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Intercontinental Exchange, Inc. (ICE)

Q2 2015 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the ICE Second Quarter 2015 Earnings Conference Call. All participants will be in listen-only mode. [Operator Instructions] After today's presentation there will be an opportunity to ask questions. Please note this event is being recorded.

I would now like to turn the conference over to Kelly Loeffler. Ms. Loeffler, please go ahead.

Kelly Loeffler
Senior Vice President, Corporate Communications, Marketing & Investor Relations

Good morning. ICE's second quarter 2015 earnings release and presentation can be found in the Investors section of theice.com. These items will be archived and our call will be available for replay.

Today's call may contain forward-looking statements. These statements which we undertake no obligation to update represent our current judgment and are subject to risks, assumptions and uncertainties. For a description of the risks that could cause our results to differ materially from those described in forward-looking statements please refer to our 2014 Form 10-K.

In addition to GAAP results we also refer to certain non-GAAP measures including adjusted income, adjusted operating margin, adjusted expenses, adjusted EPS, adjusted EBITDA and adjusted tax rate. We believe our non-GAAP measures are more reflective of our cash operations and core business performance. You'll find a reconciliation to the equivalent GAAP term in the earnings materials and an explanation of why we deem this information to be meaningful as well as how management uses these measures. When used on this call net revenue refers to revenue net of transaction-based expenses, adjusted net income refers to adjusted net income from continuing operations and adjusted earnings refer to adjusted diluted continuing operations earnings per share.

With us on the call are Jeff Sprecher, Chairman and CEO; Scott Hill, Chief Financial Officer; and Charles Vice, President and Chief Operating Officer.

I'll now turn the call over to Scott.

Scott A. Hill
Chief Financial Officer

Thank you, Kelly. Good morning, everyone, and thank you for joining us. I'll begin on slide four by highlighting our strong performance in the first half of 2015. We grew adjusted earnings 27% year-to-year on 6% revenue growth with commodities, cash equities, data services and listings all contributing top-line growth. Adjusted expenses declined 6% and adjusted margins expanded 6 points. The revenue growth and margin expansion generated operating cash flow of $770 million in the first-half, which enabled us to deploy around $300 million in capital expenditures and business investments like Amex and OCC while returning $560 million to investors.

Now please turn to slide five where we detail our second quarter financial results. Adjusted earnings per share rose 27% from the prior year to $2.90. Net revenues grew 6% year-over-year to $797 million. This includes record revenues for data services and for NYSE listings and strong growth in commodities revenues. Adjusted operating expenses declined 8% from the prior second quarter and adjusted operating margin reached 59%. Our adjusted tax rate of 28% was at the lower end of our range in the quarter due to a number of discrete items. For the second half of the year we expect our tax rate to be closer to the middle of the 28% to 31% range.

Let's move on to slide six and I'll discuss the drivers of our 6% revenue growth. Transaction revenue accounted for 56% of net revenue during the second quarter. Our net transaction and clearing revenues declined 3% year-to-year due primarily to continued interest rate volume weakness in Europe. Commodities revenue increased 8% year-to-year on strength in our oil, natural gas and ag markets and revenues also grew in our FX and cash equities markets. Non-transaction revenues grew 20% and represented 44% of net revenues. This included data services revenues, which were up 29% to a record $191 million driven by the addition of new users and product offerings. NYSE listings revenues grew 12% year-to-year to a record $101 million, reflecting the NYSE's continued global leadership in IPOs and capital raisings.

Next, on slide seven I'll detail the revenue performance across our futures exchanges for the second quarter. Despite muted activity and interest rates markets, revenues from futures and options declined just 2% from the prior second quarter. Energy and ag volume in revenue growth was solid, including global oil and sugar revenues which increased 11% and 20% respectively versus the prior year. Total open interest across all of our exchanges had increased 3% from the beginning of 2015 and notably volatility in European short-term interest rates picked up during the month of July with daily volume in our rates complex up 17% over the prior July, contributing to overall derivatives volumes which were up 1%.

Total volumes in July actually grew 7% when you exclude European single stock equities volumes. The revenue associated with that trading activity is capped and thus there is very little correlation between volumes and revenue. To ensure our volume metrics better align with transaction revenues, we will exclude single stock equities volumes from our volume and RPC metrics beginning in August and we will provide updated historical information on that same basis on our website.

Turning to slide eight, I'll expand on the performance of our energy markets. During the quarter, global oil revenue increased 11% including Brent and Other Oil revenues up 11% and 15% respectively. ICE Brent along with hundreds of related oil product remains the global benchmark relied upon by producers and consumers. Revenues also grew in gasoil and WTI as did volume and open interest. From the beginning of the year through the end of June, open interest in our global oil complex is up 8%. Our natural gas market also performed well in the second quarter, benefiting from increased volatility resulting in revenue and volume growth of 7% year-over-year.

Moving along to slide nine, I'll provide an update on revenues from our swaps markets. Total credit derivatives revenues for the quarter were $34 million including $22 million in CDS clearing revenues. The sequential decline in clearing revenues was primarily due to the $3 million accounting adjustment that we noted in our first quarter results. For the full year 2015 we expect clearing revenues to increase from the prior year and to exceed $100 million as we continue to add more products and see increased interest from buyside clients.

Growth in European buyside participation continued in the quarter and accounted for 34% of the gross notional cleared in the first half at ICE Clear Credit, our U.S. swaps clearing house. CDS clearing activity in the U.S. remains robust due to our comprehensive product offering, portfolio margining and the relative regulatory certainty in the U.S.

