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VNTV - Q2 2015 Vantiv Inc Earnings Call

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PRESENTATION

Operator

Good day, and welcome to the Vantiv Q2 2015 earnings conference call. As a reminder today's call is being recorded. At this time I would like to turn the conference over to Mr. Nathan Rozof, Senior Vice President of Investor Relations.

Nathan Rozof - Vantiv Inc. - SVP of IR

Good morning, everyone, and thank you for joining us today. By now everyone should have access to our second-quarter 2015 earnings release, which can be found at Vantiv.com, under the Investor Relations section. During today's call Charles Drucker will review Vantiv's second quarter operating performance. Mark Heimbouch will then review our financial results and address our outlook for the remainder of the year.

Throughout this conference call we will be presenting non-GAAP and pro forma financial information, including net revenue, adjusted EBITDA, pro forma adjusted net income, and pro forma adjusted net income per share. These are important financial performance measures for the Company, but are not financial measures as defined by GAAP. Reconciliations of our non-GAAP pro forma financial information to the GAAP financial information appear in today's press release.

Finally, before we begin our formal remarks, I need to remind everyone that our discussion today will include forward-looking statements. These forward-looking statements are not guarantees of future performance and, therefore, you should not put undue reliance on them. These statements are subject to numerous risks and uncertainties that could cause actual results to differ materially from what we expect. Please refer to the



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forward-looking statement disclosure in today's earnings release and in our periodic filings with the SEC. Additional details concerning our business risks and the factors that could cause actual results to materially deviate from our forward-looking statements can be found in our annual report on form 10-K under the headings, Risk Factors and MD&A, and in our other filings with the securities and exchange commission, which are available at SEC.gov.

Now I'll turn the call over to Charles Drucker, our CEO. Charles?

Charles Drucker - *Vantiv Inc. - CEO*

Thank you, Nate, and thanks to everyone for joining us this morning. This was another great quarter for Vantiv. In addition to delivering strong financial results and raising our guidance for the full-year, we were also successful in a number of areas. First, our high growth channels continue to out perform and win market share, growing above 20% on a pro forma basis during the second quarter. Second, we continue to successfully win new clients and gain market share, including the recent signing of the United States Postal Service and Capital One Bank. And third, in connection with our strategy of allocating capital, we recently terminated more TRA liabilities, which Mark's going to describe in more detail. In light of these successes, I'm going to start the call today by reviewing our operating performance during the second quarter, including our competitive position and recent key wins. Mark will then review our financial performance, including our increased guidance for the year and TRA termination.

Starting with operating performance, we continue to build on our strong momentum as net revenue grew 28% to \$424 million, and pro forma adjusted net income per share increased to \$0.56, both exceeding expectations. Our net revenue upside was primarily driven by growth in the Merchant segment, up 37% year-over-year. Organic growth within the Merchant expanded again this quarter, reaching 11% on a pro forma basis, reflecting strong execution in our core business, as well as our ability to successfully expand into high growth channels and verticals. Our Financial Institutions segment continues to deliver consistent trends, with net revenue growth of 1% and transaction growth of 6%, and EMV remains an opportunity for improving growth over the next few quarters. Company-wide, we continue to build on our core advantages and our consistently winning market share. As the number two acquirer by transaction, our scale sets us apart. We process for merchants and financial institutions of all sizes, large and small, including processing for approximately one-third of the largest merchants in the country, and we continue to win more than our fair share of new business of these leading clients. We process for merchants both online and off-line and across omni-channel environments, add value-added services for card in our present transactions, are a key differentiator for us and contribute to the ability to win market share. We believe that our breadth and diversity of our distribution channel is also unique. We have strong presence in all major sales channels, including direct, eCommerce, integrated payment, merchant bank, and ISO. Many of our peers have strength in a handful channels, but few of them can claim capabilities in all channels, particularly our leading position in integrated payments.

In addition to our leading competitive position, we are leveraging capabilities from across the Company to create compelling solutions for our clients. Solutions that are generating strategic new wins. We have described on past calls how we are leading omni-channel capabilities and suite of security services that differentiate the marketplace. These play an important role for the United States Post Office when they selected us to provide them with a full suite of omni-channel payment solutions. Our solutions will effectively support the scale and functionality required by a large number of retail locations and USPS.com. This is another example how the strength of Vantiv's omni-channel solutions, innovative capabilities, and service leaderships are helping us win important new clients. We are also winning within our fastest growing merchant channel, based upon a unique strengths from serving both the merchants and financial institutions. This quarter we won an important new referral relationship with Capital One Bank, and we will provide our full suite of merchant solutions to the bank's commercial customers. We're ramping up our sales force to meet the demand, significantly expanding our distribution and potential for growth within the merchant bank channel.

Meanwhile, our confidence in the integrated payment channel continues to grow, both in terms of sustainability of growth, as well as our ability to win market share. Organically within the channel continues to outperform, growing by more than 20% in the second quarter. Growth in the integrated payment channel is coming from the secular adoption of technology at the point-of-sale and continued growth in a number of our partners. We are also creating unique solutions to enhance our growth by combining Vantiv's scale and comprehensive suite of services with Mercury's integration capability, as well as a unique approach to channel management. In addition, our EMV and security solutions are helping us to further distance ourselves from the competition. For example, we have developed leading capabilities to support the developers of customer facing technology, which is popular with large merchants, including pay at the table solutions within the restaurant vertical. Our technology and



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integration enables pay at the table solutions to accept EMV transactions, which resolve the key issue for a restaurant in a chip and pin environment, where the customer needs access to a terminal equipped with a pin pad at the table in order to complete the transaction.

