Tradeweb 4Q23 Earnings Conference Call Script

This transcript should be read in conjunction with the related Annual Report on Form 10-K, the earnings release, and the earnings presentation, which includes important additional detail, and is provided for the convenience of investors and analysts only. For a full recording of this earnings conference call please see the 4Q23 Earnings Call webcast.

OPERATOR

Good morning and welcome to Tradeweb's fourth quarter 2023 earnings conference call. As a reminder, today's call is being recorded and will be available for playback.

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

PART I: INTRODUCTION AND DISCLAIMER

ASHLEY SERRAO (Slide 2-3)

Thank you and good morning.

Joining me today for the call are our CEO Billy Hult, who will review the highlights for the quarter and provide a brief business update, our President Tom Pluta, who will dive a little deeper into some growth initiatives and our CFO Sara Furber, who will review our financial results. We intend to use the website as a means of disclosing material, non-public information and complying with our disclosure obligations under Regulation FD.

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

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

Now, let me turn the call over to Billy.

PART II: OVERVIEW & FINANCIAL RESULTS

BILLY HULT (Slide 4-8)

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

I am extremely proud of our Tradeweb team that generated the best revenue quarter in our history, and again showcased the diversity of our revenue growth. We enter 2024 with strong momentum across our businesses. Many of you have heard me in the past talk about the battle against the phone as a one-way train, and in many of our businesses, that train has a long way to go.

While the secular tailwinds are powerful, we also need to be focused on making a difference and creating our own waves. Relationship building is a priority and in the past year as CEO, I've stressed the importance of engaging regularly with our customers to understand how we can work together to move markets forward and improve their trading experience. Our customers' skillsets are evolving as they continue to become more tech savvy and sophisticated in how they want to interact with the markets. We believe the world is moving towards a more algorithmic and multi-asset class ecosystem. This puts the spotlight directly on our "one-stop shop" value proposition, in a good way, which we continue to take to the next level by investing in technology and adding and linking products and geographies.

Diving into the fourth quarter, client activity and risk-appetite continued to grow which drove strong double-digit revenue growth. Specifically, on slide 4, record revenues of $370 million were up 26.3% yr/yr on a reported basis and 24.6% on a constant currency basis and adjusted EBITDA margins expanded by 15 basis points on a reported basis and 122 basis points on a constant currency basis relative to the fourth quarter of 2022.

Turning to slide 5, rates and credit led the way, accounting for 60% and 27% of our revenue growth, respectively. Record revenues across rates were driven by double-digit revenue growth across global government bonds, swaps, and mortgages. Similarly, the record revenues across credit were led by strong U.S. and European corporate credit and Muni trading, including record quarterly market share in electronic U.S. investment grade. Money markets also hit a record fueled by growth in our retail certificate of deposit franchise and continued organic growth in institutional repos. Equities was driven by institutional ETFs and our efforts to diversify and grow our other equity products. Finally, market data revenues were driven by our LSEG contract and our proprietary data products, which continue to enjoy robust growth.

Turning to slide 6, our record 4th quarter capped off a record year in 2023. Record volumes across most asset classes translated into 12.6% and 12.2% revenue growth on a reported and constant currency basis, respectively. The scale generated by our strong top-line results drove approximately 49 basis points of adjusted EBITDA margin expansion, and 19% adjusted earnings growth. As our growth initiatives continued to scale, we maintained our tradition of constant and focused organic investment.

2023 was a very productive year with numerous accomplishments to highlight. Broadly, they can be summed up as enhancing our existing product capabilities, adding new clients, forging new partnerships, and placing more bets on the table. On the capability front, we completed our integration of the Nasdaq Fixed Income acquisition, made meaningful progress across our mortgage specified pool platform and expanded our product suite across global swaps. On the client side, we continue to scale our credit, mortgage, and swaps platform as we make inroads with our largest clients. On the collaboration front, we completed the first phase of our integration with BlackRock's Aladdin, expanded our partnership with FTSE indices, went live with our FXall link for FX hedging, and announced our new data licensing agreement with LSEG. Finally, we spent $205 million, in a mix of cash and equity, on our acquisitions of Yieldbroker in August 2023 and r8fin in January 2024.

