Visa Inc (V) CEO Discusses F3Q 2013 Results - Earnings Call Transcript

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Jack Carsky - Head, Global Investor Relations

Charlie Scharf - Chief Executive Officer

Byron Pollitt - Chief Financial Officer

Analysts

Andrew Jeffrey - SunTrust

Dan Perlin - RBC

Don Fandetti - Citigroup

Chris Brendler - Stifel

Tien-Tsin Huang - JPMorgan

Glenn Greene - Oppenheimer

Craig Maurer - CLSA

Tom McCrohan - Janney

Moshe Katri - Cowen

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Rod Bourgeois - Bernstein

Dave Koning - Baird

James Friedman - Susquehanna

Darrin Peller - Barclays

Visa Inc (V) F3Q 2013 Results Earnings Call July 24, 2013 5:00 PM ET

Operator

Welcome to Visa Incorporated Fiscal Q3 2013 Earnings Conference Call. All participants are in a listen-only mode until the question-and-answer session. Today's conference is being recorded. If you have any objections, you may disconnect at this time.

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

Jack Carsky

Thanks Brad. Good afternoon. And welcome to Visa Inc.'s fiscal third quarter 2013 earnings conference call. With us today are Charlie Scharf, Visa's Chief Executive Officer; and Byron Pollitt, Visa's Chief Financial Officer.

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

Let me also remind you that this presentation may include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. By their nature, forward-looking statements are not guarantees of future performance, and as a result of a variety of factors, actual results could differ materially from such statements. Additional information concerning those factors is available on the Company's filings with the SEC which can be accessed through the SEC's website and the Investor Relations section of the Visa website.

For historical non-GAAP or pro forma related financial information disclosed in this call, related GAAP measures and other information required by Regulation G of the SEC are available in the Financial and Statistical Summary accompanying our fiscal third quarter press release. This release can also be accessed through the Investor Relation section of our website.

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

Byron Pollitt

Thank you, Jack. Let me begin with my usual call outs and observations. First, some color on the third quarter's 17% net revenue growth. It is important to note that this growth rate benefited from the absence of significant one time client incentives incurred in the prior year. without these one time client incentives, revenue growth for Q3 would have been closer to 14%. That said, payment volume growth was broad based globally for the March quarter and we're seeing double-digit growth rates in the June quarter for both credit and debit on a constant dollar basis. Based on these trends, and with three quarters of the fiscal year now on the books, we are raising full year 2013 revenue guidance from to low double-digits to around 13%.

Second, service revenue, though up 7% on year-over-year basis, it was down sequentially from the fiscal second quarter. This was primarily due to the signing of the 10 year Chase deal which was executed in fiscal Q3 but was retroactive to the beginning of Q2. This contract, as discussed on the Q2 earnings call, disproportionately impacted the service revenue line and resulted in offsetting reductions in gross service revenue and related client incentives. Because it was signed in fiscal Q3, the service revenue impacts for both Q2 and Q3 were recorded in the current quarter. This means that Q4 service revenue growth rate should be a more representative indicator of underling growth.

Third, client incentives for the quarter, as a percentage of gross revenue, were 14.8%. As described previously, two quarters of Chase related incentive reductions were booked in Q3. This impact was constant inflation in our most recent full year guidance and we remain comfortable with client incentives as a percent of gross revenue in the 16% to 17% range for the full-year 2013.

Fourth, now that we have fully left implementation of the Dodd-Frank routing rules, beginning in June, quarterly Interlink payment volume growth has turned positive for the first time in over a year. Going forward as we lapse a period during which Visa's post Dodd-Frank debit strategies took hold, we would expect healthy but moderating revenue growth rates for U.S. debit.

Fifth, given our earnings result year-to-date and our expectations for the fiscal fourth quarter, we are increasing our fiscal 2013 adjusted EPS guidance from around 20% to the low 20s. Lastly, as we remain commitment to returning excess cash to our shareholders, during the quarter we've spent approximately $1 billion to repurchase 6 million shares at an average price of approximately $177.00. this leaves $61 million remaining in our prior authorization. And as we announced earlier, our Board recently authorized a new $1.5 billion share repurchase program which will run through July of 2014.

Now, let's turn to the numbers. As is our practice I will cover our global payment volume and process transaction trends for the fiscal third quarter, followed by our results through July 21st. I'll then cover the financial highlights of our fiscal third quarter and conclude with our guidance outlook for the balance of fiscal 2013 and fiscal 2014.

Global payment volume growth for the June quarter, in constant dollars was 18%. Payment volume growth for the June quarter incomes in dollars was 13% above the March quarter's 9%. This was driven by sustained growth in all of our regions including the U.S. which saw some incremental benefit from the lasting effects associated with U.S. debit regulations.

More recently, in the U.S., through July 21, payment volume growth was 10% compared with 11% in the June ending quarter. Drilling down further, U.S. credit growth of 10% held at Q3 levels while debit, which also grew at 10% experienced a healthy but moderating growth rate as we lap the growing impact of the Visa's U.S. debit strategies.

Global cross-border volume delivered a solid 11% constant dollar growth rate in the June quarter which compares to a 10% rate in the March quarter. The U.S. grew 9% and the rest of world 12%. Through July 21, cross-border volume on a constant dollar basis grew 7% with the U.S. growth rate of 9% and the rest of world at 6%.

The slowing growth in July is most pronounced outside the U.S. and we believe is due in large part to the timing of Ramadan versus last year. Based on historical travel patterns, we estimate the Ramadan impact to be in the 250 to 300 basis points range for the month and if pass this prologue, we should see a bounce back in August.

Transactions processed over Visa's network totaled $15 billion in the fiscal third quarter, a 14% increase over the prior year period. The U.S. grew 12% while the rest of world delivered 23% growth. We have now fully lapped the negative impacts associated with U.S. debit regulation. Through July 21, process transaction growth was a positive 14%.

Lastly, please note that in our operational performance data pack, that was released with today's earnings results, we updated the cash volume in our LAC region to account for several quarters of underreporting by one of our largest issuers in Brazil. As a reminder, these cash volumes have no impact to our revenue.

Now, turning to the income statement. Net operating revenue in the quarter was $3 billion, a 17% increase year-over-year driven by solid growth globally in both domestic and international transactions and as mentioned earlier, aided by significant non-recurring incentives in the prior-year quarter. Currency hedging resulted in only a modest foreign exchange headwind on net revenue in the quarter. Looking ahead, after factoring in our hedging program, we anticipate continued headwinds in the next fiscal quarter and for fiscal 2014.

Moving to the individual revenue line items, service revenue was $1.3 billion, up 7% over the prior-year period. On a sequential basis, growth was negatively impacted by the Chase agreement which as I previously outlined, resulted in lower service revenue offset by a lower level of incentives paid to Chase.

Data processing revenue was $1.2 billion, up 15% over the prior year's quarter based on solid growth rates in Visa, process transactions inside and outside the U.S. and strong cyber storage transaction growth. With the full lapping of the implementation of U.S. Debit Regulation, data processing revenue growth is now relatively on par with process transaction growth.

International transaction revenue was up 14% to $854 million reflecting solid strength in cross-border volume and some modest benefit from higher currency volatility. As I highlighted earlier, client incentives as a percentage of gross revenue for the quarter came in at 14.8%, positively impacted by the Chase deal.

That said, we anticipate a meaningful step-up in both incentive dollars and the percentage rate in Q4 due to anticipated deal activity both domestic and international which should put us within our 2013 guidance range of 16% to 17%.

Total operating expenses for the quarter were $1.2 billion, up 9% from the prior year adjusted results. This was primarily due to higher costs associated with investments in our growth strategy.

Marketing expenses were up 4% from the prior year and stepped up from the prior quarter as we increased marketing to support a number of sponsorship campaigns including the 2013 FIFA Confederations Cup in South America and the 2014 Sochi Winter Olympics.

Operating margin for the quarter was 61% and is consistent with our current guidance. Our effective tax rate for Q3 was 33.2% while higher than our full year guidance of 30% to 32%, the year-to-date figure of 31% is tracking to that range.

Net income at $1.2 billion was up 16% over the prior year adjusted results. Fully diluted EPS was $1.88 for the quarter, up 20% over prior year adjusted results. Stronger than anticipated revenue and more aggressive share repurchases were key drivers and as noted earlier our full year adjusted EPS guidance is now low 20s.

Capital expenditures $122 million in the quarter and continue to be in line with our full-year expectations. At the end of the June quarter, we had 645 million shares of Class A common stock outstanding on a S converted basis. The weighted average number of fully diluted shares outstanding for the June quarter totaled 651 million.

Finally, in terms of guidance, other than our refinement of full-year 2013 revenue guidance to around 13%, and adjusted diluted earnings per share growth to the low 20s, all other outstanding guidance metrics for the full-year fiscal 2013 and 2014 remain the same.

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

Charlie Scharf

Thank you, Byron, and good afternoon everyone. First of all, I just want to reiterate that we feel very good about our performance this quarter. There is very little new news in the underlining revenue trends as Byron has just described, which means that we continue to see broad based growth geographically and also by product. And these are at growth rates consistent with what we've seen in prior quarters.

