Corrected Transcript

04-Feb-2021

Intercontinental Exchange, Inc. (ICE)

Q4 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Kate, and I will be your conference operator today. At this time, I would like to welcome everyone to the Intercontinental Exchange Fourth Quarter Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Please note, this event is being recorded.

Mr. Gardiner, you may begin your conference.

Warren Gardiner

Vice President-Investor Relations, Intercontinental Exchange, Inc.

Good morning. ICE's fourth quarter 2020 earnings release and presentation can be found in the Investors 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 2020 Form 10-K and other filings with the SEC.

In our earnings supplement, we refer to certain non-GAAP measures including pro-forma revenues, 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-K.

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 are 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 key highlights from 2020 and a summary of our strong fourth quarter results. Earnings per share of $4.51 were up 16% year-over-year on record revenues of over $6 billion. Free cash flow totaled a record $2.4 billion, and we returned nearly $2 billion to shareholders through buybacks and dividends.

We also used some of that cash and our strong credit profile to make the important strategic acquisition of Ellie Mae in September, an acquisition that was nearly 3% accretive to our full-year 2020 earnings per share. Our fourth quarter results were an exclamation point on a great year. Our earnings per share totaled $1.13, up 19% year-over-year. Net revenues totaled approximately $1.7 billion, a 14% increase on a pro forma basis.

While we've now transitioned to new segment reporting, I'll mention that fourth quarter data services revenues totaled $595 million, which was at the high end of our guidance range and up 6% year-over-year. For the full year, despite the challenges brought on by the pandemic, our data sales teams focused on serving our customers, deliver data services revenues that grew 5% over the prior year, and were near the top of our guidance entering the year.

Fourth quarter adjusted operating expenses totaled $712 million. We were above the high end of our guidance, largely driven by lower levels of capitalized labor as our technology teams, who delivered near flawless execution, while largely working from home for most of 2020, took some well-deserved vacation to recharge from an extraordinary year.

Now let's move to slide 5, where I'll provide an overview of the performance of our Exchange segment. Fourth quarter revenues totaled $871 million, up 6% year-over-year. Transaction revenues increased 7%, driven by 6% growth in our Energy business and 21% growth in cash equities and options trading.

Importantly, through the end of January, our Energy Open Interest, which we believe is the best indicator of long-term growth, was up 4% versus a year ago, including 11% growth in our global natural gas business and 5% growth in our environmental complex.

Recurring revenues, which include our exchange data and listing services, increased 3% year-over-year. These results were driven by the NYSE share of strong year-over-year growth in industry SIP revenues. Looking to the first quarter, we expect recurring revenues in the Exchange segment to be between $310 million and $315 million.

Turning now to slide 6, I'll discuss our fixed income and data services segment. Fourth quarter revenues for the segment grew 3% year-over-year, while transaction revenues declined 16%, recurring revenues, which account for nearly 90% of total segment revenues grew 6% year-over-year.

Fixed income data and analytics, which includes our leading pricing and reference data and index business increased by 7%, an acceleration from 6% growth in the third quarter. Other data and network services grew 5% in the fourth quarter, driven by continued growth in customer demand for both ICE Global Network and consolidated feeds.

Looking to 2021, we expect recurring revenues in this segment to grow 5% to 6% on a constant currency basis for the full year, including $395 million to $400 million in the first quarter. These expectations are supported by ASV growth of 5.7% exiting 2020.

Please flip to slide 7, where I'll discuss the results in our Mortgage Technology segment. Please note that my comments on revenue growth are on a pro forma basis. Mortgage Technology revenues grew 65% year-over-year in the fourth quarter and 56% for the full year.

Fourth quarter transaction revenues increased 92% year-over-year. Favorable financing conditions, accelerating millennial homeownership trends, and demand for digital workflow tools, such as our Network, Closing Solutions, and analytics all contributed to our strong results.

Recurring revenues increased 29% versus the prior year as increased utilization and new customer adoption of both our Origination Technology and Analytics continue to expand our subscription base. We expect recurring revenues in the first quarter to range between $122 million and $127 million, representing around 30% growth versus last year on a pro forma basis.

I'll conclude my remarks on slide 8 with some additional guidance. We expect 2021 adjusted operating expenses to be in the range of $2.83 billion to $2.88 billion. We expect the spinout of Bakkt to reduce expenses versus last year by $50 million. And as I mentioned on the last earnings call, we expect roughly $20 million of additional D&A expense in our Mortgage segment.

In addition, we plan to invest $25 million to $30 million to enhance our Mortgage Technology platforms to support the significant growth in customers and volumes that we've seen over the past few years, and which we expect to continue.

With those items roughly netting out, our year-over-year expense growth will be largely consistent with prior years, including investments in our people and tied to revenue growth. We expect compensation expense across ICE to increase by $40 million to $50 million.

Expenses tied to revenue growth are expected to increase $15 million to $25 million, and FX, based on current spot rates, will add $10 million to $15 million, which will be more than offset by a positive impact to revenues. For the first quarter, we expect adjusted operating expenses to be in the range of $720 million to $730 million, including roughly $23 million related to Bakkt.

