

VISA INC. AND THE GLOBAL PAYMENTS INDUSTRY¹

Professors Neil Bendle and Dan Horne wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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Amy Wilkins² was nervous. She was preparing for what was arguably the most important job interview of her career. She was fascinated by the global payments industry and working at Visa Inc. would be a dream come true. To prepare for her interview, Wilkins wanted to make sure she clarified her understanding of the payments industry and sat down to complete her analysis. She knew that a strong performance in the interview would give her an excellent chance to get her dream job. It was a risk, but she decided to be bold – she would come up with a recommendation for some action that Visa should take.

VISA COMPANY HISTORY

Bank of America launched the first successful credit card, the Bank Americard. The product began with a small, unsolicited mailing of live cards in 1958. By offering an easy consumer credit facility to the American middle class, it was able to steadily increase market penetration. The company grew across the United States and expanded internationally in the 1970s. A major change occurred with the addition to the Visa range of a debit card in 1975.

Visa emerged from Bank of America to become an independent entity united by a global and less America-centric brand name. Also in the 1970s, Visa created the VisaNet, an electronic authorization, clearing and settlement system.³ This made facilitating payments much simpler, and Visa grew in its importance to cardholders, merchants and financial institutions. Growth was by no means assured in this two-sided market as merchants were only willing to invest in new payments technology once a significant number of consumers demanded card acceptance. At the same time, getting and using the card was not valued unless there existed a large number of merchants who could actually use the cards to take payments. Visa succeeded because it solved the problems faced by all of the key players in this arena. For example, VisaNet made interactions between financial institutions smoother. Cardholders could use their

¹ This case has been written on the basis of published sources only. Consequently, the interpretation and perspectives presented in this case are not necessarily those of Visa Inc. or any of its employees.

² Amy Wilkins is a fictional character. All the data is from publicly available sources.

³ Visa website, <http://usa.visa.com/about-visa/our-business/history-of-visa.jsp>, for the company history, accessed March 27, 2014.

plastic either for convenience or to instantly purchase on credit while merchants limited the cash they needed to hold and saw increased sales when they began accepting Visa payments.

Visa was structured into a number of different regional groupings. In addition to the core of Visa USA, Visa Canada and Visa Europe had major operations. The other regions were Asia Pacific (Visa AP), Latin America (Visa LAC), Visa Central and Eastern Europe, Middle East and Africa (CEMEA); together, these regions formed Visa International. In 2007, Visa USA, Visa Canada and Visa International merged to form Visa Inc. Visa Europe maintained an affiliation with a separate ownership structure, owned by participating European banks. Visa Europe, though running independently, held various contractual relationships with Visa Inc. and owned shares in the global entity.⁴ When Visa Inc. was established, a balance sheet was created for the company and a notional “purchase price” was created. The values of the assets and liabilities were then entered into the new balance sheet of Visa Inc. at estimates of their fair value (see Exhibit 1). Shareholdings were divided between the regional entities based upon the proportions of projected net income due from each region in 2008.⁵

In March 2008, Visa Inc. underwent an initial public offering (IPO), which meant that the financial institutions held only a minority of the shares.⁶ This large and successful IPO left the bulk of shares in Visa Inc. to be publicly traded.

THE GLOBAL PAYMENTS INDUSTRY⁷

The global payments industry consisted of:

- Paper-based payments: cash, cheques, money orders, etc.
- Card-based payments: credit cards, debit cards, ATM cards, etc.
- Other electronic payments: wire transfers, electronic benefits transfers, automated clearing-house payments, etc.
- So-called “emerging payments” like cloud-based services (PayPal), cryptocurrencies (Bitcoin), and mobile phone-based payments (such as the Starbucks phone payment app). These payment accounts might be prepaid or linked to a credit card or a bank account.

Visa Inc., though traditionally associated with credit cards, had broadened its offerings to a wide range of cards. The company also saw great opportunity for growth in various electronic forms of payment. Visa Inc. expected the trend away from paper-based payments to continue – a trend that it had helped to pioneer – given the convenience, security, enhanced service and rewards associated with cards and other-electronic based payments.