People often ask us about what we see in the economy and what I guess we can say is we don't see meaningful changes to the path of the economic recovery. And while accelerating and certainly a more broad based recovery would be beneficial to us and our clients, we do continue to feel very good about our business and our ability to deliver strong results in the current economic environment.

We did host our Investor Day on June 6th and I want to thank all those who attended both physically and listened in. we know it was a lengthy call but hopefully you found it productive. We certainly appreciate all the feedback that we received. Just a couple of quick reminders of some of these important themes that we covered.

First of all, you know, we feel great about the strong foundation that this company has been built on. There has been strong historical growth. We have great partners and the company has a tradition of innovation. Second, the macro trends have and will continue to provide tailwinds. The opportunity to move transactions from cash to electronic means is still huge. And we believe we'll be there for years to come. This is true in both the developed and the developing parts of the world. As you pointed out on Investor Day, we have 22% share TCE in the emerging, I'm sorry, within the developed markets and 9% in the emerging markets. So there is still much room to grow. In addition to us growing along with the growth of TCE across the world.

We love our core network. It's served us well and think it provides us tremendous opportunities to leverage and grow our business. Historically, what's really benefited us has been the global acceptance, the network reliability, safe and security and soundness, and our risk related tools are just a huge value added component to the network. While we continue to build on these historical strengths as we pointed out at the Investor Day, the future for us will be about using the network is a tool, to continue to create more value for issuers, acquires and merchants, and that include us building broader capabilities but also giving them access, it's our network as a device that connects to them together.

Third, the company has and continued to make huge investments in the future. We walk through some of the additional spending that's been done to the tune of an additional $700 million versus prior years, which are for the most part all geared towards growth opportunities.

And lastly, we talk about our evolving rules and practices, recognizing how the payments world is evolving. We recognize the needs to evolve our company. But we also feel strongly that we need to continue to preserve some core principles, those include the importance of the Visa brand, the safety, security and soundness of the payment system that we continue to protect and control our intellectual property, and that we enable clients of all sizes to compete. So in short, these of things that while we think we can continue to do more and more for all of our clients we think these things could also add value to the Visa network.

We turn now to little bit of an update on some of the regulatory and litigation items that are both been in the news and we've spoken about. First of all in the United States on the MDL case. The deadline for the opt outs was May 28th. As expected I am sure you show lawsuits that were filed against Visa, MasterCard and in some cases the banks from retailers which opted out of the merchant settlement agreement last year.

The final figures are still being calculated but our estimate of the opt out is that they represent slightly above 25% of our U.S. credit volume. We continue to expect approval from a core sometime in the fall.

I do want to stress that these are proceedings that have been on going for a long period of time. We remain committed to figuring out how to work with merchants of all sizes to resolve all of our differences amicably and we as you heard from us we are focused on finding new ways to work with them in conjunction with acquires and issuers to support all of the individual constituents growth objectives.

Secondly, Canada, yesterday Canada's competition tribunal issue this decision to dismiss the competition bureau's case and uphold our no surcharge and Honour All Cards rule. We have and we'll continue to engage with legislators and regulators around the world to promote the understanding of a value of electronic payments to consumers, merchant and governments broadly.

Let me now turn to Europe, and as a reminder, Visa Inc. and Visa Europe are separate independent operating companies. First of all, let me talk about, in May we alerted you to a European Commission inquiry by the Director of General Competition related to inter-regional credit interchange rates.

That investigation specifically relates to the interchange applied to transactions between a non-European Union cardholder and the merchant located within the European Union. We continue to assess their claims and we are working in a productive and professional manager with them and hope to reach resolution but there is nothing more to report at this time.

Separately, the European Commission earlier today released proposed legislation for the payments industry in the European Union which had been expected. The proposed regulation covers a wide range of topics related to the European payments industry including domestic and intra-EU cross-border interchange rates, [co-batching] requirements, process requirements and point-of-sale rules such as Honour All Cards.

Most recent announcement submission appears to address issues similar to the Commission competition case, but the propose regulation would only applied to transactions when the issuer and an acquirer are located in the European Union.

We understand that proposed legislation is to beginning of what we expect could be a long process which could take 18 to 24 months. We'll continue to keep you updated if we learn of any more developments in either these two proceedings.

Also in Europe, I'm sure we would get a question about the Visa Europe put and there is no update on that.

Let me move now and just talk for a second about a topic which has lot of you are writing about and has gotten a lot of press and that's tokenization. And to start with, stating the obvious which is we all know that transactions are increasingly moving to digital card, not present channels due to the growth of web commerce, mobile and digital wallet.

As you've heard from us in the past we've been building our capabilities to deal with transactions like this both technically and through our rules and requirements, V.net and CyberSource are just two examples where we've made significant investments to build capabilities in this space. And as we talk about tokenization I do want to just make a point that tokenization is not a new concept to us. Historically, we define the 16-digit account number [method] set and we effectively operate as tokens in the payment system today.

The reality is the development of digital commerce and related risks makes the evolution of these existing tokens -- the evolution of these existing tokens to a more secure form very necessary in a way that works both in the physical and the digital worlds. We need to eliminate the flow of sensitive data that might be vulnerable to a breach and new entrance into the payment ecosystem has also brought into question whether the appropriate information will continue to flow between merchant, acquirer, issuer and consumer. And rightly so, the entire payments industry is focused on this.

You read earlier this month about efforts that the Clearinghouse has underway with its 22 U.S. banks to do some work on this topic as well. We believe that we play a critical role in helping define the standards for token implementation broadly. We're working closely across the entire payment ecosystem defined very broadly to do this. This is an area where everyone needs to work closely together and it's paramount that we ensure transparency, security, and integrity so that the integrity of the payment system remains. Successful tokenization initiatives must also be interoperable and standardized and do several very important things.

Number one is they need to deliver value to all stakeholders, that includes issuers, consumers, merchants, acquirers, payment gateways, and everyone involved in the digital commerce platform. It's got to be standards based, technology agnostic such that a tokenization solution builds on the existing open nature of the payments industry while also aligning with emerging payment innovation systems mobile and digital wallets. As I said before, it needs to deliver at least the same level as transparency and reliability that exists today. And equally important it needs to address the needs of everyone globally, not just in the United States.

As I said before, we're committed to working on this broadly with all of our partners. it’s something that we are working on and we feel very good about the progress that we're making with our partners on this one.

In conclusion, I just want to also talk about the repurchase program that Byron mentioned. It’s the ninth share repurchase program that the Company has authorized, since the IPO, our Board of Directors has authorized over 11 billion in share repurchase programs. And as we’ve talked about I think almost on every call and at the Investor Day since I’ve joined, we remain committed to returning excess cash to shareholders both through repurchase programs like this as well as further dividend increases. So, you know, having been here for nine months, as I commented at Investor Day, I remain more bullish as each day goes on when we look at the opportunities that exist in the industry and the assets and the ideas and the people that we have at Visa.

So with that, operator, Byron and I are ready to take any questions that are out there.

Question-and-Answer Session

Operator

(Operator Instructions) Our first question comes from Andrew Jeffrey of SunTrust. Your line is open.

Andrew Jeffrey - SunTrust

Good afternoon. Thanks for taking the question. Charlie, could you speak broadly about Visa’s U.S. consumer credit share and how you feel you’re positioned to expand share and continue above trend line growth especially as some of your competitors are potentially sharpening the pencil a little bit in the U.S.?

Charlie Scharf

Sure. Listen, I think, we are blessed with just an outstanding U.S. credit franchise which has been build up through the years through terrific relationships for sure. We look at the partners that we have and look at their performance and certainly our performance has been helped by their strong performance and that’s’ true both on the issuer side, as well as on the co-brand side.

We’ve also been certainly beneficiaries in the United States credit market as the affluent customer has recovered more quickly than the non-affluent customers and as we look forward more broad-based recovery is something which should be additive to the affluent business that we have today.

Ultimately, our ability to compete as effectively as we have within the United States revolves around all other things that we've been talking about here that we know we need to continue to build out. Those include what we are doing in the digital space. They include what we are doing in the mobile space, as well as just the continuing to provide the flexibility that we’ve talked about in terms of our core product set.

So listen and I know from the prior roles that I played, the market has always been a competitive one. There always been networks out there competing for the same business. The pencil have been sharped for a period of time and as we think about what we've got to do going forward, we certainly expect that to continue.

Operator

Our next question comes from Dan Perlin of RBC. Your line is open.

Dan Perlin - RBC

Thanks. I’m just interested to know, how important, local market processing through, DPS and VPS is you guys, from a long-term growth perspective, it does represent an important enhancement to the yield as you’ve talked about, you highlighted at the Analyst Day and it seems to be kind of coming up, with some pros and cons in various economies as you kind of outlined in your prepared remark. So if you could just speak to that point, I would appreciate it? Thank you.

Charlie Scharf

Yeah. Listen, I mean, as we talked about at Investor Day, processing we think is the second part of the equation that we can provide for our customers. When we process the transaction, when press -- when the transaction goes over our network, we are enable to, that give us the opportunity to do all things that we can do, both from a risk perspective, as well as being able to provide all the analytical information that we can provided back to the issuers in order for them to help grow their business.

