

## **Q411 Earnings Call Prepared Remarks**

### **February 2, 2012**

- ◆ Thank you for joining us today on the CME Group fourth-quarter earnings call.
- ◆ I am going to highlight CME Group's 2011 accomplishments and then share some thoughts about 2012. Afterwards, Jamie will review our Q4 financial results.
- ◆ Overall, 2011 results were strong, despite a challenging backdrop. 2011 volume averaged a record 13.4 million contracts per day, up 10 percent from 2010. Highlights for the year included record annual average daily volume for our FX, commodity, energy and metals product lines, as well as double-digit average daily volume growth in our interest rate, equity index, commodity and metals product lines.
- ◆ Fourth-quarter volume averaged 11.7 million contracts per day, down 2 percent from Q4 2010, but included 24 percent average daily volume growth in equity index products and 8 percent growth in energy products.
- ◆ During the year we increased global market share relative to our top three competitors. On the short end of the interest rate curve, despite the continued zero interest rate policy, our Eurodollar volumes increased by 9 percent while Liffe's Euribor volumes were essentially flat. On the long end, our Treasury product volumes grew by 13 percent, outpacing Eurex's interest rates volumes, which grew at 10 percent. Our commodity product volumes were also quite strong during the year.

- ◆ After an extremely robust third quarter, we saw decreased volumes and open interest in November and December due to the Euro zone crisis, the failure of MF Global and normal seasonal patterns. Nevertheless, we have seen a strong rebound in open interest since the beginning of this year. You may recall that open interest peaked on September 14<sup>th</sup> at 103 million contracts and that open interest declined by 14 percent, from 91 million contracts to 78 million contracts, between Q3 and Q4 of last year. However, open interest has now increased by 11 percent to 87 million contracts, since the beginning of the year, with growth in all 6 product areas.
- ◆ While macroeconomic conditions in 2011 were challenging, many believe that the U.S. economy is poised for a much better year in 2012. There are increasing signs that the zero interest rate policy of the Federal Reserve is finally getting some traction. Most segments of the economy, including consumers, corporations, and state and local governments, appear to have completed their adjustments to the post-2008 reality of less leverage and more modest income expectations. Moreover, the economy is learning to live with greater policy and regulatory ambiguity. All of this suggests that the U.S. economy could realize better than expected real GDP growth in 2012 despite existing headwinds.
- ◆ While we cannot control macroeconomic influences, I would like to highlight that we made excellent progress in 2011 in executing all three components of our global growth strategy. First, we have continued to successfully drive increased core business growth from our non U.S. customers and to increase volumes and revenues from Europe, Asia and Latin America. Second, we have significantly increased our exposure to non-transaction fee based revenue streams. These include our successfully launched co-location

services on January 30<sup>th</sup>, and our Dow Jones index services business which we plan to combine with the S&P index services business. Third, we have made excellent progress in expanding CME ClearPort, launching CME Clearing Europe and continuing our substantial progress in clearing interest rate and clearing default swaps. Let me briefly discuss each area.

### **Global Growth**

- ◆ In 2011, we reached record levels of non-U.S. electronic trading revenues estimated at more than \$550 million. Additionally, 2011 volumes during non-U.S. hours grew by 16 percent compared to 11 percent during U.S. trading hours. We are driving this growth through new global product offerings, increased sales staffing in Europe, Asia and Latin America, and by attracting new international clearing member firms.
- ◆ Looking forward, we expect continued higher growth in non-U.S. hour's volumes and revenues. We have completed our restructuring of our Products and Services Division and now have all of our key leaders in place in each business line, in our global sales function and in our Europe and Asia offices. Each of these new leaders is developing business plans in those regions to accelerate our growth and expand revenues from those regions. Within Asia, one of many areas that we are currently focusing on, there are increasing signs that China is beginning to open up and we are working with three new intermediaries who will be able to accommodate the trading activity of other Chinese FCMs. In addition, we recently announced an agreement with Mysteel, China's leading provider of ferrous price and indexing services, to develop risk management products for the ferrous metals industry based on Mysteel's market-leading price data services.

