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VNTV - Q3 2015 Vantiv Inc Earnings Call

EVENT DATE/TIME: OCTOBER 28, 2015 / 12:00PM GMT



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**Darrin Peller** *Barclays Capital - Analyst*

**David Togut** *Evercore ISI - Analyst*

**George Mihalos** *Credit Suisse - Analyst*

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## PRESENTATION

### Operator

Good day, and welcome to the Vantiv third-quarter 2015 earnings call. Today's conference is being recorded. At this time, I would like to turn the conference over to Nathan Rozof, Senior Vice President of Investor Relations. Please go ahead, sir.

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

Thank you, Operator, I appreciate it. Good morning everyone, and thank you for joining us today.

By now everyone should have access to our third-quarter 2015 earnings release, which can be found at Vantiv.com under the Investor Relations section. During today's call, Charles Drucker will review our third-quarter operating performance. Mark Heimbouch will then describe our financial results and address our fourth-quarter outlook.

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 discussions today will include forward-looking statements. These forward-looking statements are not guarantees of future performance, and therefore, you should not put undue reliance upon them. These



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statements are subject to numerous risks and uncertainties that could cause actual results to differ materially from what we expect. Please refer to the 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?

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**Charles Drucker - Vantiv Inc - CEO**

Thank you, Nate, and thanks to everyone for joining us this morning.

I'm happy to announce another great order for Vantiv. Our business is hitting on all cylinders, with strong performance in our merchant and financial institution segments, and we returned capital to shareholders through the repurchase of stock and the termination of additional TRA obligation. Our operating performance exceeded expectation during the third quarter. Net revenue grew 13%, to \$430 million, and pro forma adjusted net income per share reached \$0.59. Our merchant business grew 16% year over year, and as we now have lapped the Mercury acquisition, this is all organic. In addition, our financial institution segment delivered its best results in several quarters. Net revenue grew 3%, which was aided in part by EMV card re-issuance and continued new sales executions.

We've described in the past how our omni-channel capabilities and our full suite of security products are creating competitive advantages for us, and helping us to win new clients. We continue to win new business, including large national clients like the United States Postal Service, which was announced last quarter. We will provide them with our full set of omni-channel capabilities, as well as our suite of security solutions.

So speaking of security, the EMV liability shift occurred October 1, as expected, marking another milestone in this multi-year journey towards EMV. Our financial institution clients are in various stages of reissuing EMV cards. We saw a bump in net revenue growth during the third quarter, including the benefit of EMV card issuance, which we expect to continue through 2016. Within our merchant business, we are processing EMV transactions for several leading retailers, and are now processing well over 1 million EMV transactions a day. We expect many of our large merchants to deploy EMV between now and the end of next year, and for the small to midsize businesses to deploy EMV over the next several years, based on timelines that meet their individual needs.

EMV helps to generate new sales, because it really creates a catalyst for a broader conversation about security. We recently launched Vantiv OmniShield, a robust portfolio of leading-edge security services that includes point-to-point encryption, tokenization, PCI compliance, as well as EMV validation and certification services. Vantiv OmniShield is available to merchants of all sizes, with bundled solutions for our small and midsize merchants as well as a fully customized solution for our larger merchants. In addition, we offer advanced analytics in fraud products within our financial institution business that are specific to these clients' needs, and are working with our e-commerce merchants, offering them fraud tools, educating them, and working with them to help them succeed with the card re-issuance of EMV cards.

So turning to new wins, we had two notable wins within our merchant bank channel this quarter. First is Rabobank, which we announced during the quarter. We'll help them grow their business banking program by enabling them to compete toe to toe with the largest banks in the country, as they offer our leading merchant services solutions to their clients. I'm also excited to announce another new win, and a great partner, with Umpqua Bank, on today's call. It is the largest community bank in the Pacific Northwest, with approximately 350 stores, that will significantly expand our distribution and continue the rapid pace of organic growth within our merchant bank channel.

So in conclusion, while this was another great quarter for us, what's even more exciting is that all of the highlights that I described today indicate a bright future for Vantiv, both near- and long-term. Within the payments industry, the pace of change is quickening, and the need to invest in new products and technology is greater than ever before. The payment industry is becoming more complex, and this complexity is good for large payment companies like us. We have the knowledge and capabilities to develop advanced technology, and we have the scale to efficiently spread our cost of these investments across 20 billion-plus transactions. These capabilities, as well as our scale, represent a significant competitive advantage.



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We believe the industry will consolidate, as some smaller players may struggle to keep up. We are seeing it with the EMV. Our full suite of security products is enhancing our competitive position and helping us win new clients. So as the payment industry continues to evolve at this rapid pace and become more complex, I am excited about how well we are positioned for the future.

So with that, I'm going to hand the call over to Mark. He will review our financial performance, discuss capital allocation, and address our outlook for the fourth quarter. Mark?

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**Mark Heimbouch - Vantiv Inc - COO & CFO**

Thanks, Charles, and good morning everyone.

As Charles said, we delivered another excellent quarter. Net revenue grew 13% to \$430 million, primarily driven by an 8% increase in transactions and a 5% increase in net revenue per transaction. Pro forma adjusted net income increased 22% to \$119 million, and pro forma adjusted net income per share increased 20% to \$0.59. Our merchant segment generated net revenue growth of 16%, principally due to an 8% increase in transactions and a 7% increase in net revenue per transaction.

