TP ICAP Interim Results 2018

Presentation transcript

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Introduction
Rupert Robson, Chairman

1.0 Introduction (00:00:01)

Good morning everyone. Can you hear me? Yes. Thank you very much for coming. For those who don't know me, I am Rupert Robson, Chairman of TP ICAP.

You will have seen from today's announcement that the first half of 2018 saw progress, with revenues up 3% on a constant currency basis and underlying operating profit up 8%.

We will also be paying an unchanged dividend of 5.6p per share.

However, behind those numbers there was significant disappointment regarding the synergies relating to the acquisition of ICAP's Global Broking business. In last month's announcement we also said that we needed to reinvest in the business to promote growth. And this means that delivery of the firm's full potential will take more time.

I recognise that announcement came as a surprise and I want to give you a little bit more context now.

At the beginning of the second quarter the Board initiated a detailed review of progress on the integration and on our forward plans, against the background of an evolving and changing regulatory and industry landscape.

As a result of that review the Board decided that new leadership was required to execute our medium term growth strategy and complete the detail of the integration.

The Board and I are confident that we now have the right management team in place to deliver the integration and at the same time harness the medium term potential of the business. And you will hear more on both of those themes today.

I'd like to say a few words about Nicolas and Robin before I hand over to them. Nicolas has extensive experience across the Global Broking industry. He joined us in 2016 as Chief Commercial Officer, which gave him an overview of the entire business, before going on to lead the largest part of the firm, the Global Broking business line.

Prior to joining us Nico was Chief Executive of Newedge, one of the largest derivatives brokers in the world.

He is a well-rounded leader, having occupied a number of senior management positions from front office to back. Included within that was running Risk at Fimat, the brokerage arm of Société Générale. He is well recognised across the industry and serves on a number of industry Boards, both here and in the US.

You all know Robin Stewart, who has been confirmed as our new Chief Financial Officer. Robin has a deep understanding of the business having joined Collins Stewart Tullett as Head of Tax, all the way back in 2003, before then going on to become Deputy CFO and Financial Controller of Tullett Prebon in 2010.

The Board has been impressed by the way in which Robin has approached his role over the course of the last six months.

Nicolas and Robin, along with the senior management team, will continue to accelerate the work done on the integration, while also building a valuable and exciting business for the future. And with that I'm going to hand over to Nico.

Background and context
Nicolas Breteau, Chief Executive Officer

2.0 Background and context (00:08:22)

Thank you Rupert and good morning everyone. I will start with the key highlights and then talk about the business as I see it, three weeks into my new role, before Robin provides a detailed review of our financials. After my closing summary we'll move on to Q&A.

I want to start with a clear message; our business is in good shape and is performing well. Revenue grew 3% to £910m on a constant currency basis in line with guidance.

There was a strong performance in Rates and Equities, where revenues were up 7% and 20% respectively year on year.

Operating profit was up 8% at £155m, the operating margin increased to 17%, and profit before tax was also up 8%.

Earnings per share increased to 19.2 pence and the interim dividend of 5.6 pence remains unchanged.

That is not to say that we do not have challenges. I am conscious of the significant disappointment caused by our revised view of the integration. I will talk more about this later.

Before I do that I'd like to tell you why we have great opportunities ahead of us. We are the largest interdealer broker in the world and the leading provider of over the counter data. We have the deepest liquidity pools in a wide range of products. We are truly international and well balanced geographically. We have great brands. And customer service is part of our DNA. So I think is a very good foundation to build on.

When we brought Tullett Prebon and ICAP together in 2017, it gave us greater resources to attract new desks, incubate new products and accelerate our entry into the buy side.

It also gave us greater expertise and capability in technology, in operations, and in regulation. So the TP ICAP combination has already delivered benefits - but there is more to come.

But we can only achieve our full potential if we get the integration right. And quite frankly we need to get this done so that we can move on and devote our energy to build for the future.

As you know, in April the Board initiated a detailed review after concern about the way we were managing the integration. At the outset of the deal we said we would achieve £60m of synergies. This number was later raised to £100m. After the review we concluded that the more appropriate number was £75m. It was unrealistic to deliver another £25m without seriously damaging our business and increasing operational risk.

