IG GROUP

H1 results and presentation

Tuesday, 23 Jan 2018

Peter Hetherington, Chief Executive Officer

Welcome everyone to IG's half year results presentation. I'm Peter Hetherington, CEO. I'm going to give you a brief introduction before handing over to Paul, our CFO, who will take you through the numbers in detail.

If we do the housekeeping first. At the end of the presentation we'll take questions from the room and then go over to the phones. If you could all please remember to introduce yourself, tell us who you work for before asking your question it would help. Also please ask one question at a time so you don't confuse us. We won't steal the mic off you to prevent a follow up.

I'll give you all the obligatory two seconds to look at the disclaimer and then move on.

We've had a really strong first half, delivering record revenues and profits whilst positioning the business for a regulatory change. The last 12 months has seen our industry come under increasing regulatory scrutiny and before we go into the detail of the results I wanted to first give you a few reminders about what IG is and what it stands for.

In 1974 IG was founded. The name IG stood for Investors Gold and the company existed to allow clients to speculate on the price of gold. It was an innovation in the financial markets and the start of a journey that led us to where we are today, offering over 15,000 markets to in excess of 150,000 clients worldwide.

We were the first company in our space to launch an online dealing solution, the first to launch a mobile app with live price streaming and topically we started offering Bitcoin trading back in 2013.

Throughout our history we've always targeted the sophisticated trader. We understand that leverage trading is not for everyone and we believe that we target our marketing appropriately and only on-board the clients for whom our product is suitable.

The rapid expansion and success of online marketing has changed the accessible market for many industries, ours included. This has created new problems in the industry which regulators are now seeking to address.

We believe that through the actions we've taken over the past 12 months IG is in a strong position to adapt to the changing regulatory landscape and to continue to grow following this period of change.

IG's client base is dominated by the sophisticated trader today and we believe this will remain the case in the future.

Looking at the agenda: today's presentation breaks down into six areas. Paul will take you through the first two of those in a moment, the performance and financial position of the Group, before I take you through the rest. Paul.

Paul Mainwaring, Chief Financial Officer

Thanks Peter. Good morning everyone. I'm going to take you through our financial performance in the first half and then our financial position at the end of the period.

We are very pleased that the first half of this year has seen us deliver record revenue and record profit before tax when the business has been dealing with a number of other challenges. I'll take you through the detail of the income statement and the cash flow on the following slides.

In summary these results show that IG is a high margin and growing business which is highly cash generative. The Board has declared an interim dividend of 9.69p per share, which in line with our policy is calculated as 30% of the 32.3p per share paid for the full year last year.

Page seven shows the income statement for the half year in more detail. Net trading revenue of £268.4m was up 10% which drives the 10% increase in net operating income. Total operating expenses were 4% lower than a year ago and therefore all of the increase in net operating income has slowed through to profit before tax, which was 29% higher at £136.2m. That dynamic has pushed our PBT margin for the first half up to 50.7%, a significant uplift on the 43% in the first half of last year. As I will explain later operating costs are expected to be higher in the second half than in the first, so please don't simply extrapolate the margin for the first half into the rest of the year.

The tax rate applied to the interim PBT is the forecast effective rate of tax for the full year of 20.6%. That rate does not include £1.3m that we will charge in the second half as a result of the recently enacted reduction in the US corporation tax rate which reduces the value of our deferred tax assets in the US.

Our profit after tax is up 30% to £108.1m, with our diluted earnings per share also up 30% to 29.3p.

This next slide shows more detail on the 10% increase in net trading revenue. Our revenue from OTC leveraged derivatives was up 9% at £259.3m and the number of active clients in OTC leveraged derivatives was, as expected, 5% lower than overall in the first half last year and was 11% lower in the UK.

As we explained at the prelims we have seen a higher than usual level of attrition of the large number of new clients in the first half last year who were attracted by the trading opportunities around the time of the EU Referendum and the US election, many of whom have not continued to trade after that time.

In addition we've seen a lower level of new client recruitment this half year as a result of the introduction of a new appropriateness test for prospective clients, increased wealth hurdles and a lower level of advertising and marketing in the early part of the year.

The decrease in the number of active clients was more than offset by the increase in the average revenue per client, which increased by 15% to £2,290. As we set out in the first quarter trading update revenue per client in the first quarter was up 25% and revenue per client in the first quarter of the prior year had been dampened by the impact of management actions to protect clients from the potential volatility around the time of the UK's EU

Referendum and by the strong new client inflow in that period. Our revenue per client in the second quarter of this year was 4% higher than in the same period a year ago.

All of our revenue in the US comes from Nadex. We continue to see good growth in client numbers for Nadex up 13% with a small increase in average revenue per client.

