Q112 Earnings Call Prepared Remarks
April 26, 2012

<u>Craig</u>

- Thanks John. Good morning and thank you for joining us today. Before I turn this over to Gill to review our first quarter performance, I wanted to say that our succession transition has been going extremely well. As I'm sure everyone appreciates, the close working relationship and teamwork between me, Gill and Terry over these past 9 years is making this transition very easy. Since the announcement of my retirement, we have been and are continuing to transition internal responsibilities. We have also been spending time with our customers, partners and industry colleagues to ensure a smooth hand-off in areas where I was playing a more active role. Given our exceptional progress, I would expect that the formal part of my transition can be completed in the coming weeks and prior to our annual shareholders meeting. This will give us the ability to accelerate Gill's assumption of the CEO role and to ensure that we keep moving forward with purpose on the execution of our global growth strategy.

- Given that this will be my last earnings call, I want to thank each and every one of you for your friendship and support during these last eight and a half years. I will miss interacting with you, and want to wish all of you and my CME Group colleagues much continued success. CME Group is a very strong institution with great people, products and partners and I will enjoy watching the company thrive and prosper with your continued support.

- With that, I will turn it over to Gill.

Gill

- Thank you, Craig. The CME Group is certainly blessed to have had Craig at our helm over the last nine years.

- During the first quarter, global trading volumes were impacted by low levels of volatility. The uncertainty about market direction has led to greater focus on the release of economic data that measures the overall health of the economy. While concerns remain, there are some positive signs that an improving economy would bode well for our product set, as the trading community responds to better news.

- With that as a backdrop, I am going to spend my time today talking about the areas that are well within our control, and those include product, technology and clearing offerings. We have accomplished a great deal during the first 90 days of the year. Let me provide some examples.

- First, in terms of products, a couple of takeaways. While volume has been muted, we are performing fairly well compared to our peers in several product areas, and second, we've seen a nice pick up in open interest which has jumped by 16 percent from year-end 2011 to 90.5 million contracts. Lastly, we continue to lead the industry with the breadth of our product innovation and our global relationships.

- Interest rate volume was down from a year ago, but down significantly less than our European peers. Although volumes for us have been hindered on the short end, it is important to note the deepened liquidity in the middle of the curve has helped. For example, at the beginning of 2011, we launched mid curve options on year 4, the so-called blue mid curve options. This contract averaged almost 250,000 contracts per day in March, and was very active as volatility picked up temporarily. Another important innovation was our weekly treasury options, which continue to gain traction each quarter. On Thursday, March 8th, in anticipation of the non-farm payroll report, we traded 78,000 contracts, and it has become a popular gamma product for trading economic events. These new products build on the success we had two years ago with our Ultra Bond Treasury offering. In addition, longer-dated treasuries -- 10's, 30's and Ultras -- are growing faster than shorter-dated treasuries. Bottom line is, while others have created look-alike products of our benchmarks, we've created new rates products which are generating revenue, and serve as important tools for our customers.

- FX ADV was down, primarily due to government intervention in Japan and Switzerland, and uncertainty related to the Euro. CME Group's emerging market currencies, which have been a major focus area, were up 20 percent year-over-year. Our total FX open interest exceeded the all-time record set in June 2007, nine times in March. Most importantly, March marked the all-time high in CME Group value traded relative to the current FX market leader – EBS, with CME Group reaching approximately 96 percent of the EBS volume.

- Within equities, open interest has jumped 18 percent from year-end 2011. While down, volumes in our equity products outperformed the other most actively traded index futures products around the world. Volatility was low during the quarter, with the VIX averaging 18 relative to 30 in Q4 2011. So, within financial products at CME, we are performing well relative to our peers.

- We have been quite active in terms of innovation in our agricultural product area. We recently announced the launch of CBOT Black Sea Wheat

Futures to begin trading on June 6th, subject to regulatory approval. This is an important next step for CME Group as it relates to our new market development efforts in Eastern Europe. In addition, along with the Minneapolis Grain Exchange, we launched MGEX-CBOT Wheat Spread Options.

- Within metals, similar to some of the financial products, we have seen a pickup in open interest, primarily gold which was up 10 percent compared to the end of 2011. We have seen continued growth in metals volumes traded during non US hours, which has jumped from 21 percent of electronic volume in Q1 of 2009 to 27 percent in Q1 2012. Of note in metals, copper trading has increased significantly so far in 2012, with the most pronounced pick-up occurring in electronic activity during Asian trading hours. Average daily volume for copper products increased more than 40 percent versus Q1 2011, and now represents more than 15 percent of our metals volume. Interest in copper has been driven by the supply/demand picture, as well as an interest in trading copper on the basis of economic growth in Asia, as China has become the world's largest consumer of this metal.

