IG Group, H1 FY14 Results, 14 January 2014

<u>Christopher Hill - Chief Financial Officer</u>

Right good morning everyone I'm Chris Hill, CFO, and of course with me here is Tim Howkins, CEO. Welcome to IG's half year results presentation. Thank you for coming along this morning and thank you to everyone on the line for your interest in IG.

You will have seen the announcement that we put out today. I'll take you through the first half numbers and the outlook for the second half; and then Tim will go through the initiatives that we've been working on over the last six months and the things that we will be working on going forward.

Slide 4: H1 FY14 Summary

So getting straight in, Slide 4 is the H1 summary. Revenue of £182.7m was up 8.1% against the prior year. And we've seen some gearing through the P&L due to the one-off costs and the slightly inflated tax rate last year. PBT of £95.1m is up 17.3% with diluted earnings of 19.6p up 22.4%. The business continues to have strong cash generation, with £79.1m of funds generated. The interim dividend is flat at 5.75p and this reflects the market's more cautious outlook for the full year.

On the right hand side we show the half on half mix. For the last two years there's no real pattern. The first half of '12 was 53% of the year, the first half of '13 was 47% of the year. But H2 last year was very strong, particularly in the final quarter with record quarterly revenue. Second half comparatives are, therefore, clearly tougher.

For PBT, last year was unusual. Hopefully we were very clear about that at the time, the first half had some additional one-off costs and the second half had the record revenue in the final quarter combined with one-off credits in other income and operating costs, but more of that later.

Slide 5: Income Statement

A bit more P&L detail on Slide 5 here, the income statement. As I said net trading revenue was up 8.1%, driven mainly by revenue per client, up 13.3%.

Betting duty was flat on the same period last year, although I will remind you that this picked up later in a busier second half of FY13 as you might expect.

Other net operating income includes interest on client money and, with the decline in rates, we are seeing a lower return. Over the last couple of years we've only seen a real return here in Australia and rates here have fallen markedly in the last 12 months. As the effect of this fall feeds through this is on a downward trend until interest rates increase. It's also worth reminding you that the second half of '13 had a one-off recovery item in this line and the income on the Spreadex client list will finish at the end of this year.

Operating costs were down 2% and I'll come on to this in some more detail. And we had a lower tax rate than last year at 24.6%. This is pretty much in line with what I expect for the full year.

Slide 6: Revenue Bridge

Slide 6 - the revenue bridge. This has become a useful way of laying out what is shaping revenue period on period. Using H2 of last year as the base, the pattern is what one should expect in a quieter period following a busier one. Remember that the second half of '13 was only £2.5m off the record first half of '12 period, and the fourth quarter was our first £100m quarter. Hence you'll understand why we are emphasising how comparatives get tougher.

In a quieter period we see a reduction in trading by existing clients who trade in both periods, and the proportion of clients from the previous busy period that don't trade in the current period, but they don't close their accounts. And in this case the sum of new clients and existing clients who began to trade again in the period is not sufficient to outweigh the other two negatives.

Slide 7: Active Clients

So Slide 7 - active clients. This slide shows that revenue was ahead everywhere except Australia. As I mentioned earlier the upside in revenue versus H1 last year was very much driven by the positive movement in average revenue per client. We don't normally talk in constant currency because currency movements are the very lifeblood of FX trading but it is worth a mention that the Australian result is obviously affected here by the pretty severe weakening in the Australian dollar.

Europe is definitely more encouraging with growth both in clients and average revenue. The near term growth opportunity here remains substantial. Almost every country in Europe was ahead of last year. And I won't steal Tim's thunder on client numbers but I will remind you that although account opening isn't easy at this time there has been some specific management action which has significantly reduced the flow of new low value accounts.

Slide 8: Revenue Composition

Slide 8 - revenue composition. I won't spend long on the revenue composition slide but I think this really shows the value of offering the broad range of asset types. The market backdrop is different for different assets. Here you can see that indices performed well, while Forex struggled a little bit due to lack of volatility. Indices was almost half of the business in the period.

Slide 9: Volatility of Trading Days

You'll see once again on Slide 9 the daily revenue trend. You can see how tight the revenue range was in the period, in fact it was particularly tight; but I think the main point you should take away from the slide is that the IG business model and the way that we manage risk has meant that consistently revenue has correlated very well to trading volumes, not to movements in the book.

