

Case Study: Mastercard (MA) — Quality at a Reasonable Price, Ten Years On

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Buy world-class businesses, don't overpay, and let compounding work its magic.

I run a concentrated, quality-focused equity strategy: roughly 120 businesses I know well, evaluated against the same checklist every time, held with a multi-year horizon. What follows is one real example of that process — Mastercard (MA), which I wrote up publicly on Seeking Alpha on 15 September 2016 as part of a series titled *Building a Buffett-Inspired Portfolio of the World's Best Businesses*. It sets out the checklist as I applied it then, and what the business and the stock did over the following ten years, to 15 September 2026.

What happened

The call itself. The write-up went out with the stock at \$99.39, the 13 September 2016 close quoted in the article. On 15 September 2026 Mastercard closed at \$573.27. Put simply, \$1 million invested at the price of the call would have grown to about \$5.8 million — about 19.1% a year for ten years — and to about \$6.1 million with dividends reinvested (19.8% a year). The same \$1 million in the S&P 500, with dividends reinvested, would have become about \$4.2 million (15.3% a year).

The business did the work. Over the same ten years (June 2016 to June 2026) revenue grew from \$10.2bn to \$35.1bn, net income from \$3.8bn to \$16.3bn, and free cash flow from \$4.0bn to \$16.0bn. With the share count down a fifth, free cash flow per share grew about fivefold — a compound annual growth rate of about 17.4%. The stock rose because the cash flow did.

The price question

Nobody in 2016 disputed that Mastercard was a great business. The dispute was the price. At \$99.39 the stock traded at 29x trailing and 24x forward earnings and 26x enterprise value to free cash flow, against 20x and 17x for the S&P 500. Readers said so within an hour of publication: *"This is a great business but its very expensive. Its FCF yield is only 3%... I would recommend you wait for a better price"*, and *"MA stock is currently too expensive."* My answer, posted in the thread that afternoon, was the argument the piece was built on: in his 1983 letter Buffett says a business earning 25% on net tangible assets is worth 20x earnings or more, and Mastercard was earning 114%. A generic multiple was being applied to a business whose capital needs were close to zero, so almost every extra dollar of revenue arrived as cash. I called it *quality at a reasonable price*: expensive on the usual screens, reasonable for what the business would earn.

The arithmetic was tested in public too. A reader challenged the 174% return on invested capital, citing 44% from Bloomberg. I replied the same afternoon with the whole calculation — \$3,900m of after-tax operating profit over \$2,243m of average invested capital, after netting Mastercard's cash — and the source of every input, so anyone could check it.

Ten years on, the price question has a clean answer. At the call the stock stood at about 27.5 times trailing free cash flow per share; on 15 September 2026 it stood at about 31.9 times. The multiple rose only modestly, by about a sixth, so almost all of the return came from the business, with a little from the

multiple and the dividends. That is exactly what a fair price for a predictable compounder is supposed to deliver.

What kind of business, and what kind of price

Free cash flow per share can compound in three ways: a business can grow the cash flow itself, through a durable competitive position and high returns on capital (the permanent compounder); it can shrink its share count by buying back its own stock at sensible prices (the cannibal); or it can buy cash flow, acquiring smaller businesses cheaply and without issuing shares (the serial acquirer). Mastercard is the first kind, and the 2016 article said so: what I was looking for were *"companies that some would describe as 'permanent compounders'. These are businesses that by virtue of their superior business model, brand excellence and capable management, possess a demonstrable and durable competitive position allowing them to compound earnings and cash flow per share at an extraordinary rate today and far into the future."*

The article was just as clear about what that demands of the investor — the strategy *"necessitates a predisposition on behalf of the investor to seek long term alpha as opposed to short term speculative returns"* — and about the catch: *"Perhaps the most important piece of the puzzle is of course the price. Companies that fulfill the above criteria are a rare breed and are unsurprisingly seldom priced cheap — unless of course we are lucky enough to find them as a result of Mr. Market's occasional, momentary lapse of reason."*

That gives two kinds of opportunity. In one, a great business suffers a temporary setback and the market prices it as if the damage were permanent, so it trades at a substantial discount to fair value. In the other, nothing is wrong and nothing is cheap: the business is fairly priced, and the return comes from the compounding in the numbers. Mastercard in 2016 was the fair-price case. This is not a story about a mispricing. It is a test of whether paying a fair price for predictable compounding works over ten years.

Linearity: why it matters

The principle behind everything that follows. A world-class business shows linearity: its revenue, earnings and free cash flow per share rise steadily, not in fits and starts. That steadiness makes it predictable. Predictable and sustained growth over many years gives its free cash flow quality — cash that can be counted on, not cash that happened to arrive. The market recognises that quality and pays a higher multiple for it, which is why such businesses are seldom priced cheap. So a world-class business becomes a world-class investment only through the price paid for it. Bought at fair value, the compounding does the work. Bought during a temporary setback — when the market prices a passing problem as if it were permanent — the investor gets the compounding and the multiple re-rating as well. Mastercard in 2016 was the fair-price case.

The heart of a permanent compounder is not only how fast it grows, but also how steadily. A company that doubles its free cash flow per share in a straight line over ten years is a different proposition from one that goes nowhere for nine years and then doubles in the tenth, even though the end points are the same. The steady one is the one you can underwrite. I measure that steadiness as the correlation of the series with time, using half-yearly figures: a perfectly straight line rising scores 1, and around 0.9 and above is what I look for. This is the basis of how I work.

On trailing-twelve-month figures at every half-year from December 2005 to December 2015 — the record available when the article was written — Mastercard scored 0.99 on revenue, 0.96 on net income, 0.95 on free cash flow and 0.95 on free cash flow per share. That is despite two genuine interruptions: large litigation settlements with American Express and Discover in 2008, which pushed that year to a loss, and a large one-off charge in 2006. The steadiness was the reason to pay up.