The EMV deadline is fast approaching, and security and EMV are top priorities for our clients. They are passionate about protecting their customers data. This creates a catalyst for us to deliver additional value for our clients, and we are implementing our suite of security services, including EMV, encryption, and tokenization, at new and existing clients. Our systems are ready. We are already processing EMV transactions today and helping our merchants to implement and certify for EMV, including many of our largest clients. We are also working with the ISV to help them deploy pre-certified EMV solutions, all in an effort to make the liability shift deadline as seamless as possible. Our consultative approach, as well as the way we execute for our clients, makes us more embedded and reinforces our value proposition to our clients.

In conclusion, this was another great quarter for us. It highlights the strength of our competitive position and demonstrates how we are winning, differentiating ourselves, and gaining market share. To that, then, I'd like to thank all of our employees for their hard work and dedication. Their efforts have positioned Vantiv as the leader in the payments industry. With our new wins and unique solutions, I'm excited about the we continue to build momentum in the market and about where we are going to take this Company in the future.

I will now hand the call over to Mark, who will review our financial performance more detail, describe our plans for strategic capital allocation, and address our outlook for the rest of the year. Mark?

Mark Heimbouch - Vantiv Inc. - CFO

Thanks, Charles, and good morning, everyone. As Charles discussed, we had another excellent quarter, that revenue grew 28% to \$424 million, primarily driven by continued strong growth within our Merchant Services segment. In addition, pro forma adjusted net income increased 22% to \$113 million, and pro forma adjusted net income per share increased 19% to \$0.56. Our Merchant segment generated net revenue growth of 37%, principally due to a 23% increase in transactions and a 12% increase in net revenue per transaction. On an organic basis, that revenue growth within the segment was 11%, exceeding our expectations and increasing our confidence for the full-year. Performance in our Financial Institution segment was consistent with expectations with net revenue growth of 1% and transaction growth of 6% year-over-year. Total operating expenses, including sales and marketing, other operating costs in G&A increased by 29% in aggregate, primarily due to the Mercury acquisition. Other operating costs in G&A declined as a percent of net revenue, and adjusted EBITDA margin continues to improve as we realize synergies. Having now officially marked the one-year anniversary of the Mercury acquisition, I'm pleased to report that the integration is going very well. Mercury continues to exceed our business case, and we remain on track to achieve \$15 million to \$20 million in cost synergies during 2015. Appreciation and amortization expense, excluding the impact of amortization of intangibles related to acquisitions, was \$20 million, consistent with the past several quarters. And net interest expense increased to \$26 million, up year-over-year, but, again, consistent with the past several quarters, as well as with the expectations given the Mercury acquisition.

Moving on to capital allocation. Since the Mercury acquisition, we have de-levered from 4.9 times to 3.7 times on a net debt basis, and the business will continue to de-lever given the combination of adjusted EBITDA growth and debt amortization. While we have focused on de-levering following the Mercury acquisition, now that we have reduced leverage to levels closer to our historical ranges, we can also focus on our historical priorities, which have remain unchanged and include first, investing for growth and second, returning excess capital to shareholders. As Charles announced, we recently terminated TRA liabilities associate with the Mercury acquisition. As you're aware, the termination of the TRA results in significant returns, which generate meaningful earnings accretion. We expect the termination to result in \$0.05 of accretion to earnings per share in 2015, increasing from \$0.05 to \$0.08 of earnings per share in 2016, and ultimately growing to \$0.15 of earnings per share in 2019 and beyond. These benefits continue for approximately 15 years. We also expect that there will be other opportunities in the future to terminate additional TRAs owned by Fifth Third Bank. In addition to terminating TRAs, we have the ability to utilize \$275 million remaining under an outstanding share repurchase authorization, which is not included in our revised guidance that I'll get to in a minute.

Now turning to our outlook for the remainder of 2015, our strong financial performance year to date, including very strong growth within our high growth channels, increases confidence and our full-year expectations. For the third quarter, based on current trends and new business activity, we expect to generate net revenue of \$410 million to \$415 million, representing growth of 8% to 9%, and we expect pro forma adjusted net income per share of \$0.54 to \$0.56. For the full-year, we now expect net revenue of \$1.625 billion to \$1.645 billion, representing growth of 16% to 17%,



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and we expect pro forma adjusted net income per share of \$2.15 to \$2.20, representing growth of 15% to 18%. The outlook does include \$0.05 of accretion associated with the termination of the TRA that I mentioned earlier. Our net revenue expectations for the third quarter are organic now that we have lapped the Mercury acquisition, and our net revenue guidance for full year assumes organic net revenue growth of 7% to 10% for the total company, or 9% to 11% for the merchant segment.

I'll now turn the call back to Charles for closing comments. Charles?

Charles Drucker - *Vantiv Inc. - CEO*

Thanks, Mark. To conclude, we delivered another strong set of results this quarter. I am confident in our ability to win market share and drive strong results for our shareholders. I believe we have one of the best competitive positions within the US payment industry, driven by our capabilities to serve merchants large and small, online and off-line, and across all the major distribution channels. We are winning clients by delivering innovative new solutions and leveraging the best capabilities across our Company. We continue to integrate Mercury in a deliberate and strategic manner in order to win new business relationships, as well as expand existing ones, by leveraging our full suite of capabilities and cross selling our comprehensive suite of service. And finally, we continue to execute on behalf of our shareholders by harvesting cost synergies to increase margin and strategically allocating capital to drive returns.

Ol want to thank everyone today for joining this morning's call, and if operator, if you would open the call for calls.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Darrin Peller, Barclay's Capital.

Darrin Peller - *Barclays Capital - Analyst*

Thanks guys, it looks like trends are going well, so congrats on that. Just want to start off first with your guidance. On the EPS side, I know you raised by \$0.05, and just want to really understand if there's anything on the expense side that is coming in a little above expectations that would've accounted for not raising more? Just given operationally you seem like you're beating, obviously, without just the TRA.