Slide 10: Operating Cost Bridge

The walk on Slide 10 - the operating cost bridge - shows the transition from last year's £86.6m, which included the £4.6m of non-recurring costs that we detailed at this time last year. That was £1.3m of redundancy, £2.3m of Echelon legal fees and £1m spent on the rebrand. That then rebases the underlying number to £82m. From that we have £0.5m lower on salaries with lower than expected headcount numbers. And marketing was down, even after excluding the rebrand. Marketing never splits evenly across the year; this time it's weighted to the second half and I expect it for the full year to be about flat on last year. The bonus reset, we mentioned last year, this remains flexible and obviously depends on H2 revenue.

And then 'other' includes bad and doubtful debts. Last year was the final significant recovery of some of the bad debt from 2008, which occurred before we developed our automatic close out process. So you're now seeing more clearly the real provision and this is still less than 1% of revenue.

Slide 11: Cost Base Detail

Slide 11, here's the cost detail. I've already described the key movements in the period but I'll remind you of what Tim says in his statement in the results release; the second half will be higher than the first half, reasonably substantially.

The Swiss office costs are in the second half. I've mentioned the marketing phasing already. We'll also have new roles coming in around the investment in the initiatives that Tim will take you through in a few moments. And of course there's a link between revenue and cost, especially around variable remuneration.

Notwithstanding this, assuming revenue comes in line with expectations, and this remains a reasonable challenge due to the strong prior year performance, the overall increase in costs will be lower than was outlined in July by a few million.

Slide 12: Net Own Cash Available

Slide 12 - cash. Hopefully this layout of cash is familiar and helpful. It's also rather unsurprising. In terms of free cash there is always a second half weighting because we pay around 75% of the dividend in the first half. But cash generation was once again strong, £79m against £59m. There was a working capital outflow due to the bonus payment, remember we're paying out the full bonus from last year but only booking up half a year. So after paying tax and allowing for the dividend and working capital flows own funds are basically flat.

Broker margin was up by approximately £28m since the end of the year, and ended the period at its high point. As usual you can see the detail in the appendix. It averaged £240m in the period and hit a low of around £210m.

On the right hand side you can see the application of own cash available. Own cash available for liquidity has risen by £41m over the last 12 months to £111.5m. The things to note here are the rise in the liquid assets buffer in the period to around £83m. This is held as short dated gilts, and I mentioned this back in July. You'll remember that this is an FCA requirement and it's more stable now at this level.

We also say in the footnote on this page that we had drawn down £25m of our facility at the period end and this has since been repaid. As we said previously there will be an additional specific regulatory capital requirement and we've now announced that that's for Switzerland and that'll be around £15m.

Slide 13: Regulation

Slide 13 - regulation. On regulation the European FTT debate rumbles along. There's nothing specific to add at this point I'm afraid and we haven't changed our view that this is ultimately going to end in a significant compromise. We're also not really seeing any material impact, positively or negatively, from the unilateral taxes in France and Italy.

We now have clarity in Japan but not enough time to fully understand the impact. The new binaries regulations came in at the start of December. They essentially outlaw many of the products being offered by our competitors and actually have allowed us to expand our range. But there is now an online test which new binary clients need to take and pass. This will inevitably slow down recruitment.

There's no new news in Singapore but we continue to assume that additional FX leverage restrictions will be imposed. You'll remember that in Singapore there is the concept of accredited investors. We believe that most of our clients will qualify here and won't be restricted beyond the current. So still a net negative but not that material.

In his statement Tim provided some thoughts on the UK spread betting tax position. We think that the Treasury fully understands the advantages of the current tax structure and we don't see them as having any desire to reopen that debate.

Slide 14: Summary

In summary then it was a pretty good performance, given the lack of explicit market activity in the period. But this was against the prior year which, as we said at the time, was pretty weak and also was dampened by some one-off costs. As I've said a few times H2 last year provides a challenge for this year's second half given the record revenue in the fourth quarter and the one-off credits.

Operating costs will be high in the second half but we expect to come in slightly below our previous guidance. And cash delivery was once again strong and the balance sheet supports our liquidity needs in more choppy markets.

So on balance a good first half which provides a strong foundation for the rest of the year. With that I will conclude the financial review and hand you back to Tim to cover the business update.

Tim Howkins - Chief Executive

Slide 16: Strategy

Thanks Chris. Good morning everybody. First of all just a quick recap of the strategy. I'm sure that the left hand side of the page is very familiar to you so I won't read through all the elements of our strategy, but I think that the key theme running through all of this is about offering active retail traders the products, platforms and level of service that they demand and obviously the more active you are the more demanding you tend to be.