And in share dealing and investments we had over 29,000 active clients at the end of the period, more than double the number we had at the end of the previous half year and 43% higher than at the end of May.

Although the direct revenue from these products increased by 85% it is still small, but these positions help to retain OTC leveraged clients and the share dealing business provides an acquisition channel to attract new clients for whom it is appropriate to trade OTC leveraged derivatives.

The donut chart on the right of the slide shows the makeup of the OTC leveraged revenue by asset class. We offer our clients the opportunity to trade a huge range of financial markets through our platform and clients choose to trade in those markets that are the most interesting. The proportion of our revenue that comes from each asset class therefore varies from one period to another.

Unsurprisingly, given the current level of interest in cryptocurrencies, we have seen a significant uplift in the revenue from clients trading in those markets and that revenue is included in FX.

Around 5% of our revenue in the first half of this year came from clients trading cryptocurrencies compared with less than half of 1% in the first half last year. We would expect that if clients weren't trading cryptocurrencies they would trade something else that was interesting. At the full year results last year we were talking about the proportion of our revenue from clients trading commodities which had increased from 8% to 14%.

This next slide shows the bridge of how revenues increased from the first half last year through to the second half last year and then through to the first half this year. We have presented these revenue bridges for a few years now and in fact they've generally been similar each time. This half year however it is notable that the increase in revenue from existing clients trading more, together with the revenue from returning clients, more than offsets the revenue lost from clients who had traded in the previous half but who didn't trade in this half. As a result all of the £22m of revenue from new clients in the period has come through with higher revenue compared with the second half last year.

This analysis illustrates how important client retention is to our business. Developing and maintaining long relationships with clients by providing excellent client service and the leading technology in the market and crucially by operating a business model through which our interests as a business are aligned with the interest of our clients is fundamental to our success as a growing business.

Our business model of internalising client flow and hedging as a residual market risk exposure when it reaches predetermined limits aligns the interests of the business with the interests of our clients. It means that our revenue is the transaction fee we earn from clients trading less the cost of hedging. We do not seek to make money by actively taking market risk and we do not trade against our clients. Under our business model we want our clients to trade well and to enjoy it as they are then more likely to keep on trading.

Our model means that we hold a very low level of residual market exposure which, as you can see from the chart at the left-hand side of this slide, does result in low variability in revenue. We experience very few loss making days. We have not had any loss making days since August 2015.

On the right hand side of this slide is our usual presentation of the benefit of internalisation. The top line shows client income from commission, spread and funding; and the bottom line shows the net trading revenue we would earn if we hedged every client trade back to back; the dark blue line in the middle shows our actual net trading revenue, with the shaded area representing the benefit of internalisation.

We want to continue to attract new clients, but in the interest of the clients and in the interest of the company and the industry we want to only attract clients for whom the product is appropriate and who understand the risks of the product as well as its rewards. To that end we introduced a new appropriateness test at the start of this financial year and higher wealth hurdles. As we expected the number of first trades in OTC leveraged derivatives has come down. It's early days but we believe that this reflects a reduction in the number of lower value clients who make it through the process, without reducing the number of higher value clients who start trading with us.

The number of OTC leveraged first trades in the period was 18,000 with nearly 12,000 new share dealing in investments accounts. Within those numbers just over 2,500 clients opened accounts and traded on both products in the period.

The chart on the left-hand side of this slide shows the total number of first trades, excluding Nadex, in each of the last five half years and the overall cost per first trade. That overall cost per first trade has continued to come down to £1,050 in the first half, but the reduction reflects the increasing number of share dealing and investments accounts and because those accounts have a much lower value than OTC leveraged accounts this overall measure is not as useful a metric as it was.

We offer you another measure: the estimated cost per first OTC leveraged equivalent trade, discounting the value of a non-leveraged account and this cost was around £1,400 in this half year. This is a little higher than in previous periods, but as the chart on the right of this slide shows the payback on this marketing spend was between three and four months and the value of new clients remains strong.

The revenue from the FY18 cohort is the line at the top. It is too early to conclude from this data, but if we continue to focus on attracting higher value clients we do expect the cumulative average value to increase.

We are reviewing the metrics we use to explain our marketing effectiveness, which we hope to be able to set out later in the year.

And the summary of our operating expenses is shown on slide 12. We are pleased with how we've been able to manage our costs in the first half, with the operating expenses excluding variable remuneration 7% lower than in the first half last year. The main driver for this is the lower level of advertising and marketing spend. All of that lower spend year-on-year was in the first quarter of the financial year. This year we reduced the level of expenditure to allow the business to assess the impact of the revised appropriateness test and wealth hurdles on account applications and openings. The spend in the first quarter of the prior financial year was elevated and reflected in the client recruitment opportunity in that period due to the EU Referendum.