In summary, we delivered a very strong finish to another record year. We once again grew revenues, operating income, free cash flow, and earnings per share. We grew our dividend and returned nearly $2 billion to our shareholders. At the same time, we invested in our business to meet the needs of our customers, while also expanding our Mortgage Technology network through the acquisition of Ellie Mae. As a result, we've set the stage for continued top and bottom line growth and enhance shareholder returns into 2021 and beyond.

I'll be happy to take your questions during Q&A, but for now, I'll hand it to Ben to discuss some additional business highlights and key growth initiatives.

Benjamin R. Jackson

President, Intercontinental Exchange, Inc.

Thank you, Scott, and good morning to everyone on the call. Please turn to slide 9, where I'll begin with some of the highlights and key initiatives across our Global Energy business. While inflation, economic growth, and geopolitics will always influence volume trends in a particular quarter or year, we are focusing on investing in the structural growth opportunities that exist across global energy markets.

Investments that have been critical to the 7% average annual revenue growth we have generated across our energy and environmental network over the last five years. In our oil markets, we soon plan to launch ICE Futures Abu Dhabi, or IFAD. This is a launch in partnership with the Abu Dhabi National Oil Company, or ADNOC, and nine of the world's largest energy trading firms.

For the first time, this new Exchange will offer Futures on Murban crude oil, an important price benchmark for crude flowing through to Asia. And by leveraging the existing breadth of our energy network, we will launch an array of related differentials, cracks, and intercommodity spreads against our Brent, WTI, Gasoil, and Naphtha benchmarks.

In our natural gas markets, the demand centers of Europe and Asia are increasingly at the forefront of global price formation. We began investing in the globalization of gas markets over a decade ago, at a time when exchange-traded volume in our TTF contract was less than 10% of total trading activity.

Today, exchange-traded volume is approaching 50%, with open interest in TTF, growing at an average annual rate of nearly 40% since 2015. This growing network also plays an important role in the growth of our global environmental markets, where the number of market participants has grown by 40% since 2017, as customers increasingly seek solutions to help navigate the long tail and the complex evolution of global energy markets.

Turning to slide 10, ICE Mortgage Technology is at the center of an analog-to-digital conversion, as customers demand greater workflow automation. In addition, an acceleration of millennial home buying and attractive refinancing conditions continue to provide a tailwind to our robust results. Pro forma Mortgage Technology revenues totaled $1.2 billion in 2020, ahead of the high-end of the range we expected for all of 2021 when we announced the acquisition of Ellie Mae back in August.

As we execute against this $10 billion addressable market, our approach has been and will be similar to the blueprint we apply across our other networks. We will invest behind secular growth, both organically and through acquisition, by adding new tools and content to enhance the value proposition of our network.

As a recent example, during the fourth quarter, we launched our credit analyzer. A product that leverages our artificial intelligence engine, or AIQ, to reduce the time it takes to perform a credit review by up to 80%. In 2021, we plan to begin rolling out new eClose solutions, an initiative that we believe has a $1 billion addressable market. And we continue to see strong customer uptake across our network and our data and analytics offerings as we execute our strategy of relieving the pain points and inefficiencies that exist across the workflow.

Turning to slide 11, our proprietary price evaluation serve as the cornerstone of a network that is uniquely positioned to capture growth opportunities across the fixed income ecosystem. As an example, we are a leading solutions provider to the fixed income ETF industry, which, as many of you know, has seen assets under management grow at an average annual rate of 25% over the last 5 years.

Our decades-long position as a leading provider of price information and reference data has served as the foundation for what is today the second largest provider of fixed income indices globally. While critical, our price information and our indices are only a part of what we offer to this growing industry.

In late 2019, we launched our ETF Hub, a network we designed to reduce the workflow inefficiencies that exist within the ETF create/redeem process. Late last year, we integrated ICE Chat, a platform that we acquired in 2008 and have since grown to over 100,000 users. We also linked ETF Hub to our ICE Fixed Income Select platform, providing access to our fixed income data and analytics, as well as seamless connectivity to our trading venues.

As a leading provider of these proprietary data services, we have also developed an expertise in the gathering and cleansing of unstructured data, essentially, a skill in building the databases that serve as the foundation for developing actionable insights and identifying opportunities, not only in the fixed income markets, but across many other asset classes as well.

This is an expertise we are leveraging through new product development, such as our suite of ESG data services and some early mortgage data initiatives, which will leverage our growing Mortgage Technology network. This also applies to new partnerships, such as our announcement to apply our data services expertise to ADP's unstructured workforce data to help bring additional insights into the municipal bond markets.

As we move into 2021, we are excited about the many opportunities for growth that lie ahead, opportunities that we're able to capture because of the investments we've made in the past and the strategic investments we will continue to make across our networks into the future.

With that, I'll turn the call over to Jeff.

Jeffrey Craig Sprecher

Chairman and Chief Executive Officer, Intercontinental Exchange; Chairman, New York Stock Exchange, Intercontinental Exchange, Inc.

Thank you, Ben, and thank you all for joining us this morning. Please turn to slide 12.

