

Interactive Brokers Group (IBKR)

Q2 2014 Results - Earnings Call Transcript

July 15, 2014

Executives

Thomas Peterffy - Chairman & CEO
Paul Brody - Group CFO
Debbie Liston - Director, IR

Analysts

Chris Harris - Wells Fargo
Rich Repetto - Sandler O'Neill
Niamh Alexander - Keefe, Bruyette & Woods
Mac Sykes – Gabelli
Sean Brown - Teton Capital
James Lee - Kylin Management

Operator

Good day, ladies and gentlemen, and welcome to the Interactive Brokers Group Incorporated Second Quarter Financial Results Call. (Operator Instructions) As a reminder, this conference is being recorded. I would now like to introduce the host for today's conference, Ms. Debbie Liston, Director of Investor Relations. Ma'am, you may begin.

Debbie Liston - Director, IR

Thank you, operator and welcome everyone. Hopefully, by now you've seen our second quarter earnings release, which is released today after market close, and which is also available on our website. Our speakers today are Thomas Peterffy, our Chairman and CEO; and Paul Brody, our Group CFO. They're going to start the call with some prepared remarks about the quarter and then we'll take some questions.

I just want to remind everybody that today's call might include forward-looking statements, which represent the company's belief regarding future events and by their nature are not certain and outside the company's control. Our actual results and financial condition may differ possibly materially from what's indicated in these forward-looking statements. We ask that you also refer to the disclaimers in our press release. You shall also review a description of the risk factors contained in our financial reports filed with the SEC.

And with that, I would like to turn the call over to Thomas Peterffy.

Thomas Peterffy - Chairman & CEO

Good afternoon, everyone, and thank you for joining us to review the second quarter performance. Compared to the first quarter, the market environment for our business was a bit more subdued, which is evident in our results for both segments.

The broad market theme in the second quarter was low volatility and lower trading volumes despite record market valuations. Accordingly, our client trading volumes, which are directly correlated with industry volumes, have come off the record-breaking highs we saw in the first quarter. Yet, despite the quieter trading environment, new customers continued to flock to our platform and our growth rates are continuing to outpace the industry.

This was, in fact, our second highest quarter for total number of new account additions with the first quarter taking the lead. And thanks to our efficient business model, we were still able to realize a robust pre-tax profit margin of 60%, despite the sequential decrease in commission revenues. We also continue to be the largest U.S. electronic broker by number of revenue trades due to our very active customer base, which is exactly the reason they choose us as their broker.

Trading actively, our customers' performance is greatly impacted by overall trading costs and given our low commissions and excellent executions, they do not have other alternatives but to come to us. The Flash Boys book that I discussed in detail last quarter has generated a great deal of discussion with our current and prospective clients, about a key point in the book which is the widely accepted practice of brokers selling their customers' order flow to firms that trade against it. IB does not engage in this practice, which is why we are able to deliver substantially better execution than our peers.

In the second half of 2013, when measuring average price improvement over the NBBO, IB achieved a \$0.23 advantage on average over the industry on 100 shares of stock and \$0.20 advantage on average over the industry per options contract.

This is because our Smart Routing technology, which continues to evolve and has by now become quite a complex but also a very effective piece of software. The key here is to understand that while overall some venues may give you better executions than others, you must route each order to the venue which will provide a probable best execution for that specific order at that specific instance.

For example, in certain instances, the best price may be at the dark pool that also pays a rebate, half of which we pass back to our customers further improving their execution.

We've also started running advertisements to emphasize our stance with respect to payment for order flow. We want to be sure that customers of those brokerage firms that do engage in this practice understand that their broker's primary objective is not to maximize their execution quality, but rather to maximize the firm's own revenues. These firms get paid hundreds of millions of dollars a year in payment for order flow.

Last week, it was announced that following the SEC investigations of broker dealers, an additional 10 Brokers received sweep letters from FINRA, asking a large number of questions about order routing, payment for orderflow and controls of execution quality. We were happy to be one of the 10 firms who received this letter because we hope that this will give the regulators

an opportunity to compare the differences between our policies and that of other firms and eventually lead to some favorable publicity for us.

We go to great lengths to provide our customers with the best possible price and the lowest transaction cost in order to help them maximize their returns. We have always believed this was the key to growing our business and as our results show, this has been a very successful strategy that we will continue to maintain.

There have also been recent media reports that the SEC is looking at forcing trading away from dark pools. We do not believe that all trading in dark pools is bad, in fact, as I mentioned earlier, our customers can often get a better price in a dark pool. Lastly, in connection with this topic, we are working on generating some statistical measures that once and for all would definitively demonstrate the total cost of execution our customers pay and the categories that make up those expenses.

We expect to be able to release these results as part of our monthly brokerage metrics in sufficient detail, so that other brokers will be able to perform the same calculations and compare their results to ours, although I doubt that they would want to release them without the SEC mandating that they do so.