Advertising and marketing spend in the second quarter of this year was in line with the spend in the same quarter a year ago and in line with the rate of spend in the second half last year.

Our fixed remuneration costs are unchanged. We have increased headcount overall to continue to administer the business well and provide excellent client service, but we have reduced the average cost per head as roles have moved out of London to the Group's resource hubs in Poland, India and South Africa.

Operating costs in the second half are expected to be higher than in the first half. We are required to charge the FSCS levy in full in the second half, which last year was around £4m. We expect marketing and advertising spend to be higher as we believe it is appropriate to maintain the second quarter run rate.

We expect that our remuneration and other costs will be higher as a result of investments we are making in strategic initiatives, including the MTF at the US OTC business and our EU subsidiary.

As we set out in the outlook statement in the prelims in July last year and again this half year, we are giving guidance that we expect operating expenses in FY18, excluding variable remuneration, to be at a similar level to FY17.

The charge for variable remuneration for the year will depend upon the actual profit outcome. At this stage, in line with the guidance we gave at the prelims, you should expect that the full year charge for variable remuneration for FY18 will be at least as high as for FY16.

The split of our costs between the first and second halves this year is more pronounced than usual and in your projections for next year and beyond I suggest that you base your modelling on the full year costs for FY18 rather than on the run rate in either the first or second half.

Moving on from income and costs I want to take you briefly through our financial position, covering cash, capital and liquidity.

Our business is highly cash generative. We receive the cash from our revenues the next day. Our own funds generated from operations in that period are higher than our operating profit, reflecting the non-cash charges in the P&L which more than offset the working capital outflow in the first half.

After tax payments of £22m, after investment spend that includes the £3m final payment for DailyFX, £5.5m of capex and the £4.6m purchase of IG shares by the employee benefit trust, we generated net own funds before dividends of £103.7m.

We paid the £84m final dividend for FY17 during the first half and our own funds balance at the end of the half year was £627.8m, £75m higher than at the end of November 2016.

The balance sheet on slide 15 shows that the Group continues to be in a strong financial position. Our net assets at the end of November are £70m higher than a year ago, reflecting the net profit earned in the last 12 months less the dividends paid. Our liquid assets at the end of November totalled £790.6m including short-term bank borrowings and client funds on the balance sheet which come from two sources: the £69m that clients have transferred to us through title transfer arrangements and the £44m of client deposits with IG Bank of Switzerland.

On the right hand side of the slide we show the deployment of our liquidity and our available liquidity at the end of November. We calculate our available liquidity by deducting from total liquid assets the amount that's been deployed as broker margin, the client deposits with IG Bank, the other liquid assets held in non-UK entities and the amount of our own funds that are held within client money.

The available liquidity at any point in time is largely driven by the level of broker margin. To ensure that we'll be able to meet our broker margin requirements we have access to a committed revolving credit facility of £160m. We had £50m drawn down on the RCF at the end of the half year, as we did at the same time last year, to ensure we had sufficient liquidity after the payment of the final dividend in October.

The RCF is an important liquidity risk management tool, particularly as the level of broker margin has continued to rise. As we've discussed before the increase in margin requirements is not surprising. Our notional hedging positions, the blue line on the left-hand chart, are driven by the size of our clients' notional positions, the grey line at the top and the extent to which we can internalise client flow. The flat red line at the bottom shows the notional size of the residual market positions we hold after internalisation and hedging.

These residual market positions are really small. We internalise or hedge more than 99% of our clients' positions.

And the other factor in determining broker margin requirements is percentage of the notional that our brokers require us to hold with them as margin. Excluding cryptocurrencies, which throughout the period shown here we've hedged by holding the underlying assets and which therefore have a margin rate of 100%, the average margin rate on the notional value of our hedging positions is between 6%-7%. Our margin requirement at end of the period was £371m, including holdings of cryptocurrencies and cash on crypto exchanges of £67m.

We are now using the future products at the CME and CBO to hedge some of our Bitcoin exposure from client trading and we continue to manage our risks by limiting the absolute amount of cryptocurrencies and Bitcoin futures that we hold. The average level of broker margin in the first half of £359m and the peak requirement which is the more important measure for liquidity management, reached £411m during the period. Peter, over to you.