Please turn to slide 10. The New York Stock Exchange continues to grow revenue and gain share reaching 24.4% share of the U.S. cash equities market in the second quarter, up from 22.7% in the prior second quarter. We have improved revenue capture and grown revenue consistently since completing the acquisition in 2013 by focusing on the needs of our customers and simplifying markets. Share in our equity options markets was stable versus the first quarter. And after purchasing the remaining 16% stake in the Amex business at the end of June, we saw a share increase in July. Importantly, we will retain 100% of the profit from the Amex options business starting in the third quarter. So, in our equity options business, share is stable to improving, and the profit contribution from the business is increasing. We continue to focus on the evolution of our options market as we shift from a neutralized structure to one that is focused on innovating across the NYSE, Amex and Arca options markets.

We've historically focused on aggregate expense management and revenue performance by business line. That notwithstanding, I want to eliminate any misperception about the significant profit contribution we are realizing from the New York Stock Exchange. The combination of improved share and stable revenue capture in cash equities continued listings leadership, diverse data offerings, the elimination of corporate redundancy and significant operational improvement increased NYSE's adjusted operating margin above 50% in the second quarter of 2015. That's a nearly twofold increase versus 2012. And as we continue to serve our customers, implement technology improvement and streamline NYSE's operations, we expect the profit contribution from the NYSE business to continue to increase as margins expand.

Moving on to slide 11. As I just mentioned, we continued to extend our global leadership in listings in the second quarter and the first half of 2015. Listings revenue grew 12% over the prior second quarter to $101 million. We also led in global proceeds, raising $95 billion in 264 transactions during the first half of the year. We have a robust IPO pipeline for the second-half and we are investing in our team and resources to support our listed companies.

Slide 12 reflects the continued strength of our data services business. For the quarter, data services revenues were a record $191 million, up 29% over the prior second quarter. This was primarily driven by the addition of new data products and growth in our customer base coupled with the addition of SuperDerivatives and the emergence of ICE Benchmark Administration.

Turning to slide 13, I'll move from a focus on revenues to a discussion of our second quarter expenses. As you can see, adjusted expenses declined 8% year-over-year to $328 million. Expenses were better than guidance, primarily due to accelerated synergies coupled with reduced non-cash compensation expenses related to a large number of resource reductions during the quarter and a large recovery in technology expenses. Compensation, professional services and SG&A expenses continued to decline as we integrate our businesses, eliminate overlapping roles and reduce contractor levels.

Technology and D&A expenses increased from the prior second quarter due to investment to improve our NYSE technology platform, to enhance our listed customer offerings and to enable our ongoing integration and the consolidation of our global real estate footprint. This continued focus on strong expense management enabled adjusted operating margins to expand to 59% in the second quarter, a 6-point improvement versus the prior year. We expect expenses in the third and fourth quarters to be in the range of $330 million to $335 million, which means our full-year expense should be at or slightly below the low-end of our prior guidance and approximately 4% lower than in 2014.

If you move to slide 14, I'll quickly cover our cash flow and capital structure. In the first half of 2015 we generated $770 million in operating cash flow. At June 30 we had $700 million in unrestricted cash and short-term investment including just under $200 million in additional regulatory capital that will be required when ICE Clear Europe receives EMIR authorization. On June 30 we paid off our $1 billion 2015 Euronotes. Our total debt now stands at $3.3 billion and our adjusted debt to EBITDA is 1.6 times.

I'll conclude my remarks on slide 15 with an update on our uses of capital. As you can see we have used all of our operating cash for capital return, opportunistic M&A and capital expenditures. In the second quarter we returned nearly $290 million to our shareholders. We repurchased $203 million of shares during the second quarter and continued to opportunistically buy back our shares. We also paid $85 million in dividends, representing a 15% increase in demonstrating our commitment to grow dividends as we grow. We expect to maintain around $500 million in unrestricted cash and equivalents and a leverage ratio around 1.5 times. We otherwise expect to use 100% of cash flow to return capital to shareholders and to deploy towards growth investments that meet or exceed our return expectations. Importantly, our strong balance sheet and cash generation coupled with our access to debt market should enable us to return significant amount of capital without limiting in any material way our ability to act opportunistically when we identified growth opportunities.

Our strong first-half performance reflects the execution of our financial and strategic objectives. Revenues grew 6% and adjusted earnings grew 27% even as we integrated multiple acquisitions, invested in growth initiatives and returned $560 million to shareholders. And importantly, we have established solid momentum that will carry through the remainder of this year and into 2016. I'll be happy to answer any questions during Q&A. And I'll now hand the call over to Jeff.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

Thank you, Scott, and good morning. Our 27% earnings growth in the quarter was driven by strength across our company. And our record first-half revenue and record first-half earnings are consistent with our objective of delivering strong top-line and bottom-line growth. We delivered growth in our energy, agriculture and equities markets, as well as in market data and in listings; we're integrating our acquired companies, and advancing numerous technology and strategic initiatives to address our customers' needs.

Our team is adept at managing change, consistently evolving and growing our business since its inception. We've moved from an electronic trade execution venue for over-the-counter markets to becoming a global network of exchanges and more recently pursuing clearings, data services and expanding our listings franchise. And we're striking a balance between high value, recurring revenues and more commoditized volumetric revenues.

Our progress in quickly reshaping historically low margin businesses to increase margins through improvements is evident in the NYSE and Liffe operations. Significant cost efficiencies remain in our sights; and as our revenues continue to rise, this should amplify our earnings growth in the coming years.

We've also positioned ICE alongside long-term secular trends coupled with improving cyclical dynamics. And I'll walk through some f these starting on slide 16. Demand continues to rise for our products and services due to the globalization of markets and the increasing need for risk management. The significance of data services and clearing is rising with the additional collateral, treasury, benchmark and v aluation services that we are developing. As such, much of the value we add today cannot be measured through trading volume. This is evident in the chart on slide 16 where trading volume trends have become a less reliable indicator of our earnings growth.