Now, before I get into the segment details, I'd like to give you an overall picture of our second quarter results before any currency or tax effects.

For the quarter we reported pretax income of \$174 million. Excluding currency effects this was \$159 million, composed of \$131 million of Brokerage, \$31 million in Market Making and a loss of \$3 million in Corporate.

Now I'd like to review the performance of our brokerage segment.

As I discussed earlier, this was a softer quarter for global trading volumes compared to the first quarter and the year ago quarter. However, on a year over year basis, our total customer DARTs rose 5% compared to the second quarter of 2013.

Despite this modest increase in DARTs, our commission revenue fell 10% year over year. This is because the average commission per DART fell 11% during the same period. This decrease was due to a number of factors, the dominant one being smaller number of shares in the average stock trade but also a shift in product mix and larger institutional customers getting the benefit of lower price tiers with higher monthly volume. In terms of product mix, there has been a large increase in customers trading low-priced stocks, and because we cap our commission at .5% of trade value, our platform is an attractive venue for investors trading these products.

In terms of account growth, as I mentioned, we had the second highest number of quarterly account additions in Q2 of 10,600, finishing the quarter with 262,000 accounts, which represents a 17% year-over-year increase, or 19% annualized for the first half of the year. It's very encouraging to see this momentum in account growth, which can widely be attributed to strong word-of-mouth referrals and our growing brand awareness which is largely associated

with being a platform that offers high value through low transaction costs, execution quality and state-of-the-art trading technology.

This account growth is geographically diversified, with 60% of new accounts coming from outside the U.S. We're seeing an ever growing number of international investors who seek low cost access to US and other markets and in almost all cases, we can offer this access at much lower costs than the local brokers.

Our total customer equity is now \$54 billion, a 44% annual increase, while the average equity per account has increased 23% to \$206,000. This trend is driven by faster growth amongst institutional accounts that bring larger accounts to IB, including hedge funds, independent advisors with very high net worth clients and proprietary trading firms. Nevertheless, in spite of these large accounts, the average account is still small. This is illustrated by the median account balance, which is \$26 thousand. Splitting the universe of accounts into two halves, the average of the lower half is around \$13,000 and the average of the higher is around \$400,000. It's also useful to know that largest 100 accounts have a combined balance of slightly in excess of \$10 billion.

Margin balances rose to a new high of \$15.4 billion thanks to our industry-low margin lending rates, which for U.S. dollar loans currently range from half of one percent to 1.6% depending on the size of the loan. Margin as a percent of customer equity has stayed pretty consistent, currently at 29%.

We started publishing additional regulatory financial data on our website where customers can view daily information about our customers' segregated capital and our excess regulatory capital going back for one year. While some of this is now required under new CFTC rules, we went beyond the minimum reporting requirements as we are happy to show how well capitalized we are and how we protect our customers' money. This information can be found on our website under "About IB" and "IB Regulatory Reports".

Now I will review the performance of our Market Making segment.

Market making pretax profits totaled \$46 million compared to a gain of \$8 million in the year ago quarter and \$88 million in the prior quarter. However, if we back out the currency effects, we have a clearer picture of our performance. As I mentioned earlier, this period's trading gains were positively impacted by a translation gain of \$15 million. After backing this out, pretax market making profits totaled \$31 million, compared to \$50 million in the year ago quarter and \$67 million in the prior quarter.

As I mentioned, the environment for market making deteriorated in the second quarter which is evidenced by this performance.

Volatility levels, which are directly correlated with our market making trading gains, reached the lowest quarterly average since the first quarter of 2007. This quarter the average VIX totaled 12.8, 14% lower than the prior quarter and 14% lower than the year ago quarter. In addition, the ratio of actual to implied volatility, which impacts our profit captured versus our cost of hedging, fell to 73% this quarter, compared to 81% in the prior quarter and 95% in the year ago quarter.

According to data obtained from the exchanges where we do business, exchange traded options volumes decreased 9% in the U.S. and 7% globally for the second quarter. By comparison, our firm's total option volume decreased by 10% and as a result our firm's market share fell slightly from 11.6% to 11.4% in the U.S., and fell from 9.0% to 8.7% globally.

This decrease in overall market share is due to the combination of our continuing relative shrinkage of our market making volume offset by the continuing relative expansion of our brokerage volume.

In the market making segment alone our option volume decreased by 12% during the second quarter, driving our market share down from 5.3% to 5.1% in the US and from 5.0% to 4.7% globally.

We continue to pay a 10 cent quarterly dividend from market making capital. This quarter, we earned an 8% return on equity, below our 10% hurdle rate, and as such we naturally reduced capital in this segment.

