

Trading update, first quarter FY16

16 July 2015

Strategic and Operational Review

Brian Cassin
Chief Executive Officer, Experian

1. Introduction

Good morning, ladies and gentlemen, and thank you for joining our Q1 Trading Update call. I am here today with Lloyd Pitchford, who will take you through the trading performance following my opening comments. We will then open the lines for your questions.

2. Q1 Performance

We had an encouraging start to the financial year with organic revenue growth of 3%, driven by good execution against our strategy to focus on our biggest opportunities for growth, while taking aggressive steps to improve performance in some parts of the portfolio. As a result, we saw good progress in key areas, including software and analytics, fraud and identity management, consumer and business information, and further improvement in performance in Brazil. We made considerable progress in our North America Consumer Services business by building the Experian.com brand and transforming our proposition to consumers.

As we progress through the year, we expect to build on our momentum. Our aim is for gradual improvement in organic growth as we continue to execute on our growth strategy and as the declines in North America Consumer Services moderate as we move into the second half.

3. Regional Update

North America

Now I will briefly summarise the results by region. In North America, the environment for lending is healthy, and activity levels for credit marketing and new-account origination are high across all types of lending products, which is driving good volume growth for consumer and business information and for value-added products like scores and fraud indicators. Our high-growth vertical markets are doing very well. In healthcare, we closed FY15 with record levels of sales bookings, and our sales momentum continued into the first quarter, with additional new business wins. Our integrated product strategy is working very well, and our average deal size has doubled and now includes an average of about seven products. Automotive information continues its track record of double-digit growth, which has really been fuelled by a good new and used-car market, and by further penetration into the dealer and manufacturing segments.

In Consumer Services, the rate of decline further moderated to 10%, as we continued to make significant progress in transforming this business. Consumer awareness of

the Experian.com brand continues to grow, driven by our 'Swagger' advertising campaign, and the enhancements to our core product have been well received by consumers. Growth in the Experian.com brand was up 20% in the quarter, and we completed the migration of all of the other direct-to-consumer brands to Experian.com, which will greatly simplify our business going forward.

We see opportunity in Consumer Services to operate both in the paid-for space and in the free space, serving the needs of two clearly different consumer segments. During the quarter, we piloted the introduction of a truly free proposition to consumers using our well recognised FreeCreditReport.com brand. This brand is deeply embedded in the minds of US consumers and we have attracted nearly half a million members in our pilot-testing phase without any advertising. It is still early days but we are encouraged by the response and by our ability to monetise the traffic coming through the site.

Latin America

Turning to Latin America, we are building on our momentum and we delivered another quarter of good growth. The macroeconomic environment in Brazil is expected to remain weak through the calendar year, so success here is really down to our own efforts in finding and exploiting new pockets of growth. Growth in Credit Services was 8%, with solid growth in Brazil and a positive contribution from our other Latin American bureau.

UK and Ireland

Our UK and Ireland business delivered another quarter of good growth. We made good strategic progress as we secured new client wins by combining capabilities from across all of our main business lines. These are the kinds of deals that have set us apart from our competitors and create high-value, long-term relationships with our clients.

EMEA/Asia Pacific

Our performance across EMEA/Asia Pacific is steadily improving, following the actions we have taken there in recent years. The region is now on a path to consistent, more profitable growth, and that is starting to come through in the numbers.

4. Disposal of non-core Businesses

In our strategy presentation in January, we told you that we had begun a process of evaluating non-core business lines, with an expectation of disposing of a few small operations. We are well down that path and expect a few announcements over the coming weeks. While we did not formally announce it, we did complete the sale of our interest in the Morocco credit bureau. This was a very simple operation and simply not core to our global position in credit services. In aggregate, we do not expect these disposals to result in a big change to our overall financials but it will clarify our strategy and free up resources and management time to focus on our main growth priorities. You will begin to see that happening from this point on.

With that, let me turn the call over to Lloyd, who will take you through the trading performance.

Financial Review

Lloyd Pitchford
Chief Financial Officer, Experian

1. Highlights

Thank you, Brian, and good morning everyone. Turning to our trading performance in the quarter, we started the year in line with the expectations we laid out at our annual results, with total revenue growth at constant exchange rates of 3% and organic revenue growth of 3%. At actual exchange rates, total revenue was 6% lower due to FX movements relating to the strength of the US dollar.