Peter Hetherington

Thank you, Paul. So I thought we'd start by taking a slightly deeper look at who our clients are. You've all seen this graph before. Roughly 2% of our clients still generate half our revenues and roughly 10% generate fully 80% of our revenues. Our clients are clearly concentrated. These revenue-generating clients are all informed, decisive, adventurous, prosperous individuals that are determined to trade and understand our products well. Our most valuable clients come from a range of backgrounds, but to give you some colour as to what some may look like, here are a few examples. One client might be a fund manager that is now trading their own personal wealth at IG. Another might be an IT contractor who works three or four days a week and trades in their downtime. Or finally perhaps an individual who has made money on property but now runs a number of businesses and trades as part of their daily routine. Our clients come from a range of backgrounds, but what most of our valuable clients share is an extensive knowledge of the financial markets and significant levels of wealth.

Our client base is also established. I want to tell you how long clients trade with IG. The stat we've provided before is that more than half our revenues come from clients who have been trading with us more than three years. That stat still holds true. If you look at the chart on the left hand side I want to draw your attention to the very top band. That band represents clients who have traded with IG for over 10 years and shows that these clients generated 8% of Group revenues in the first half of the financial year.

Looking at client attrition on the right hand side, again a graph you've seen before, you can clearly see that this year's cohort is following exactly the same trajectory as the rest, with retention levels remaining strong.

Looking a bit more at our product offering. If you look at clients who trade with us on a multi-product basis, that is how we define clients who traded both on a leveraged account and a non-leveraged account with IG, we have over 5,000 multi-product clients generating revenue from leveraged trading and by simultaneously holding stockbroking positions. These clients are interesting and were 13% more valuable to the Group than a standard client in the same period, the first graph at the top. They also continued trading for longer, with 72% still trading after a year, versus 60% when looking at leveraged only clients, as you can see in the second chart. We believe that the complementary products IG offers its clients helps us to build higher value longer lasting relationships with our client.

Looking a bit more at client acquisition. We've put this slide in to tell you more about how we target our marketing. MiFID II requires us to define a target market, ensure that our marketing is not attracting clients who fall outside of this definition, the negative market in the correct terminology. On the left hand side we show the determining categories that we use to define our target market. I'm not going to take you through all the detail now, but I wanted you to have the data to be able to reference. Needless to say that at a high level our target market are individuals that have experience with trading derivatives, are wealthy and have a speculative attitude towards risk as part of their investment portfolio.

So, defining the market is step one. Step two is ensuring that our marketing spend reaches this market. We do this by bidding on key terms that associate positively with the target, continually refining our in-house algorithms to improve the effectiveness of the spend. We also flex our spend according to the market conditions to ensure it remains effective. Finally, we employ specialist on-boarding teams to assist appropriate clients through the account opening process. This includes those that cannot or choose not to elect to a professional categorisation.

I'm now going to move on to tell you a little bit about what we've been doing over the last six months. Firstly, you will remember from our full year result presentation that we believe our clients closely associate with the professional categorisation, as defined under MiFID I. As a refresher, that is that they trade at least 10 times a quarter in size, or that they have at least €0.5m of investable assets, or that they have relevant professional experience. Clients need to meet two of these three hurdles in order to qualify as professional. Let me also remind you that all of the regulatory concern is focused on the retail client. To date no regulator has voiced concerns regarding the offering of CFDs to clients that are correctly categorised as professional.

So with that context, let me tell you about our clients. The chart on the left shows the position as it stands today. It shows that most of our revenue is generated from standard retail clients and that these clients are currently the ones under regulatory focus. It also shows you that we had similar amounts of revenue being generated by Limited Risk and Professional accounts. Let me tell you also that both those account types grew over the period.

Now the right hand side shows you where we've moving to as a business. In time, assuming the regulators do indeed impose disproportionate leverage limits, we believe the majority of our revenue will be generated by professional accounts and the standard retail account will cease to exist within the UK and the EU. That account will be replaced by the Limited Risk account, which will grow in value as all of our non-professional client base migrate to that account type.

Moving on to the professional categorisation – this is a subject relevant at the moment to the UK and the EU – will explain that migration is happing. This slide clearly shows that this has already happened to a degree and that is without any regulatory advantage for clients to choose this categorisation. In November we rolled out an online process that enabled clients who qualified to request to become professional. Before we rolled out this process, around 5% of our revenue was generated by professionals. Last Friday over 25% was already generated by clients now classified as professionals. Looking only at those clients who had an open position as at Friday, over a third of our revenue came from professional clients. We believe we're well on track for over half of our revenues to be generated from the professional client base within the UK and EU if regulation is implemented as proposed, including disproportionate leverage restrictions.

I also wanted to draw your attention here to the robustness of the process. Firstly, clients request the change. Then our client teams assess their application before accepting or rejecting the request. To date we have rejected around half of all applicants that we've received as they have not met the hurdles, leaving just over 2,400 clients classified as professional today. It is fair to say that smaller clients are much less likely to be able to pass, which was, after all, the regulator's intention when this categorisation was first introduced. Let's also remember here that the bottom 50% of IG's active client base only generate 1% of our total revenue.