- In addition, we also added to our OTC offering by announcing the April 30th launch of Aluminum Swap Futures based on a Platts index. Increasing industrial demand from Asia, and growing competition for resources, have led to increased price volatility in some raw materials.

- Within energy, the main driver of the quarter was strength in natural gas, and we had an all-time high in revenue on CME ClearPort. While the WTI/Brent spread widened a bit during the quarter, we believe that the reversal of the Seaway pipeline, which will be operational in May, is an initial factor which should help narrow the spread by relieving supply stocks in Cushing. Over the last month, concerns about the situation in Iran have decreased, and the spread has tightened.

- From a longer-term perspective, we increased our investment in the Dubai Mercantile Exchange from 28 percent to 50 percent. Our goal is to build this product into a third crude oil benchmark that appeals to traders in Asia. Increased trading volumes and wider acceptance of the contract should encourage producers and buyers of Middle Eastern oil to adopt it as a benchmark for long-term crude sales to Asia. We are pleased to see some very encouraging early signs with a record DME Crude electronic volume day yesterday of 13,000 contracts, as well as expecting April to be the fourth consecutive record trading month.

- Turning to the clearing area, our OTC clearing momentum has continued, as customers have utilized our multi-asset class platform well ahead of the regulatory mandate. To date, more than 1,800 buy side accounts have cleared more than $515 billion in total notional in IRS and CDS, with $283 billion cleared during Q1. In addition, the pipeline is expanding with 2,500 additional accounts currently testing with us and 15 of our intermediaries. We are viewed as the leader in D-to-C OTC clearing in the US, clearing more business in Q1 than we did in all of 2011.

- In rates swaps we now offer and clear the top seven currencies, which represent 95 percent of the vanilla interest rate swap market clearable at CME. Earlier this month we successfully added Australian Dollars, Swiss Francs and Japanese Yen. We remain focused on expanding this business globally, and plan to launch OTC interest rate swap clearing through CMECE later this year.

- We will provide portfolio margining of OTC interest rate swap positions and Eurodollar and Treasury Futures for house accounts beginning on May 7. The risk reduction achieved will result in capital efficiencies of up to 85 percent for certain portfolios, figures that remain unparalleled in the industry. We expect the same capital benefits should be available for customer accounts prior to the mandatory clearing date. Based on recent comments by the CFTC, our working assumption for the initial phase of mandatory swaps clearing is in the October/November time period for swap dealers, major swap participants and active hedge funds, while smaller banks and asset managers will potentially follow in early 2013.

- In terms of technology, we had a seamless launch of our co-location services at the end of January, which took considerable effort by our technology and operations group. Based on strong demand, we expect to open the second phase of the facility for customers in the second quarter of 2013. We will give more clarity on the additional revenue opportunity later this year.

- Shifting to our global efforts, in terms of Q1 trading volume, we continue to see faster growth from customers outside the US. Our overall electronic volume in Q1 was up 3 percent sequentially, with US volume up 2 percent, while volume from Asia and Europe each jumped 10 percent. We have made significant headway with educational efforts particularly in Asia, and as we mentioned last quarter, we have a healthy pipeline of new Asian intermediaries, which we plan to leverage.

- During the quarter, we signed on with the Bank of China to explore and collaborate in a long-term business relationship that will harness the strengths of both organizations to provide mutual benefits as both parties grow their global businesses. These efforts include commercial banking and collateral management activities with BOCI's Hong Kong, London and U.S. branches as well as potential product offerings.

- We also further expanded our relationship with BM&FBOVESPA by implementing a cross-listing and cross-licensing agreement. Under the arrangement, the IBOVESPA, the main Brazilian stock index, will be listed and cleared by CME Group as U.S. dollar denominated IBOVESPA futures. BVMF will launch U.S. dollar denominated S&P 500 Index futures to be settled in Brazilian real, along with soybean and WTI futures.

- In summary, it was a busy first quarter for us, and we continue to execute on our plans to position the company for the long-term in an efficient way. Looking out a few quarters and into next year, we expect much of the uncertainty related to Dodd-Frank to be mostly behind us. We expect our OTC, globalization and non transaction related opportunities to continue to take flight. We are optimistic the U.S. economy will continue to progress in the right direction, which should bode well for our product set and the confidence of a cautious trading community.