Our expansion in rate reflects continued growth in the small- to mid-sized merchant segments, through our high-growth channels, as well as the contribution from value-added services, like security products, that Charles mentioned. Growth in our financial institution segment improved during the quarter, with net revenue growth of 3% and transaction growth of 7%. We are seeing increased momentum in EMV card re-issuance, which we expect to continue through 2016. Total operating expenses, including sales and marketing, other operating costs and G&A, increased by 12% in aggregate, resulting in significant margin expansion.

Adjusted EBITDA margin expanded by 70 basis points year over year, as we continue to drive efficiency and realize synergies related to the Mercury acquisition. We expect margin expansion to continue in the fourth quarter and into 2016, as our integration of Mercury continues to track to our schedule. Mercury continues to exceed our business case, and we remain on track to complete the migration of Mercury's existing clients to our processing platform in the first half of next year.

Depreciation and amortization expense, excluding the impact of the amortization of intangibles related to acquisitions, was \$22 million, consistent with recent trends. Net interest expense decreased \$27 million, declining on a year-over-year basis, as we continue to de-lever. Moving 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 we recently have returned capital to shareholders. We expect the business will continue to de-lever, given the combination of adjusted EBITDA growth and debt pay-downs.

In line with our strategic priorities of investing for growth and returning capital to shareholders, we recently terminated a portion of the tax receivable agreements that were established at the time of our IPO with Fifth Third Bank. With this transaction, we terminated TRAs on an attractive rate of return, for approximately \$49 million. The transaction occurred during the fourth quarter, and will reduce the \$597 million in tax receivable obligations to related parties on the balance sheet by \$140 million. Termination of these obligations will also generate approximately \$0.05 in accretion to pro forma adjusted net income per share, through increased cash tax benefits beginning in 2016, but note it will not impact 2015 EPS. We also recently repurchased approximately \$200 million of stock, of which \$161 million was repurchased during the third quarter.

Before I turn the call back to Charles, I'd like to address our outlook for the fourth quarter and for the rest of the year. Based on current trends and new business activity, for the fourth quarter we expect to generate net revenue of \$429 million to \$437 million, representing growth of 7% to 9%. And we expect pro forma adjusted net income per share of \$0.61 to \$0.63, representing growth of 15% to 19%. This would result in full-year net revenue of \$1.657 billion to \$1.665 billion, and pro forma adjusted earnings per share of \$2.21 to \$2.23 per share for the full year.

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



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**Charles Drucker** - *Vantiv Inc - CEO*

Thanks, Mark.

As you can tell, we're very happy with our performance and execution so far this year, and even more excited about what the future holds for our Company. For that reason, I'd like to thank the people at Vantiv for their passion, character, and attitude that really drive our success every day. Because of these strong values, I'm confident in our ability to help our clients securely and successfully navigate the changing payment landscape. And by doing so, we will continue to win market share and drive strong results for our shareholders.

So thanks -- thank you for -- everyone for your time this morning. And, Operator, we are ready to open up the line for questions.

## QUESTIONS AND ANSWERS

**Operator**

Thank you.

(Operator Instructions)

Jim Schneider.

**Jim Schneider** - *Goldman Sachs - Analyst*

First of all, on the merchant side, can you maybe give -- I may have missed it. But can you give us an update on the growth in integrated and Mercury in the quarter? And any signs of any slowdown in that trajectory? And specifically, what you're seeing by vertical, if you can give that detail?

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, hey Jim, it is Mark Heimbouch. On -- yes, on the integrated payments business, it actually continues to perform very consistent with the prior quarters. Revenue growth, again, for the quarter is over 20%. And we have seen that remain now pretty steady, for an extended period of time. So continue to be pretty bullish on that business. And in terms of continued penetration of the existing base, as well as the addition of new partners, the trends are pretty positive.

**Jim Schneider** - *Goldman Sachs - Analyst*

That's helpful. Thanks. And then maybe as a follow-up, I want to ask about the OpEx run rate at this point. Clearly, you've got some investments going on that you mentioned in the last quarter, in terms of the bank channel, et cetera. But then also, at some point in 2016, you're going to start to see the benefits of the platform consolidation for Mercury.

So is there a point at which you think that OpEx is going to flatten out, or potentially start to decline at some point? Just wondering how to think about that inflection in OpEx overall, in terms of both SG&A and sales and marketing.

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, so you're asking in terms of total expenses, right, as compared to just operating costs?



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**Jim Schneider** - *Goldman Sachs - Analyst*

Yes. Right.

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

I think the growth in sales and marketing is going to continue. Some of that is investment in the channel, as well as the high-growth channels. Your first question was specific to the integrated payments channel, but the merchant bank channel, as well, is going tremendous growth. So we continue to see continued growth in sales and marketing, relative to those higher rates of growth. And by the way, the third high-growth channel in there would be e-commerce. It, as well, is growing very high.

So we continue to expect sales and marketing to continue to grow. Below the line, though, you can actually see we start to get more and more leverage on the OpEx line, and we haven't fully completed the Mercury integration. But actually, I think if you look over the last few quarters, you'd see a significant slowing in the rate of operating expense growth. And below the line, G&A, I think you're starting to see more of the same. So we're really starting to see the benefit of leverage and scale on the other two line items.

**Jim Schneider** - *Goldman Sachs - Analyst*

Great. Thank you.

**Operator**

Smitti Srethapramote

**Smitti Srethapramote** - *Morgan Stanley - Analyst*

It seems like (technical difficulty) FI business is seeing some momentum from the EMV upgrade cycle. I was just wondering now, going forward over the next couple quarters, can we expect to see growth at the higher end of the low single-digit range, given that tailwind?