Over two years ago and in collaboration with Starbucks and Microsoft, among others, we seeded a venture within ICE called Bakkt. Our vision was to leverage our collective core competencies to build a regulated ecosystem that would support the full life cycle of a digital asset. And, through efficiency gains and greater transparency, a platform that would have strong network effects within a nascent, but rapidly growing asset class.

Since launching Bakkt in 2018, we've applied our blueprint. We've invested in organic product development by building a consumer wallet and launching futures and options contracts. And we've made inorganic investments by purchasing Bridge2 Solutions and adding digital custody services.

In January, Bakkt announced that it will merge with a SPAC, managed by Victory Park Capital. The transaction valued Bakkt at an enterprise value of approximately $2.1 billion, of which we will retain a 65% economic interest. Our decision to merge Bakkt was threefold. First, the combination will provide significant incremental capital, enabling Bakkt to maximize its future growth potential.

Second, by listing as a public company on the New York Stock Exchange, Bakkt will benefit from elevated consumer brand recognition. And third, we believe this transaction will unlock value for ICE shareholders. Value that we believe was not fully recognized within the ICE share price. And as you've often heard us say, I believe one of the most important parts of my job and the job of the management team here at ICE is to leverage our infrastructure and our expertise to create value for our shareholders.

In that vein, and shifting to what was another successful year, 2020 marked our 15th consecutive year of record adjusted earnings per share, a track record of growth that began with our initial public offering on the New York Stock Exchange in 2005 and has compounded at an average annualized rate of 17% ever since.

Our strategic approach to delivering this growth and building shareholder value has been consistent since our inception. Through the application of our world-class technology, leading operating expertise, and our unique position, both as a creator and distributor of proprietary data services, we create workflow efficiencies that add transparency and that drives powerful network effects across the asset classes that we operate.

And as we've expanded into new asset classes, we've grown our addressable market, broadened our expertise and further solidified a foundation for growth well into the future.

2020 was a year of incredible global challenges. Our customers needed to find ways to protect their employees while continuing to do business as they procure and access our products. Our ICE colleagues responded with extraordinary resourcefulness to meet our customer needs. So thank you to our customers for their business and their trust, and thank you to my colleagues at ICE for their remarkable contribution to the best fourth quarter in our company's history, resulting in another consecutive record year of revenues and earnings.

With that, I'll now turn the call back to our moderator, Kate, and we'll conduct a question-and-answer session until 9:30 Eastern Time.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] The first question comes from Rich Repetto of Piper Sandler. Please go ahead.

Richard Henry Repetto
Analyst, Piper Sandler & Co.

Q

Yes. Good morning, Jeff, Scott, and Ben. Congrats on the great year. I guess the question is on the recurring revenue. Thanks for the breakout and transparency on that, Scott. So I think the exchange you said are the SIP revenues. What I didn't understand is how – what's recurring in the mortgage side? And it looks like you're about – almost half of your revenue is recurring now overall, if I have it calculated accurately.

Scott Anthony Hill
Chief Financial Officer, Intercontinental Exchange, Inc.

A

Yes, Rich, you picked up on it exactly right. We did want to continue to give transparency in our guidance on those elements of our business that are recurring and a little easier to predict in some of the volume-based business. And you're exactly right, that if you add up the total of the recurring guides, it's around midpoint $830 million of revenue, which is just less than half of the overall business.

If you look at, we've given you that detail on a pro forma basis, historically, and if you do the math on the guide in the first quarter, those recurring revenues are growing 7% to 9%. So very strong performance on a very stable part of our business right out of the gate.

Obviously, led by a strong performance in the Mortgage business, which has picked up customers, picked up volume from existing customers, but then also the data business, which, again, despite the pandemic, as I said in my remarks, sales team did a remarkable job and put us in a position where ASV was nearly 6% entering this year. So we feel very good about those recurring businesses, and we intend to continue to give you each quarter, our perspective on what we expect of those revenues to be.

You asked specifically about the recurring nature of the Mortgage business. I'll let Ben give you a little color on what's driving that great performance.

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Hi, Rich. We saw this. So, the first thing to start with is on the Mortgage side of the business, when someone subscribes to come on to our network, they're getting our full platform and our network services as part of that. So, there's a base level of subscription fee that someone's paying to be a part of that, and that's really what that recurring revenue piece is.

And when we analyze the deal, one of the exciting things that we saw under the covers here and that I've talked about in terms of the different TAMs that we can go after here with this business, out of that $10 billion TAM, $4 billion of it alone is just in the origination side and automating that whole origination process. And we had seen that Ellie Mae had increased market share from 38% to 44% in a pretty short period of time. And we had conviction, they're going to continue to grow market share in that space.

And I'm pleased to say that under the covers, what we've seen in terms of sales performance, and I even highlighted this on the last quarterly earnings call, back in October, that the sales results have been phenomenal, in terms of selling new versions of our loan origination system into new customers and then also cross-sells of our products into the customer base.

And to go into that even a little bit further, in Q3 and Q4, the company set all-time records in terms of bookings, on the Encompass loan origination system. So Q3 and Q4 were the two highest quarters ever in the company's history.