It is absolutely right that the integration achieves synergies: that was one of the reasons for the deal in the first place. But it is equally important that we provide clients with exceptional service, both now and in the medium term. So we have rebased our integration programme to balance these two imperatives better.

We have achieved so far a run rate of £65m, more than the original target and earlier than expected. We now have a further £10m to go, which we believe is realistic and achievable.

To get to where we are today we have spent just over £100m on consulting, severance, IT staff and other costs; Robin will provide further detail later. To complete the integration we will incur another one off cost of £60m. This will allow us to integrate the Tullett Prebon and ICAP front office applications, simplify our infrastructure and merge our networks.

We also still have to consolidate our HR data, align our policies and remove disparities in our working practices. This in fact will bring the cost to achieve the synergies to just over two times, which I believe is a more realistic number.

Once we have achieved this we will be able to upgrade our business more simply and cost effectively in the future. It will make us more agile so that we can respond quickly to changing client preferences and also regulation.

Iain Plunkett our Chief Operating Officer has left the business and his responsibilities have now been taken by John Hughes, our new COO of Global Broking. John is here in the audience today. John came from Bank of America/Merrill Lynch, where he delivered the global integration of their interest rate derivatives business.

I want to talk now about the broker compensation ratio which we have used to measure our performance as a business. I think it's very important to emphasise that TP ICAP is a people business, and our brokers are the centre of it. They are absolutely key to the Group's ability to earn revenues.

Our focus on the broker comp ratio has delivered a lower ratio over the last years, but at the cost of slower growth, or even loss of revenues. What is more is that it did not take into account use of valuable technology or financial resources. Our competitors were frankly delighted when we talked about cutting broker pay. We struggled to recruit good brokers. We became sitting ducks for them to target our biggest revenue earners.

In response we had to adopt defensive measures to protect ourselves, but that ultimately cost us money. That is not a sensible way to run the business. We need to give ourselves the flexibility to pay the market rate. We want not just to protect our franchise and our strong market position, but we want to grow. So in the future we will focus on revenue and also contribution. Contribution is defined as brokers' revenue minus direct front office costs. In a nutshell, the broker comp ratio is an output of the strategy not an input.

None of this means that we will be wasteful, absolutely not. In fact we will be relentless in driving out unnecessary cost. Our aim is to grow our business and deliver good returns for all our stakeholders, but we need the right metrics in place to do that.

Now, I'd like to give you my view of each of our four business lines, and our plans for them.

I will start with Global Broking, the division I have run for the last year, which grew by 5% at constant currency, to £672m in the first half. Our strategy in Global Broking is to fill the gaps in our product coverage and embed more technology so that clients can transact with us more easily. For example - we've improved functionalities in volume matching, in requests for quotes in new products, and extended our post rate matching services.

We operate separate and competing brands in Global Broking, and this has proven to be a wise decision, both for our clients and for the business. In order to leverage the liquidity in some asset classes, clients can see an aggregated view on one screen with one single sign on. They get the best price and we increase our overall business.

For example, we have migrated Tullett Prebon's interest rate business onto our i-Swap platform that we acquired when we bought ICAP. And this has been a success for both brands and generated additional volume.

As we increase our hybrid capability this helps clients to access liquidity in the most efficient manner. But importantly it also enables us to harvest even more of the valuable data that is created every day in the company.

We are cautiously optimistic regarding market conditions for Global Broking. Major investment banks are returning to more trading activity. Low interest rates are coming to an end and quantitative easing is being slowly curtailed. This should result in increased demand for rates and credit strategies. We have already seen some signs of this with rates up 7% in the first half.

Energy & Commodities is our second largest business. Revenue for the first half was slightly down by 3% to £167m. Energy & Commodities includes oil, power and gas, coal, iron-ore, base and precious metals, soft commodities and renewables. It operates in every major energy centre in the world and serves clients including banks, trading companies, government organisations, corporates and hedge funds.

We are adding expertise in our Energy & Commodities to deepen and broaden our offering. We are also taking advantage of our global footprint to improve client coverage. For example we have just started to link our crude oil desks in Singapore and London. So at the end of the Singapore day London can take over and they can work an order for another five hours or so. So we therefore improve the likelihood of getting the right outcome for the client.