Over the last four quarters, while trading volumes have declined on a year-over-year basis, our earnings per share has consistently grown at a strong double-digit rate. Our continued top-line revenue growth including revenues up 6% in the first half of the year is driven by our anticipation of changing customer needs. At the same time we compete in our trading volume based businesses from a position of strength, owning globally relevant benchmark contracts integrated with risk management and data services.

We differentiated our approach by locating in the major market centers where our customers operate. As we reach for global growth, we plan to launch our Singapore-based exchange and clearing house in the fourth quarter and we built ICE Trade Vault data repositories in the U.S., Canada, Europe to serve unique reporting requirements. We believe that our geographic diversity is increasingly important as regulation and capital requirements continue to diverge across these jurisdictions.

In response to customer requirements for products that are more capital efficient we've launched our ERIS products which replicate the economics available in swaps within a futures contract, while we are also taking a leading role in meeting the demand for swaps clearing in the U.S. and Europe. And, as you saw during July our leading European interest rate franchise demonstrated that when volatility returned during the month trading volumes responded with a 17% increase year-to-year, driven by Euribor and Sterling. We are very well positioned across our global financial products franchise including our MSCI index volumes, which are up more than 30% and foreign exchange volumes up more than 100% year-to-date through July.

In our equities markets we're focused on innovating and growing the NYSE. We're introducing new technology, reducing market complexity and promoting liquidity by developing a mid-day auction. As the global leader in capital raising, we're focused on all aspects of our listings business. We continue to lead in IPOs across virtually all segments, including technology, REITs and ETFs. This is due to the clear advantages that we offer from our strong visibility, issuer advocacy and our unique market model which improves the ability of our listed companies to issue new equity or buy back their shares.

Turning to slide 17, I'll highlight how our diverse global markets continue to provide near-term and long-term growth. Recently we've seen growth in our European rates and U.S. natural gas trading volumes, demonstrating how quickly volatility can return to markets. Longer term, as Western economies continue to move towards natural gas, we're very well positioned with over 100 listed natural gas contracts, including key natural gas benchmarks across the U.S., Canada, the U.K. and Continental Europe.

In our global oil complex we continue to benefit from price volatility and the demand for energy price hedging that is coming out of Asia through ICE Futures Europe. With nearly two decades of record annual volumes in the ICE

Brent contract, there continue to be many drivers of its long-term volume growth. These include price volatility, changing supply and demand expectations, regulations, the adoption of Brent as a global oil benchmark, geopolitics and the shifts in hedging strategies.

Turning to what's next, I mentioned earlier that we have a number of technology initiatives that are underway. For example, immediately after closing on the NYSE transaction, we began investing to reduce the complexity of the exchange's five trading platforms into one modern system. We plan to begin broad industry testing of our new NYSE Pillar platform over the next couple of months.

I'll now turn to ICE Benchmark Administration and the important role that we're playing to rebuild confidence in the benchmark setting process. We've been working closely with the industry and regulators since beginning our work on LIBOR, and have deployed improved governance, transparency, systems and oversight that's required for this new era.

With over $350 trillion in gross notional value that is tied to LIBOR, ICE Benchmark Administration is applying significant resources to reform the rate setting process. And through a market consultation that was announced last week, we're reviewing each aspects of LIBOR's methodology and calculations including more transaction data included in the process. We've received very strong feedback from the 22 banks that are now submitting rates as part of our process. In addition, the new gold price auction has proceeded very well with record volume since its launch this year and with the number of direct participants expanding from 4 to 10 in the recent months.

In our data services business we're working on building out our Safety network which is an increasingly valuable piece of market infrastructure that we acquired with the NYSE. As secure connectivity becomes increasingly vital to market participants, we've seen strong interest in access to our network.

I'll conclude on slide 18 which is the same slide on which Scott opened his remarks in order to emphasize that we're delivering consistent growth by executing on our strategic plans. We're off to a great start in 2015 with record first-half revenues, record operating income and record earnings. We've transitioned from generating revenues that were approximately 90% transaction based related to one asset class to an approximate 60% transaction based revenue business that is now levered to multiple asset classes, multiple geographies and multiple growth drivers. This is why we're confident in our strategy.

We've uniquely delivered growth each year through all phases of the business cycle. Our margins are rising, earnings growth is consistently strong and we're delivering the best revenue and earnings performance in our history. And as we move into the back-half and the coming year, we've identified significant opportunities across revenues and expenses that are yet to be realized to ensure that our strong track record continues.

So, on behalf of the ICE team I want to thank our customers for trusting us with their business in this excellent quarter for us.

And I'll now ask Keith, our operator, to open up the call for the question-and-answer session.

QUESTION AND ANSWER SECTION

Operator: Yes. Thank you. [Operator Instructions] And the first question comes from Mike Carrier with Bank of America Merrill Lynch.

Michael R. Carrier
Bank of America Merrill Lynch

Q

Thanks, guys. Maybe just an update on some of the regulatory items that are going on in the industry and I guess, most importantly, [indiscernible] (21:17) EMIR points. You mentioned with Singapore launching you're going to have the clearing houses in the exchanges globally. [indiscernible] (21:28) update on your thoughts on where the potential concentration or where those [ph] end markets (21:33) will be going depending on how some of these regulations turn out?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Sure. Why don't I move – I'll move geographically across the globe. So starting with the U.S., we've been participating in a number of panels and hearings and conversations that have been going on with the CFTC regarding the potential implementation of position limits and how those should go into markets. Particularly, we're concerned about how the commodity markets operate. I think you're aware that the – we built our business around the commercial users of hedging tools and commodities.