On the right hand side we've listed a few of the major projects we've been working on for the last six months and actually, in many cases, for quite a lot longer than six months. Almost all of these continue into the second half and, indeed in many cases, for some considerable time beyond that. So I'll come to each of those over the next few pages.

Slide 17: Client Focus

First of all, I just wanted to touch on our focus on active retail traders, and this really runs through everything which we do, whether it's platforms, websites, marketing, brand. And I think this has possibly been slightly misunderstood and slightly misreported, particularly in some elements of the press. And it's just been reported as a focus on the very largest clients. And that's certainly an element of it, we are certainly making sure that we offer our very largest clients the best possible, most personalised service we can, because clearly there's a lot of value in that element of the client base. But it's also about making sure that we don't squander resources on clients who are very, very tiny in value. And our analysis shows that a client who starts very, very small, either in terms of the value of their first few trades, or in terms of the amount that they deposit in their early days as a client, those clients almost never go on to have any significant value; they tend to be short-lived and very low-value.

The chart on the left shows the mix of our new clients, and particularly the lower end of our clients. So the red line is clients, so this is monthly value; the red line is clients who are worth less than £1 a month, and you can see they were a significant proportion of new client recruitment, and that has fallen off really quite dramatically, from a peak of around 15% of all new clients recruited, down to more like 5% of all new clients recruited, and that reflects the impact of a number of initiatives we've taken.

And we're not absolutely closing the door on very low-value clients, but we are doing things which either discourage them or, conversely, encourage them to flip into higher value. And you can see some of that element of the client base has simply gone away, some of it has shifted into this blue line, which is clients who are worth between £25 and £100 a month, and clearly you don't need to get many clients to flip from that to that for it to be a very positive message.

Some of the things we've done are to increase the minimum amount you can deposit with us using a debit or credit card, albeit it's still only £100, so it's still relatively modest. We've increased some of the minimum transaction sizes during your initial period as a client. And we've introduced some elements of differential pricing, so that if you choose to trade with us on very small contracts, those are slightly more expensive than larger contracts. And all of that we think will have a progressive impact on average client value.

You can see here the impact on new clients. We haven't shown you the impact on the client base as a whole, it's quite a lot more complicated as a picture. The effect is most noticeable in the UK, where there is a distinct shift away from these very low-value clients, but I think it will take some time before this effect is completely washed through the established client base.

Slide 18: IG.com

Turning on, IG.com has been a big project that we've been working on for probably about a year now. A significant project involving migrating 15 different countries on to a single website in nine different languages, something like 100,000 different pages. We've talked about the benefit of this before, which is to consolidate all of our global traffic on to a single domain; the effect of that is that each country should get the benefit of the traffic that every other country drives to that website.

Inevitably, there is a short-term adverse impact, because you're going from websites that have many years of history, or as search engines describe it, domain authority, to something which is brand new and not recognised by the search engines as an authoritative site on the subject matter, i.e., on spread betting and CFDs, and it takes a little while for that domain authority to build up. We are progressively building up that domain authority and steadily climbing through the search engine rankings with the new site.

The other key aspect of this was moving Insight, which is our market information portal, from being only accessible to logged in clients to being accessible to the general public. On Insight, again, it will take time for that to build in authority as the search engines begin to recognise it as an authoritative source of information on financial markets, but we are beginning to build our ranking for individual equity searches, particularly using PCs; it will take a little bit longer for the same effect to take place for searches done on mobile.

All of this will, over time, drive an increasing volume of traffic to IG.com, and that's a source of potentially valuable potential clients, particularly as we begin to expand the product set introducing cash equities, which I'll talk about in a few minutes.

Slide 19: Forex

On Forex, it's worth saying we are the market leader in Forex in a number of the markets in which we operate, but generally our market lead is less decisive than it is for CFDs as a whole, and therefore one of our aims has been to raise awareness of IG as a Forex provider and increase our market share, at least our market share measured by revenue.

I've listed a number of ongoing initiatives here and I'll just talk about the first couple of those. First of all, MetaTrader 4. We really had two objectives when we launched MetaTrader. The first was very much about retaining and nurturing our existing client base, there was quite a strong feedback from all the research that we did, that our existing clients would welcome us offering MetaTrader as a tool. And the second reason was to access the large pool of clients internationally, who use MetaTrader and aren't using IG.