We believe our investments have not only positioned us well for the future, but also helped make 2023 another banner year for Tradeweb. Moving to slide 7, 2023 continued the streak of robust revenue growth that we have worked hard to deliver for multiple years now. Specifically while the majority of our revenues still come from rates, 40% of our revenue growth came from our other businesses. In fact, over the last 5 years, we have nearly doubled our overall revenues. Over 50% of that revenue growth coming from our non-rates businesses, with nearly 40% of the revenue growth coming from our international business, which has averaged 18% since 2016.

Our international revenues are anchored by our European business but our Asian business produced fourth quarter revenue growth in excess of 50% yr/yr. Looking ahead, we believe Asia Pacific, and more broadly emerging markets, will continue to become a larger component of our international growth story over the next few years. We are focused on expanding our client footprint across domestic markets and protocols, and cross-selling our leading products. Our cross-selling initiatives continues to pay dividends with the recent Yieldbroker acquisition, which we believe will unlock more opportunities.

Relentless innovation has been critical to our success. Throughout our history we have prioritized being first to market, which requires constant investment. In the last 8 years, we have invested over $630 million in technology to help shape the future of electronic markets, growing those investments at an average of 13% since 2016. And as our investments bear fruit, adjusted EBITDA margins have expanded methodically.

Looking ahead, we expect 2024 to be another investment year. Our investments remain heavily concentrated in rates and credit, and we are in the early stages of building out our emerging markets franchise. We are optimistic about the long-term durability of our growth across the business, given our market share gains and pipeline of innovations.

Turning to slide 8—I will provide a brief update on two of our main focus areas — U.S. Treasuries and ETFs and turn it over to Tom to dig deeper into U.S. credit and global interest rate swaps.

Starting with U.S. Treasuries—fourth quarter revenues achieved a new record, increasing by 18% yr/yr. This was driven by our institutional business that had its best revenue quarter ever, led by record ADV across our institutional streaming protocol and growing adoption of our RFQ+ offering. The high rate environment continued to propel our retail business where fourth quarter revenues grew 10% yr/yr. The leading indicators of the institutional business remain strong— we gained share and we achieved record quarterly market share of long-dated U.S. Treasuries versus Bloomberg. Client engagement was healthy with institutional average daily trades up 55% yr/yr. Automation continues to be an important theme with institutional U.S. Treasury AiEX average daily trades increasing by more than 120% yr/yr and over 50% of our institutional tickets utilizing our AiEX functionality.

Our U.S. Treasuries wholesale business produced its best revenue quarter in our history, led by record volumes across our sessions protocol and the 2nd best quarter for our streaming protocol. Our central limit order book ADV was down 1% yr/yr given tougher CLOB market conditions, though the team remains focused on onboarding more liquidity providers over the coming quarters as they deliver on a holistic strategy across our wholesale protocols.

Within equities, our ETF business outperformed the overall market with fourth quarter revenues up 10% yr/yr, with industry activity picking up. Other initiatives to expand our equity brand beyond our flagship ETF franchise continue to bear fruit. Fourth quarter institutional equity derivatives revenues were up nearly 30% yr/yr, driven by strong double-digit growth across options and convertibles. Looking ahead, the client pipeline remains strong as the benefits of our electronic solutions continue to resonate. We believe we are well-positioned to capitalize on the long-term secular ETF growth story, not just in equities, but across our fixed income business.

With that I will turn it over to Tom.

TOM PLUTA (Slide 9-12)

Thanks Billy.

Global Credit

Turning to slide 9 for a closer look at Credit. Strong double-digit revenue growth was driven by 31% and 46% yr/yr revenue growth across U.S. and European Credit, respectively. Munis produced high-single digit growth driven by a pickup in tax loss harvesting, while credit derivatives continued to see softer industry trends. Automation continued to surge with global credit AiEX average daily trades increasing 90% yr/yr.