Mark Heimbouch - *Vantiv Inc. - CFO*

Hey John, it's Mark. So actually the businesses are performing extremely well, particularly on the merchant side. There is some additional investment in the second half of the year, and a big driver of that, actually, is, as you guys saw, we signed an agreement with a large financial institution, Cap One Bank. So standing up of the sales force to support that channel is leading to a little bit more expense without all of the revenue, so that will contribute to additional revenue growth, particularly going into 2016. The second thing is, we are taking advantage of what we see occurring in the market in terms of security and EMV, and that's leading to some market share gains. It's also leading to some additional channel costs, as we're pursuing that a little bit more aggressively. Those are, I think relatively short term in nature, and as we look, typically given the high-growth, long-term client relationships and think forward to 2016, those investments should contribute to expansion.



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Darrin Peller - Barclays Capital - Analyst

Yes, no, that's great to see with Capital One, in particular. Obviously, I think that's the largest thing I think you guys have signed. On that note, number one on the merchant side, if you could just comment on what same-store sales, I'm not sure if I missed that or not, were in the quarter? And then, Capital One as the example here, but the merchant bank referral channel, how is that growing now? I know last quarter or two, it's been growing substantially and is a very big boost to your overall merchant growth rate. It looks like with Capital One that very well could continue now, so can you give us a little more color on the growth trajectory there?

Mark Heimbouch - Vantiv Inc. - CFO

Yes, just two things you talked about there, same-store sales. Same-store sales trends have been very consistent now, really for a number of quarters, and you've heard us talk about it in the mid-single digits. That's what we saw again for this quarter, so same-store sales trends, 6.5%, and pretty consistent across-the-board. And pretty stable, as you've heard us say now for the last few quarters. With respect to the merchant bank channel, it is experiencing tremendous growth. In fact, I think it's more than doubling over the past couple of years. It is, by far, one of our highest growth channels. So with revenue expectations, given relationships like Capital One, as well as a solid pipeline, we still remain highly optimistic on the channel.

Charles Drucker - Vantiv Inc. - CEO

Our pipeline is strong in the merchant bank and we're continuing to win, and these banks and financial institutions we're bringing on, they're very hungry to expand in the merchant area, so it's exciting partnerships that we're working with.

Darrin Peller - Barclays Capital - Analyst

Yes. Who was Capital One with before, if anybody?

Charles Drucker - Vantiv Inc. - CEO

We'll come back to you with that one off-line.

Darrin Peller - Barclays Capital - Analyst

All right, well great job, guys, thanks.

Mark Heimbouch - Vantiv Inc. - CFO

Thanks.

Operator

David Togut, Evercore ISI.

David Togut - Evercore ISI - Analyst

Thank you, good morning. Sounds like you're seeing accelerated growth from integrated payments, you indicated over 20% in the quarter. Could you drill down a little bit into the drivers of that growth, and to what extent is that sustainable beyond Q2?



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Mark Heimbouch - Vantiv Inc. - CFO

Hey David, its Mark. We've actually, just to be clear, we've seen our business combined on a pro forma basis. I remind you that there was core business to the Vantiv platform prior to the acquisitions. The acquisitions being Element and Mercury. The businesses combined have been growing pro forma organically over 20%, so continuing to exceed expectations.

Charles Drucker - Vantiv Inc. - CEO

The businesses are doing well. They continue to win developers and dealers. They do -- that team does an extraordinary job in taking care of the client, and then helping the clients advanced their software products. So we'll continue to see the success there. I think as we put our companies together, and they continue to get -- we all get comfortable together, the leadership at Mercury, with Matt Taylor, have really tremendously leaned forward to help the clients navigate through EMV and navigate on how to grab business. We continue to be excited about that and see a long runway for that business, and very optimism about where we're taking that.

David Togut - Evercore ISI - Analyst

Any specific call outs on integrated payments, in terms of which verticals you're seeing the highest growth, which verticals you're targeting for improvement?

Charles Drucker - Vantiv Inc. - CEO

You know, the exciting part about this, it's in the continued areas that Mercury and Element were good in, and we're getting more market share in those areas, but right now, we're developing other verticals that they can go into and those things, we're spending some time in developing new verticals and that will help sustain our growth as we move forward. But it's really in our traditional verticals that we continue to execute and take more share.

David Togut - Evercore ISI - Analyst

Thank you.

Operator

Jason Kupferberg, Jefferies.

Jason Kupferberg - Jefferies LLC - Analyst

Morning guys, so just drilling in on the revenue guidance raise for the year, which, obviously, seems attributable to the Merchant segment. If you break that down further into the different channels within Merchant, Integrated, the banks, eCommerce, the direct piece and the ISO piece, would you say that the higher forecast is attributable to more so one in particular channel, or is it more broad-based than that?

Mark Heimbouch - Vantiv Inc. - CFO

I think that it's fairly broad-based but some of the trends are consistent. The contribution of our high growth channels, including eCommerce, including Merchant bank, and including integrated payments, are continuing to over-perform, and so that's leading to some upside. In terms of



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our more traditional channels, we're still continuing to see very solid low-single- to mid-single-digit rates of growth in some of the more traditional channels, so those trends continue. Our high-growth businesses continue to win and continue to take market share.

Jason Kupferberg - *Jefferies LLC - Analyst*

Okay, and then just following up on some of your comments around capital deployment, obviously you still have the big buyback authorization that you highlighted, and I understand that's not baked into guidance at all. But, as we think about the second half of the year, given how much the leverage ratio has come down, should we be thinking, at least, about some nibbling against that buyback? Or is it really more dependent on whether or not anything emerges from an investment opportunity perspective?

