Q1 2019 Earnings Call

Company Participants

- Ajay Banga, President and Chief Executive Officer
- Sachin Mehra, Chief financial operations
- Warren Kneeshaw, Head of Investor Relations

Other Participants

- Bryan Keane, Analyst
- Craig Maurer, Analyst
- Darrin Peller, Analyst
- David Togut, Analyst
- Donald Fandetti, Analyst
- Eric Wasserstrom, Analyst
- Lisa Ellis, Analyst
- Ramsey El-Assal, Analyst
- Robert Napoli, Analyst
- Sanjay Sakhrani, Analyst
- Tien-tsin Huang, Analyst
- Tim Murphy, General Counsel
- Tom McCrohan, Analyst

Presentation

Operator

Good morning. My name is Tasha, and I will be your conference operator today. At this time, I would like to welcome everyone to the Mastercard Q1 2019 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speaker's remarks, there will be a question-and-answer session (Operator Instructions) Thank you.

I'd now like to turn the call over to your host Warren Kneeshaw, Head of Investor Relations. Please go ahead.

Warren Kneeshaw {BIO 16549173 <GO>}

Thank you, Tasha. Good morning, everyone, and thank you for joining us for our first quarter 2019 earnings call. With me today are Ajay Banga, our President and Chief Executive Officer; and Sachin Mehra, our Chief Financial Officer.

Following comments from Ajay and Sachin, the operator will announce your opportunity to get into the queue for the Q&A session. It is only then that the queue will open for questions. You can access our earnings release, supplemental performance data and the slide deck that accompany this call in the Investor Relations section of our website, mastercard.com. Additionally, the release was furnished with the SEC earlier this morning.

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.

Please note that the growth rates we provide for switched volume, switched transactions and cross-border volume have been adjusted to normalize for the effects of differing switching days between periods. These adjustments have been made in current and prior quarters. This information is being provided so that you can better understand the underlying growth rates of these operating metrics. Our comments on the call today will be on the basis of these adjusted growth rates. We do not normalize GDV growth rates.

Finally, as set forth in more detail in our earnings release, I would like to remind everyone that today's call will include forward-looking statements regarding Mastercard's future performance. Actual performance could differ materially from these forward-looking statements. Information about the factors that could affect future performance are summarized at the end of our earnings release and in our recent SEC filings. A replay of this call will be posted on our website for 30 days.

With that, I'll now turn the call over to our President and Chief Executive Officer, Ajay Banga.

Ajay Banga {BIO 4676567 <GO>}

Thank you, Warren, and good morning, everybody. We are off to a solid start this year, revenues up 13%, EPS up 24% versus the year-ago. As Warren said, on a currency neutral basis and excluding special items. I think these results reflect our strong operational focus and our continued growth across each of our regions. And at the same time, we are continuing to invest in the business for the long term. As you probably noticed with some of our recent product and acquisition related announcements.

Let me start with the macroeconomic environment as usual. You may recall that last quarter we said that the expected solid overall growth to continue in 2019 with some moderation. And our view has not changed from that. That said, we are still monitoring a number of items, this is ongoing trade negotiations and other economic and political factors that could affect growth over the medium to longer term.

US economic growth remained strong, low unemployment, healthy consumer confidence, retail sales grew 3.5% versus a year ago ex-auto, ex gas, according to our SpendingPulse estimates. And that reflect some moderation as expected, as there are some impact from the shift in the timing of Easter this year.

In Europe, we continue to see moderate growth, consumer confidence remains mixed with declines in places like the UK, Ireland and The Netherlands. But despite the uncertainty surrounding Brexit, UK retail spending remains healthy, again, according to what we see in SpendingPulse.

Asia Pacific has been impacted by trade policy uncertainty, we continue to monitor the strength of the Chinese economy. But having said that, we're seeing modest GDP growth in the region overall, and that's kind of underpinned by favorable monetary policies and generally stable labor market conditions.

In Latin America, the outlook is mixed. There is positive signs in Brazil and Chile and that's tempered by some weakness in Mexico. Similarly, in the Middle East and Africa region, we are seeing healthy growth in countries such as Egypt with some softness in the oil producing markets. Meanwhile, our business continues to drive healthy double-digit volume and transaction growth across most of our markets by successfully executing against our strategy.

What I'm going to do is, give you few examples of how we're growing our core products, diversifying our customer base and building new areas for our business. Let me start with growing our core products, where I believe we continue to make good progress in providing people with simple and safe ways to pay with credit, debit, prepaid and commercial products. And it's not a card, the physical card is just one form factor as you've heard me say in the past, we are equally focused on seamlessly delivering our products digitally.

Earlier this month Apple announced the Apple Card with Mastercard and Goldman Sachs. And available this summer, this is a credit product, it is designed for the iPhone that leverages Mastercard's tokenization technology of fraud tools and our chargeback KPIs. Customers can immediately access the digital version of the card in their Apple Wallet, they can also get a physical companion card. With attractive rewards and extensive security features the user experience is friction less.

In addition, we look forward to collaborating further with Goldman's consumer business markets by bringing new products and services to market overtime. We are pleased to be the payment center for T-Mobile's new mobile first checking account, T-Mobile Money. Which consumers can open and manage online, all with an app on their smartphones and they can withdraw funds using a Mastercard debit card.

Coming to markets outside of the US. I think we continue to make significant progress. We are pleased to announce the expansion of our partnership with Santander in Brazil to expand our share of the credit, debit and commercial portfolios of the fast growing customer [ph]. We also extended our long-term agreement with Rogers Bank, which is a key strategic partner for us in Canada. Further expanding the services we provide on their card portfolios. And we are advancing our efforts to increase market share in Europe with BNP Paribas in France, flipping more than 4 million credit cards in a long-term deal that will be accompanied by a full suite of services, including spending controls and alerts, as well as identity check mobile security features.

