

30-Jul-2020

Intercontinental Exchange, Inc. (ICE)

Q2 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Intercontinental Exchange First (sic) [Second] (00:00:02) Quarter 2020 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. Please note that this event is being recorded.

I would now like to turn the conference over to Warren Gardiner, Vice President of Investor Relations. Please go ahead, sir.

Warren Gardiner

Vice President-Investor Relations, Intercontinental Exchange, Inc.

Good morning. ICE's second quarter 2020 earnings release and presentation can be found in the Investor section of theice.com. These items will be archived, and our call will be available for replay.

Today's call may contain forward-looking statements. These statements, which we undertake no obligation to update, represent our current judgment, and are subject to risks, assumptions, and uncertainties. For a description of the risks that could cause our results to differ materially from those described in forward-looking statements, please refer to our 2019 Form 10-K, second quarter Form 10-Q, and other filings with the SEC.

In our earnings supplement, we refer to certain non-GAAP measures, including adjusted income, EPS, operating income, operating margin, expenses, effective tax rate, and debt-to-adjusted EBITDA. We believe our non-GAAP measures are more reflective of our cash operations and core business performance. You'll find a reconciliation to

the equivalent GAAP term in the earnings materials and an explanation of why we deem this information to be meaningful, as well as how management uses these measures in our Form 10-Q.

When used on this call, net revenue refers to revenue net of transaction-based expenses and adjusted earnings refers to adjusted diluted earnings per share. Throughout this presentation unless otherwise indicated references to revenue growth is on a constant currency basis. Please see the explanatory notes on the second page of the earnings supplement for additional details regarding the definition of certain terms.

With us on the call today are Jeff Sprecher, Chairman and CEO; Scott Hill, Chief Financial Officer; and Ben Jackson, our President.

I'll now turn the call over to Scott.

Scott Anthony Hill

Chief Financial Officer, Intercontinental Exchange, Inc.

Thanks, Warren. Good morning, everyone, and thank you for joining us today. I'll begin on slide 4 with some of the key highlights from our strong second quarter results. Net revenues totaled \$1.4 billion, up 8%, driven by 13% growth in Trading and Clearing revenues and record data services revenues of \$574 million, up 4% versus last year. This solid revenue performance combined with expenses at the low end of our guidance range helped deliver second quarter adjusted earnings per share of \$1.07, up 14% over the prior year.

We returned \$564 million to shareholders during the quarter, including \$400 million through share repurchases and a nearly 10% increase in our dividend per share. Through the first half, we have returned over \$1.4 billion to shareholders through both buybacks and dividends, an increase of 31% versus last year. As I mentioned, second quarter adjusted operating expenses of \$575 million were at the low end of our guidance.

COVID-related impacts delayed IPOs, which reduced marketing spend at the NYSE. In addition, the high productivity of our technology team and reduced vacation due to COVID-related travel restrictions drove higher capitalized labor expense during the second quarter. With a strong IPO pipeline and the reopening of many communities this summer, we expect these factors to begin to reverse in the third quarter, yielding an incremental \$5 million to \$7 million in expense. We also anticipate a modest ramp in strategic investments during the quarter, all of which is expected to result in third quarter adjusted operating expense in the range of \$580 million to \$590 million.

Now, let's move to slide 5, where I'll provide an overview of the performance of our Trading and Clearing segment. Trading and Clearing revenue totaled \$710 million in the second quarter, up 13%. In our energy markets, revenues increased 9%, driven by a 26% increase in global natural gas revenues. Importantly, open interest across our energy market is up 17% year-over-year through July. Global natural gas open interest is up 30%. And despite a double digit percentage decline in WTI open interest, total oil open interest is 3% higher than a year ago.

In our ag complex, revenues decreased largely reflecting continued economic uncertainty associated with COVID. Within financials, equity index ADV rose 8%, including MSCI volumes up 15%. These higher RPC products represent only around 20% of our financials volumes, but contribute nearly half the revenue. Thus, the strong performance largely mitigated the softer interest rate activity reflective of global interest rates at or near all-time lows.

At the NYSE, trading revenues increased 37%, supported by a 61% increase in cash equity ADV and a 44% increase in equity option ADV. And finally, in our fixed income and credit businesses, revenues totaled \$111 million in the second quarter. Results were led by our Mortgage Services business, which continues to benefit from strong refinancing trends as well as continued adoption of digital mortgage solutions. Revenues from ICE Mortgage Services totaled over \$90 million through the first six months of this year, up 40% on a pro forma basis versus the prior year.

Turning now to slide 6, I'll discuss the Data and Listings segment. Second quarter data services revenues was up 4%, totaling a record \$574 million. This marks the 42nd consecutive quarter of year-over-year data services revenue growth. We expect that trend to continue based upon acceleration in ASV, which enters the third quarter up 4.5% year-over-year on a constant currency basis.