As you know, I have been very vocal about market structure, and you may have heard about my proposal that I submitted to the SEC in May with my recommendations for how to level the playing field between HFT's and investors. There has been extensive debate about whether HFT's are harmful or beneficial to the markets but the fact is, they can be both. HFT's that add liquidity and facilitate price discovery are beneficial to the financial markets. However, we must end abusive HFT trading, which is why I am proposing to slow down all liquidity removing orders on all U.S. exchanges by a random period ranging from 10 to 200 milliseconds before releasing the order to the matching engine. This would not only prevent HFTs from front running investors, it would reduce price volatility and mini crashes. There have been other proposals to address these issues but I don't believe the solution is to rebuild market structure or introduce more regulations. My simple proposal would be very effective and eliminate these problems.

I'm optimistic that regulators will be focusing their efforts on these issues and I think any outcome that leads to a reduction in predatory trading and enforcement of brokerage and advisory fiduciary duties would be very beneficial to small and large investors alike and therefore to our business.

And now, here is CFO, Paul Brody.

Paul Brody - Group CFO

Thank you, Thomas. Thanks everyone for joining the call today. As usual, I'll first review the summary results and then give segment highlights before we take questions. Following the strong first quarter performance, second results were off in both Brokerage and Market Making, generally in line with the subdued market volumes.

However, the year-over-year comparison showed certain favorable factors. As compared to the year-ago quarter, the drop in Brokerage segment commission revenues was more than offset by higher net interest income. In addition, a shift to the currency translation gains on the weaker U.S. dollar set higher trading gains in the Market Making segment.

Our financial results include the GAAP accounting presentation known as comprehensive income. Comprehensive income reports all currency translation gains and losses, including those that reflect changes in the U.S. dollar value of the company's non-U.S. subsidiaries that's known as other comprehensive income or OCI.

These are reported in the statement of comprehensive income. With a few exceptions, the U.S. dollar weakened relative to other currencies during the second quarter of 2014. As a result, the currency basket in which we keep our equity, which we call the GLOBAL, strengthened against the U.S. dollar by 0.5%.

OCI is a component of the total GLOBAL effect and the rest is contained in trading gains. We estimate the total GLOBAL effect on our reported earnings per share for the quarter to be \$0.05 with \$0.03 reported as OCI and \$0.02 as trading gains.

Overall operating metrics for the latest quarter were mixed, volumes were up in stocks and down in options and futures versus the year ago quarter. Average overall trading volume was 1.08 million trades per day, down 2% from the second quarter of 2013.

Electronic Brokerage metrics showed solid increases in the number of customer accounts and customer equity. Total and cleared customer DARTs were both up 5% from the year ago quarter though down sequentially. Orders from cleared customers who clear and carry their positions in cash with us accounted for 91% of total DARTs holding steady with recent quarters.

Market Making trade volume was down from the prior year quarter, as were contract and share volumes across product types. Other metrics were generally negative as the level of volatility and the actual to implied volatility ratio were both down this quarter. However, Market Making results were aided by currency movements this quarter.

Net revenues were \$309 million for the second quarter, down 13% from the year ago quarter. Trading gains were \$84 million for the quarter assisted by the currency translation effects. While trading gains compared to the year ago quarter increased by 42%, excluding the currency translation, trading gains would have fallen by 32% from the year ago results.

Commissions and execution fees were \$124 million, down 10%. Net interest income was \$83 million, up 33% from the second quarter of 2013 and Brokerage produced \$77 million of that and Market Making \$6 million. Other income was \$18 million, down 26%.

Non-interest expenses were \$135 million, down 10% from the year ago quarter. Within the non-interest expense category, execution and clearing expenses totaled \$52 million, down 20% from the year ago quarter, driven by lower volumes in both segments.

Compensation expenses were \$54 million, an 8% decrease from the year ago quarter. At June 30, our total headcount was 922, an increase of 3% from the year ago quarter and 5% from the prior year-end. Within the operating segment, we continue to add staff in Brokerage and cut back in Market Making.

As a percentage of net revenues, total non-interest expenses dropped to 44% from 53% in the year ago quarter. Out of this number, execution and clearing expense accounted for 17% and compensation expense accounted for 17%. Our fixed expenses were 27% of net revenues.

Pre-tax income was \$174 million, up 30% from the same quarter last year. For the quarter, Brokerage accounted for 74% and Market Making 26% of the combined pre-tax income. Ex-currency effects, the contributions were 81% for Brokerage and 19% for Market Making.

For the second quarter, our overall pre-tax profit margin was 56% as compared to 47% in the second quarter last year. Brokerage pre-tax profit margin was 60%, up from 58% in the year ago quarter. Market Making pre-tax profit margin was 51%, up from 11% in the year ago quarter and excluding translation effects, Market Making pre-tax profit margin was 41% in the latest quarter.

Comprehensive diluted earnings per share were \$0.29 for the quarter as compared to \$0.14 for the second quarter of 2013. On a non-comprehensive basis, which excludes OCI, diluted earnings per share on net income were \$0.26 for the quarter as compared to \$0.21 for the same period in 2013.