Mark Heimbouch - *Vantiv Inc. - CFO*

We have to keep our eyes open for investment, but I think the point we are trying to convey on the call was we are now nearing historical rates of leverage, we continue to de-lever. So we are at the point in time of being comfortable in terms of deploying the capital.

Jason Kupferberg - *Jefferies LLC - Analyst*

Okay, good to hear. Thanks guys.

Operator

Dan Perlin, RBC Capital Markets.

Dan Perlin - *RBC Capital Markets - Analyst*

Thanks, guys, just a couple things. On the FI side of the business, I just wanted to get an updated thought process of what you're seeing there. I mean, Merchant was, obviously, very strong this quarter, but FI keeps that growth rate muted a bit. I'm just wondering what you're seeing there in terms of competition, price compression, because the transaction's still holding up pretty well.

Charles Drucker - *Vantiv Inc. - CEO*

The FI business continues to be in a steady state. We're seeing the consistency in the low-single digits. We have a good amount of small mid-sized banks, and we believe that EMV opportunities for us are more in the back half of the year and into 2016. So what I've been seeing in the market is, the very large issue is being very aggressive in reissuing cards, and the small and mid-sized banks are still in a wait and see, as far as through reissues. So we think that business has opportunity in the second half of the year. We're still in the low-single-digit type of area, but actually, it's been consistent for us. Nothing has dramatically changed in pricing, our attrition rates have remained constant. The compression that we may see in the business has remained at historical levels, and we are winning banks. When we win banks these things take a while. The sales pipeline is very strong, but they're typically six-month implementations that happen, but that business has been very steady for us.

Dan Perlin - *RBC Capital Markets - Analyst*

Okay, so the call out is the second half is EMV driven on re-issuance of cards, and then the incremental wins maybe just have to layer in, in 2016, is that a fair assessment?



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Charles Drucker - *Vantiv Inc. - CEO*

I believe so. I think we'll see some of the benefit of some of the sales in the first half of the year, but that's how this business moves. The back half of the year, with card re-issuance that the small- or mid-sized banks have probably waited closer to the liability shift than some of the large financial institutions in the country.

Dan Perlin - *RBC Capital Markets - Analyst*

Got it. And then, I didn't hear then, and if you guys have said it already you don't have to repeat it, but the revenue per transaction and merchant was up a lot, which is fantastic to see, and I'm just assuming that is all a function of incremental transactions via Mercury and maybe other alternative channels? And then I had one other follow-up.

Mark Heimbouch - *Vantiv Inc. - CFO*

Actually, you're right. To the extent we're seeing the higher growth and the high-growth verticals, or channels, contributing to that. But actually I was going through on a channel by channel basis and seeing really pretty strong support trends in terms of revenue per transaction across the business. As well, I think it's important to point out value-added services including Security Solutions are contributing to pretty strong pricing trends, or revenue per transaction trends.

Dan Perlin - *RBC Capital Markets - Analyst*

Okay, so the market's willing to bear a slightly higher price point when they're adding security around it, and that's the appetite in the market right now? Is that what you're saying?

Charles Drucker - *Vantiv Inc. - CEO*

Like we said, the security products we put on are incremental, and we're bringing value to clients. Whenever you bring value, the clients are open to paying for that value bringing across, and our security products and then encryption and tokenization are starting to layer in.

Dan Perlin - *RBC Capital Markets - Analyst*

Is there any reason to believe that the third quarter's revenue-per-transaction, for some reason, wouldn't be sustainable at current levels? Thank you.

Mark Heimbouch - *Vantiv Inc. - CFO*

I wouldn't -- I've got to take a look at core. I would expect it to continue to expand on a year-over-year basis [particularly] given the growth in channels.

Charles Drucker - *Vantiv Inc. - CEO*

But we won't have the benefit of Mercury in the third quarter that we had in the second quarter, so the expansion will be less.

Dan Perlin - *RBC Capital Markets - Analyst*

I was actually talk about the absolute revenue per transaction, not the year-over-year growth. Okay, thanks guys.

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Operator

Tien-tsin Huang, JPMorgan.

Tien-tsin Huang - JPMorgan - Analyst

Great, good morning, thanks, good quarter here. Just want to ask on Capital One, and was that -- I'm sorry if I missed this -- was that an existing FI client? When did that contribute to you giving that business as a take away? And I'm curious, what were the factors that lead you to win that? I always felt like Capital One that was underrepresented in terms of their shares, so potentially a lot of upside there.

Charles Drucker - Vantiv Inc. - CEO

So it was the Capital One on the debit side, and FI was an existing client, is an existing client today for a while. So they know how we deliver on our services. We had an opportunity to talk with them, and we've been talking with them over a period of time. And they're very committed in the mid-sized lending area and driving value into their treasury book. And when we showed them the value that we bring, how the merchant business can be additive, help bring treasury, help round the whole type of offering, it really resonated with them. Our experience in the financial institutions coming out of history, where people have come from, it played very well.

So their confidence level in what we can help them, and then it's exciting, their existing base, because you're right, they've realized they've been underrepresented in their existing base, plus the appetite for new business, but they needed the products, features, functions, the scale, to be able to compete. So the combination worked very well, and we're excited, and I said when I sit down with them, they're very excited, which is what you want to see. They're going to start to ramp as we go into this quarter and through the year. It's about getting the sales force in place, trained on our products and then training their group, but we've gotten so much better in that, as far as the speed of the ramp. I'm excited to see, as we pull into 2016, seeing some in 2015, and as we pull into 2016 really seeing the impact of them.

