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FXCM - Q4 2015 FXCM Inc Earnings Call

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CORPORATE PARTICIPANTS

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Robert Lande *FXCM Inc. - CFO*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome, to the fourth-quarter 2015 FXCM Inc. earnings conference call.

(Operator Instructions)

I would now like to introduce your host for today's conference, Ms. Jaclyn Klein, Communications and Investor Relations. Please go ahead.

Jaclyn Klein - *FXCM Inc. - Communications & IR*

Thanks, Operator.

Good afternoon, and thank you, for joining us for the FXCM fourth quarter 2015 earnings conference call. Joining me today, are Drew Niv, FXCM's Chief Executive Officer and Robert Lande, our Chief Financial Officer.

A live audio webcast, a copy of FXCM's earnings release, which was sent earlier this afternoon and presentation slides used during the conference call are all available at www.FXCM.com under the Investor Relations tab. A replay of this conference call will also be available later tonight on our website.

Before I turn the call over to Robert, I'd like to remind everyone that in today's remarks we will refer to certain non-GAAP financial measures included adjusted EBITDA. These measures should not be considered in, isolation from or as a substitute for measures prepared in accordance with Generally Accepted Accounting Principles.

Reconciliations of these non-GAAP financial measures to the most comparable measures and calculated and presented in accordance with GAAP are available in the earnings release on the Investor Relations portion of our website. As usual, this call is intended for investors and analysts and may not be reproduced in the media in whole or in part without express written consent of FXCM.

Drew Niv - *FXCM Inc. - CEO*

Before we begin, we'd like to remind everyone that the remarks that we provide today may contain forward-looking statements. These statements do not guarantee future performance and undue reliance should not be placed on them. These statements are based on current expectations of Management and involve inherent risks and uncertainties as could cause actual results to differ materially from those indicated in any forward-looking statement including risk associated with the events that took place in the currency markets on January 15, 2015, and our subsequent financing agreement.

As well as the cyber security incident that was reported in the press release on October 1, 2015, and those identified in the risk factors section of our annual report on Form 10-K filed with the SEC and available on our website as such factors may be updated from time to time in our SEC filings. FXCM assumes no obligation to update any forward-looking statements. With that, let's turn the call over to CFO, Robert Lande.

Robert Lande - *FXCM Inc. - CFO*

Thanks, Drew.

Turning to slide 3, highlights for Q4, 2015. On the financial side, it was a pretty good quarter for us. Net revenues from continuing operations were $67 million, that's up from $59.6 million in the quarter before. Our net loss from continuing and discontinued ops attributable to FXCM, was $105 million, or $19.29 a share. That's versus a profit of $73.6 million or $13.86 last quarter.

But as always, this includes a number of non-cash items and in this quarter, namely it was a $99.9 million non-cash loss on the derivative liability to do with the Leucadia Letter Agreement, as well as a $21.8 million of non-cash expenses, such as deferred interest amortization of debt, discount amortization of debt issuance costs and other depreciation and amortization. In essence, there was a fairly significant rise in the stock price in the fourth quarter and that ends up translating into a loss on the derivative liability, the way it's estimated its value.

Adjusted EBITDA for the quarter from continuing and discontinued ops, was $12.6 million, a decent improvement from $5.2 million sequentially. On the operating side, our revenue per million was $67 per million and that's the highest it's been in a couple of quarters, versus $56 million last quarter. I think that we've been getting better performance from the CFD desk and I would hope that has to do with launching enhanced CFDs as we will talk about in a little bit.

As well as our dealing desk initiative, as you can see at the bottom of the slide has now reached 16% of our retail volume is from dealing with desk initiative for smaller clients. That is the highest it's been since we launched it. That has favorable impact on revenue per million, as well. Retail volume in the quarter, was $956 million. That's down 2% sequentially.

Turning to the next slide, slide 4, our cash position is very similar to where it was last quarter. $207 million of operating cash versus $210 million at September 30. Together with discontinued operations, we had $240 million in operating cash at December 31. You can see the breakout in the table down below between continuing ops and disc ops and then combined.

Our regulatory capital position, our minimum capital requirements from continuing of discontinued ops was [$61 million, and we had $143 million] (corrected by company after the call) of capital in our regulated businesses. That's a surplus of $82 million, versus a surplus of $85 million last quarter.

Turning to slide 5, this graphically highlights some of the key metrics on our retail FX business. You can see in the top left chart, we did $14.7 billion a day in Q4, similar to Q3. But turning to the right, you can see the nice improvement in revenue per million going to $67 per million. Our daily average revenue trades in the bottom left, you can see was 501,000 a day and our volume mix was pretty unchanged from the prior quarter as you can see in the bottom right chart.

Turning to slide 6, and Drew will talk more about this in a bit. Post-January 15, we committed ourselves to a number of growth initiatives. We set them forth on the Q4 earnings call, and I think we've been able to execute well on those initiatives and demonstrate the strength of our core business. The big initiatives in the year that we had announced were to enhance our CFD offering with an agency-like offering, which we did launch in October, and that allows us to manage our flow much better.

