CME Group 1Q 2020 Earnings Script – April 29, 2020

John Peschier

Good morning and thank you for joining us. I am going to start with the safe harbor language. Then I will turn it over to Terry and John for brief remarks, followed by questions. Other members of our management team will also participate in the Q&A.

Statements made on this call – and in the other reference documents on our website – that are not historical facts, are forward-looking statements. These statements are not guarantees of future performance. They involve risks, uncertainties and assumptions that are difficult to predict.

Therefore, actual outcomes and results may differ materially from what is expressed or implied in any statements. More detailed information about factors that may affect our performance can be found in our filings with the SEC, which are on our website.

Also, on the last page of the earnings release, you will find a reconciliation between GAAP and non-GAAP measures.

With that, I would like to turn the call over to Terry.

Terry Duffy

- Thank you all for joining us this morning. We hope you and your families are healthy and staying safe. Today, we have Julie Winkler joining us, along with Ken Vroman. Julie heads our global sales and research areas, and she has taken over our data business. Ken is now running our optimization area and our international business. Julie and Ken are taking on several of Bryan Durkin's responsibilities as he transitions to his role as an advisor. Also, I am going to have Derek make a few comments regarding the energy markets at the end of my remarks.

- These are extraordinarily difficult and challenging times for all of us. The COVID-19 pandemic has taken a devastating toll on human life and created unprecedented uncertainty around the world. It has also changed our daily lives in ways that seemed unimaginable only a few weeks ago.

- The heroes in this crisis are clear. Our sincere thanks go out to the entire medical community fighting this disease on the front lines and aggressively working toward a vaccine. We also want to thank the many first responders who continue to risk their lives to keep us safe.

- At CME Group, we remain focused on the health and safety of our entire community. We took early action and were the first in the industry to close our trading floor to protect our employees and market participants who access that facility on a daily basis. We also implemented 'work from home' mandates and travel restrictions to protect employees across our global offices.

- We are proud of the resilience of our team and how they have risen to this new challenge. Our employees continue to work incredibly hard to help our customers and partners navigate through this unique period with its increased uncertainty and volatility.

- With that in mind, I'd like to highlight a number of metrics that we think reflect our performance this quarter and are important to consider as we look forward:

- Our systems and processes performed extremely well with peak order traffic during the quarter, and we saw very consistent response times. Our highest volume day on record took place in the first quarter, when we traded 58 million contracts on February 28th.

- Aside from the peaks, Q1 volumes set records across many different product areas as our global clients managed risk. Average daily volume for the quarter was 27 million, up 45 percent from first-quarter 2019.

- In addition, our volume in the first quarter from clients outside the United States was particularly strong, averaging 7.3 million contracts per day - up 56 percent. As a result, clients continued to be able to manage their risk across all products and all time zones.

- We also maintained our industry-leading clearing function to provide safeguards for every trade. In response to increased volatility, we raised margins on many products across most asset classes.

- These prudent risk management policies were reviewed with both our clearing house risk committees and our regulators. We are in daily contact with our regulators to ensure the health of our markets during these unprecedented peaks of volatility.

- Turning to the trading floor for a moment:

- Our options volumes in key products, especially interest rates and equities that have traditionally relied on the floor, have held up well since we closed it. We successfully assisted many clients who traded on the floor to the screen, leveraging our own front-end platform in order to quickly register and onboard a significant number of new users over a short time period.

- And, in the six weeks since then, interest rate options as a percentage of interest rate futures, have remained at roughly the same levels. So far, these volumes are actually ahead of where they were on the last few days that the pits were open.

- As many of you know, we have made a significant effort to increase our global sales presence. We began to make an investment several years ago to deepen our client coverage around the globe, and that has served us extremely well with our regionally-focused sales model.

- Today - more than half our sales staff is based outside the United States. We have sales professionals in 19 cities located in 15 countries around the world.

- Our sales, product management, clearing and operations teams have worked closely together to handle client engagement during this pandemic, with client interactions at a record high. Client feedback consistently mentions that our proactive outreach stands out compared to others in our industry.

- We believe these efforts will continue to pay off. We saw broad-based strength in volumes across all customer groups including:
  - asset managers,
  - hedge funds,

    - banks,
    - proprietary trading firms,
    - commercials and retail.
- Our retail business was up 75 percent with significant strength in the U.S., Europe and Asia, and support from our broker partners

- Last, but certainly not least, we made considerable progress during Q1 to integrate the NEX business. We divested NEX Exchange, and we integrated our London offices where more than 600 of our employees work. We completed over 290 cross-selling meetings to clients from both our traditional futures business, and those of the cash and optimization businesses we acquired. For reference, that compares to 400 of those cross-selling meetings during the full year of 2019.