Within the card-based payments sector there were three primary types of products.

- “Pay now” cards or “debit cards”. These allow a purchaser’s funds to be automatically debited when a transaction occurs.
- “Pay later” cards or “credit cards”. These allow the cardholder to “borrow” to make the purchase. This is either paid off at the end of a specified period or the balance is allowed to “revolve”, typically accruing interest.

⁴ Visa Inc. 10K 2007, Note 4, pp. 102-104.

⁵ Visa Inc. 2007 10K, Note 5, pp. 104-06.

⁶ Visa Inc. 2008, 10K, p. 5.

⁷ Visa Inc. 2008 10k, p. 6.

- “Pay before” cards or “prepaid cards”. These cards act like debit cards but are not tied to a bank account. Rather, they have a certain amount of funds loaded onto them and they can be used for electronic payments.

In the global payments environment, Visa faces a set of entrenched, successful competitors as well as some potentially disruptive new comers. These include:

- MasterCard: Visa’s long-time biggest challenger, the two are often seen by consumers as undifferentiated. Although MasterCard is smaller than Visa, it operates on a nearly identical business model.
- American Express: Long considered a more elite product, AMEX has both fewer cardholders and fewer merchants. As it acts as both issuer and merchant acquirer, AMEX, which already charges more for its services, does not have to share the income with two separate banks. It is thus very profitable.
- China Union Pay: Now the number one issuer of cards in the world, CUP has its eye on expanding rapidly out of its Asian base, 98 per cent of its 2.9 billion, mostly debit, cards are issued in China. While transaction volume lags behind Visa, if it begins to successfully internationalize, it will be a formidable competitor.

Others card issuers like Japan-based JCB and Discover Card have smaller but still substantial numbers of card holders and transaction volume.

While they have very limited adoption by consumers, Visa is also paying attention to some new market entrants. For example, PayPal, with its web-based and mobile platforms, hopes to provide a direct link between customers and merchants, thereby replacing the current middlemen (Visa, MasterCard, etc.).

WHAT DOES VISA INC. DO?

First Wilkins asked herself, what does Visa Inc. do? Outsiders often compared Visa to a bank but she did not think that was correct. Despite the Visa brand’s long history, the current company, Visa Inc., had only been created in 2007 followed by an IPO in 2008. Wilkins dug into the past accounts of the company to find out more about the business. Visa gave a diagram of its business model that involved four players in addition to Visa itself:⁸

1. Merchants: places that accept Visa cards. For example, Joe’s Pizza is a merchant.
2. Merchant Acquirer: a financial institution that signs up the merchants. For example, Joe’s Pizza banks with TD Bank and the bank worked with Joe to allow him to take Visa payments.
3. Issuer: another financial institution that produces and distributes Visa-branded cards to consumers and businesses. For example, Chase offers a variety of credit cards and credit limits to its customers.
4. Cardholders: the user of the card. For example, Manuel, a student, applied for a Chase Visa credit card. Chase issued him one with a \$1,000 line of credit. Manuel borrows from Chase when charging a pizza to his credit card and pays back the loan either at the end of the billing cycle or over time.

In a transaction, VisaNet provides the linkage between the acquirer — such as the merchant’s bank — and the issuers — such as the cardholder’s bank. They process the request for funds from the merchant and transfer the funds from the cardholder’s account. Visa Inc. thus facilitates the interaction between acquirers and issuers, ensures that the technology works smoothly and maintains the Visa brand that

⁸ Visa 10K, 2007, p. 13.

internationally signals hassle-free payment. Yahoo finance summarized Visa Inc. as “a payments technology company [that] operates as a retail electronic payments network worldwide.”⁹

Wilkins had a quick look at how much Visa spent on non-marketing expenditures in the hope of better understanding the technological and other capabilities as the potential source of competitive advantage (see Exhibit 2). She wondered whether “payments technology company” entirely captured what Visa Inc. did. At the beginning of the 2008 10K – a company’s annual returns to the U.S. Securities and Exchange Commission (SEC) – the company explained the business as follows: “Visa operates the world’s largest retail electronic payments network and manages the world’s most recognized global financial services brand.”¹⁰

Wilkins turned to a broader consideration of the global payments industry to better understand both the industry and Visa’s competitive position.

