that's the focus, simple experience, simple standards, focused on security, secure every transaction, make sure we do good stuff with labs, make sure the open APIs and SDKs are available in venues, and make sure that we focus on all forms of payment, not just card rails but ACH, Fast ACH, all those so that you enable banks and merchants to do the best thing for their consumer. That's our digital strategy, not changed. PayPal, eBay, other issues will come and go. We bring what we need to do.

<Q - Jason Kupferberg>: Just two quick ones, first on your rebate incentive expectations for 2018. And then can you just give us the latest update on what you're thinking in terms of what might happen in Europe with the European Commission looking at some of the inter-European cross-border interchange fees, some of the potential fines? I know you've disclosed this in your 10-Q. Is there any way you could frame up what percent of your cross-border business is actually inbound into Europe just so we have some sense of reference in case we get some headlines on this?

<A - Martina Hund-Mejean>: All right. Jason, first of all, on your first question, I'm not going to give you any guidance on rebates and incentives in 2018, and it is because of the new revenue recognition rules coming in. There are so many moving parts between gross revenue and contra-revenue that I just feel, given all the work that we were able internally to do, I just feel that the net revenue number is just the best guidance that I can give you. But I do want to take the opportunity to deep dive into that just a little bit more.

As you know, I called out $300mm benefit on the net revenue line due to the new revenue recognition rules. $100mm of that is really in relation to customer business agreements and to incentives. And there are a number of effects that we had to be estimating in this. So first of all, as you know, we had amortization of incentives from previous deals that have been previously expensed, so in prior years we expensed those. And they will be now expensed over the life of the deal. And that will be a negative, right? We estimate actually that roughly about $0.5B of incentives will need to be re-recognized as contra-revenue under the new rules starting 2018. And the average life of this recognition is approximately seven years, so it's a headwind, it's not really material in the context of our size.

But then in addition to that, we would have had some incentives in 2018 or later that will now have to be carried back to prior years to the original deal inception or carried forward. So that will actually reduce the amount of incentives recognized in 2018. So you can see these two things are toggling with each other. And then the last – the third thing is that obviously we will be having new deals coming in, and that could impact this calculation too, depending on the terms and conditions in these kind of deals.

So when you put all of this together, we do estimate the net benefit of that $100mm that I just referenced, but obviously that could change over time. And then beyond 2019, we will continue to amortize the remainder of that $0.5B, of that roughly $500mm that we have to re-recognize as contra-revenues under the new rules. So you can see this is a relatively complex area, and that's why we're staying with net revenue guidance and we're not going to split it up in gross and into contra.

With respect to your second question, there's really not much more that we can say to you. And quite frankly, what our cross-border business, inbound business in Europe, it has actually no relationship in terms of how the European Commission would be looking at fining us, if they fine us. But we have at this point in time really no new news. So I'm still going to point you back to the last Q that we filed. That was a pretty accurate statement in there. And unless something happens between now and when we file the 10-K on what, February 14 or 15, if we have an update, obviously the 10-K will be updated by that time.

<A - Ajay Banga>: Martina is in accounting heaven for the last few weeks and months.

<Q - Jason Kupferberg>: Yes, between rev-rec and tax, I'm sure it's been a party.

<A - Ajay Banga>: Yes, and you've also got Venezuela, which she's done an outstanding job of in trying to put her arms around how to manage that through the next period of time. In Venezuela, we're still very much on the ground doing all the right things. We've got a great team. We are supporting a lot of our clients there. We're not pulling out of the business on the ground. That would be a very unfortunate thing to do, and I think it will spark all kinds of humanitarian issues given the role we play in that economy. In fact, we try to work with other players, including multilateral institutions, to try and find a way to make this a sensible outcome because there will be an outcome one day in Venezuela. So this is not a – you've got to think out long term on what we're doing is all of these things, whether it's European cross-border or Venezuela or these rules.

At the end of the day, we're trying to give you guys some part of what we're thinking in terms of what the impact could be. But Martina has laid out a pretty good estimate of where we think our 2018 revenues and expenses and EPS and our combined 2016 to 2018 goals will go, right? And I'd say to you, over 2016 to 2018, we've had a good run. We gave you an update in September when we raised our guidance. Now what we are doing basically is making sure the accounting flows through. Yes, there's a small improvement in 2018, which you pointed out. Some of it gets eaten up by Venezuela. Some of it gets eaten up by the lapping of the acquisitions. That's where we are. We are running our business to win share and keep taking advantage of the secular trend in the business. That's what we're trying to do and not getting ourselves tied up between rebates and incentives and gross revenue and net revenue at a time when there are so many moving parts and asking someone to estimate accurately would be asking for the moon.

<Q - Bryan C. Keane>: Thanks. I just wanted to talk or ask about two things. One, just the strength in U.S. credit and debit, is that just lapping of some of the headwinds? Obviously, USAA, but the numbers are obviously picking up there, or maybe straightened.

<A - Martina Hund-Mejean>: It is, Bryan. It is.

<Q - Bryan C. Keane>: Okay, so there's nothing else to call out there?

<A - Martina Hund-Mejean>: No.

<A - Ajay Banga>: No, most of it is just tax. And then all the other things you heard about us winning, they're all coming on board. So you'll see some benefit from Bank of America when it starts issuing. It will take time. You'll see some benefit from the Kroger co-brand, the Cabela's co-brand. But these things take time. Meanwhile, there's the natural spending pattern that SpendingPulse shows up. And there, as I said, fourth quarter growth was actually lower y-over-y than third quarter, just to be clear.

<Q - Bryan C. Keane>: Yes. Yes. And it doesn't seem there's no flips going the other way, like that created the headwind like USAA.