I think we've made good progress on the first of those, we've got something like 2000 clients regularly logging in to MetaTrader, and actually the majority of those are using MetaTrader's tools, particularly the charting tools, but continuing to trade with our existing platforms, and that's actually the preferred outcome that we want from existing clients. It's obviously too early to see what impact that's having on client retention, but we think it should be beneficial over time.

In terms of the second aim of accessing new clients, we're seeing, I think slow steady progress there, we have some hundreds of new clients trading on MetaTrader, but I think it will take a while for that to build as we begin to become known as a place that does offer MetaTrader after, for very many years, being somewhere that didn't.

Still some ongoing development to do here. In response to client feedback, we'll be adding equity indices as well as Forex to the platform in the next couple of months, and also adding spread betting; it's currently a CFD only offering.

The second initiative, that we haven't actually talked about before, is the launch of Sprint Markets, which we did a couple of months ago. Sprint Markets are a way of presenting our very shortest term binary options, and we didn't talk about it particularly because we very much saw it as appealing to the existing audience who are trading binary options. Actually, over the last couple of months, against a backdrop of very low volatility in Forex, we've seen quite good take-up in Sprint Markets from existing and previous Forex traders, so a slightly unexpected consequence, but we have launched this and it does appeal to Forex traders.

Slide 20: Mobile

We're now at a point where roughly a third of all client transactions are done using mobile. I think the trend on that chart is pretty obvious, it's pretty much a straight line going up, and it's clearly heading in only one direction. I don't think there's much doubt that within the foreseeable future, probably within the next year or two, mobile will be the dominant way in which clients interact with IG. Not just for trading, but increasingly for all aspects of their interaction with us, including managing their account, and the early stages of the client journey, so researching our products and opening account. We are seeing increasing numbers of clients coming to us via that route.

We are, I think, well positioned in terms of what we've got already compared to the competition, but we can't be complacent. There is considerably more work to do to ensure that we bring all of the tools and features that are available to our clients on the web into the mobile environment, and that will probably occupy us for the next year or so. And then beyond that, there's quite a big subject, which is turning mobile into a really effective recruitment and conversion tool. We are already seeing significant numbers of account applications via mobile, and I think that will become an increasingly dominant source of clients for us over time.

So in summary, I think we're in a strong position on mobile, but there's still plenty more to do and it's going to remain a significant subject of development over the coming years, as it becomes the dominant way that clients interact with us.

Slide 21: International Expansion

Six months ago, I was talking rather coyly about the three countries where we were working with the regulator. We're now at a sufficiently advanced stage with the first of those, which is Switzerland, that we can reveal that it's Switzerland. The regulatory regime we'll be operating in in Switzerland is relatively unusual for us, in that we have to do much more of the pre-preparation than has traditionally been the case when we've opened a new office. So effectively, we have to have that office fully fitted out, fully staffed, and we have to demonstrate through an audit process that the office is fully functional and ready to go, before the regulator will finally consider whether to grant the licence.

That does mean there's quite a long and relatively expensive lead time into the launch. We're well advanced in that process, we're in the process of hiring the last few staff at the moment, so we will have pretty much a full cost base for that office throughout the second half. It's unlikely that we'll get our licence much before the end of the financial year, so I think we'll start generating revenue round about the end of the financial year.

I think the attractions of Switzerland are relatively obvious, it's clearly a country with a very good wealth demographic. It's not quite a greenfield site, there is some existing CFD competition, but it's a relatively undeveloped market for our products and we think it's an attractive market. In terms of scale of opportunity, I think it's probably a similar sort of scale of opportunity as, say, Italy or Spain, and remember, those are both businesses that four or five years into their existence are generating £10 million to £12 million of revenue.

We're obviously in talks in a number of other countries. We're at a slightly earlier stage in discussions with another regulator. I think it's now reasonably clear that they would be prepared to grant us a licence to offer CFDs to a retail audience. It's not yet quite clear what conditions they would attach to that licence in terms of restrictions on who we could offer them to or other restrictions we might have to apply to those clients. So until we've worked through those subjects with that regulator, we're not yet going to say who it is. I think in six months' time we'll have a good idea as to quite how that subject is panning out.

And then beyond that, we obviously continue to look at other countries, and indeed, to make it progressively easier for clients, or potential clients, who are in countries where we don't have an office to open accounts with us.