Q4 across the entire Ellie Mae product set was the largest bookings quarter ever in the company's history. So all of that are real tailwinds, and Scott gave the guide to the Q1 recurring revenue, for the business as well. And why we feel really strong about the business' ability to grow that recurring revenue base, regardless of volume environments.

Operator: The next question is from Alex Kramm with UBS. Please go ahead.

Alex Kramm
Analyst, UBS Securities LLC

Q

Hi. Thank you. Just to follow-on, on that Mortgage discussion just now, since you gave some recurring revenue guidance, et cetera. Can you just give us an update how you feel about your outlook for the full year, in general? And it's a two-part question.

One, obviously, you gave that 8% to 10% outlook, that you're comfortable for 2021, you said when you closed Ellie, but that was just for Ellie. And now you're obviously running ahead. So one, how should we be thinking about that guidance going forward now?

And how should we really hold you accountable, now that you're obviously talking about pro forma numbers, you're integrating the business? So, how should we think about it from a combined ICE plus Ellie Mortgage outlook for the year? Thanks.

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Thanks, Alex. It's Ben. So obviously, fourth quarter blew away all industry estimates in terms of volume. So you got to set that aside. And when we did this deal, we were very clear that we saw this as a long-term growth trend. And that we are convinced that, on an annual basis, we can grow this business. And this business will grow 8% to 10% per year on average over 10 years.

And underneath the covers, as I just referenced, in the answer I gave to Rich. If you look under the covers of what's happened with that business, since we've acquired it, sales strength has been very strong. So I mentioned a couple of the Encompass records that we saw over the last couple of quarters.

Also – and that's $4 billion of the $10 billion TAM, another $4 billion of that $10 billion TAM is around data and analytics. And we also saw record sales of our AIQ platform, so record bookings of the analyzers that are automating, that origination workflow, in the fourth quarter. We continue to see strength across Encompass as well as AIQ in January, and we're ahead in January than where we thought we were going to be, in terms of our model.

What this means, is that, as we're hitting these types of sales results and sales records for the company, it obviously means there's going to be more recurring revenue, into the business. It means there's going to be more customers, on the business. There's going to be more loans that are on the platform, that are now on our network, loans that we did not interact with before.

And more loans on our network interact with the third parties on the network that we have. And for the efficiencies that we provide to people ordering services like a flood report or a credit report off that network, we monetize that, and charge a service fee for the efficiency that we're providing.

So all of these we see as significant tailwinds into the business that give us confidence that we can grow regardless of the volume environment over a long period of time with that 8% to 10% guide.

Operator: The next question is from Mike Carrier of Bank of America. Please go ahead.

Michael Carrier
Analyst, Bank of America Merrill Lynch

Q

Hi. Good morning, and thanks for taking the question. I just wanted to get an update on the data outlook. And I guess, mostly on the equity side, you've just given some of the changes with the SEC on the data rules. Just wanted to see how you think about, if that can impact the business, how you guys are thinking about it, whether it's from a product standpoint, new competition coming in to the industry? And how you're, let's say, to navigate?

Scott Anthony Hill
Chief Financial Officer, Intercontinental Exchange, Inc.

A

Yeah. Hi, Mike, it's Scott. I'll take this and then if Jeff wants to jump in, he can. I think your question, as I understood it, was looking at kind of the recurring revenues in the Exchange business and specifically Exchange data, what are our expectations in terms of any revenue impacts from ongoing dialogue with the SEC, and the answer is none.

We're in conversations about changes they've discussed. But right now, we haven't seen any impact. We don't anticipate any impact. I'll tell you what I think is consistent with what we've said for probably the last 2 or 3 years, which is that's not a line we expect to generate a lot of growth for us. It's not a line that we expect it's going to go down much. It's just kind of be stable. And again, we've given you some history on the recurring revenue and if you look 3Q, 4Q, the guide to 1Q, they're all right in that same number.

So, there is no expectation on our end that there are any changes that are likely to impact revenue this year. We've also said in the past, and I think it's still true that any changes that did come will likely come in over the course of 2, 3, 5 years, not immediately. So the net-net answer is that no real impact is expected on that bucket of revenue for us this year.

Operator: The next question is from Ken Hill of Loop Capital. Please go ahead.

Kenneth Hill
Analyst, Loop Capital Markets

Q

Hey. Good morning. I was hoping to go back to one of the smaller portions of the Mortgage business there on data analytics. I think that run rate is about $70 million annually. But the opportunity you said, as you mentioned, is about $4 billion of addressable market there. So I was hoping you can talk to maybe what infrastructure you're putting in place, what processes you're putting in place to build that out? Maybe help us with the vision for there over the longer term?

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Thanks, Ken. This is Ben. So, this is an area that we have invested heavily in, the business has invested heavily in. And when we're looking at and analyzing doing the acquisition of Ellie Mae, it's one of the areas we were absolutely most excited about. And the area of this business under data and analytics is really that AIQ business. That's an acquisition that Ellie Mae had done a few years ago.

