Tradeweb 2Q24 Earnings Conference Call Script

This transcript should be read in conjunction with the related Quarterly Report on Form 10-Q, the earnings release, and the earnings presentation, which includes important additional detail, and is provided for the convenience of investors and analysts only. For a full recording of this earnings conference call please see the 2Q24 Earnings Call webcast.

OPERATOR

Good morning and welcome to Tradeweb's second quarter 2024 earnings conference call. As a reminder, today's call is being recorded and will be available for playback.

To begin, I'll turn the call over to Head of Treasury, FP&A & Investor Relations, Ashley Serrao. Please go ahead.

PART I: INTRODUCTION AND DISCLAIMER

ASHLEY SERRAO (Slide 2-3)

Thank you and good morning.

Joining me today for the call are our CEO Billy Hult, who will review our business results and key growth initiatives and our CFO Sara Furber, who will review our financial results. We intend to use the website as a means of disclosing material, non-public information and complying with our disclosure obligations under Regulation FD.

I'd like to remind you that certain statements in this presentation and during the Q&A may relate to future events and expectations, and as such, constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Statements related to, among other things, our guidance and the ICD acquisition are forward-looking statements. Actual results may differ materially from these forward-looking statements. Information concerning factors that could cause actual results to differ from forward-looking statements is contained in our earnings release, earnings presentation and periodic reports filed with the SEC.

In addition, on today's call we will reference certain non-GAAP measures as well as certain market and industry data. Information regarding these non-GAAP measures, including reconciliations to GAAP measures, is in our earnings release and earnings presentation. Information regarding market and industry data, including sources, is in our earnings presentation.

Now, let me turn the call over to Billy.

PART II: OVERVIEW & FINANCIAL RESULTS

BILLY HULT (Slide 4-8)

Thanks, Ashley. Good morning everyone, and thank you for joining our second quarter earnings call.

This was another outstanding quarter. As central banks step back, private sector intermediation continues to be in vogue. From evolving inflation prints to snap elections across Europe and the UK, the macro debate continues to flourish globally and our one-stop solution is resonating with our clients. At our core, we are a technology company that caters to the financial services industry. We have a simple job – how can we continue to save our clients time and money and provide them with more efficient means of trading in the financial markets. Change is constant, and we are focused on being on the forefront of that change, be it technological, market structure, or behavioral. As the markets and our clients evolve, we continue to position Tradeweb for the future. After closing our acquisitions of Yieldbroker and r8fin, we are pleased to have announced the signing of an agreement to acquire ICD in April. We are on track to close ICD shortly, which will add corporates as our fourth client channel.

Diving into the second quarter, we achieved our best second quarter in our history. Specifically, strong client activity, share gains and a risk-on environment drove 30.4% yr/yr revenue growth on a reported basis. We continue to balance investing for growth and profitability as Adjusted EBITDA margins expanded by 98 basis points relative to the second quarter of 2023.

Turning to slide 5, rates and credit led the way, accounting for 61% and 29% of our revenue growth, respectively. Specifically, the rates business was driven by continued organic growth across global government bonds, swaps and mortgages and was also supplemented by the addition of r8fin and Yieldbroker. Credit was led by strong U.S. and European corporate credit, with record quarterly market share in electronic U.S. investment grade, and aided by strong growth across municipal bonds, China bonds, and credit derivatives. Money markets was led by continued growth in institutional repos. Equities posted low single-digit revenue growth despite challenging industry volumes in our core ETF business. Finally, market data revenues were driven by growth in our LSEG market data contract and proprietary data products.

Turning to slide 6—I will provide a brief update on two of our focus areas — U.S. Treasuries and ETFs and then I will dig deeper into U.S. credit and global interest rate swaps.

Starting with U.S. Treasuries—record second quarter revenues increased by 28% yr/yr led by records across all our client channels. Our institutional business saw record adoption of our streaming protocol and growing usage of our RFQ+ offering. The leading indicators of the institutional business remain strong—we gained share and achieved record quarterly market share of U.S. Treasuries versus Bloomberg, crossing the 50% threshold for the first time, which we have maintained. Client engagement was healthy with institutional average daily trades up 45% yr/yr. Automation continues to be an important theme with institutional U.S. Treasury AiEX average daily trades increasing by nearly 100% yr/yr.