Moving on to our Limited Risk accounts and on-boarding, here I want to provide you with an update on the uptake of this account. In the last six months 56% of new leverage trades were Limited Risk, 42% if you strip out Nadex, as all of their accounts have always been Limited Risk. In Germany and France, where variants of this account are now mandatory, we have seen continued good revenue growth. As you know, we implemented increased wealth hurdles and a much stricter take on appropriateness testing back in June. Six months in we're beginning to see the results of these changes and the initial indications suggest that new clients in the period are more valuable than in the prior period. This is really pleasing for us, it shows that the hurdles are doing the job they're intended for, preventing the less experienced, less suitable clients from opening an account with us.

I'm sure all of you well know MiFID II has been a huge project across the whole financial services industry. For IG more than ten man years' worth of effort have gone into delivering the wide-ranging changes to reporting that are now required. We provide more data on product behaviour, greater transparency on risk, costs and charges and for clients in the EU and Australia we now have national identifiers for individual clients and LEIs for all corporate clients. I'm very proud of the work we have done to deliver these changes and get ready for them.

Quite separately we've also reviewed our partner relationships. We've reduced the number of partners IG works with in the UK and EU and now have less than 25 relationships that we continue to work with. Each of these partners must be committed to providing good client outcomes, have a transparent and appropriate fee structure and be of sufficient scale for it to be worth our while conducting the ongoing monitoring required. We believe we can effectively monitor these relationships to ensure compliance and we believe that we're compliant with the FCA regulations.

Now moving on to something I think most of you have been waiting for, future regulation. After more than 12 months we're now closer to regulatory certainty. It's been a bumpy ride, but it looks like we'll have clarity by the end of our financial year. Believe you me, no one will be happier when this happens than those of us who work at IG. Following ESMA's call for evidence last week, we have greater clarity on their proposals and as a result can categorise each theme according to its potential impact on our business and as you can see the impacts are mixed.

We think the leverage levels as proposed are disproportionate and I'll cover that in more detail later. We're also concerned about binary product restrictions, the no negative protection and the automated close out proposals. These are all restrictions that we agree with to an extent, but we do have concerns around the specific wording and the underlying methodology as it stands in the call for evidence.

With regard to the proposed restrictions on cryptocurrencies, we believe that provided these changes are proportionate they could be effective. However, as with the wider leverage restrictions, there remains the risk of clients opening accounts with offshore providers and losing the benefit of the protections afforded to clients of regulated EU firms if severe disproportionate rules are put in place.

The implementation of standardised risk warnings and the restriction on trading incentives are both proposals that we do support and feel there will be no impact on IG. The one thing that's completely certain is that we're working determinedly to try and ensure regulators identify the best measures to achieve their aim of improving client outcomes.

Going in to more detail around the points of concern, this slide shows the potential impact of the regulations assuming they're implemented as proposed, the potential actions that our clients may take in response to those regulations and the mitigations that we have already put in place.

Tackling leverage limits first. Obviously this is the most significant area and proposes the greatest potential impact to IG and to our clients. The key mitigating action we have taken is to enable clients to elect to be professional. As a professional client, to remind you, you'll be out of scope of the proposed regulatory changes. If a client can't or chooses not to elect to be professional, they have a number of other choices.

First, they could simply trade in exactly the same way as they did before but with less headroom. As we can see from the chart on the right, our clients typically have significant excess margin on their account and so a reduction in the leverage available may just cause clients to trade with less headroom.

Secondly, they could increase the funding on their account and continue to trade exactly as they did before. Again, we can see just how much client funds have increased at IG over the previous six months.

Thirdly, they could trade with an offshore provider. This is the first action that we think may impact IG's revenue. If clients elect to leave IG to trade with an offshore provider, unless that broker is itself another IG entity, we would lose that revenue.

Fourthly, they could continue to trade an alternative product that is or is not offered by IG. Finally, they could simply trade less. Only the final three options *could* impact IG's revenue. When looking at the binary proposals the mitigations and actions are very similar and again it is only those that go offshore to a non-IG entity, trade alternative products, or stop trading entirely, that *could* impact IG.

Looking at the negative balance protection, we think there is very limited impact on IG from this restriction due to the already established Limited Risk account. Those that we have not included on this slide are automated margin close out, standardised risk warnings and bringing restrictions on trading incentives. We believe the latter two could be a net positive to IG.

The concerns we have around the automated margin close out is that operationally we do not think whatever ESMA have proposed is actually possible. However, we do agree with an automated close out in principle and if implemented appropriately we do not think this proposal would impact IG's business.

