

## **Q110 Earnings Call Prepared Remarks**

### **April 29, 2010**

#### **John**

Thank you for joining us. Craig Donohue, our CEO, Terry Duffy, our Executive Chairman, and Jamie Parisi, our CFO, will spend a few minutes outlining the highlights of the first quarter and then we will open up the call for your questions. Also joining us for participation in the Q&A session are Phupinder Gill, our President; Bryan Durkin, our Chief Operating Officer; Kim Taylor, President of CME Clearing; Laurent Paulhac, Managing Director OTC Products and Services; and Rick Redding, Managing Director Products and Services Initiatives. Some of our folks are in New York and some are in Chicago.

Before they begin, I'll read the safe harbor language. Statements made on this call, and in the accompanying slides on our Web site, 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. More detailed information about factors that may affect our performance may be found in our filings with the SEC, including our most recent Forms 10-K and 10-Q, which are available in the Investor Relations section of the CME Group Web site.

Now, I would like to turn the call over to Craig.

## Craig

- ◆ Thank you for joining us.
  
- ◆ I'm pleased to be speaking to you today from a very different place, both in the macroeconomic sense and from CME's perspective, than we found ourselves during last year's first-quarter earnings call.
  
- ◆ To begin with, first-quarter volumes tell a positive and compelling story, with 12 percent growth in average daily volume and a 24 percent increase in open interest since Q109. With the exception of Equities, exchange-traded volumes by asset class are up by double digit percentages from first quarter last year. April ADV of 11.6 million contracts is strong, and up from the first quarter. This is notable, as April has traditionally been one of the slowest months for us the last few years.
  - Interest rates were up 33 percent in Q1, and this month's volume is up 64 percent compared to last April.
    - Recognizing that Q109 was an extremely depressed volume environment for Interest Rates, we are pleased with these growth percentages but continue to look toward potential indicators of ongoing growth.
  
    - To that end, we continue to believe that the growing inventory of Treasuries will need to be hedged in a more volatile interest rate environment. The expectation for treasury issuance this year is \$2.3 trillion, up 7 percent from \$2.1 trillion in 2009.
  
    - In addition, the Federal Reserve officially ended its \$1.25

trillion program to purchase mortgage-backed securities, a plan that was one of the single largest initiatives ever undertaken by the federal government to support the U.S. economy. In terms of trading activity, the Fed's participation in this market restrained hedging and futures trading, as they acted to keep the mortgage market range bound, thereby suppressing the need to hedge.

- Additionally, Eurodollars have historically been used to express opinions about future Fed activity, and expectations are for a more active Fed once the zero interest rate policy draws to a close. CME Group's Fed Funds Futures are currently reflecting a 34 percent probability of a rate hike at the September FOMC meeting, a 52 percent probability of an increase at the November meeting and a 68 percent probability by the December meeting.
- As we have mentioned before, we have seen the depth of our central limit order book significantly expand in many product areas, and our average bid/ask spread has tightened, particularly in interest rates, since the credit crisis. Slide 8 shows the growing liquidity available in our treasury and Eurodollar market, along with other products. The recently announced interest rate offerings from other exchanges and consortiums have captured some headlines. However, our focus has been, and will continue to be, fostering liquidity in our markets, which supports customer trading, helps us attract new customers and reduces overall trading costs.

- Equities have been challenged in the first quarter by the weight of decreasing volatility, a slow upward rise in equity values and difficult comparables in Q109. Low volatility has impacted the cash equities market, and other futures products such as the EuroStoxx and FTSE. However, we have had 2 days over the last few weeks, including this Wednesday, when equity volumes exceeded 4.5 million contracts, so as equity markets become less range bound, we would expect the volume to rise as well.
  
- In addition, we're very pleased with the success we've had increasing the volume and revenue contributions from other asset classes.
  - The FX asset class had a record revenue quarter and energy and metals were near peak from a revenue perspective. Taken together, revenue from these three asset classes was up 18 percent from Q109. Trends in these products during the month of April continue to show strength with volume up 45 percent compared with April last year.
  