Growth in Pricing and Analytics accelerated to 5% in the second quarter from 4% in the first, driven by resilient customer demand for our pricing in reference data products as well as continued strong contribution from our fixed income index business. Desktops and Connectivity revenue grew 6%, supported by a 13% increase in capacity on our ICE Global Network. And finally, Exchange Data and Feeds grew 2% as growth in futures exchange data in our consolidated feeds business was moderated by flat revenue at the NYSE.

Looking to the second half, we expect data services revenues to accelerate sequentially to between \$575 million and \$580 million in the third quarter, and then to increase sequentially again by an additional \$7 million to \$10 million in the fourth quarter.

Moving to our Listings business, revenues totaled \$111 million in the second quarter. While revenues are largely recurring in nature, results were somewhat impacted by a slower IPO calendar towards the end of the first quarter and into May. However, with the floor of the NYSE now partially reopened, issuers are returning to market and we see a very healthy backlog heading into the remainder of the year. This should help us build on our solid performance during the first six months of 2020 when NYSE was the leader in US IPO capital raise, including 10 of the 15 largest IPOs. The NYSE was also far and away the leader in capital raise from special purpose acquisition vehicle or SPAC, which are increasingly being chosen as an alternative path to the public markets.

The second quarter was one of the strongest in our company's history. We once again grew the top line. Our data revenues and futures open interests continue to increase. We delivered double digit earnings per share growth. Our ROIC continues to improve and our cost of capital continues to decline. And we've returned a record \$1.4 billion to shareholders, while continuing to strategically invest in our future. We're focused on a strong finish to a record year this year and more importantly on setting ourselves up for more success in 2021.

I'll be happy to take your questions during Q&A, but for now I'll hand it to Jeff.

Jeffrey Craig Sprecher

Chairman & Chief Executive Officer, Intercontinental Exchange, Inc.

Thank you, Scott, and good morning to everyone on the call. Before I begin, I'd like to thank our customers who continue to turn to our global markets, data services and leading technology to navigate these unprecedented times. And I'd like to recognize my colleagues at ICE for their outstanding contribution to our first half results.

Now turning to slide 7, our record first half performance, which was highlighted by revenue growth of 15%, adjusted operating income growth of 19%, and adjusted earnings per share growth of 25% is a testament to our asset class diversity, balanced mix of recurring and transaction-based revenues, and ultimately the growth potential of our platform.

In our first full quarter of operating in a work-from-home environment, I'm very pleased to say that our teams responded. Driven by our multi-year investment in both information and technology, our data services business delivered a remarkably strong performance. We generated key wins with our pricing and reference data, where the quality of our end-of-day and real-time fixed income prices attracted both new customers and increased consumption from existing customers.

We saw major financial institutions adopt our new ESG and regulatory products, while in our Index business, ETF assets benchmarked to our indices reached a record \$263 billion as of the end of June.

And lastly, in our consolidated feeds business, a number of large institutions are transitioning away from competitors to ICE Data Services for their real time data needs. While our consolidated feeds business and our index business are each less than \$100 million of revenue today, they're both well-positioned to grow and capture market share, while also serving an important role in our broader enterprise sales strategy.

The second quarter was also marked by continued progress for our ETF Hub, which continues to gather a robust network of key industry participants. With the addition of Credit Suisse and Wells Fargo during the second quarter, we now have seven authorized participants active on the platform. These authorized participants in aggregate account for over two-thirds of the industry's create/redeem activity. And their commitment to our ETF Hub represents an important milestone towards adding other issuers and institutional customers in the coming quarters.

Turning to slide 8, open interest across global energy futures remains near all-time high, as we continue to benefit from long tail, secular growth trends, unfolding across the global oil, natural gas and environmental markets.

In our oil markets, commercial customers continue to demand additional, more precise hedging tools that we're in a unique position to provide, given their correlation to our benchmark contracts such as Brent crude oil. This trend is best illustrated by the growth in our other crude and refined products line item, which has seen average daily volume grow double digits on average over the last five years, and are up 37% in the first half of 2020.

The liberalization of the global natural gas markets and the rise of LNG use is driving accelerated adoption of our European TTF and Asian JKM benchmarks. Combined with average daily volumes across these contracts, they have grown in average annual rate of 55% over the last five years and increased by 80% year-over-year in the first half of 2020.

And demand for environmental products such as our European carbon credits and US renewable energy credit is also growing rapidly, with open interest across our US environmental portfolio now 4 times the size of what it was just five years ago, and recently crossing 1 million lots of open interest for the first time.

Collectively, as you can see on slide 8, this group of energy products has grown double digits on average over the last five years and now accounts for nearly a third of our total energy revenues. Along with the strength of our global crude and refined oil benchmarks, our global energy platform is uniquely positioned to continue to evolve and grow in the years to come.

Turning to slide 9, I'll now provide some additional color on Mortgage Services, which has recently become the fastest-growing business within the ICE platform. While strong refinancing volumes have provided a tailwind in the first half results, the secular shift towards the adoption of an electronic workflow is accelerating.