2. Performance by Principal Activity

Looking at results by principal activity:

- Credit Services continued strongly, up 7% overall.
- Decision Analytics had a strong quarter, up 9%.
- Marketing Services declined by 2%.
- Trends in Consumer Services continue to improve, down 6% overall for the Group but on an improving trajectory.

3. Regional Performance

North America

Turning to performance by region, in North America, both total and organic revenue growth were flat.

- Credit Services had organic growth of 8%.
- Decision Analytics was down 1%.
- Marketing Services declined by 4%.
- Consumer Services declined by 10%.

We had a good quarter in Credit Services. In consumer information, we saw growth in credit acquisition and prospecting volumes. Business information performed well. There was strong growth across both the automotive and healthcare verticals. While Decision Analytics posted a small decline in the quarter, this was largely due to phasing, and we continue to see good progress in software, with new PowerCurve deployments and strength in fraud and identity management.

In Marketing Services, we continued our strong progress in cross-channel marketing (CCM), which partially offset weakness in the legacy email channel. We expect this to

continue to be a drag as we progress through the year, while the CCM platform builds scale.

As Brian has already referenced, declines on Consumer Services continue to moderate with the growing contribution from newly acquired Experian.com members, where revenues rose 20% in the first quarter.

The next milestone for our direct-to-consumer business is expected in the third quarter, when we launch our new technology platform and we expect second-quarter growth rates to be similar to the first quarter, as we prepare for that launch.

Finally, as expected, Affinity remains weak, although we are seeing some clients beginning to resume marketing activities to their customers, which will likely benefit as we move into FY17.

Latin America

In Latin America, at constant exchange rates both total and organic revenue growth was 7%. Organic revenue was up 8% in Credit Services, flat in Decision Analytics and, while Marketing Services was down 26%, this was off a very small base.

In Credit Services, we saw strength in both consumer and business information in Brazil. Consumer information benefited from a weak comparative as we lapped the period of the World Cup but, excluding this, the underlying growth remains solid and we saw strong growth in other Latin American bureaux.

Decision Analytics was flat for the quarter, largely down to phasing, and we see good prospects for the remainder of the year.

The decline in Marketing Services was due to reduced levels of demand for prospecting by clients, as they cut back on marketing activity, given the difficult economic backdrop.

UK

At constant exchange rates in the UK, total and organic revenue were up 5%. Organic revenue growth was 2% in Credit Services, 15% in Decision Analytics and 5% in Consumer Services, with Marketing Services down 1%.

In Credit Services, we had a solid quarter, with good progress on securing new client wins in the banking sector, and further progress in business information, particularly from sales of more sophisticated products.

Decision Analytics had an exceptionally strong quarter, up 15%, down to a very strong performance in identity verification and some elements of contract phasing. We are also seeing a first-time revenue contribution from some of the 41st Parameter wins we had last year.

There was also an element of phasing in Marketing Services, where the decline was due mainly to the lag between contract bookings and revenue recognition in our data-quality business. Cross-channel continues to progress well in the UK and build scale.

Consumer Services had another solid quarter, as we continued to add new members.

EMEA/Asia Pacific

Finally, in EMEA/Asia Pacific, at constant exchange rates both total and organic revenue growth was up 7%.

- Credit Services was flat.
- Decision Analytics performed very strongly, up 17%.
- Marketing Services also had a strong quarter, up 8%.

In Credit Services, we have seen some impact from political uncertainty in markets like Russia but, on the whole, conditions in Europe for us are stable and we have seen good growth in Asia Pacific.

Decision Analytics is seeing a very strong revival on the back of the strength in software, fraud and analytics, and we signed a significant new contract for 41st Parameter with a major e-commerce provider in Asia Pacific.

Marketing Services reported good growth as we made further progress with cross-channel marketing and in winning new clients.

4. Outlook

Looking ahead, our expectations for the full year are unchanged, barring movements in foreign exchange. We continue to expect organic revenue growth to progress during the year as we focus on our growth initiatives, and during the second half in particular, as declines moderate in North America Consumer Services.

For the full year, we expect margins to be stable at constant currency, and to deliver progress in constant-currency benchmark earnings per share.

