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- Q4 2014 First Data Corp Earnings Call

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CORPORATE PARTICIPANTS

Rich Wilhelm *First Data Corporation - Director of IR*

Himanshu Patel *First Data Corporation - EVP, Strategy, Planning & Business Development*

Michael Neborak *First Data Corporation - EVP & Director of Finance*

PRESENTATION

Operator

Good morning, ladies and gentlemen. Welcome to the fourth-quarter 2014 First Data financial results conference call. My name is Vanessa, and I will be your operator for today's call.

(Operator Instructions)

Please note this call has been pre-recorded, and there will be no question-and-answer session. As a reminder, this conference is being recorded for replay purposes. I would now like to turn the presentation over to Mr. Rich Wilhelm, Director of Investor Relations of First Data. Sir, you may begin.

Rich Wilhelm - *First Data Corporation - Director of IR*

Thank you, operator, and good morning, everyone. I would like to welcome you to our fourth-quarter earnings call. Our Executive Vice President of Strategy, Planning & Business Development, Himanshu Patel; and Executive Vice President and Director of Finance, Michael Neborak, will lead the discussion of the fourth-quarter and full-year 2014 financial results.

Himanshu and Michael will be referencing a slide presentation during their prepared remarks. A copy of the slide presentation, as well as our earnings release and supplemental analyst schedules, are available on our website at investor.firstdata.com.

I would like to remind you that any forward-looking statements made during today's call are subject to risk and uncertainty. Factors that could materially change our current forward-looking assumptions are described in today's presentation and in our Form 10-K and subsequent reports on file with the SEC.

We also will discuss items that do not conform to Generally Accepted Accounting Principles. We reconcile those measures to GAAP measures in the appendix in this presentation and as part of our quarterly results press release. With that, I will hand the call over to Himanshu Patel.

Himanshu Patel - *First Data Corporation - EVP, Strategy, Planning & Business Development*

Thank you, Rich, and good morning, everyone. Before I hand it over to Mike to go through the numbers in detail, I wanted to first step back and reflect on the year. It was a historic year of transformation at First Data.

In 2014, the Company introduced innovative solutions for our merchant and financial institution clients, rebuilt our Financial Services business, expanded into new geographies and significantly increased the depth of our talent. 2014 also marked a clear-cut improvement in the Company's financial profile. For the full year and for Q4, we saw the benefits of improving top-line growth, positive operating leverage and capital structure improvements.

For the full-year 2014, adjusted revenue and adjusted EBITDA grew 4% and 10%, respectively, on a constant currency basis, and operating profit grew 28%. And for the first time since First Data's 2007 LBO, we had a profitable quarter, with net income of $12 million in Q4. And lastly, of course, we were very pleased with the substantial improvements we made to our capital structure over the past year, including the $3.5 billion private placement this past summer and the full pay down in December of the HoldCo PIK notes.

Let me spend a few more minutes on some of the business progress we made last year. On the product front, 2014 saw multiple innovative new products being launched by First Data.

We rolled out Clover Station, our tablet-based integrated point-of-sale solution. Clover combines cutting edge functionality and a unique open architecture, which, in less than a year from launch, has quickly attracted a long list of innovative developers who realize the value of being present on the industry's leading tablet POS platform for small and medium sized businesses.

We also rolled out Insightics and Perka to our merchants, two cloud-based applications that work on Clover and off Clover. Insightics is an analytics software that transforms payment data into actionable intelligence for SMBs, while Perka is a mobile loyalty app that helps SMBs drive repeat traffic.

And in the second half of last year, we rolled out recently acquired Gyft, our virtual gift card platform that allows businesses of all sizes to distribute digital gift cards and allow consumers to quickly and securely purchase, upload and send gift cards to nearly anyone. And in early 2015, we'll be rolling out Clover Mobile, which gives businesses all the great functionality of Clover Station, but with the freedom of being entirely untethered from the countertop, whether it be within their store or on the road.