In totality, as we communicated to the market on 18 December, we feel that the total impact of regulatory change in the UK and EU following the mitigating actions we have taken, would have been less than 10% if applied to the prior financial year's numbers.

Looking at regulation from the client's perspective. We have started to explain ESMA's proposals, including the suggested leverage limits to our clients, so that they have an opportunity to comment before this very brief consultation closes. Well over 2,000 clients have already raised concerns to us and we simply don't know how many have also raised concerns with ESMA. We do know that their site appears to be suffering from some issues.

On this slide you can see a small selection of the comments we have received and I want to tell you that in all honesty in the 24 years I've been working here, I have never known our clients to react so strongly to something before. Maybe they did over the FCA announcement, but we never saw those comments.

We're now setting up a site, which hopefully will be live by tomorrow, which explains the proposals and allows clients to comment. We will then upload these comments to ESMA for the clients. The site is www.replytoESMA.trading Don't look at it now, it's just got a holding page, it will be fully live by tomorrow. It will be very interesting to see to what extent regulators take on board the views of consumers who regularly use the product.

Why are we doing this? We feel it's our job to voice concerns raised by our clients in response to these proposals. We also think that a revenue hit, albeit sub-10%, is meaningful and something that should certainly not be ignored. We think the leverage proposals are wholly disproportionate and may inadvertently cause worse outcomes for clients in our industry. We also think the paper is very short and unclear with no detailed evidence, data, or logic, explaining the significant consumer detriment or the reasoning behind the leverage limits proposed.

One of our three core values is championing the client and this is obviously a crucial issue for our clients. Whilst a large amount of our revenue will be exempt because of the professional classification, this will not exempt a large number of our clients who really enjoy the services which we offer. Another of our core values is leading the way and we're concerned about how this new power is being used. It's designed as an emergency power of last resort to be used to protect consumers from poor outcomes. But this is an industry with hundreds of thousands of happy clients and a tiny and falling number of complaints. We agree with regulators that there are some parts of the industry that need to be significantly cleaned up, but disproportionate leverage rules will not necessarily achieve this. We will work hard to try and achieve the best regulatory outcome for our clients.

Moving away from regulation, I'll move on to the future growth opportunities for the Group. Firstly I'll take you to Germany. We have two new developments here. The first is the establishment of an EU subsidiary to mitigate the impact of Brexit on our European operations. This will be in Düsseldorf, the location of our existing branch sales office which we've had for more than a decade.

We've applied for a BaFIN licence and are progressing well, targeting to be ready by June 2018. This office will serve as the regional hub for the EU and be resourced appropriately for its role with key local management, control and oversight functions.

The second development in Germany is the MTF. We started telling you about this in June. We believe that the MTF will enable IG to address the significant on exchange market in the EU. This market is significantly larger than the OTC market and provides IG with the opportunity to appeal to a wider client base. Our product will be fully limited risk with a mandated guaranteed stop.

Looking now at the US. We have filed an application for a US retail FX dealer licence, have a CEO in place, with further recruitment under way. We believe this market is currently underserved following the exit of the largest provider of services last year. That leaves just three providers in a growing market of 85,000 active Forex traders.

We see this as an opportunity to build the IG brand in the US, alongside Nadex, by also utilising the reach of our daily FX site. Where previously we sold the leads generated from the site in the US we'll now be able to convert these leads directly ourselves.

Looking outside of the EU, I wanted to remind you that IG operates in a number of locations around the globe and there are a number of expanding opportunities outside the EU and UK. We're allocating more resources to these expanding areas in order to be able to develop these opportunities effectively. This is highlighted by the chart on the left-hand side. You can see we've been steadily allocating more marketing resources to the APAC region over the last few years and this has generated results. Revenues have grown consistently in this region over the last two and a half years, reflecting this increased allocation.

The non-EU segment of EMEA has also grown well and contributed an increasing amount to Group performance. The business is strong.

Conclusion. We've delivered record revenues and profits while positioning the Group for regulatory change. We believe that had the measures currently being considered by ESMA been in place throughout the previous financial year the reduction in revenue in that year would have been less than 10%, including the impact from lower binary revenue. If such measures were implemented the company would expect to flex marketing spend and resource allocation, according to opportunity.

The second half of the year has started strongly and we were able to continue to make investments in the business while holding costs flat. There continues to be growth opportunities for IG. IG has delivered a sustainable business for 40 years by placing good outcomes at the heart of everything we do and will continue to do this. IG will lead the way.

Following this period of regulatory change we think now will be a good time to provide you with more detail around our strategy and operations and as such we'll be hosting a capital markets day on 23rd May.