POSITIONING WITHIN THE GLOBAL PAYMENTS INDUSTRY

In the global payments industry, an industry full of big names, Visa Inc. stood out from the crowd. The Visa brand name was widely understood to stand for easy payments. Merchants all around the world posted the Visa logo on their doors to let cardholders know they were ready to accept payments. Visa Inc. sponsored sporting events and its marketing-related expenditures were sizable (see Exhibit 3).

Visa used the tagline “everywhere you want to be” to convey their global nature and ubiquitous merchant network. Clearly, if customers were concerned about being able to use their cards in most places, Visa was the hands-down winner.

Still, there were a number of notable competitors. MasterCard was well known with a high profile communications strategy and would surely be a tough competitor. MasterCard’s positioning strategy also involved access to a wide variety of merchants and experiences. This was echoed in slogans such as “There are things money can’t buy. For everything else, there is MasterCard” and “Master the possibilities.”

Then there was American Express. When she secured her first AMEX card, Wilkins remembered feeling that the simple act of using it illustrated that she was successful. Wilkins wondered how American Express accounted for such an emotional association; it had to be worth a huge sum. AMEX tried to capture this sentiment by emphasizing that cardholders were not customers but “members” who were treated differently; this exclusivity was emphasized in its tagline: “Membership has its privileges.”

Wilkins thought China Union Pay was the wildcard here. While they had not actively pursued customers outside their base in China, they were clearly positioned to begin expansion. In China, they were known as Yin Lian, which meant “banks united.” Clearly, they would need a repositioning to move out of their home base. Wilkins created a Porter’s Five Forces Model for the industry. It was not that easy and she was not entirely sure how to classify some of the major players. The future seemed to hold all sorts of possibilities for new payments technologies but how would that impact the current players? That said, the exercise was probably useful and she felt she had a better understanding of the industry once she had completed it.

⁹ Yahoo finance, Visa Inc. (V) <http://ca.finance.yahoo.com/q?s=v>, accessed March 21, 2014.

¹⁰ Visa Inc. 10K Year Ending 30th September 2008, p. 4.

As a data person, Wilkins wanted some hard numbers to better understand the Global Payments Industry. She again looked at Visa Inc. 10Ks. These reports contained details of the relative position of the companies in the industry (see Exhibit 4). This information was designed to allow investors to understand the strengths and weaknesses of Visa Inc.

Wilkins wanted to have an objective measure of how competitive the industry was. To do this, she constructed a Herfindahl-Hirschman Index (HHI). This index was created by summing the squares of the market shares of the competitors in the industry. The HHI measured how concentrated any industry was. Higher concentrations, often described as those above 0.25, were suggestive of less competition as this indicated a smaller number of large players. She felt the HHI was quite informative and this led her to wonder what the finding meant for the likelihood of government intervention, but it also left her thinking about how the market could be defined in something the size of the global payments industry.

VISA'S COMPETITIVE ADVANTAGE

Something was clearly going right for Visa Inc. She looked at the record of the stock price compared to the Standard and Poor's 500 and the Data Processing Index (see Exhibit 5). It was a record any company would be proud of and clearly the Visa brand was important to the company (see Exhibit 6). She was not sure exactly what the brand stood for, or how it was positioned against its competitors, but she talked to a few of her friends and put together an informal positioning map. After that, she felt she had a slightly better understanding of the big picture within the industry and how the players related to one another.

One thing that was hard to miss was the relative success of Visa Inc. within the global payments industry. She wondered what role success played in creating success in this industry. This phenomenon, known as the Matthew Effect (from the Biblical story), suggested that those who were successful would become more successful due to their past success. Market share seemed to capture the idea of relative success within the industry. She wondered what Visa Inc.'s market share was. What should Visa Inc.'s approach to market share be?