Market conditions in the Energy & Commodities sector are heavily influenced by factors which are unpredictable and outside our control, such as weather, global shipping patterns, economic growth or geopolitical events.

The solid performance of this business is testament to our diversification both by product and geography.

Turning to Institutional Services, this is our newest business division and targets buy side clients. It grew revenues by 6% to £17m in the first half. My last company, Newedge, was focused on this part of the market so I understand it well. In this division we provide agency execution services, in the US and in Europe, on foreign exchange, foreign exchange options and listed derivatives.

The development of this division has taken longer than we originally envisaged for a number of reasons. We have to go through a long process to onboard new clients because there are complex agreements to put in place. We also have to improve our electronic connectivity with clients and we have to adjust our post rate services to deal with the multiple allocations. So I think we underestimated the complexity and the time it takes to do this.

As a result the organic growth of this business has been slower and more expensive than we expected. The good news though is that we in the meantime our COEX acquisition, part of this division, is performing very strongly, with revenues up 36% in the first half.

We remain completely committed to winning buy side business because it's a large opportunity. But we must adapt our execution to achieve this at a cost and at a time scale that produces acceptable returns.

I will now turn to Data & Analytics; this is the leading provider of neutral OTC pricing data, with a huge range of products and a library going back several years. In the first half year the business delivered revenues at constant currency of £54m, up 4%. This is still a small business, but it has great potential and we are planning to invest to accelerate growth.

Eric Sinclair, who is here, joined us at the end of last year to run this business and I have asked him to speak briefly to us today about what he found on arrival, what he has achieved since then and his focus going forward. So, over to you Eric.

Data & Analytics
Eric Sinclair, CEO, Data & Analytics

3.0 Data & Analytics (00:24:34)
Thank you Nico, and I'm delighted to be here today. I met you all in November at the Capital Markets Day when I had only been on the job for three weeks, now I've been on the job for eight months and I'm getting on with it.

I wanted to share with you two observations, the first was just what I mentioned in November and it's worth repeating, what we have at TP ICAP is rare content. No one else has as much OTC content as TP ICAP. The value of market data is largely attributed to its scarce availability and so we are in a great starting position and can build on a strong foundation.

Second, we have data inventory in the Group well beyond indicative data that we have not yet tapped and commercialised, but it is there and waiting for us. We plan to get it, cleanse it, test it, prep it, package it and finally sell it. And we can do that at low cost and at low risk.

So what have we done in the last eight months? Well, we've restructured the business for growth and efficiency. First we have unified the sales team to deepen our client relationships and win more business more efficiently. In fact the sales force has shrunk in absolute numbers, the targets for sales have increased and we have more services to talk about in meetings, so more to sell with a higher return on sales.

Second, we developed a closer collaboration between Data & Analytics and the Global Broking business to link them more closely together and ensure that we extract the untapped data that resides there. And by the way, this is a win-win for all business divisions because from the data we extract, we'll be able to produce better curves and analytics and we can redirect that back to the broking desk so they will be able to better inform their clients.

Third, we've introduced a dedicated channel management function to put proper focus on our relationships with our distribution partners.

Fourth, we started a programme of client data audits to ensure that we are fully remunerated for all the data usage our clients obtain from our products.

And fifth, we are building a product management team to meet the unmet needs of our clients and build our business for the future.

That is what we have done and here is what we are going to do in the near future.

We are developing a pipeline of new product launches. One of the consequences of MiFID II and other regulation is that it's not just us but our clients who have new reporting obligations and they may also need to demonstrate best execution. They need more data and often from neutral source and we can fulfil that need.

We also plan to provide our data products, available through cloud technology, opening them up to a larger diverse customer base at low cost.

In H1 we increased our contribution margin from 61% to 64%, with contribution growth of 9%. The efficiencies from the restructuring will enhance divisional profitability in H2 of 2018. The sales unification will drive future revenue growth. And the product management team will drive long term profitable growth.

So it's been exciting and busy times in Data & Analytics - and now back over to Nico.