Thank you all very much for your time. Any questions?

Question and Answer Session

<u>Question 1</u>

Alistair Ross, Investec

Morning guys. Five questions from me. I'll take them one by one. Just timing on ESMA and FCA. Any idea? I'm talking about the impact to the P&L.

Peter Hetherington

Well I don't know anything. I'll tell you what I expect, but I don't know. The consultation will close early in Feb. We believe there's a board of supervisors meeting, which is all of the heads of all the NCAs on 22nd, 23rd March, which is the point where we believe that's the first point where decisions can be made. So they could be announced say a week after that and then we expect firms to be given a short period to get ready for those changes.

Alistair Ross

Short, as in? Roughly.

Peter Hetherington

We're working on the basis it would be very hard for these to be enforced before 1st May and most likely you'd be looking around the start of our new financial year, 1st June.

Alistair Ross

And on the back of that, are any brokers absorbing the impact in FY18? Any idea? The only reason I ask is because when I look at consensus and I look at H2 implied PBT it's down 10% on company consensus, which just doesn't make sense to me. Either consensus is completely wrong or people are absorbing the impact, in this year.

Paul Mainwaring

I expect that consensus will move as a result of the information we've given today about the first half and the start of the second. So I would wait until we see what the consensus comes out at before we're able to understand where that goes. We don't think any of the live forecasts now assume impact of regulation in FY18.

Peter Hetherington

And if you're also thinking, if we're saying less than 10% and you've got a maximum impact of one month…

Alistair Ross

It's just wrong. Fine.

Peter Hetherington

It's not my number.

Alistair Ross

Just understanding H1, I understand there was almost zero advertising for cryptocurrency in H1?

Peter Hetherington

Not almost zero, I mean we did advertise, we found it didn't work terribly well. There was enormous demand but it brought through clients who were unable to pass our on-boarding processes. They were not appropriate for the product and failed on our wealth bars. So we did try it, it didn't work terribly well. Crypto for us was far more an asset class that existing clients wanted to trade, rather than a way of bringing in lots of new clients.

Alistair Ross

And can you just remind us when you launched Ethereum and Ripple, as opposed to Bitcoin?

Peter Hetherington

Ripple, a month or so ago, Ethereum, I'm going to say a year ago, roughly? Yes, getting nods, roughly a year ago.

Alistair Ross

Sorry and just on the back of that, I understand that you're going to be advertising more in H2?

Paul Mainwaring

Yes, more spend than we had in H1.

Alistair Ross

On cryptocurrency I mean.

Peter Hetherington

No.

Alistair Ross

No?

Peter Hetherington

Definitely not. What we did with advertising is we turned the taps down in the first quarter, because we'd just changed so many things around appropriateness and wealth and everything else, we let it settle down, got to understand the picture and then turned it up in the second quarter and we expect to maintain it at the sort of level we had in the second quarter of this year. We do not expect to be spending much money on crypto advertising for the second half.

Alistair Ross

Fine. Have you heard anything about blocking of offshore operators at all?

Peter Hetherington

It is a subject which does move, I mean the Americans have been very aggressive at blocking their offshore providers into the US, they did it by going to the payment providers which we've long argued is one of the more effective ways of doing it. They've also done it by Apple, removing apps from the app store which are not licensed, which we believe was initiated by regulatory pressure. So I'd say some countries are getting more aggressive, certainly the app providers are getting much stronger on making sure apps are properly licensed, which definitely will help if you think of how most people trade. I mean, the most powerful weapon is to actually block the websites.

Alistair Ross

I mean, is that something you're trying to push?

Peter Hetherington

Yes.

Alistair Ross

Okay. And then, just on the US, how significant is that opportunity?

Peter Hetherington

We wouldn't have done it if we didn't think it would be at least as significant as the other recent offices which we've opened, by which I'd say Dubai and Switzerland. Whilst America is a big place with lots of clients you have to remember that it's only one asset class that you're able to offer, so it would be wrong to extrapolate it into a huge number. We think at least as significant as the other recent offices that IG has opened.

<u>Question 2</u>

Hayley Tam, Citigroup

Just two questions please. First of all, just the partner reduction that you talked about on slide 26 could you remind me how many partners you had before and when this reduction actually took place and whether that's already had any impact on your flow or whether it will do in the future?

Peter Hetherington

Okay, I mean if you go back three or four years we had 300, 400, 500 partners of one form or another, the vast majority of which were small. This is a journey we've been on for a long time of progressively whittling the number down and in the last six months we went from circa 60 to sub 25, it's that sort of order of reduction. We're not forecasting any particular impact on the revenues from doing that. Existing clients, often when you remove the introducer, remain anyway because they like the service and offering that we have. Obviously the partner stops introducing new accounts, but we're not expecting any financial impact from this risk reduction measure, or very, very limited.