Byron Pollitt

And I would just add the more of the, the more we integrate into the processing pipeline. The -- we have an opportunity to differentiate our service offering. So in the case of DPS, this creates an opportunity for us to introduce more innovative product services via mobile as an example and to add to phone trackers that expand the activation capability or opportunity for our clients. So where we can provide processing services like DPS which have the single larges debit scale potentially outside of China, I suppose. This is an area where we can excel in delivering client service.

Operator

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

Don Fandetti - Citigroup

Yeah. Charlie, I'm just curious if there are any updates on the Visa-Chase network deal in terms of timing. I think it was, there was going to be some type of pilot or something by the end of year and then also, I was wondering if you have any sense on the scope of that initiative, will it just be for merchants or transactions that are acquired through payment tackle that be broaden to other merchants indirectly?

Charlie Scharf

Okay. So, on the first part of the question, I continue to say this, which is, when it comes to what Chase merchant service is doing, there are series of questions that, you need to ask them about. What we are doing is providing the capabilities that we outlined several quarters ago. We are on schedule to deliver the ability for CMS to be in the marketplace by the fourth quarter. What actually winds up in the marketplace is really driven by them through their discussions with merchants. And again so that, that's a question for them.

And the agreement holds that they need to have a direct relationship with a merchant in order to take advantage of whatever it is they intend to provide through CMS. And so, you know as I've said I would, I would expect that sometimes as we get into next year that we would start to see some things in the marketplace and at that point we'll all be in a position to evaluate what we think the benefit of the mark.

Operator

Our next question will come from Chris Brendler of Stifel. Your line is open.

Chris Brendler - Stifel

Hi, thanks. Good afternoon. I was wondering if you would give us an update on V.me specifically on merchant acceptance. It seems from my perspective that I haven't seen as broader acceptance as I would expect at this point. I think you had some concrete goals for top hundred retailers by the end of this year. Is there an acceleration coming? What's the issue? Is it difficult to get merchants to add V.me and then along those lines, MCX, is this something that you think potentially as a competitor threat. It seems to be gaining a little bit of momentum? And is V.me a key part of your strategy in combatting merchant mobile wallets? Thanks.

Charlie Scharf

Let me start with V.me. You know I guess when we talk about V.me, you can't, and it's hard to separate out how we're doing with this issuers versus how we're doing with merchants because in our discussions with each, we really need to have to grow both sides in order to be successful. Right, it's the chicken and the egg which is, you know, merchants aren't going to want to spend the time and the effort and the money to establish V.me on their site unless they think there is a real need for it. And the issuers are going to be careful about marketing it to their clients until there is a meaningful amount of acceptance.

Having said that, we now have about 90 U.S. national institutions as partners. they include BofA, PNC, BBBA, ICBA, and others. And some of those have started actively to market these programs. We have signed an additional 72 merchants this past quarter, bringing the total signed number of merchants to 253, many, many of which will go live in the coming weeks and months. So there is a lot more coming here. There is, you know, a fairly significant pipeline of merchants. As we continue to work with acquirers on this to get in the marketplace, we'll report back.

And MCX was the second question. Listen, I think MCX we know what you know about MCX which is, you know you might know more than us. So, you know, our view on MCX is that we will learn as they continue to disclose what it is they're doing and we're focused on doing what we can to build the right kind of tools to work with merchants so that they want to do business with us.

Operator

Our next question will come from Tien-Tsin Huang of JPMorgan. Your line is open.

Tien-Tsin Huang - JPMorgan

Great. Thanks. That sounds pretty clean. I guess I'd just ask about U.S. debit growth. That did bounce back nicely to 12%. Let's just look at the 10-Q. It says intra-link process transactions were up 25%. I notice it running down pretty sharply so that was a pretty big step up. I'm curious is that sustainable and what's driving it? Did you clip on some new cars or is that paid, any details that would be great. Thanks.

Byron Pollitt

Now, Tien-Tsin, remember we're lapping the implementation of the Dodd-Frank, not suppose to say Durbin anymore, Dodd-Frank rules which took effect April 1st of last year. So it was in that quarter that we experienced the single largest negative growth rate in terms of intra-link volume. In fact, it was a 54% reduction in payment volume growth in the June ending quarter 2012 and then in the coming quarters as our strategies began to gradually take hold, we started to see a less negative growth rate. So one could deduce from that that in terms of actual year-over-year growth rate, it's considerable that the -- this June ending quarter might be high tide and then as we begin to lap the other quarters, the subsequent quarters that the relative growth will just have a tougher comp to deliver.

I'd also just like to underscore that there is no way we're going to recover all that market share that we have considered as a result of the legislative change. So I think that there will be -- we still need a few more quarters in order to get to some sort of normalized state.

But as I said in my earnings commentary, in the subsequent quarters we still expect healthy growth rates in debit, U.S. debit. But everything else being equal they should moderate a bit as they begin to lap the strategies we put into place which in turn had growing effectiveness as time pass.

Byron Pollitt

Let me just add to that. So the follow up is we still think we have from our perspective a business, which can grow at a reasonable rate, understanding that we believe we permanently lost share because of legislation and those two things can coexist.

Operator

Our next question will come from Glenn Greene of Oppenheimer. Your line is open.

Glenn Greene - Oppenheimer

Thank you. Just regarding the EU proposal, I wanted to just get some context from you regarding whether or not it's having any bearings on your discussions with Visa Europe regarding their potential to exercise the put, as well as negotiation of these specific terms, meaning is this then somewhat of a stumbling back -- stumbling block getting clarity on the EU proposal?

Charlie Scharf

I think you've got to ask, Visa Europe has a put. So, that means, we don't have a call and we it's -- and we can't proactively engage them in a discussion on price or things like that. So what impacts their thinking relative to their desire to put the company, you really have to ask them.

I mean I think it's a complicated set of circumstances. There is a lot going on in Europe right now. I think you can make arguments either way, whether it makes -- if you're sitting in their position, whether it would make you more willing or less willing, but it's their decision. So they're the appropriate people to answer the question.

Operator

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

Craig Maurer - CLSA

Yeah. Hi. Thanks for taking the questions. Two question. First, could you comment on China? There seems to be some movement in terms of issuers being allowed to issue cards in China. Some discussion regarding processing, I'm just wondering if you could discuss there's been any sign of those discussions or your thought process around timing of when the market might become open to you?

Secondly, on incentives, like so you've got two quarters of benefit from the Chase field in this quarter, I believe this what you said. But looking out to next year, is it reasonable to believe that you could come in as a percentage of gross revenue below the bottom end of this year's guidance due to the new arrangement or are other clients increasing and therefore that's a false assumption? Thanks.

Charlie Scharf

Why don't I start with China and unfortunately there's still not a lot of new news to talk about with China. The agreement with the WTO requires China to issue regulations by the end of July to open up the domestic market to foreign competition.

From what we've seen, there has been some very small incremental things announced by the Chinese government but they have not been clear as we read the information to lay out a roadmap to open up the domestic marketplace. So we're waiting with everyone else until that happens. We have no better idea than anyone else, how, what form that will take, what time period. The opportunity for us, in what time period that opportunity would evolve. And so, you know, there is not a lot there.

Now having said that we're still in the same place with, we feel, from a long term perspective, putting aside whether it's, one quarter, four quarters or eight quarters away, the opportunity to compete in a domestic marketplace in China with the capabilities that we have, we think could be significant over a long period of time. Unfortunately we still don't know what the time period is and what the requirements to participate will be.

Byron Pollitt

Over to incentive.

Charlie Scharf

You asked an interesting question. There is clearly two forces at work here. One of which is the Chase contract where the pricing has been restructured so that it is more per transaction. There is still incentives related to the contract but not nearly at the magnitude that they were pre contract. At the same time, the vast majority of our issuers are in growth mode with their portfolios. The larger they grow their portfolios, the more incentives we pay. And that has been our business model for decades.

And so, as is our practice, we will schedule those out over the next coming, the next two months. We will also take a hard look at what contracts are likely to renew in the coming year, which also raise into that copulation and then give you a report out in October. Let me just signal in the spirit of your question, that it's best, in our view, it is best to model incentives on a full-year basis recognizing that they can have a lot of variation between quarters and as I said in my earnings remarks, in Q4 we expect an above average level of deal activity as we move to the closing out of our fiscal year. And therefore we expect a higher percent as a -- incentive as a percent of gross revenue. And you should not consider that representative of the go forward trend.

Operator

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

Tom McCrohan - Janney

Hi, thanks for taking the question. Just a quick question on card not present (CNP) given the growth of the eCommerce, how much Visa's volume today is card not present eCommerce volume and is the revenue yield on those type of transactions the same as for transactions that are card present? Thanks.

Charlie Scharf

Good question. That's not something that we're, that we have decided to speak about publicly at this point. Inevitably though I think that's something that we will be talking about much more in the future since that is the fastest growing channel that we have and by way of form factor within Form Factor, the fastest growing factor is mobile. And the two of them clearly are linked. So I would say we're short on detail today but more to come in the future.

Operator

Our next question will come from Moshe Katri of Cowen. Your line is open.