Nicolas Breteau, Chief Executive Officer

4.0 Nicolas Breteau, Chief Executive Officer (00:24:34)

Thank you, Eric. So we see great potential in Data & Analytics. To capture this fully will require sustained commitment, financial investment and expanded capacity in the division. This will be done at a managed pace over the medium term, bearing in mind investment to be made elsewhere in the Group.

As we have said we are investing in front office technology and client facing initiatives. We also have an ongoing programme to build a more resilient infrastructure, better security and cyber protection and improved post rate processing.

We spend about £130m a year in cash terms on technology. In addition to this ongoing work we have decided to invest £15m in 2019: £9m will go into Data & Analytics, which represents almost 25% of their annual operating costs. £6m will be invested in electronic projects in our Broking divisions. We expect these investments to be cash flow positive and earnings accretive by 2020.

So in short we have a business which is performing well, we operate in markets where there is a lot of opportunity and we have a realistic plan to deliver the integration and build for the future.

I will now hand over to Robin to take you through the financials.

Financial Review
Robin Stewart, Chief Financial Officer

5.0 Key financials (00:24:34)

Thanks Nico. I'll talk first about the results for the last six months and then give guidance for this year and next in the light of our recent trading update. I will use comparatives on a constant currency basis for revenue and I will focus on the underlying performance of the business before exceptionals and acquisitions.

Starting with the income statement, overall revenue increased by 3% on a constant currency basis and fell by 2% on a reported basis to £910m.

Operating profit of £155m was up 8% on the prior year. And this led to an operating profit margin of 17%.

Net finance costs were £16m and together this resulted in profit before tax of £139m.

The tax rate of 26% is in line with our guidance. Overall net income before exceptionals was £107m. And earnings per share increased by 0.9 pence to 19.2 pence.

Moving on to look at revenue, the business has benefitted from being well diversified by both product and geography. Global Broking grew 5% to £672m with Rates and Equities in particular performing well, as you heard earlier from Nico.

I will talk you through the asset classes of Global Broking on the next slide.

Energy & Commodities revenue was down 3%, to £167m. Growth in oil, European power and gas and metals was more than offset by weaker US energy markets and a reduction in coal and iron ore.

Institutional services grew 6% to £17m, driven by the strong performance of COEX business and in particular the US desks.

Data & Analytics was up 4% to £54m, as the business continued to expand and grow both its client base and product offering.

Looking at Global Broking in more detail, the Rates business grew 7% as it benefitted from volatility triggered by increases in the US Federal Funds rate, the ECB's proposed withdrawal of quantitative easing and the impact of the Italian election. Conditions in credit markets were challenging, and revenue was down 8%.

Foreign Exchange, Money Markets and Emerging Markets were broadly in line with the prior year. And Equities grew 20% as a result of increased volatility in the first quarter, especially in the Americas.

Moving on to look at revenue by region. Revenue in Europe, the Middle East and Africa increased 2% and the Americas grew 6%. These were both driven by strong performance in rates and equities.

Revenue in Asia Pacific was down 1% due to challenging conditions in Energy & Commodities markets, as well as the loss of some brokers to competitors in Hong Kong and Sydney.

As you know, we have rebased our expectations around the integration, so the overall synergy target has been reduced from £100m to £75m. We have already achieved £65m of run rate synergies, of which £31m were recognised in the period. We now have a further £10m to go by the end of 2019.

We expect the additional costs to complete the integration to be around £60m, with around half incurred in the second half and the reminder next year. This cost is one off and will be spent on completing the integration of the two companies, in particular the IT infrastructure.

In the interests of greater transparency we are giving you more information on our administrative expenses today. This shows you how we look at costs within the business, breaking them down into front office costs and management and support costs. Front office costs tend to have a large variable component to them and are directly linked to the output of our brokers. The largest element of this is broker compensation. Other front office costs include travel and entertainment, communications and information services and clearing and settlement fees.

Management and support cost are costs incurred to support the Group, including Data & Analytics, other staff costs, technology and premises.

This slide shows a breakdown of administrative expense movements in the last 12 months in order to show synergies versus net costs. We have recognised £31m of synergies since the beginning of the integration and the movement between the first half of this year and the first half of last year was £23m.