And we are trying to make sure that those kinds of reliable and diligent people have access to markets so that they can use them to hedge and continue to manage risk in their businesses. I feel like that constituency is much more engaged now in this conversation and our regulators are listening and trying to find their way through that. So, honestly, we feel like there is a very good, healthy dialog going on in the United States. And we feel like, as a company, we've positioned ourselves with the right group of customers to continue to grow as we have been through all phases of increased regulation in the United States.

In Europe, you mentioned the equivalents conversation. We're deeply involved in the conversations on both sides of that. Publicly, the regulators have stated that they're moving closer to a deal. It looks like, to us, from basically everything we see that they are working in earnest that a deal is within sight. We think that they've done a very good job of gathering a lot of data, so that the policies that they implement will be data-driven, which has been important for us and we've participated in providing data and running analytics and scenarios so that people can be educated.

So we feel good about the direction of that and have no reason to believe that they won't come to a deal as they, both sides, have suggested they are moving towards. Based on our conversations, it looks like the areas that they're negotiating over would be helpful for the markets in that. It will continue to allow for strong risk management, but won't necessarily impede or significantly change the way people do business.

Moving to Asia, we are anxious to launch our Singapore exchange in clearing house. We've done all the work that we've needed to do, put the staff in place, the systems in place, and are basically ready to go, but we really benefit as a company from being a global network, a global distribution, and our goal is to bring a lot of non-traditional global players to Singapore to do business.

And so, it's taken our customers longer to get set up than we anticipated. We don't want to launch the exchange until major customers can have access. We think the best – it was in our best interest to slow down and give our customers a chance to catch up to us, and so we're now planning that in the fourth quarter of this year we think there'll be significant mindshare there around the exchange that will allow us to have a successful launch.

That's kind of the lay of the land, it's all work in progress but broadly speaking a lot of really good healthy dialog going on across the world as regulators are struggling to implement a lot of new rule changes but do it in a way that's consistent globally and also that doesn't impede people that are trying to use the markets in healthy ways.

Michael R. Carrier
Bank of America Merrill Lynch
Q

Okay. That's helpful. And then, Scott, you gave an update on the second half on expenses. They continue to be well managed, but just wanted to get an update on 2016 and 2017 just on the synergy timeline, if anything's changed or more or less in line with what you've said in the past.

Scott A. Hill
Chief Financial Officer
A

No. I think, Mike, we continue to make very good progress on the projects that made us that $550 million of synergies. As I mentioned the performance in the quarter really reflects an acceleration of those synergies and the efforts around it. So I feel good about the projects we've identified, I feel good about the progress that we're making, and we continue to be very focused not just on the synergies but on expense management generally.

Michael R. Carrier
Bank of America Merrill Lynch
Q

Okay. Thanks a lot.

Operator: Thank you. And the next question comes from Ken Hill with Barclays.

Kenneth W. Hill
Barclays Capital, Inc.
Q

Hey. Good morning, guys.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer
A

Good morning.

Scott A. Hill
Chief Financial Officer
A

Good morning.

Kenneth W. Hill
Barclays Capital, Inc.
Q

Just wanted to kind of follow up there last on the Singapore exchange. I know the timeline's been a little bit more drawn up than you guys initially expected, but you've mentioned the fourth quarter launch you have customers get on board. I was hoping you could remind us as to what your initial goals are as we turn into 2016 what we should be looking for there with the Singapore exchange.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Really, as managers, our hope is that we have a successful launch. We have a handful of products that we have talked to a lot of customers about in Asia that they want to trade, and we want to have a successful launch of the exchange, get people used to using the exchange in clearing house, get the connectivity around it and so – and be able then to plug that into our global distribution network. And the goal is to just have this nice, successful launch because we have the intention of launching a lot of new products and there's a lot of demand coming from our Asian customers for new products in the region.

So what you see us doing is trying to find a couple of products that we think will have appeal, that the appeal will be broad enough that it will bring global distribution to Asia. But, the real intent there is not that any one of those things is necessarily a homerun, we want to have a solid start to the business because we do intend to continue to invest in there and there really does seem to be strong demand for trading in the region.

Kenneth W. Hill
Barclays Capital, Inc.

Q

Okay. And just a follow-up on CDS business, I know you guys on the slide deck have the target there for clearing revenues of above $100 million. Versus where we were in 2Q I know you had some one-off adjustments. Can you give us some color on what you're hearing from clients that gives you a little bit more confidence in that greater than $100 million number?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Yeah. That's a really good question, Ken. And really our willingness to commit that we'll be over $100 million for the year is based on customer feedbacks. We're seeing a lot of positive momentum now with buyside customers in particular and single-names and importantly in advance of any mandate. I mean, we've got mandates from the CFTC on indexes, but we don't have mandates in single-name and that notwithstanding we're seeing growth in interest because I think there is a view that for the market to really succeed, clearing is an important element of that.

And so you've seen a couple buyside firms that have written about that, we have the most comprehensive offering of single-name products, the most comprehensive offering of sovereign names, have talked – talked about our intention during the second half to launch the U.K., France and Germany sovereign names. So I'm encouraged by the product launches that we have in front of us, the buy-side customer feedback that we're getting and just the nature of the business that we've built which I think provides not only a foundation for us to do well the rest of this year but to continue to grow out into 2016 and 2017.

Kenneth W. Hill
Barclays Capital, Inc.

Q

Great. Thanks. That's helpful color. Thanks for taking my question.

Operate: Thank you. And the next question comes from Rich Repetto with Sandler O'Neill.