We achieved another fully electronic quarterly market share record across U.S. IG helped by our highest quarterly IG block market share. Our institutional business continues to scale to new highs as we continue to provide our clients with a diverse set of protocols that meet their execution needs across a variety of market environments. Our primary focus on growing institutional RFQ continues to pay off with ADV growing 28% yr/yr, with strong double-digit growth across both IG and HY. Overall, portfolio trading ADV rose over 40% yr/yr, led by growth across U.S. and European PT. In the fourth quarter, we produced record ADV across IG portfolio trading. Our clients continue to get more sophisticated in their usage of PT, with 75% of our PT volume done in-comp, the highest percentage since the second quarter of 2022. Retail credit revenues were up over 20% yr/yr as financial advisors turn their focus towards more spread-based yielding products to complement buying of U.S. Treasuries.

AllTrade produced a record quarter with over $157 billion in volume. Our all-to-all volumes grew over 30% yr/yr while we also saw over 40% yr/yr growth in our dealer-RFQ offering. The team continues to be focused on broadening out our network and increasing the number of responses on the AllTrade platform. In the fourth quarter, the number of A2A responders rose by over 20% and responses increased by 60% yr/yr. We also continue to increase our engagement and wallet share with ETF market makers, where inquiry and traded volume was up over 300% yr/yr. Finally, our sessions ADV grew over 40% yr/yr while Rematch produced 10% yr/yr growth.

Looking ahead, US credit remains our biggest focus area and we like the way we are positioned across our three client channels. We believe we have a long runway of growth ahead of us and are focused on serving the growing passive markets, investing in our auto-responding and algorithmic technology, increasing our wallet share across our A2A and DRFQ protocols, and looking at ways to help our dealer clients more efficiently recycle their risk. Additionally, we are focused on improving the analytics around pre- and post-trade data. Specifically, across high yield, we have more work to do to drive increased client engagement. We believe we can replicate the success we've had across IG with a particular focus on increasing our penetration with ETF market makers and leveraging our Aladdin collaboration to grow our A2A network post integration.

Beyond U.S. Credit, our EM expansion efforts continue to progress steadily—in the fourth quarter, we went live with our non-deliverable forward for FX swap hedging in collaboration with FxAll, and we continue to build out functionality for multi-asset package trading.

Global Swaps

Moving to slide 10, global swaps produced record revenues as vigorous debate on the timing and direction of central bank rate moves and market share gains drove record results across U.S., European, APAC, and emerging market swaps. The fourth quarter saw continued impacts from lower duration as clients traded on the shorter end of the yield curve, and we had record compression activity in November. Variable swaps revenues increased 65% yr/yr despite an 8% decrease in duration yr/yr. Overall, global swaps revenues in the fourth quarter grew 51% yr/yr and market share rose to 23.6% with record share across all currencies. Additionally, over the last 2 years, we have produced strong double-digit active user growth across currencies with the fastest growth happening across our early-stage penetration into EM swaps.

We continue to make progress across emerging markets swaps and our rapidly growing RFM protocol. Our fourth quarter EM swaps revenues increased over 150% yr/yr, and we believe there is still a lot of room to grow given the low levels of electronification while our RFM protocol continued to see strong adoption with ADV rising over 160% yr/yr. The strong fourth quarter capped off another record year for our swaps business, with overall swaps revenues increasing 18% yr/yr.

Moving to slide 11, over the last 5 years, our variable swaps revenues have grown at a CAGR of 26%. We produced this strong 5-year revenue growth despite an evolving macro backdrop and tepid industry volume growth of 4%. From falling rates to zero rates back to the highest short-term rates we've seen since 2001, the durability of our swaps revenue growth continued to shine through despite COVID, elevated volatility driving a risk-off environment and the failure of several banks. In fact, since the beginning of 2019, the swaps business has produced positive revenue growth in 18 out of the last 20 quarters, with 15 of those 18 quarters producing double digit yr/yr revenue growth. The two quarters with negative yr/yr revenue growth were due to extreme factors – market dislocation related to Covid in 3Q20 caused revenues to fall -2% yr/yr and excess market volatility prompting clients to take risk off of the table in 4Q22 led to a -4% drop in revenues.

As debate has picked up in the market around the level of rates and the shape of global yield curves, industry volumes rose 21% yr/yr. However, it's important to note that most of this increase has been driven by a pick-up in short-end activity which we monetize at very low levels. In fact, we generate over 95% of our swaps variable fees on longer-dated trades >1 yr and 82% on trades > 2 yr. Based on LCH data, over the last two years since central banks started to hike rates, short-dated industry volumes, which are defined as anything less than 2 years, grew over 80% versus 2021 while longer-dated industry volumes grew only 15%.