- ◆ I would now like to provide you with an update on our globalization strategy as this past quarter has been a very active period for us, with a number of significant accomplishments. Our globalization strategy is primarily oriented to expanding our core businesses, and building deep liquidity in our products 24 hours a day. We have a multi-pronged effort which includes expanding our own global sales efforts and technology distribution, and by also partnering with leading exchanges in markets where we see high growth potential. The partnerships allow us to accelerate our market penetration, expand our customer reach and develop our product sales channels with local brokers. Nearly all of our

products are global benchmarks that have universal appeal to customers, both domestically and internationally.

- ◆ We are selectively adding sales and marketing staff in the EMEA, Latin American and Asian markets. Including CMA, we now have 50 sales and marketing, and business development employees outside the U.S. contributing to our strong progress and future growth potential in these areas.
- ◆ In the first quarter, we enhanced the liquidity and volume in our core products and markets during non-U.S. trading hours in order to better serve our European and Asian customers, which you can see on Slide 10. Volumes on CME Globex during these periods grew 58 percent compared to Q1 '09, with volume during European hours up 55 percent and during Asian hours 75 percent higher.
- ◆ Another way we measure our progress is to look at volume processed through our 8 international telecommunications hubs. These low-cost/high reliability services continue to generate excellent results in our core business. Volume through these hubs represented 12 percent of our overall electronic volume in Q1, up from 10 percent in Q1 of 2009, and the hub volumes grew 35 percent versus the prior year - faster than our overall volume growth rate.
- ◆ We are focusing on core growth in global markets because we fundamentally believe that Asia, Latin America and other emerging markets will experience superior economic and financial markets growth over the next decade, compared with the more mature North American and

European markets. Slide 11 shows expected GDP growth in countries around the world between now and 2020.

- ◆ As I mentioned, our approach also includes launching or partnering with premier exchanges to launch more foreign products on the CME Globex platform that are attractive to our international customers. In recent months, we have been very active and successful in expanding the range of foreign products to be traded on or accessed through the CME Globex platform, including:
  - 5 of the world's most actively traded equity futures contracts – the Brazilian iBovespa, the Korean Kospi 200, the Indian Nifty 50, the Mexican IPC index futures contracts, and trading hours extension on our already successful Japanese Nikkei 225 contract
  - 2 of the world's most actively traded interest rate products – the Brazilian overnight interest rate contract and Mexican bond futures (TIIA and Cetes)
  - All of the Malaysian and Dubai derivatives products, including the benchmark crude palm oil and Oman Sour Crude contracts
  
- ◆ Our efforts to globalize our business are in an early stage, but we are encouraged by our progress to date, reflected in both the current volume numbers and the quality of the firms with which we have partnered. Based on our track record of helping our partners prosper, we believe we are well positioned to maximize the revenue generated from the trading of the entire suite of CME Group products.

- ◆ In conclusion, volume and open interest in all of our business segments, with the exception of equities, is considerably stronger than a year ago, with double digit growth from year-ago levels. Second, we continue to focus intently on growing our core businesses through expanding distribution, global client acquisition, new product development and further enhancing the technology and clearing services we provide our clients. Finally, we believe that Financial Services Regulatory Reform will likely serve as a positive catalyst for both our core business results, as well as our growth initiatives in OTC clearing services, and I will now turn it over to Terry to discuss recent developments in this area.

## Terry

- ◆ Thanks Craig.

I would like to update you on the most recent developments with Regulatory Reform. In general, the focus continues to be consumer protection and increasing transparency and safety and soundness in OTC derivatives markets. Our transparent and regulated exchange markets continue to be the model that market users and policy makers are looking to in crafting new legislation.