Richard H. Repetto
Sandler O'Neill & Partners LP

Q

Yeah. Good morning, Jeff. Good morning, Scott.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Good morning.

Scott A. Hill
Chief Financial Officer

A

Good morning.

Richard H. Repetto
Sandler O'Neill & Partners LP

Q

Congrats on the strong quarter here. I guess my first question is on the market data and, Jeff, you spent a fair amount of time emphasizing on calls and this demand for more data by the customers and what you do – that it isn't just price increases, but it's content increases too. So I guess could you get into more color on what exactly you're providing the value here? And then, Scott, you said it was going to be – or I think the guidance was flat; it grew by $4 million. So, where can it go for the next couple of quarters?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Sure. So I think the trend that we see and that we saw and have moved towards is this demand for more and more data. We all know, all of us that follow this industry saw the emergence of algorithmic traders that were consuming a lot of data and then figuring out very quickly how to place trades, well that kind of an analytics is now making its way on to desktops and into buyside firms and people now are increasingly having the capability to handle a lot of data and to analyze it and to find trends or other opportunities or to use it for risk management and hedging activities in this dataset.

And one of the things that has the nice luxuries of the company that we've built is that we've now moved into multiple asset classes as you've seen, including over-the-counter products, listed commodities and listed derivatives and now equities and equity options, and we've done that globally. And so we have quite a package of data and are able to put things together in interesting ways to help serve the needs of our customers. And so, when we were a small company our data wasn't this rich and honestly we didn't have as deep of appreciation as how data was going to be consumed as we do today.

So what you've seen us do is put Lynn Martin now in charge of a new data operation to organize across all of our businesses to gather data, and it's paying dividends. Like Scott mentioned in his prepared remarks that revenues were up 20% in that area which is – or 20% across our fixed businesses and 29% in data, which is an interesting place for us to position the company, it's why Scott and I both mentioned in our prepared remarks.

We think we're just scratching the surface. We just are integrating these businesses, we just put Lynn as an executive to oversee the integration and so we have strong appetite, we think, to continue to grow these businesses.

Scott A. Hill
Chief Financial Officer

A

And I won $10, Rich, that you called me out on my guidance being a little off. The point I've made is the – it's an expansive business that Lynn is running. It's through traditional data services that ICE has had where we sold data in the back offices that allow them to mark their books. The Safety business at NYSE that Jeff talked about in his prepared remarks where people want to get connectivity into our exchange, it's direct connect into ICE's exchanges. And so there are a number of pieces that move around, the overall visibility is good not perfect.

My expectation is the data services revenues are going to grow strongly every single quarter. Sequentially, I still think a relatively accurate projection for the year is that 3Q and 4Q look like 2Q. Could it be a couple of million higher in those some of those quarters based on the more connections or greater data sales or continued customer growth or SuperDerivatives' performance? It could be. I think that's the conservative assumption. I think the more important point versus what do we think about the third quarter or the fourth quarter is what do we think long-term, and this is a growth business for us. And it's a significant growth opportunity for us as you move into 2016 and then out into 2017.

Richard H. Repetto
Sandler O'Neill & Partners LP
Q

Got it. I'll rebate you that $10, Scott. My follow-up question, Jeff, would be every quarter you position the company as a growth company and it has been. And I guess it has to do with the NYSE and you've talked a lot about the improvement in margins of 50% and the growth and now you're 100% of the Amex contribution; I'd love to understand what that is. But I guess the bigger question now is once the synergies are done and looking at the company, the key – if revenue was – wanted revenue to grow mid-single digits, can you still grow when you don't have the synergies?

And then looking at the NYSE, again, I would assume a lot of the growth is from cost savings and I know you've done well with market share but the point being, you may not be getting the value for that either. So again the question about growth after the synergies are done at the NYSE and the valuation there.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer
A

Well, you're right in that. We've taken a lot of costs out of the business and we've been able to do that because we're a larger organization that can lever off of other businesses. And there's more to go there. We still haven't put our technology in place, we're making large investments in the way we oversee our markets and compliance and other tools that we think will really make us a better compliance organization and more efficient. So there's still a lot to go there on the expense side, but we've really been growing revenues.

And this idea that we had in simplifying markets we now want to simplify technology, we are really – have a new team in place that's really pursuing a lot of listings and the top-line is growing. And we think the trends are in our favor. We're going to put a mid-day auction in, the SEC has worked with us on a tick pilot that's going to go into place that's going to test various market models around the listed business. And we see potential upside in all of that.

The other thing that happens, Rich, is that, what, the exhaust of the New York Stock Exchange is a pretty rich dataset. And that dataset is something, along with the Safety network that we inherited with that, is something that we've now been exploiting to add to it and enrich it with other data. And so, we think that we will be able to grow the top-line of that business when you look at it collectively for years to come.

Richard H. Repetto
Sandler O'Neill & Partners LP
Q

So, I guess the point is you think you can grow earnings post-synergies?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Oh yes. Absolutely. Absolutely. And we don't see right now any limitations. And the levers that we're pulling seem to be working and the trends, really. If all things being equal, we really believe markets – that buyers are looking for sellers and sellers are looking for buyers, and that markets don't want to be fragmented. The fragmentation comes when there's payment for order flow where intermediaries are incented to do something on their personal behalf, and less so on their customer behalf. Where algorithmic traders benefit from the fragmentation, where corporate traders may not have balance sheet attached to their – the use of the corporate balance sheet attached to their pay. And so they are looking for economic incentives and we'll actually trade slightly off-market in order to lower execution costs, if you will, that they get paid against.

