








Earnings announcement season has been underway for a few weeks now. The acquiring industry broadly reported revenue, volume, and transaction growth during the fourth quarter of 2014 compared to the same quarter in the prior year. Acquirers and networks continue to focus on security, including EMV education and implementation; tokenization; and encryption. Fewer acquirers made strategic acquisitions in Q4 than previous quarters, but acquisitions that did occur remained largely focused on strategic channels.

Earnings Summary

Company	Date of Call	Quarterly Revenues - \$M	Y/Y %Δ	Quarterly Net Income - \$M	Y/Y %Δ	Commentary
 VISA	29Jan2015	\$3,382	7%	\$1,569	12%	Payment volume on a constant dollar basis was up 11% over the prior year.
 MasterCard	30Jan2015	\$2,416	14%	\$801	29%	Gross U.S dollar volume increased 8% Y/Y; international gross volume increased 15% Y/Y.
 FirstData	10Feb2015	\$947	5%	\$12	n/a	Core merchant acquiring revenues are up 3%, merchant products down 1%.
 globalpayments	8Jan2015	\$697	10%	\$75	19%	Raised annual earnings growth estimates up from 13%-15% to 15%-17%
 vantiv	12Feb2015	\$318	41%	\$69	64%	Excluding recent acquisitions, reported net revenue growth of 8% Y/Y.
 Heartland PAYMENT SYSTEMS	13Feb2015	\$188	26%	\$21	12%	Reported annual organic net revenue growth of 8% in 2014.
 TSYS	27Jan2015	\$108	(2%)	\$83	26%	Quarterly merchant services revenues were down 2% Y/Y.

Acquirers reported a wide range of revenue growth Y/Y, which in some cases includes the impact of recent acquisitions. Excluding acquisitions, the acquiring industry broadly reported organic Y/Y net revenue growth of 5% - 10% in the U.S. with most international markets posting growth that outpaced the U.S. market. Individual institutions differed substantially from the averages.

Trends in Payments Security

EMV, encryption, and tokenization continue to receive focus from acquirers and networks. There are still adoption challenges, and many initiatives are focused on merchant education.

Earnings Call Excerpts:

- “We’re seeing more terminals starting to be sold. I would tell you the small merchant today is not as educated on EMV. So when our ISO partners or our direct channels are going in and talking to them, it’s about education.” -Vantiv
- “We are actively engaged with our merchant community to educate and provide support to ensure they understand the impact of the fast approaching October liability shift deadline. As of this date, approximately 45% of our direct merchants have EMV-capable terminals in place.” -TSYS
- “What you’ll see from [the integrated payments line of business, OpenEdge] is the consolidated roll out of the security that includes EMV tokenization as well as point-to-point encryption into one bundled security solution, which really is the way to think about security particularly as you’re dealing with small to medium-sized merchants around the country.” -Global Payments
- “Our strategy is one that we believe will significantly improve current POS technology. It’s widely acknowledged that hackers have exploited the security weaknesses of many integrated systems to gain access to card information. We’ve greatly reduced this vulnerability with encryption and out of scope technology.” -Heartland

Focus on Sales Channels

Strategic sales channels, such as ISV and dealer partnerships, continue to outperform traditional ISO sales channels. Heartland formed a new business unit, Heartland Commerce, consolidating its POS solution assets. Feet-on-the-street oriented sales channels may find growth opportunities educating small and medium sized businesses on the EMV liability shift.

Earnings Call Excerpts:

- “Some [ISOs] are growing very strong who have niche markets. And some of them who are more generalist are feeling some pressure in general with integrated or other solutions.... I think EMV terminal upgrades over the next probably 18 months will be helpful to the entire ISO group.” -Vantiv
- “By virtue of our POS acquisitions, we’ve gained several dealer networks, augmenting the significant success we achieved in signing over 175 dealers.” -Heartland
- “Heartland Commerce represents a natural and logical extension of our basic payments business into a market we think offers outstanding growth potential...We are in the process of consolidating all of our POS technologies...under the evolving Heartland Commerce umbrella. As presently constituted, Heartland Commerce would have over 90,000 POS locations and \$30M in annual revenue, primarily in the hospitality industry.” -Heartland
- “The merchant bank channel continues to be our fastest or highest growth channel within our group of high growth channels.” -Vantiv
- “Our E-Commerce channel also continues to perform better than we expected which has contributed to our European top line growth.” -Global Payments

M&A Activity

Acquirers continue to evaluate acquisition opportunities that align with strategic interests but remain selective. In this most recent quarter Heartland continued its push into retail POS with the acquisitions of Dinerware and pcAmerica, while impairing recent early-stage investments.