These savings were offset by the following cost increases. We incurred additional costs of £5m on new initiatives, which comprised £3m on Institutional Services, £1m on Belfast, and £1m on the Early Talent programme. There were also net cost increases of £3m and within this £5m of additional corporate costs included an extra £2m on premises, and this was offset by lower travel and entertainment costs.

Net one off cost movements of £9m include £2m in relation to MiFID II, an increase in revenue provisions and the charge reflecting lower capitalisation of staff costs relating to IT projects.

Additional broker compensation of £14m was driven by the increase in broking revenue and the broker compensation ratio. And this excludes £9m of broker compensation within the net one off movements and net impact of acquisitions shown here separately.

I'll move on now to look at contribution. This is an important metric because an improvement in contribution drives earnings growth for the Group assuming a stable management and support cost base. Broking contribution represents the revenue of the Broking business, less total front office costs. In the first half of 2018 Broking contribution increased by 5% to £325m as a result of revenue growth and a reduction in other front office costs. This was despite an increase in the broker compensation ratio due to competitive pressure.

Data & Analytics contribution represents the revenue of the business less direct costs, but excluding the internal charge for data from the Broking businesses. Data & Analytics contribution increased by 9% to £35m in the first half. The overall contribution margin increased by over 3 percentage points to 64.8%.

As I told you earlier the overall operating profit grew to £155m, with an increase in operating profit margin from 15.6 to 17%. This was a result of revenue and contribution growth as well as synergy savings.

This slide gives you a regional breakdown of operating profit, and as you can see the Americas performed especially well with growth of 15% year on year.

So let's look in more detail at the exceptional and acquisition related items which amounted to £94m after tax. This includes integration costs, the amortisation of intangible assets as a result of the ICAP acquisition, the impairment of intangible assets arising on consolidation, as well as charges relating to legal settlements.

Integration costs of £24m include running the integration work streams, staff severance costs, and the non-cash charge for the management LTIP. In our recent six monthly impairment review we impaired intangible assets by £58m, reflecting the impact of our revised synergy target on future cash flows. This is a non-cash adjustment and has no impact on our regulatory capital position since intangible assets are excluded from the calculation.

Earnings for the year of £107m, translated into earnings per share of 19.2 pence, we are maintaining the dividend of 16.85 pence throughout the integration period and we have announced an unchanged interim dividend today of 5.6 pence, in line with this policy.

Moving on to cash, operating cash flow reduced to £5m in the period. Capex increased to £48m, mainly as a result of office moves and their associated technology costs in the US, London and Belfast. The net outflow in initial contract payments in the period was £16m, reflecting increases in payments made to lock in brokers in response to competitive pressure. And there was a working capital outflow of £104m. June is always the bottom of our working capital cycle, but this outflow also includes a settlement fail of £45m which then cleared after the reporting date. Excluding this fail the operating cash inflow would have been £50m.

Other items of note include the integration costs I mentioned earlier of £24m and net interest costs of £15m that now reflect a full period of paying interest on the January 2024 £500m bond.

Looking at our overall cash position, the Group had net funds of £63m at the end of the first half. This represents a decrease of £109m due to the cash outflow and payment of dividends.

£87m of the revolving credit facility was drawn down at the end of June to enable the Group to meet an increase in capital requirements in its UK regulated entities imposed by the FCA after their 2017 audit of our risk management processes.

At the end of the first half total cash held in the Group amounted to £739m, almost 90% of this was in our regulated entities and is restricted for both regulatory and operational purposes.

In the balance sheet you can see the impact of the goodwill impairment I mentioned earlier in the goodwill and intangibles line, which is also reflected in the reduction to shareholders equity.

As I mentioned earlier we have drawn down £87m of the revolving credit facility to finance an increase in our capital for our UK regulated entities. We are planning to refinance this facility by the end of the year at a higher level and as a result we expect net finance costs to increase to £35m for 2018.