In addition, we have some great examples of customers with closed loop systems who continue to see value in open-loop Mastercard cards, because of broader acceptance and digital capabilities. One of these as example is Cred-System in Brazil, which is converting 7 million private label cards to Mastercard contactless co-branded cards to open up international acceptance to their cardholders.

Now in the commercial side, we are pleased to be Citibank's chosen network for its cross-border B2B virtual card program in China. And the initial focus there is on enabling Chinese online travel agencies to make payments to hotels, hotel aggregators and airlines outside of China. That same vein [ph] to help our customers provide greater transparency and certainty in cross-border payments. As you know, we have announced an agreement to acquire Transfast, a global cross-border account-to-account money transfer network. We look forward to complementing and enhancing our solutions with their network reach, with their strong compliance capabilities, flexible technology and some very robust foreign exchange tools.

By the way, we currently work with Transfast in support of our P2P and B2B capabilities through Mastercard Send. And why not Mastercard Send, just to give you a quick update. We continue to see healthy growth and we are continuing to develop a number of different use cases. Send currently powers seven of the major mobile P2P program in the United States, and we are working to grow our customer base. On the cross-border front, a number of our issuers are leveraging Send to provide faster and more cost effective and transparent cross-border payments to their customers. Bank of Montreal is the latest to announce that it will implement Send for it's Canadian business and commercial banking clients. And the initial focus there is on bank account transfers, and there are additional plans for payments to mobile wallets and cards internationally.

So now from growing the core, turning to the second pillar of our strategy, the work we are doing on diversifying our customer base and strengthening our footprint in some of these new geographies. We are building relationships with merchant, processors, digital players, and a number of other partners to help drive their businesses forward.

So I'm going to highlight a few specific examples on the core brand area, including our renewal with Target in the US, a new program with Japan Airlines, and with Falabella, which is the largest retailer in Chile. We also entered into an agreement with Mercado Libre, the largest e-commerce marketplace in Latin America to make their platform safer and more convenient with tokenization, seamless authentication tools and contactless prepaid card programs across Brazil, Argentina and Mexico.

Now while doing all this, we are trying to find ways all the time to look for methods to improve our local presence, particularly in areas where there is low electronic payment penetration. That's why our partnerships with and the investments in Network International, which is a preeminent local processor in the Middle East and Africa region. And also Jumia, an e-commerce platform spanning 14 countries in Africa. We think these will accelerate our efforts to deliver a sustained shift from cash and checks to electronic payments in these markets.

Mastercard will be Network International's preferred partner for processing, acceptance and value-added services with safety and security and data analytics. And our relationship with Jumia will include co-brand card issuance for consumers, as well as commercial payments on their platform and also the use of our payments gateway.

And finally, the third pillar of our strategy is building new areas of our business. And we do this in a way that leverage at the core and differentiates our offerings, in particular, with services and new payment flow. So a few examples for you. Safety and security products remain a key area of focus, we recently announced the acquisition of Ethoca, a globally e-commerce fraud and dispute management network. What this does is, it enable the sharing of intelligence between merchants and insurers in over 40 countries. Wherever a fraudulent or disputed transaction is identified, near real-time information is sent to the merchant, so they can stop delivery and refund the cardholder and avoid the chargeback process.

And as a result, both merchants and issuers benefit from reduced costs. With more than 5,000 merchants including top e-commerce brands, such as Google and Walmart and over 4,000 issuers already participating, we look forward to continuing to scale Ethoca's network.

Now we are also looking for ways to help our partners improve their customers' user experiences. That's why we acquired Vyze, a platform that connects merchants with multiple lenders, opens up a wide range of financing options, including instalments for consumers online and in-store, and complements Mastercard's existing card and ACH-based solutions. While this merchant customers like Home Depot, Microsoft, Samsung, for them multiple lenders help to increase customer financing approval rates, decreased cart abandonment and ultimately therefore increase sales. At the same time, they benefit lenders by providing access to new customers through these channels. And just to be clear, we are not changing our model in taking credit risk, we are merely the platform provider here, connecting retailer and multiple lenders.

Now with respect to our processing services. Pleased that Citibank will be using our Payments Gateway to support digital commerce enablement for their existing institutional clients. Now our gateways connection to numerous acquirers and digital wallets will provide a signal consolidated payments view for these large merchants who have a relationship with Citibank and make it simpler for them to accept payments on a global scale.

And moving onto the work we are going to capture new payment flows, beyond traditional card rails. We have this quarter reached a number of significant milestones in expanding our real-time account-to-account capabilities with our Vocalink assets. First, you must have heard recently that we have been chosen to enhance the Instapay real-time retail payment system in the Philippines. Now this includes operating the infrastructure for and providing anti-money laundering tools to an institutional called BancNet, which is the national clearing switch in the Philippines. We will do this through a regional payments hub in Asia Pacific using leading edge ISO 20022 messaging, which streamlines communications and provides enhanced transaction data.

Second, we are licensing our real-time payment software to the Saudi Arabian Monitoring Authority, SAMA, to upgrade their system, providing similar capabilities to what we already have in place in the United States, Thailand and Singapore. These wins build upon the announcements we made late last year about our partnership in Peru to modernize and operate the Peruvian Electronic Payments infrastructure and we remain involved in a number of similar RFPs around the globe.

So, as you can see, we're making real progress in expanding our geographic footprint for real-time payments in Asia, in the Middle East, and Latin America, while adding value to governments and Central Banks to help their citizens and their economies.

So before I turn the call over to Sachin, I'd like to thank Martina, who's not on this call, who's probably on a beach somewhere for both the years of dedication to Mastercard's growth, but also for ensuring that we were left in good hands upon her retirement with a very well prepared and chosen successor. And now it's my pleasure to introduce Sachin Mehra, our Chief Financial Officer. Sachin?