The following is an overview of the House and Senate derivatives provisions. Of course, the legislative process is not yet final, and these provisions, as well as others, could be changed as the process continues. With respect to futures markets, the current draft bills generally provide for limited changes:

- ◆ First, the House Bill requires the CFTC to establish position limits for

physical commodities and limits exemptions to pure commercial hedgers. It also requires that the CFTC's position limits apply simultaneously to OTC participants and foreign boards of trade. The Senate version requires the CFTC to establish aggregate position limits across markets for contracts based on the same underlying commodity, but preserves the authority of exchanges and swap execution facilities to establish position limits that are not higher than the maximum limits set by the CFTC. The Senate version does not limit hedge exemptions to commercial hedgers. Apart from the draft bills, the CFTC has already proposed a position limits regime for energy markets. We continue to oppose position limits on US futures markets until such time as the Commission has imposed similar requirements on foreign boards of trade, exempt commercial markets and OTC market participants.

◆ Second, both the House and Senate versions propose extensive changes for the OTC markets.

- All swaps listed for clearing by a clearing house would be required to be cleared, as well as traded on exchanges or swap execution facilities pursuant to CFTC rules and procedures. The Senate bill would extend this requirement to foreign exchange swaps.

- Both the House and Senate bills include exemptions for end users. The House bill provides an automatic exemption for legitimate hedging by parties that are not swap dealers or major swap participants. The Senate version is more limited, applying only to commercial end users hedging their own commercial risks.

- The Senate language provides that in the case of cleared swaps between either swap dealers or major swap participants, and financial entities, the

financial entity has the sole right to select the clearing house at which the swap will be cleared. The House bill does not include such a provision.

- Similarly, the Senate version provides that, even where a swap is not required to be cleared, a financial entity or end user counterparty to such swap can elect to have the swap cleared and has the sole right to select the clearing house at which the swap will be cleared. The House bill does not include this provision.

- Both the House and Senate language require that clearing houses must provide for “open access” and non-discriminatory clearing of a swap executed on an unaffiliated platform. Unlike the House bill, the Senate version stipulates that a clearing house is not required to clear any swap that adversely affects its business operations or financial position, or which could pose systemic risk to the clearing house.

- The Senate language requires banks to spin off swap dealing activities or forego Federal protections such as deposit insurance or access to the Fed discount window. The House bill does not include such a requirement.

- The Senate language prohibits Federal assistance to swap dealers, major swap participants or exchanges and clearing houses. This provision is counter to the Senate Banking Committee language reported in March that grants clearinghouses the ability to seek loans from the Federal Reserve. The House Bill does not preclude the Federal Reserve from providing assistance to clearinghouses or exchanges.

- Under both the House and Senate versions, swap dealers and major swap participants will be subject to registration, record-keeping and reporting

rules, as well as capital and margin requirements. Finally, customized, non-standardized swaps would not be subject to the mandatory clearing requirement but would be subject to higher capital requirements.

- ◆ While we have urged lawmakers to adopt capital and other incentives to encourage the adoption of central counterparty clearing systems for OTC derivatives versus mandatory requirements, we nevertheless believe the draft legislation will be a positive catalyst for our various OTC clearing services initiatives in interest rate swaps, OTC FX and CDS.

- ◆ We believe that our demonstrable expertise in clearing, our strong financial safeguards system, and our substantial portfolio and cross-margining capabilities, make us well positioned to work with swap market participants to develop clearing services that meet their needs as the OTC business evolves.

- ◆ I will now turn the call over to Jamie to discuss our financial results.

## Jamie

- ◆ Thank you Terry.
  
- ◆ CME Group turned in a strong first quarter financial performance, as average daily volume climbed to 11.5 million contracts per day, up from the 10.1 to 10.3 million ADV range we experienced in each quarter last year, and up 12 percent compared to the first quarter 2009. We generated \$693 million in revenue, and operating expenses were up 5 percent sequentially. This resulted in \$415 million of operating income and diluted earnings per share of \$3.62.
  