Tien-tsin Huang - JPMorgan - Analyst

Okay, very good, that was my follow-up. Just on the potential pipeline for similar deals like Capital One, are there other deals out there of that size?

Charles Drucker - Vantiv Inc. - CEO

You know, we've landed several big clients. I think our pipeline is full with nice mid-sized 100 branch-type of banks. And as we pull into 2016, there are other opportunities in their range, but that's still off into 2016. So this year, I have -- we can see sight to 100 -- which are phenomenal, 100 branch-type of banks, but somewhat large for the rest of this year, it's more into next year there are other ones that are in sight.

Tien-tsin Huang - JPMorgan - Analyst

All right, great. One more if you don't mind, just on the FI business. I guess with sales and marketing down a touch, I know it's not a ton in nominal terms, but I'm curious what's the thinking in terms of back half investments on the FI to drive 2016 growth?

Charles Drucker - Vantiv Inc. - CEO

On the FI we continue to be focusing and working with them to get there EMV, their card issuance. We continue to get their security type of products, and we're bringing other analytical products to the FI group. So our focus is new business, which our pipeline, we're feeling good about, and bringing new business in, but also really bringing products, like I said, helping them navigate EMV, the security aspect, and data analytics and activation on their debit cards is our focus with our existing embedded phase.



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Tien-tsin Huang - *JPMorgan - Analyst*

Great, thanks so much.

Operator

Smitti Srethapramote, Morgan Stanley.

Smitti Srethapramote - *Morgan Stanley - Analyst*

Thank you. First question on Mercury. From talking to the point-of-sale terminal manufacturers it seems like a lot of the smaller business and smaller merchants haven't upgraded to EMV yet. I'm just wondering, as the EMV cycle moves -- upgrade cycle moves towards those guys, you think you could see an acceleration in growth rate in the Mercury business?

Charles Drucker - *Vantiv Inc. - CEO*

I think in general, we're deploying all new terminals -- generally all new terminals have the EMV capability. I think we'll see as the deadline hits, you'll see a lot of the large clients have upgraded, and I think the EMV tale for all our business, including integrated business, follows through into 2016 and potentially into 2017 and it's going to take a while, so I think there's a great opportunity there. I think our team in the integrated payment area is really working with the software developers to deliver a product that allows seamless integration for these clients. So I think the tale for EMV and terminalization, or software upgrades has a long tale 2016 and 2017.

Smitti Srethapramote - *Morgan Stanley - Analyst*

Understood. Just on Litle, was wondering if you could just give us an update in how things are going in that business?

Charles Drucker - *Vantiv Inc. - CEO*

Really, we had the Litle contributing to the high-growth area, or eCommerce, has really continued to perform. We've had a great quarter in that. It's the combination, so the US Post Office coming up in the beginning of next year is going to be another shot in the arm, and a lot of mid-sized clients, and the eCommerce business continues to accelerate. So it's working very well and I think our security products, or our fraud detection products, on the front-end, because all these guys are gearing up that as EMV comes in, there could be even a bigger shift towards online. And our clients want more enhancements to the security products to be predictability in the front-end, so I'm feeling good about eCommerce business.

Smitti Srethapramote - *Morgan Stanley - Analyst*

Thank you.

Operator

James Schneider, Goldman Sachs.



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James Schneider - *Goldman Sachs - Analyst*

Thanks, good morning. Thanks for taking my question. I was wondering, on the integrated business you talked about excess of 20% growth in that channel, can you maybe give us any kind of color? I think that was similar to what it was last quarter in terms of growth rate, but can you give us any color on whether that was an acceleration or deceleration from what you saw in Q1?

Mark Heimbouch - *Vantiv Inc. - CFO*

It was actually pretty consistent. So we've -- I guess, the acquisition closed end of June a year ago. The rates of growth across the board in the business have actually stayed very stable, and continuing to grow, I guess, above 20%. So it's been very stable in terms of growth.

James Schneider - *Goldman Sachs - Analyst*

Understood, thanks. And then just in terms of the revenue per transaction in the FI business, I understand that's been coming down a bit due to pricing pressure, but can you give us any sense about your visibility on whether the security offerings are going to enable that to pick up, at least low single digits or potentially positive at some point in 2016?

Mark Heimbouch - *Vantiv Inc. - CFO*

I think our expectations for the second half of the year is you're going to see some improvement truly given the growth of the EMV, and that will continue beyond 2015. So I'd expect third quarter it starts to look a little bit better.

James Schneider - *Goldman Sachs - Analyst*

Great, thanks so much.

Operator

Bryan Keane, Deutsche Bank.

Bryan Keane - *Deutsche Bank - Analyst*

Hi, guys, just a couple clarifications. The organic growth in the quarter for total Company, I have it at about 8% is that about right?

Mark Heimbouch - *Vantiv Inc. - CFO*

Yes, that's about the right ballpark, yes.

Bryan Keane - *Deutsche Bank - Analyst*

And then in the quarter itself, the \$14 million, about \$14 million of revenue over your top-line guidance, what drove that surprise for you guys?

Mark Heimbouch - *Vantiv Inc. - CFO*

Actually, we saw it in the high growth channels that we've referred to, as well as our traditional direct business coming in a little bit better than expected.



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Bryan Keane - *Deutsche Bank - Analyst*

Okay, so the high growth channels you had thought that it was slow a little bit from those higher growth levels, but it maintained the first quarter growth rate?

Mark Heimbouch - *Vantiv Inc. - CFO*

Yes. Comparing results to expectations, our expectations were little bit lower.

Bryan Keane - *Deutsche Bank - Analyst*

Okay, and then just going over to third quarter, I think it sounds like it's about 8% to 9% growth, could potentially be an acceleration in the third quarter. Is that some of these larger deals ramping? And then just thoughts on the fourth quarter. Should we see a similar growth rate in the third and fourth?