Finally, foreign exchange rates continue to be volatile. We now expect the translation drag for the full year to be around 7% on EBIT year on year, which includes about a 40-basis-point impact on margin, based on current spot rates.

With that, let me hand you back to Brian.

Summary

Brian Cassin

Thanks, Lloyd. To summarise our comments this morning, our Q1 results are consistent with the direction we laid out at our year-end results. We are executing well and we are on a clear path to returning to sustainable, mid-single-digit growth. With that, I will open the line to your questions.

Questions and Answers

Robert Plant, JP Morgan

At the full-year stage, Brian, you seemed a little more confident than at Q3 about Affinity coming back. Is that still the case? More generally in Consumer Services in North America, do you think there will be any quarter this year when this business could get back to growth?

Brian Cassin

I will let Lloyd come in on the growth point in a second. On the Affinity point, I do not think anything has really changed. We have seen some very significant renewals with some of our key clients, which gives us a lot of confidence about the long-term direction of the business. I think we referenced one major client we thought was going to get back in marketing earlier this year. We are seeing some of that come through, but the forces that we laid out at the end of the year are still in play – a market which is not yet fully back to really aggressive marketing on these platforms – but our belief is that that will come. I think we have another year, really, where Affinity is still relatively fluid, but I think the longer-term trends are becoming a bit more visible for us.

Lloyd Pitchford

On the overall rates, you saw, in the first quarter, we were down 10%, and we have been improving on that by 3-4% each quarter. As we said, Q2 is more likely to be stable, at around a 10% decline. I would say we would resume a similar sort of trajectory from Q3 onwards and into FY17. It will, then, be in FY17 before we get to positive-growth territory across the segment overall.

Paul Sullivan, Barclays

First, is the decline in Marketing Services not a bit of a wakeup call that it requires more radical action, or are we still in a sit-it-out mode there?

Second, with great growth coming through in Credit Services in both Latin America and the US, they are very high-margin activities. Does that not point to some upward pressure on the underlying margin? Is your confidence in terms of stable underlying greater than perhaps what it was three or four months ago?

Brian Cassin

I will let Lloyd comment on the margin point, and I will take Marketing Services. Paul, we are not sitting it out in Marketing Services; we are taking a huge amount of operational activities in that business. What you are seeing here is a business which is yet to see the benefit of that. We talked in January, and then at the year-end results, about some of the shape of that portfolio. There are a lot of peripheral activities in there and, as I said in my script, you are going to see some action on that coming up relatively soon.

If you look at the business across the UK and EMEA/Asia Pacific, we are back into growth. We are down, really, to a couple of issues in North America, and the encouraging thing around that is that our Cross-Channel Marketing Platform (CCMP) is

growing very rapidly. It is from a small base but, quarter on quarter, that business is growing at over 100% now, and that has been the case for several quarters.

What we are really seeing, then, is attrition on our email base. Again, some of that was due to past operational issues, which we spent a lot of time fixing and we have stability in the platform. We expect, then, to see improvement in this business, as we said in January and again in May. That is our focus and our expectation going forward.

Lloyd Pitchford

On the margin, we said earlier in the year that our priority this year was getting the business back into our mid-single-digit organic-growth rates, and that continues to be the case. We are investing a lot in preparing the Consumer Services business, for example, for that technology launch. There is no change to our margin guidance. Flat at constant exchange rates this year is still good, and we are clearly investing in the growth trajectory of the business.

Joel Spungin, Merrill Lynch

First, you talked with regard to a possible reorganisation of the portfolio. In terms of organic capital allocation, however, which is something that you discussed earlier in the year, could you talk about what changes you have made internally to the way you think about capital allocation for the ongoing businesses.

Second, with regard to your comments on US Consumer Services, you said you saw opportunities in both paid and free. Do you see the free channel as just being a way of siphoning people towards the paid channel, or are you talking about creating a product there that would stand alone?

