Q312 Earnings Call Prepared Remarks
October 25, 2012

Gill

- Thank you for joining us this morning. I will discuss our performance in the third quarter, and provide updates on a few of our strategic initiatives, before turning things over to Jamie to review the financials.

- During the third quarter, we continued to take steps to strengthen our business in a dynamically changing environment. One of the main things we think about and have focused on during the last few years is how to position the company to address customer needs as the market rapidly shifts. I'll talk about that a bit today.

- Let me start with Interest Rates. We have worked hard over the last few years to enhance our interest rate product offering in light of the Fed's zero interest policy and have had several successful product introductions since 2010. These developments have added more than 305,000 of average daily volume, and 3.8 million of open interest, to our interest rate complex. More recently, we announced that we will launch deliverable Interest Rate Swap Futures contracts in November. This innovative new product will benefit clients by providing a unique new way to access interest rate swap exposure. Our customers will now have a complementary standardized product that provides the advantages offered by futures contracts including pricing transparency, ease of legal documentation, the automatic netting of positions, and margin savings. Interest Rate Swap Futures were created to meet strong demand from financial market participants including banks, hedge funds, asset managers and insurers. Citi, Credit Suisse, Goldman Sachs, and Morgan

Stanley are among the firms who are planning to serve as market makers for the product, enabling market participants to access deep and liquid markets.

- Turning to FX, for the first time ever, CME Group's FX ADV surpassed the volumes of all of the OTC FX platforms to become the largest FX venue globally, with CME Group's September average daily notional traded of $129 billion. This was driven by strong growth with asset managers and particularly with banks. In addition, FX open interest reached its highest level ever in September, and the CFTC's Traders of Financial Futures report also shows a record level of large open interest holders for CME Group FX products. This confirms that the an increasing number of market participants are holding more FX risk in the form of CME Group FX Futures, a trend which counters much of the "risk-off" sentiment in the OTC Cash FX markets.

- Moving on to energy, we are in the process of expanding our OTC energy offering. Dodd-Frank regulation is driving changes to the OTC energy markets. CME Group has a long history of providing customer choice and flexibility within a strong regulatory framework, and with this background we are well positioned to help customers adapt their current practices to new regulations. Customers can now access the CME ClearPort slate via multiple execution methods, including the ClearPort EFS offered historically, our Globex central limit order book, the trading floor, cross trades and block trades. These expanded execution options provide futures regulatory treatment, for those customers to whom this is a concern. To help energy markets manage through this transition period, ClearPort EFS transactions are exempt from counting towards swap dealer thresholds through the end of this year.

- In this evolving regulatory climate, we continue to roll out new tools to bolster customer choice including CME Direct, a platform for side-by-side online trading of Exchange listed and OTC markets and CME Direct Messenger, a sophisticated messaging platform integrated with CME Direct, and ConfirmHub trade confirmation services. CME Direct Messenger will be powered by market-leading instant messaging software developed by Pivot, Inc., which we recently acquired. Additionally, we are in the process of applying to be a Swaps Data Repository, which will allow us to assist customers in managing their swap reporting needs.

- We understand our customers' concerns during this state of regulatory flux. We continue to lead the effort with other market participants to ensure our offering meets their needs and to advocate on behalf of our customers for clear, logical regulatory policy that protects end users' ability to manage risk safely and effectively. Our leadership here, the strength of our product offering and its flexibility going forward, as well as our strong focus on meeting customer needs will continue to make CME ClearPort a key risk management tool for energy markets during and after this period of regulatory change.

- CME Group's agricultural commodities continue to meet the demand of our customers. ADV for the third quarter was up 14 percent compared to the same period last year. Open interest has also grown from 6.1 million open contracts at the beginning of the year to 8.8 million open contracts on October 23, 2012, which represents growth of 44 percent.

- Moving on to our growth initiatives, we continue to expand our product offering and enhance our global partnerships. We announced the launch of U.S. dollar denominated Ibovespa Futures that have recently started to trade. This new cross-listing arrangement provides our customers access to Brazil's key benchmark product and this initiative allows our clients to improve their ability to manage market and counterparty credit risk exposure across various asset classes. In addition, BM&FBOVESPA has begun trading in the S&P 500 futures contract settled in cash to the price of the S&P 500 Index futures contract. This is the first futures contract traded on the Brazilian Exchange to reference a U.S. stock index.