Charles Drucker - *Vantiv Inc. - CEO*

So the large client that we talked about, a lot of them are going to start right at the -- the US Post Office starting in the beginning of the year --

Mark Heimbouch - *Vantiv Inc. - CFO*

Beginning of 2016.

Charles Drucker - *Vantiv Inc. - CEO*

Yes, next year. Capital One will -- our merchant banks will start to ramp-up and we have to invest in the sales force for the future sales that will start to come in more stronger in 2016. And I actually feel really good about our businesses as a whole and where the sales force is hitting and executing and then starting to board, that allows us confidence in the second half of the year and into 2016.

Mark Heimbouch - *Vantiv Inc. - CFO*

We've probably maintained a little bit more conservative stance in the fourth quarter in terms of organic rates of growth, just given some of the noise that has occurred over the past couple of years given the holiday season spend. So there's a possibility that we're somewhat conservative in the fourth quarter.

Bryan Keane - *Deutsche Bank - Analyst*

Yes, just back in the envelope, it looks like 6% to 9% growth in the fourth, maybe 8% to 9%, which would be a slight uptick, potentially, in the third from the second on an organic basis. That's why I was asking the question.

Mark Heimbouch - *Vantiv Inc. - CFO*

Yes.



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Bryan Keane - Deutsche Bank - Analyst

All right, thanks guys.

Operator

Steven Kwok, Keefe, Bruyette & Woods.

Steven Kwok - Keefe, Bruyette & Woods - Analyst

Hi, thanks for taking my questions. I guess I just wanted -- I know it's kind of early, but just wanted to pick your brains on 2016 given your recent signings of Cap One, the US Post Office. When we look at the growth rates, should they accelerate from your core organic bases as we look ahead into 2016, and just any sense of that would be helpful? Thanks.

Mark Heimbouch - Vantiv Inc. - CFO

You know, I think we'll certainly probably defer most of that conversation until we get to the fourth quarter, but the way think about that, the rates of organic growth we're seeing in the business really are stable to up. So it's a continued higher growth on the high growth channels. We feel that going into 2016 that they're stable with some upside. There are some things that probably represent some impact to revenue potential growth in next year, things like OptBlue, post conversion of the Mercury platform to the Vantiv platform. There are other opportunities and more rapid deployment of some of the things that I think others in the industry may be seeing a little bit sooner, they'll probably represent a little but more growth in 2016. So sitting here today, we feel pretty good about continuation of that growth, and continuation of new sales activities, but I think we defer in terms of giving guidance for 2016 right now, until we get to the end of the fourth quarter.

Charles Drucker - Vantiv Inc. - CEO

I look at our sales pipeline as very optimistic of our ability with the changes in the market, whether it is EMV, security, OptBlue, things like that, that will continue to execute strong. So our focus is make sure that we get our share, and better than our share, in the remaining part of the year, so that 2016 has that good momentum going into it.

Steven Kwok - Keefe, Bruyette & Woods - Analyst

Got it, and then just wanted to follow-up, given now that you're more in a comfortable leverage range, how should we think about capital managements going forward? What's your bias towards it? Is it continuing to take down some of these TRAs or the share repurchases?

Mark Heimbouch - Vantiv Inc. - CFO

You know, I think obviously we're getting closer to historical levels, and we've operated in the past between 3 and 3 times leverage, and we now have pretty significant line of sight towards that, and we'll be there very shortly. So we're at the point, in terms of thinking about managing the balance sheet and allocating capitals to drive returns. TRA again, an additional TRA, would be the subject to negotiation with Fifth Third Bank, because you're aware, that could be an opportunity, but as well, on the opportunity it does place capital to buy back shares. Both are alternatives.

Steven Kwok - Keefe, Bruyette & Woods - Analyst

Yes, understood. Thanks for taking my questions.



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Mark Heimbouch - Vantiv Inc. - CFO

Before we go to the next call, I just want to clean up one thing from Bryan Keane's question on organic growth for the total Company in the second quarter, was 9%, not 8%, so apologies for that.

Nathan Rozof - Vantiv Inc. - SVP of IR

Operator, you can take the next caller.

Operator

Ashwin Shirvaikar, Citigroup.

Ashwin Shirvaikar - Citigroup - Analyst

Thank you, guys, and congratulations on the [beat raise here]. You spoke about the pipeline for merchant banks, but can you also speak to the pipeline for large deals like USPS? And as you look at your own growing penetration of the large merchants base, is that maybe a multi-year concern that causes you to focus more so on other channels? Or is there any opportunities still?

Charles Drucker - Vantiv Inc. - CEO

No, I think that if you stay in the large channel, Post Office they have a lot of transactions, but we are going to consistently win in the large space. Sizes like the Post Office, or some of the other large clients, they're more lumpy, but we're winning in that large space. With people with very good transaction type of growth, that combining a few of the wins equals a very large [guy], so we're performing very well there, however, the other channels are hitting also. So it's our diversity of channels, I think that's what makes us unique as a Company, that we're able to play in all the pieces. And, on the Merchant side, it's hitting on the cylinders we need, we need to take shares.

Ashwin Shirvaikar - Citigroup - Analyst

Great. And the security product that you launched last, I believe it was last October, and so the comp is coming up. From a product perspective, can you talk about the product road map, the evolution that enables you to continue to grow something like the security offering over a longer time frame?