- ◆ Since we completed the NYMEX integration in the fourth quarter last year, we are no longer providing proforma comparisons. Rather, this quarter we will provide our results on a GAAP basis only, and explain any unusual items which are included. First-quarter 2010 results did include \$6 million in non-operating income for the recovery of a bankruptcy claim and a \$6 million reduction in certain tax reserves, offset primarily by \$10 million of professional fees related to establishing the company's joint venture with Dow Jones. These three items increased net income by less than \$2 million. Additionally, first-quarter 2010 figures include the results of Dow Jones Indexes beginning March 19<sup>th</sup>, and there is a new line in the Income Statement and Balance Sheet related to The Dow Jones Inc. minority interest in the CME Group Index Services business.
  
- ◆ Turning to customer segmentation, we made some enhancements to the data we provided last year by adding in the NYMEX user data, and allocating the "other member" total more precisely to other categories including individual members, hedge funds, etc. We also now show a new category, which is the

volume from corporate participants for those we can track, with the remainder of these types of users falling in with the rest of the nonmember customer category. Slide 15 shows this new break down going back to the second quarter of 2009, which is as far back as the NYMEX data is available on a comparable basis. Sequentially, we saw an increase in bank/dealer and buy-side prop firm volume, while the individual member percentage decreased.

- ◆ The overall pro forma rate per contract for all CME Group volume decreased 2 percent to 82.1 cents, compared with 83.9 cents in the first quarter 2009, primarily due to an increase in our lower priced interest rate contracts to 44 percent of total volume from 37 percent a year ago.
- ◆ Sequentially, the rate per contract decreased 2.8 cents from 84.9 cents to 82.1 cents also due to product mix shifts. We experienced higher volume from our lower priced interest rate and currency contracts and a smaller percentage of volume originating from the ClearPort products. Additionally, the proportion of contracts traded by members increased slightly from Q4 2009 to Q1 2010.
- ◆ Some of you may have noticed the decrease in our rolling 3-month RPC from February to March. This was driven primarily by a higher mix of member trades in the month of March versus the month of December, as member trading grew at 23 percent and non-member trading grew at 9 percent between these two periods.
- ◆ Market data revenue of \$88 million for the quarter was up 7 percent sequentially, driven by our price increase, and slightly offset by lower professional screen counts. At the end of the first quarter, users subscribed to 386,000 base devices across CME, CBOT and NYMEX, down 10 percent versus Q1 of last year, and down 3 percent sequentially. We had a

professional screen fee increase from \$55 to \$61 per month beginning in January of 2010. In addition, we booked \$1.1 million in this category related to the Dow business during the first quarter.

- ◆ I'll now take a few minutes to review expenses.
- ◆ Total operating expenses were \$279 million for Q1, which included \$10 million in professional fees this quarter for banker and legal fees related to negotiating and closing the Dow Jones transaction.
- ◆ Drilling into Q1 expenses, compensation and benefits was \$98.8 million, up \$9.8 million from the prior quarter. This increase was due primarily to higher base comp and benefits resulting from a \$7 million sequential increase in vacation accrual and FICA expenses, and \$1 million related to merit and promotion increases. Our combined headcount at the end of Q1 stood at 2,415, an increase of 25 people since the beginning of the year, plus the impact of 130 related to the Dow Jones transaction. We expect to add more resources in the coming year to support our core and non-core growth initiatives.
- ◆ Our first quarter bonus expense was \$13 million, basically in line with the target 2010 annual bonus guidance we gave of \$54 million.
- ◆ Non-compensation expenses totaled \$180 million, or \$170 million excluding the Dow transaction related expense I mentioned earlier. Excluding the Dow, this is roughly flat versus Q409.
- ◆ Q1 operating income was \$415 million, the high water mark since Q3 of 2008. During the first quarter, our operating margin was 60 percent, or more than 61 percent excluding the Dow transaction related expenses.