Slide 22: Nadex

Nadex obviously remains a long-term project, but a number of key initiatives should come to fruition over the next few months. We've finished Nadex Connect, which is our out-of-the-box software solution, which enables brokers or, technically, FCMs, to connect up to Nadex in a very simple, easy fashion, and then to offer those products to their clients. We're actively in discussions with about half a dozen brokers, and we won't necessarily get all of those over the line, but I'm reasonably optimistic that within the next few months we will have at least one broker connected up to Nadex.

You'll recall that at the moment IG is the only market maker on Nadex. We are talking to a couple of potential market makers, and again, we're reasonably confident that before too long we'll add at least one more market maker. There are obvious advantages to the clients in terms of greater liquidity and narrower spreads, and over time that should make the market more attractive to active traders; it should drive increasing volumes.

And then the final initiative is that we are continually improving our offering, and that includes rolling out a full suite of improved mobile apps across all of the main devices.

All of this taking place against a very beneficial regulatory backdrop. The CFTC has been clamping down on illegal offerings of OTC binary options to retail clients. And it is now very clear that Nadex is currently the only legal way that a US resident can trade binary options.

As you can see, strong steady growth in both numbers of members and in volumes. Revenue was up 85%, albeit from a very low base; however revenue for the first half still only £1.4m. Roughly speaking we've got to double the number of active accounts before we achieve profitability; and clearly that's not the limit of our ambitions in the US.

Slide 23: Online Stockbroking

As I said earlier, a key ambition is to address the needs of active retail traders, and over time become the default way in which active retail traders access the financial markets. And the initiative of launching online stockbroking is clearly a key plank in that ambition. If you think about where we started from we already had a number of the key building blocks needed for a really good stockbroking offering, because we were already offering equities in a more complicated fashion via spread betting or CFDs. So, we already had real-time pricing, streaming pricing sourced from multiple execution venues so that we could stream the best possible prices. We already had smart order routing so that client orders could be routed virtually instantaneously into the best possible execution venue. We were already able to offer our clients the ability to see market depth and to interact with the exchange order book. All of those things are very attractive to high volume active traders; and they're all things that aren't offered by the online stockbrokers here in the UK.

What we didn't have is the basic infrastructure needed to offer stockbroking. So we've been building that over the last year or so in terms of putting in place custody arrangements, settlement, client accounting and all of those sorts of things. And we're at a point where we're now testing that infrastructure. The remaining step in the development is to add these products into our front end, that's both web and obviously mobile. And that is work that we'll be doing over the next few months.

We see this project going live in the autumn of this year, and that will very much be a UK only offering.

In terms of who we're trying to target with this, really two main audiences: First of all existing spread betting and CFD traders. Something like 70% of all our clients have an online stockbroking account, and whenever we've questioned them the answer has come back that they'd be very interested in using a stockbroking offering from us, particularly if we give them the ability to use that long-term share portfolio as collateral against their short-term trading.

The second target market is people who are active traders but trading in cash equities rather than using spread betting or CFDs, and there is quite a large number of those. And I think they're doing that for one of two reasons: either because they're not fully aware of the benefits of spread betting and CFDs, particularly the availability of leverage, the ability to avoid stamp duty; or alternatively that they don't have the risk appetite for those products, probably because they don't have the risk appetite for leverage.

We're clearly interested in both of those targets, but for slightly different reasons. The first group we see as a conversion or an upselling opportunity, because ultimately we would like to have them as spread betting and CFD clients. The second group we think are valuable in their own right. But I would emphasise that we're very much targeting the active trader and the offering will be structured accordingly. We're not really targeting the person who only does long-term buy and hold and doesn't actively trade.

So I think in summary we see benefit here, not just in the stockbroking revenue line in the future, but also a benefit to our spread betting and CFD revenue.

In terms of the scale of opportunity I think we'd be reasonably happy or at least reasonably content if in five years' time the stockbroking revenue line was something like 5% of Group revenues. Clearly it will take a while to build to that sort of level. Predicting what the uplift might be on spread betting and CFDs I think is much harder at this stage.

Slide 24: Summary

So just in conclusion I think this is a satisfactory set of results against a very subdued market backdrop. We have achieved good levels of both revenue and particularly profit growth but that does need to be considered in the light of relatively weak comparatives; and certainly from now on comparatives become progressively more challenging.