And if you look at the heart of what that business is all about and investments that have been made, it's all about automating the very manual part of the origination workflow. And we've used statistics in the past of it costing around $8,000 per mortgage to [ph] manufacture loan (00:30:40). And out of that $8,000, $5,200 of it is just associated to manual processing. And at a minimum, we believe through our AI offerings, there is a great opportunity to chip away at a minimum half of that. So $2,600 in savings is ripe for automation.

And this is things like I mentioned in the script, around credit analyzers and last quarter, I talked about our income analyzers. This is taking all the stare and compare work that happens when you get a credit report to see what was the date of it? What was the score? You compare the score on the credit report to the information that we have in our AllRegs business around what are the underwriting requirements for the particular product that this customer has applied for.

And we're able to automate a ton of the process right now that is done manually, and it's one of the highest growth sales items we've seen. And as I said in answer to a prior question, that we hit a record in Q4 of new sales of this product.

And in terms of the $4 billion TAM, it's a pretty easy number to get to. If you look at the efficiencies that we provide and assume conservatively, it's $2,600 in savings per loan that we can provide to customers, if we monetize a part of that, say some subset of that, and you use a round number of around 10 million loans being done per year, which is way down from what it was last year, you do the math on 10 million loans, we roughly have almost 50% market share in loan flow that's going through times one subset of that save, and you get to a very big number very quickly. And as our customers are seeing that benefit, we're obviously monetizing it for providing that to them.

Operator: The next question is from Brian Bedell of Deutsche Bank. Please go ahead.

Brian Bedell
Analyst, Deutsche Bank Securities, Inc.

Q

Great. Thanks. Good morning, folks. Maybe just to dig a little bit deeper on the Mortgage recurring revenue, the guide of the $122 million to $127 million, it's a bit of a wide range. Maybe if you, Ben, if you could talk about the variables that you're seeing that impact the low versus the high end of that range.

And then if you can – I think you gave guidance for the recurring revenue in fixed income for the full year. I'm not sure if I missed the recurring revenue guide for Mortgage Technology for the full year or if you have a view on that.

And then if I could just layer in the synergy on the data side in terms of coming up with real-time, more real-time mortgage production data. I know you're working on that; maybe just an update on – a progress report on that.

Scott Anthony Hill
Chief Financial Officer, Intercontinental Exchange, Inc.

A

Wow, okay. So that one question, I think, had three parts. But let me see if I can hit them. First of all, I don't know that $5 million wide on an over $100 million guide is that wide, and it's simply a matter of customers that we've on-boarded and that we expect to continue to onboard.

I mean, that's the thing – again, if you look at the history that we've provided on that line, our recurring Mortgage Technology revenues in fourth quarter of 2019 were $92 million. They were $95 million, $100 million, $108 million, $119 million. So we've seen that consistent growth on a sequential quarterly basis because of everything Ben talked about: more customers, customers that had a certain number of seats signing up for more seats. And so we expect growth to go through the quarter and exactly whether or not that growth is going to add $1 million or $3 million, again, on an over $120 million guide, plus or minus a little bit, doesn't seem like that's that wide a guide, because it's not $5 million wide; it's actually plus or minus $2.5 million. But so we feel good about it.

What I said on the data business, and to be specific, the fixed income recurring revenues was that based on a 5.7% ASV, we fully expect the business to, again, grow right around that at 5% to 6% for the year. As you know, that ASV figure now is effectively 100% of the revenue in that segment. And so we're able to tell you that plus or minus a little bit, given that ASV is at 5.7%, we think 5% to 6% growth is the right view in terms of thinking about the full year for that fixed income recurring revenue.

With regards to the data piece on mortgages and how they're working with the sales teams – or sorry, the – Lynn's team to do that, I'll hand that to Ben. See if he's got any thoughts.

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Yeah. As I mentioned in the script, we have identified some early opportunities on the data side. As you can imagine, there is an absolute treasure trove of information and data sets that are within the Mortgage Technology business segment across all the businesses that are in there. So you have the merged business in there, you have Simplifile, and you have the Encompass system and the Ellie Mae business in there.

Some of the areas that we're looking to leverage the data sets and the power of the data sets in there are simple things, like when you're going through a mortgage origination process, one of the most common areas where you'll see errors is very late in the process when you get to the closing. And what happens at the closing is that you have to compare the original estimates of what your closing fees were going to be at the closing table from what the original estimates were that were provided 60-plus days ago.

And if those numbers are off by any amount, and it's not even a material amount. It could be zero tolerance to 10% tolerance, you have to go back through the entire origination process again. What we found is that Simplifile has all of that information. They know exactly what the closing requirements are, what the fees are in every jurisdiction around the US so we manage all of that reference data for our clients in the closing process.

Pulling that type of information all the way up front to the origination process, and then combining that with our Artificial Intelligence expertise and automation expertise that we have in our AI tools is able to create a significant amount more efficiency and a higher quality loan asset that's going to be less subject to errors as you get to the closing table. And a lot of these capabilities in the Artificial Intelligence area and how to leverage this type of information and data is directly coming from the expertise that we have on the data side of the business.

Jeffrey Craig Sprecher
Chairman and Chief Executive Officer, Intercontinental Exchange; Chairman, New York Stock Exchange, Intercontinental Exchange, Inc.