Moshe Katri - Cowen

Okay, thanks. Byron can you talk a bit about credit in the U.S., maybe compare what you're seeing on the corporate side versus on the consumer side of the business and if there're any changes during the quarter?

Byron Pollitt

I would say that the, in terms of health, the corporate side is healthy but the factors that are fueling the really strong performance we've been experiencing in consumer credit constitute more of a tailwind. When we look across the corporate spend, a lot of that has to do with the degree of recovery in the economies, across the globe. Our view is that the recovery, this is a technical term, is sluggish, which is one step above anemic and given that enthusiastic description, the very fact that we are seeing positive growth in corporate spend on cards in categories like airlines and the T&E components, we view as encouraging.

Having said that, there is for us in our view a significant opportunity to further penetrate a commercial sector, we have invested significantly in our commercial information platforms that support that part of the business with our commercial clients. And we believe with the investments we've made in our IntelliLink platform that we are well positioned to experience meaningful growth in this market segment in years to come.

Operator

Our next question will come from Arvind Ramani of BNP. Your line is open.

Arvind Ramani - BNP

Hi. Thanks for taking the question. Good quarter. I just had a quick question on your -- clearly the affluent has kind of -- has come back. But what are your assumptions for continued growth from the affluent market and also what's your view on the non-affluent market?

Charlie Scharf

So the affluent part of our portfolio really has been the driver of the credit spend that we have been recording over the past year. In the last quarter or two, we are starting to see some participation from the next income cohort down but it is not yet significant and therefore it's not a material driver in our results today.

As we look out into the coming year, when I describe the economic -- underlying economic growth as sluggish, if I would relate that to the U.S., creating 200,000 jobs a month, which is kind of the minimum to make any progress against unemployment. We would describe that as non-anemic but as sluggish growth. And -- but it is creating new jobs and those new jobs ultimately translate into spend.

And so our outlook is that the non-affluent spend will contribute more but not significantly more to the payment volume spend in the coming year. That's how we're thinking about it. And when we gave our guidance for '14, the limited guidance at this point, that was the assumptions that underpinned the growth rates we expressed.

Operator

Our next question comes from Smittipon Srethapramote of Morgan Stanley. Your line is open.

Smittipon Srethapramote - Morgan Stanley

Great. Thank you. International revenue growth was strong in relation to cross border volume growth. Can you talk about the drivers behind that and how much of the lift that you guys get from makeshift toward the tighter yielding geographies?

Byron Pollitt

Yeah. So I would say that there is a little bit of mix. There is a lot of volatility. So whenever there is significant volatility in the currency markets that translates into higher international revenue for us. That's something that can be -- can appear in one quarter and disappear the next relative to whatever an average volatility is.

We have been seeing with the strengthening of the dollar, the volatility in the Australian dollar, Japanese Yen to a lesser extent to Euro and Sterling, the turbulence in those markets is really -- and the associated volatility is the principal driver of the difference in international revenue versus the actual number of -- versus the growth in payment volume that we experienced.

Operator

Our next question comes from Rod Bourgeois of Bernstein. Your line is open.

Rod Bourgeois - Bernstein

Okay. Great. Just a two-part question about Europe. So if you were a network impeding in the vast majority of Europe, what do you like and not like about the EC's regulatory proposals that have recently been released. And do, the second part of the question is, is there any worry that Europe's regulatory moves might fuel merchants to push for regulation in other countries such as the U.S. and/or emerging countries?

Charlie Scharf

Yeah, this is our view, if we were Europeans which we are certainly not, I guess when we read it the things that we like about it are I guess first of all there is recognition in the value of interchange. We can argue about what that number is but we've heard lots of things through the years about whether interchange should exist or not exist in some parts of the world and recognition that it belongs, it's a statement in itself. And certainly I put no surcharge into that category as well. And, well then I would say which straddles both sides, the good and the bad, is level playing field. And so our networks that operate both three party and four party models fall into both sides of the camp. So on the one hand, it's a positive thing to bring some parts of their business into this level playing field. But the fact is there is still a meaningful part of the marketplace that there is just, you can argue an unfair advantage has been given and doesn't actually solve whatever the underlining regs are supposed to solve.

The second thing I would put in the negative category is [co-bashing] and the third thing I would put is this, the splitting of processing from the brand. And the second part of Rob's question was …

Byron Pollitt

(Inaudible) is reasonable.

Charlie Scharf

Yeah and so I think it is the whole world, you know the world is a big place, but everyone sees what everyone else does, for sure. Everyone, so people will see what happened here in the U.S. on debit. We've seen Australia. They've been watching Canada. They've been watching Europe. So it's certainly, you know you have to believe that when one significant part of the world does something that the other part of the world looks at it. You know in this case, you know remember this is proposed legislation. It will take several years for comments and for it to work through its process. So the things that have been decided here as best I can tell are not set in stone. And we'll see how these things actually evolve in the marketplace.

Operator

Our next question will come from Dave Koning from Baird.

Dave Koning - Baird

Yeah, hey guys. Just looking at the 10-Q, rest of world revenue, not just the international line but actual rest of world revenue is up 24% this quarter. The last four it was up about 10% to 14%. And I think the explanation is some FX volatility probably helped on cross border part of that but it was a pretty big acceleration, maybe you can talk through maybe a couple of other reasons that that also accelerated so much.

Byron Pollitt

There are two reasons that matter. You hit the first one which is the boost in international is reflective. We booked that into the rest of world line. and the second, if you recall, when I mentioned that the 17% revenue growth for the quarter benefited from significant non-recurring incentives that brought the growth rate down by several percentage points if you were to exclude those. All of those significant nonrecurring incentives were outside the United States. So they had the effect of amplifying the growth rate of rest of world. And those are the two main drivers.

Operator

Our next question will come from James Friedman of Susquehanna. Your line is open**.**

James Friedman - Susquehanna

Hi, a quick question on EMV. It looks like we're about 18 months from the deadline set in 2015. Are you seeing banks accelerate the issuance of EMV cards ahead of the deadline and any comments on EMV with regards to merchant acceptance would be interesting. Thank you.

Charlie Scharf

We certainly hear a fair amount being discussed about it. And we also have, I think, more issuers in the United States issuing Chip Cards due to the importance of making for an easy acceptance experience when people travel outside the United States.

I don't have the numbers in terms of the amount of EMV cards that are being issued today. It is bigger than it's been but it's not, by any stretch, imagination of the majority of the cards yet. But I did read something recently that suggested that the percentage of issuers that are attending to do it is growing but I don't think we know any more than that today.

And on the merchant side, I would say it's a similar conversation with the exception being to the extent that machines in merchant's facilities have to be replaced. They appear to be being replaced with machines that will accept the new form of card.

Jack Carsky

Brad, at this point, we have time for one last question.

Operator

Our last question comes from Darrin Peller of Barclays. Your line is open.

Darrin Peller - Barclays

Thanks guys. Just want to jump in year-to-date we're clearly seeing a more meaningful margin expansion for this year again versus what we saw in the prior year, really prior to average margins. Average margins to the first three quarters are around 62.5%. So really more than 100 basis points expansion year-over-year. Is there anything unique about the years, quarterly revenues or maybe the operating leverage in the model on the past quarter is that shouldn't appear as there is something that we can expect this type of margin upside just from thorough operating leverage embedded in the model?

Byron Pollitt

Let me respond to that in two ways. First of all, I just want to anchor the group back into the guidance for '13 since we are talking margins and you begin with year-to-date. So we held our guidance at around 60% operating margin, which implies -- the math implies that the year-to-date is trending higher than what we would expect for the fourth quarter, which is why we kept it at around 60, so point one.

Point two, there is fundamental operating leverage in the business as you know. We have been very consistent in that we don't solve for operating margins. We don’t have targets. We don't have internal requirements, what we do solve for our investments that drive shareholder value. It is the nature of our business that many of those investments are expense versus capital. And therefore as we continue to ramp up the investments that support our growth strategies, it is -- they often carry a significant expense component to them and would immediately put down downward pressure on the margins.

And I think it's safe to say that that philosophy of investing for growth and value both today and tomorrow is the philosophy we intend to follow. And that is -- that means some sacrifices of theoretically higher-margin, we’re fully prepared to do that in the name of shareholder value.

Charlie Scharf

And let me just add one more thing to that which is, as it has been pointed out by bunch of you and also on this call, we do operate in a competitive marketplace. And it wouldn’t be right for our long-term shareholder interest to be thinking about how our services should be priced based upon a commitment that we would make to you all to continue to increase the margin levels that we have.

We have to look at each transaction. How does the market price those transactions, what value do we think we’re providing and have the ability to compete effectively if we think it makes sense. And so that August factored into the guidance that’s given.

Jack Carsky

With that, we want to thank you all for joining us here today and if anybody has follow-up questions, please feel free to call investor relations. Thanks.

Operator

Thank you for your participation on the conference call today. At this time, all parties may disconnect.