We plan to refinance the drawdown on the revolving credit facility and the maturing June 2019 £80m bond in H1 2019. And we are committed to maintaining our investment grade rating and gross debt to EBITDA of less than 2.5 times. We expect net finance costs to increase to about £40m in 2019, including all fees associated with the issue.

So to conclude I'd like to give you guidance for this year and next, taking into account what we told you in our recent trading update.

We repeat our guidance of low single digit revenue growth for 2018 in line with consensus, with broker compensation ratio remaining at about 51%. As we said on July 10th, we expect costs to increase by £10m this year due to the impact of Brexit, MiFID II, regulatory and legal costs, and IT security. These costs will increase to £25m in 2019, £10m of this increase will be one off and £15m will be recurring.

We are also planning to spend £15m on strategic investments in 2019, £9m of which will be on the Data & Analytics business. As you heard from Nico, we expect this to be cash flow positive and earnings accretive by 2020.

We are planning a further £10m of integration synergies by the end of 2019, with the costs to complete the integration of around £60m.

In the second half of 2018 we will include the provision of around £15m in relation to the office moves the Group is currently undertaking. We expect this to be reported as an exceptional item in the P&L with minimal cash impact this year.

As I have just mentioned we expect net finance costs to increase to £35m for 2018 and about £40m in 2019 as our gross debt increases. The effective rate of tax will reduce to around 25% in 2019 as a result of a reduction in the UK and US corporate tax rates.

Finally, capex is likely to be in the region of £80m by the end of 2018, coming down to about £70m in 2019, taking into account the cost of our premises relocation programme.

So in summary we have seen a robust performance by the business, with a 5% increase in contribution. And we are working hard to address our cost base and deliver the integration. We expect a return to strong cash generation by 2020 and a business that is much better positioned for the future. We will monitor progress against this guidance at future reporting dates.

Thank you very much, I'll now hand back to Nico.

Conclusion
Nicolas Breteau, Chief Executive Officer

4.0 Conclusion (00:24:34)

Thank you Robin. So to sum up I want to tell you why I'm excited to be the Chief Executive of TP ICAP. When I joined in 2016 I could see that this industry was going through enormous change. With that comes both challenges and opportunities. Nothing has changed my assessment in the last two years.

Markets are becoming more varied, our broad offering, diversification and international footprint positions us very well for this. Clients are looking for new ways to access products and services; our ability to offer many execution models gives us a competitive advantage.

Regulation is increasing, our size means that we can afford the investment required to remain compliant. So I believe we are in a good position to take advantages of those opportunities as the industry evolves.

Our business is fundamentally strong, resilient and performing well. We have a realistic plan to complete the integration and invest for growth in the future. It will take time for the full benefit to come through, but we are building on our strong foundation to deliver a successful, sustainable business with good financial performance and attractive returns from 2020 onwards.

Thank you very much, we are happy to take your questions now. I would just ask you to wait for the microphone and please give your name and organisation before you ask your question, thank you.

Questions & answers

5.0 Questions and answers (00:36:37)

Owen Jones, Citi

Morning, a couple of questions please. You mentioned that the Board had some concerns about the progress with regards to the integration. What was the catalyst for that concern, where did that come from, because at least from a revenue perspective everything seems to be going in line with expectations? What was the time line of events thereafter? And could you just remind us where the additional £25m of synergies were coming from that you've pulled back from please?

And then the secondly, in terms of guidance for broker compensation you've said 51%, I think that probably implies a contribution margin less than the 38% that you've just reported, so how should we think about that for 2019 please? Thank you.

Nicolas Breteau, Chief Executive Officer

Alright, your first question is about the integration. I think it's fair to say that we - as you know we started in 2017, we worked with some external consultants, the original synergy target was £60m, this was later raised to £100m. What happened is that in an integration phase I would say you start with the low hanging fruit, and you finish with the more difficult heavy lifting. And at the beginning we realised some synergies because we got rid of the duplication in management for example, so that's painful to do but it's not very difficult to execute.

And when we went on with the integration it became apparent that the integration programme was running late. So it became more and more difficult to reconcile the increased ambition of the £100m and the reality of what the programme was delivering. This is when the Board ran a study to look at where the additional synergies had to come from.