**Charles Drucker** - *Vantiv Inc - CEO*

So on the FI side, we're seeing both the positive momentum on the EMV, but also, the new sales execution and bringing clients aboard has contributed to improve that. So from our perspective, we think some of the EMV stuff sales will go through 2016, but our focus is still low single digits on the business, but we are seeing positive momentum in the new sales plus EMV.

**Smitti Srethapramote** - *Morgan Stanley - Analyst*

Great. Thank you. Then maybe just a follow-up. A couple days ago, Chase announced -- Chase Pay, which is partnering with MCX, and a couple of the [MSX] merchants for your clients. Just wondering if could share with us your early thoughts on what that could potentially -- what that announcement could potentially [bring to you] guys?

**Charles Drucker** - *Vantiv Inc - CEO*

Yes, so we saw the announcement at (inaudible) 20 with Chase Pay. Let me just break this up in two pieces. First of all, Chase Net was introduced a few years ago, and we've continued to be -- successfully compete in the market, and win new merchants. And we have an ability to compete on the strength of our solutions, and to compete on price, if have to. So we have that type of scale. So we continue to win, and Chase Net has been out there a while.



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We saw the announcement, and the way we looked at it, for us, was about the wallet. We already support several mobile wallets today, including CurrentC, that we're attached to. And we continue to enable our clients to support them in the future, and we're committed to options and bringing different payment solutions in.

From my perspective, banks are really looking for ways to protect their relationship with the consumer. And this wallet is one way to do that, for the banks to stay close with the consumer. So we likely see the beginning of more large banks, like JPMorgan, issuing these wallets and talking about it more aggressively. So we always think options are good, and we're -- we continue to be able to compete and win business, so we want to give merchants choices.

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**Smitti Srethapramote** - *Morgan Stanley - Analyst*

Thank you.

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**Operator**

Darrin Peller.

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**Darrin Peller** - *Barclays Capital - Analyst*

Congrats on the quarter. I just want to start off, as a follow-up on the merchant services side, just given how fast the growth rate was there. I want to make sure A, there was nothing unusual or inorganic in the quarter. I mean, I'm pretty sure you did now grow past the addition of Walmart, and the Mercury deal is entirely organic -- is anniversaried. So this is all organic, first of all.

And secondly, just if you can give some color on what you see as the sustainability of this growth rate? It seems like it's really coming from iPOS from the merchant bank referral channel. And it doesn't feel like there's any reason why those two channels should slow. So here we are at 16%, as we approach next year, where you've historically talked about a high signal digit growth rate for that segment. Can you give us some color as to what you're really thinking about this growth rate now? And what kind of sustainability this has?

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**Charles Drucker** - *Vantiv Inc - CEO*

So it was organic. And you're right, we lapped Walmart, I think, in the second quarter, and we've lapped Mercury. So it's a real good quarter in the business. We're seeing strong results coming out of integrated payment. We're seeing strong results out of the bank channel. And we're adding Umpqua, and we continue to add banks, and banks continue to ramp up. The e-commerce business is doing very well, and our core business has continued to do well. So I'm confident in our ability to continue to grow the business strong in these channels. Mark?

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, Darrin, this is Mark. We continue to be very optimistic on our merchant revenue expectations. But as we've said before, we're setting expectations that we feel highly confident, in terms of attaining. But if you really think about what's leading the higher rates of growth, what's -- higher rates of market growth is our ability to continue to win share.

And so when the integrated payments channel is growing 20% plus, and our merchant bank channel is contributing to the rates of growth at the rate it is, we're certainly winning clients, and Charles gave you some reference points on the call. But we're winning clients, we're continuing to benefit from strong organic growth, and the contribution of EMV and security solutions, and other value-added services in that space. But again, we do continue to take and win share in the market.



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**Darrin Peller** - Barclays Capital - Analyst

All right. And just, have we even seen the impact of Capital One at all yet? Or is this still to come, in terms of referrals coming in there? And then obviously, Umpqua is a pretty nice addition for next year, too.

**Charles Drucker** - Vantiv Inc - CEO

Yes, we're starting to see the impact of Capital One, the referrals are happening. We have some existing clients of theirs that have moved over to us. And we see Capital One, plus our other banks, continuing to ramp as the referrals move up. And then we get these new banks coming in that will continue to ramp as we move forward.

**Darrin Peller** - Barclays Capital - Analyst

All right, makes sense. Just a quick follow-up on the TRA now, and then I'll turn it back to the queue. But again, so it's nice to see you move forward with some of that, with Fifth Third. Can you just give us a sizing on how much that represents, as a percentage of what is remaining with Fifth Third? I know there's a pretty big portion out there still, I think. And what that could be over time, as well?

**Mark Heimbouch** - Vantiv Inc - COO & CFO

Yes, I think a simple way to think about it for you is, it roughly represented \$140 million of liability on the balance sheet. I think post this transaction, it leaves another \$450 million on the balance sheet, plus or minus. So there's meaningfully more that is available. On top of that, to the extent that Fifth Third would sell some of their equity, that, again, continues to contribute more and more TRA. So there is ongoing opportunity, in terms of TRA, and how we think about that.

**Darrin Peller** - Barclays Capital - Analyst

That's good to hear, guys. All right, thanks again.

**Operator**

David Togut.

**David Togut** - Evercore ISI - Analyst

Quick question on pricing in the merchant business, up 7% year over year. That's really an extraordinary, extraordinary number. Could you just break down the drivers of that 7% growth in revenue per trans in more detail? And to what extent did the lapping of the Walmart business in Q2 affect that number?