Executives

Jack Carsky - Head, Global Investor Relations

Charlie Scharf - Chief Executive Officer

Byron Pollitt - Chief Financial Officer

Analysts

Andrew Jeffrey - SunTrust

Dan Perlin - RBC

Don Fandetti - Citigroup

Chris Brendler - Stifel

Tien-Tsin Huang - JPMorgan

Glenn Greene - Oppenheimer

Craig Maurer - CLSA

Tom McCrohan - Janney

Moshe Katri - Cowen

Arvind Ramani - BNP

Smittipon Srethapramote - Morgan Stanley

Rod Bourgeois - Bernstein

Dave Koning - Baird

James Friedman - Susquehanna

Darrin Peller - Barclays

Visa Inc (V) F3Q 2013 Results Earnings Call July 24, 2013 5:00 PM ET

Operator

Welcome to Visa Incorporated Fiscal Q3 2013 Earnings Conference Call. All participants are in a listen-only mode until the question-and-answer session. Today's conference is being recorded. If you have any objections, you may disconnect at this time.

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

Jack Carsky - Head, Global Investor Relations

Thanks Brad. Good afternoon. And welcome to Visa Inc.'s fiscal third quarter 2013 earnings conference call. With us today are Charlie Scharf, Visa's Chief Executive Officer; and Byron Pollitt, Visa's Chief Financial Officer.

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

Let me also remind you that this presentation may include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. By their nature, forward-looking statements are not guarantees of future performance, and as a result of a variety of factors, actual results could differ materially from such statements. Additional information concerning those factors is available on the Company's filings with the SEC which can be accessed through the SEC's website and the Investor Relations section of the Visa website.

For historical non-GAAP or pro forma related financial information disclosed in this call, related GAAP measures and other information required by Regulation G of the SEC are available in the Financial and Statistical Summary accompanying our fiscal third quarter press release. This release can also be accessed through the Investor Relation section of our website.

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

Byron Pollitt - Chief Financial Officer

Thank you, Jack. Let me begin with my usual call outs and observations. First, some color on the third quarter's 17% net revenue growth. It is important to note that this growth rate benefited from the absence of significant one time client incentives incurred in the prior year. without these one time client incentives, revenue growth for Q3 would have been closer to 14%. That said, payment volume growth was broad based globally for the March quarter and we're seeing double-digit growth rates in the June quarter for both credit and debit on a constant dollar basis. Based on these trends, and with three quarters of the fiscal year now on the books, we are raising full year 2013 revenue guidance from to low double-digits to around 13%.

Second, service revenue, though up 7% on year-over-year basis, it was down sequentially from the fiscal second quarter. This was primarily due to the signing of the 10 year Chase deal which was executed in fiscal Q3 but was retroactive to the beginning of Q2. This contract, as discussed on the Q2 earnings call, disproportionately impacted the service revenue line and resulted in offsetting reductions in gross service revenue and related client incentives. Because it was signed in fiscal Q3, the service revenue impacts for both Q2 and Q3 were recorded in the current quarter. This means that Q4 service revenue growth rate should be a more representative indicator of underling growth.

Third, client incentives for the quarter, as a percentage of gross revenue, were 14.8%. As described previously, two quarters of Chase related incentive reductions were booked in Q3. This impact was constant inflation in our most recent full year guidance and we remain comfortable with client incentives as a percent of gross revenue in the 16% to 17% range for the full-year 2013.

Fourth, now that we have fully left implementation of the Dodd-Frank routing rules, beginning in June, quarterly Interlink payment volume growth has turned positive for the first time in over a year. Going forward as we lapse a period during which Visa's post Dodd-Frank debit strategies took hold, we would expect healthy but moderating revenue growth rates for U.S. debit.

Fifth, given our earnings result year-to-date and our expectations for the fiscal fourth quarter, we are increasing our fiscal 2013 adjusted EPS guidance from around 20% to the low 20s. Lastly, as we remain commitment to returning excess cash to our shareholders, during the quarter we've spent approximately $1 billion to repurchase 6 million shares at an average price of approximately $177.00. this leaves $61 million remaining in our prior authorization. And as we announced earlier, our Board recently authorized a new $1.5 billion share repurchase program which will run through July of 2014.

Now, let's turn to the numbers. As is our practice I will cover our global payment volume and process transaction trends for the fiscal third quarter, followed by our results through July 21st. I'll then cover the financial highlights of our fiscal third quarter and conclude with our guidance outlook for the balance of fiscal 2013 and fiscal 2014.

Global payment volume growth for the June quarter, in constant dollars was 18%. Payment volume growth for the June quarter incomes in dollars was 13% above the March quarter's 9%. This was driven by sustained growth in all of our regions including the U.S. which saw some incremental benefit from the lasting effects associated with U.S. debit regulations.

More recently, in the U.S., through July 21, payment volume growth was 10% compared with 11% in the June ending quarter. Drilling down further, U.S. credit growth of 10% held at Q3 levels while debit, which also grew at 10% experienced a healthy but moderating growth rate as we lap the growing impact of the Visa's U.S. debit strategies.

Global cross-border volume delivered a solid 11% constant dollar growth rate in the June quarter which compares to a 10% rate in the March quarter. The U.S. grew 9% and the rest of world 12%. Through July 21, cross-border volume on a constant dollar basis grew 7% with the U.S. growth rate of 9% and the rest of world at 6%.

The slowing growth in July is most pronounced outside the U.S. and we believe is due in large part to the timing of Ramadan versus last year. Based on historical travel patterns, we estimate the Ramadan impact to be in the 250 to 300 basis points range for the month and if pass this prologue, we should see a bounce back in August.

Transactions processed over Visa's network totaled $15 billion in the fiscal third quarter, a 14% increase over the prior year period. The U.S. grew 12% while the rest of world delivered 23% growth. We have now fully lapped the negative impacts associated with U.S. debit regulation. Through July 21, process transaction growth was a positive 14%.

Lastly, please note that in our operational performance data pack, that was released with today's earnings results, we updated the cash volume in our LAC region to account for several quarters of underreporting by one of our largest issuers in Brazil. As a reminder, these cash volumes have no impact to our revenue.

Now, turning to the income statement. Net operating revenue in the quarter was $3 billion, a 17% increase year-over-year driven by solid growth globally in both domestic and international transactions and as mentioned earlier, aided by significant non-recurring incentives in the prior-year quarter. Currency hedging resulted in only a modest foreign exchange headwind on net revenue in the quarter. Looking ahead, after factoring in our hedging program, we anticipate continued headwinds in the next fiscal quarter and for fiscal 2014.

Moving to the individual revenue line items, service revenue was $1.3 billion, up 7% over the prior-year period. On a sequential basis, growth was negatively impacted by the Chase agreement which as I previously outlined, resulted in lower service revenue offset by a lower level of incentives paid to Chase.

Data processing revenue was $1.2 billion, up 15% over the prior year's quarter based on solid growth rates in Visa, process transactions inside and outside the U.S. and strong cyber storage transaction growth. With the full lapping of the implementation of U.S. Debit Regulation, data processing revenue growth is now relatively on par with process transaction growth.

International transaction revenue was up 14% to $854 million reflecting solid strength in cross-border volume and some modest benefit from higher currency volatility. As I highlighted earlier, client incentives as a percentage of gross revenue for the quarter came in at 14.8%, positively impacted by the Chase deal.

That said, we anticipate a meaningful step-up in both incentive dollars and the percentage rate in Q4 due to anticipated deal activity both domestic and international which should put us within our 2013 guidance range of 16% to 17%.

Total operating expenses for the quarter were $1.2 billion, up 9% from the prior year adjusted results. This was primarily due to higher costs associated with investments in our growth strategy.

Marketing expenses were up 4% from the prior year and stepped up from the prior quarter as we increased marketing to support a number of sponsorship campaigns including the 2013 FIFA Confederations Cup in South America and the 2014 Sochi Winter Olympics.

Operating margin for the quarter was 61% and is consistent with our current guidance. Our effective tax rate for Q3 was 33.2% while higher than our full year guidance of 30% to 32%, the year-to-date figure of 31% is tracking to that range.

Net income at $1.2 billion was up 16% over the prior year adjusted results. Fully diluted EPS was $1.88 for the quarter, up 20% over prior year adjusted results. Stronger than anticipated revenue and more aggressive share repurchases were key drivers and as noted earlier our full year adjusted EPS guidance is now low 20s.

Capital expenditures $122 million in the quarter and continue to be in line with our full-year expectations. At the end of the June quarter, we had 645 million shares of Class A common stock outstanding on a S converted basis. The weighted average number of fully diluted shares outstanding for the June quarter totaled 651 million.

Finally, in terms of guidance, other than our refinement of full-year 2013 revenue guidance to around 13%, and adjusted diluted earnings per share growth to the low 20s, all other outstanding guidance metrics for the full-year fiscal 2013 and 2014 remain the same.

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

Charlie Scharf - Chief Executive Officer

Thank you, Byron, and good afternoon everyone. First of all, I just want to reiterate that we feel very good about our performance this quarter. There is very little new news in the underlining revenue trends as Byron has just described, which means that we continue to see broad based growth geographically and also by product. And these are at growth rates consistent with what we've seen in prior quarters.

People often ask us about what we see in the economy and what I guess we can say is we don't see meaningful changes to the path of the economic recovery. And while accelerating and certainly a more broad based recovery would be beneficial to us and our clients, we do continue to feel very good about our business and our ability to deliver strong results in the current economic environment.