In addition to these great new products, First Data entered into a host of collaborations and partnerships with technology and payment industry partners that we believe will further differentiate us to our customers. We led the industry with landmark collaborations with Visa and MasterCard to accelerate EMV adoption, with American Express to roll out its new US acceptance program called OptBlue. With VeriFone to help US merchants reduce exposure to payment data breaches with the help of First Data's data protection solution, with Apple to help launch Apple Pay to both issuer and acquiring customers. And announced just last week a global alliance with Capgemini to broaden the leading position of First Data's world-class international issuing platform known as Vision.

On a related note, also worth noting, we now have nearly 100 employees on the West Coast, allowing us to stay close to payment start-ups and attract high-quality engineering talent. And lastly, 2014 also marked our entry into the Brazilian acquiring business. 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.

Looking forward to 2015, while we do not provide earnings guidance, we do expect our business to continue to grow this year. We plan to launch additional new products, deepen the penetration of recently launched products, and opportunistically improve our capital structure when it makes sense.

We anticipate this to occur within the backdrop of a good economic picture, particularly in the United States. Indeed, we are optimistic on US consumer spending, given improving labor markets and the recent fall in gas prices. Although some of this benefit will be tempered on our financials by the strengthening dollar through growing adverse currency translation.

With that, I'll hand it over to Mike to cover the financials in detail.

Michael Neborak - *First Data Corporation - EVP & Director of Finance*

Thanks, Himanshu, and good morning, everyone. I'm going to jump right into the quarterly results on slide 4. Consolidated GAAP revenues were $2.9 billion, up 3% on higher revenue from merchant and card services, and an increase in product sales and other. And as Himanshu said, this was the first time in 29 quarters we've shown positive net income -- the fourth quarter net income of $12 million -- vastly improving on the loss of $123 million in the prior-year period.

Driving this increase was, first, a material improvement in operating profit, which increased 17% to $420 million. Second, a reduction in interest expense. And third, positive other income, which was favorably impacted by foreign exchange valuations.

As you know, we manage the business using adjusted revenue, which excludes certain items, including debit network fees, and conforms the presentation for other items. We believe this presentation is more meaningful in terms of understanding our performance, margins and related operating metrics.

Adjusted revenue for the fourth quarter was $1.8 billion, up 4% versus the prior-year period, with continued growth posted in our Financial Services and International segment. On a constant currency basis, revenue grew 6%. Adjusted EBITDA was $712 million, up 6%, and up 8% after adjusting for currency.

Expenses were up 2%, or 5% on a constant currency basis, as we continued to invest in the business, such as in our merchant suite of products and our expansion in Brazil. And even with this continued investment in the business, margin rose 1 percentage point to 39%.

Now let's move into the segment performance, starting with Merchant Solutions on slide 5. Revenues were $947 million, up 1% compared to the prior-year period, while EBITDA was down 2% to $426 million. Margin was 45% for the quarter, also down 2% versus the prior-year period, as expenses increased $24 million on costs related to equipment and plastic sales, as well as merchant suite investments, as we continued to provide our clients with solutions to help them grow their businesses.

Now let's decompose our 1% revenue growth in Merchant Solutions. In core merchant acquiring, which accounts for the largest majority of the segment, revenues were up 3%, as volume growth and revenue from our merchant suite were partially offset by lower spreads. And the remaining components of the segment -- prepaid, equipment and check services -- were down 1%.

Prepaid revenues were down low-double digits, due to a $12 million negative impact from the EFS divestiture. Please note that the prepaid business continues to grow, as our money network payroll cards benefit from increased activity and usage.

Equipment revenues were up double digits, as an increase in hardware sales was complemented by growth in our leasing business, driven by portfolio growth. And finally, revenues in check processing were down high-single digits, as check volumes declined again, due to the secular shift due to electronic payments.

Now turning to the results of the Financial Services segment on slide 6. Financial Services continued to show strong performance, as revenue increased 8% versus the prior-year period, a record since going private in 2007. We are continuing to see benefits of new business, solid growth in volumes, as well as growth in network revenues, driven by transaction growth and pricing.