Looking ahead, from a cyclical standpoint, we believe as the yield curve normalizes, this should boost longer-dated activity. In terms of what we can control, we continue to make further inroads across products, and are seeing early success across inflation swaps, swaptions, and EM swaps. We are also looking at expanding our presence across multi-asset package swaps in the coming year. The focus on building solutions that matter to clients is paying dividends. With the market still only about 30% electronified, we believe there remains a lot that we can do to help digitize our clients' manual workflows while the global fixed income markets and broader swaps market grow.

Before I pass it onto Sara, let me touch on compression and the impact to our swaps fee per million. Compression trading is a natural part of the market. Clients put new risk on, and then collapse old risk as the market environment changes. Given that we primarily charge clients for new risk put through the platform, we do not earn meaningful amounts of revenue from pure compression flow as that activity is mainly related to clients reducing line items that they have traded in order to reduce operational costs. Stripping out compression activity, our risk fee per million has been relatively steady over the last few years with the movement really being driven by product mix shift and duration which impacts the calculation of risk being put on by clients.

While compression alone isn't meaningful for revenues, it has become essential to our client workflow, increased platform stickiness and has driven higher risk trading which we can monetize. Across our top 10 compression clients, as they have picked up their compression flow, this has also led to a material pickup in the amount of risk volumes put through the platform. Additionally, our top 5 compression clients have maintained or improved their overall risk flow ranking over the last year.

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

SARA FURBER (Slide 13-16)

Thanks Tom and good morning.

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

Slide 13 provides a summary of our quarterly earnings performance.

- As Billy recapped earlier, this quarter we saw record revenues of $370 million that were up 26.3% yr/yr on a reported basis and 24.6% on a constant currency basis. Specifically, we derived approximately 37% of our 4Q revenues from international customers, and recall that ~30% of our revenue base is denominated in currencies other than dollars, predominantly in Euros.
- Our variable revenues increased by 35% and total trading revenues increased by 27%.
- Total fixed revenues related to our four major asset classes were up 7.0% on a reported and 5.5% on a constant currency basis.
    - Rates fixed revenues growth was driven by the addition of new dealers across our mortgage specified pools platform and our U.S. Treasury streams and CLOB protocols.
    - Credit fixed revenue growth was driven by the previously disclosed dealer fee increases which we instituted at the start of the fourth quarter.
    - And other trading revenues were down 6%-- as a reminder, this line fluctuates as it reflects revenues tied to periodic technology enhancements performed for our retail clients.
- Full year 2023 adjusted EBITDA margin of 52.4% increased by 49 bps on a reported basis, and 100 bps on a constant currency basis, from the full year 2022.

Moving on to fees per million on Slide 14 and a highlight of the key trends for the quarter. You can see slide 20 of the earnings presentation for additional detail regarding our FPM performance this quarter.

- Overall, our blended fees per million decreased 15% yr/yr, primarily due to a shift away from Cash Rates and a decrease in cash credit and cash equities fees per million.
- For cash rates products, fees per million were up 2%, primarily due to an increase in the European government bond fee per million.
- For long tenor swaps, fees per million were down 29%, primarily due to an 8% decline in duration yr/yr and an increase in compression trades. This was partially offset by growth in EM, European swaps and our RFM protocol.
- For cash credit, average fees per million decreased 4% due to a mix shift away from munis partially offset by an increase in European Credit fee per million.
- For cash equities, average fees per million decreased by 6% due to a reduction in US ETF fee per million given an increase in notional per share traded. Recall in the U.S., we charge per share and not for notional value traded.
- Finally, within money markets, average fees per million increased 3% driven by an increase in U.S. CDs FPM.

Slide 15 details our adjusted expenses

- At a high level, the scalability and variable nature of our expense base allows us to continue to invest for growth and grow margins—we have maintained a consistent philosophy here.
- Adjusted Expenses for 4Q increased 24.7% on a reported basis and 20.7% on a constant currency basis.