And so you have a lot of disincentives in the markets that have caused a lot of fragmentation, and as there's more regulation, as there's more focus on the bottom-line as people are really having a really healthy debate about the fiduciary responsibility of exchanges and brokers and intermediaries, those trends are allowing what the natural market wants, which is for buyers to find sellers and for these things to come back to more organized listed venues. And we've seen that trend. I'd like to say that everything we're doing has caused it, but it's not, that is not the cause. There is a macro trend in place that we're moving the business into.

Richard H. Repetto
Sandler O'Neill & Partners LP

Q

Understood. Thanks. Very helpful, Jeff. Thank you.

Operator: Thank you. And the next question comes from Dan Fannon with Jeffries.

Daniel Thomas Fannon
Jefferies LLC

Q

Thanks. Good morning. I guess one more question on market data. You talked about the growth in new users, and I was wondering if there's any kind of stats or kind of color you can put around where they're coming from geographically or anything to be a little more helpful there.

Scott A. Hill
Chief Financial Officer

A

Yeah. I mean, not a lot that we put out publicly on that, but what I can tell you is similar to what I said in the first quarter. We saw a lot of growth in the energy space in particular, and more narrowly interest in oil markets, which is not surprising if you look at what's happening. There's a lot of growth in the world in oil, a lot of new sources of oil, a lot of discussion around the oil markets, and so that's an area where we've seen a significant growth in the number of customers.

And then the other thing I mentioned earlier is it's not just an interest in the data, but we're seeing more customers grow. I forget what the number was, but I think we were up something like 30% in terms of people who are buying access to our exchanges. And so, it's growth in data consumption in energy, it's growth in connectivity in energy, and then as Jeff alluded to, there's a lot of valuable information at the New York Stock Exchange as well and we continue to see more customers who are interested in consuming that data. So it's across the business.

Daniel Thomas Fannon
Jefferies LLC

Q

Great. And then just on M&A and your kind of outlook today, versus other periods how much time you guys are thinking you're spending on potential acquisitions and, kind of, how you would characterize, kind of, the environment today for potential activity?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer
A

Well, there's definitely a lot of opportunities available for M&A in the market. We see it – similarly there's a lot of private equity firms that are coming to be listed on the New York Stock Exchange, and some of those companies are not really ready for listing and those private equity firms have been looking to sell them privately. So we see activity on both sides.

Nothing has changed for us. We are driven by return on invested capital metrics and whether – where we can place our money, so that it has the highest return for shareholders as part of that graph that we have shown which is we like to buy businesses where we – not to own them but where we think we can transform them because of the unique nature of the network we've put together. And so they become high value, high return on invested capital businesses for us, so we'll always look at things like that, but we weigh them against the other opportunities we have in the way we can return capital to shareholders or reinvest in organic growth. And I would say nothing has changed other than it does seem like there's a lot of private equity-based companies around that are looking for new owners both in the public and private markets.

Scott A. Hill
Chief Financial Officer
A

And just extending that point, in the first slide in the appendix we do put out each quarter what our return on invested capital is. And as I said, I thought we'd be by the end of the year we're now back at 8% and it's above our cost of capital. So just to build on Jeff's point, we do focus on return on invested capital as we think about investments, as we think about synergies in the businesses we buy and the integration plans for those acquisitions. I think that's an important milestone. The ROIC for our company remains above that of our closer competitors, and more importantly it's back above cost of capital which means every day we come to work we're creating value for shareholders.

Daniel Thomas Fannon
Jefferies LLC
Q

Great. Thank you.

Operator: Thank you. And the next question comes from Alex Kramm with UBS.

Alex Kramm
UBS Securities LLC
Q

Hey. Good morning.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer
A

Good morning.

Alex Kramm
UBS Securities LLC
Q

Just wanted to ask quickly about the – I don't think you mentioned, the Russell-FTSE agreement that CME just struck, and maybe also give a little bit of history there. I remember when you've taken this over you were very excited, I think you paid a pretty big price for it to get that over and it never took off. So, maybe just what happened? why did it never become a big area for you? Why did you not get more competitive in keeping this contract? And what's the, kind of, like profitability or impact when that is going to CME in the future?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Sure. So let me answer the second part first which is the move away from us is immaterial to us. And the reason that that happened is really the first part of your question, which is what we found in marketing the Russell complex was that the natural hedging user which is our, always our target customer, is a large institutional buyside or smaller – medium institutional buyside that has a mid-cap or small-cap U.S. portfolio that wants to hedge that. What we found is very strong competition from our competitor who was marketing to that same asset base, the use of the S&P 500 as the hedging instruments. And the Russell indices and the S&P 500 have become very highly correlated, and so there was very robust competition.

The deal we struck had the cost of that marketing borne by us and over time we had been putting in more and more market making programs and other incentives to try to attract liquidity that was lowering our rate per contract and lowering the take that ICE got out of that deal. And so, it is now moving to that competitor, it's going into a vertical, it's going to be exclusive and basically the market's going to be carved up by the index providers and their distributor on those economics. We understand why they would want to do that. It's not material, the loss is not material to us.

The thing we find incongruous, however, is claims that somehow that that is pro-competition or somehow this is open access, when in reality it's exactly the opposite. It's a market carve up putting all those in one place and have the economics split between people. A similar thing has happened with respect to the equity side of the Russell business which has moved exclusively recently to CBOE. Again, CBOE being a person that – an equity options exchange that puts out unique content, has been very successful in its unique content. And a decision made to put all that together in a vertical and carve up the economics.

Alex Kramm
UBS Securities LLC

Q

All right. Great. And then, maybe secondly, for Scott, I guess, capital returns have come up a few times already, but if I just look at your buybacks here, around $200 million per quarter over the last three quarters. Absent any other things I think is that a good range to think about for now? And then in general how do you feel about, again, absent any sort of M&A, adding more leverage to balance sheet, any recent discussions with the ratings agencies? I know you're just getting to know them still, but how do you feel about leverage in general?