And quite frankly, if we had continued on that path the extra £25m would have had to come from pure headcount reductions because the integration programme was running late. So what I mean by running late is that we still have to centralise our data centres, we have to merge our networks, we have to decommission - migrate and decommission - a lot of the front office applications. This is costly and this is difficult to execute. So this is why the target was revised down.

Now we have £10m more to go, this will come from a few reductions in headcount, but limited. It will come mainly from what we call non-compensation expenses reduction. So we are working really hard to revisit our procurement policy, we are looking at our contracts, so there are savings to be achieved there. And also from further decommissioning of our IT infrastructure.

You had another question about contribution, I suggest Robin.

Robin Stewart, Chief Financial Officer

Broker contribution as I said earlier is a function of revenue less broker comp and other front office costs. And so whilst we've talked about the broker compensation remaining at around about 51% we will also be seeking to grow revenue, but also to control and manage as best we can other front office costs. So I think we don't expect the contribution margin to decline.

Alevizos Alevizakos, HSBC

Hello, two questions from me. Question number one; there are £40m of one off costs for 2019, £25m of which go for regulatory costs plus £15m for investment. How much of that will be sticky going into 2020, both in terms of regulation and then in terms of investment?

And the second question is Data & Analytics, the growth was slightly low for H1, however do you remain comfortable that in H2 you would see a pick up and what do you think would be the kind of - over the cycle growth rate for the next couple of years? Thank you.

Robin Stewart, Chief Financial Officer

Thank you. Of the increased cost base that we go into 2019 with, we expect £10m of that to fall away as I said earlier, but the rest will remain sticky.

On the Data & Analytics, do you want to say something Eric?

Eric Sinclair, CEO, Data & Analytics

Sure, thank you and thank you for your question. When we put this presentation together initially Nico commented, why are the Data & Analytics revenue growth numbers so small? So I thought we should use a larger font!

Laughter

Obviously we have much larger ambitions for what we're going to do with the business. So we saw 4% growth in H1. The industry has actually got a five year CAGR at 2%, so we're in line with our peers, but we're not here to perform like our peers. So we did 4%. Last year the industry CAGR was 3.4%.

However, what we've done and what's really important to understand is what we've done in restructuring the business for growth - we will perform much stronger being repositioned for growth. Like many participants in the industry we weren't positioned as a growth engine.

My entire Executive Team was all running the day to day business; they all had aspects of their portfolio - running the day to day business which made them very good at solving client problems. And everybody had a day to day function in their portfolio. There was nobody who was specifically targeted at growing the business.

So the restructuring has allowed us to rebalance this. The first thing that we did was we got rid of the non-performers, including the non-performers in sales. So we have a smaller sales team, but the important thing is to rebalance the team. And we now have a channel management function which we've never had before.

So we created a channel management team because 75% of our revenue goes through our top three channel partners, and there is enormous operating leverage out of those three partners if we can have a focused channel management unit, and we have built that. And we will also add other channel partners in due course from that.

From a sales point of view, this actually pre-dates my arrival, this is something Nico observed when he originally started with the firm, we had two sales teams, so the unification of the sales team is critically important. We would have two reps going into the same client. So picture that we sent a rep from here to London - or from London to Germany to go and see a client to sell the TP product and then we would have a separate rep going in a week later to sell the ICAP product. From a sales efficiency point of view that was incredibly inefficient.

And on a go forward basis we have built these MiFID products which we launched on January 3rd, earlier this year, that combines the 11 venues across all our brands. So you actually would have the same client being seen by two sales reps from our organisation to sell the same product. That made no sense. So the efficiency we're gaining is the sales reps have bigger territories and they are bringing in bigger sales.

The other thing that we're very bullish on is just to give you an example of what's different in our business from the Global Broking. Global Broking starts out at zero every day and the execution services drives revenue. We are in the recurring revenue business in our business.

So just to give you a modest example, in April we launched two products, we launched a product for the buy side clients, for specific access to Pacific data from the Pacific region and a Scandinavian product. We launched it in April, the revenue started to trickle in in June, a modest amount of revenue trickled in June. These modest products are already driving recurring revenues of over a million quid a year. We are only going to see half of that in H2, but obviously going into 2019 we'll see the full million quid benefit. And there will be other products that come to the market in due course that will help drive the revenue.