Today, ICE Mortgage Services is focused on helping to automate various parts of the US loan closing process. Upon a loan closing, two key events occur, first all relevant mortgage information is transmitted to MERS and registered with the MERS database. And second, in order to consummate the transaction, a settlement agent is required to record certain information with the relevant local county recorder. Together, these two events help ensure that the loan can be seamlessly sold into the secondary market. And so with the combination of MERS and Simplifile, we have a business that is part of nearly every US mortgage closing process, collecting, marshalling and storing critical data.

After acquiring MERS, we quickly engaged with Fannie Mae and Freddie Mac to digitize some of their required paper documentation, starting with the mortgage promissory note known as eNote. eNotes have seen rapid adoption over the last few quarters, and the adoption rate has only accelerated in the wake of COVID-19.

At only around 3% of the US market, there's a tremendous market share upside for this product to continue to grow. And our 2019 acquisition of Simplifile allowed us to facilitate the recording of key documents over an electronic highway that is plugged into over 2,000 jurisdictions across the United States. Importantly, this connectivity includes a database of reference data that has cataloged the various terms and conditions required by each of those 2,000 jurisdictions, as well as the fee schedules for tens of thousands of settlement agents across the country.

As you can imagine, each county has its own recording nuances and each settlement agency has its own unique fee schedule, which if navigated manually, as is often the case today, can be costly, time consuming and very prone to human error. In other words, the US mortgage back-office workflow is ripe for automation and greater efficiency.

We see the opportunity to build new products and services to add more content to what is already a robust and expansive network. We believe the addressable market for further automation is in the billions of dollars, and it's one that our platform is well-positioned to capture. We're executing a business plan that we already applied to our futures markets and are currently applying in our fixed income businesses as markets embrace digital networks to replace past workflow practices. And we're excited about the mortgage market opportunities that lie ahead and what could prove to be another important chapter in ICE's 20-year evolution.

Turning to slide 10, the first half was another example of strong execution across our platform. We delivered record revenues, record operating income and record earnings per share. We have a vision for ICE as a public company to deliver growth in all economic environments, and I think that this vision distinguishes us from our peers. We've deliberately positioned the company to have a mix of transaction and compounding subscription revenues to give investors revenue upside exposure while hedging our downside risk.

We target markets where there's a tailwind of macroeconomic analog to digital conversions taking place to smooth over microeconomic issues. We mix our footprint between financial markets, which react to Central Bank acts of man and physical markets, which react to disruptive supply chain acts of God. We diversify across our global footprint, because at all times, somewhere in the world, there are risks that our customers and potential customers need to manage.

So, as we look forward to the second half and beyond, we're excited about the growth opportunities that lie ahead. And we'll continue to work closely with our customers and our key industry participants to help them navigate these times, while creating value for all of our stakeholders.

With that, I'd like to, again, thank our customers for their business and their trust in this quarter. And I'd like to thank my colleagues at ICE for their remarkable efforts and their contributions to our first-half results.

I'll now turn the call back to our moderator, Chuck, to conduct the question-and-answer session, which will run until 9:30 Eastern time.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] And our first question will come from Rich Repetto with Piper Sandler. Please go ahead.

Richard Henry Repetto

Analyst, Piper Sandler & Co.

Q

Yeah. Good morning, Jeff, and good morning, Scott. I guess my – thank you for going through all the details on the open interest, the energy open interest. And I guess, my question was – I'm just trying to differentiate why yours – and I know you went through natural gas being very strong, but why your open interest, say, has separated from your peers? And is it – do you think I'm right when I'm saying, as of yet, it hasn't played out in volumes? And is that sort of the view that you have, but it will later or could you sort of explain that? And maybe I just don't have the right picture.

Jeffrey Craig Sprecher

Chairman & Chief Executive Officer, Intercontinental Exchange, Inc.

A

Sure. Good morning. What we've been doing over the last decade or so is really expanding the footprint of our energy's futures markets. And, obviously, we started when we acquired the International Petroleum Exchange of London that had four energy contracts and today we have over 900, approaching 1,000. And so, the growth that you're seeing is in the global markets, and it's in customers trading in these smaller niche contracts that give them more precision for hedging something locally or some product oriented to energy that is specific to their geography and business.

And that's why I mentioned in my prepared remarks, Rich, that a third of our revenues now in energy come from these other energy products, and they're the ones that are growing the fastest. They are correlated to the benchmarks, which is why it's important that we continue to market and push the main benchmarks, but the growth is in these other areas.

And when energy markets are in contango, which for non-traders means the normal market conditions, where there is storage available in the world, we have always seen that open interest in these energy products is a good precursor to future volume trends. And actually when the markets reverse and do what they call backwardate, these open interest becomes a poor metric. So, one has to use open interest cautiously. But we see the opportunity for this business to continue to grow as customers come back to these open positions and manage them through the duration of their life. So, it's a very bullish sentiment that we're using inside the company for our own forecast.