- Turning to the clearing area, we remain well positioned to benefit from the regulatory mandate as we continue to focus on our capability to onboard new customers and expand our OTC product offering. We have worked extensively with the buy-side and sell-side for a purpose built solution to meet the needs for real-time clearing, unlike some of our competitors. Overall, we continue to experience a significant increase in firms finalizing their internal OTC clearing readiness, and setting up production accounts to prepare for clearing.

- In addition, we recently announced the approval to provide portfolio margining of OTC interest rate swap positions and Eurodollar and Treasury Futures for customer accounts beginning in the fourth quarter of 2012. The risk reduction achieved will result in capital efficiencies for customers of up to 90 percent for certain portfolios, figures that remain unparalleled in the industry. This offering complements the same portfolio margining for house accounts that went into effect earlier this year.

- Also, we recently incorporated a pricing discount plan for high turnover swaps participants who tend to maintain risk neutral portfolios that do not require large amounts of initial margin. This is an important step for us to continue to onboard a more diverse portfolio of customers, which we feel benefits our markets by providing liquidity and higher efficiencies.

- Shifting to our globalization efforts, we continued to make progress during the quarter. We applied to the FSA to create a London-based derivatives exchange with an expected launch in mid-2013 pending regulatory approval. This will allow us to build on the success I mentioned earlier in FX. Similar to the demand we have experienced in the U.S. with customers migrating to our FX products, there has been strong demand from market participants in Europe to have access to the FX futures market under the umbrella of the FSA. With that in mind, we will initially begin trading foreign exchange futures products and then expand into other asset classes. We continue to see an increase in business coming from our diverse set of customers in Europe, with more than 16 percent of our total volume now originating from the region, and 24 percent in FX products. Having an exchange in London that can leverage the central counterparty model of CME Clearing Europe will allow us to align ourselves even more closely with our regional customers in both listed futures and OTC markets, and provide additional opportunities to expand our non-U.S. customer base through regional trading and clearing solutions for Europe and Asia.

- Additionally, we continue to make significant progress in our efforts in China. As we have mentioned before, our objective has been to facilitate operational readiness of the Chinese FCMs. This progress was evident when 35 Chairmen and CEOs of Chinese FCMs visited Chicago last month, including one week at the CME Group, to bridge knowledge and operational gaps in market access and on-boarding, clearing and risk management, regulatory readiness, and products and hedging.

- We also renewed the existing Memorandum of Understanding with the Shanghai Futures Exchange, which has created a forum for information sharing between the two organizations regarding the potential development of derivatives products in China. In addition, we expanded our overall suite of Chinese Renminbi products to include deliverable Renminbi futures. We also announced the launch of Chinese Steel Rebar Swap Futures, which allows customers who have exposure to the Chinese construction and rebar industries to manage their price risk by using the most relevant price data.

- Lastly, we also announced last week that we have entered into a definitive agreement to acquire the Kansas City Board of Trade, the world's premier exchange for trading hard red winter wheat futures and options contracts, which serves as the international benchmark for wheat used in bread. This acquisition will expand and diversify our agricultural product offerings to include high protein wheat, which is the largest physically produced U.S. wheat grade and the primary export of wheat globally from North America. In addition, it will provide us the opportunity to grow the core through spread opportunities between wheat products as well as growth in options, including new products. It also will give an enhanced opportunity to provide capital and operational efficiencies for customers.

- In summary, I want to reiterate that we have taken steps to strengthen our business in this environment and we will not be complacent. We remain efficient and continue to generate a lot of cash while also investing in the business. We are working hand-in-hand with customers, including an expanding group of intermediaries, to help them navigate in this new world.

- Now, I will turn the call over to Jamie to discuss the financials.

Jamie

- Thank you Gill and good morning everyone. Today, I am going to review the results of the quarter. It was a tough environment with regard to trading volume, but we continue to make progress in terms of what we can control. Excluding the non-recurring tax entries, our earnings per share would have been $.70 per share[1].

- Let me start the detailed discussion on the quarter with revenue – as Gill mentioned, average daily volume was down compared to an exceptionally strong third quarter last year, however, we saw an uptick in the rate per contract for the same period.