- The largest percentage of these meetings continue to be focused on new clients in our interest rates and FX futures and options businesses – and we also are seeing success within optimization, EBS, BrokerTec and data services.

- To summarize the first quarter, the market environment was challenging for all of us on a professional and a personal level. I am proud of the dedication of our employee base as they stepped up to the challenge. We also appreciate the trust that our market participants have in our ability to deliver results.

- Looking ahead, we do not yet know what the long term impact of COVID-19 will be. But we do know that financial markets are an important part of maintaining our economy and – ultimately – recovering from this tragedy.

- As we move forward through 2020, our strategy remains the same:
    - To build strong global benchmark offerings with deep liquidity around the clock
    - To continue our commitment to offer all of these asset classes on common platforms
    - To deliver world class risk management and capital efficiencies
    - To promote broad participation, offer robust distribution and continue developing our strong channel partnerships

- We look forward to answering any questions you have, but before that, I will turn the call over to Derek. Thank you.

- **<u>Derek Sammann</u>**

- Thank you. As Terry mentioned, the COVID-19 pandemic has caused increased uncertainty and elevated volatility across all of our asset classes, including our global crude oil market.

- I'd like to take a moment to provide our perspective on what happened in the crude oil market last week to offer further context for these events. Overall, the WTI futures markets performed as they were designed in a challenging market environment – and I'll share a few comments on what we saw in the market to illustrate that further.

- Continued downward price pressure and a significantly steepening contango have created unique challenges for the global oil market for the past few months. Along with a significant oversupply of oil, there has also been a drastic reduction in global demand – with global daily oil consumption decreasing from 100 million barrels a day to 70 million barrels per day. Heightened concerns about storage capacity in the U.S. and abroad intensified the downward pressure on oil prices as well.

- In early April, anticipating that these market dynamics may create the potential for negative pricing, CME Group proactively informed our regulator, our clearing firms and the marketplace that our trading and risk management systems were capable of handling negative prices in the WTI contract should market dynamics require it.

- Prepared for such an eventuality, we saw WTI trade negative on April 20, driven by the same fundamentals I mentioned a moment ago: oversupply, reduced demand, and increasingly full US storage. Our WTI contract reflected these challenging underlying dynamics on Monday as the cash and futures markets were converging going into Tuesday's final settlement.

- I should also note that, while negative prices are rare, they are not entirely new in energy markets. We have seen multiple examples of negative pricing in energy and power markets in the US, Germany and the UK.

- I'd also like to briefly comment on the strength of WTI as a global benchmark. Today, WTI represents 56% of the global trade in crude oil futures, including more than 60% in April. WTI is the market's choice for managing crude oil exposure, and we believe that is because optimal commodity benchmarks are based on physically-delivered products. Physical delivery is the gold standard for these contracts because it ensures convergence with the underlying cash market. Commercial and end-user customers who participate in physical oil markets need the certainty that convergence provides so that they can optimally manage their underlying risks. WTI futures settle with actual transactions that result in physical delivery as opposed to other products which are disconnected from the physical and settled via assessments.

- We are pleased that WTI markets continue to reflect broad participation from all client segments around the world, and in every time zone. Year-to-date our overall crude and refined products volume during Asian trading hours is up 148% and Europe has increased by 48%. Importantly, we also continue to provide our clients with the leading crude oil options tools, which have grown 57% in the first quarter and are particularly important to our clients in times of heightened volatility.

- In summary, against this backdrop of extremely challenging market dynamics, our benchmark physically-delivered WTI crude oil contract continues to perform to help our clients hedge and transfer their risk in global oil markets.

- With that, I'll turn the call over to John.

John Pietrowicz

- Thanks Derek.

- As Terry mentioned, the investment in our technology and the dedication of our employees served our clients well during this unprecedented time.

- During the first quarter, CME generated more than $1.5 billion in revenue, up approximately 29% from last year. Expenses were very carefully managed and on an adjusted basis were $459 million for the quarter and CME had an adjusted effective tax rate of 23.6%, which resulted in an adjusted diluted EPS of $2.33.

- Capital expenditures for the quarter were approximately $38 million.

- During the quarter, CME paid out $1.2 billion to our shareholders in the form of our annual variable dividend of $2.50 per share and our regular dividend of 85¢ per share, which is up 13% from a year ago. CME's cash at the end of the quarter was approximately $1.0 billion.