Sachin Mehra {BIO 20981382 <GO>}

Thanks, Ajay. And good morning, everyone. First, I would like to say that I'm very excited about the opportunity ahead. And I look forward to working with each of you and to meeting those of you I have not met yet.

Turning to page three, we had a solid start to the year. Here are a few highlights on a currency-neutral basis and excluding special items related to certain tax and legal matters. Net revenue grew 13% driven by solid momentum in our core and was slightly ahead of our expectations due to services growth. Operating income grew by 20% and net income was up 21% reflecting our strong operating performance. EPS was $1.78, up 24% year-over-year, with share purchases contributing $0.04 per share. During the quarter, we repurchased $1.8 billion worth of stock and an additional $467 million through April 25 2019.

So now let's turn to page four, where you can see the operational metrics for the first quarter. Just as a reminder, as Warren said, we don't normalize GDP growth rates. Worldwide gross dollar volume or GDV growth was 12% on a local currency basis, down 2 ppt from last quarter, in part due to the impact of the different number of processing days between periods, as well as some other factors such as the delay in the timing of Easter this year. This was much as expected.

US GDV grew 8%, down approximately 2 ppt from last quarter with credit and debit growth of 9% and 6%, respectively. Outside of the US, volume growth was 13%, down 3 ppt from last quarter. Cross-border volume grew at 13% on a local currency basis, in line with expectations and driven by double-digit growth in several regions. This Q1 growth was down sequentially, due primarily to difficult year ago comps.

Turning to page five, switched transactions continued to shows strong growth at 17% globally. We saw healthy growth in switched transactions across all regions, led by Europe and the US. In addition, card growth was 7%. Globally there are 2.5 billion Mastercard and Maestro branded cards issued.

Now let's turn to page six for highlights on a few of the revenue line items. Again, described on a currency-neutral basis unless otherwise noted. The 13% net revenue increase was primarily driven by strong transaction and volume growth, as well as growth in our services offerings, partially offset by rebates and incentives. Looking quickly at the individual revenue line items: Domestic Assessments grew 16%,while worldwide GDV grew 12%. The difference is mainly due topricing and the differing number of processing days between periods, partially offset by mix.Cross-border volume fees grew 15%, while cross-border volume grew 13%. The 2 ppt difference is mainly driven by pricing, partially offset by mix. Transaction processing fees grew 16%, in line with the 17% growth in switched transactions. Finally, other revenues were up 14%, driven by growth in our Cyber and Intelligence and Data and Services solutions.

Moving to page seven. You can see that on a currency-neutral basis and excluding special items total operating expenses increased 5%, primarily related to the company's continued investments in strategic initiatives. This was lower than expected due to the timing of certain marketing initiatives, which we now expect will mostly occur in the second quarter.

Turning to slide eight, let's discuss what we've seen through the first three weeks of April where all of our drivers are up versus what we saw in Q1. Please remember that year-over-year comparisons across all drivers in April our aided by the timing of when Easter fell this year and that three weeks does not make a quarter. The numbers through April 21 are as follows: starting with switched volume, we saw global growth of 18%, an increase of 4 ppt to the first quarter. In the US, our switched volume grew 15%, a sequential increase of 5 PPT with strength in both credit and debit. Switched volume outside the US grew 21%, up 4 ppt from the first quarter, primarily driven by Europe. Globally, switched transaction growth was 20%, a sequential increase of 3 ppt, primarily driven by Europe and the US.

With respect to cross-border, our volumes grew 17% globally a sequential increase of 4 ppt, in part due to the timing of Easter, as well as the tougher year-ago comps we saw in Q1. This was consistent with our expectations. For the year, we continue to expect cross-border volume growth to be about mid-teens and this is what is contemplated in our thoughts for revenue growth for the year.

Turning to our thoughts for the year that I will describe on a currency-neutral basis, excluding special items and acquisitions. I will separately comment on acquisitions in a moment. Overall, not much has changed. We had a solid first quarter and our view on the economy is broadly similar with continued overall growth albeit with some moderation versus 2018.

In terms of net revenue, we continue to expect growth at a low teens rate for the year, with second quarter growth consistent with or slightly better than what we saw in Q1. We expect FX to be a 2 ppt headwind to revenue for the year and about 3 ppt headwind for the quarter. On operating expenses, we are still planning to grow at a high-end of high single digits rate for the year. We expect Q2 operating expenses to grow at approximately twice the annual growth rate due to the lapping of a significant hedging gain a year ago and increased marketing spend. Year-over-year FX will be a tailwind to OpEx of about 1 ppt for both the year and Q2. In terms of the tax rate, we now expect to be closer to the bottom end of the 19% to 20% range for the year. Due to the higher-than-anticipated discrete tax benefits we saw in Q1.

Now moving on to the impact of acquisitions. As Ajay mentioned, we announced a number of acquisitions that either have closed or expected to close this year. We estimate there will be about $0.06 to $0.08 dilutive for the year with the impact starting in Q2 and building progressively throughout the year, driven primarily by purchase accounting and integration related costs. One further item, as a reminder, as of January 2018 certain equity investments are required to be mark-to-market based on observable price movements. We have been following this new standard and it has had a relatively minor impact on our results since inception.

In April, we made investments in two companies as Ajay mentioned, that have since become public. Valuation volatility will therefore increase as a result of the unpredictable nature of public equity markets. Accordingly, starting in Q2, we will be updating our non-GAAP methodology to exclude the impact of fair market value gains and losses on our equity investments. We are excluding these items as we believe this will facilitate a better understanding of our operating performance and provide a more meaningful comparison of our results between periods.

Please note, that our long-term performance objectives and our thoughts for 2019 exclude such gains or losses. We will provide you full visibility to the impact of fair market value gains and losses on our equity investments as we do with the impact of special items and foreign currency, which we will continue to exclude from our non-GAAP measures.