**Mark Heimbouch** - Vantiv Inc - COO & CFO

Yes, so -- this is Mark. So clearly, any time we add a large client like Walmart, that's going to put pressure on that metric. But that metric is made up of contribution of value-added services, contribution of pricing. It also is significantly influenced by the high-growth and integrated payments, e-commerce and merchant bank. So the comment that I made on the call is, those channels are principally going after small to mid-sized clients. And as you're all aware, the pricing equation in those verticals, and in those client mix, represents an opportunity to see that rate continue to expand.

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And I think that's really been our history, really since the time of the IPO. When we closed on the Mercury transaction just over a year ago, I think we called out for everybody that those high-growth channels represent about 30% of our net revenue, in total Company. Today, they represent about 40% of total company net revenue. They're actually starting to approach being equal to about half of our total merchant net revenue.

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**David Togut** - *Evercore ISI - Analyst*

And just as a follow-up, as some of the high-growth channels drive more of the top line expansion, should we expect to see a pickup in margin expansion? You had 7% net revenue growth, on a high fixed cost structure. Shouldn't that lead to a pickup in the rate of margin gains, going forward?

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

We called out on the call, actually, that we expect EBITDA margins to continue to improve. So some of that comes from the synergies, with respect to integrating Mercury. But I think over time, yes, our expectation is that we still have the opportunity to see expansion in EBITDA.

The other thing I would call out is, it also leads to our ability to continue to reinvest that benefit back in the business. And so it gives us a pretty sustainable run rate, in terms of continued investment to support growth.

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**David Togut** - *Evercore ISI - Analyst*

Thank you very much.

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**Operator**

George Mihalos.

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**George Mihalos** - *Credit Suisse - Analyst*

Great, thanks for taking my questions, guys, and congrats on another good quarter. Wanted to start off asking you, we're hearing more about the PINless debit opportunity now in select verticals, certainly supermarkets come to mind and the like. Are you seeing more of a push to the PINless debit side in some of those verticals? And maybe, how do you think about that as an opportunity for Vantiv? And does that make Jeanie, in your opinion, a more valuable asset?

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**Charles Drucker** - *Vantiv Inc - CEO*

So PINless debits. So Jeanie has the capability to do PINless debit in the market. And we see overall debit routing, which started with the Durbin change that, because of our strong presence in debit, and a lot of everyday spend clients, we are very sophisticated and able to route transactions. PINless debit is another avenue for us to help our clients to route transactions differently.

There is more activity happening around PINless debit, and we're helping, working with our clients, and to navigate the best way to approach PINless debits. So it will continue to pick up steam, just like the routing of PIN transactions have picked up steam. So I think it is an opportunity for the future.



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**George Mihalos** - *Credit Suisse - Analyst*

Okay. And then just on that, to David's question on the [night to coloration] we saw on the revenue [per trend] on the merchant side. How should we be thinking about that, going into 2016, given that you are ramping some larger customers that we think are coming at a lower price point?

And then also, just on the FI side, if I'm not mistaken, your transaction growth was a little over 7%. I think that's the highest it's been, on the debit side, since you've gone public. What's driving that?

**Charles Drucker** - *Vantiv Inc - CEO*

Driving on the FI side is, we're putting up the clients, our sales execution that we talked about several quarters ago has started to drive new business. And that new business is starting to converge, so we are seeing more volume and more growth coming out of the FI business.

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

I think that that is the case. By the way, 7%, I don't think it has been the high point since the IPO, but it's certainly been the high point, in terms of transaction growth, over the last several quarters. I think the last half of the year was maybe around 5%. Ticked up a notch to 6% in the third -- in the second quarter, I'm sorry. And then, most recently, 7%.

So yes, it did contribute to stronger revenue and operating performance in the segment. As well, I would say, value-added services, which includes EMV, has also started to contribute to that lift. Our portfolio consists of small to mid-sized and regional financial institutions, and we've just started to see them more recently, over the last few months, in terms of increased card re-issuance. So that continues to contribute to some expansion going forward, and we think that will continue through 2016.

**George Mihalos** - *Credit Suisse - Analyst*

Okay. Thank you.

**Operator**

Jason Kupferberg.

**Jason Kupferberg** - *Jefferies LLC - Analyst*

So as we start to think about 2016, obviously, it is preliminary to give any detailed guidance. But it does seem like there's a bunch of tail winds that are going to continue to help you. You've got the Postal Service win, OptBlue, the bank referral channel, the Mercury de-conversion, the TRAs, et cetera. Are there any headwinds we should be thinking about, as we contemplate our models for next year, that you guys see on the horizon? Whether it be anything around year-over-year comparisons, or other dynamics in the business?

**Charles Drucker** - *Vantiv Inc - CEO*

From the business execution standpoint, and where the sales forces are at, and how I see them going to market and winning share, I feel very positive about that. And the tail winds that you did mention, the OptBlue, EMV has a longer tail with the terminal aspects and different opportunities around EMV.

So from execution from bringing new sales in, from where we're positioned in the market, I'm feeling good, going into the end of the year and closing out the business. And my merchants, with the EMV conversion, our large clients have done a really good job getting the security products

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up, and more of them will be converting. So I think there -- feel positive going into the close of the year, and into next year, with our ability to execute and continue to win share.