Brian Cassin

I will deal with the question on Consumer Services and then hand over to Lloyd on the organic capital allocation point. As I said in the script, we see products at both ends of the marketplace. The response that we have had to literally making a product free in the marketplace has been very encouraging. That is a pretty large number of consumers to come on without any real acquisition effort. We will look to monetise that in a variety of different ways. One of the things that we are seeing almost immediately is that the up-sell from free into the paid-for product is quite strong. It is already proving to be quite an effective acquisition channel for the Experian.com memberships. We are not yet monetising it in any other way. I said in my comments that it is still early days. This is a pilot phase, so you would expect us to develop our thoughts and plans on that over the coming months. We will have a bit more to say about that when we stand up in front of you in November.

Lloyd Pitchford

On capital allocation, I would just reiterate the things we talked about in January. There are two real changes to organic capex. First, a better and more systemic accounting of risk whereby we look across our matrix and our discount rates differ, depending on the market, the type of activity and the stage of development of the business that we are investing in, and differential hurdle rates.

On our budgeting and budget-allocation process, rather than allocating a single capital item down into our individual businesses globally, we have broken our budget up into

three elements: we spend capital on data, on infrastructure and on products. Those budgets are held centrally, and allocated and optimised globally in those three streams now, rather than a single capital budget. That is new for the company and we are making progress with that, but the goal is to better optimise our spend to our highest-priority opportunities during the year.

Rajesh Kumar, HSBC

I have one question on the consumer division in the US. When you transitioned the customers from the free brand to Experian.com, what level of churn did you see? Are you seeing a profile change from the subprime to the prime segment as you transition to the new brand?

Brian Cassin

We did not really see very much churn at all. The transitions went incredibly smoothly. When we talked to you in May, we had some issues like duplication. We discovered that we had some consumers who liked our products so much they were paying us twice for it, which is not sustainable. That had a bit of an impact but nothing major. We are very pleased with the way that went. It was a pretty major logistical and operational exercise, and to get through it without any real impact is pretty amazing, so we are very pleased with that.

The profile has not really changed because there is an amalgamation of members on the different platforms. Across our portfolio, we probably have a bit more of a bias to prime than subprime, but I do not think we have seen any major shift in that just yet.

Matthew Walker, Nomura

Could you remind us of your thoughts about the consumer product in the UK? Have you seen much in the way of free services coming in, in a Credit Karma fashion, in the UK? Why is the UK different or why is the business more protected in the UK versus the US?

Brian Cassin

We already have a free service in the UK. It is called Noddle and it has been around for a long time. From time to time, you see additional people popping up, so that is not something that we disregard and we are constantly on the lookout for that. Our own strategy in the business is going to take us down a similar path that we have in the US, which is that you will see us providing products and services across the whole spectrum. We will be prepared, and the trends that we have seen in the business over the last few years, even though we have had quite a lot of members on the Noddle platform, have not stopped our ability to grow our business. We think that there is opportunity, notwithstanding developments in the marketplace.

Tom Sykes, Deutsche Bank

Could you elaborate qualitatively on where you are getting the positive leverage to offset some of the investments that you are putting in to stem the declines in Consumer Services and where you are scaling up some businesses to get growth?

Just to be clear, your margin guidance is pre disposals. Would you be tempted to change your margin guidance at all post any disposals that you think are going to happen in the near term?

Lloyd Pitchford

I will start with the margin guidance. Clearly, you will have to wait for those disposal announcements but, as Brian mentioned, they are very much ancillary to the portfolio, so I would not expect anything material to come out of those.

On the leverage, our core Credit Services business is growing well, as referenced earlier, and we get operational leverage there. As we called out in some of the previous presentations, there are a lot of moving parts. We have increased regulatory and legal costs, which we have been absorbing into that mix as well. Some of the more recent changes to our investment and capital-allocation approaches are helping us allocate more of our capital and investment through the P&L to some of our priority areas. If you wrap all of that up together, it comes back to our priority this year being to get back to that mid-single-digit organic growth. If we can do that with a flat constant currency margin, that is our goal.

Tom Sykes

On the Consumer Services business, what is happening to pricing on the paid part? In terms of Credit Services North America, while you do not split out the Passport business in the text, could you perhaps give us a view on the extent of growth within the collective previous core business – consumer and autos etc together?

Lloyd Pitchford

Auto and healthcare are growing strongly double-digit, and while the Passport element is becoming increasingly more integrated, those growth rates continue at around 20%.

On consumer pricing, we made some changes earlier in the year on the launch of the new product but that only applies to new members, not the older members. Pricing, then, had a very small effect on the 20% revenue growth for Experian.com.