- The rate per contract for the third quarter was 82.2 cents, which was up 6 percent from the third quarter last year and up 1 percent sequentially. Compared to last quarter, the product mix was favorable, and lower incentives had a positive impact on the RPC.

- Turning to expenses, total operating expense was $287 million. Although the lower expense was partially driven by the removal of costs previously associated with the Dow Jones and CMA businesses, it also reflects our continued focus on managing the organization as efficiently as possible while still progressing with key longer-term growth initiatives. That said, we also had some positive timing-related benefits in Q3, which will result in additional Q4 expense.

- Starting with Compensation and Benefits, this line item was $118 million, which included a $12 million bonus accrual, down 38 percent from Q3 last year, and $14 million in stock based compensation. In addition, due to the 6 percent increase in the equity market in Q3, we booked $1.9 million in deferred compensation expense, which is offset with higher investment income, compared to a ($1.7) million credit to expense in Q2 for deferred compensation losses.

- Our overall headcount went down during Q3, from 2,604 to 2,546, driven primarily by the S&P Dow Jones transaction with 110 employees having moved off the CME Group payroll in July. Additionally, in the quarter, we added 33 employees from the Pivot acquisition, and we hired 13 folks in Northern Ireland as we continue to staff up there.

- Turning to non-compensation expense, the main items that dropped sequentially were amortization and professional fees, both as a result of the S&P/Dow transaction. In addition, other expense which includes marketing, dropped sequentially due to timing related items in marketing, and a reduction tied to changes in foreign currency exchange rates.

- Looking ahead to Q4, we expect expenses to come in between $300 to $305 million, which includes a full quarter of expense from the Pivot transaction. The two line items which will likely rise are other expense, due primarily to higher marketing expense driven by several events in the fourth quarter, and professional fees mainly due to regulatory related expenditures. During our last earnings call, I said I expected our 2nd half expense to be $595 million; with today's results combined with the new Q4 guidance, that drops to between $587 and $592 million.

- Turning to non-operating income, we received $9.7 million from dividends from our investments in BM&FBOVESPA and IMAREX up from $6 million last quarter. Also, in the third quarter, we issued $750 million of 10-year debt at an all in cost of 3.4 percent. We will be using these funds to retire our outstanding 5.4 percent notes due next August. In terms of modeling this, the interest expense this quarter was partially impacted and increased to $30.2 million. The run rate for interest expense the next few quarters will be approximately $35.5 million, and then once the lower rate kicks in we will save approximately $15 million annually due to the lower rate over the next 9 years. Lastly, equity in gains and losses of unconsolidated subsidiaries was $16.5 million, with our share of the S&P Dow business coming in at $17 million, stronger than we originally projected.

- Capital expenditures net of leasehold improvement allowances totaled $35 million in the third quarter. For 2012, our CAPEX expectations are now in the $140 to $145 million range.

- The pro-forma tax rate was 40.7 percent[1] in the quarter and we expect the Q4 tax rate to be slightly below this. Turning to the balance sheet, we had $2.1 billion of cash and marketable securities at the end of September, which included the $750 million of debt that we took on.

- As Gill mentioned we announced the potential acquisition of the Kansas City Board of Trade last week. We think the combination of the two major wheat products will lead to capital and operational efficiency for our customers, while we work to expand the business. We will be investing $126 million of cash in this transaction, and we expect the deal to generate returns in excess of our cost of capital, while also being slightly accretive.

- Even with this transaction, we will have excess cash at year-end. As I mentioned last quarter, we remain focused on returning this excess to our shareholders, and our board will meet prior to the end of the year to discuss our plans.

- In summary, we continue to focus on investing for the future, being ever more efficient and generating and returning excess capital to our shareholders.

- With that, we'd like to open the call up for your questions. Only one question and one follow up please.

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1) ***A reconciliation of the non-GAAP financial results mentioned to the respective GAAP figures can be found within the Reconciliation of GAAP to Non-GAAP Measures chart at the end of the financial statements. Third-quarter 2012 results included a non-recurring $16 million increase to the company's income tax provision related to increases in deferred income tax liabilities associated with S&P Dow Jones Indices and the company's acquisition of Pivot, Inc.***