A

This is Jeff, let me just bridge a wider point, which is we've been building a technology base in the mortgage space, and it's obviously a very hot space, and we've got a really great platform and commodity. And the Ellie Mae business that we acquired was really – turns out has been a really great business since we've owned it. But don't underestimate that a lot of the acceleration of the growth that we've seen comes from the vision that we're articulating of an end-to-end platform managed by ICE.

We live in a society today where many of the platforms that we interact with, you have to ask yourself, am I actually their customer? They're providing a service to me, but am I actually the customer? Because is the customer, the person who's buying the data off of that platform? Or is the customer the person that's giving up the data in exchange for free usage?

And we're seeing a lot of examples right now in our society of people that believe that these free services are – that they are actually customers. And in reality, they're not providing any revenue to them. The revenue is coming from a different source. And so as we're out selling our vision, we're having that conversation with people in the mortgage industry, and it is resonating. The very data that you asked been about and the way that artificial intelligence will interact with that data. Is an area that ICE has built decades of trust in the financial services industry about how we manage that data? Who owns it? Where it's going to go? And how we're going to protect it? And I think that, that bodes well for us as we continue to have a broader conversation in our society about data privacy and data rights.

Operator: The next question is from Alex Blostein of Goldman Sachs. Please go ahead.

Alexander Blostein
Analyst, Goldman Sachs & Co. LLC

Q

Great. Good morning, everybody. Jeff, question for you around maybe some of the regulatory things potentially might be on the comp, but really I was hoping to get your perspective on everything that's going on in the retail trading side of the equation.

It feels like concept of payment order flow has come up a bunch of times in the past. I don't know if this time is going to be any different. But curious to kind of get your perspective on how things might evolve and, whether or not, with 50% of volumes now trading off exchange, could there be an opportunity for the lit venues to grab some of that market share back?

Jeffrey Craig Sprecher
Chairman and Chief Executive Officer, Intercontinental Exchange; Chairman, New York Stock Exchange, Intercontinental Exchange, Inc.

A

It's a great question, one, obviously, we've been thinking about over the last week or so. I guess I'll remind you that when we bought the New York Stock Exchange, we were pretty vocal about the fact that we thought that the market structure in the US equity space was flawed and that it needed a holistic review.

And in fact, we tried to come up with a grand bargain that we talked to many, many people across the industry about that would have resulted in some major change. We were unsuccessful and the last SEC seem to spend an inordinate amount of time on governance of industry consortium basically that manage infrastructure and didn't really step back and look at the totality of the infrastructure and, whether or not, it operates properly.

And I think as you've heard through the guidance that Scott gave, fortunately or unfortunately, that infrastructure paralyzes the industry somewhat and stifles innovation in my view. And so we're going to have a new SEC chair. And if Chairman Gensler is confirmed and actually takes that seat, he's a person that worked in the derivative space and part of his career, worked in the regulated commodities and derivatives space for part of his career and has a deep interest in and knowledge of market structure.

The SEC has got a dual role into a sense that it's an enforcement agency and a consumer protection agency, as well as a market structure agency. And historically, the people that have chaired the agency have been lawyers by training, who are much more comfortable on the enforcement and compliance side of things.

And I think there's an opportunity, and we'll see if it results, but there's an opportunity with a new chair and a new vision inside the SEC to potentially talk about a grand bargain again, which we would welcome. And by that, I mean, we would give up some unique positioning that we have, if others did the same thing and try to get back to a more innovative, transparent regulated market where we could see innovation as it's unique to the United States, continue to grow our capital markets.

Operator: The next question is from Ari Ghosh of Credit Suisse. Please go ahead.

Ari Ghosh
Analyst, Credit Suisse Securities (USA) LLC

Q

Hey. Good morning, everyone. Ben, just a quick one on Mortgage Tech. Even on the origination and tech revenue piece, just curious how we should think about the sensitivity to market conditions over here? Is there either like a backlog or do you have any visibility for a portion of these transaction-based revenues? Again, just curious because I think you were embedding pretty conservative industry and refi assumptions for the year and the outlook perhaps looks a little more favorable than it did three to four months ago. Thanks.

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Thanks, Ari. Yeah, I'll go through it. How we see the business' ability to grow through various volume cycles, and I'll answer your direct question around volumes. So if you think about this business, this business and what really excited about us and just the results that we've seen in the few months that we've owned it now, have just further confirmed the business's ability to grow through volume environments are that: one, it's continuing to gain market share. I've shared the sales results, so you can see that.

Number two, more customers equals more loan flow. And when you have more loan flow going onto that network, on average, a loan that's going through our network with customers of ours on the platform, we see that, that loan interacts around seven times with various third parties on the network.

So each new loan that comes on to that network. There are seven different times that it's interacting with third party service providers and services that we provide on that network and for third party service providers, we get a fee for the efficiency that we provide for somebody interacting with that loan.

The third area is just – it's a process that's ripe for automation. And I touched upon the opportunity there. Around 10 million loans and at least $2,600 in efficiency and some subset of that, you do the math, and it's a big number.