Charles Drucker - Vantiv Inc. - CEO

Are you talking about the financial -- the whole business? The security offerings on the merchant side with our large clients, as we get closer to -- some have been implemented, but the majority of the large clients are around the EMV type of cut over as they get encryption tokenization, because it has complexity to it. One of the beauties of our system and our consultative approach, and why we're winning is we can execute and has complexity to it, and we continue to see that type of opportunity layering in. On the financial institution side -- was it last year we put in the security products? That the EMV card reissuing and then the banks are starting -- the financial institutions are really starting now as they get through the EMV, the card reissue. In 2016, we're having a lot of conversations with them around data mining analytics to activate their debit cards. And be able to do marketing programs to them using data analytics on the FI side, which as we roll in towards 2016, it still has us low in single-digit-type of thought process and consistence on the FI side.



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Ashwin Shirvaikar - Citigroup - Analyst

Okay so there's plenty of traction, and it looks like for the value-added service part of the FI business, as you look forward?

Charles Drucker - Vantiv Inc. - CEO

Yes.

Ashwin Shirvaikar - Citigroup - Analyst

Okay. Last question, if I can sneak one in. Could you remind us what Mercury synergies are for next year? This year I know obviously, but for next year what is it supposed to be?

Mark Heimbouch - Vantiv Inc. - CFO

We'll drive some incremental Mercury synergies next year as we migrate the transaction processing from Global's platform to ours, and we'll size those synergies on the fourth quarter call when we provide 2016 guidance.

Ashwin Shirvaikar - Citigroup - Analyst

Okay. Thanks.

Operator

Dave Koning, Robert W Baird.

Dave Koning - Robert W. Baird & Company, Inc. - Analyst

Hey guys, great job. I just have a few quick ones. First of all, the TRA benefit the \$0.05, is that split pretty evenly or that accelerating? I'm wondering, Q3 is it \$0.025, Q4 for \$0.025?

Mark Heimbouch - Vantiv Inc. - CFO

Yes, that's a reasonable way to think about it for this year. And then -- so we're effectively, we pick up all the benefit given the timing of agreement this year. It will expand to \$0.08 on an annual basis in 2016, so an additional \$0.03 of accretion, and it continues to grow up to the point that it will reach effectively \$0.15 of EPS by 2019. So, it's, as you guys are aware, it's really a very significant return and there are additional TRAs available to us, possibly.

Dave Koning - Robert W. Baird & Company, Inc. - Analyst

That's great. Secondly, in the free cash flow statement, there's a line, acquisition of customer portfolios is about \$35 million this quarter. It was bigger than it's been for many quarters. Is that you actually making acquisitions and, if so, how much revenue might that contribute?



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Mark Heimbouch - *Vantiv Inc. - CFO*

We have continued to acquire portfolios, and in some cases it is related to the third-party channels, as well, in certain situations, with respect to the merchant bank relationships, we have acquisition of portfolios. So it has been consistent with some of the prior deals we've signed, as well as with respect to the Capital One transaction.

Dave Koning - *Robert W. Baird & Company, Inc. - Analyst*

Okay. But is there like, you pay 5 times rev, 3 to 5 times rev and so it's not overly meaningful obviously.

Mark Heimbouch - *Vantiv Inc. - CFO*

Yes, haven't disclosed the valuations, but it does allow us to immediately start servicing a portfolio and converting that portfolio onto our platform. Sometimes revenue doesn't show up until we get it converted to our platform, so you see an upfront purchase price, with revenue to come at a later date.

Dave Koning - *Robert W. Baird & Company, Inc. - Analyst*

Got you. And then finally, the transition cost ramped up just a bit, somewhat in Q2. Are we at a stable point now? And maybe when do those start to fade again?

Mark Heimbouch - *Vantiv Inc. - CFO*

We would expect to be stable really through the end of the year. Those are primarily related to the Mercury acquisition, we continue to make progress on transition costs.

Nathan Rozof - *Vantiv Inc. - SVP of IR*

I would actually say we are running slightly ahead of plan, and are moving to try and get as much of it put behind us in terms of actual activity. So the trend will continue, but we're running ahead of plan, we like to get as much behind us before we go into busy season.

Dave Koning - *Robert W. Baird & Company, Inc. - Analyst*

Great, thanks, good job.

Mark Heimbouch - *Vantiv Inc. - CFO*

Thank you.

Operator

Tim Willi, Wells Fargo Securities.



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Tim Willi - Wells Fargo Securities, LLC - Analyst

Thanks, good morning. Question on integrated payments, Mark or Charles. Just curious, since you've bought Mercury, and obviously there are lots of other acquirers and processors trying to get in this space. Have you seen -- I'm curious what you're seeing from dealers and developers in terms of the discussions around new agreements that you're signing, whether it's them looking for even more enhanced capabilities, or security, or pricing? Has anything changed relative to how the discussions and the RFPs were being done a year ago, or anything that Matt and his team shared with you guys about how it was even two years ago around this environment and the selling process?

Charles Drucker - Vantiv Inc. - CEO

As I worked closely with Matt Taylor, he's told me it's pretty much been consistent, has slight ebbs and flows, uptick, nothing dramatically different. They really focus right now, and that's what he is most excited about, is the dealers and developers, how do I get my client to EMV, how do we have the security encryption, how do you help me there, and then how will you help me expand into a bigger addressable market? There are always some dealers or software providers that are in the cycle of their software that says, how do I get more out of this revenue? I've got to tell you, in talks with them, a lot of it is -- most of his growth dealers, and the ones that are bringing lots of business, are about, how do help me with products, features, functions for the future to begin to grow? He's told me that it hasn't -- there's been no significance around historic levels, could be slightly, but nothing that has changed dramatically, but the conversation is about, how do you help us grab -- take share and get product into more restaurants and retailers? It's actually been a good dialogue.