We also have launched a beta version of CFDs on single shares such as Apple or individual shares, which is an important initiative for us. And I think that's going to be an important initiative, as well, in 2016. As always, we did a number of enhancements to our platform adding things like market depth and volume indicators, which are our really quite unique in our space and on our platform. And we launched the dealing desk, as well, for smaller clients.

Overall in the year, despite the events of January 15, and the hits to the business that we took following that, we did increase volume 10% to [$3.9 trillion] (corrected by company after the call), an 8% increase in our total active accounts. So 165,000 and daily average trades as well. All in all, we're happy with where we were able to achieve in the business.

On slide 7, this is the table where you can see the breakout of adjusted EBITDA between continuing operations. The adjustments we make then from GAAP to adjusted continuing operations. You can see then our discontinued operations and then combined. Last year, before the SNB event, Q4 2014, was a very strong quarter for us. We did $40.8 million in EBITDA, not really comparable to where we are today post SNB. But, you can see in the table that from our continuing ops, this past quarter, we were able now to generate $10 million in adjusted EBITDA, which I think portends well for 2016 and then [$2.6 million] (corrected by company after the call) from the remaining discontinued operations that are there; altogether, $12.6 million in adjusted combined EBITDA.

On slide 8, part of the story as it's been throughout the year, is cost control and our efforts on that. You can see our key operating expenses on the slide, see that at $56.97 million in the quarter, it was our lowest quarter in terms of operating expenses with some savings on compensation and benefits and referring broker fees driving that. You can expect us to continue to be vigilant on operating expenses as we manage the business post SNB.

On slide 9, before I turn things over to Drew, you can see our balance sheet between September 30, and December 31. The big items, you can see [$204 million] (corrected by company after the call) in operating cash, obviously. Our client equity was $685 million, down a little from the previous quarter at $713 million. Current assets held for sale are down quite a bit. That's in large part as we closed the sale of our equity brokerage business in the UK, FXCM Securities, and that had a fair amount of assets attributed to that.

On the right side of the page, you can see the derivative liability increased in the quarter. It's now $448 million, and that's pretty much the big change on the liability side. So with that, I'm going to turn things over to Drew to talk about the state of the business and as well take you through what we just announced today, which is strengthening and deepening of our relationship with Leucadia. Drew?

Drew Niv - *FXCM Inc. - CEO*

Thank you, Robert.

On slide 10, I'd like to start off by providing an update on the sale of non-core assets. So far, we have paid $117 million in principal due to Leucadia. We have $193 million remaining of the 300 notes from January 2015. You see that we have sold three of the six non-core assets we designated and we continue to market these actively.

It is still FXCM's number one priority to pay back the Leucadia debt. While FXCM believes it is possible to sell sufficient assets to payoff the credit agreement, Leucadia and FXCM concluded that greater value could be realized for all stakeholders through additional time to complete the asset sale. That is why Leucadia has proposed to amend the credit agreement and extend it by one year to mature in January of 2018.

Moving to slide 11, I'll walk you through the press release we sent today where Leucadia and FXCM announced that we've entered into a memorandum of understanding to amend the terms of our Amended and Restated Credit Agreement and our Amended and Restated Letter Agreement from January 2015. This MOU is non-binding and present and is subject to the execution of definitive agreements, as well as regulatory approval. We would expect to complete the amendments by June 2016.

As I mentioned on the previous slide, Leucadia has agreed to provide FXCM greater flexibility to accommodate a longer sales process for non-core assets to help realize potentially greater value for all shareholders. The proposed modifications include an extension of the term of the note by one year. It now matures in January 2018, instead of January 2017, as it is presently written.

In addition, FXCM will be given the right to defer any three of the remaining interest payments by paying interest in kind. These payments in kind allow FXCM to honor its debt obligation while maintaining maximum flexibility to invest and grow its core business. Until the loan and interest under the trade agreement are fully paid, all distributions of sales proceeds will continue to be used to repay the loan plus interest.

Moving to slide 12, as many of you know, the Letter Agreement reached with Leucadia last January is treated as a derivative liability on our balance sheet. The swings in the size of this liability, both positive and negative, can be quite large. Leucadia has agreed to convert a portion of the Letter Agreement rights into direct equity stake, which should reduce the size and volatility of the derivative liability. This is an example of Leucadia's commitment and support to FXCM, and their confidence in our core business. And it's particular important point we would like to stress to all FXCM customers and business partners.

Part of this restructuring, FXCM Newco will be renamed FXCM Group LLC. The previous Letter Agreement will be terminated and replaced by an agreement with FXCM Group. This agreement provides Leucadia a 49.9% common membership interest in FXCM Group, while FXCM Holdings retaining 50.1% common membership interest.

An eight member Board will be established for FXCM Group, consisting of three directors appointed by Leucadia. These are contemplated to be Richard Handler, Brian Friedman and Jimmy Hallac. Three directors will by appointed by FXCM. And two independent directors will be appointed, one to be nominated by Leucadia and one to be nominated by FXCM.