We did host our Investor Day on June 6th and I want to thank all those who attended both physically and listened in. we know it was a lengthy call but hopefully you found it productive. We certainly appreciate all the feedback that we received. Just a couple of quick reminders of some of these important themes that we covered.

First of all, you know, we feel great about the strong foundation that this company has been built on. There has been strong historical growth. We have great partners and the company has a tradition of innovation. Second, the macro trends have and will continue to provide tailwinds. The opportunity to move transactions from cash to electronic means is still huge. And we believe we'll be there for years to come. This is true in both the developed and the developing parts of the world. As you pointed out on Investor Day, we have 22% share TCE in the emerging, I'm sorry, within the developed markets and 9% in the emerging markets. So there is still much room to grow. In addition to us growing along with the growth of TCE across the world.

We love our core network. It's served us well and think it provides us tremendous opportunities to leverage and grow our business. Historically, what's really benefited us has been the global acceptance, the network reliability, safe and security and soundness, and our risk related tools are just a huge value added component to the network. While we continue to build on these historical strengths as we pointed out at the Investor Day, the future for us will be about using the network is a tool, to continue to create more value for issuers, acquires and merchants, and that include us building broader capabilities but also giving them access, it's our network as a device that connects to them together.

Third, the company has and continued to make huge investments in the future. We walk through some of the additional spending that's been done to the tune of an additional $700 million versus prior years, which are for the most part all geared towards growth opportunities.

And lastly, we talk about our evolving rules and practices, recognizing how the payments world is evolving. We recognize the needs to evolve our company. But we also feel strongly that we need to continue to preserve some core principles, those include the importance of the Visa brand, the safety, security and soundness of the payment system that we continue to protect and control our intellectual property, and that we enable clients of all sizes to compete. So in short, these of things that while we think we can continue to do more and more for all of our clients we think these things could also add value to the Visa network.

We turn now to little bit of an update on some of the regulatory and litigation items that are both been in the news and we've spoken about. First of all in the United States on the MDL case. The deadline for the opt outs was May 28th. As expected I am sure you show lawsuits that were filed against Visa, MasterCard and in some cases the banks from retailers which opted out of the merchant settlement agreement last year.

The final figures are still being calculated but our estimate of the opt out is that they represent slightly above 25% of our U.S. credit volume. We continue to expect approval from a core sometime in the fall.

I do want to stress that these are proceedings that have been on going for a long period of time. We remain committed to figuring out how to work with merchants of all sizes to resolve all of our differences amicably and we as you heard from us we are focused on finding new ways to work with them in conjunction with acquires and issuers to support all of the individual constituents growth objectives.

Secondly, Canada, yesterday Canada's competition tribunal issue this decision to dismiss the competition bureau's case and uphold our no surcharge and Honour All Cards rule. We have and we'll continue to engage with legislators and regulators around the world to promote the understanding of a value of electronic payments to consumers, merchant and governments broadly.

Let me now turn to Europe, and as a reminder, Visa Inc. and Visa Europe are separate independent operating companies. First of all, let me talk about, in May we alerted you to a European Commission inquiry by the Director of General Competition related to inter-regional credit interchange rates.

That investigation specifically relates to the interchange applied to transactions between a non-European Union cardholder and the merchant located within the European Union. We continue to assess their claims and we are working in a productive and professional manager with them and hope to reach resolution but there is nothing more to report at this time.

Separately, the European Commission earlier today released proposed legislation for the payments industry in the European Union which had been expected. The proposed regulation covers a wide range of topics related to the European payments industry including domestic and intra-EU cross-border interchange rates, [co-batching] requirements, process requirements and point-of-sale rules such as Honour All Cards.

Most recent announcement submission appears to address issues similar to the Commission competition case, but the propose regulation would only applied to transactions when the issuer and an acquirer are located in the European Union.

We understand that proposed legislation is to beginning of what we expect could be a long process which could take 18 to 24 months. We'll continue to keep you updated if we learn of any more developments in either these two proceedings.

Also in Europe, I'm sure we would get a question about the Visa Europe put and there is no update on that.

Let me move now and just talk for a second about a topic which has lot of you are writing about and has gotten a lot of press and that's tokenization. And to start with, stating the obvious which is we all know that transactions are increasingly moving to digital card, not present channels due to the growth of web commerce, mobile and digital wallet.

As you've heard from us in the past we've been building our capabilities to deal with transactions like this both technically and through our rules and requirements, V.net and CyberSource are just two examples where we've made significant investments to build capabilities in this space. And as we talk about tokenization I do want to just make a point that tokenization is not a new concept to us. Historically, we define the 16-digit account number [method] set and we effectively operate as tokens in the payment system today.

The reality is the development of digital commerce and related risks makes the evolution of these existing tokens -- the evolution of these existing tokens to a more secure form very necessary in a way that works both in the physical and the digital worlds. We need to eliminate the flow of sensitive data that might be vulnerable to a breach and new entrance into the payment ecosystem has also brought into question whether the appropriate information will continue to flow between merchant, acquirer, issuer and consumer. And rightly so, the entire payments industry is focused on this.

You read earlier this month about efforts that the Clearinghouse has underway with its 22 U.S. banks to do some work on this topic as well. We believe that we play a critical role in helping define the standards for token implementation broadly. We're working closely across the entire payment ecosystem defined very broadly to do this. This is an area where everyone needs to work closely together and it's paramount that we ensure transparency, security, and integrity so that the integrity of the payment system remains. Successful tokenization initiatives must also be interoperable and standardized and do several very important things.

Number one is they need to deliver value to all stakeholders, that includes issuers, consumers, merchants, acquirers, payment gateways, and everyone involved in the digital commerce platform. It's got to be standards based, technology agnostic such that a tokenization solution builds on the existing open nature of the payments industry while also aligning with emerging payment innovation systems mobile and digital wallets. As I said before, it needs to deliver at least the same level as transparency and reliability that exists today. And equally important it needs to address the needs of everyone globally, not just in the United States.

As I said before, we're committed to working on this broadly with all of our partners. it's something that we are working on and we feel very good about the progress that we're making with our partners on this one.

In conclusion, I just want to also talk about the repurchase program that Byron mentioned. It's the ninth share repurchase program that the Company has authorized, since the IPO, our Board of Directors has authorized over 11 billion in share repurchase programs. And as we've talked about I think almost on every call and at the Investor Day since I've joined, we remain committed to returning excess cash to shareholders both through repurchase programs like this as well as further dividend increases. So, you know, having been here for nine months, as I commented at Investor Day, I remain more bullish as each day goes on when we look at the opportunities that exist in the industry and the assets and the ideas and the people that we have at Visa.

So with that, operator, Byron and I are ready to take any questions that are out there.

Question-and-Answer Session

Operator

(Operator Instructions) Our first question comes from Andrew Jeffrey of SunTrust. Your line is open.

Andrew Jeffrey - SunTrust

Good afternoon. Thanks for taking the question. Charlie, could you speak broadly about Visa's U.S. consumer credit share and how you feel you're positioned to expand share and continue above trend line growth especially as some of your competitors are potentially sharpening the pencil a little bit in the U.S.?

Charlie Scharf - Chief Executive Officer

Sure. Listen, I think, we are blessed with just an outstanding U.S. credit franchise which has been build up through the years through terrific relationships for sure. We look at the partners that we have and look at their performance and certainly our performance has been helped by their strong performance and that's' true both on the issuer side, as well as on the co-brand side.

We've also been certainly beneficiaries in the United States credit market as the affluent customer has recovered more quickly than the non-affluent customers and as we look forward more broad-based recovery is something which should be additive to the affluent business that we have today.

Ultimately, our ability to compete as effectively as we have within the United States revolves around all other things that we've been talking about here that we know we need to continue to build out. Those include what we are doing in the digital space. They include what we are doing in the mobile space, as well as just the continuing to provide the flexibility that we've talked about in terms of our core product set.

So listen and I know from the prior roles that I played, the market has always been a competitive one. There always been networks out there competing for the same business. The pencil have been sharped for a period of time and as we think about what we've got to do going forward, we certainly expect that to continue.

Operator

Our next question comes from Dan Perlin of RBC. Your line is open.

Dan Perlin - RBC

Thanks. I'm just interested to know, how important, local market processing through, DPS and VPS is you guys, from a long-term growth perspective, it does represent an important enhancement to the yield as you've talked about, you highlighted at the Analyst Day and it seems to be kind of coming up, with some pros and cons in various economies as you kind of outlined in your prepared remark. So if you could just speak to that point, I would appreciate it? Thank you.

Charlie Scharf - Chief Executive Officer

Yeah. Listen, I mean, as we talked about at Investor Day, processing we think is the second part of the equation that we can provide for our customers. When we process the transaction, when press -- when the transaction goes over our network, we are enable to, that give us the opportunity to do all things that we can do, both from a risk perspective, as well as being able to provide all the analytical information that we can provided back to the issuers in order for them to help grow their business.

Byron Pollitt - Chief Financial Officer

And I would just add the more of the, the more we integrate into the processing pipeline. The -- we have an opportunity to differentiate our service offering. So in the case of DPS, this creates an opportunity for us to introduce more innovative product services via mobile as an example and to add to phone trackers that expand the activation capability or opportunity for our clients. So where we can provide processing services like DPS which have the single larges debit scale potentially outside of China, I suppose. This is an area where we can excel in delivering client service.