Brett Huff, Stephens Inc

First, can you tell us what is going to change and what we should think about for margin expansion in fiscal '17 from fiscal '16? I know that some of the investments in the direct-to-consumer business will likely taper, but could you be more specific on what kind of margin expansion we should think about and what the specific moving parts that will get us there?

Second, could you update us on your buyback status, what we did this past quarter and what we are looking for in the rest of the year?

Lloyd Pitchford

On the buyback, we are a little over half complete on the 600 million programme. We said that that programme would last through to the end of the fiscal year in March next year, and we will carry on with that programme in the quarter ahead.

In terms of margin guidance, we said earlier this year that we were changing our approach and that we would give guidance just for the year ahead. Overall, we will see our margin as an output of the investment decisions that we are making, rather than as a constraint. We are very focused on some of the great investment

opportunities that we have. We will update on FY17 margin guidance when we get to May next year.

Suhasini Varanasi, Goldman Sachs

On North America Consumer Services, the Experian.com brand has improved its growth over the last few quarters. What is the revenue mix looking like right now between legacy Experian.com and Affinity?

Second, on Credit Services in North America, you mentioned that the deal size has doubled. Could you give any more detail on this? Do you have any plans to expand this in other geographies?

Lloyd Pitchford

On Consumer Services, just to be clear, the 20% expansion in Experian.com does not include our Affinity customers. Again, just to be clear, while we have transitioned customers from the free sites onto the Experian platform, that 20% number is a clean number and is pure growth in Experian.

We said in Q4 that Affinity, data breach and other, which is the bundle outside of our direct-to-consumer, was declining at mid teens, and that decline rate continued into the first quarter on some of that weakness in Affinity, but particularly a strong comparative in data breach that we had from the prior year.

On Credit Services, I think you are referencing the expansion in some of the products and the average contract size in health. Our health business is a North America business just now, and we have great opportunities with some very particular situations in the North America healthcare industry to really expand that. Right now, then, we have no plans to take that internationally. We are very focused on that North American business for now.

Suhasini Varanasi

Following up on the Affinity business within Consumer, is it still 50% of the business there? You mentioned the declines. When do you expect these declines to moderate? Is it the second half of this year? What do you think will be the trigger for increased spend from the Affinity channel?

Lloyd Pitchford

Affinity, data breach and other, taken as a bundle, is a bit less than 50% of the Consumer business, so you have to then look into it. On data breach, as I said, the declines will moderate and will improve as we go through the year. That is principally a prior-year effect. On Affinity, it is really down to the marketing campaigns of our customers. We have seen new contracts signed and renewals signed in that space. We are seeing new marketing activity. In a similar way to the Experian.com launch, however, it will take time for that to gather pace. We are expecting that to continue to be in decline through this year before returning to a more stable position in FY17.

David Phillips, Redburn

I would like to ask about the acquisition pipeline and how you are seeing inorganic opportunities over the next 12 months or so.

Brian Cassin

I do not think we have a particular comment on that. We always have a number of opportunities across the spectrum, but there is nothing specific to call out at this stage.

David Phillips

With the enhancements to Experian.com that you mentioned for Q3, do you think marketing spend on Experian.com will be steady through the year or will you phase it through the year to target extra spending around the launch of the new front end?

Lloyd Pitchford

We have already had a good spend in marketing this year, with some getting behind the launch of the new product set that we have. You have seen the advertising campaign that we launched as part of the 'Swagger' campaign in the last few weeks in North America. The key thing about the new technology platform is that it helps us spend our marketing dollars better, because it will be a much more flexible platform that can target products based on the method and the route by which customers come to the site. That will allow us to much more accurately measure the effectiveness and response to marketing spend. We are, then, not envisaging a big expansion of marketing spend on the back of this launch; it will be much more about using it in a more focused way.

George Gregory, Exane BNP Paribas

First, in terms of Decision Analytics, there was a strong performance in the UK and in EMEA. To what extent could we or should we extrapolate those performances into future quarters? I know that the big piece of the Decision Analytics business in the UK is scoring, whereas the EMEA is perhaps slightly lumpier.