Scott Anthony Hill

Chief Financial Officer, Intercontinental Exchange, Inc.

A

Yeah. And Rich, the only thing I'd add to that is, don't get lost in the overall totals with some of the dynamics going on underneath, because a lot of what Jeff just talked about is growing right now. So, our other oil products are up

15% year-over-year in July. Our natural gas products are up 5% year-over-year in July. Our emissions products are up 21% year-over-year in July.

And you know looking at our website, those are our higher RPC contracts. And so, not only do we have the mitigation of commercials on the platform, not only do we have the mitigation of the diversity across the products, but the growth right now is a mitigation to some extent against the revenue impact that we'll see. And as you know, you can't spend volume, you can spend revenue. And that's where the cash capital returns and things like that are afforded. So, it just – I'd encourage you – the things that Jeff went through in his prepared remarks, take a look at how those businesses are performing because they're growing right through this.

Richard Henry Repetto

Analyst, Piper Sandler & Co.

Q

Got it. Got it. And great insight especially on the – you can't – the volume translating into revenue. But anyway my follow-up question, Jeff, was going to be on the ETF Hub, but I think your excitement in as you communicated and talked about Mortgage Services just sort of [indiscernible] (00:22:52) me, let's say. So, I guess the question on Mortgage Services is that it appears ripe for digitization and automation, but there is a slight difference I think from some of the markets or maybe it isn't. Maybe you can sort of draw the connection.

With the other markets that you automated, there was certainly a matching engine in the exchange and trades and a matching platform. Here, it is – maybe goes through the database management side of it but it seems like you've just got some great tools that leverage this potential for automation in this big market. But could you, I guess, give us a little bit more insight on the connection there and maybe what the differences between that and say the trading platforms that you've automated again and again?

Jeffrey Craig Sprecher

Chairman & Chief Executive Officer, Intercontinental Exchange, Inc.

A

Sure. It's a good question coming from you, Rich, because I know you and I have talked in a number of public forums about the fact that you've seen ICE really focus on the settlement process in the markets that we serve. In 2007, we moved into clearing our own futures products, and I think that was pivotal moment in the history of the company and a light went on for me and the management team and the board that we really can do something to this back-office workflow that is incredibly sticky.

So, you've now seen with the ETF Hub and the way we're approaching the fixed income markets, we entered through the back office with the reference data initially and now moving into the ETF Hub, which is a settlement essentially infrastructure. And we're using the same playbook in mortgage, which is let's get into the settlement workflow, and as I mentioned in my prepared remarks, with MERS. Right now, we touch almost all of the mortgages in the United States through what we've already built.

And once you have that settlement scheme, it's easy to expand upstream and into the data business and into adjunct markets, where that create value for customers that are very, very plugged into your network. And so, think of what we're doing as building the clearing house, if you will, for the mortgage industry.

Operator: And the next question will come from Ken Worthington of JPMorgan. Please go ahead.

Kenneth B. Worthington

Analyst, JPMorgan Securities LLC

Q

Hi good morning. Thank you for taking my questions. ASV growth improved sequentially this quarter to 4.5%. It is still at the low end of the range you set forth when you guys announced the IDC deal. Are we on the path forward to the midpoint of your range or maybe even at the higher end of the range?

The backdrop on the transition to fixed income indexation seems to be coming together quite well. You have indicated more new account wins. So, it seems like things are getting better, you indicated towards the – improving as you move through the year. So, is the outlook here – or what is the outlook here over the next couple of years for ASV growth? Should we expect it to continue to improve from these levels?

Scott Anthony Hill

Chief Financial Officer, Intercontinental Exchange, Inc.

A

Hey, Ken, it's Scott, thanks for the questions. Yeah, look, I do think we certainly expect that our ASV growth will continue to accelerate as we move through the rest of this year. And by the way, I think in addition to the total ASV accelerating from the first quarter, importantly Pricing and Analytics, which is half the business, moved from 3% in the first quarter to 4% in the second quarter and again I expect that trend to continue as we move into the back half of the year.

I've said back in February I thought Pricing and Analytics would grow 5% to 6%. I still think that's true for the year, which indicates I also think the revenue growth for Pricing and Analytics will accelerate in the back half versus the first half. And I think there are a number of trends that are really driving. And by the way, I think I'll give a shout out to Lynn and the team because they're leveraging those trends from home without traveling, without being able to go and meet customers face to face. And yet, we just had the best quarter of signings we've ever had. Lynn has told me she feels better about the pipeline entering the third quarter than she did entering the second quarter. And it goes to a lot of what Jeff was talking about. It's a flight back to quality on prices. We see customers consuming more of our prices. We see customers adding the names, adding our reference data because what we saw through the crisis is our prices were the de facto price discovery.