- Compensation costs increased 30.7% due to increases in headcount and performance-related compensation.
- Technology and communication costs increased 24.8% primarily due to higher data fees, and our previously communicated investments in data strategy and infrastructure.
- Professional fees decreased 18.0% mainly due to a decrease in legal fees.
- Adjusted general and administrative costs increased due to a pickup in marketing and philanthropy and unfavorable movements in FX. Unfavorable movements in FX resulted in a $500k loss in 4Q23 versus a $2.6 million gain in 4Q22, a delta of over $3.1 million between 4Q23 and 4Q22.

Slide 16 details capital management and our guidance

- On our cash position and capital return policy
    - We ended the 4Q in a strong position, with $1.7 billion in cash and cash equivalents. Free cash flow reached approximately $684 million for the trailing twelve months, up 19% yr/yr. We spent $90 million in cash as partial consideration for R8Fin on January 19th of this year.
    - Our net interest income of $20.3 million increased due to a combination of higher cash balances and higher interest yields. This was primarily driven higher by recent Fed hikes and more efficient management of our cash.
    - Non-acquisition capex and capitalized software development for the quarter was $12.2 million, with the decrease driven primarily due to timing of our investment spend.
    - With this quarter's earnings, the Board declared a quarterly dividend of $0.10 per Class A and Class B common stock, an increase of 11.1% yr/yr. The Board periodically evaluates our dividend along with the consistency of our earnings and free cash flow generation over time.
    - And finally, there were no share repurchases during the fourth quarter of 2023 under our share buyback program, as we already offset equity related dilution earlier in the year, this leaves approximately $239.8 million at the end of the quarter authorized for future deployment.
- Turning to guidance for 2024
    - We will continue to invest in 2024, and are expecting Adjusted Expenses to range from $755 - $805 million.
    - Excluding the impact of acquisitions, the midpoint of this range would represent an approximate 10% increase, in-line with our average expense growth from 2016. We believe we can drive adjusted EBITDA and operating margin expansion compared to 2023 at either end of this range, although, we expect the incremental margin expansion to be more modest relative to last year as overall margins are higher and we continue to focus on balancing margin expansion with investing for the future. As compared to first half of last year, we expect to accelerate investments given the anticipated healthy revenue environment.
    - We continue to invest for the future with credit, rates and emerging markets as key focus areas with a long runway for growth. We also continue to invest in technology that allows us to sustain and build our leading platform. Some of these investments will take some time to scale but we continue to prize innovation and have a technology pipeline that continues to grow.
    - We expect professional fee expenses to be above 1Q23 levels as we continue to augment our technology effort with consultants.
    - For forecasting purposes, our assumed non-GAAP tax rate ranges from 24.5% - 25.5% for the year. The primary driver of the increase in our tax rate is related to revenue mix skewing towards higher tax states.
    - We expect capex and capitalized software development to be about $75 to $83 million. We estimate that approximately 60% will be spent on software development to support our growth initiatives, and ~40% will be related to growth and maintenance capex. The midpoint

of our capex guidance implies roughly a 28% yr/yr increase, primarily due to the acquisitions of Yieldbroker and r8fin. Excluding these M&A related investments and other one-time spend, midpoint growth would be ~15% yr/yr.
  - Acquisition and Refinitiv Transaction related D&A, which we adjust out due to the increase associated with pushdown accounting, is expected to be $142 million.
  - As we highlighted last quarter, we continue to expect 2024 and 2025 revenues generated under the new master data agreement with LSEG to be ~$80M and ~$90M, respectively.

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

BILLY HULT

Thanks, Sara.

As I embark on my 24th year at Tradeweb and my 2nd year as CEO, we continue to see ample opportunity to grow our One Tradeweb mantra and build better markets for the future. We are focused on ensuring our DNA continues to evolve as we remain in the catbird seat as we look to innovate and find new ways to modernize the fixed income markets. Innovation, collaboration, and transformation are at the core of our DNA, and I continue to be excited about the road ahead. On that note, we reported strong January volumes yesterday which translated into revenue growth in January in excess of 20% yr/yr.

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

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

ASHLEY SERRAO

Thanks Billy. As a reminder, please limit yourself to one question only. Feel free to hop back in the queue and ask additional questions at the end. Q&A will end at 10:30 am Eastern time. Operator, you can now take our first question.

THANK YOU

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