Our wholesale business produced record volumes led by our streaming offering. Our other protocols also saw strong growth, particularly our CLOB which has begun to trend higher. Our recent acquisition of r8fin is off to a strong start, contributing approximately 2.3% to our overall U.S. Treasury market share complementing our CLOB and streaming protocols. The team remains focused on onboarding more CLOB liquidity providers over the coming quarters as they deliver on a holistic strategy across our wholesale protocols.

Within equities, our ETF revenues grew mid-single digits, but faced a tough industry backdrop given lower equity market volatility. Other initiatives to expand our equity brand beyond our flagship ETF franchise continue to bear fruit with second quarter convertible bond revenues increasing by 10% yr/yr. Looking ahead, the client pipeline remains strong as the benefits of our electronic solutions continue to resonate. We believe we are well-positioned to capitalize on the long-term secular ETF growth story, not just in equities, but across our fixed income business.

Global Credit

Turning to slide 7 for a closer look at another strong quarter for credit. Strong double-digit revenue growth was driven by 33% and 29% yr/yr revenue growth across U.S. and European Credit, respectively. We also achieved strong double-digit growth across munis, China Bonds, and credit derivatives. Automation continued to surge with global credit AiEX average daily trades increasing by about 45% yr/yr.

We set another fully electronic quarterly market share record in U.S. IG helped by record IG block market share of 9%. We also achieved our 2nd highest fully electronic market share in U.S. HY. Our institutional business continues to scale as clients adopt our diverse set of protocols to improve liquidity, price transparency, and efficiency. Our primary focus on growing institutional RFQ continues to pay off with ADV growing 30% yr/yr, with strong double-digit growth across both IG and HY. Moreover, portfolio trading ADV rose 100% yr/yr with IG portfolio trading reaching record levels. We continue to focus on leading with innovation, and this is resonating with our clients. We saw portfolio trading users grow by over 20% yr/yr, a record number of line items traded in the quarter, and our largest ever PT trade in excess of $3B. Retail credit revenues were up over 20% yr/yr as financial advisors continue to allocate investments towards credit to complement their buying of U.S. Treasuries and retail certificate of deposits.

AllTrade produced a solid quarter with nearly $190 billion in volume, up over 45% yr/yr. Specifically, our all-to-all volumes grew over 20% yr/yr and our dealer-RFQ offering grew over 10% yr/yr. The team continues to be focused on broadening out our network and increasing the number of responders on the AllTrade platform. In the second quarter, the average number of responses per A2A inquiry rose by 35% yr/yr. We also continue to increase our engagement and wallet share with ETF market makers. Finally, our sessions ADV grew over 60% yr/yr and produced the 2nd highest quarterly ADV ever.

Looking ahead, US credit remains our biggest focus area and we like the way we are positioned across our three client channels. We believe we have a long runway for growth with ample opportunity to innovate alongside our clients. Our strategy is focused on expanding our network, increasing our wallet share, enhancing our pre- and post-trade analytics and continuously improving our protocols and client experience. In the second quarter, we enhanced our RFQ offering with our rollout of RFQ Edge where we're already seeing over 25% of our RFQ users utilizing RFQ Edge. RFQ Edge takes the traditional RFQ list ticket and incorporates real-time trading data, charting functionality, and execution cost analysis.

We also remain very focused on chipping away at high yield, and we believe we are well positioned to replicate the success we've had in IG. Specifically, we're making progress in our Aladdin integration with the goal of improving the client experience and increasing electronification in these markets. We're still on Phase 2, which is focused on Alltrade and RFQ, but our teams are already out on the road meeting with respective clients and walking them through all the enhancements made to date. With our Aladdin integration closing a gap and providing a foundation for growth, we expect HY growth from here to be driven by the expansion of our client network led by strategic sales hires, functionality enhancements, and stronger penetration with ETF market makers.

Beyond U.S. Credit, our EM expansion efforts continue with growing adoption of our PT and RFQ offerings, and early positive signs across wholesale EM. On the product side, we are focused on leveraging our diverse product expertise, enhancing our integration with FXAll and continuing to build out functionality for multi-asset package trading.