INTERVIEW PREPARATION

Wilkins looked at the all the information that she had accumulated. What did it mean? More specifically, why had Visa Inc. been successful? If she could find the source of competitive advantage, was that advantage sustainable? What did Visa have to do, or continue doing, to ensure success?

She scribbled seven notes to remind her of items she would cover at the interview:

- Global Payments Industry
- Five Forces
- Herfindahl-Hirschman Index
- Positioning Map
- Source of Competitive Advantage
- Market Share
- Going Forward

EXHIBIT 1: ASSETS AND LIABILITIES

<i>All Millions</i>	<i>09/30/2013</i>	<i>09/30/2012</i>	<i>09/30/2011</i>	<i>09/30/2010</i>	<i>09/30/2009</i>	<i>09/30/2008</i>
Total Current Assets	\$7,822	\$11,786	\$9,190	\$8,734	\$9,241	\$11,174
Investments & Client Incentives	\$2,849	\$3,341	\$796	\$195	\$620	\$997
Property, Equipment & Technology, Net	\$1,732	\$1,634	\$1,541	\$1,357	\$1,204	\$1,080
Total Other Assets	\$521	\$151	\$129	\$197	\$125	\$634
Intangible Assets	\$11,351	\$11,420	\$11,436	\$11,478	\$10,883	\$10,883
Goodwill	\$11,681	\$11,681	\$11,668	\$11,447	\$10,208	\$10,213
Total Assets	\$35,956	\$40,013	\$34,760	\$33,408	\$32,281	\$34,981
Total Current Liabilities	\$4,335	\$7,954	\$3,451	\$3,498	\$4,442	\$7,165
Deferred Tax Liabilities	\$4,149	\$4,058	\$4,205	\$4,181	\$3,807	\$3,811
Total Other Liabilities	\$602	\$371	\$667	\$715	\$839	\$1,728
Total Liabilities	\$9,086	\$12,383	\$8,323	\$8,394	\$9,088	\$12,704
Total Equity	\$26,870	\$27,630	\$26,437	\$25,014	\$23,193	\$22,277

Source: Visa Inc. 10Ks 2007-2013

EXHIBIT 2: NON-MARKETING EXPENDITURES

Year Ending	Personnel expenses	Network & processing¹	Professional fees²	Depreciation & amortization	General & administrative expenses³	Litigation provision (benefit)
09/30/2009	\$1,143	\$393	\$353	\$226	\$338	\$2
09/30/2010	\$1,222	\$425	\$286	\$265	\$359	-\$45
09/30/2011	\$1,459	\$357	\$337	\$288	\$414	\$7
09/30/2012	\$1,726	\$414	\$385	\$333	\$451	\$4,100
09/30/2013	\$1,932	\$468	\$412	\$397	\$451	\$3

All \$ Millions

Notes¹ Called Network, electronic data processing (EDP) & communications expenses prior to 2012³ Called Professional & consulting fees prior to 2012⁴ Called Administrative & other operating expenses prior to 2012

Source: Visa Inc. 10Ks 2007-2013

EXHIBIT 3: MARKETING SPENDING OF VISA INC.

Year Ending Sept 30	Marketing Expenditures*
2005**	\$457,000
2006**	\$474,000
2007**	\$581,000
2008	\$1,016,000
2009	\$918,000
2010	\$964,000
2011	\$870,000
2012	\$873,000
2013	\$876,000
	\$ Thousands

Notes:

*Advertising, marketing & promotion prior to 2012 accounts

**2007, 2006 & 2005 figures for Visa USA and Subsidiaries

Source: Visa Inc. 10Ks 2007-2013

EXHIBIT 4: COMPETITOR DATA FOR PAYMENTS INDUSTRY

<i>Company</i>	<i>2006</i>	<i>2007</i>	<i>2008</i>	<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>
Payments Volume (Billions)							
Visa Inc.	\$2,127	\$2,457	\$2,727	\$2,793	\$3,273	\$3,768	\$4,018
Master Card	\$1,417	\$1,697	\$1,900	\$1,852	\$2,047	\$2,430	\$2,693
American Express	\$556	\$637	\$673	\$613	\$702	\$808	\$884
Discover	\$96	\$102	\$106	\$100	\$107	\$114	\$122
JCB	\$63	\$55	\$63	\$75	\$87	\$160	\$179
Diner's Club	\$22	\$29	\$30	\$25	\$26	\$28	\$27
Total	\$4,281	\$4,977	\$5,499	\$5,458	\$6,242	\$7,308	\$7,923