And then the fourth area is the electronification of the close that we are in a very unique position with the MERS and Simplifile assets and the network that we have on the closing side that's extremely unique, integrating that with our origination network through Encompass by connecting that into an eClose room. And we have several big deliveries this year, one in Q2 of our hybrid eClose offering and then followed shortly after in the second half of the year, a full eClose offering, we see that's going to be an area of growth for 2022 and beyond.

When it comes to volumes itself, we do have a bit of a unique insight because we are an origination platform, we see almost 50% of loans that are originated in the US. We do see that the loans very early on in the process. So we see them when the original applications coming through for a refinance or a purchase, which gives us a 60 to 90-day preview of what the market is going to look like.

When you look at industry analysts, you see the estimates that are out there, if you go beyond a quarter or two, anyone that follows these estimates know that they're subject to revision and significant revision. It's very hard to predict mortgage origination volumes out beyond the couple of quarters just like it's hard to predict US equity market volumes and oil volumes going out a few quarters to a year.

What I would say is based on the data that we see in our platform, if you take the estimates like Fannie and Freddie, for the next quarter to maximum two quarters, those are as close to what we see in the data on our platform as being indicative of what we expect volumes to be. But beyond that, it's difficult to forecast, but underneath the covers, with all the other growth areas that we have, regardless of volume environment, we are very optimistic this business can grow.

Operator: The next question is from Chris Allen of Compass Point. Please go ahead.

Chris Allen
Analyst, Compass Point Research & Trading LLC

Q

Good morning, guys. I just wanted to follow-on the mortgage beat. I just wanted to ask, just in terms of the share gains that you're seeing, how much is coming from existing customers versus new customers? And any update in terms of penetration of the independent mortgage banks, which I think as you've talked about in the past is potentially 20% to 25% share opportunity over the longer term?

Jeffrey Craig Sprecher
Chairman and Chief Executive Officer, Intercontinental Exchange; Chairman, New York Stock Exchange, Intercontinental Exchange, Inc.

A

Sure. So, we're actually seeing – thanks, Chris for the question. So we're seeing growth literally across every segment of customer in our platform. So yes, independent mortgage bankers, we are seeing their share of the market. It'd be very strong, in particular, on the purchase side of the market. With refinances, you do tend to see some refinance volume to go to some of the large banks, just because that's where you have a lot of your banking relationship with, people tend to go there.

But in the purchase market, we are seeing that independent banks are continuing to grow. That said, we're growing in each segment. So we service the large banks. We service the independent mortgage banks. We service correspondent banks, wholesale banks, you name it. And what we looking at that sales strength that I referenced earlier, we're seeing that strength across the entire portfolio.

And one other thing, I'd just highlight on the volume front. We tend to – if you look at our share and our strengths, a lot of it is balanced in the purchase market, albeit we do interact a lot with the refinance market as well. When we look at the trends of what happened in 2020 and going into this year, we're seeing application volumes up significantly in refi. They are up as well, is significantly in purchase, but not as much as refi.

And on the refinance side, if you look at estimates that Fannie and Freddie have, for example, for 30-year mortgages of 2.7% to 2.9% right now for calendar year 2021, that puts up to 20 million units significantly in the money for refinancing, which is a higher number than what we said when we actually announced this deal. So we still see a tail in refinance volumes. We're seeing underneath the covers, one of the things on purchase, we are seeing pent-up demand on the purchase side. There's just not a lot of inventory out there.

So as vaccines roll out, as the economy starts rolling, as people are willing to move and actually sell, I think you have a decent amount of purchase demand pent up there as well, which given that our market shares tend to be a little bit more tilted towards purchase than refi is another tailwind for us.

Operator: The next question is from Owen Lau of Oppenheimer. Please go ahead.

Owen Lau
Analyst, Oppenheimer & Co., Inc.

Q

Good morning, and thank you for taking my question. So on slide 20, you disclosed that you have a 1.4% ownership in Coinbase. Could you please talk about the cost basis? Why did you make that investment? And is there any synergy with ICE OPEC? Thank you.

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Yes, that's a good question. First of all, as a company, we've never thought that we were a private equity firm or a venture firm and that we should be stewards of our shareholders' money in that regard. We've always thought that excess capital should be returned. But we have made investments in a number of businesses that are adjacent to us where we thought there was some strategic advantage by having a relationship with the company, either by partnering with them or by knowledge transfer and what have you.

And so we invested in Coinbase in its early rounds because we were trying to understand the blockchain and the significance of digital currencies in payments. And obviously, that company has been phenomenally successful. And I'm sure the value of our stake has increased. And our investment was just almost insignificant, honestly, so, in terms of a monetary number.

I would also say, we have, obviously, a similar kind of investment in Bakkt, which again, was driven by us trying to understand blockchain. And as you may recall, three years ago, two and three years ago a lot of people were asking us whether blockchain was going to be used for clearing, whether it was going to disrupt the traditional financial services industry, and we wanted to be on top of that technology and have that knowledge. And so we also invested and helped stand up Bakkt, which again, I think is a company that we have a small basis or a basis that has dramatically increased, say it that way.