## **Index Services and Co-location**

- ◆ Our Dow Jones Index Services business contributed \$91 million in revenue in 2011, and grew at more than 20 percent year over year. Pending regulatory approvals, our new agreement with McGraw Hill will give CME Group a 24 percent ownership interest in the combined business. This will further strengthen our position in index services and index products and allow us to continue to be innovative with product development and co-branding across asset classes. We are looking forward to completing this transaction as soon as reasonably practicable.
- ◆ We are also pleased to announce that we went live with our co-location services offering this past weekend, which will enable us to generate \$40 - \$45 million in new revenues in 2012. Initially, there will be more than 100 firms housed in the facility and more have expressed interest to join. Based on strong customer demand, we anticipate starting to build the next phase of the facility in the second half of 2012 to expand capacity and to enable us to ultimately reach our goal of \$100 million in annual revenues from this new business.

## **OTC Clearing**

- ◆ Our existing OTC clearing offerings have also gained significant traction. January ClearPort volume is up 27 percent since January 2011, with particularly strong growth in natural gas.
- ◆ In May 2011, we launched CME Clearing Europe and we have made steady

progress. We now have more than 130 clients and brokers connected through CME ClearPort, with 13 more clearing firms in the pipeline. Through CMECE, we are clearing more than 170 different energy, commodity, metal and freight contracts and we continue to expand the range of products that are eligible for clearing. In January 2012, we experienced a significant increase in cleared volumes, clearing approximately 75 percent of the activity that was cleared for the entire year in 2011. We believe these volume and open interest trends are evidence of non-U.S. customer demand for clearing CME products in Europe. Next steps for CMECE in 2012 include additional metals contracts, the launch of interest rate swaps and cross-margining with CME Clearing U.S.

- ◆ Turning to cleared interest rate and credit default swaps, we continue to make very good progress. Since inception, we have now cleared more than \$247 billion of interest rate and credit default swaps transactions, \$209 billion in IRS and \$38 billion in CDS. We now have more than 1,300 customer accounts with open positions and several thousand additional accounts actively testing with us. Our diverse client base includes asset managers, hedge funds, regional banks, government sponsored enterprises, and insurance companies. In addition, in January of this year we started to charge for OTC clearing and the fee schedule can be found on our web site.
- ◆ The European crisis and overall market conditions have been a catalyst for customers to reduce counterparty credit risks through CME Clearing – well ahead of the implementation of the swaps clearing mandate. The firms who have been early adopters at CME Clearing are viewed by their clients as market leaders, and they're using this as a selling point to their clients. The catalyst has shifted from government rulemaking to internal firm mandates to reduce counterparty credit risk and make central counterparty clearing as

efficient as possible.

- ◆ We are working closely with our clients to meet their expanding needs by broadening our product offering in OTC clearing. In Q4 last year, we successfully launched interest rate swaps in Eurodollars, British Pounds and Canadian Dollars, and we are targeting the launch of interest rate swaps in Australian Dollars, Swiss Francs and Japanese Yen in April of this year. At that point, we will be making 95 percent of the plain vanilla interest rate swap market clearable at CME. As an example of our success in introducing new products, we have cleared more than €58B in Euro-denominated interest rate swaps since launching them on October 17<sup>th</sup>.
  
- ◆ Finally, before wrapping up, I thought I would spend a few minutes on the Fed's recent announcement to extend its guidance that the federal funds rate will remain at exceptionally low levels through 2014, as compared to the previous time-frame of mid-2013. The data provided by the Fed about diverging opinions on timing certainly will only heighten interest in economic data. When additional signs of an improving economy emerge, then the debate about the timing of the next Fed move should intensify. We expect that debate to eventually be a catalyst for significant hedging and trading activity, as existing exposures will be adjusted along the entire yield curve. Fortunately, the market will hedge the risk of rising rates well before the Fed actually moves. If more optimistic real GDP forecasts prove correct, the FOMC will see a substantially improved economy by early 2013 and the debate over whether to accelerate the normalization of monetary policy could erupt in the second half of 2012. Rate volatility will follow economic data and relate to the FOMC debate, not the actual timing of the rate rise.