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**Jason Kupferberg** - Jefferies LLC - Analyst

Okay. And then just in terms of same-store sales, what did you see in the quarter? What's your general take on the health of the US consumer? There's still some cross-currents out there. So would just love to hear your latest thoughts on that topic.

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**Mark Heimbouch** - Vantiv Inc - COO & CFO

While there's been a lot of noise in the environment, actually, I remind everyone that we tend to be in some pretty predictable resilient everyday spend categories. And along with those lines, we've continued to see very stable same-store sales trends.

So if you recall, we've focused on same-store sales trends being mid single digits, six and better. Always seems to be a positive outcome. And for the third quarter, we saw that trend continue. So same-store sales trends continue to be above 6% modestly, so that's pretty positive. And we've seen that trend continue.

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**Jason Kupferberg** - Jefferies LLC - Analyst

And you expect that to persist into Q4? Is that what's built into the guide?

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**Mark Heimbouch** - Vantiv Inc - COO & CFO

Yes. We've -- so that would be consistent with our expectations for the fourth quarter. I think you have to sometimes be suspicious a little bit about retail spend during the holidays, right? The last couple of years have been so-so. But we have seen now, for over a period -- for more than four quarters, including the fourth quarter last year, as I recall, mid single digits, around 6% same-store sales. So pretty consistent for a period of time.

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**Jason Kupferberg** - Jefferies LLC - Analyst

Okay. Thank you for the comments.

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**Mark Heimbouch** - Vantiv Inc - COO & CFO

And by the way, I just want to remind, also, that same-store sales metric is a card-based transaction trend, right? So it's not the same way a retailer would look at same-store sales revenue trends. It's a metric for us, on a same location, same merchant basis, but card-based transaction trends, or trends -- or transactions that we process.

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**Operator**

Dan Perlin.

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**Dan Perlin** - RBC Capital Markets - Analyst

I do have a question going into the fourth quarter. The -- it looks like -- and I might just have it wrong in my model. But it looks like, if we just carried some of the metrics across sequentially, the revenue number would be a lot higher than what you guys are guiding. So I'm wondering, I guess,



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two things. One is, where do we -- where are you driving this tilt down? Is it in revenue per transaction in one of the divisions? It sounds like, based in your comments on same-store sales, it's probably not the transaction number. So I'm just trying to reconcile that.

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Dan, it's Mark. And I think our approach, over the last several quarters, has been pretty consistent, with merchant net revenue growth at the low end, upper single digits to low teens. And that would be a net revenue metric.

I think our guide in your model would probably result in a little bit less expansion and revenue per transaction. And then on the FI side, it would continue to be in the low single digits, in terms of net revenue growth.

So in terms of setting guidance or setting expectations, we've adopted a methodology that the expectations are our numbers that we have a very high level of confidence, in terms of achieving. And we have tended to stay with that policy.

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**Dan Perlin** - *RBC Capital Markets - Analyst*

And can you give us an insight as to what you've seen thus far, as we approached into the fourth quarter? I appreciate the conservatism, but you obviously have a pretty good look. And there is a pretty significant step-down in that revenue per transaction, if you're (multiple speakers) numbers.

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, up -- so we're sitting close to the end of October. Halloween's a pretty big week for us, actually, given our merchant categories. But I would say trends through October have been pretty consistent with trends through the third quarter.

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**Dan Perlin** - *RBC Capital Markets - Analyst*

That's great. And then, can you maybe parse out a little bit the -- this benefit that you're seeing in this mix shift? You're seeing it in your rate. You're also seeing it, obviously, through margins. But just in the SMB channel, in the value-added services, you called those out a bunch of times on the call. Can you just give us a sense as to the incremental benefit that that's providing you guys in the merchant segment right now?

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

I think actually, it probably led to -- so the increase in rate being up pretty significantly in the third quarter, I would say actually, the high growth in all of those categories is contributing pretty significantly to that expansion, and should continue.

The impact of some of the value-added services, and pricing and other things, I would say that has probably a little bit longer tail on it. So it's somewhat contributory in the third quarter. But we would expect that there's -- that should also contribute to expansion. But for the near term, I would say right now, it is -- mix is contributing more significantly than some of the other components.

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**Dan Perlin** - *RBC Capital Markets - Analyst*

That's great. And then one last one, if I could. The EMV card conversion, it sounds like still early days for you guys. But can you just give us some sense?

I know you said it is going to go through 2016. But it could be -- it sounds like it could still be very meaningful. So I'm just trying to get a sense of maybe percentage reissued, or what you still have in front of you? Thanks.



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**Charles Drucker** - *Vantiv Inc - CEO*

Yes, so we've seen pickup in the business. Like I talked to you earlier, that our portfolio was more second half of the year, going into 2016. So we've started to see the benefit of the reissued during the quarter. And we're still in the early stages, because a lot of our clients are mid to smaller size.

Some of our larger clients had executed re-issuance of EMV. But we're seeing the smaller clients really lined up, as we move through 2016. So we see positive momentum with the EMV card re-issuance, moving through 2016, for our FI business.

**Dan Perlin** - *RBC Capital Markets - Analyst*

Great. Thank you.

**Operator**

Bryan Keane

**Bryan Keane** - *Deutsche Bank - Analyst*

Mark, is there a way to quantify the boost that EMV brings to a particular quarter, like in the third quarter?

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, I think EMV, one, it's creating an opportunity to have a conversation around security with clients. And clearly, it's leading to an opportunity, in terms of EMV re-issuance, on the issuing side. By the way, we'll have more cards, I think, left in 2016 to reissue than we will have reissued in 2015.