Total Volume (Billions)							
Visa Inc.	\$3,230	\$3,822	\$4,346	\$4,423	\$5,191	\$6,029	\$6,409
Master Card	\$1,922	\$2,276	\$2,533	\$2,454	\$2,727	\$3,249	\$3,647
American Express	\$562	\$647	\$683	\$620	\$713	\$822	\$888
Discover	\$114	\$119	\$120	\$109	\$114	\$122	\$130
JCB	\$70	\$61	\$68	\$83	\$93	\$166	\$186
Diner's Club	\$22	\$30	\$31	\$26	\$27	\$29	\$28
Total	\$5,920	\$6,955	\$7,781	\$7,715	\$8,865	\$10,417	\$11,288

Transactions (Billions)							
Visa Inc.	44	50.3	56.7	62.2	70.8	77.6	81.6
Master Card	23.4	27	29.9	32.1	34.8	39.8	46.3
American Express	4.5	5	5.3	5.1	4.8	5.3	5.9
Discover	1.4	1.6	1.6	1.7	1.8	1.9	2.1
JCB	0.7	0.6	0.7	0.8	0.9	1.4	1.6
Diner's Club	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Total	74.1	84.7	94.4	102.1	113.3	126.2	137.7

Cards (Millions)							
Visa Inc.	1,254	1,592	1,717	1,808	1,897	2,011	2,128
Master Card	817	916	981	966	975	1,059	1,158
American Express	78	86	92	88	91	97	102
Discover	57	57	57	54	56	59	62
JCB	59	58	60	61	64	77	79
Diner's Club	7	7	7	7	6	6	6
Total	2,272	2,716	2,914	2,984	3,089	3,309	3,535

Source: Visa Inc. 2007 10-K 2008 10-K 2009 10-K 2010 10-K 2011 10-K 2012 10-K 2013 10-K
All Data for Calendar Years

Source: Visa Inc. 10Ks 2007-2013.

EXHIBIT 5: PERFORMANCE OF VISA INC. SHARES

Company/Index	9/30/08	9/30/09	9/30/10	9/30/11	9/30/12	9/30/13
Visa Inc.	100	113.4	122.6	142.6	225.1	323.0
S&P 500 index	100	93.1	102.6	103.7	135.1	161.2
S&P 500 Data Processing Index	100	98.6	99.7	110.1	156.3	218.3

Source: Visa Inc. Annual Report, 2013, p. 2

EXHIBIT 6: VISA STATEMENT ON THEIR BUSINESS

Our business primarily consists of the following:

- We own a family of well known, widely accepted payment brands, including Visa, Visa Electron, PLUS and Interlink, which we license to our customers for use in their payment programs;
- We manage and promote our brands for the benefit of our customers through advertising, promotional and sponsorship initiatives and by encouraging card usage and merchant acceptance;
- We offer a wide range of branded payments product platforms, which our customers use to develop and offer credit, debit, prepaid and cash access programs for cardholders (individuals, businesses and government entities);
- We provide transaction processing services (primarily authorization, clearing and settlement) to our customers through VisaNet, our secure, centralized, global processing platform;
- We provide various other value-added services to our customers, including risk management, debit issuer processing, loyalty services, dispute management and value-added information services;
- We develop new products and services to enable our customers to offer efficient and effective payment methods to their cardholders and merchants; and
- We adopt and enforce a common set of rules adhered to by our customers to ensure the efficient and secure functioning of our payments network and the maintenance and promotion of our brands.

Source: Visa Inc. 10K, Year Ended 30th September 2008, p. 4.