Brian Cassin

I guess the first point I would make about Decision Analytics is that it is very hard to look at one quarter's performance in Decision Analytics, and I think you should really look at it from a global perspective. For example, in the UK in the first quarter, we had a pretty exceptional performance. We do not expect that level of growth to be repeated there. In the US, we were softer, and we do not expect that performance to repeat there. You have to really look at it in the round.

Standing back from it and looking at the year-ahead view, we feel very good about where Decision Analytics is globally. That is both from the point of view of scoring triggers, the fraud and ID space, the software implementations and the traction we are getting with new products. The business is in good shape and I think we expect to be able to continue to grow well.

I will hand over to Lloyd to deal with the quarterly outlook.

Lloyd Pitchford

Pretty much as Brian said, if you look across the group it is lumpy. I think it will continue to be lumpy, but probably in different regions. We see a good outlook for North America into Q2 and Q3. We would call out that Q1 in the UK was probably a bit exceptional, particularly around some of the fraud and ID work that we are doing

there. It will be a little bumpy but, overall, we are pretty pleased with progress and prospects in Decision Analytics globally.

George Gregory

Second, in terms of the US Marketing business, you have flagged the declines in the email marketing business. Looking forward and modelling out the attrition in email marketing against the growth in cross-channel, how long do you think it could take for the two to cross over to the extent that that business might return to growth?

Lloyd Pitchford

Clearly, the scale of the business is still weighted towards the email platform. That said, we are seeing some really great growth and wins in our cross-channel business, so I think it is about gathering that scale and momentum on the new product. Realistically, however, that will take the rest of this year to do.

Hector Forsythe, Stifel

I have a question on the Consumer Services side. There is lots of talk about the change in the technology platform, and you have the FICO scores coming through on Experian.com. How does that change the offer and the take-up that is flowing through the Affinity channel?

Brian Cassin

It does not really change the Affinity channel. The Affinity channels are usually bespoke platforms for each contract that we do. There is a certain similarity across all of the different platforms, but they are highly customised for each customer. We are looking at all the product enhancements that we have in the pipeline and looking to add them to the Affinity channel where appropriate. The product-development effort that is going on across the business is going to have relevance in the Affinity channel as opposed to the technology platform itself. As a reminder on the technology platform, we have come from a place where we had a lot of different brands, all of which were on separate platforms, so I think you can see some of the complexity that we had in that business. Consolidating to one new platform which gives us much more flexibility is really going to make a difference to how we operate the business on a day-to-day basis.

Hector Forsythe

Does that technology platform spread across the Affinity offering?

Brian Cassin

Elements of it will but, as I said, the Affinity channel tends to be customised to each customer. We have a very large customer with several million consumers on that base who will be configured to their requirements, so it will not be completely the same as the direct-to-consumer (D2C) one.

Hector Forsythe

Would you be offering the FICO scoring through the Affinity channel?

Brian Cassin

That is an option and it really depends on case-by-case agreement with the customers.

Ed Steele, Citigroup

Decision Analytics is growing well. It has had a very disappointing margin performance over the last few years. Even though the amortisation charge is still probably picking up a bit, given all the investments you made in the last few years, do you feel that this sort of momentum, at 9% organic growth, is enough to turn the corner margin-wise and give us an up-year this year?

Brian Cassin

Let me give some context on that. The real change in margin in Decision Analytics came in the period from 2010 to about 2013/14. What you saw there was a significant mix change as well as some competitive pressure in the marketplace. In the last couple of years, that has been more due to some of the investments that we are making, and particularly 41st Parameter, which is in there and in which we said we have invested more. It is, then, more about what we are doing structurally to the business which is driving that change year on year. The business today is performing well from a revenue perspective, and we are making good EBIT translation from that revenue across the board.

Lloyd Pitchford

That is right. We are not giving any individual guidance on it. Also, whilst we break it out, we think very much of our Credit Services and Decision Analytics businesses together. The package of those two businesses to our financial services clients is really where we can add value across multiple streams. In some contracts, it is delivered in Credit Services; in others, it is delivered in Decision Analytics. We look, however, at total contract and total customer value. There is no individual guidance, then, but we are feeling good about the progress.

Concluding Remarks

Brian Cassin

Thanks, everybody, for joining us this morning and we look forward to speaking to you again in November with our half-year results.