With that, let me turn the call back to Warren to begin the Q&A session.

Warren Kneeshaw {BIO 16549173 <GO>}

Thanks, Sachin. Tasha, we're ready for the question-and-answer session.

Questions And Answers

Operator

Thank you. (Operator Instructions) And our first question comes from the line of Sanjay Sakhrani from KBW. Your line is open.

Q - Sanjay Sakhrani {BIO 7390132 <GO>}

Thank you. Good morning. I guess, I had a question unrelated to some of the stuff you talked about, which was TSB Bank's decision to stick with Visa after committing to you guys. Could you just talk about the observation there? Thanks.

A - Ajay Banga {BIO 4676567 <GO>}

Sure. Hi, Sanjay. TSP is staying with us on credit and it's currently staying with Visa on debit. The reason is very simple. As you know, they had to focus their attention on their technology circumstances when they were doing a migration of their technology platform. And the bank is very focused on getting that done right and looking after their customers and meeting their responsibilities on that front. In the midst of that, to add the migration of a debit book would have added unnecessary risk as well as customer repetitional issues to them and therefore, what they have thought about is, hold on and we'll see later. And I think that's the right thing to do if I was in there place. And I actually respect their decision.

Q - Sanjay Sakhrani {BIO 7390132 <GO>}

Got it. Thank you.

Operator

Our next question comes from the line of Tien-tsin Huang from J.P. Morgan. Your line is open.

Q - Tien-tsin Huang {BIO 6065319 <GO>}

Hey, thanks. Good morning. Can you hear me?

A - Ajay Banga {BIO 4676567 <GO>}

Good morning, Tien [ph].

Q - Tien-tsin Huang {BIO 6065319 <GO>}

Hi. Good morning. Just want to make sure you can hear me. Just maybe a couple of quick ones. Just on the modernizing payment systems in the Philippines, in Peru, and et cetera. Just curious, once you're beyond the build period, what's the run opportunities for Mastercard? Do you become an intermediary? Are you in advantage position to power these intermediaries? Just trying to understand what happens beyond the build phase? And then maybe for Sachin, just the incentives line with so some of the fintech deals like Apple coming in and then TSB as Sanjay asked, any considerations throughout the next two, three quarters?

A - Ajay Banga {BIO 4676567 <GO>}

So Sachin will answer that incentive and then I'll give you the answer later on the Philippines. Go ahead.

A - Sachin Mehra {BIO 20981382 <GO>}

Okay. Hey, Tien-tsin. So on your question as it relates to incentives. Our incentives continue to be very much in line with our expectations. We expect for deal activity to pick up in Q2, but other than that, not much in the nature of changes as it relates to our expectations on incentives.

A - Ajay Banga {BIO 4676567 <GO>}

Hi, Tien-tsin. On the ACH platforms. So what we are trying to do, it depends on what kind of RSP and what kind of deal is constructed. In the Philippines and Peru, the deal is a bit more complete in the form of having infrastructure operation, also included in it. In others, it could be only the software as it is in Saudi, or in the clearing house in the United States or in Singapore's case.

If it's only software, then it becomes a different ability to intervene in the payment flow. So if it's only software, what we're trying to do is to build app which work off that software. But also to build a value added data analytics tools like the anti-money laundering tools and so on, which we have built in other markets and so we can bring them to these countries that has software. Also to provides scheme related thinking around chargebacks, disputes, fraud management, that kind of thing. So that's the software idea, whereas infrastructure, it's little different. It will be a little bit more like the UK in some ways, where we actually run the basic infrastructure and then we can build products and scheme rules on top of that as well.

So I give you the two slightly divergent paths, and it depends on what each country wants for their local instant or fast ACH payment system, as these RFPs sort of open up over the next few years. What I was trying to say today was that, if this has been some time coming, because these RFP processes are slower than the usual. But they get done, and we just -- this quarter there were two, there's others as well. And there is more RFPs in the process that we are deeply in negotiation on.

Q - Tien-tsin Huang {BIO 6065319 <GO>}

Got it. Thank you.

Operator

Our next question comes from the line of David Togut from Evercore ISI. Your line is open.

Q - David Togut {BIO 1496355 <GO>}

Thank you. What impact do you see from the two big mergers just recently announced, Pfizer, First Data and then FIS, Worldpay on Mastercard's growth opportunities. And then, as a related question, both companies or both -- in both merger situations they called out growth opportunities in B2B. I'm curious, how you can work with them in addressing B2B?

A - Ajay Banga {BIO 4676567 <GO>}

Sure, Dave. Look we work very closely with issuer processors in many markets. And especially in the United States, which has the more fragmented payments ecosystem than a number of other markets. And I fully expect to continue to partner with these folks, we've talked to all of them. As you can imagine including me personally. The M&A

doesn't change that, we got teams working with them to determine how best to collaborate to make them win, while also getting our work done. Remember, they play a really important part in the ecosystem for banks and credit unions of all sizes. And mostly they have to distribute our products and services.

And so, I kind of feel like there's lots of opportunity ahead, both in the consumer payments side, but also in the B2B side. But it's just too early to demand any of them down. They're both very busy with their own transactions, as you can imagine. And they need to get that done well, because that's their first commitment. And then we can really get deeply involved in what else we can do together with the merged entity.

Meanwhile, individual [ph] partnerships with the separate entities continue, okay. Just to be clear. The merged entities will have a whole new game, so the merger got to finish before you can do that.

Q - David Togut {BIO 1496355 <GO>}

Thank you.

Operator

Our next question comes from the line of Bob Napoli from William Blair. Your line is open.

Q - Robert Napoli {BIO 1526298 <GO>}

Thank you, and good morning. I mean, Mastercard has been very active on the M&A front. And I was just hoping, Ajay, to get a little more clarity on additional potential areas that you're looking to build up through the M&A. And is there still a very healthy pipeline? Maybe an update on the strategy, the M&A strategy and pipeline?