And in a world where you don't want tracking error, you come to ICE Data Services to buy those prices. That's what we're seeing. Our existing customers are buying more. We're seeing new customers join. Jeff talked about the index business. We now have \$263 billion indexed against our indices, our fixed income indices. We went from single digits to nearly 20% share in that space in a very short period of time. And as Jeff said, that's still not a \$100 million business for us, and it will be one.

You look at the Feeds business, where that business didn't exist when we bought IDC, five years later, it's approaching \$100 million in revenue. And there, we can compete not just on quality, but on price because we're not protecting anything. We're going after new business and we're seeing competitive wins, competitive wins against stable competitors and competitive wins against competitors that where customers aren't quite sure who owns them and who's controlling them at this point.

So, I think you're seeing all of those trends. A lot of that built up in the quarter and allowed us to do a little better than the high end of our guide. It allowed me to mention in my prepared remarks that we're going to accelerate sequentially in the third quarter and then again in the fourth quarter. And again, in a world, where our sales team is sitting at home, they're doing a fantastic job, and have allowed us to hold our guidance and to see acceleration in growth. So, you're going to see it in revenue, you're going to see in ASV. And by the way, I feel very good about how it sets us up for 2021 as well.

Kenneth B. Worthington

Analyst, JPMorgan Securities LLC

Q

Great. Thank you. And then we have some distance between the challenging April WTI delivery and negative prices for TI that resulted. Has there been any noticeable fallout? And at this point, do you think ICE might see a benefit in Brent trading from more participants switching to Brent or has that transition already happened over the last decade?

Benjamin R. Jackson

President, Intercontinental Exchange, Inc.

A

Hi, Ken, it's Ben Jackson, I'll take this one. So, the short answer to that question is, yes, there is opportunity for Brent here, and we're seeing it in a number of different areas. Jeff touched on one in some of his prepared remarks and in the first answer to Rich's question, where I think that market participants have seen now firsthand a lot of the issues that can be created by that landlocked infrastructure around WTI versus the truly global demand pool that Brent has and can service. And what that's led to is not only growth in our Brent contract itself, but also in all of the refined products that come off of a barrel of oil, all the different locations where you can make and take delivery, which is very unique on our platform, where we have those hundreds and hundreds of different locations and refined products that customers can trade that are very deep and very liquid and are high growth opportunities for us.

The other areas that we're seeing new opportunities for growth in Brent are for example in ETF space. So, we are having an unprecedented number of conversations now with ETF providers about adding Brent for the first time. Another area that we're exploring is retail demand. So, retail and in particular in Asia, we're assessing what that opportunity is, but given some of the dislocations that happened in WTI, there are markets across Asia that we're looking to expand and offer a retail offering for Brent.

And then the third, the discussions around the Gulf Coast, so as I mentioned in a Q&A in our last quarter, when oil hits the water coming out of the Gulf, its price reference is most often Brent. So, commercial customers are now engaging us more than ever around opportunities in the Gulf Coast around Houston-related benchmarks and Gulf Coast-related benchmarks because Brent, they see as the most logical benchmark to differentiate those contracts off of and create a differential market against. So, we're engaged more than ever with commercial customers around what is that right US benchmark going forward and what changes may need to be made to that. So, the short answer is, yes, there's a lot of opportunity ahead of us in Brent.

Operator: Our next question will come from Alex Kramm with UBS. Please go ahead.

Alex Kramm

Analyst, UBS Securities LLC

Q

Yeah. Hey, good morning, everyone. Just wanted to follow up on the mortgage discussion, thanks for the detail here. I saw an industry poll in the mortgage industry the other day that basically echoed what you're saying in terms of the digitization and the spending that's going there. That said, I think only 20% of that spend is going towards the closing portion. I think the majority is going to servicing and processing, and I think underwriting is a smaller part. So, first of all, do you agree with that? It was an informal poll, but then, if those other areas are getting more spending, how quickly can you expand from your base [ph] year (00:33:19) and does it have to be potentially inorganic because in terms of time to market?

Benjamin R. Jackson

President, Intercontinental Exchange, Inc.

A

Thanks, Alex. It's Ben, I'll jump in on this one. So, I think Jeff went through in his prepared remarks that focus on the closing and post-closing process. And a lot – you answered some of the question in the way that you framed

your question. In that the post-closing and closing process is the one that's the most ripe for innovation right now. It's been the most manual [ph] laid in (00:33:53) part of the entire process. And with the two assets that we have being very unique, with MERS that we've talked about a lot, and then with Simplifile, as Jeff mentioned in his prepared remarks having a very unique network, and it paved the road to all these different settlement agents in jurisdictions that no one else has and then that unique reference data set that we have puts us in a position for new growth opportunities that have a significant TAM, \$1 billion TAM across them.

And to unpack how we're executing and how to think about that growth opportunity in front of us and how huge it is and how right in front of us it is, I'll give you a couple of examples. So, first is with Simplifile, a key business being the e-record business. We've mentioned on calls that right now we're in jurisdictions and plugged into jurisdictions that represent 85% of the US population. But in those jurisdictions, if you go back to 2019, we were only capturing on our e-record business about 25% of the eligible documents that we would take a toll on, and we would get a fee on.