Global Swaps

Moving to slide 8, global swaps produced record revenues driven by a combination of strong client engagement in response to the macro environment and continued market share gains. Strength here was partially offset by a 3% reduction in duration and elevated quarterly compression activity. All in, global swaps revenues grew 56% yr/yr and market share rose to 23.6% with record share across dollar, G-11 and EM-denominated currencies.

Central to our ethos is our focus on helping clients by connecting the dots across fixed income products. Given the heightened market volatility across money markets, our repo clients have been increasingly referencing swaps curves when evaluating fixed rate repo trades. Yet their process was cumbersome, and our clients asked for a better solution. During the quarter, we became the first electronic trading platform to make overnight index swap curves available during the repo trade negotiation process, helping institutional clients assess the price competitiveness of different repo rates across different currencies and maturities.

Finally, we continue to make progress across emerging markets swaps and our rapidly growing RFM protocol. Our second quarter EM swaps revenues more than doubled yr/yr, and we believe there is still significant room to grow given the low levels of electronification. Our RFM protocol saw ADV rise over 115% yr/yr with adoption picking up.

Looking ahead, we believe the long-term swaps revenue growth potential is meaningful. With the market still about 30% electronified, we believe there remains a lot we can do to help digitize our clients' manual workflows while the global fixed income markets and broader swaps market grow.

And with that, let me turn it over to Sara to discuss our financials in more detail.

SARA FURBER (Slide 9-12)

Thanks Billy and good morning.

As I go through the numbers, all comparisons will be to the prior year period, unless otherwise noted.

Slide 9 provides a summary of our quarterly earnings performance.

- As Billy recapped earlier, this quarter we saw record second quarter revenues of $405 million that were up 30.4% yr/yr on a reported basis and 30.8% on a constant currency basis. We derived approximately 38% of our 2Q revenues from international clients, and recall that ~30% of our revenue base is denominated in currencies other than dollars, predominantly in Euros.
- Our variable revenues increased by 40% and total trading revenues increased by 31%.
- Total fixed revenues related to our four major asset classes were up 4.2% on a reported and 4.5% on a constant currency basis.
    - Fixed revenue growth was primarily driven by previously disclosed dealer fee increases in Credit that were instituted at the start of the third quarter of 2023.
    - And other trading revenues were up 9%-- as a reminder, this line fluctuates as it reflects revenues tied to periodic technology enhancements performed for our retail clients.
- Year-to-date adjusted EBITDA margin of 53.6% increased by 117 bps on a reported basis when compared to the 2023 full-year margins.

Moving on to fees per million on Slide 10 and a highlight of the key trends for the quarter. You can see slide 16 of the earnings presentation for additional detail regarding our FPM performance this quarter.

- For cash rates products, fees per million were up 4%, primarily due to an increase in European and Australian government bond fees per million.
- For long tenor swaps, fees per million were down 2%, primarily due to a slight increase in compression as well as an 3% decline in duration.
- For cash credit, average fees per million decreased 12% due to a mix shift away from munis and sessions trading.
- For cash equities, average fees per million were flat due to lower US ETF fees per million given an increase in notional per share traded. Recall in the U.S., we charge per share and not for notional value traded. This was offset by a mix shift towards higher FPM EU ETFs.
- Finally, within money markets, average fees per million decreased 8% driven by a mix shift away from higher FPM U.S. CDs and towards our growing institutional repo business.

Slide 11 details our adjusted expenses

- At a high level, the scalability and variable nature of our expense base allows us to continue to invest for growth and grow margins—we have maintained a consistent philosophy here.
- Adjusted Expenses for 2Q increased 25.8% on a reported basis and 27% on a constant currency basis.
- Adjusted compensation costs increased 32.2% due to increases primarily in performance-related compensation, headcount and severance. Excluding $2.9 million related to severance, compensation costs increased 29.4%.
- Technology and communication costs increased 29.6% primarily due to our previously communicated investments in data strategy and infrastructure.
- Adjusted professional fees increased 6% mainly due to an increase in consulting costs. We expect professional fees to continue to grow over time as we spend more on technology consulting to support our organic growth.
- General and administrative costs increased due to a pickup in travel and entertainment which on a reported basis was partially offset by FX gains year on year. Favorable movements in FX resulted in a $1.7M gain in 2Q24 versus a $150k loss in 2Q23.