A - Ajay Banga {BIO 4676567 <GO>}

Yeah. I mean, I mean I think Sachin's sort of baptism by fire on this is the fact that in his first quarter we delivered a couple of extra everyday deals to him, just to keep him happy and make him realize that he needs to do a little bit of work. It won't be an easy thing to follow with Martina's somewhat large shoes. So I hope she is not listening for God sake. But the -- your questions is a much deeper one. Here is the deal, we have not changed our M&A strategy over the years and I've been talking about this. We are trying to use both organic and inorganic ways to grow in the spaces that we think give us possible growth areas for the next decade or two. Hence, safety and security, hence, data analytics and information systems, hence, digital identity systems, hence B2B and cross-border payments. All of these AI, all of these are intertwined in the idea of building out new capabilities and new services. More or less pretty neatly placed in the third block of our strategy, which is in the grow, diversify, build, most of these are in the build space.

And that's how we've built these services organically and inorganically to now 26%, 27% of our revenue. That's the objective. At the same time, I'm also trying to build the capability to be available and present across all rails of payment. Not just card, but also non-card rails, and hence the Vocalink acquisition and the acquisitions that are going on in B2B spaces to deliver sort of usage results again those. So that's what's going on, nothing is changed in that, you will find us active participants in these spaces, in loyalty and rewards, and those kinds of spaces over the next few periods as well. We have a relatively active pipeline. I mean, Sachin could tell you that his team has -- I don't know, Sachin, during the year '20 to '30 such deals?

A - Sachin Mehra {BIO 20981382 <GO>}

Yeah, that will be correct. 20 to 30 such deals, which would be actively due diligence.

Q - Robert Napoli {BIO 1526298 <GO>}

Okay.

A - Sachin Mehra {BIO 20981382 <GO>}

The list of deals we would actually scope out will be much broader than that. And just to reiterate what Ajay said, it all kind of starts with the strategy and then we kind of figure out from there on, what's the best way to achieve the strategy between build, buy and partner. And so the M&A component is one big piece of that, but not the only one.

A - Ajay Banga {BIO 4676567 <GO>}

Some of these deals, actually, a number of them emanate from us partnering with these people on a commercial deal first, Transfast is an example of that recently. But this has been the case in the past as well, with a number of the transactions we have done, we end up like Brighterion, we ended up being a constructive partner there, having a commercial relationship and then it changes over time into the possibility of an acquisition. So we are trying to use the mix of these, I would say, the acquisition as well as minority stakes, as well as in the case of Fintech's and start-ups a series of early investments as a way of making the company has a layer of its business exposed to all that's new and exciting, which we don't believe we have a full always 100% right to be the only one thinking of new ideas. And so this is a good way to get external thinking, external quality of people, get external -- maybe some product quality or some distribution strength that we may not have. So Ethoca, for example, has both product and software, but also distribution to 4,000, 5,000 merchants, and 4,000 issuers whom they are tied up with. Transfast has compliance capabilities, FX capabilities, but also distribution in a number of countries and licenses to operate in a number of those countries.

So different things come together in how we make the transaction, but the pipeline is robust. And if we can do one or two transactions a year out of the 20 or 30 we look at, that will be a good year. It just happened that in this quarter a couple of extra ones came through.

Q - Robert Napoli {BIO 1526298 <GO>}

Great, thank you. I appreciate the answer.

Operator

Our next question comes from the line of Tom McCrohan from Mizuho. Your line is open.

Q - Tom McCrohan {BIO 5827846 <GO>}

Hi guys. Can you remind us how much of your cross-border volume occurs in the first quarter. I think there is some seasonality. Just wanted to confirm that? Thanks.

A - Sachin Mehra {BIO 20981382 <GO>}

Tom, I just want to make sure I heard the question correctly? How much of our cross-border volume? What was your question?

Q - Tom McCrohan {BIO 5827846 <GO>}

Yeah. Occurs in the first quarter. I think you has -- I think there is one of the weaker quarters? Just want to confirm the seasonality.

A - Sachin Mehra {BIO 20981382 <GO>}

Yeah. From a seasonality standpoint, what I tell you is, Q3 typically sees a little bit more in the nature of volume on cross-border, but for the most part in the remaining quarters it's pretty stable.

Q - Tom McCrohan {BIO 5827846 <GO>}

Great. Thank you very much.

Operator

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

Q - Ramsey El-Assal {BIO 17528014 <GO>}

I had a two-part question on some regulatory items. First is on the secure customer authentication rules coming out later in Europe this year. Whether you think that will be any type of -- constitute any type of pressure on European volumes later on in the year? And then second is a more broader question about data localization requirements and having to build out redundant processing capabilities in different national jurisdictions. Over time whether that also constitutes anything like a headwind to operating leverage or any type of incremental pressure? If you can comment on those two things. I appreciate it.

A - Ajay Banga {BIO 4676567 <GO>}

Sure. So, the secure authentication rules, as you can imagine, we've been kind of looking at the entire PSD2 implications for both us, merchants and banks in the system, as well as the new entrants PISPs and AISPs who are entering into the European payment system. I actually think that secure customer authentication is an opportunity for a company like ours that has the capability, skills and tools set to provide this for all the players there. Merchants will need it, banks will need it, these new PISPs and AISPs will need to connect properly into the system to ensure that the entire payments ecosystem is kept safe and secure.

So for us, I see this actually as an opportunity to deliver new value-added services. And in past meetings we've talked about how that's one of the planks of what we are building out as part of our PSD2 strategy. I'm sure other networks are too, this is not a -- this is not about trying to be competitively advantaged. This is about trying to do the right thing for the payments ecosystem.