Tim Willi - Wells Fargo Securities, LLC - Analyst

Yes, that sounds like it. A healthy kind of discussion to have versus price. Just a follow-up on that, I guess. Are there examples, or do think there will be, where developers or dealers who have been looking to get their software to much larger enterprises, you're able to bring them those introductions and get a software developer into a much larger market? Is that happening, or is it something you can point to, or you will be able to point to in the near-term?

Charles Drucker - Vantiv Inc. - CEO

Yes, I don't think we've announced them, but basically there was a set of large, mid to large national clients, that a lot of their dealers had their software in, but they couldn't be as competitive in that market space, like we do in the mid- to large national, and we've already had some success of clients that we've been able to go out with the dealer or the developer and win that middle to largest -- large kind of clients. So the attraction there has actually been very good, in that space, that Mercury was not able to get to before because you needed to have the scale to get to a certain competitive national type of price points. So the answer is yes.

Tim Willi - Wells Fargo Securities, LLC - Analyst

Great, that's all I had. Everything else was answered in prior questions. Thanks very much.

Operator

David Hochstim, Buckingham Research Group

David Hochstim - Buckingham Research Group - Analyst

Hi, thanks. Just to follow-up on a couple things. The same-store sales growth you mentioned, Mark, was mid-single digits. Is that exactly similar to the first quarter which I recall was higher than normal?



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Mark Heimbouch - *Vantiv Inc. - CFO*

Yes, so the second quarter was 6.5%. If you recall the first quarter, I think, was roughly 8%. But remember the impact of the year-over-year comp given the bad weather a year go. So when we normalized, it would have normalized in the 6%, 6.5%, as well.

David Hochstim - *Buckingham Research Group - Analyst*

Okay. Were there any changes in consumer spending or behavior that you saw this quarter?

Mark Heimbouch - *Vantiv Inc. - CFO*

I was actually looking across the different verticals. I still think you actually do probably see some benefit from slightly lower gas prices, so knowing they're up a little, but our trends have been pretty stable, really, across many of our categories. The everyday spend category, that you guys -- we're very strongly placed in, continue to have pretty good growth. The takeaway for me is the consistency now over a handful of quarters. Just puts us in a pretty confident position going into the rest of the year.

David Hochstim - *Buckingham Research Group - Analyst*

Okay. Thanks. And the just on TRAs, is there something new or different happening with Fifth Third that you've highlighted that?

Mark Heimbouch - *Vantiv Inc. - CFO*

No, I just wanted to remind people that it does represent an opportunity and, by the way, as Fifth Third, or when Fifth Third will decide to sell down those TRA liabilities really get created. So much of what we're referencing actually doesn't exist yet. So those opportunities are in the future.

David Hochstim - *Buckingham Research Group - Analyst*

Okay, and is possible to say who the acquirer was for the USPS before?

Mark Heimbouch - *Vantiv Inc. - CFO*

We can talk about that off-line.

David Hochstim - *Buckingham Research Group - Analyst*

Okay, thank you.

Mark Heimbouch - *Vantiv Inc. - CFO*

Thanks.

Operator

Tom McCrohan, Sterne, Agee & Leach



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Tom McCrohan - *Sterne, Agee & Leach, Inc. - Analyst*

Yes, thanks for squeezing me in. Assuming stable same-store sales trends and merchant for the back half of the year in light of the over 20% growth and integrated you are seeing today, and the contributions from the new wins you have, should the organic growth rate, 11% number that you talked about and had in your press release, should we expect that to accelerate from here?

Mark Heimbouch - *Vantiv Inc. - CFO*

So consistent with a couple of comments we made with respect to the outlook we provided, we're a little bit more conservative than that. And I think Bryan Keane asked a comment with respect to the fourth quarter. There has been some noise over the holiday spending period over the last couple of years, so we'd like to see a good holiday spend period going in the fourth quarter. Aside from that, we're feeling pretty good about the trends we're seeing in the businesses and we are not really seeing -- I'm not aware, or thinking of, any degradation in terms of the trends trickling in the near-term.

Tom McCrohan - *Sterne, Agee & Leach, Inc. - Analyst*

Okay and my last question was related to operating leverage. As you lap these acquisitions, and some of the benefits from some of the big wins last year, last few quarters we've had revenue growth exceeding adjusted EPS growth, just glide into more of an organic growth rate in high-single digits, 9% this quarter. Can you just talk about the walk between top-line growth and that kind of high digit category, and where EPS growth might be?

Mark Heimbouch - *Vantiv Inc. - CFO*

Yes I think the initial view on that would be EPS growth should exceed that revenue growth going forward. So we've gone through the lapping, if you will, of the Mercury transaction and the incremental indebtedness with respect to the transaction. You'll probably also seen a little bit higher spend just given that integrations. I think as we lap and get into 2016, you'll start to see more leverage from top-line to bottom line, as well is the opportunity to deploy capital like TRAs, like share repurchase, that results in measurably higher EPS growth.

Tom McCrohan - *Sterne, Agee & Leach, Inc. - Analyst*

So that implies operating margins expansion from here?

Mark Heimbouch - *Vantiv Inc. - CFO*

Yes, I think operating margin expansion, probably year-over-year, not necessarily think about the sequential expansion for the next couple of quarters, as we're still pretty heavy into the integration, but I think post that integration you start to see more operating margin expansion.

Tom McCrohan - *Sterne, Agee & Leach, Inc. - Analyst*

Thanks.

Operator

At this time I like to turn it back over to our speakers for any additional or closing remarks.



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Nathan Rozof - Vantiv Inc. - SVP of IR

Thank you, and thanks to everyone for joining the call today. If you have any additional questions after today's call then please reach out to me using the contact available on our website and I will be happy to help you. Thanks again and goodbye.

Operator

That does conclude today's conference. We thank everyone, again for their participation.

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