We've made good progress on a number of long-term initiatives to drive longer-term future revenues and to broaden the appeal of IG to a wider range of active retail traders; but these are mainly long-term initiatives. Near term I think the key driver of growth will continue to be the development of our existing markets particularly some of the newer markets across Europe.

As we've said many times before, we are a market leader, and our market leadership is reinforced by strong cash generation, the positioning of our brand and continuous delivery on these new initiatives.

And then finally just to touch on current trading; we are really only a few weeks into the second half, and that period does include Christmas, so it's very hard to draw any conclusions from that early period. However December was a good month.

With that I will open it up to questions.

Question and Answer session

Question 1

Cormac Leech – Liberum

First thing that stuck me was, if I joined the dots correctly, it looks like the costs might be around 100m in the second half. I think you previously guided costs might be of 20m year-on-year; and then today I think you said that might come back a few million – so you're up roughly 14m, 15m on 176 of costs for 2013. And then you take away the 90 you get to about 100m for the second half. And then looking at the revenues in the first half relative to consensus it looks like you've got your work cut out for you to hit the implied consensus for the second half of probably around 198. I think it implies 8% half-on-half increase. I'm just wondering how comfortable you feel with consensus. If my maths are right it looks like PBT maybe is going backwards year-on-year most likely.

The broader question there is you seem to be doing a lot of heavy lifting at the moment, which will drive the business forward over the next couple of years, but will be a drag on near-term earnings. Longer term when can we start to see the business growing double-digit top line growth? It strikes me that this franchise should be able to grow its revenues consistently 10% plus year-on-year.

Answer: Christopher Hill

Let me take the cost question. When you're talking about cost you're including depreciation and amortisation that's the number you're coming to. Operating cost last year 163 plus the 20 gets you to 183. And you're right what I clearly said was I guided the 20, and we're going to be a few million down on that.

And as far as revenue is concerned, Tim and I have clearly said the second half is a challenge. Do we think we can do it? Yes, we do. But we're clear that revenue visibility over the short term is very difficult. And that is precisely why the initiatives that Tim has been through all of which we're doing is to drive the longer-term growth of the business. I think Tim gave a fairly clear steer as to what we thought would be a reasonable outcome for stockbroking over a period.

Further question

Is it fair to say that that will be the main driver of incremental growth? Because the active customer base is shrinking for quite a few periods now. I suppose the follow-on question might be: when will the active customer base on the CFD and spread betting side stop shrinking, as it were, as you stop shifting towards higher ARPU customers?

Answer: Christopher Hill

Two things: one is we were clearly talking about the growth that is there to come through in Europe. So, we pushed Europe out; the business is there; they've just posted some strong numbers. And we see Europe as being an opportunity continuing to grow.

Secondly, in terms of active clients Tim has pointed to how the management action that we're taking is having an impact on the mix of clients. And that has an impact on the level of active clients and the level of revenue per client that you're seeing. And our focus is around active clients, because active clients are the ones that drive volume and it's the volume that drives the revenue. So it's a focus on the active clients.

<u>Question 2</u>

Hugo Mills – Citigroup

Just to build on Europe, can you give us a bit more granularity I guess particularly to France and Germany as to how things are going there?

And secondly, Tim, just on the shares story; two questions there. One is, who do you see as your most direct competitors out there? And secondly, 5%, five years out, if I heard you right, seems relatively cautious to my mind.

Answer: Tim Howkins

Both France and Germany grew. Germany was the stronger growing in the period. But if you look at their history over the five years they've both been in existence they have constantly flip-flopped in terms of which was the faster growing. I don't read anything particular into the fact that Germany is currently growing faster than France.

Sorry, your second question was?

Hugo Mills

Around the shares competition and also ambition, I guess.

Answer: Tim Howkins

The UK online stockbroking market is dominated by Hargreave Lansdown, Barclays Stockbrokers and one other, which I think is TD Waterhouse. The three of them have the majority of that market. I think all of them are pitching their offering principally at long-term buy and hold investors rather than the very active trader. Some of them will offer streaming live prices but the offering is relatively limited compared to what we plan to offer.

Further question

Sorry, just to come back to Europe; the competitive landscape, has that changed at all?

Answer: Tim Howkins

No, I think the position remains as it has been. In Germany CMC remain somewhat ahead of us. There are some signs that we're closing that gap slowly. Generally across Europe the market is more fragmented than it is in either the UK or in Australia.