So a majority of our accounts will -- or I'm sorry, accounts on file, probably won't be reissued in 2015. So there's more to go.

And then I think the opportunity is -- continues to evolve around security-based solutions. So I think it's still early innings. Charles, I don't know if you'd agree with that comment, but it's early innings and -- go ahead.

**Charles Drucker** - *Vantiv Inc - CEO*

Yes, so on the merchant side, it is early innings. And we've started to have some of our large clients, they've converted, they'll continue to convert through the first half of the year. So the way we look at EMV is more around re-occurring type of revenues, with the tokenization point-to-point encryption that we do for the clients.

There's -- in our business, there's some hardware, not significant hardware. To us, it's about getting the hardware and the programs in the merchant's hands. So therefore that we can get them the security programs that create ongoing revenue streams for us.

So that's been our focus, where some, potentially, in the market may be more focused on hardware, we're more focused on the re-occurring revenue that we can bring to protect the clients. And that's what we're very passionate about.

Tokenization and point-to-point encryption, that also enables EMV, because that goes to protect our clients. And there is a tail into 2016 that will continue to give energy for re-occurring revenue for us.



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**Bryan Keane** - *Deutsche Bank - Analyst*

Okay. And then just specifically on FI, does it drive a couple points of the revenue growth that we're seeing, just by the re-issuance alone?

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

No, I'd say it's actually a little bit less than that in the quarter. So it is contributory, but it's probably -- it's not -- it's less than a couple percentage points. It's probably around a percentage point, I guess.

**Bryan Keane** - *Deutsche Bank - Analyst*

Okay. No, that's helpful. And then just on your comments on fourth quarter, Mark, it sounds like you're being somewhat conservative, which is great. But just on revenue per transaction in the fourth quarter, obviously, you said it dropped. I'm just wondering if there are any reasons for that drop. Just looking at it from -- on the fourth quarter versus third.

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, actually, the team is just reminding me. Yes, so we actually -- again, back to the conservative posture, that's one point. The other thing is, we do actually have a slight comp issue fourth quarter last year.

We went through the conversion, in the fourth quarter of last year, of a bank portfolio conversion on the merchant bank side. So another reason for setting that a little bit more steady or constant is the lapping of that growth last year.

**Bryan Keane** - *Deutsche Bank - Analyst*

Okay. And then anything on the revenue per transaction, in particular, that would cause it to drop from fourth to third?

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, maybe seasonality. You're going to see -- that's a good point. You're going to see high transaction growth in large clients in the fourth quarter, with the holiday spend. So that will create some pressure on revenue per transaction. I think you tend to see that, year over year.

**Bryan Keane** - *Deutsche Bank - Analyst*

Okay, that's helpful. Just last question. Maybe Charles, you can just comment on Chase Pay, since it's got a lot of the buzz here at Money 20/20. Just when you look at it, it looks like the MCX merchants will route volumes away from the traditional acquirers over to Chase payment tech. I'm just curious how worried you are about the potential loss of that volume?

**Charles Drucker** - *Vantiv Inc - CEO*

I don't see it as that way. I see -- we -- you have the CurrentC that we support, and most of our clients want a single type of reporting, a single settlement. And those are the things that we provide them. I could see us attaching to various types of solutions, potentially, Chase Pay. Most of -- a lot of our clients come right through us, and get to CurrentC. So I could still see it moving through us, and getting to Chase Pay. So I don't see that.

Obviously, they've just recently made this announcement. But it seems like there's a focus on the wallet, and those potentially, also, even if you go the other way, those would be wallet transaction. And wallet transaction are, even with one of the largest wallets in the world that is out there, it's



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a pretty slow ramp. So we have good relationships with our clients, and we want to enable our clients, and they want the efficiencies, on the back end, for that. So I see us as being able to navigate the different things that changes to provide the solutions for our clients.

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**Bryan Keane** - *Deutsche Bank - Analyst*

Okay. Congrats on the results.

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**Operator**

David Hochstim.

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**David Hochstim** - *Buckingham Research Group - Analyst*

I had a couple things. I wondered, could you talk about, in the merchant bank channel, you're seeing a big improvement in productivity. I remember, a couple of years ago, there was some frustration in the lag, in terms of new branches becoming productive, in terms of selling your services. Has that improved materially?

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**Charles Drucker** - *Vantiv Inc - CEO*

Yes, so the modifications, about a year or so, we put in to accelerate that has worked. It has worked with several of the banks that we've named earlier, some of the large banks that came on, and we're seeing the ramp much quicker. It's also helped us that payments are so predominant in the industry now, whether it's the Apple Pay wallets, the EMV, that the banks are very in tune to that. And it's a value equation that they need to help their overall business customers.

So the changes -- look, I'm pretty -- I'm very happy with the cost corrections we made in two areas -- and this is about a year -- I think about a year ago, which is in the FI business, around new sales. We're seeing the execution, and more business coming. And in the ramp-up of the banks that we're bringing up. So those two are really working well, and the adjustments that we've made are showing up in our numbers.

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**David Hochstim** - *Buckingham Research Group - Analyst*

And is there any update on your thoughts about international in the last quarter?

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**Charles Drucker** - *Vantiv Inc - CEO*

I think international is something, as we've de-levered down, we've looked at deployed capital, that it's something on our road map for our Company. But we continue to explore and look at the best ways to return capital to our shareholders.

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**David Hochstim** - *Buckingham Research Group - Analyst*

And then just finally, I guess, PayPal announced the partnership with Macy's during the quarter. I wondered, does that have any effect on your relationship with Macy's?