Turning to the balance sheet, as a result of the growth of our Brokerage business and the withdrawal of capital from our Market Making operations through regular and special dividends, Brokerage now accounts for about 74% of our combined balance sheet assets from the two segments. From the year ago quarter, cash and security segregated for customers rose 22% and secured margin lending to customers rose 35%, while positions in securities held by our Market Maker units were paired back by 27%.

According to our announced policy, regular quarterly dividends will continue to temper the capital employed in the Market Making segment. In the second quarter, our Market Making earnings fell short of the amount needed to fund the dividend.

Our balance sheet remains highly liquid with low leverage. We actively manage our excess liquidity and we maintain significant borrowing facilities through the securities lending markets and with banks. As a general practice, we hold an amount of cash on hand that provides us with a buffer should we need immediately available funds for any reasons. At June 30, we maintained over \$3 billion in excess regulatory capital in our broker dealer companies around the world, of which about 64% is in the Brokerage segment.

We continue to carry no long-term debt. And our consolidated equity capital at June 30, 2014 was \$5.28 billion, of which approximately \$2.7 billion was held in Brokerage, \$2.3 billion in Market Making and the remainder in the corporate segment.

Segment operating results are summarized in the earnings release and will be more fully detailed in our quarterly 10-Q report. So I'll just highlight the noteworthy items. Starting with Electronic Brokerage, customer trade volumes were mixed across the product types, down in options and futures but up in stocks.

However, cleared customer options contract volume was up 8%, while futures contract volume was down 16%. A decline in foreign exchange volume also contributed to the overall reduction. In contrast, stock share volume was up 66% from the year ago quarter, and while much of this increase came from trading in low price stocks, volume also increased in other stocks.

Customer accounts grew by 17% over the total at June 30, 2013 and by 4% in the latest quarter. Total customer DARTs were 529,000, up 5% from the year ago quarter but down 9% from the first quarter of 2014. Our cleared customer DARTs were 484,000, also up 5% on the year ago quarter but down 8% sequentially. The average number of DARTs per account on an annualized basis was 473, down 10% from the 2013 period and 12% sequentially.

Commission revenue fell on a product mix that featured larger average trade sizes in futures and stocks and smaller in options. This resulted in an overall average cleared commission per DART of \$4.07 for the quarter, lower by 11% from the year ago quarter and 2% sequentially. As Thomas mentioned, large volume executed in low price stocks on which our commission is capped, can skew these numbers somewhat. Also, note that our commissions include exchange fees which can vary widely.

Customer equity grew to \$53.9 billion, up 44% from June 30, 2013 and up 10% sequentially, well outpacing the S&P 500 index which rose 22% over the past year and 5% over the last quarter. The source of this growth continues to be a steady inflow of new and larger accounts and customer deposits, as well as customer profit. Margin debits continue to build steadily, increasing 38% over the year ago quarter.

Customer credit balances also continue to grow progressively, increasing 20% over the year ago quarter, though spread compression persists in restraining net interest income. Lower options and futures trade volumes resulted in top line revenue from commissions and execution fees of \$124 million, a decrease of 10% from the year ago quarter and 9% sequentially. These revenues are mainly spread across options, futures, stocks and foreign exchange.

Net interest income rose to \$77 million, up 32% from the second quarter of 2013 and 16% sequentially. Low benchmark interest rates, which continue to compress the spreads earned by our Brokerage unit, have been offset by steadily higher customer credit balances in each successive period. And our aggressive lending rates continue to boost customer margin borrowing.

Our fully paid stock yield enhancement program continues to provide an additional source of interest revenue that is shared with our participating customers. Net interest income, as a percentage of net revenues, rose to 35% as our brokerage revenues are increasingly diversified between commissions and net interest income.

With a growing customer asset base, we believe we're well positioned to benefit from a rise in interest rates. Based on current balances, we estimate that a general rise in overnight interest rates to 25 basis points would produce an additional \$62 million in net interest income annually. Further increases in rates would produce smaller gains, because the interest we pay to our customers is pegged to benchmark rates, less the narrow spreads.

Execution and clearing fees expenses decreased to \$35 million for the quarter, down 14% from the year ago quarter and 6% sequentially, reflecting lower trading volumes. Fixed expenses increased to \$54 million, up 12% on the year ago quarter. And pre-tax income from Electronic Brokerage was \$131 million for the second quarter, up 7% on the year ago quarter and down 2% sequentially.

Now, looking at Market Making, the trade volume was down 21% from the prior year quarter, spread across the product types. Options and futures contract volumes were down 33% and 23%, respectively and stock share volume was down 27%. Trading gains from Market Making for the second quarter of 2014 were \$84 million, up 42% on the year ago quarter. Currency translation effects positively impacted the second quarter's reported earnings by \$15 million, a substantial swing from the year ago quarter when reported earnings were decreased by \$43 million.

Our overall equity, as measured in U.S. dollars, was increased by the weakening of the U.S. dollar against most other currencies. More specifically we measure the overall gain from our strategy of carrying our equity in proportion to the basket of currencies, we call the GLOBAL, to be about \$26 million for the quarter. Because an \$11 million translation gain is reported as other comprehensive income, this leads a gain of \$15 million to be included in reported earnings.