<u>Question 3</u>

Arnaud Giblat – UBS

I've got three questions please. Firstly on the equity stockbroking. Previously you indicated I think that a lot of the costs to set up that business have already been incurred from an IT expenditure side. Are we going to see the cost base inflate further from further developing this?

Secondly, on your ambition to achieve a 5% share of revenues from stockbroking; could you maybe outline the assumptions behind that? What sort of conversion rate are you looking at for putting existing clients on CFD for example into equity stockbroking, converting that into your business?

Thirdly, could you maybe comment on Boursorama and Comdirect? It seems as though they have been more active in offering CFDs. Have you seen more of their clients take up CFD activity and maybe longer-term perhaps converting towards an IG offering?

Answer: Christopher Hill

On the first question, stock broking and the costs incurred; most of the development cost is involved with IT development as Tim said in terms of the platforms. You've got to remember, we are going through a test phase and Tim's outlined the timetable that we're working on. So inevitably when you get to operationalise this you then have operating costs that you will then incur; and the challenge then will be around what it is that we use the development heads as far as IT is concerned. So you have a switch of costs. But inevitably when you operationalise this, and then depending on what happens to the scale, you have an impact on the cost. But in terms of the IT development, that's all contained in what we've been doing.

Answer: Tim Howkins

In terms of the detailed assumptions underlying our 5% in five years, I think it's just too early to talk about that. This is a business line that we're not even going to launch for another nine or ten months, so I think it's a little bit premature to be giving a forecast for six years hence and detailed modelling assumptions underpinning that.

In terms of Boursorama and Comdirect, yes both have been offering CFDs now for some time, Comdirect for a couple of years, Boursorama for probably about getting on for a year now. I think both of those, because they are stockbrokers with a big installed base, they have been successful at bringing more clients into the industry and raising awareness of CFDs in both France and Germany. Long-term I think that's beneficial. If you look at the short-term impact in terms of market share measured by number of clients, all of the existing CFD providers in Germany certainly saw a percentage point or so reduction in market share when Comdirect came into the market. I suspect if you looked at it in value of client terms you'd see a very different picture because it's inevitable, I think, that the clients who are with those online brokers are likely to be less active than the ones who have made a conscious decision to go to a specialist CFD provider. But I think long-term the fact that those players have entered the market is good because it helps to legitimatise the product and raise awareness of the product.

<u>**Question 4**</u>

James Hollins – Investec

A few from me. The first one's on Switzerland. Perhaps you could give us some guidance on what the office costs will be in H2 pre-revenue, and maybe what they'll be in full year '15? And on that, you seem super bullish you'll get a licence, it's fairly obviously you seem bullish. What sort of hoops do you have to go through to make sure that is the case?

The second one is just pushing on a question earlier, it was about the client declines. Clearly this is a strategic thing and one I think I get. In terms of looking forward I assume the declines will continue for the rest of this year. In terms of that strategy rolling out, would we expect active client declines next year as well, or does it start to sort of grow again?

And the final one is just on does the UK stock broking business change your capital commitments and regulatory stance for the business as a whole?

Answer: Christopher Hill

Thanks James. In terms of Switzerland costs going into the second half, it's a couple of million, which essentially we'll extrapolate into a full year number. The number I would reserve the right on is the level of marketing spend, which I think inevitably as that office gets up and running you'd expect us to spend more on that.

And then in terms of what hoops do you have to go through in order to get a licence, there are an awful lot of hoops that we have had to go through, and we've had to design how the entity will work. We've also had to start employing some of the heads. And you have to have that up and running to have a full review by the regulator, which we are in the process of doing. And obviously the final word rests with the regulator, but as far as we are concerned we are doing everything that we need to do in order to get it across the line.

Your second question on clients, and yes you're right. By focusing on active clients it gives us some discipline when we are focusing our levels of discretionary spend, being where we put our IT development in and how we roll out the marketing; and inevitably as Tim is showing, it's having an impact on the mix and that will take some time to come through. It's actually quite difficult to say to you when I think that will all have wound through, because you've obviously got the short-term volatility in the markets and the active clients that then come back to trade, so it's difficult to see. I do take the overall point that it bottoms out at some stage. It's very difficult to point to exactly when.

Then your third question around capital commitments for stock broking, does that have an impact on the Group as a whole? Pretty insignificant really because we act essentially as an agent when we are doing the stock broking business, whereas we are trading as principal in the markets when we're doing our leveraged trading.