<A - Ajay Banga>: Don't go there. You're giving me nightmares. Don't go there.

<Q - Bryan C. Keane>: Yes. And then my follow-up is just on tax reform. I just was trying to quantify total tax reform investments. I got the $100mm for the Inclusive Growth, and then just thinking about employee retirement and then some of the accelerated investments that you talked about, Ajay. Just in all, it seems like maybe we're getting to 20% to 25%. I was just trying to get to a number of what we're reinvesting total of the tax benefit. Thanks.

<A - Martina Hund-Mejean>: Okay. So just to let you know, the total cash tax benefit as a result of the tax reform on an annual basis is in the zip code of $450mm, right, and we're doing then two things. One, we're taking the $100mm in order to invest it into the Center for Inclusive Growth. And the other part that Ajay was mentioning in terms of the employee benefits as well as the additional investments we're doing, we have that embedded in the baseline of the operating expenses, okay? And it's all embedded in the low double-digit guidance that I have been giving to you for 2018 based on the new revenue recognition rules.

<A - Ajay Banga>: I don't want to run a business in which I am paying employees for their retirement long term because this is not a one-year $1,000 contribution kind of thing. We are adding to our already good 401(k) and defined contribution plans around the world. And secondly, we're investing in data and digital and Fast ACH. You don't run a business where that stuff is kept as a separate item. So Martina has got those embedded in the way we look at the future of our business.

The only thing that's not embedded in that is these lumpy contributions that are going to the Center for Inclusive Growth because honestly, $100mm going into that center being directed for workforce training and financial inclusion in the U.S. and elsewhere, that kind of lumpy contribution is the one that we've not got embedded in our guidance [ph] schemes (55:48). We're telling you about it, but it's embedded in the total but not in the net that we're looking at. Right, Martina?

<A - Martina Hund-Mejean>: It's in the low double-digit operating expense guidance. We put 2 ppt for that particular contribution.

<A - Ajay Banga>: In the total.

<A - Martina Hund-Mejean>: In the total.

<A - Ajay Banga>: But not in the organic growth.

<A - Martina Hund-Mejean>: No.

<Q - Craig Jared Maurer>: I wanted to ask you on Brazil considering the recent IPO drawing attention there, plus you're seeing the recovery finally seeming to be on firmer ground. You've gained a fairly enormous market share against Visa there over the last few years, and I believe last summer you're now the biggest new issuance brand in Brazil. I was wondering if you expect to see: A), Visa be able to rebound against you there; and B), how you look at that market going forward considering the big gains you've had recently.

<A - Ajay Banga>: First of all, I will always expect my competitors to make every effort possible there. They're a good and strong company. They've got good people on the ground. They're going to make efforts to win back share. And that's just the reality, and I believe that we survive by being competitively paranoid about all our competitors. So that's to me just a particular given that they'll attempt.

There's a lot of competition on the ground. It's not just Visa. It's Elo. It's the local methods of doing – there's a lot of competition on the ground locally. There are also a lot of regulatory changes that are going on in Brazil, including with the bankers association attempting to look at the idea of the way installments are paid and the whole installment method is managed, including the settlement time. There's a ton of things going on in the market in which we are today a very large market share player there.

The political environment in Brazil, yes, this year, 2017, showed an improvement, but you've got to remember you're comparing 2017 to 2016, which was not a politically, let's say, delightful year in Brazil. It was a hard year, and they got some political stability. 2017 turned out to be better. Good economic policies were getting put in place.

Remember that 2018 has an election, and that election has currently identified two players to come there, none of whom are in the current government. And so it's a little unclear to me what instability that could cause in the economic environment. That's why Martina pointed out and I pointed out that there are pockets of instability across the world to be careful of, and Brazil is one of those, for this reason of the political circumstance and the longevity of their economic reforms. I've been around a long time working with Latin America, and I've learned that you cannot take for granted what happens for a couple of years because it does find its way through changes on where politics goes.

So that's where we are. I'm relatively constructive about Brazil. We're investing on the ground. The number of people we have in our office has increased. Our capabilities on the ground have increased. Our technological investments on the ground have increased, and we're going to keep seeing growth there is what I'm hopeful for. But 2018 is a year to watch out for.

<Q - Tien-Tsin Huang>: I won't ask my accounting question. I just want to ask about deal activity maybe because based on Craig and Bryan's questions. How would you characterize, guys, the pipeline for new deals and renewals this year, in 2018 vs. 2017? It seems like you have a good backlog going, so I'm curious what the pipeline might look like for this year, especially in things like B2B, if you at all can comment on that.

<A - Martina Hund-Mejean>: So, Tien-Tsin, obviously the numbers in Q4 that you saw on the rebates and incentives, we had given you a little bit of a heads-up on our November call that that number might be coming in a little bit higher than what we had forecasted before. That should show you that we have actually terrific deal activity in Q4, and those deals will be rolling in over the next 6 to 18 months. It depends which year you're looking at. I, quite frankly, with everything that I'm seeing from the pipeline, from our regions around the world, I think that we are going to have similarly robust deal activity in 2018. I don't think there's any letting up. I think there are a lot of players in the market that are looking to do things with us as a network, and it will be similarly robust.

<A - Ajay Banga>: On B2B, Tien-Tsin, the global travel deals that we did over the last couple of years, they're actually helping us in our cross-border, as an example. In fact, somebody's question, I forget, on cross-border. But there's all this work we're trying to do with the B2B hub. We've announced that one partner signed up. There's a bunch of partners in the pipeline. Hopefully a few of them will come in to locking on. There's all the work we're trying to do with Fast ACH and send in different parts of the world. So B2B is pretty active for us right now. We consider ourselves to have good assets in place. So we're working on pipeline hard.