Operator

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

Don Fandetti - Citigroup

Yeah. Charlie, I'm just curious if there are any updates on the Visa-Chase network deal in terms of timing. I think it was, there was going to be some type of pilot or something by the end of year and then also, I was wondering if you have any sense on the scope of that initiative, will it just be for merchants or transactions that are acquired through payment tackle that be broaden to other merchants indirectly?

Charlie Scharf - Chief Executive Officer

Okay. So, on the first part of the question, I continue to say this, which is, when it comes to what Chase merchant service is doing, there are series of questions that, you need to ask them about. What we are doing is providing the capabilities that we outlined several quarters ago. We are on schedule to deliver the ability for CMS to be in the marketplace by the fourth quarter. What actually winds up in the marketplace is really driven by them through their discussions with merchants. And again so that, that's a question for them.

And the agreement holds that they need to have a direct relationship with a merchant in order to take advantage of whatever it is they intend to provide through CMS. And so, you know as I've said I would, I would expect that sometimes as we get into next year that we would start to see some things in the marketplace and at that point we'll all be in a position to evaluate what we think the benefit of the mark.

Operator

Our next question will come from Chris Brendler of Stifel. Your line is open.

Chris Brendler - Stifel

Hi, thanks. Good afternoon. I was wondering if you would give us an update on V.me specifically on merchant acceptance. It seems from my perspective that I haven't seen as broader acceptance as I would expect at this point. I think you had some concrete goals for top hundred retailers by the end of this year. Is there an acceleration coming? What's the issue? Is it difficult to get merchants to add V.me and then along those lines, MCX, is this something that you think potentially as a competitor threat. It seems to be gaining a little bit of momentum? And is V.me a key part of your strategy in combatting merchant mobile wallets? Thanks.

Charlie Scharf - Chief Executive Officer

Let me start with V.me. You know I guess when we talk about V.me, you can't, and it's hard to separate out how we're doing with this issuers versus how we're doing with merchants because in our discussions with each, we really need to have to grow both sides in order to be successful. Right, it's the chicken and the egg which is, you know, merchants aren't going to want to spend the time and the effort and the money to establish V.me on their site unless they think there is a real need for it. And the issuers are going to be careful about marketing it to their clients until there is a meaningful amount of acceptance.

Having said that, we now have about 90 U.S. national institutions as partners. they include BofA, PNC, BBBA, ICBA, and others. And some of those have started actively to market these programs. We have signed an additional 72 merchants this past quarter, bringing the total signed number of merchants to 253, many, many of which will go live in the coming weeks and months. So there is a lot more coming here. There is, you know, a fairly significant pipeline of merchants. As we continue to work with acquirers on this to get in the marketplace, we'll report back.

And MCX was the second question. Listen, I think MCX we know what you know about MCX which is, you know you might know more than us. So, you know, our view on MCX is that we will learn as they continue to disclose what it is they're doing and we're focused on doing what we can to build the right kind of tools to work with merchants so that they want to do business with us.

Operator

Our next question will come from Tien-Tsin Huang of JPMorgan. Your line is open.

Tien-Tsin Huang - JPMorgan

Great. Thanks. That sounds pretty clean. I guess I'd just ask about U.S. debit growth. That did bounce back nicely to 12%. Let's just look at the 10-Q. It says intra-link process transactions were up 25%. I notice it running down pretty sharply so that was a pretty big step up. I'm curious is that sustainable and what's driving it? Did you clip on some new cars or is that paid, any details that would be great. Thanks.

Byron Pollitt - Chief Financial Officer

Now, Tien-Tsin, remember we're lapping the implementation of the Dodd-Frank, not suppose to say Durbin anymore, Dodd-Frank rules which took effect April 1st of last year. So it was in that quarter that we experienced the single largest negative growth rate in terms of intra-link volume. In fact, it was a 54% reduction in payment volume growth in the June ending quarter 2012 and then in the coming quarters as our strategies began to gradually take hold, we started to see a less negative growth rate. So one could deduce from that that in terms of actual year-over-year growth rate, it's considerable that the -- this June ending quarter might be high tide and then as we begin to lap the other quarters, the subsequent quarters that the relative growth will just have a tougher comp to deliver.

I'd also just like to underscore that there is no way we're going to recover all that market share that we have considered as a result of the legislative change. So I think that there will be -- we still need a few more quarters in order to get to some sort of normalized state.

But as I said in my earnings commentary, in the subsequent quarters we still expect healthy growth rates in debit, U.S. debit. But everything else being equal they should moderate a bit as they begin to lap the strategies we put into place which in turn had growing effectiveness as time pass.

Byron Pollitt - Chief Financial Officer

Let me just add to that. So the follow up is we still think we have from our perspective a business, which can grow at a reasonable rate, understanding that we believe we permanently lost share because of legislation and those two things can coexist.

Operator

Our next question will come from Glenn Greene of Oppenheimer. Your line is open.

Glenn Greene - Oppenheimer

Thank you. Just regarding the EU proposal, I wanted to just get some context from you regarding whether or not it's having any bearings on your discussions with Visa Europe regarding their potential to exercise the put, as well as negotiation of these specific terms, meaning is this then somewhat of a stumbling back -- stumbling block getting clarity on the EU proposal?

Charlie Scharf - Chief Executive Officer

I think you've got to ask, Visa Europe has a put. So, that means, we don't have a call and we it's -- and we can't proactively engage them in a discussion on price or things like that. So what impacts their thinking relative to their desire to put the company, you really have to ask them.

I mean I think it's a complicated set of circumstances. There is a lot going on in Europe right now. I think you can make arguments either way, whether it makes -- if you're sitting in their position, whether it would make you more willing or less willing, but it's their decision. So they're the appropriate people to answer the question.

Operator

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

Craig Maurer - CLSA

Yeah. Hi. Thanks for taking the questions. Two question. First, could you comment on China? There seems to be some movement in terms of issuers being allowed to issue cards in China. Some discussion regarding processing, I'm just wondering if you could discuss there's been any sign of those discussions or your thought process around timing of when the market might become open to you?

Secondly, on incentives, like so you've got two quarters of benefit from the Chase field in this quarter, I believe this what you said. But looking out to next year, is it reasonable to believe that you could come in as a percentage of gross revenue below the bottom end of this year's guidance due to the new arrangement or are other clients increasing and therefore that's a false assumption? Thanks.

Charlie Scharf - Chief Executive Officer

Why don't I start with China and unfortunately there's still not a lot of new news to talk about with China. The agreement with the WTO requires China to issue regulations by the end of July to open up the domestic market to foreign competition.

From what we've seen, there has been some very small incremental things announced by the Chinese government but they have not been clear as we read the information to lay out a roadmap to open up the domestic marketplace. So we're waiting with everyone else until that happens. We have no better idea than anyone else, how, what form that will take, what time period. The opportunity for us, in what time period that opportunity would evolve. And so, you know, there is not a lot there.

Now having said that we're still in the same place with, we feel, from a long term perspective, putting aside whether it's, one quarter, four quarters or eight quarters away, the opportunity to compete in a domestic marketplace in China with the capabilities that we have, we think could be significant over a long period of time. Unfortunately we still don't know what the time period is and what the requirements to participate will be.

Byron Pollitt - Chief Financial Officer

Over to incentive.

Charlie Scharf - Chief Executive Officer

You asked an interesting question. There is clearly two forces at work here. One of which is the Chase contract where the pricing has been restructured so that it is more per transaction. There is still incentives related to the contract but not nearly at the magnitude that they were pre contract. At the same time, the vast majority of our issuers are in growth mode with their portfolios. The larger they grow their portfolios, the more incentives we pay. And that has been our business model for decades.

And so, as is our practice, we will schedule those out over the next coming, the next two months. We will also take a hard look at what contracts are likely to renew in the coming year, which also raise into that copulation and then give you a report out in October. Let me just signal in the spirit of your question, that it's best, in our view, it is best to model incentives on a full-year basis recognizing that they can have a lot of variation between quarters and as I said in my earnings remarks, in Q4 we expect an above average level of deal activity as we move to the closing out of our fiscal year. And therefore we expect a higher percent as a -- incentive as a percent of gross revenue. And you should not consider that representative of the go forward trend.

Operator

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

Tom McCrohan - Janney

Hi, thanks for taking the question. Just a quick question on card not present (CNP) given the growth of the eCommerce, how much Visa's volume today is card not present eCommerce volume and is the revenue yield on those type of transactions the same as for transactions that are card present? Thanks.

Charlie Scharf - Chief Executive Officer

Good question. That's not something that we're, that we have decided to speak about publicly at this point. Inevitably though I think that's something that we will be talking about much more in the future since that is the fastest growing channel that we have and by way of form factor within Form Factor, the fastest growing factor is mobile. And the two of them clearly are linked. So I would say we're short on detail today but more to come in the future.

Operator

Our next question will come from Moshe Katri of Cowen. Your line is open.