The second part, the part about data localization, that's an interesting question. It came up a couple of earnings calls ago as well. It's mostly right time to do with India in that case. And I'd say around the world, in some cases data localization like in India has got real policy ratifications. I others, countries that they engage with us realize that data localization may not be to their benefit. And let me explain that for a second first. The challenge for data localization is actually not the expense, which is what your question comes from. Because that's just a question of putting up some more servers and storing the data on, so on. And to be honest with you, in an expense base of our type, putting a few more servers on soil in a country even as larger as India with the volumes of in India is interesting, but not really the big deal.

The bigger deal is the fact that by doing so you end up with data that loses its predictive power compared to the wealth of data that generates much higher predictive power when it's combined across many more countries, many more types of transactions, many more types of consumers, many more types of customers. If you talk to anybody in the space of AI or machine learning or good old-fashioned data analytics, you will find that they will tell you that the more the data, the more varieties of data, the more widespread and ubiquitous data you get the better the predictive power. The moment countries balkanize that data they may say they're doing it for security reasons, it is not completely clear to me that in actual fact it give them better security on predicting for fraud and anti-money laundering and capabilities on that front than data which is more widely shared.

Now we will comply and they have complied in India and we will comply elsewhere, but whatever rules a country finally chooses, because we operate there, because that's what the rules are. But it's our job to try and educate them to what we think and it's their job to decide what's right for them and then we do what we got to do after that. So that's what we got in India, we comply. In other countries we've managed to turn back that thinking based on this logic that I gave you.

Q - Ramsey El-Assal {BIO 17528014 <GO>}

Thanks so much.

Operator

Our next question comes from the line of Bryan Keane from Deutsche Bank. Your line is open.

Q - Bryan Keane {BIO 1889860 <GO>}

Hi, guys. Just wanted to ask about the higher expenses expected in Q2. It sounds like most of that is going to be marketing spend, maybe some of that is from acquisitions. Just trying to understand, maybe where the higher expenses are going, especially on the marketing side, anything in particular? And then secondly, just on the strong data so far through April 21. Is there a way to think about how much of that is from Easter versus easier comps versus better economy, share gains, et cetera? Thanks.

A - Ajay Banga {BIO 4676567 <GO>}

Yeah. Bryan, let me make sure I'm clarifying the Q2 comment over here, which is, we are expecting double the growth rate relative to our full year thoughts on OpEx in Q2. And that growth rate differential is being driven, as I mentioned in my prepared remarks by the fact that, last year in our operating expenses we had the benefit of a fairly sizable FX hedging gain. So I think you need to take that into consideration as you think about the marketing expenses for -- or rather the operating expenses for Q2. In addition to that, we also expect for increased marketing spend in Q2. As I mentioned in Q1, our marketing expenses came in lower than expected. This is just part of what goes on as we run our business. We kind of make evaluations as it relates to when is the optimal time for us to put marketing out in relation to various sponsorship assets and other initiatives, which we've got going on. And this is just par for the course as part of that process. So nothing unusual that I would flag.

On your second question on April 21 data. I will tell you, look, I mean April 21 data is impacted by the timing of Easter and I think you need to take that into consideration. Just especially given the fact that this 21 days worth of data which we're presenting to you and -- three weeks is not going to make the quarter. So, I would tell you that, by and large the growth trends look solid as we've mentioned for Q1 and we continue to see that going forward as well, but timing of Easter plays a big part in terms of what we're seeing in our April 21 metrics.

Q - Bryan Keane {BIO 1889860 <GO>}

Okay, great. Thank you, guys.

Operator

Our next question comes from the line of Craig Maurer from Autonomous Research. Your line is open.

Q - Craig Maurer {BIO 4162139 <GO>}

Yeah. Hi, thanks. Two questions. One, have you seen any uptick in local network competition anywhere around the world? And secondly, the settlement with the European Commission that you seemingly announced yesterday on inter-regional cross-border. Obviously, that will have an effect on the fee income of banks issuing cards that are being used in Europe. So thinking Citi for you guys. Do you -- can you foresee an impact on the rewards that those banks are offering on those cards for cross-border business, if you're going to see a significant reduction in that fee income? Thanks.

A - Ajay Banga {BIO 4676567 <GO>}

Sure. So, Craig. First, the second one. That settlement with the European Commision as you know, we kind of discussed it in the fourth quarter earnings call. I've Tim Murphy, my GC sitting here. He is dying to answer that question, but maybe you could -- was it in Q2, Tim?

Q - Tim Murphy {BIO 15846989 <GO>}

Yes, Ajay. So we briefed investors in December of last year and there is really no change following what we shared in December, it's just a process update. So that's what you've seen since December, nothing new.

A - Ajay Banga {BIO 4676567 <GO>}

Big part of our (inaudible) impact, the rewards that different banks offer, not just Citi, but this is for all banks that would have people traveling into European union territory. It impacts anybody, Australians and Chinese and Americans and everybody else (inaudible). So the fact that it's a relatively small proportion of the total interchange revenue that most of these banks generate. It's also a relatively small proportion of the total revenue, which comes out of not just interchange, but revolving and other fees and therefore, it is not my assessment that there will be that big an impact on the P&L, no. Remember that the reduced rates of 20 and 30 apply to physical card present, whereas for card-not-present e-commerce transactions the rate for debit are 115 basis points and the rate for credit is 150 basis points. And so that's factored into the commentary I'm giving you about the impact for banking institutions. It's not that it's not relevant, it's relevant. It just that it's not enough to, I think, their marketing practices directly in this form.

Your question about local networks. I haven't seen an uptick or downtick in any relevant strong way over the last six months to a year. Local networks have been strong across the world in different forms over the years. I mean, the EU -- every country in the EU has had a local networks since well before, I mean, since 20, 25 years ago. Mexico has had them, Canada has had them, Brazil and Colombia and Argentina used to have them. China has had it since a long time, Korea has had them. It's not one kind of example here, in fact, if you look at the number of our transactions, if you actually passed through our own rails of the total, today at 56% of our transactions. 10 years back when I joined, it was 40 something percent. So even 10 years ago the majority of our transactions were being taken by local networks in some form for the actual processing of that transaction. We in other ways to raise revenue from the activity around that transaction, but the processing was going through local rails very often. Now actually that number has reduced over the years as they've made inroads in a number of market places.