To summarize this, if we eliminated all currency effects, pre-tax income from Market Making for the second quarter of 2014 would be about \$31 million versus \$50 million for the year ago quarter on the same basis.

Execution and clearing fees expenses fell to \$17 million for the quarter, down 33% on the year ago quarter, driven by lower trading volumes, primarily in options. Fixed expenses were \$29 million, down 18% from the year ago quarter, primarily due to our devoting fewer software development resources to this segment. We've continued our aggressive expense management as we monitor the performance of the Market Making business.

Pre-tax income from Market Making was \$47 million for the quarter, up 512% from the year ago quarter. Taking into account the currency effects from each period, the year-over-year change in pre-tax income from Market Making would be a decrease of 38%.

Now, I will turn the call back over to the moderator and we will take questions.

Question-And-Answer Session

Operator

Thank you. (Operator Instructions) Our first question comes from the line of Chris Harris with Wells Fargo. Your line is now open.

Chris Harris - Wells Fargo

Thanks. Hey, guys. So a few questions, I guess, on the margin. Maybe starting in Brokerage, I was kind of curious to get your thoughts, we've been at 60% margin here for the last couple of

quarters. Do you think that there's a lot more room to grow the margin in Brokerage from here or is this kind of likely to be kind of the high point we see that Interactive Brokerage is able to do?

Thomas Peterffy - Chairman & CEO

I think it's going to go in steps. If anything, I would in the near future expect a slight drop in margins as we add to expenses, having to do with adding more people, especially on the sales and customer service and we keep trying to ratchet up the increases in new accounts and new money, the new volume and as we expand the expenses, they are going to be less gradual.

Chris Harris - Wells Fargo

Okay. That was going to be my follow-up question.

Thomas Peterffy - Chairman & CEO

I think ultimately we could approach 70%, but that's probably two, three years down the road.

Chris Harris - Wells Fargo

Okay. Yeah, because your expenses in that segment were flat quarter-on-quarter and year-on-year which was kind of surprising given all the hiring you've been doing or the growth in that segment, and so maybe you've got a little bit of pressure in the back end of this year as far as incremental expenses coming on.

Thomas Peterffy - Chairman & CEO

We lowered some expenses on the Market Making side and they are more expensive people.

Chris Harris - Wells Fargo

Okay. All right. Then kind of in the Market Making, kind of wondering about you did have a big drop in revenues. We know the reasons why. You guys did a good job of laying that out, but really no movement on the expense side of the ledger so maybe you didn't have enough time to kind of right-size the expense given the fall-off in revenue. Assuming that the environment stays as it is, which obviously is pretty bad, is there more room to kind of take some costs out of that business from here or do you feel like you're running pretty lean today in that segment?

Paul Brody - Group CFO

Actually, Chris, we've been right-sizing for some time now, well over a year, maybe close to two years. We steadily dropped the compensation costs. That showed up certainly in the year-over-year figures and in the headcount. And other expenses are pretty aggressively managed in terms of general administrative and so forth and as I mentioned in my part, less expense is devoted toward software development on the Market Making side. Is there more room? Yes. There's more room, but we're in a monitoring mode to see how well this business does.

Thomas Peterffy - Chairman & CEO

You see -- it would be incorrect to believe that we have completely given up on working on getting our Market Making better. We are still working on that, but I assume so did everybody else. So as you're well aware, we don't see into the operations of other folks who are basically not publicly owned organizations. But I think that in order to at least keep pace with others, we have to keep on spending money on programming these things.

Chris Harris - Wells Fargo

Okay. Understood. And really just the last one from me, real quick. The commission per DART, you guys kind of laid out some of the reasons for the decline there. It's kind of a challenge for us to model this because the number tends to be really all over the map. But what I'm trying to figure out is some of the decline we have seen over the last year, I know you started against a very difficult compare, if you go back a few quarters but is a lower level maybe reasonable to assume for you guys going forward? I just don't know if any of the changes that you've had in customer mix over the last few years or other factors might make a lower revenue capture kind of more of the norm for you than not.

Thomas Peterffy - Chairman & CEO

We're almost as puzzled as you are. So we just -- for example, quite recently discovered a hole that we didn't put too much money down on, but as we said here during the conference, we have this maximum commission which is 0.5% of trade volume and we also have commission tiers which go by number of shares. So we discovered a customer every month who started out with doing hundreds of millions of company shares, which immediately put him in the lowest volume category, commission tier category, and then he was trading for practically nothing.

Chris Harris - Wells Fargo

Got it. Okay. Thank you very much, guys.

Operator

Our next question comes from the line of Rich Repetto with Sandler O'Neill. Your line is now open.

Rich Repetto - Sandler O'Neill

So on the Brokerage segment, I guess one thing that, well, first do we just change that pricing structure or is it going to stay the same that you just talked about.