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**Charles Drucker** - *Vantiv Inc - CEO*

It -- so we have some large clients that are constantly, because of social media [in the ways], trying new things. So we have a strong relationship with Macy's. They're -- it's actually fun when you're with these clients, because they're trying to figure out how to navigate all the things that are happening, and increase their sales. And Macy's will always do one-off type of testing of things. And we have a strong relationship with Macy's. I think the biggest thing that's happening that we're helping our clients with is, how do we connect to these places that give buy buttons?

So that when they're shopping, the button gets pushed. And we've done a lot of -- we've done several buy buttons for our clients that the transaction, we connect and it comes right through us. So remember, large clients, they want to capture the sales, which is great. And they want to have a consolidated backend with scale, which we bring. So you could see one-off type of experiments, here and there.

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**David Hochstim** - *Buckingham Research Group - Analyst*

And then finally, just Mark, could you give us a sense of what interest expense should be in Q4?

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

I think actually, interest expense should be pretty stable, if not slightly down. So not a lot of change, in terms of interest expense. I think it's been running about \$27 million in the third quarter. I'd expect it to be pretty much that in the fourth quarter.

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**David Hochstim** - *Buckingham Research Group - Analyst*

Okay. Thanks a lot.

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**Operator**

Tien-tsin Huang.

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**Tien-tsin Huang** - *JPMorgan - Analyst*

I know you're getting a lot of questions on the merchant yield, or pricing, but just one more. Just the value-added service, just wanted to make sure. Are those repeatable or one time in nature? Just trying to understand that component of the price for merchant.

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**Charles Drucker** - *Vantiv Inc - CEO*

So value-added services around security, point-to-point encryption, is a repeatable, re-occurring type of revenue stream. And that's been our -- the biggest part of our focus. And the hardware part is a very small piece of our components. Because we believe we've got to get the hardware into their hands, so that we can get the point-to-point or end-to-end encryption, so that we can have a re-occurrence. So we're focused on things that are re-occurring, and the answer is yes.

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**Tien-tsin Huang** - *JPMorgan - Analyst*

Great. Thanks for that clarification. Then just also, Charles, just I'm curious, given your comments on banks looking for ways to protect their relationships with their customers, et cetera, and Fifth Third. Obviously, your ties there, and them being -- I think they're top 15 in debit and credit. Is there more opportunity to do more, I suppose, with Fifth Third?

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**Charles Drucker** - *Vantiv Inc - CEO*

Yes, my comment was focused more around, yes, protect their clients and the wallet. And we have always worked closely with Fifth Third. They're a great partner that -- we work with them around EMV, around security solutions. We always have strategic conversations about various wallets, how those things work.

So the partnership continues to be strong. But when you think about, with Chase, with the wallet, there is a type of scale that you need to launch those wallets. That Chase has. I have a lot of respect for what Chase, and what they do, and them as a competitor.

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**Tien-tsin Huang** - *JPMorgan - Analyst*

Yes, that make sense. Just one more, and I'll drop off. Just ISO growth in the quarter, any change in trend there?

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

No -- hey, Tien-tsin, it's Mark. That's actually continued to be pretty consistent, too. We've seen single digits, in terms of ISO and net revenue growth. So it's actually continued to perform pretty well.

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**Tien-tsin Huang** - *JPMorgan - Analyst*

Thanks. Good stuff. Appreciate it.

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**Operator**

Dave Koning.

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

Great job again. Asking a question that's been asked, just a little different way. Normally, the last few years, sequential revenue growth in Q4 is 5% to 6%. It's been very stable. This quarter, you're guiding to 0% to 2%, despite what seems like things continued to get better. Is that what you've just been saying, conservatism? Or maybe is there something driving a little worse sequential growth than we've seen in the last few years?

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

You're talking sequential growth, year over year?

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

Just sequential -- like just --

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**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Quarter to quarter?

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

Yes, quarter to quarter, right.

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes, I think we've taken -- I talked a little bit about the lapping of the fourth quarter impact, from growth in the merchant bank business in the fourth quarter last year. And then our stance, in terms of maintaining expectations that we have a high little of confidence, in terms of achieving.

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

Okay. That's fine. That's good. And then two really short ones. TRA add-backs this quarter, I think \$16.8 million or so. It sounds like next year, you're getting an incremental benefit. Should we just expect like \$19 million per quarter, next year, of add-backs?

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

I might have to follow up with you on that number, David. So keep in mind, so we just closed on the TRA with Fifth Third Bank. We also have the opportunity, on the TRA from the prior Silver Lake transaction coming in next year, too. So there are a couple of added TRA benefits coming in 2016. But we could follow up with you in more detail on that.

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

Cool. And then just one real short one. Transition costs down a lot sequentially, cut in half basically. Does that continue just to trail down?

**Mark Heimbouch** - *Vantiv Inc - COO & CFO*

Yes. We're getting close to the goal line here, in terms of integration costs. So I think through the first half, you'll see some in the fourth quarter, you'll continue to see it wind down, I think, during the first half of next year. And then yes, start to see pretty significant declines in that number.

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

All right. All good, guys. Thanks.

**Operator**

Ashwin Shirvaikar.

**Ashwin Shirvaikar** - *Citigroup - Analyst*

Congratulations on the solid quarter here. My question is, as contracts come up for renewal, you commented on pricing, and how your scale lets you fight that battle. I agree with your point of view. The question really is, as the point-of-sale choices multiply and that setup becomes more complicated, how are your renewal conversations changing because of that? What -- is there anything particular that becomes more important now? Could you comment on just your renewal conversations in general?