- 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, and then I'll talk a little bit about our focus on efficiency from a financial perspective.

- Let me start with revenue – while average daily volume jumped 5 percent compared to the fourth quarter, ADV was down 11 percent versus the same quarter a year ago, when we posted exceptionally strong quarterly average daily volume due to the impact of significant unrest in the Middle East and the natural disaster in Japan at that time.

- The rate per contract for the first quarter was 81.1 cents, which was up slightly from the first quarter last year and the same as the RPC in Q4. Looking at the sequential comparison, various mix related items offset each other. Product mix was slightly positive to the rate, and that was offset by a negative venue mix and member-non/member mix, as member volumes grew faster than non-member volumes.

- In terms of non volume-related revenue, we saw a 12 percent increase from the fourth quarter, driven by an increase in market data revenue, and the addition of co-location which launched at the end of January. Total co-lo-related revenue during Q1 was $9.7 million, offset slightly by decreases in other connectivity offerings as customers migrated to co-lo. This revenue is found in the access and communication fees line.

- Total expense was $323 million, up about $4 million compared with the fourth quarter, excluding the MF Global items from last year.

- Starting with Compensation and Benefits expense, this line item was $135 million, following the typical higher first-quarter seasonal pattern due to a jump in the FICA and vacation accrual areas, along with our merit and promotion increases for employees which typically hit in February. These three areas accounted for an increase of $11.4 million from the fourth quarter. In addition, due to the 12 percent increase in the equity market in Q1, we booked $4.1 million in deferred compensation expense, which is offset in investment income, and was $2 million more than Q4. For modeling purposes, typically every 3 percent change up or down in quarterly equity market value will drive about $1 million of expense in this category.

- We saw a reduction in headcount during Q1 of approximately 35 positions, from 2,737 to 2,702. During the quarter, we incurred approximately $3 million of severance expense as we reorganized certain functions. In total, the seasonal accruals, deferred compensation and severance-related costs resulted in a $15 million increase from the 4th quarter.

- In addition, we announced internally that we will be offering a voluntary exit incentive plan to a select group of employees, and we will likely provide some detail on this next quarter. At this point it is difficult to quantify based on the uncertainty of acceptance and the potential to backfill some of the positions.

- Lastly, we are currently in the process of opening an office in Northern Ireland, which is initially focused on certain technology functions we are augmenting overseas. Our plan is to initially hire between 80 and 90 employees there, which will eventually allow us to reduce consulting costs.

- In terms of non-compensation expense, in Q1 we recorded $190 million, compared to $203 million in Q4, and $185 million in Q1 of 2011. Some specific items to focus on there -- we spent approximately $3 million during the first quarter on the index joint venture with S&P, down a bit from the fourth quarter. We also had the strongest ClearPort quarter in our history, with approximately $83 million of revenue, which increased the ClearPort rebates by $2.4 million sequentially. This is reflected in the license fee line. In addition, co-lo was operational in February and resulted in an incremental $1.3 million related to depreciation, utilities and maintenance from Q4.

- Turning to non operating income, last year during the first quarter, we received dividends totaling $17 million, which included $2.7 million from an investment in IMAREX, and $14 million from BVMF.   This year we received a $6.6 million dividend from BVMF, which is paid at the discretion of the board.

- Our tax rate came in at 38.6 percent, which included a one-time favorable adjustment. We expect our effective tax rate to come in at 41 percent for the remainder of the year, which represents the lower end of our original guidance for 2011.

- Turning to the balance sheet, we had $1.1 billion of cash and marketable securities at the end of March, following the $147 million regular quarterly dividend and the $200 million annual variable dividend, both paid in March. You may have seen the news earlier this week about our sale of the CBOT building. The total sales price was approximately $151.5 million, and based on using some capital losses associated with other portions of our business, we expect to retain more than $145 million of the proceeds.

- Capital expenditures, net of leasehold improvement allowances, totaled $30 million in the first quarter. For 2012, our CAPEX expectations are in the $140 to $150 million range.

- A couple final comments on expenses. For the remainder of the year, the sale of the CBOT building will reduce expenses by approximately $15 million, with a similar amount of revenue eliminated. We expect second quarter expenses to drop by approximately $10 million from the first quarter driven primarily by a reduction in compensation and building-related costs. Lastly, we expect to close the Dow/S&P transaction during the third quarter, and we will provide additional clarity on the impacts for this and the voluntary exit program next quarter.

- In summary, we are very focused on being as efficient as we can to maximize our results, while also investing in long-term growth areas like co-location, globalization and OTC clearing.

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