Thomas Peterffy - Chairman & CEO

Of course, we changed it. Yes, definitely. We will no longer count the trades on which we kept the commissions as part of the tier.

Rich Repetto - Sandler O'Neill

Got it. And then the next – you talked about investment in sales and customer service, I don't know, Paul, can you give us a feel for what we might see in increased expenses in the second half or on an annualized basis?

Thomas Peterffy - Chairman & CEO

We are increasing the advertising budget, that is probably going to go from \$25 million to \$30 million per annum and we are increasing the sales force to, I mean we are trying to increase the sales force probably by about another five employees, so you could put in there another couple of million dollars.

Rich Repetto - Sandler O'Neill

Got it. Okay. And then, one more thing on Brokerage, quarter-to-quarter, not year-over-year, but quarter-to-quarter, the net interest income grew 17% just in the Brokerage and the margin loan balances only grew 7%, I know that's end of period, but I was just trying to see, Paul, is that a issue with the credit, the spread and the credit balance or I'm just trying to figure out how you grew just because it's tough to model it year-over-year when you have the most recent sort of spreads and rates from the prior quarter.

Paul Brody - Group CFO

Understood. Actually we think most of it is in the given that the low rates compressed the spreads on the credit, it's mostly coming from the debits which increased – it depends on the tier that the customers are in as to how much spread they are producing for us, the smaller balances are producing a greater interest spread, but the mix of that whole thing produces a greater proportionate amount of income, net interest income than that actual rise in the underlying balance.

Thomas Peterffy - Chairman & CEO

So it also has to do with the -- to what extent our customers are borrowing, hard-to-borrow stocks that we happen to have and these are fairly unpredictable. I understand the problem.

Rich Repetto - Sandler O'Neill

And then, the last question sort of on the market structure issue, Thomas, so you advocated this delay of the 10 to 200 milliseconds, it appears, and who knows what the regulators implement, but it seems like there is a growing momentum against the make or taker model or at least caps on fees from SIFMA recommending it to some former SEC Chairman today. So anyway, my question is if they went to a limit – putting a cap on fees of 5 mils or eliminating make or taker, does that accomplish – how does that – what are the pros and cons doing that versus your delay recommendation and how would the elimination affect IBKR?

Thomas Peterffy - Chairman & CEO

We are doing extremely well executing our orders. And here I'm talking about customer orders. And we have gone to great lengths building the software that is really has become quite a complex system. So to the extent that they will simplify the market structure, that may be good for the world, but will probably be not so good for us. It is my proposal about the holding up the only the liquidity removing orders I am talking about. If that were implemented, that would not impact IBKR much but I think it would be good for generally for the markets.

Rich Repetto - Sandler O'Neill

Okay. And just one follow-up on that answer then, in your routing practices then, is a significant component looking at the rebates as well or were you looking at all-in price to the customer because I know, like you stated earlier, that you are sharing half the rebate with the customer, so is that, so rebates in your order routing tables and priority play a pretty meaningful role there, is that reasonable?

Thomas Peterffy - Chairman & CEO

Yes, yes. I think you will have more clarity on that at the end of the month.

Rich Repetto - Sandler O'Neill

With the increased disclosure?

Thomas Peterffy - Chairman & CEO

That's right.

Operator

Our next question comes from the line of Niamh Alexander with Keefe, Bruyette & Woods. Your line is open.

Niamh Alexander - Keefe, Bruyette & Woods

Hi, thanks for my taking my questions. And if I can just go back to that just to clarify Thomas, you are saying that you definitely take the rebates into consideration when you are routing and that's routing in your broker order flow or is it in the market maker?

Thomas Peterffy - Chairman & CEO

You see, we route to wherever the customer gets the best total price. So we pass the rebate, half the rebate on to the customers so it becomes a difference in the customers' final total price.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. And then, just there are, I guess, today we've seen Senator Levin's letter of proposing just eliminate maker taker pricing and what Richard was referring to was maybe the SIFMA letter which comes from a different group but am I hearing correctly that if you oversimplify the market, it doesn't help a sophisticated broker necessarily like you where the sophistication is an advantage and because it differentiates you versus competitors. Would you be supportive of eliminating market make or taker pricing?

Thomas Peterffy - Chairman & CEO

I think I would be, yes.

Niamh Alexander - Keefe, Bruyette & Woods

You would, okay, that's interesting. Thank you. And then, I guess if you could just go back to the market maker because you do kind of make pains to say look, we're not getting out of the business, we'll scale back but there could be some big opportunities down the road especially if we see some market structure changes. But the other thing that's happening is big M&A deals appear to be kind of resurfacing and back on for sure. Historically, that's not the best environment for an options market maker, are you kind of – is that maybe one of the reasons as well we're starting to see a pull back a little bit more or is it just overall generally volatility has been awful?