Hayley Tam

Thanks. And the second question was just on slide 34, the APAC revenue opportunity that you identify. Am I right in thinking that's mostly Japan and Singapore and could you give us some idea of is it just marketing spend you have to do here, or is there anything else that you would do on the ground to attack this revenue pool?

Peter Hetherington

There certainly are local sales teams, there are certainly people, I mean our Australian office now has almost 100 people in it, when a couple of years ago we kind of had 60, that sort of thing. We run the APAC region from our Australian hub, the significant businesses in the APAC region, obviously Australia, followed by Singapore, followed by Japan and some reverse enquiry business from other countries in the region. Not that significant.

<u>Question 3</u>

Mark Thomas, Hardman and Co

Two again if I may. Just in terms of what percentage of customers failed the appropriate test and wealth test last year compared to what percentage fail this year?

Peter Hetherington

I'll have to come back with exact numbers. It went from an order of about a quarter to more than half is what I would guess. I don't know if anyone wants to…? Mike, is that right? Right, well we might come back and correct that answer if it's materially wrong.

Mark Thomas

Sorry to focus on crypto again but given the sort of hedging markets becoming more liquid does that change any of your appetite in terms of leverage ratios for existing clients?

Peter Hetherington

I mean, you've now got two futures exchanges offering it, both have a 40% initial margin. We've said in our statement we don't offer any on more than 3:1, so we're actually 35% minimum initial margin on all crypto, so I'd say we're pretty much in line with the futures exchanges in terms of the leverage we offer, i.e. very little. The futures exchanges only offer one Bitcoin. Bitcoin is not the most significant cryptocurrency that our clients are trading, that's been easily overtaken by Ethereum now.

So yes, there is a futures market, yes that's great, but we can only use it for the second most important and decreasing in importance cryptocurrency and the futures exchanges are only open five days a week with breaks during that. We're now open six and a half days a week, cryptocurrencies trade 24/7. We've had quite a big shift when our clients are trading these products on a Saturday morning, Sunday morning, Sunday night, whatever, when the futures markets just are not open.

So it would not be a suitable place for us to put too much of our exposure, partly because it's in the second biggest, partly because you might not be able to trade it when you actually need it, because our hedging is simply a function of what the clients do which is going to mean we're always going to need to keep quite a bit in exchange where we can actually get it when we need it.

<u>Question 4</u>

Richard Taylor, Barclays

Morning. A question on hedging with regard to cryptos. Can you help us understand what could happen if you have a Swiss franc type event in any of those instruments, or all of them? What happens to IG? What happens to your clients?

Peter Hetherington

There are two principal risks which we run in offering a crypto product. The first is what happens if you get a Swiss franc style price move. If the price of crypto, all the cryptos we offer, were to halve in the next second, with no trading whatsoever in between, the total amount of debt that clients would have on their account at IG would be well under £1m. And that is simply a function of us not offering much leverage on crypto.

So everyone's got 35% cover, most have actually got significantly more than that. So the first risk we're talking about is what happens if the price moves. You'll be unsurprised to hear it's one of the stress tests I do look at each day, one of the more interesting ones and I look very much at that and we've modelled that on a 50% gap number, which is a very harsh measure, but the number is still extraordinarily small.

The second risk is what happens if our non-futures hedging were in some way compromised. So if the vault or the exchanges we put this in had coins stolen, which as we all know does happen and we mitigate that risk by distributing our hedging across lots of venues and lots of vaults so we're not concentrated in any one place to mitigate that risk. Clearly the stuff which is on the CME and CEBO goes through the clearing house, so that's all fine, the rest of our hedging we've got to put in various places, often slightly unconventional financial institutions. Therefore we distribute it a lot and that's why we limit how much exposure we want to it. So they're the two interesting risks we see from the crypto side. And that's how we manage them.

<u>Question 5</u>

Justin Bates, Liberum

Hi. Could you just tell us what revenue did on a constant currency basis year on year and what proportion of costs are sterling based?

Paul Mainwaring

On the first one, no. I had a brilliant paragraph that I had in my presentation at the prelims that set out that it's just there are so many factors that impact upon the currencies and the translation, there's a wide range obviously of underlying instruments clients can trade in their own account currency or the currency of the instrument. So we don't seek to calculate the impact. And of course all the market risk is managed centrally in a sterling equivalent entity, so we don't do that. The costs we say are a fifth? 50%? You'll have to shout a little louder to me Wendy? 50% in sterling.

Concluding Comments, Peter Hetherington

Thank you very much for your time.