- ◆ Having greater transparency from the FOMC, including yearly federal funds rate projections, is not likely to significantly impact rate volatility over time. Indeed, if anything, the increased transparency may allow for a better tracking of the degree of dissension within the FOMC, and that could lead to heightened volatility around times in which the FOMC appears to be divided over critical policy issues.
- ◆ I would like to reiterate that we remain intently focused on what we can control, which positions CME Group to maximize the amount of free cash flow we can generate no matter what is happening from a macro perspective. This was evident by the results of a very productive 2011, which I highlighted earlier. As Jamie will touch on, we will remain disciplined on discretionary spending, and we also intend to return excess cash to shareholders. We are determined to remain as efficient as we can to successfully guide the CME Group through 2012 and beyond.
- ◆ Last, I'd like to discuss two additional announcements that we have made this morning.
- ◆ The first is related to our dividend policy, which Jamie will cover in more detail in a moment.
- ◆ The second is a \$100 million dollar Family Farmer and Rancher Protection Fund that CME Group announced as one step to restore the confidence of market users following the collapse of MF Global, particularly those farmers and ranchers who hedge agricultural risks in CME Group markets. In addition, we will continue to work with the rest of industry, including the National Futures Association, the Futures Industry Association, our fellow exchanges, FCMs

and customers, to determine what additional safeguards will best serve the interests of all market users and strengthen protection of customer funds at the firm level.

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



## Jamie

- ◆ Thank you Craig and good morning everyone.
- ◆ In 2011, we generated approximately \$3.3 billion of revenue, up approximately 9 percent versus the prior year, while our operating income was up 11 percent, and we saw a 1 percent increase in our operating margin to 62 percent. These results exclude the impacts of MF Global in 2011, the \$20.5M investment write-down related to CMA in Q2 of 2010, and the non-cash deferred tax impacts that impacted both years, some of which I will touch on later in my remarks. Turning to the fourth quarter, at a high level, the notable items impacting our results included a slowdown in trading activity due to the factors that Craig mentioned earlier, a non-cash deferred tax adjustment, which had a positive impact on EPS of \$7.97; and like many of our customers, we were negatively impacted by the MF Global situation. We realized a \$30 million decrease in operating income related to MF Global, made up of a \$3.2 million reduction in rental revenue, and a \$27 million increase in expenses, related primarily to a write-down of MF receivables. These impacts are non-recurring in nature. Excluding the deferred tax benefit and the MF Global impact, our EPS would have been \$3.55.
- ◆ The rate per contract for the quarter was 81.1 cents, similar to a year ago, but up 4 percent compared to the third quarter. The main drivers of the sequential increase in the overall rate were a greater proportion of higher-priced commodity products during Q4, and to a smaller degree, the member-non member and venue mixes were each slightly positive.
- ◆ It is worth noting that as of January <sup>1st</sup>, we have begun charging OTC clearing fees for Interest Rate Swaps and Credit Default Swaps. The overall blended rate for IRS, which is priced based on tenor, will eventually be approximately

\$5 to \$6 per million of notional value cleared, and \$7 to \$8 per million for CDS.

- ◆ Turning to Compensation and Benefits expense, this line item was \$116 million, down from last quarter and a year ago. We saw a decrease in our bonus driven primarily by lower volumes and the negative impact of the additional MF Global expenses. Our stock-based compensation increased due to the timing of our annual grant, which occurs in mid September. While we increased headcount during the year, and as of December, our total global headcount stood at 2,737; this was basically flat relative to the prior quarter. Lastly, the Compensation line is down approximately \$4 million vs. Q3 due primarily to an unfavorable variance in earnings on deferred compensation balances which is offset dollar for dollar in the investment income line.
- ◆ Last quarter, we gave full-year expense guidance of \$1.23 to \$1.235 billion, with expected increases in stock-based compensation, marketing and professional fees, potentially higher deferred comp balances impacting compensation, and lastly, higher professional fees. Excluding only the MF Global-related impacts, our total expenses for Q4 would have been \$319 million, and the full year would have been within the range we provided. Additionally, included in the Q4 expense was approximately \$5.3 million related to the joint venture with McGraw Hill. Offsetting that expense was a decrease in our bonus and the license fees based on lower volume in Q4.
- ◆ I'd like to now turn to expense guidance for the full year 2012. In 2010, our expense growth was approximately 12.5 percent following a significant cost reduction program we had instituted in 2009 during the credit crisis. Coming into 2011, based on many growth initiatives, we started the year with guidance of 9.4 percent, and we ended at approximately 7 percent for the

year with a focus on continuing to invest in growth, including areas like OTC and co-location, while also being as efficient as possible on the discretionary side. At our analyst day in October, we mentioned we intend to drive long-term expense growth below 5 percent.