So what you're seeing is enormous efficiencies that will benefit in H2. And you're going to see the sales ramp up contribute to better performance in 2019. And the product management team will be critical to our long term growth. And those product managers are going to be hired, they're going to be subject matter experts who have domain expertise that would be new for the firm to build drive works and other products to build us out for the future. But you need to hire them, they need to assess unmet needs with our clients, work with a sponsored client, build a product, work with our team to launch it and then it starts to generate revenue. So that is more, longer term investment which is highlighted by the investment numbers the Nico described earlier.

Robin Stewart, Chief Financial Officer

Thanks Eric.

Nicolas Breteau, Chief Executive Officer

Just to complete I would say it's fair to say that we expect the growth rate to be in line with last year's growth rate in Data & Analytics for 2018.

Adedapo Oguntade, Morgan Stanley

Just two questions from me. On the increase in working capital requirements from the FCA, if you could give specifics on that?

And then maybe if you could just give some comments on what you are seeing in your credit business, and why that area is currently challenging? Thanks.

Nicolas Breteau, Chief Executive Officer

Maybe Robin would you like to say a few words about our risk framework and the FCA review?

Robin Stewart, Chief Financial Officer

I will - so the FCA as you know come and do visits every couple of years, and the latest one was in 2017, mid-way through our integration, following previous visits that they had done to both brands prior to the acquisition. And it's fair to say I think they were disappointed with the progress we'd made on implementing our risk management frameworks and embedding them down to the coalface.

That's not to say we're not already doing a lot of the work that we're required to do it's more of pace of change, hampered very much by the integration. And so the outcome of that second visit was - which we received in June this year was an increase in our ICG scalers across several of our UK regulated entities, which has driven up our regulatory capital requirement in the period - through which we'll seek to remediate those issues and then reassess the situation with the regulator.

Nicolas Breteau, Chief Executive Officer

Thank you, I think your second question was about credit, and we suffered a disappointing performance on credit. I think the overall business on credit declined and it was a result of I think the market environment. But if I look specifically at what happened in Europe, our teams suffered from MiFID II because they used to make most of their activity based on taking a spread on the match principle business, and post MiFID II they only charge commission per million. So there's a bit of a reset on the way the performance of the business goes.

So we are planning three things, to remediate this situation, we are investing in the electronic, so we have partnered with a firm to launch - to link if you want our clients and our desks together, to pool our liquidity. And David Perkins who is the Head of Electronic Markets, maybe you could say a word about this initiative.

David Perkins, Global Head of Electronic Markets

I can't promise I'm going to be as funny as Eric. So as an example we have done a JV with a FinTech firm called LiquidityChain and what that does, it provides a very lightweight web based service which allows our clients around the world to connect all of their indications of interest and credit products so that we create basically an electronic network.

The proof of concept behind that is that we've got all of these brokers based around the world, but they are very inward looking, they just deal with the six people around one desk. The idea is to be able to connect a desk in Sydney with a desk in London and a desk in Singapore. So that if we have an indication of interest in a very liquid bond that's made available to the entire network with the correct enablement, etc, being in place.

I think the credit markets are very difficult, they're very liquid and they rely very much on liquidity provision from the top six or seven banks. It's also an area where we haven't invested as much as perhaps some of our competition. And I think you see some of the figures from some of the competition, their credit market results are perhaps not quite as heavily hit as ours, but I think that's because we're deciding where we invest and at the moment the credit markets are not a good return.

Nicolas Breteau, Chief Executive Officer

So investment in technology is clearly one, second is to link our liquidity. We used to have competing separate units, separate desks across Europe for example. So we are creating a global P&L, we are unifying these teams. And the third that we're doing is that we're also investing in the buy side.

So a new team has joined us recently and we are working, I mentioned that earlier, we're working on client connectivity. We want to put in place the electronic connectivity to OMS and EMS with the clients. When it's ready we will be able to generate a new line of revenue on the buy side on credit.

Are there any other questions? No. So thank you very much if there is no other question we can take the time back. Thank you for coming.