Expenses were flat versus last year, and combined with solid top-line growth, resulted in a 52% EBITDA margin, the highest since the Company went private, and up 4 percentage points over last year. EBITDA in the fourth quarter was a post-LBO record $201 million, up 17%.

Drilling into the Financial Services revenue components, processing revenues were up high-single digits versus the prior-year period on a continued increase in active credit and retail card accounts on file, new business wins and increased debit issuer transactions. Output services showed strong growth versus the prior year in both print and plastics, with print up on increased volume and new business, and plastic showing growth, primarily on new business and increased EMV volumes. We have a solid EMV card production pipeline, and expect to see continued momentum throughout 2015.

Now to slide 7 for a review of International. Reported revenues for the quarter were up 4%, or 13% after adjusting for currency, continuing to show solid growth year over year. Within the major businesses, on a constant currency basis, merchant acquiring revenues were up 14% on volume growth, higher terminal sales and a portfolio sale in EMEA. Issuing revenue grew 12%, due to organic growth in new card portfolios.

EBITDA was $154 million, up 15% compared to the prior-year period, and up 23% in constant currency. This is the highest recorded EBITDA for the International segment since the Company went private.

Despite an adverse tax outcome and an unfavorable settlement funds revaluation, both in Latin America, International expenses were slightly favorable to the prior-year period, primarily due to currency tailwinds stemming from the strong dollar. Margin for the fourth quarter was 33%, up 4 percentage points versus the prior year.

Now let's look at revenue growth on a constant currency basis in each of the regions of our International business. Revenue in EMEA, our largest region, was up 13% on solid transaction growth in acquiring, and the continued year-on-year benefits of new card portfolios in the issuing business.

This quarter also benefited from a portfolio sale, impacting revenue growth favorably by 5%. APAC revenues were up 5%, as strong volume growth in acquiring was offset by continued declines in our Australian ATM business. Revenues in Latin America and Canada were up 21% on transaction growth in terminal sales, as well as price inflation in Argentina.

Slide 8 provides a roll-forward of cash. We ended the quarter with $358 million in cash and cash equivalents, and available liquidity of $1.1 billion. We had $10 million in borrowings outstanding on the revolver.

Cash interest payments were $220 million, approximately $81 million less than the prior-year period, primarily due to lower interest payments and a timing shift of coupon payments related to the pay down of debt as a result of our equity raise in July. For 2015, we anticipate cash interest payments of approximately $1.6 billion, down $132 million compared to 2014. Our capital expenditures for the quarter totaled $157 million, and $567 million for the full year, versus $379 million for the full-year 2013, reflecting investments in data centers and hardware, along with new products and security functionality.

Now I'd like to take a few minutes to discuss First Data's capital structure on slide 9. As Himanshu mentioned, throughout the year we made significant improvements to our capital structure, most recently redeeming, in December, the remaining $232 million of principal balance of the 14.5% HoldCo PIK notes.

With the actions we took this year, we reduced total debt by $3.3 billion, including HoldCo, improving net leverage by 1.3 turns and significantly reducing annual cash interest payments. We have a weighted average interest rate of 7.4% across our debt.

As of December 31, approximately 80% of our debt is fixed rate or swapped to fix rate, providing a measure of protection if interest rates begin to rise. Continuing to strengthen the Company's capital structure and liquidity position paves the way for us to invest in and provide the solutions that enable our clients to grow their businesses.

Lastly, I want to take a few minutes to walk through the full-year numbers on slide 10. For the full year, consolidated revenues were $11.2 billion, up 3%, or 4% after adjusting for currency. Full-year operating profit was $1.4 billion, up 28% versus the prior year.

Adjusted revenue and adjusted EBITDA for the full year were $7 billion and $2.7 billion, respectively, with adjusted revenue up 3% and EBITDA up 9%. On a constant currency basis, revenue was up 4% and EBITDA up 10% for the full year.

And finally, we look forward to 2015 and beyond to continue to build upon the momentum we've seen over the past year. And with that, I would like to thank you for joining us today. Have a great day.

Operator

Thank you for your participation in today's call. This concludes the presentation. You may now disconnect.