Earnings Call Excerpts:

- “We couldn’t have asked for a more ideal backdrop against which to announce our new strategic acquisitions in the point of sale market. pcAmerica and Dinerware had 55,000 new locations that will further scale our existing cloud based POS solutions and provide a solid platform to support our aggressive growth initiatives.” -Heartland
- “...As such related [POS] development efforts at Leaf would be redundant, and we determined it was best to hold these efforts - necessitating the recognition of impairment charges related to the investment ... Separately, during the 4th quarter we determined that our investment in TabbedOut was impaired.” -Heartland
- “We’re happy with the pace of integration [of recently acquired PayPros and APT]. More to come and we’ll feed in those integration benefits over time over the next year or year two.” -Global Payments
- “In terms of location of the pipeline, we’re opportunistic. So as we’ve said before, we’ve got to find something that’s for sale with a good partner with attractive returns to our shareholders ... So we’re very focused on the IRR.” -Global Payments
- “In December, we acquired the payment gateway services business of Transaction Network Services. That deal gives us the ability to expand our payment gateway to the U.S. and Mexico and to position ourselves more competitively around the world.” -MasterCard

Company	Target	Announced	Target Description	Purchase Price (\$M)
Heartland Payment Systems	Dinerware	Feb 2015	Integrated Payments (food service)	n/a
Heartland Payment Systems	pcAmerica	Feb 2015	Integrated Payments (retail)	n/a
MasterCard	Transaction Network Services	Nov 2014	Gateway	n/a
Heartland Payment Systems	xpient	Oct 2014	Integrated payments (food service)	\$30
Global Payments	FIS	Oct 2014	Integrated payments (gaming)	\$237
Global Payments	eZidebit	Sep 2014	Integrated payments (Australia, NZ)	\$275
Heartland Payment Systems	Leaf	Aug 2014	Tablet-based POS Solution	n/a
First Data	gyft	Jul 2014	Digital gift card platform	n/a
Heartland Payment Systems	TouchNet	Jul 2014	Integrated payments (education)	\$375
Heartland Payment Systems	MCS Software	Apr 2014	Integrated payments (education)	n/a
Vantiv	Mercury	May 2014	Integrated payments	\$1,650
MasterCard	PinPoint	Apr 2014	Loyalty and rewards (Asia Pacific)	n/a
MasterCard	C-SAM	Feb 2014	Mobile wallet software developer	n/a

Discussion of International Markets

Many acquirers and networks are looking outside of the U.S. for growth opportunities. Latin America, and specifically Brazil, was highlighted as an opportunity by multiple acquirers.

Earnings Call Excerpts:

- “Late last year we began processing for merchants in Brazil. While it’s still early days, we remain optimistic about our ultimate presence in this lucrative and fast-growing market.” - First Data
- “If I had all my wishes kind of come true, we would be expanding presence in Latin America... We have our business that we

started about a year-and-a-half ago in July of 2013 in Brazil. We’re currently up to 6,500 merchants...we’ve also talked a lot about other Latin American markets like Mexico, given its size and its prominence, that we’re not in directly, that we really wish we could be.” -Global Payments

- “In the Middle East and Africa, we signed a number of new business agreements in the quarter. That should help us increase our credit, debit, commercial and prepaid businesses in countries such as Nigeria, Tanzania, Rwanda, Jordan, Kuwait and the UAE over the course of 2015.” -MasterCard

What to Watch

The impact of Apple Pay is still top of mind for networks. China recently announced that it would open its market to competition, but few details have emerged.

Continued Focus on Apple Pay

- “Since Apple Pay was announced in September we had 500 different merchant and developer leads we are working with on supporting Apple Pay and bringing it to their customers.” -Visa
- “We’re very excited about what Apple is doing. We think it’s a very elegant [tokenization] solution that we are thrilled with our participation in, but we want to enable as many scalable solutions that have wonderful customer interfaces that adhere to the highest security standards.” -Visa

- “The remaining opex growth of 12% was primarily driven by some opportunistic spend, such as adding [marketing] spend around our Apple Pay and Priceless initiatives.” -MasterCard

Opening of the Chinese Market

- “We continue to work with our Chinese partners and meet with the government, but relative to when the market will open, what the rules will look like, and how meaningful it would be, we really don’t know.” -Visa

Industry Reminder that Credit Risk Always Exists

- “Processing and servicing cost were up 35% in the quarter. 22% was due to a loss on chargebacks from a single merchant that declared bankruptcy in the 4th quarter.” -Heartland