Thomas Peterffy - Chairman & CEO

Well, no, we were – the volatilities have really hurt us or rather the lack of them. I agree with you that many M&A deals are not the best for the market maker because of insider traders, but maybe there is so much going on with insider trading that maybe people will be a little bit more fearful and abstain I hope.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. Fair enough. And then, just on your capital levels, are you comfortable where you are, you have \$3 billion of excess capital, you've had excess for a while. But historically in the past you kind of said you wanted to get to a certain level to have a certain rating and you've continued to kind of compete more for that institutional business, is there a goal in mind, is there a level of capital, would you like to continue to grow \$5 billion plus level of combined capital, is there a goal there?

Thomas Peterffy - Chairman & CEO

Up until further notice, we are growing.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. Fair enough. And then, sorry, if I could just go back to Paul real quick, what was the trade execution cost in the broker?

Paul Brody - Group CFO

The trade execution and clearing expenses for the quarter were about \$35 million.

Niamh Alexander - Keefe, Bruyette & Woods

For the broker?

Paul Brody - Group CFO

For the Brokerage segment, yes.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. Got it. Thanks so much. I'll get back in the line.

Operator

Our next question comes from the line of Mac Sykes with Gabelli. Your line is open.

Mac Sykes - Gabelli

Thomas, do you feel you've capitalized enough on the public investors --.

Thomas Peterffy - Chairman & CEO

Sorry, what was the word, do you feel --.

Mac Sykes - Gabelli

I'm sorry. Do you feel you've capitalized enough on the public investors' negative reaction to the Lewis book. And then, secondly what has surprised you, whether it's the market structure or client changes since the events have unfolded?

Thomas Peterffy - Chairman & CEO

We believe that we've capitalized enough, we are better capitalized than I think any of the non-ben brokers, especially relative to our debits – I'm sorry I missed your second question.

Mac Sykes - Gabelli

So my first question was necessarily on capital, it was do you feel that you've benefited enough through your actions, whether it's marketing or client acquisition since the Louis book, the events of Louis book unfolded. Do you feel you've made a good enough progress on that?

Thomas Peterffy - Chairman & CEO

No, I do not believe that we benefited as much as I had expected, but we still on this kick and going forward it's still something that I don't plan to let up on, namely try to convince the world that coming to our platform is a compelling proposal because they would save so much money relative to wherever else they go. So that's what we have to keep on pushing.

Mac Sykes - Gabelli

And my second question was really since the events have unfolded, we've had public reaction, we've had some hearings, we've had some reactions from government officials et cetera, I was just curious if you had seen any kind of element or anything that's come out of sort of the reactions that would have surprised you given the uproar about the market structure, just anything that the industry may have missed in terms of public sentiment or where we may be moving.

Thomas Peterffy - Chairman & CEO

We are following this very closely, maybe we are too deeply in it but we don't see – I at least haven't seen anything that I had not expected, the SEC, I expected the SEC to put together a committee and they indeed will put together this market structure reform committee and I expect that they eventually will do something, recommend something early next year and they probably be some resolutions and rule changes sometime in the next – towards the middle of next year, that's what I expect.

Operator

(Operator Instructions) Our next question comes from the line of Sean Brown with Teton Capital. Your line is open.

Sean Brown - Teton Capital

Hi guys, this is Sean. Congrats on the continued accounts momentum. Just a few quick questions around good growth areas of the Broker segment. First one is, I know you've touched on introducing brokers as a sort of key to growth outside the U.S., wondered if you could give an update or some color on how that initiative is going?

Thomas Peterffy - Chairman & CEO

Introducing brokers are growing probably faster than any other segments, a little bit faster than any other segments, actually in the last quarter, yes.

Sean Brown - Teton Capital

Got it. And then, on the domestic front, it seems advisor, you guys have been iterating on the advisor platform a lot the past several months, I'm just wondering who are the other players that you are going up against directly when you are competing for the business of these RIAs, is it like an Ameritrade or a Schwab or someone as big as an LPL? And then, what do you feel are

sort of the two to three biggest comparative advantages that you guys have over the competition in the advisor space?

Thomas Peterffy - Chairman & CEO

Well, you put your finger on the advisors of the large advisor houses that we are competing with. The advantages are very simple. We believe that we give technologically more sophisticated platform. Our commissions are much lower than the commissions of the competitors, therefore the client keeps more and that would enable the advisor to keep more, but also when you mentioned the competitors, you can't forget about Morgan Stanley and UBS and we got a large number of advisors, new advisor accounts from these firms.

Sean Brown - Teton Capital

Got it. Yes, I guess as advisors and RIAs move their fee structure more towards a straight percentage of AUMs, they'll be looking to reduce trading costs however they can. Is that a correct assessment?

Thomas Peterffy - Chairman & CEO

That's absolutely correct. Yes.

Operator

Our next question comes from the line of Chris Harris with Wells Fargo. Your line is open.