Slide 12 details capital management and our guidance

- On our cash position and capital return policy
    - We ended 2Q in a strong position, with $1.72 billion in cash and cash equivalents and free cash flow reached approximately $722 million for the trailing twelve months.
    - Recall we intend to pay $785 million in cash consideration for ICD once it closes.
    - Our net interest income of $21.0 million increased due to a combination of higher cash balances and interest yields. This was primarily driven by the higher interest rate environment and more efficient management of our cash.
    - With this quarter's earnings, the Board declared a quarterly dividend of $0.10 per Class A and Class B shares.
- Turning to updated guidance for 2024
    - In light of strong business momentum and the anticipated closing of ICD shortly, we are increasing our adjusted expense guidance from ~$805 million. We now expect to be in the $830-860 million range for 2024. Including the anticipated closing of ICD, we are currently trending towards the midpoint of this range, which would represent an approximate 22% increase versus our 2023 adjusted expenses. Focusing on organic growth, the midpoint of this range would represent an approximate 16% increase.
    - Bridging the gap from $805 million to the midpoint of our new range, 63% of this increase is coming from the inclusion of ICD, with 30% and 7% coming from better business momentum and recently announced management changes, respectively.

- Provided that ICD closes shortly, revenue from ICD is expected to be ~$40M over the next 5 months. Recall, we plan to invest in technology and marketing during the first 12 months post-closing which we expect may temporarily push ICD's adjusted EBITDA margin to 47%-49%.
- All in, primarily factoring in the better business momentum, we now expect our 2024 adjusted EBITDA margin expansion to slightly exceed 2023 levels.
- At the same time, we expect to capitalize on the anticipated healthy revenue environment by accelerating investments to support our current and future organic growth.
  - This includes infrastructure related investment such as further enhancements to our global credit tech stack, expanding our integration capabilities to allow for cloud-based Python integration, and retail platform enhancements to support the growth in trading activity we've seen in the past few years.
  - We are also selectively making small investments in emerging digital technology such as blockchain and digital assets in order to leverage and benefit from their technical expertise without having to make significant investment to experiment in-house.
- We now expect our capex and capitalized software development to be about $77-85 million for 2024.
- Acquisition and Refinitiv Transaction related D&A, which we adjust out due to the increase associated with pushdown accounting, is now expected to be $158 million.
- We continue to expect 2024 and 2025 revenues generated under the new master data agreement with LSEG to be ~$80M and ~$90M, respectively.

Now I'll turn it back to Billy for concluding remarks.

BILLY HULT

Thanks, Sara.

Tradeweb thrives on change and we look forward to solving complex problems. Change can happen very fast or very slowly, but we want to be that trusted partner that our clients look towards to drive innovation in the market. It's a great time to be in the risk intermediation business. I feel good about our future growth outlook.

With a couple of important month-end trading days left in July which tend to be our strongest revenue days, average daily revenue growth is trending at a high teens growth rate relative to July 2023. The diversity of our growth remains a theme. We are seeing strong volume growth across global government bonds, mortgages, interest rate swaps, corporate credit and repos. Our IG and HY share are trending above 18% and 7%, respectively, in July.

I would also like to welcome Amy Clack to the team who will be joining Tradeweb in August as Chief Administrative Officer and as a member of the Executive Committee. Amy brings more than 25 years of experience and will oversee operations, business integration risk and corporate services.

Finally, I would like to conclude my remarks by thanking our clients for their business and partnership in the quarter, and I want to thank my colleagues for their efforts that contributed to the best second quarter revenues and volumes at Tradeweb.

With that, I will turn it back to Ashley for your questions.

ASHLEY SERRAO

Thanks Billy. As a reminder, please limit yourself to one question only. Feel free to hop back in the queue and ask additional questions at the end. Operator, you can now take our first question.

THANK YOU

Ashley Serrao, CMA, CFA
Head of Treasury, FP&A & Investor Relations
Tel: 646-430-6027
Email: ashley.serrao@tradeweb.com

Sameer Murukutla, CFA
Managing Director, Investor Relations
Tel: 646-767-4864
Email: sameer.murukutla@tradeweb.com

Isha Rao
Associate, Investor Relations
Tel: 646-560-7232
Email: isha.rao@tradeweb.com