Scott A. Hill
Chief Financial Officer

A

As I mentioned in my prepared remarks, our leverage target is still 1.5 times. I think that's where – we'll need to be around that in order to maintain the current rating we have, which is important to us as clearing house operators. I also mentioned that we will maintain about a $500 million cash balance. After that it's our intention, as I said in our prepared remarks, is to continue to return cash to shareholders as we have been doing.

If you look, I think it was slide 15 in the deck, we've already returned almost $600 million this year, that's versus around $900 million for the full-year last year. We've, as you mentioned, been very consistent in buying back our shares because I think it clearly expresses the view that we think that is the best investment and the best use of our capital and we've grown our dividend.

So I think what you should continue to expect is other than CapEx and to the extent we find M&A that generates higher return on invested capital, we're going to continue to deploy our cash strongly towards share repurchases and dividends.

Alex Kramm
UBS Securities LLC

Q

All right. Very good. Thank you.

Operator: Thank you. And the next question comes from Brian Bedell with Deutsche Bank.

Brian B. Bedell
Deutsche Bank Securities, Inc.

Q

Hi. Good morning, folks. Scott, maybe if you could, just talk a little bit more about the expense outlook trajectory as we move into the fourth quarter. I think you said last quarter that the expenses could trend – that trajectory could trend down into the fourth quarter and then as we move into the first quarter 2016. I think a couple of quarters ago you gave guidance on the expense synergy realization road map and obviously, I think you're tracking ahead of that. So just maybe an update on, I think the $450 million of annualized expense synergies that you thought you'd be at a run rate basis in 1Q 2016, if you think you might be ahead of that, and maybe what is that number as of 2Q, as of this quarter?

Scott A. Hill
Chief Financial Officer

A

Yeah. I think what's really important is to focus on our overall expense trajectory and the margin expansion that you're seeing. We're three years removed almost from announcing the deal, almost two years removed from closing the deal. In the intervening period of the time, we bought four new businesses, we've invested in growing organically our internal businesses. So we're really very focused on our overall expense trajectory. Inside that, we are well on track towards our synergy objectives. As I said in the quarter, you mentioned that it was going to decelerate over the course of the year, but synergies actually accelerated into the second quarter, and so if you look at the guidance relatively, we're now at or likely, slightly below our full-year guidance. If you'd taken the mid-point of our original guidance, it was down 3%. We're now down 4%, and that's against the backdrop of growing revenues.

The other thing, I think, that's important is we just don't manage expenses through synergies. We manage expenses across all of our businesses. And so as we move forward, we're going to be really focused on what is the net trajectory of our overall expenses. We expect those expenses to continue to improve, which will allow margins to continue to expand. And I think the real visibility to our progress is going to be found in the margin expansion, which, as I mentioned, in the quarter, 6 points up year-to-year to 59%; right on track, frankly, to where we thought we'd be a couple years ago.

Brian B. Bedell
Deutsche Bank Securities, Inc.

Q

Yeah. Yeah, I know, it sounds like that trajectory would have you at a lower overall expense rate as we get into the fourth quarter and particularly given the projects that you're working on for NYSE with the margins over 50% for the NYSE business. Is that fairly accurate?

Scott A. Hill
Chief Financial Officer

A

Yeah. Again, I think we gave pretty clear guidance on where we thought third quarter and fourth quarter would be. I definitely think the trends are positive because embedded in that guidance, frankly, are investments to enable, as Jeff said earlier, improvements in our compliance functions and the efficiency of that organization. It's investments that are necessary to integrate our SuperDerivatives acquisition, our Holland Clearing House acquisition, so despite those investments, which are reflected in the third quarter and fourth quarter guidance, the expenses will be down year-to-year. And then once those investments are made, we'll realize the benefit of them as we move into 2016.

Brian B. Bedell
Deutsche Bank Securities, Inc.

Q

Okay, great. Thanks. And then maybe just back on the market data, it sounds like you've got great traction in the core businesses. If you can, comment about SuperDerivatives a little bit and the ICE Benchmark Administration from a revenue contribution? Is that – were they not as bigger growth contributors in the second quarter? And then as we move into 2016, do you expect them, both of them to become much more meaningful in that growth trajectory?

Scott A. Hill
Chief Financial Officer

A

Yeah. So we gave guidance at the beginning of the year that I think was we expected our acquisition to be $50 million to $55 million in revenues. And that was largely SuperDerivatives and that was incremental revenue. And I think we're largely right on track to that. And what I would suggest to you is that's not inconsistent with their prior year performance. I do expect as we move into 2016 that that business can grow for us, because what we're doing right now is we're really integrating it, we're leveraging their resources to help us build out our clearing offerings. And so, I think as we get that business more integrated, invest in resources to expand it, it will certainly contribute to growth as it moves into 2016. So, I'd characterize SuperDerivatives as pretty much on track to what we thought it would be this year and definitely a growth opportunity in the next year.

And look, ICE Benchmark Administration is still a relatively new business. We've just recently kicked off the Gold Fix, the ICE swap rate is still relatively new. And so I definitely do that business – it's certainly already contributing this year, but I do think it's a business that can grow next year and we're making significant investments in that business to help it grow as we move into the future.

Brian B. Bedell
Deutsche Bank Securities, Inc.

Q

Okay. Great. Thanks very much.

Operator: Thank you. And the next question comes from Alex Blostein with Goldman Sachs.

Alexander V. Blostein
Goldman Sachs & Co.