You go to the first – accelerate to the first six months of this year and that has accelerated to 35%. So, we've gone from 25% to 35% capture of what was manual and paper-based documentation to now automated.

A second example that we've talked about is eNotes and Jeff mentioned this in his prepared remarks that we're doing about 3% of the MERS volume is now – so when somebody is registering a mortgage, about 3% of those loans also include the registration of an eNote. If you go back to last year, that was 1%. So, we're seeing a nice pick-up in acceleration there. In addition to that, we're adding customers and have added customers like Ginnie Mae, Chase, Rocket, US Bank onto this platform, which gives us good visibility into a tailwind that will continue to grow that percentage.

A third area of growth that we haven't talked about is a business that Simplifile really built organically by itself as a startup business. And that's the automation of the closing and post-close process. Think of this as very complementary to what I just discussed that MERS has an eNotes. And this is the automation of all the other elements of the closing and post-close process. That business has gone from a startup to now if you use MERS volumes as a proxy, during the first six months of this year, has captured about 3% of that market, and we see similar to the eNote trend, we're seeing adoption pick up, customers – significant customers onboarding onto that. And we have a very big TAM ahead of us there.

The last thing I'd highlight is that while we have a bunch of other opportunities for growth in this market, the other thing to look at is there's a very strong refi trend in the market, where each one of the services that we provide in every refinance that's done, we're collecting a transaction fee associated to each of those transactions. And if you look at where mortgage rates are now, there's an estimation from industry estimates that about [ph] 18.5 million (00:37:13) outstanding mortgages are in the money at current rates. And in the money means they're 75 basis points lower than where rates are currently set. So, we see ahead of us a significant refinancing boom that's going to last for quite some time and with the Central Bank action that has happened, it's likely to continue in the years ahead.

Operator: Our next question will come from Brian Bedell with Deutsche Bank. Please go ahead.

Brian Bedell

Analyst, Deutsche Bank Securities, Inc.



Great. Thanks. Good morning. Thanks for taking my questions. Maybe that's a good segue, Ben, into my question on fixed income and credit broadly. Obviously, the mortgage side of that has fantastic tailwinds. Can you talk about the revenues efforts within fixed income trading and tell me if this is accurate, it sounds like you've got

faster near-term growth trends on the mortgage side, and we have a little bit of a longer term build on the fixed income trading side, but maybe if you can flush how you see the revenue in that area growing in the second half and then into next year? I think ETF Hub obviously has got great momentum but I believe – correct me if I'm wrong, but I believe you're not charging much for that right now, and there's more of a cross-sell game plan on that. So, maybe if you could just [ph] flush that part (00:38:39) out of that?

Benjamin R. Jackson

President, Intercontinental Exchange, Inc.

A

Sure. Thanks, Brian. So, I think the way you characterize that is correct in terms of revenue. So, with mortgage, we obviously have had and have in front of us near, medium and long term a significant TAM to go after. We're very well positioned to capture it, and we're capturing it actively now.

In fixed income, as I've said on the last few quarterly calls, what our play here has been on execution is to really establish a network for the first time, an institutional network, leveraging the strength that we have in our ICE Data Services business that has that institutional network, plugging into very inefficient workflows that are in the fixed income marketplace and then combining our execution venues, our capabilities on the ICE Data Services side and plugging into these workflow inefficiencies to solve real world problems.

And the first example of that, as we've talked about on calls of the ETF Hub and we gave a lot of great updates last quarter, so a couple of things to look at in terms of network expansion and also volume expansion on that, that we've achieved this past quarter, is that we've added our first three market makers onto the platform. So, significant market makers like Jane Street, Old Mission and Chicago Trading are now on the platform.

Jeff mentioned in his remarks, we had two more APs, significant ones in Credit Suisse and Wells Fargo that have joined the other five that are on the platforms. We've added a new issuer as a development partner on the advisory committee in JPMorgan Asset Management. We continue to enhance our workflow automation capabilities in the custom basket facilitation or the ability to customize what are the securities that I can provide to somebody to swap for an ETF in that primary trading vehicle. And last but not least, volumes growing, so quarter-over-quarter, our volume continues to grow in our primary trading venue. And we've done now over \$330 billion in transactions since inception.

What's ahead of us and getting to your question around execution, one of the key things ahead of us is I had mentioned on our last call that we just launched ICE Select. And ICE Select is our aggregation venue of all of our protocols, all of our venues, as well as our rich ICE Data Services, data sets and analytics like best execution and real-time pricing. We've integrated all that into an aggregation venue that, in the coming weeks, is going to be integrated into the ETF Hub. So, for the first time, our venues will compete in the secondary market for flow to fulfill orders and procurement of bonds versus voice and other venues. And with the \$330 billion that we've executed to-date in the primary market, that's a meaningful portion of the market that's out there for us to get started in.