We also made an investment in Euroclear, which is European custody solution that again, we have adjacency to. Company is doing very, very well. And so we do have, as your question I think is trying to allude to, a number of very, very interesting assets that have value that I think over time, we'll try to unlock for our shareholders as those partnerships and knowledge transfers come to some fruition.

Operator: The next question is from Kyle Voigt of KBW. Please go ahead.

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

Q

Hi. Good morning. So in the fourth quarter, S&P Global announced its acquisition of IHS. And just last week, we had the LSE-Refinitiv deal close. Just given the size of these transactions, can you just talk about the kind of broad competitive environment or landscape in your fixed income and data segment? And maybe how you'd expect the environment to evolve as some of these competitors gain scale or add product breadth?

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Sure. Well, I'm glad to say that we recognized early the adjacency of data and information and analytics around risk management and move relatively quickly to formalize our internal offerings and also make acquisitions, similar large acquisitions for us that is really now probably half of our business in serving data and analytics. And I use that number roughly, but it's somewhat how we think of the business. They're intertwined; a virtuous circle of risk management along with the data and information that it takes to manage a portfolio of risk.

And so, it's not surprising to us that others are making moves in that space. With respect to all the companies actually that you mentioned, we have some relationships with them. And both – at times, we use some of their platforms, and at times, they use some of our platforms and data and indices. And so you've seen a movement of large exchange and data information groups advancing their own businesses, but also somewhat collaborating across the industry where necessary. So we have a good relationship with the managers of all of those companies, even though in some areas, we're fierce competitors. And in other areas we cooperate for the betterment of the industry.

Operator: The next question is from Simon Clinch of Atlantic Equities. Please go ahead.

Simon Aistair Vaughan Clinch
Analyst, Atlantic Equities

Q

Hi, there. Thanks for taking my question. I was wondering if we could jump back to the Mortgage Tech side again. And just to your comments about just under 50% market share on the origination side, I was wondering if you could talk about how you see the future competitive environment developing in origination. And what you think – and where you think that market share can go. Is there a natural cap to that market share for you [indiscernible] (00:56:25)?

Benjamin R. Jackson
President, Intercontinental Exchange, Inc.

A

Thanks, Simon. What's amazing when we – as we've – over the last decade, looked at the mortgage space, you've got an area of the marketplace that you can't emphasize enough how analog it is. When you look at that market share that I'd mentioned and you say, what's second behind that? What's second behind that is a lot of either homegrown systems, excel spreadsheets, or stitched together systems. And that's what gave us a ton of confidence in doing this transaction that there is a long way to go in terms of market share just on the origination side.

But the other piece that I can't emphasize enough is that we are in a very unique position where not only do we have this very strong origination network that's helping to write a ton of benefit to our customers in automating this manual workflow. We're in a unique position where we also have the significant network in the electronification of the close in that closing process.

And where the magic we see is really going to happen in this deal is not only in the automation of the origination front, but by standing up, which we have done, an eClosing room, that for the first time, will link your underwriter of your loans, the bank or independent mortgage company and the underwriter that's underwriting your loan to your attorney, your settlement agent, your title insurance provider, et cetera, all into a digital closing room, to be able to codify that transaction, close it electronically, register it on MERS, both the note as well as the loan, be able to electronically vault all the documentation associated to it and file it in the local county courthouse electronically by a Simplifile.

That is an incredible capability that we're introducing to the market. We already have several key strategic pieces of it launched because we had a partnership with Ellie Mae prior to doing the transaction. And as I mentioned earlier, we have some very key pieces of functionality that are in the pilot phase and rolling out in Q2 on our eClose solution. And then we have another big set of functionality coming out in the second half of this year. That's all going to lead to long-term 2022, 2023, additional tailwinds for this business.

Jeffrey Craig Sprecher
Chairman and Chief Executive Officer, Intercontinental Exchange; Chairman, New York Stock Exchange, Intercontinental Exchange, Inc.
A

Yeah. And just focus on how we're thinking about mortgage right now. The real opportunity for us is to take the loan origination customers that were on Ellie Mae and get them to use the other services on our network that we find that the customers that use the entire network have a multiple of revenues for us beyond those that are simply using the loan origination platform.

So the market share, if you are – that we're looking at internally is the bigger TAM of end-to-end services that Ben just described. And we have seen, and I've been involved and Ben has been involved and Scott's been involved. Actually, all of the three of us here have all been involved in helping Ellie close some LOS deals where we've been able to articulate the end-to-end vision, and that's brought the new customer to the platform for the loan origination system.

But it is that full vision, I think, that is helping to increase the market share if you solely look at loan origination. But the bigger addressable market for us is taking those already loan origination customers and getting them to use the end-to-end network.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Mr. Sprecher at this time.

Jeffrey Craig Sprecher
Chairman and Chief Executive Officer, Intercontinental Exchange; Chairman, New York Stock Exchange, Intercontinental Exchange, Inc.

Thank you, Kate. Thank all of you for joining us this morning, and we look forward to speaking to you again soon. But in the meantime, I hope that you stay safe and that you and your loved ones stay healthy. And with that, we'll conclude the call, and have a great day.

Operator: This concludes today's conference. You may now disconnect.