Q - Craig Maurer {BIO 4162139 <GO>}

Thank you.

Operator

Our next question comes from the line of Lisa Ellis from MoffettNathanson. Your line is open.

Q - Lisa Ellis {BIO 18884048 <GO>}

Hi. Good morning, guys. And welcome Sachin to the call. Couple from me. First, Ajay, can you comment on China and specifically the news reports about potential joint venture announcement with Nets Union there? And then second one is related to the Vyze acquisition and around doing enabling extension of credit trends actually at the point of sale. Just from a vision perspective, can you comment as you look out about building this out, this capability out with Mastercard over the next few years? What that's going to look like, or how should we be thinking about it? Is it almost like another rail and what's Mastercard's role in differentiation exactly there? Thank you.

A - Ajay Banga {BIO 4676567 <GO>}

Okay. So, China, I'm not going to comment on a newspaper article. I mean, I wish I was asked for comments in the newspaper articles that give me blood pressure, but nobody does. This one doesn't really give blood pressure, it just what somebody wrote based on what they picked up locally. We are -- this much I will tell you, I'm very committed to finding an appropriate and sensible way to enter the domestic Chinese market and I'm making every effort possible across the company to get to the right place and getting the requisite licenses to be able to do that. And I think as soon as we've got something substantial or real to tell you, we will, trust me. We just don't have anything real or substantial today, because this movie hasn't played out yet.

So it's going to take some time to play out. And even after it plays out in terms of, let's say, we do get some form of an approval even after that, there's a year long process of national security clearance before you can actually start operating domestically on the ground in China. So this is like a couple of years away at least before we can give you something that's more interesting than just desires. Right. That's the first.

On Vyze, Vyze to me is interesting. I don't yet know how well to answer that question for you, because I don't yet know how big this could be. Installment lending to me is a really interesting aspect, installment lending at the point of sale. Installment lending through a bank has been going on for a long time, but the idea of allowing a consumer at the point to sale to opt into an installment loan in some ways it's been going on for a long time in sales finance businesses in places like Brazil where ever since by years -- years back at Citibank, we used to see this happening where the transaction at the point of sale had a automatic installment plan built into what was the card payment that is being used by a consumer. That's kind of -- it didn't spread everywhere, it's spread in different ways into the US in the consumer finance business mostly, it didn't really spread to the middle class or the upper class there. But it's spreading around the world in some ways. In Australia there were a couple of players who have launched installment lending. In the US those players have -- one or two of them are coming here, others locally are doing this. It's bank's, it's Fintech's, it's merchants, everyone seems to be interested in this space, but I don't know yet how to tell you how big it could be or where it could go, because I don't really know yet how well it will catch on with the consumer.

We are certainly putting our foot in the water with this acquisition. Remember, it's not us extending the credit, we are just creating the platform between the merchant and the institution -- the bank or the Fintech which may in turn pass the loan on to a bank, that's what we are really doing. I think I can add a lot of differentiated value in the form of AI, in the form of better tools to identify consumers and help to -- help people underwrite. There is a lot of things we could do with our data analytics and our information services business. Remember that we could also do a lot of things with loyalty and rewards, which could be connected over time into the instalment loan system. So I don't yet know where this will go. It's interesting. I've got my foot on the water and we'll see, it's not different from the way we entered other services four, five years ago, put our foot in the water before we took the full-fledged.

Q - Lisa Ellis {BIO 18884048 <GO>}

Perfect. Thank you. Well, you know, it's a good quarter when Ajay has to answer all the questions. Thanks, guys.

A - Ajay Banga {BIO 4676567 <GO>}

Although, I'm trying to give -- I gave (inaudible)

Operator

Our next question comes from the line of Eric Wasserstrom from UBS. Your line is open.

Q - Eric Wasserstrom {BIO 3626772 <GO>}

Thanks. If -- I was wondering maybe, Sachin, could you help remind us about sort of all of the components that attribute to your strength in cross-border. I think you have some portfolio wins that should be helping year-over-year, some Maestro conversions. Can you just remind us of all the factors that support that figure?

A - Sachin Mehra {BIO 20981382 <GO>}

Sure. Look, I mean, as a company we remain incredibly focused on cross-border drivers. And as we've said in previous earnings calls, Mastercard had set up the center of excellence within Mastercard, where basically there is a tremendous focus on how we can do good knowledge sharing across the company on what can drive cross-border volumes for this company. Really it all kind of starts with making sure that we have actually truly identified what are the right portfolio to go after from a cross-border standpoint. As we sit back and think about it, we leverage our services business with the data analytics capabilities to identify what are the right portfolio to go after. And those are the ones where there's a larger propensity of cross-border. Thereafter, we go after trying to optimize those portfolios in the best way possible. So to the extent we identify portfolios of our customers, which might be underperforming, we work with them through our consulting practice and our managed services practice in our advisors business to try and actually drive for better and more optimized cross-border focus there. But even beyond that, it's about focusing on the right vertical. So for example, in the wholesale travel space, this is an area where Mastercard has been historically very much focused and has been actually a leader and that contributes to cross-border.

And then finally I would say on a similar basis, if you think about digital banks and things of that sort, these would be areas where we would focus. Again, going back to the theme of what are the right portfolio to go after and how do you optimize those. That's really what we're doing and it sounds like basic blocking and tackling, but sometimes you actually really have to go down that path to actually make it come through and that's what we're doing.