Also ahead of us is really introducing for the first time, our chat and instant messaging platform that's very well established in the energy and commodities markets and introducing that for the first time into the fixed income markets. And late this year, we'll have international ETFs added on top of that. We will be in the latter part of this second half of this year, we will also start to share and publish on a regular basis volumes as our institutional network is starting to be established.

Scott Anthony Hill

Chief Financial Officer, Intercontinental Exchange, Inc.

A

And Brian, the only thing I'd tag onto that, because it gets overlooked a little bit is we've got a CDS business that did \$100 million of revenue in the first half of the year, which is 20% higher than it was a year ago, on track to be a \$200 million business. So, that's another fact similar to my answer to Rich that I hope people don't miss, because in a world, where people are looking to hedge their credit exposures, they can do it with the bonds themselves, but they're also turning more and more to CDS. And we've built – to Jeff's point earlier about building clearing solutions and backend solutions that facilitate risk management, we did that in that CDS clearing business, and its performance through the first six months has been outstanding.

Operator: Our next question will come from Alex Blostein with Goldman Sachs. Please go ahead.

Sheriq Sumar

Analyst, Goldman Sachs & Co. LLC

Q

Hi. This is Shერიq filling in for Alex. You issued some long-term debt in this quarter. Can you talk about the rationale for building up a little extra dry powder? And is there an opportunity to accelerate the share repurchase on the back of higher cash balances now?

Scott Anthony Hill

Chief Financial Officer, Intercontinental Exchange, Inc.

A

Yeah. So, look, we did – we have some bonds that were coming due later this year. And we also had through some of the M&A activity that we've done a rather accelerate – or higher balance in CP. Looking at the debt markets and looking at the interest rates that were available, we thought it was a good time to move into the market and to term some of the CP out and to go ahead and take out the bonds.

If you look, we actually – those bonds that were due in December of 2020 were actually going to cost us more from a coupon standpoint than the blended money we got that averages out at 20 years maturity. So, our blended cost on what we raised is a weighted average maturity of 20 years and a cost of about 2.5% to 2.6%. That was lower than what we're paying on bonds that were due at the end of the year.

So, we felt that was an opportune moment to move. Reducing the CP creates a little bit of flexibility for us in terms of the revolver capacity that we have. And in the uncertain period that we're in, having some additional flexibility is good and it was a relatively inexpensive ask to go out and get it.

In terms of the repurchases, what you saw in the quarter is we were steady. We said originally \$2.4 billion authorization from the board, roughly cover six quarters, that's about \$400 million a quarter, that's what we did this quarter. Did a little bit more in the first quarter when the share price was a little bit beaten down. And given where we sit today, that was a good move. So, I would again – as is typically my answer over the last few years, it's steady as she goes on capital returns.

We continue to grow our profitability. We continue to grow our capital returns. We continue to grow our dividend, and we'll continue to look that – look to do that and we will continue to look to the debt markets opportunistically to continue. As I mentioned again in my prepared remarks, another thing I want people to make sure that [ph] you note is (00:45:24), our return on invested capital is now back at 10%, and our weighted average cost of debt is now about 5.5%. So, the overall balance sheet management has reduced our cost even as the business has generated increasing returns.

Operator: And our next question will come from Mike Carrier with Bank of America. Please go ahead.

Michael Carrier*Analyst, Bank of America Merrill Lynch*

Q

Hi, good morning. Thanks for taking the questions. You guys have been making good traction and you just talk a lot about some of the newer areas at ICE, including the ETF Hub, mortgages. Ben, I think you mentioned a large [indiscernible] (00:46:03), just how you're thinking about that longer-term revenue opportunity? What maybe slice is ICE focused on? And given the potential pace of traction that you're seeing, it seems like you're a little bit faster than you would have expected. How do you see that maybe playing out relative to the expectations? Thanks.

Benjamin R. Jackson*President, Intercontinental Exchange, Inc.*

A

Thanks, Mike. Similar to the answer I gave in a question a couple ago that Alex had. I think the way to think about it is that the real near-term revenue growth opportunities that are right in front of us that we're already capturing is really in that Mortgage Services business and how well-positioned we are for the automation of that close and post-close process that especially with COVID, the assets that we have went from nice-to-have assets to absolute must-have assets. And we are onboarding customers at an unprecedented rate into our platforms for the registration of eNotes, for getting on to Simplifile, to plug into those more jurisdictions coming onboard, more agents coming onboard and looking to rapidly, rapidly onboard on to these products and increasing adoption.

And as I mentioned, there is right in front of us three to four significant growth opportunities that we're capitalizing on in terms of new business opportunities that we're capturing in that Mortgage Services business.

For fixed income, we're establishing that network. It takes a while to get established into that institutional space for execution. And all of the data points that I've been talking about on each of these calls, how fast we're getting this platform up, the volume that's coming through the platform, how much of our network is already established, and as the network gets established, it really feeds on itself. So, we think we're very well positioned there for a medium to long-term growth opportunity in execution.