- ◆ In the non-operating income and expense category, on the investment income line, we received a \$9.4 million dividend from BM&F/BOVESPA. Also, interest expense increased due to the \$612.5 million of additional debt we incurred for the Dow transaction. The normalized interest expense, including the Dow related debt, is expected to trend from \$38 million in Q2 to \$34 million in Q4 as we plan to pay down \$300 million of debt due in August. The detail related to our debt structure is available on Slide 18. In addition, as I mentioned earlier, during Q1, we had a \$6 million gain from a settlement related to a currency hedge we had with Lehman.
- ◆ During the quarter we repurchased 935,000 shares of CME stock totaling \$282 million at an average price of \$301.25. As part of our announced transaction with BM&F/BOVESPA, which Craig spoke about earlier, we plan to issue them 2.2 million shares at the close of the transaction following regulatory approval, which we expect in the June/July timeframe.
- ◆ For the quarter, our effective tax rate was 39.8 percent, which was lower than normal due to a favorable adjustment of \$6 million related to the deductibility of merger costs related to the CBOT transaction. For the full year 2010, we expect an effective rate of between 41 and 42 percent.
- ◆ Capital expenditures, net of leasehold improvement allowances, totaled \$26 million in the first quarter, driven primarily by hardware and software attributed to migration of trading systems to our new data center as well as continued build out in our office facilities.
- ◆ Since we provided our previous expense guidance of \$1.1 billion of full year 2010 expense, we have completed the Dow transaction, which added \$10 million of transaction related expense, plus approximately \$21 million in terms of 2010 operating expenses. For modeling purposes, the ongoing quarterly

net impact on expenses related to Dow is \$7 million, with increases spread primarily across compensation, amortization and professional fees and a reduction in license fees.

- ◆ In addition, our share of the multi asset class trading platform we are building with BM&F/BOVESPA is expected to result in \$10 million of expense in 2010, which will likely be offset in revenue from our partner. So, with the addition of these recently announced transactions, we now expect full year expense of \$1.13 to \$1.14 billion.
  
- ◆ In summary, we started the year by posting a strong improvement in our top line and bottom line results, relative to a challenging environment in 2009. So far in April, we are averaging 11.6 million contracts per day up 24 percent, despite counting Good Friday as a trading day with 3.3 million contracts traded that day. Excluding that day, our average daily volume is up more than 30 percent in April versus the prior year.
  
- ◆ We will now open up the call for your questions, but, in order to get to everyone, we are limiting all of you to one question and one follow up, and then please feel free to get back in the queue if time permits.

*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. 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 and implementation of the enhanced functionality required by our customers; 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; our ability to adjust our fixed costs and expenses if our revenues decline; our ability to generate revenues from our processing services; our ability to maintain existing customers, develop strategic relationships and attract new customers; our ability to expand and offer our products in foreign jurisdictions; changes in domestic and foreign regulations; changes in government policy, including policies relating to common or directed clearing and changes as a result of legislation stemming from the recent financial crisis, including the proposed regulatory reform of the over-the-counter derivatives and futures market and any changes in the regulation of our industry with respect to speculative trading in commodity interests and derivative contracts; the costs associated with protecting our intellectual property rights and our ability to operate our business without violating the intellectual property rights of others; our ability to generate revenue from our market data that may be reduced or eliminated by the growth of electronic trading, the state of the overall economy or declines in subscriptions; 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 financial safeguards package to adequately protect us from the credit risks of clearing members; the ability of our compliance and risk management methods to effectively monitor and manage our risks; changes in price levels and volatility in the derivatives markets and in underlying fixed income, equity, foreign exchange and commodities markets; economic, political and market conditions, including the recent volatility of the capital and credit markets and the impact of current economic conditions on the trading activity of our current and potential customers; our ability to accommodate increases in trading volume and order transaction traffic without failure or degradation of performance of our systems; our ability to execute our growth strategy and maintain our growth effectively; our ability to manage the risks and control the costs associated with our acquisition, investment and alliance strategy; 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 on futures and options on futures transactions and/or the repeal of the 60/40 tax treatment of such transactions; the unfavorable resolution of material legal proceedings and the seasonality of the futures business. More detailed information about factors that may affect our performance may be found in our filings with the Securities and Exchange Commission, including our most recent periodic reports filed on Form 10-K and Form 10-Q, which are available in the Investor Relations section of the CME Group Web site. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise.*