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**Charles Drucker** - *Vantiv Inc - CEO*

So I think with the complexities, you're right. The renewal conversations are really about -- right now, at least, they're about the security sweep, the end-to-end encryption tokenization. How do you enable more wallets, if we need, at the point-of-sale? What if you need alternative type of payment mechanism?

So it's actually very good for us, because the conversations are around more feature-based. So what was brought up earlier was your ability to route transactions. Do you have the ability to do PINless? And all of this has made it very sticky with our clients. And those are positive.

It's still competitive out there. So it's -- we want this, and we want a competitive price. And that's why I think the scale, the capabilities, really are going to matter. And you'll see people that don't have that breadth having more difficulty managing through that.

But you are absolutely right, the conversations are different. And I'm not saying that price isn't a component of it, but I'm saying it's much different. And client -- we've won new business because of our ability to implement. And we've kept business because of our ability to execute. So --

**Ashwin Shirvaikar** - *Citigroup - Analyst*

Thank you for that answer. And I apologize if this other question was asked, I did get bumped off the call. Connections here at (inaudible) are terrible. The pipeline of other merchant bank, if you could address how that pipeline looks? And now that you've done several, does that on-boarding process continue to get easier? Does it take less time? Or should we just assume the same, call it 6 to 9 months, for that process?

**Charles Drucker** - *Vantiv Inc - CEO*

So we've had a lot of great successes this year. And we have a good line of sight for what I'll call the mid-side, that 100 branch type of banks. So the pipeline is still rich with those. And the big ones that you've seen this year, they have [in full]. The contracts come up at certain times, we'll be one of them bidding on it. But the site is really good for these financial institutions that have that 75, 100, 150 branches. So it's pretty full.

I would tell you that -- your second question is, when we made the readjustment about how we ramp things up and implement and convert, we just keep getting better at it. And when we do a cut over and conversions from various places, once -- you're correct, once you do one of those from the bank, the second one is easier. But there's always differences in the bank. But this last one, we did one, this last one we just did with the large financial institution went extraordinarily well.

And I'm really proud of my team. Those are the people that make it happen every day for us.

**Ashwin Shirvaikar** - *Citigroup - Analyst*

Great. Thank you for that. Congratulations again. See you in a couple of weeks.

**Operator**

Thomas McCrohan.

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

Great quarter. Congratulations. Lapping Mercury with 16% organic revenue growth, all the new business wins that you announced and execution on the bank channel side. Obviously, you're growing just fine, without being a closed-loop network. And as many people have expressed, this Chase Pay announcement is getting a lot of attention. Because people are trying to figure out, longer-term, while Vantiv is growing just fine right now.



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But as we think, Charles, longer-term, if other big banks decide to try to replicate what Chase did, help us think through how Vantiv competes in a world of these hybrid closed-loop networks?

**Charles Drucker** - *Vantiv Inc - CEO*

So let's talk. First, Chase net has been out there a couple of years now. One of the things that you've got to think, as you talk to big retailers, is that one of the biggest challenges in the payment network, it works great, but retailers have always been concerned about interchange. And some of these large banks are the biggest recipient of interchange that happened. So a lot of times, merchants, whether they potentially think they can save money -- and quite frankly, with our scale, and the way we do the other percentages of transactions, we're very competitive.

Even if there's -- if the Visa network, given there are some economies of how a Chase net would do it. So that's one in the psyche. Two, we have a lot of transactions. So these networks potentially, in the future, could look for us to connect to them. And we make our money on the click fee, not on the interchange, on the components. So we could view them as just another network.

That instead of doing it to the three or four AmEx fees networks, we could potentially, if those happened, put a pipe to these places, and route transactions. Because the plumbing. I'll call it, is more difficult than people think, to put the plumbing and the tracks there.

And for us, it's a click. We're processing the transactions where we send it, to get the merchant the best deal, is -- we're Switzerland.

So I don't see a lot of those happening. But if they are, we're one of the -- having scale like us leaves us in the best position to be able to compete.

So a lot of things changing in the world. And I have a high respect for what these organizations can do, but we have a lot of capabilities that we can help either -- we can help accelerate it, if things happen there.

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

Excellent. Thank you for that. Just one follow-up. In the bank channels, what kind of merchants are you boarding through that channel? And is that channel also feeding the integrated, like Mercury and those integrated channels that you have, as well?

**Charles Drucker** - *Vantiv Inc - CEO*

So it varies. It depends upon the region, what the bank specializes. Some of those bank channels are strong in retail, some of those bank channel works in different verticals. But it's kind of across-the-board. Their mid-sized type of sales, a couple of hundred to half a million. And then some of them have a large book of commercial lending that we've been able to bring to more mid-sized type of clients.

So it's across the board. And one of the uniqueness about us is that we do have an opportunity to partner up integrated payment players with banks, to really bring value to both ends of the equation. And our integrated payment space, plus the bank channel, is a unique type of connection that we have an ability to bring in the future. So it's across-the-board, but the bank channels are doing very well for us.

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

Thanks guys.

**Charles Drucker** - *Vantiv Inc - CEO*

So I want to thank everyone for joining the call today. If you have any additional questions after today's call, please reach out to us using the contact information available on the investor website, and we will be happy to help you. So thanks again, and have a great day.



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**Operator**

This does conclude today's conference call. Thank you all for your participation. You may now disconnect.

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