- We continued to pay down our debt. We have approximately $100 million of outstanding commercial paper which we will pay down by the end of the year. This quarter we achieved our 1x debt to EBITDA target.

- We continue to progress on the integration of our legacy BrokerTec and EBS trading systems. Our technology and operations teams continue to work towards a migration of the BrokerTec platform to Globex in the fourth quarter with EBS following in 2021. Our testing environment is up and BrokerTec clients are testing the system. We will be working closely with our customers during the next several months while we navigate the added complexity of remote working environments, but at this time, we continue to target the fourth quarter.

- At this point, we continue to expect our operating expense this year excluding license fees to be in the $1.64 to $1.65 billion range. In addition, our tax and CAPEX guidance remains unchanged.

- Please refer to the last page of our Executive Commentary for additional financial highlights and details.

- In summary, we are very pleased with the performance of the company. Our employees adapted to the challenges of this environment and worked relentlessly on behalf of market participants. Our global employees, along with the investments we have made in our technology systems and processes, ensured the markets operated well and risk was effectively managed.

- In closing, I hope you and your families are healthy and safe during this difficult time.

- We would like to now open the call for your questions. Please limit yourself to one question. John Peschier and I will be available today for any follow-ups you might have after the call.

- Thank you.

Statements in this document that are not historical facts are forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or implied in any forward-looking statements. We want to caution you not to place undue reliance on any forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. Among the factors that might affect our performance are increasing competition by foreign and domestic entities, including increased competition from new entrants into our markets and consolidation of existing entities; our ability to keep pace with rapid technological developments, including our ability to complete the development, implementation and maintenance of the enhanced functionality required by our customers while maintaining reliability and ensuring that such technology is not vulnerable to security risks; our ability to continue introducing competitive new products and services on a timely, cost-effective basis, including through our electronic trading capabilities, and our ability to maintain the competitiveness of our existing products and services, including our ability to provide effective services to the swaps market; our ability to adjust our fixed costs and expenses if our revenues decline; our ability to maintain existing customers at substantially similar trading levels, develop strategic relationships and attract new customers; our ability to expand and globally offer our products and services; changes in regulations, including the impact of any changes in laws or government policy with respect to our products or services or our industry, such as any changes to regulations and policies that require increased financial and operational resources from us or our customers; the costs associated with protecting our intellectual property rights and our ability to operate our business without violating the intellectual property rights of others; decreases in revenue from our market data as a result of decreased demand or changes to regulations in various jurisdictions; changes in our rate per contract due to shifts in the mix of the products traded, the trading venue and the mix of customers (whether the customer receives member or non-member fees or participates in one of our various incentive programs) and the impact of our tiered pricing structure; the ability of our credit and liquidity risk management practices to adequately protect us from the credit risks of clearing members and other counterparties, and to satisfy the margin and liquidity requirements associated with the BrokerTec matched principal business; the ability of our compliance and risk management methods to effectively monitor and manage our *risks, including our ability to prevent errors and misconduct and protect our infrastructure against security breaches and misappropriation of our intellectual property assets; our dependence on third-party providers and exposure to risk through third-parties, including risks related to the performance, reliability and security of technology used by our third-party providers; volatility in commodity, equity and fixed income prices, and price volatility of financial benchmarks and instruments such as interest rates, credit spreads, equity indices, fixed income instruments and foreign exchange rates; economic, social, political and market conditions, including the volatility of the capital and credit markets and the impact of economic conditions on the trading activity of our current and potential customers; the impact of the novel coronavirus (COVID-19) outbreak and response by governments and*

other third parties; our ability to accommodate increases in contract volume and order transaction traffic and to implement enhancements without failure or degradation of the performance of our trading and clearing systems; our ability to execute our growth strategy and maintain our growth effectively; our ability to manage the risks, control the costs and achieve the synergies associated with our strategy for acquisitions, investments and alliances, including those associated with the acquisition of NEX; our ability to continue to generate funds and/or manage our indebtedness to allow us to continue to invest in our business; industry and customer consolidation; decreases in trading and clearing activity; the imposition of a transaction tax or user fee on futures and options on futures transactions and/or repeal of the 60/40 tax treatment of such transactions; our ability to maintain our brand and reputation; and the unfavorable resolution of material legal proceedings. For a detailed discussion of these and other factors that might affect our performance, see our filings with the Securities and Exchange Commission, including our most recent periodic reports filed on Form 10-K and Form 10-Q.