The question the next ten years answer is whether it continued. From June 2016 to June 2026, on the same basis, the scores were 0.97 on revenue, 0.98 on net income, 0.96 on free cash flow and 0.96 on free cash flow per share — almost identical, through a pandemic that briefly cut cross-border travel and revenue in 2020. Free cash flow per share went from \$3.61 to \$17.99, about five times (a compound annual growth rate of about 17.4%).

The checklist, applied

The criteria are the same for every business: easy to understand and not exposed to obsolescence; a durable moat that shows up as pricing power; leadership in its industry; margins above the average business and stable or rising; a long record of high returns on capital; sustained operating leverage; durable economic goodwill — low capital needs; copious free cash flow; a strong balance sheet; management that allocates capital in shareholders' interest; a strong likelihood of continued growth; and a price that does not require heroic assumptions. The 2016 article took them one at a time, using the company's filings. Here is each, as it stood then and as it turned out.

A high-quality, easy-to-understand business with a leadership position. Mastercard makes transactions happen without taking credit risk: it does not issue cards, it charges issuers and merchants for running payments across its network. In 2016 it was, in the article's words, the second largest transactions and payments processing company in the world, behind Visa. Revenue was \$9.7bn in 2015 and \$32.8bn in 2025, about 13% a year compounded.

Likely to be around in ten or fifteen years; little obsolescence risk. The 2016 case was the global shift from cash to electronic payments, accelerated by online shopping. Ten years later the business is 3.4 times the size.

A sizeable moat. The article listed the attempts to go around the networks — the MCX retailer consortium, which had all but shut down its wallet by 2016, and Apple Pay, Android Pay, Samsung Pay and PayPal, which chose to partner with the networks rather than compete. The margins below are the evidence that the moat held.

Margins well above the average business, stable or rising. Between 2005 and 2015 operating margin rose from 13% to 52.5% and net margin from 9.1% to 39.4%. In 2025 operating margin was 57.6% and net margin 45.6%.

A long record of high returns on capital. Return on equity rose from 25% in 2005 to 60% in 2015, 64% in the twelve months to June 2016, with net cash rather than borrowing on the balance sheet. Return on net tangible assets went from 38% to 114%. (Return on equity has since become a less useful measure: ten years of buybacks have shrunk the equity base to \$7.7bn at the end of 2025, against \$15.0bn of net income.)

Sustained operating leverage. Operating leverage is how revenue growth turns into faster profit growth. Between 2005 and 2015 revenue rose 229% while operating income rose almost twelvefold (1,192%) — operating leverage of 5.2 times — and earnings per share grew seven times faster than

revenue (1.9 times faster over 2010–2015). From 2015 to 2025 revenue rose 239% and operating income 272%, from \$5.1bn to \$18.9bn, and earnings per share grew about 1.6 times faster than revenue. The leverage slowed, as it must once the operating margin is already above 50%, but it did not go into reverse.

Durable economic goodwill. This is the test Buffett set out in the appendix to his 1983 letter, and the cornerstone of my screening: a high return on net tangible assets that does not need heavy capital spending to sustain it. In total over the ten years 2006–2015, Mastercard spent \$2.1bn on capital expenditure while generating \$20bn of free cash flow — about \$10 of free cash flow for every \$1 of capital spending. In total over the ten years 2016–2025 it spent \$8.2bn while generating \$89bn — about \$11 for every \$1.

Capital spending took 2.8% of revenue in 2005, 3.5% in 2015 and 3.7% in 2025; over the same years free cash flow went from 6.5% of revenue to 38.3%, and then to 50.1%. For twenty years the business has needed the same few cents of each revenue dollar to keep growing, and has turned an ever larger share of the rest into free cash.

Copious free cash flow. Free cash flow was 38.3% of revenue in 2015 and 50.1% in 2025: half of every dollar of revenue now arrives as free cash.

A strong balance sheet. In 2016 the company had about \$3.3bn of debt against \$6.5bn of cash and short-term securities — net cash. It has since borrowed to fund buybacks: at the end of 2025 long-term debt was about \$18bn against \$10.6bn of cash, net debt equal to about half of one year's free cash flow. Still comfortable, but no longer net cash.

Shareholder-friendly management with a record of good capital allocation. The article pointed to three things: a dividend that had grown at more than 66% a year, compounded, since 2011; buybacks averaging \$3.3bn a year over the previous three years; and more than \$6 of market value created for every dollar of profit retained between 2005 and 2015. On the same three measures since: the quarterly dividend rose from \$0.19 to \$0.87, 16.4% a year compounded; buybacks averaged about \$10.6bn a year over 2023–2025; and market value rose by about \$402bn over 2016–2025 against \$69bn of profit retained, about \$5.80 for every dollar. Along the way the diluted share count fell by about a fifth, from 1,107m to 888m.

A strong likelihood of continued growth. The article named the cash-to-card shift, online payments, China and the PayPal partnership. Revenue has since grown about 13% a year and free cash flow per share about 17% a year. China came, but slowly (below).

Two judgements in the piece, checked

On China, the article called Mastercard's application to enter the domestic card market potentially "*the biggest growth opportunity*"; the licence came, but slowly, with its joint venture approved in November 2023. On legal risk, I replied to a reader that the networks were "*battle hardened against such claims*"; the UK consumer claim, put at GBP 14bn in 2016, was settled for GBP 200m in 2025.

This is a specific, dated call, checkable against public filings and a public research platform, and argued with in real time by people who had no reason to be generous. It's the standard I hold every idea in the portfolio to — not just this one.