A - Ajay Banga {BIO 4676567 <GO>}

And, Eric, as I said last time, there's -- I'm sure that other networks (inaudible) this is not rocket science, it's just -- it's in the execution and it's in getting it done. And, yes, Maestro to Mastercard conversions do give us some tailwind, because clearly Maestro utilization in e-commerce is challenging. Mastercard debit allows the better utilization and that will continue for a while, because we haven't completed those migrations in every location that we'd like to.

Q - Eric Wasserstrom {BIO 3626772 <GO>}

Great. And if I can just follow-up. Ajay, any update on the B2B hub. I know that you launched it in Australia, I think a quarter ago. And any update on its international or domestic advancement?

A - Ajay Banga {BIO 4676567 <GO>}

No, not really that -- in fact we discussed it in the last quarter call. Yes, you're right, it's physical launch is actually happening as we speak. And it's very early days, but that's one we are focused on. The whole B2B space has opportunity. The hubs, one way of getting into it, as you know the directory and track in enabling that directory to be fully built out the right way across the world as another one. Payments optimization engines are getting built into it, we are just doing a series of things and hopefully Transfast will enable and help us even more. Meanwhile, Send continues to chug along. that's why I talk more Bank of Montreal, and what it's trying to do with Send. It's doing it for its commercial and business banking clients as well. So there is a series of tools that are being played in the B2B space.

Q - Eric Wasserstrom {BIO 3626772 <GO>}

Thanks very much.

Operator

Our next question comes from the line of Don Fandetti from Wells Fargo. Your line is open.

Q - Donald Fandetti {BIO 6095992 <GO>}

Yes. Ajay, two-part question. I guess in the US Marstercard's had a pretty good track record on these program wins, but it's been a while since we've seen any kind of major sort of bank portfolio flip. Do you expect to see any market share change over the next year or two there? And then separately, any update on the Commonpay button from e-commerce that the industry had some time to digest it. How are you guys feeling about the penetration opportunity?

A - Ajay Banga {BIO 4676567 <GO>}

So on the first one, big bank portfolios. There have been some over the last year or two that we've talked about and we have won on from pass with Capital One to pass with Bank of America and the like. And those are still helping us grow share. In fact, if you look at the way our credit numbers are growing in the US, part of that is co-brands, that's Cabela's and Kroger and the like, but part of it is also these banks portfolios that have been switching over to us. I don't see any huge swings in bank books moving around right now. But they are actively in every transition and every transaction that happens. But I don't see huge runs moving around as we speak, as of now.

On the SRC progress, we are looking, as I said, the industry to launch this in the second half of 2019. It's probably going to end up first in the US, and then get to additional markets over the next six to 18 months. I think, you'll find the feedback we're getting from issuers and merchants is very constructive to EMVCo. We are trying to adapt to that feedback and get it rolled out all the technology build and branding work is happening as we speak. And I still remain pretty optimistic about what SRC could do for the industry and for the consumer and for merchant and the issuers simpler connect to one connection for all brands, easier to manage for the consumer, kind of trying to replicate the physical experience of one terminal to convert that to a physical -- to a digital experience of one button kind of idea, that's what we're trying to get.

Operator

Our next question comes from the line of Darrin Peller from Wolfe Research. Your line is open.

Q - Darrin Peller {BIO 16385359 <GO>}

Hey. Thanks, guys. You know, look, you had a -- I think you had a 200 basis points tough compare in the quarter, and then with FX it looks like you clearly outperformed this quarter growing around 13% constant currency. So first, just what drove the surprise to the upside versus what it -- I think you initially thought, when you talked about your guidance from last quarter for the first quarter trends. And then do you think that the soft spot we saw in cross-border, whether it's fourth quarter or perhaps early first quarter was more of an anomaly at this point. Do you feel better about the trends you're seeing? Thanks, guys.

A - Sachin Mehra {BIO 20981382 <GO>}

Yeah. So, Darren, I'll take that question. So as it relates to the first quarter, like I mentioned in my prepared remarks, we've slightly exceeded what our expectations were as it relates to our performance from a revenue standpoint, driven by the strength in our services business. So we also saw on an FX standpoint, slightly lower impact on FX in the first quarter relative to what we originally thought. So those were a couple of factors which you might want to kind of take into consideration as you're thinking about it. On your other question for cross-border. You've got to remember that cross-border last year in Q1, we had a 20% growth rate in cross-border. And those tough comps are a large part of what we're seeing in terms of the results in Q1 of this year.

You'll remember, when we talked about cross-border performance last year, we actually were fairly explicit about saying that, we don't expect our normal run rates to be like what we saw in the first half of last year. So as you think about our business, we continue to believe that our cross-border is trending and performing as we would normally see it, actually performing. So I wouldn't make too much of swings between quarters, because we are always doing comparisons between year-over-year tough comps.

Our business continues to grow well. We like what we see in terms of our portfolio. Just a little bit more color, if it's helpful from a cross-border standpoint. The US outbound volumes continue to hold up pretty nicely and our China business from a cross-border standpoint continues to grow also in the high single digits, much like we've seen historically. So all-in-all business carries on as we expected to be.

A - Warren Kneeshaw {BIO 16549173 <GO>}

Thanks, Sachin. Ajay do you have any final comments?

A - Ajay Banga {BIO 4676567 <GO>}

Thank you all for your questions. And I'm going to wrap up with a few closing thoughts. First, we had a solid start to the year, reflecting the strong operational focus, execution focus, and continued growth across each of our regions. And we are executing against a strategy with a couple of particularly [ph] noteworthy milestone this quarter. The first one being the progress in extending our real-time payments capabilities in Asia and Latin America and in the Middle East. And secondly, we announced these strategic acquisitions and partnerships that we think will complement our existing products and services and position the company well for the next decade or two of growth as well.

So with that, I'd like to thank you for your continued support for the company and for joining us today.

Operator

This concludes today's conference. You may now disconnect.