Chris Harris - Wells Fargo

Guys, just a quick follow-up on the earnings number, Paul, did you say the trading gains contributed \$0.02 to the number? So if you took the trading gains out and took the OCI out, you were at \$0.24 in earnings?

Paul Brody - Group CFO

Just the portion of translation gains that are contained in the reported trading gain contributed about that much.

Chris Harris - Wells Fargo

Right. But is that right? So if you took that out, you'd be at \$0.24 for the quarter?

Paul Brody - Group CFO

If you took out the currency element, then we'd be at \$0.24 for the quarter, yes.

Operator

We have a follow-up from Niamh Alexander with Keefe, Bruyette & Woods. Your line is open.

Niamh Alexander - Keefe, Bruyette & Woods

Hi. Thanks for taking my follow-up call. If I could just go back to the letter you mentioned earlier, Thomas, from FINRA, if you wouldn't mind indulging a little bit there, expanding a little bit on that. I understand it's kind of a letter to primarily kind of brokers in the retail space to expand a little bit on your routing practices. But it's not an official investigation, is it? Or what is this?

Thomas Peterffy - Chairman & CEO

Well, it's a letter that is asking a large number of questions about how you route and why you route, where you route to and who decides and how frequently you make a new decision and what drives those decisions and it's a very large number of questions.

Niamh Alexander - Keefe, Bruyette & Woods

And you haven't gotten something like that in quite a while because you all have 606 filing requirements about where you route and whatnot. But this seems kind of a little bit more detailed.

Thomas Peterffy - Chairman & CEO

Just wants to know why. How do you decide.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. So you think if there is a requirement to publish down the road, that IBKR should kind of be in a good position?

Thomas Peterffy - Chairman & CEO

I think the ultimate question is, what is the broker's fiduciary duty. And I hope the original idea with fiduciary duty was that you place your customer's interest ahead of your own and I hope that will be the final conclusion.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. Fair enough. So right now, it's kind of private, just between the brokers and the FINRA.

Thomas Peterffy - Chairman & CEO

Is it private?

Niamh Alexander - Keefe, Bruyette & Woods

Well, I don't know, you don't need to publish your responses, do you?

Thomas Peterffy - Chairman & CEO

Oh, well, that is just a letter from FINRA asking these questions. Of course, I don't think it will be published. We certainly wouldn't take it up on ourselves to publish them.

Niamh Alexander - Keefe, Bruyette & Woods

Okay. So we'll watch the space. Thanks. I appreciate.

Thomas Peterffy - Chairman & CEO

Any publicity it gets I would be happy with.

Niamh Alexander - Keefe, Bruyette & Woods

Understood. Thanks.

Operator

Our next question comes from the line of James Lee with Kylin Management. Your line is open.

James Lee - Kylin Management

Hello. My first question is, if you could update us on the Singapore issues, whether or not you collected?

Thomas Peterffy - Chairman & CEO

Yes. Well, it just circles on. We have hit, I think, a couple of milestones but we – there is still things are very, very far in the future, any resolution.

James Lee - Kylin Management

Okay. Second question is, during the – when the company went IPO --.

Thomas Peterffy - Chairman & CEO

Sorry. You've got to speak a little louder please.

James Lee - Kylin Management

Can you hear me?

Thomas Peterffy - Chairman & CEO

Yes, please enunciate your words.

James Lee - Kylin Management

During the IPO process, the prospectus talked about IBG Holdings selling down its interest in the operating company over a seven-year period following the IPO by 12.5% per year. Nothing has been done since then. I'm just wondering if there's any sort of plans for selling down.

Thomas Peterffy - Chairman & CEO

Some employees have done that. Not the larger holders but some of the smaller holders have done that.

James Lee - Kylin Management

Right. So I'm wondering if the larger holder --.

Thomas Peterffy - Chairman & CEO

That's what's in effect, let us to go from 10% publicly owned to 13.6% --.

Paul Brody - Group CFO

14.1% at the moment.

Thomas Peterffy - Chairman & CEO

14.1% you see.

Paul Brody - Group CFO

It also goes up as our stock incentive plan shares vest.

Thomas Peterffy - Chairman & CEO

100 years and it will be there.

James Lee - Kylin Management

I mean, I guess the point is IBG Holdings still owns over 80% of the company, and the listed company only owns about, what, 14%. So just wondering if that's going to be a further sell down to actual increasing of the holdings by the listed company?

Thomas Peterffy - Chairman & CEO

I'm missing the word.

Paul Brody - Group CFO

Do we have a plan?

Thomas Peterffy - Chairman & CEO

Do we have a plan? We don't have a plan, no. No, I do not have a plan.

Operator

I'm showing no further questions at this time. I would like to turn the call back to Debbie Liston for further remarks.

Debbie Liston - Director, IR

Thanks everyone for participating today. And as a reminder, this call is going to be available for replay on our website and we will also be posting a clean version of the transcript on our website tomorrow. Thanks again for your time. And have a great evening.

Operator

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