

FDC
First Data Corp.

TMT, Finance/Real Estate

01/22/2018

L LONG
PRESENTED
CURRENT

DATE	01/19/2018		PRICE	\$24.16	MARKET CAP	\$22.58B
PRICE	MARKET CAP	ENT VALUE	Image type unknown Chart http://portal.dmlc.com/storage/ideas/Chart/a08A000001E4V62IAF.jpg			
\$18.00	\$16.99B	\$38.11B				
P/E RATIO	BOOK VALUE	DIV YIELD				
23.68x	\$2.27	0%				
SHARES O/S	AVE DAILY VOL	SHORT INT				
944.00M	6,256,133	7.57%				

First Data Corp. provides commerce-enabling technology and solutions. It provides secure and innovative payment technology and services. The company operates through three business segments: Global Business Solutions, Global Financial Solutions and Network & Security Solutions. The Global Business Solutions segment provides retail point-of-sale merchant acquiring and eCommerce services. This segment also provides next generation offerings, such as mobile payment services, web store-in-a-box solutions and cloud-based clover point-of-sale operating system. The Global Financial Solutions segment provides credit solutions for bank and non-bank issuers, such as credit and retail private-label card processing; and licensed financial software systems, such as VisionPLUS bank processing application and lending solutions. This segment also offers related services, including card personalization and embossing, statement printing, client service and remittance processing. The Network & Security Solutions segment provides EFT network solutions, such as STAR Network and debit card processing solutions. It also offers stored value network solutions, including money network, ValueLink, Gyft, and transaction wireless; and security and fraud solutions, such as TransArmor and TeleCheck. The company's other services include mobile payments, eCommerce and prepaid solutions, as well as payment processing, fraud protection and authentication solutions, online banking, check guarantee and verification services and point-of-sale services to its customers. First Data was founded in 1971 and is headquartered in Atlanta, GA.

Publicly traded companies mentioned herein: First Data Corp (FDC), Global Payments Inc (GPN), KKR & Co LP (KKR), Worldpay Inc (WP)

Highlights

Despite negativity surrounding First Data Corp's (FDC) growth prospects and leverage profile, the presenter is long at \$17, and views the stock as "too cheap" compared to its global peers. In his opinion, the North America acquiring market is stabilizing, should return to growth over the next two years, and management will [continue to] use FCF to delever the balance sheet. Once investors start to value the company based on EPS, as opposed to EBITDA, the "massive" valuation discount will erode. If his model is accurate, FDC can achieve its leverage target (4x) by 2019 (down from ~6x today), and EPS could reach \$1.90-2.00 by 2020. Applying a reasonable, mid-teens multiple to this estimate results in a \$28-30 price objective (over 12-18 months).

- Valued at \$29B, FDC was one of KKR's largest deals. The LBO was nearly a failure, but management was able to weather the storm, post-financial crisis. The presenter explained that FDC had been "starved" while private, and came public at ~9 turns of leverage in 2015. CEO Frank Bisignano has been at FDC since 2013, and is "well-regarded" in the industry and by investors.
 - Prior to joining FDC, Bisignano was Co-COO for JPMorgan Chase, and CEO of its Mortgage Banking unit. He owns millions

- of shares and has been a good recruiter of talent over the years. If the stock can get to \$30+, he stands to make \$320MM. In addition to liking Bisignano, a participant noted that CFO Himanshu Patel is, “very bright” and has recruited a good team under him.
- Henry Kravis’ presence on the Board of Directors is evidence of FDC’s importance to KKR.
- FDC does not need to grow as quickly as its competition for the long position to yield meaningful positive returns. The industry is growing quickly enough that FDC, Worldpay, and Global Payments can all grow. Compared to those companies, FDC is extremely cheap, and as its leverage is reduced, investors should look at the stock on an EPS basis.
 - While First Data’s JV acquiring business and relationships with big banks haven’t been comping well, the presenter thinks trends will moderate. At the same time, the SMB business appears to be inflecting.
 - The JVs used to grow mid-single digits, before FDC experienced some well-publicized issues with the big banks. The presenter thinks, “The business will not decline at the rate it had, and will be fine”.
 - SMBs should grow this quarter (flat to low-single digits).
 - At \$17, FDC is trading at just under 12x forward Street earnings estimates, and 10x EBITDA. By comparison, Worldpay is trading at 21x Street EPS estimates for 2018, and 10x EBITDA; and Vantiv used to trade a few turns higher on EV/EBITDA. And, Global Payments is trading at 23x the Street EPS estimates, and 15x EBITDA.
 - The presenter attributes the valuation disconnect on an earnings basis primarily to FDC’s leverage, its portfolio mix (the layers of software that differentiate the businesses), and a late foray into ISV. While under KKR, the business remained stable, but it could not grow via acquisitions.
 - First Data completed the acquisition of CardConnect in in 2017, and while the presenter is “not sure it’s better than Mercury”, both are good assets. The ISV channel generates “stickier” business, and there is enough runway for growth that one solution doesn’t have to be better than another.
 - The group discussed how the Mercury deal changed the composition of Vantiv’s business for the better, and its growth rate in subsequent years was in the mid-teens. The same can be said of Global Payments’ acquisition of ATP, which “remarkably changed the whole industry”.
- FDC will benefit from tax reform. The group briefly discussed how its tax rate will decline from 35% today, to 28-29% next year, and it is expected to settle in the low 20%^s. Its NOL will be worth less under tax reform, but the lower tax rate more than offsets this.
 - FDC is expected to hit the interest cap, which is why the tax rate won’t drop to the low 20%^s immediately. It is not a “cash taxpayer” until 2020, so any concern about the tax rate is misguided.
- Putting it all together, the presenter sees a high probability of FDC earning \$1.90-2.00/ share in 2020, and with the stock trading ~\$17-18, it is sub-10x his estimate. If the multiple can expand to just 15x, which is still well-below peers’ present P/E multiples, the stock would rise by 55%. Assuming a market multiple yields a double. The business is improving with exposure to higher-growth channels, and as leverage falls toward management’s target (just two years away), investors should become more receptive to the story.
 - With a 10% FCF yield, it is reasonable to think that the upside could be even greater than the presenter is modeling.
 - Even if there is no multiple expansion, the stock could rise by ~20% if his low-end EPS forecast is accurate (based on the current 12x forward multiple).
- When asked about KKR selling stock and the shareholder base, the presenter said KKR sold less than expected, but this is a near-term overhang. More important, in his opinion, is the leverage situation. Mutual funds don’t, or can’t own FDC at 6x. It’s reasonable

- to think that the path to 4x will be clear, and as mutual fund portfolio managers see things more clearly, some may be willing to step-in at 5x or just below that level.

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