Well, remember, in fixed income, we don't look at it as just an execution business, what – to solve the real problems in fixed income, it's going to require that \$1 billion business a year that we have in fixed income that's really the cornerstone is our Pricing, our Analytics business and marrying those rich analytics and pricing services with execution and partnering with buy-side and sell-side clients to plug into real inefficient workflows because we're well-positioned and that we're the only one that has really that comprehensive all of the assets there to help solve them.

Operator: Our next question will come from Kyle Voigt with KBW. Please go ahead.

Kyle Voigt*Analyst, Keefe, Bruyette & Woods, Inc.*

Q

Hi, good morning. Maybe a question on M&A, you highlighted in your prepared remarks the diversity in your business. Just wondering where are you still seeing holes or where you're seeing more opportunities to add to your broader portfolio still, whether that's in mortgage or consumer [ph] through back (00:49:20) or elsewhere. And then maybe also an update on what you're seeing in the current M&A environment in terms of more or less opportunities say versus a year ago? Thank you.

Jeffrey Craig Sprecher*Chairman & Chief Executive Officer, Intercontinental Exchange, Inc.*

A

Sure. Well, I think it's a complicated environment. I had a very interesting conversation with one of the senior investment bankers in our space about the difficulty in two CEOs meeting and getting to know each other and determining if their businesses would be good together in a world where we're working from home and can't travel and can't have face to face conversation.

And so, the M&A market as a result of that is much more about – that we're seeing is much more about companies, particularly private equity-owned companies that are going to run a process for their sale or merger. And in those kinds of situations, we tend to be the most disciplined investor. Scott mentioned we track our return on invested capital. We track our cost of capital. And so, while it's easy to make M&A – relatively easy to make M&A accretive due to the low interest rate environment that we're in, it's harder to make rational deals that have real long-term value creation for investors as opposed to giving our investors their money back and letting them make their own choices in the market. So it's complicated.

That said, there are a lot of private equity-owned businesses, so we've participated in, boy, a number of different – took a look at a number of different processes in the last quarter, and obviously not done anything or we would have announced it. But I'm also seeing that COVID-19 environment has really created winners and losers in many spaces, including financial services. We have a lot of inquiries from fintech type companies that are worried about their future funding capabilities. These generally are companies that are loss-making companies and dealt themselves to try to get scale in a world where there was a lot of capital freely floating around, and now investors seem to be more disciplined. And these companies are looking for larger sponsors, if you will, to bolt their businesses to. Again because we're disciplined investors and target things like accretion, dilution, return on invested capital, those deals are hard for us on a just purely financial basis.

So, we're only looking at things where we think those acquisitions would accelerate an initiative that we already are working on and it's essentially a buy versus build strategy or speed the market strategy. And those things are floating around. But again – and we've looked at a lot, but not seen anything that really would move the needle for us.

So, long story short, we're in a very good position. We've got access to capital. We've got a lot of initiatives going on. Our productivity is high because a lot of what we talked about on this call is about building technology and systems to help our customers and interestingly a tech-focused firm can do well in this environment because our people are actually being pretty productive working from home. So, we're in a great position if the right thing were to come along. But it's a complicated environment for M&A just due to the social distancing that's going on.

Operator: And our next question will come from Owen Lau with Oppenheimer. Please go ahead.

Owen Lau

Analyst, Oppenheimer & Co., Inc.

Q

Good morning, and thank you for taking my questions. Could you please give us more color on the progress of your partnership with MSCI? For example, the integration of ICE pricing and reference data into MSCI platform and also the progress of launching more futures contracts based on MSCI index? Thanks.

Benjamin R. Jackson

President, Intercontinental Exchange, Inc.

A

Thank you for the question, this is Ben, Owen. Our partnership with MSCI is very strong. It's been a longstanding relationship that we continue to look for opportunities to grow and we're going to continue to engage with them actively on a number of different indices in a number of different futures that we can launch around the world. So,

it's obviously been a very strong growth business for us for a long time with the futures in that business. We've seen a little bit in recent times with the volatility and the risk that there is in the market, we've seen a bit of a pullback on things like emerging markets where when you're in a high-risk environment, people tend to pull back from the markets when you have that kind of volatility in it. But we've seen a 15% increase in Q2 in this business and a lot of that is on the back of the [ph] EFA (00:55:03) business, which is another significant contract that we have. So, we're looking with them actively, partnering with them on all kinds of new growth opportunities and the state of the relationship is very strong.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Jeff Sprecher for any closing remarks. Please go ahead.

Jeffrey Craig Sprecher

Chairman & Chief Executive Officer, Intercontinental Exchange, Inc.

Well, thank you, Chuck, for moderating the call, and I want to thank everybody for joining us. We'll look forward to speaking with you again soon, and till that happens, I hope that you and your loved ones stay safe and healthy and that you guys try to have a good day. Thank you.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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