- ◆ Today, I'd like to give you a range of expenses based on volume assumptions to assist you in modeling the year. If ADV growth were to come in close to 10 percent, we would expect expense growth to be in a range of 4 to 5 percent, and if volume were up between 0 and 3 percent, we would expect expense growth of 2 to 3 percent.
- ◆ In 2012, we expect our non-compensation expenses to be basically flat compared to 2011, with the main wildcard being our license fees. Turning to compensation, in 2012, we expect headcount growth to decrease significantly from the average 10 percent growth we experienced over each of the last 2 years.
- ◆ With non-compensation expense basically flat and minimal growth in our headcount, the vast majority of the 2012 expense increase levels I just outlined will be due to the full year impact of the 170 employees we hired last year, normal cost of living increases for our employees, and the full year impact of co-location expense.
- ◆ This expense guidance is based on our current business heading into 2012, and excludes impacts from the expected sale of the CBOT building and the closing of the joint venture with McGraw Hill, both of which we expect to complete during the first half of this year. The CBOT building and CMA are basically break even businesses, so their divestiture should increase our efficiency from an income statement and balance sheet perspective.

- ◆ Also looking ahead, we expect our effective tax rate in 2012 to be between 41 and 41.5 percent, going as low as 39.5% in 2013
- ◆ Capital expenditures, net of leasehold improvement allowances, totaled \$39 million in the fourth quarter and \$156 million for the year. For 2012, our CAPEX expectations are in the \$140 to \$150 million range. This includes current plans to begin preparation for phase 2 of our co-location build out, which we expect to start during the second half of this year. We continue to see very strong interest and positive trends in terms of more firms utilizing our facility.
- ◆ We did not repurchase any shares of CME Group stock in Q4. For virtually the entire quarter, we had a self imposed trading blackout due to Q3 and Q4 earnings, the MF Global situation, and the Dow and S&P transaction announced at the beginning of November.
- ◆ We have been fairly transparent that we intend to return excess cash to our shareholders and in support of this, CME Group's board of directors has taken two steps this week. Yesterday, they authorized an increase in our regular quarterly dividend to \$2.23 per share, which is up 59 percent compared to the 2011 dividend. At the current stock price level, that would represent a dividend yield in excess of 3.6 percent. We believe a strong and growing dividend will attract additional dividend-oriented shareholders to what we believe is an exceptional business model that is not capital intensive, and highly cash-generative.
- ◆ Our board also approved an additional annual, variable dividend of \$200 million or \$3.00 per share this year, payable along with the first quarter's regular dividend of \$2.23. Going forward, we expect this variable dividend will be considered in the first quarter of each year and will supplement the regular

dividend. The amount of the annual variable dividend will be determined after the end of each year, and the level will increase or decrease from year to year based on excess cash on hand and will be impacted by operating results, potential M&A activity, and other forms of capital return including regular dividends and share buybacks during the prior year. Both dividends, totaling \$5.23 per share, will be payable on March 26, 2012, to shareholders of record as of March 9, 2012.

- ◆ In closing, I am confident in CME Group's future and am excited about the many growth opportunities we see ahead of us and what they mean in terms of long-term value creation for our shareholders.
- ◆ We will now take your questions - please limit yourselves to one question and one follow up, so we can get to everyone. Given the number of analysts on the call, please expect us to strictly enforce this rule this quarter.

*Statements in this press release 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, implementation and maintenance 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, including our ability to provide effective services to the over-the-counter market; 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 outside the United States; changes in domestic and non-U.S. regulations; changes in government policy, including policies relating to common or directed clearing and changes as a result of legislation stemming from the implementation of the Dodd-Frank Act; 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, including our ability to prevent errors and misconduct and protect our infrastructure against security breaches and misappropriation of our intellectual property assets; changes in price levels and volatility in the derivatives markets and in underlying fixed income, equity, foreign exchange, interest rate and commodities markets; economic, 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 stemming from the financial crisis that began in 2008 and any other future crises; our ability to accommodate increases in trading volume and order transaction traffic without failure or degradation of 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 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 or user fee 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.*