Question 5

Richard Taylor – Barclays

Three questions please. First on Switzerland. Traditionally when you've gone into markets it's very clear that there's been a regulatory change that allows you to operate. Has anything changed in Switzerland for you to address this market? You say it's quite greenfield, so who else is there, and why are they are there already if you're not?

Secondly, a repeat question I'm afraid on actives down 5% overall. Can we push for you a number as to what that would be if you didn't try and get rid of some of the clients at the lower end?

And finally, the move to the IG.com domain name, how much do you think that is holding you back as well from signing up more actives?

Answer: Tim Howkins

Dealing with the first one, no there hasn't been a regulatory change in Switzerland. It is a more complicated regulatory regime than any of the previous ones that we've applied for a licence under, and that's why it's relatively late in the day, we've taken the lowest hanging fruit first. And obviously for a number of years we've been focused on rolling out across Europe once MiFID allowed us to very easily passport across the EU, and then quite clearly Switzerland is not in the EU so that doesn't apply.

The main competitor in Switzerland is Swissquote. There was a Forex only provider who were fairly recently acquired by them, and then Saxo have a small presence there. But it's a relatively undeveloped market. We do actually have a reasonable number of clients already from Switzerland, some of whom deal with the UK business in English, some of whom deal with our German office in German, some of whom deal with the French office in French, and a handful of whom deal with the Italian office in Italy. So there is already a smear of Swiss revenue around the Group which gives us some confidence that, yeah, there is appetite for these products there.

Answer: Christopher Hill

Your question on active clients, I'll give you a cautious answer which you might expect. I suspect that active clients will be closer to flat if not slightly up. And the reason I'm making that call is you've got to remember in Japan we've got an absolute drop in numbers, that's not driven by the strategy it's just the numbers of clients in Japan is going down. In Australia that business is softer than the others because it went into the recession effectively later, it's taken longer to come out and consumer sentiment there is down. However, in Europe it's clearly a strong story. Maybe that will be slightly stronger but we've got good client growth there. I think in the UK when I look at the bandings of clients by value, the drop-off as we've said is very much in the low value, there's very slight growth in the top value. And then overall client numbers is also going to be impacted by Nadex because that's growing its client numbers. So we'll probably see a little bit a growth, but I'll probably hang off and just say flat.

Answer: Tim Howkins

And then your third question was about IG.com. Undoubtedly the switch to IG.com has had some impact on account opening. Certainly for a period we have ranked lower in natural search than we have historically. However, to some extent you can compensate for that by paying up for paid search so that you're still at the top of the page, so the impact isn't clear cut. And as we've rolled out progressively the different countries the impact on each country has been different, so the UK saw the longest impact in terms of low search engine rankings, the European countries which were the last to go onto IG.com saw a very, very quick recovery in terms of search engine rankings and are pretty much back to where they were. So it's quite a nuanced subject, but certainly there has been some short-term impact on account opening.

Further question

Just a follow up then. What proportion of account opening in the UK comes from natural search, or has it done historically?

Answer: Tim Howkins

That is a question which the finest minds in our marketing department struggle to answer. For the simple reason that actually the journey most clients take to IG is quite long and complicated and can play out over six months plus where a client researches the subject matter online, they go to some webinars, they look at few different providers, they talk to their friends, and clearly search is a component in that. Unless it comes quite late in the journey then you tend to under-measure it. So it's quite hard to say exactly what the impact is.

<u>Question 6</u>

Cormac Leech – Liberum

Can I invite you to comment on capital? When I look at your balance sheet it looks like to some extent you're using equity capital to fund some of your liquidity requirements in terms of posting margin to some of your counterparties. Is there any appetite on the Board to think about maybe funding some of that margin posting requirement through other types of financing like debt and maybe swap out some equity and potentially use it to do a buy-back?

Answer: Christopher Hill

I think one of the points you're missing is that it is a leveraged balance sheet because we're trading on margin, so average margin is about 12% so it is a leveraged balance sheet. And in the face of that we manage our liquidity in a very conservative way to make sure that the liquidity is available there to post margin, and it's posting broker margin which is impacted by what the clients are doing and what's going on in the market. And you have to be able to react to that very quickly, when the brokers called because the market's crashed, you need to post the liquidity very quickly. The way the business model subsequently works is then you'll start to have money coming off the client accounts because the market has moved, and therefore that's how we manage our liquidity. But in your question you're missing one element.

Closing comments: Tim Howkins

Good. Well if there are no further questions I think that brings the formal matters to an end.