Consistent with our prior Letter Agreement, no distributions can be made until all loan and interest amounts are paid. Additionally, after January 2018, Leucadia and FXCM would each have the right to begin a process that could unwind the partnership, potentially resulting in a sales process for FXCM Group.

Finally, Leucadia and the Company have agreed to create long-term incentive plan with five-year vesting period for FXCM Senior Management to maximize cash flow generation and the growth of the business. Under this plan, FXCM Senior Management will receive 10% of FXCM Group distributions once all amounts under the loan are paid. When communal distributions after repaying of the loan and interest reach $350 million, FXCM Management share of distributions will increase from 10% to 12%. When communal distributions proposed loan repayment exceeds $850 million, FXCM Senior Management share of distribution will increase to 14%.

As we move to slide 13, the following table summarizes all of these changes from the original waterfall that was in place in the Letter Agreement January 2015. Keep in mind that the size of each tranche does not reflect the $117 million already paid against the note.

The first tranche represents a $300 million loan, plus any of the interest to Leucadia still receives 100% of all distributions until the note and all interest are paid. The second tranche, which represents the next $350 million in distribution, has been changed from a 50-50 split between Leucadia FXCM to go a three-way split, 45% to Leucadia, 45% to FXCM Group and 10% going to Senior Management.

The third tranche, which covers the next $500 million of distributions between $660 million and $1.15 billion, will be changed from the original split of 90% to Leucadia and 10% to FXCM, to 79.2% to Leucadia, 8.8% to FXCM and 12% to Management. The fourth and last tranche for distribution is above $1.15 billion. The split has been changed from 60% Leucadia, 40% FXCM, to 51.6% Leucadia, 34.4% FXCM, and 14% Management.

Moving to slide 14, as you can see here in this slide, we essentially show the old structure of FXCM and the new structure of FXCM today. FXCM Holdings is the holding company that holds all of the operating and the subsidiaries of FXCM, including its core and non-core assets. Inc was the majority shareholder and sole managing partner of FXCM Holdings, so that was the case before SNB. Post-SNB, FXCM Newco was created in the rescue deal between Leucadia and FXCM to capture all the proceeds so the debt can be paid off. That's in the middle. That's on the left-hand.

Post-restructuring on the right-hand side of the chart, essentially the new FXCM is FXCM Group. And that is the holding company that holds all of the operating subsidiaries with customers, employees, assets, the rest. That's obviously also the core and non-core assets.

FXCM Group as a private company as two public shareholders. One is Leucadia, and the other one is FXCM, the legacy FXCM Inc. and FXCM Holdings, with 51% of the vote going to FXCM and 49% of the vote going to Leucadia.

Moving to slide 15, FXCM has come a long way from the SNB event last January. Our continued operations as the core retail franchise has been a center of FXCM since its founding. It is a strong business that generate on average $64 million a year EBITDA over the prior four years. The environment for retail FX is improving and we have put into place a number of growth initiatives to advance the success of our core business.

Nonetheless, returning FXCM to a position where we can create meaningful value for all stakeholders is a great long-term proposition. We believe the revisions to the Agreement announced today demonstrate Leucadia's long-term commitment to this business and will be helpful in enabling us to move forward and deliver long-term value for all stakeholders. Our relationship with Leucadia is now moving forward in a form of a partnership.

Adding a partner with the financial strength of Leucadia will be a significant boost to FXCM's strength and stability and help us in our global efforts. Finally, we'll be changing FXCM Inc.'s name and its NYSE ticker and symbol to be determined, all these will be determined at a later date, to reflect the nature of the fact that FXCM Inc. is no longer the sole managing member and shareholder of FXCM. It is now one of two.

Turning to slide 16, our customer trading metrics. During the month of February, currency markets were choppy. Even though we had a handful of larger volume days in most major FX bearers during the month were largely confined within a broad range. That being said, year-over-year, despite selling retail entities during 2015, we continued to grow our core account base. The volume has increased and we continue to stabilize our business. I believe with the new initiatives we launched during 2015 and improved the environment for retail FX trading, along with the clarity and stability that the restricted agreements will bring FXCM, will continue to grow these metrics in the levels above where we were in January 15, of last year.

To summarize, on slide 17, since the SNB event in January 15, we're succeeding in stabilizing the business and paying a significant portion of the debt and launching a number of initiatives for growth. Our success is evident in the number of year-over-year metrics: customer loyalty and brand strength remains strong, retail volume increased 10%, active accounts increased 8%, and daily average trades increased 34%.

We've successfully rolled out our Dealing Desk offerings to small clients, which is nearly double the economics of our normal agency offering and has grown 16% of retail volume in the fourth quarter of 2015, our enhanced CFD offering launch in October has been gaining traction and we are targeting launch fully single share CFDs in 2016. We remain committed to successfully selling the non-core assets through the process that will take us longer for us to realize greater value.

Finally, Leucadia has demonstrated its commitment to FXCM by providing us a greater financial flexibility and taking a direct stake in our business, which we believe will help us immeasurably going forward. Thank you very much for joining us this afternoon, and have a great night. We look forward to speaking with you in the next conference call. Operator, we are finished.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program. You may all disconnect. Everyone, have a great day.