Moshe Katri - Cowen

Okay, thanks. Byron can you talk a bit about credit in the U.S., maybe compare what you're seeing on the corporate side versus on the consumer side of the business and if there're any changes during the quarter?

Byron Pollitt - Chief Financial Officer

I would say that the, in terms of health, the corporate side is healthy but the factors that are fueling the really strong performance we've been experiencing in consumer credit constitute more of a tailwind. When we look across the corporate spend, a lot of that has to do with the degree of recovery in the economies, across the globe. Our view is that the recovery, this is a technical term, is sluggish, which is one step above anemic and given that enthusiastic description, the very fact that we are seeing positive growth in corporate spend on cards in categories like airlines and the T&E components, we view as encouraging.

Having said that, there is for us in our view a significant opportunity to further penetrate a commercial sector, we have invested significantly in our commercial information platforms that support that part of the business with our commercial clients. And we believe with the investments we've made in our IntelliLink platform that we are well positioned to experience meaningful growth in this market segment in years to come.

Operator

Our next question will come from Arvind Ramani of BNP. Your line is open.

Arvind Ramani - BNP

Hi. Thanks for taking the question. Good quarter. I just had a quick question on your -- clearly the affluent has kind of -- has come back. But what are your assumptions for continued growth from the affluent market and also what's your view on the non-affluent market?

Charlie Scharf - Chief Executive Officer

So the affluent part of our portfolio really has been the driver of the credit spend that we have been recording over the past year. In the last quarter or two, we are starting to see some participation from the next income cohort down but it is not yet significant and therefore it's not a material driver in our results today.

As we look out into the coming year, when I describe the economic -- underlying economic growth as sluggish, if I would relate that to the U.S., creating 200,000 jobs a month, which is kind of the minimum to make any progress against unemployment. We would describe that as non-anemic but as sluggish growth. And -- but it is creating new jobs and those new jobs ultimately translate into spend.

And so our outlook is that the non-affluent spend will contribute more but not significantly more to the payment volume spend in the coming year. That's how we're thinking about it. And when we gave our guidance for '14, the limited guidance at this point, that was the assumptions that underpinned the growth rates we expressed.

Operator

Our next question comes from Smittipon Srethapramote of Morgan Stanley. Your line is open.

Smittipon Srethapramote - Morgan Stanley

Great. Thank you. International revenue growth was strong in relation to cross border volume growth. Can you talk about the drivers behind that and how much of the lift that you guys get from makeshift toward the tighter yielding geographies?

Byron Pollitt - Chief Financial Officer

Yeah. So I would say that there is a little bit of mix. There is a lot of volatility. So whenever there is significant volatility in the currency markets that translates into higher international revenue for us. That's something that can be -- can appear in one quarter and disappear the next relative to whatever an average volatility is.

We have been seeing with the strengthening of the dollar, the volatility in the Australian dollar, Japanese Yen to a lesser extent to Euro and Sterling, the turbulence in those markets is really -- and the associated volatility is the principal driver of the difference in international revenue versus the actual number of -- versus the growth in payment volume that we experienced.

Operator

Our next question comes from Rod Bourgeois of Bernstein. Your line is open.

Rod Bourgeois - Bernstein

Okay. Great. Just a two-part question about Europe. So if you were a network impeding in the vast majority of Europe, what do you like and not like about the EC's regulatory proposals that have recently been released. And do, the second part of the question is, is there any worry that Europe's regulatory moves might fuel merchants to push for regulation in other countries such as the U.S. and/or emerging countries?

Charlie Scharf - Chief Executive Officer

Yeah, this is our view, if we were Europeans which we are certainly not, I guess when we read it the things that we like about it are I guess first of all there is recognition in the value of interchange. We can argue about what that number is but we've heard lots of things through the years about whether interchange should exist or not exist in some parts of the world and recognition that it belongs, it's a statement in itself. And certainly I put no surcharge into that category as well. And, well then I would say which straddles both sides, the good and the bad, is level playing field. And so our networks that operate both three party and four party models fall into both sides of the camp. So on the one hand, it's a positive thing to bring some parts of their business into this level playing field. But the fact is there is still a meaningful part of the marketplace that there is just, you can argue an unfair advantage has been given and doesn't actually solve whatever the underlining regs are supposed to solve.

The second thing I would put in the negative category is [co-bashing] and the third thing I would put is this, the splitting of processing from the brand. And the second part of Rob's question was …

Byron Pollitt - Chief Financial Officer

(Inaudible) is reasonable.

Charlie Scharf - Chief Executive Officer

Yeah and so I think it is the whole world, you know the world is a big place, but everyone sees what everyone else does, for sure. Everyone, so people will see what happened here in the U.S. on debit. We've seen Australia. They've been watching Canada. They've been watching Europe. So it's certainly, you know you have to believe that when one significant part of the world does something that the other part of the world looks at it. You know in this case, you know remember this is proposed legislation. It will take several years for comments and for it to work through its process. So the things that have been decided here as best I can tell are not set in stone. And we'll see how these things actually evolve in the marketplace.

Operator

Our next question will come from Dave Koning from Baird.

Dave Koning - Baird

Yeah, hey guys. Just looking at the 10-Q, rest of world revenue, not just the international line but actual rest of world revenue is up 24% this quarter. The last four it was up about 10% to 14%. And I think the explanation is some FX volatility probably helped on cross border part of that but it was a pretty big acceleration, maybe you can talk through maybe a couple of other reasons that that also accelerated so much.

Byron Pollitt - Chief Financial Officer

There are two reasons that matter. You hit the first one which is the boost in international is reflective. We booked that into the rest of world line. and the second, if you recall, when I mentioned that the 17% revenue growth for the quarter benefited from significant non-recurring incentives that brought the growth rate down by several percentage points if you were to exclude those. All of those significant nonrecurring incentives were outside the United States. So they had the effect of amplifying the growth rate of rest of world. And those are the two main drivers.

Operator

Our next question will come from James Friedman of Susquehanna. Your line is open. - Susquehanna**James Friedman** - Susquehanna

Hi, a quick question on EMV. It looks like we're about 18 months from the deadline set in 2015. Are you seeing banks accelerate the issuance of EMV cards ahead of the deadline and any comments on EMV with regards to merchant acceptance would be interesting. Thank you.

Charlie Scharf - Chief Executive Officer

We certainly hear a fair amount being discussed about it. And we also have, I think, more issuers in the United States issuing Chip Cards due to the importance of making for an easy acceptance experience when people travel outside the United States.

I don't have the numbers in terms of the amount of EMV cards that are being issued today. It is bigger than it's been but it's not, by any stretch, imagination of the majority of the cards yet. But I did read something recently that suggested that the percentage of issuers that are attending to do it is growing but I don't think we know any more than that today.

And on the merchant side, I would say it's a similar conversation with the exception being to the extent that machines in merchant's facilities have to be replaced. They appear to be being replaced with machines that will accept the new form of card.

Jack Carsky - Head, Global Investor Relations

Brad, at this point, we have time for one last question.

Operator

Our last question comes from Darrin Peller of Barclays. Your line is open.

Darrin Peller - Barclays

Thanks guys. Just want to jump in year-to-date we're clearly seeing a more meaningful margin expansion for this year again versus what we saw in the prior year, really prior to average margins. Average margins to the first three quarters are around 62.5%. So really more than 100 basis points expansion year-over-year. Is there anything unique about the years, quarterly revenues or maybe the operating leverage in the model on the past quarter is that shouldn't appear as there is something that we can expect this type of margin upside just from thorough operating leverage embedded in the model?

Byron Pollitt - Chief Financial Officer

Let me respond to that in two ways. First of all, I just want to anchor the group back into the guidance for '13 since we are talking margins and you begin with year-to-date. So we held our guidance at around 60% operating margin, which implies -- the math implies that the year-to-date is trending higher than what we would expect for the fourth quarter, which is why we kept it at around 60, so point one.

Point two, there is fundamental operating leverage in the business as you know. We have been very consistent in that we don't solve for operating margins. We don't have targets. We don't have internal requirements, what we do solve for our investments that drive shareholder value. It is the nature of our business that many of those investments are expense versus capital. And therefore as we continue to ramp up the investments that support our growth strategies, it is -- they often carry a significant expense component to them and would immediately put down downward pressure on the margins.

And I think it's safe to say that that philosophy of investing for growth and value both today and tomorrow is the philosophy we intend to follow. And that is -- that means some sacrifices of theoretically higher-margin, we're fully prepared to do that in the name of shareholder value.

Charlie Scharf - Chief Executive Officer

And let me just add one more thing to that which is, as it has been pointed out by bunch of you and also on this call, we do operate in a competitive marketplace. And it wouldn't be right for our long-term shareholder interest to be thinking about how our services should be priced based upon a commitment that we would make to you all to continue to increase the margin levels that we have.

We have to look at each transaction. How does the market price those transactions, what value do we think we're providing and have the ability to compete effectively if we think it makes sense. And so that August factored into the guidance that's given.

Jack Carsky - Head, Global Investor Relations

With that, we want to thank you all for joining us here today and if anybody has follow-up questions, please feel free to call investor relations. Thanks.

Operator

Thank you for your participation on the conference call today. At this time, all parties may disconnect.