Q

Thanks. Great. Good morning, everybody. The question for you guys on just what's been, kind of, going on in the oil markets more recently, specifically curious if you could give us a little more color on any changes in, kind of, participation or client behavior we saw this time around with the slide in July versus what was happening at the end of the last year; producers versus consumers versus, kind of, financial folks, who's been more or less active on that front? Thanks.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Yeah, it's interesting, well I think the major trend that you'll see is that open interest is moved higher and is up at record levels and so there is a lot of interest in those markets. I think a lot of lay people think, oh, if the price is going down then nobody is interested in using it for hedging, but the reality is people that buy oil want to try to buy it at a low price and lock in low prices. And so these are two-sided markets and there's always one side that's interested in whatever the trend is, up or down, and that's how ultimately we would make a market.

So, we still are very focused on commercial users. You'll see in the commitment of trader reports that we file publicly that we continue to see very, very strong commercial interest in the oil markets. We have a large – we talk a lot about Brent because it's our flagship and it's now become a regulated benchmark, and has become a global benchmark. But, we have many, many other oil products, including gasoil. Gasoil, you may recall, we changed the specifications to make it closer to diesel fuel. And we also changed the settlement date on that. And so we had a lot of movement around gasoil. And that happened over the last 18 months or so. That's all in place now and what you're seeing is volumes of gasoil trading have also been rising now that that contract has landed on its ultimate design. So, we feel pretty good about that business from all of, long-term, from all of those trends that we're seeing.

Alexander V. Blostein
Goldman Sachs & Co.

Q

Got you. And then, Scott, just one for you, on the 100% retention of NYSE Amex, I'm not sure if I missed it, but what does that mean for the kind of operating results of the company on kind of whole pre-tax basis?

Scott A. Hill
Chief Financial Officer

A

We haven't disclosed what the dollar amounts are. I don't want to be trite and tell you it means we get to keep 100% of it, but that's really effectively, we've moved from getting 84% to 100%. It's not, in the scheme of things, it's not a huge amount. For that business, it's important, because what we've seen, you've seen us walk away from volumes that aren't helping to deliver profit to the bottom-line. There has been some impacts around some of those volumes as we worked our way through that Amex partnership. I think now what you saw in the first quarter and in the second quarter you see it even more clearly share seems to have stabilized, it was actually a little bit better in July versus what we saw in the second quarter. So, generally, with that business, what we're seeing is stable share, relatively stable rate capture, and as we've bought back that profit, an improving profitability to the business overall.

Alexander V. Blostein
Goldman Sachs & Co.

Q

Got it. Thanks so much.

Operator: Thank you. And the next question comes from Ken Worthington, with JPMorgan.

Kenneth B. Worthington
JPMorgan Securities LLC

Q

Hi. Okay. I think this is question six on data, so I apologize. But, as we think about growing data revenue and earnings going forward, how you are thinking about the opportunity of growing the business that goes beyond ICE's proprietary data? You've got LIBOR, Gold Fix, I guess SuperDerivatives is in there as well. What are really the next steps for growth beyond ICE's own data?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

Well, first of all, I think maybe implicit in your question is the notion that our data is the data that is the obvious data, which is the output of trading. But, the other thing that we believe that we have that is unique content that has yet to have been developed. Because of our broad relationship with a lot of companies and the way we touch them, there is a lot of, let's say, non-trade data that we collect through the various ways we touch our customers than can be organized up and potentially have value back into the market.

And we are building through the team that we have at SuperDerivatives more predictive capabilities and analytical capabilities to take all of that rich dataset and put it into context. And we think that would, sort of, be the next leg up. Couple that with the fact that we made a decision, we didn't talk a lot about it at the time but we made a decision when we spun off a lot of the NYSE technology businesses to actually keep the network that's called Safety so that we have better distribution into our client base, and more importantly in a world where people are concerned about security, and we are hyper-concerned about security, we think that the trends on the way data is delivered are going to move towards very, very highly secured relationships between us and our customers and we've got this great infrastructure to do that.

So, all of those are more than just selling the trade data, the exhaust that comes out of it; exchanges and all of the things that I mentioned as growth opportunities are quite high value and there are things that when we talked to customers increasingly they are telling us that they are willing to pay for those.

Kenneth B. Worthington
JPMorgan Securities LLC

Q

Perfect. And just lastly, China is topical today. I think both CME and Virtu had some sort of disclosure or announcement. Updated thoughts in terms of tapping China, you've got Singapore launching next quarter. I think initially you were going to do lookalike contracts. Have you, kind of, circled back on the China strategy? And if so, what are your thoughts today?

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

A

First of all we do have an FX franchise and we have the dollar index and I would just mention that RMB is not a part of the dollar index. It's been a conversation we've had for a couple years, but – so, with respect to FX it's had no real impact on us. That's China FX that has no real impact on us.

Our China strategy is we want to open an exchange and clearing house in Singapore. Honestly, we don't have a – it is a very hard nut to crack in financial services. The government there has made it very clear that they're going to control access to markets in and out, and so what we want to do is be positioned in the region. And having – we are in constant dialogs over there. We have an office in China and colleagues that are working on improving our position every day, but it is a difficult area to penetrate in the financial services space and personally I understand why that is and don't begrudge their government for wanting to have controls over that as they move their population into the middle-class.

So in any event, long story short, this Singapore launch for us is strategic and important.

Kenneth B. Worthington
JPMorgan Securities LLC

Q

Thank you very much.

Operator: Thank you. And that concludes the question-and-answer session. So, at this time, I would like to turn the call back over to management for any closing comments.

Jeffrey Craig Sprecher
Chairman & Chief Executive Officer

Well, thank you, Keith, and thank you all for joining us on the call. We'll continue to report on our future results in future calls like this. And have a good day.

Operator: Thank you. The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.