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PRESENTATION

Operator

Ladies and gentlemen, good morning. Thank you for standing by and welcome to the Thomson Reuters second-quarter 2015 earnings conference call.

(Operator Instructions)

As a reminder, today's conference is being recorded. I would now like to turn the conference over to our host, Senior Vice President, Investor Relations, Mr. Frank Golden. Please go ahead.

Frank Golden - *Thomson Reuters Corporation - SVP, IR*

Good morning and thank you for joining us as we report our financial results for the second quarter. Our CEO Jim Smith will start today's discussion followed by Stephane Bello, our CFO.

Following their presentations we'll open the call for questions. We'd appreciate it if you limit yourself to one question each in order to enable us to get to as many as possible.

Throughout today's presentation keep in mind that when we compare performance period on period we look at revenue growth rates before currency as we believe this provides the best basis to measure the underlying performance of the business. It's also the basis on which we provided our 2015 outlook.



Today's presentation contains forward-looking statements. Actual results may differ materially due to a number of risks and uncertainties discussed in reports and filings that we provide to regulatory agencies. You can access these documents on our website or by contacting our Investor Relations department.

With that I will turn it over to Jim Smith.

Jim Smith - Thomson Reuters Corporation - President & CEO

Thank you, Frank, and thanks to those of you on the call for joining us. Today we will begin with a review of the second quarter's results and our outlook for the balance of the year.

Now let's turn to the results for the quarter. As I stated on our Q1 earnings call, we've made significant progress putting the Company back on a solid footing and you can again see that in the numbers we reported today. We've had a good first half of the year both operationally and financially.

Importantly we are on track with our expectations for the balance of the year. Our guidance for 2015 is to return to positive organic revenue growth on a constant currency basis and we are on our way toward achieving that objective.

We cautioned last quarter that increased volatility in foreign currency markets would likely have a higher than usual impact on our results in 2015. That, indeed, proved to be the case again in the second quarter. Therefore, I'll provide you with both our reported results for the quarter and our results before currency so you can clearly see the underlying progress we are making.

Revenues were down 4% on a reported basis but were up 2% before currency, a full 600 basis point swing due to currency in this quarter. EBITDA was down 2% with the margin up 40 basis points on a reported basis while before currency EBITDA was up 3% and the margin was up 50 basis points.

Again on a reported basis, underlying profit was down 1% and the margin was up 60 basis points. Before currency operating profit was up 7% and the margin was up 100 basis points.

Adjusted EPS was \$0.52, \$0.01 better than the prior-year period and before currency EPS was \$0.07 better than last year, a 14% increase. We also continue to execute on the capital strategy program that we announced in 2013 and since that time we have returned over \$3.8 billion to shareholders in the form of share buyback and dividends. Lastly, given our encouraging first-half performance we again reaffirm our full-year 2015 outlook.

Some additional highlights for the quarter. First and foremost, Financial achieved its first quarter of revenue growth in more than three years, up 1% and net sales were positive in the quarter and were positive in all regions for the second quarter in a row. This marked the fifth consecutive quarter of positive net sales and we've seen year-over-year improvement in 10 of the last 11 quarters.

Second, as I discussed in Q1 the Financial business has three major migrations this year that are all on schedule. Two are revenue-related and one is cost take-out related. The two product- or revenue-related pieces involved migrating our remaining legacy foreign exchange and buy side customers onto our unified platform and making some commercial pricing adjustments.

We are on track, having converted about half the \$700 million in revenue that's involved in this program. These migrations as expected have resulted in downward pricing adjustments in some instances which is constraining Financial's revenue growth this year. Despite this pricing pressure our Financial business' revenue grew 1% organically in the quarter.

The platform migration and involves moving our large real-time global infrastructure onto Elektron. We've now moved over 90% of customers to our new Elektron platform with 85% of those customers now entirely off the old platform. We continue to incur some dual running cost which is dampening the margin and that will continue to be the case until we close the old platform in the fourth quarter, resulting in significant savings.



Turning to Legal revenue growth was 2%. Importantly US Online revenue again grew slightly for the second consecutive quarter which is very encouraging and is reflective of improving net sales and higher retention rates for Westlaw. As I mentioned last quarter we had not seen organic revenue growth in US Online Legal since 2009.

Tax & Accounting continues to execute well and had another good quarter (technical difficulty) dampened a bit by the Government business which Stephane will cover.

IP & Science returned to growth and was up 1%, a bit weaker than expected due to difficult prior-year comparison and an 8% decline in transaction revenues. Subscription revenues rose 4%.

Finally, our Global Growth businesses achieved revenue growth of 6% all organic. And I'll remind you that GGO's results are included within each of the four business segments.

So the trends that we are now seeing with each of our four businesses back in a growth mode give us reason for optimism regarding our prospects for improving organic revenue growth and profitability as we look forward to 2016. The Financial business has turned the corner and we are beginning to realize the tangible benefits of the team's good work over the past three years as evidenced by a 400 basis point improvement in Financial's organic revenue growth as compared to a year ago from minus 3% to plus 1%. And just as impressive is Financial's EBITDA margin improvement of over 100 basis points in one year as it continues to make progress toward its 30% target.

It's also encouraging to see that momentum in our Legal business continue in the second quarter reflected by revenue growth of 2%. That's 3% excluding Print. This performance was driven by 5% growth from our Solutions Businesses and marginal growth in US Online revenues for the second consecutive quarter somewhat offset by a print decline of 5%.

So in summary we're pleased with our first-half performance and growing momentum. The strategy is working which is reflected in today's results. Going forward we will continue to prioritize resources behind the highest growth opportunities with the greatest chance to improve our prospects in 2016 and beyond.

Now let me turn it over to Stephane.

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

Thank you, Jim, and good morning or good afternoon to all of you. As Jim just explained currency again had a significant impact on our results as reflected in the 600 basis points swing between reported revenues which were down 4% and revenues before currency which were up 2%.

This slide provides a snapshot of our second-quarter and six months results. For the rest of the presentation I will speak to revenue growth before currency in line with the way we have always done it.

So on a constant currency basis, second-quarter revenues were up 2% all organic. Our Financial business was up 1% organically while our three other businesses were 2% organically in aggregate during the quarter.

Adjusted EBITDA was down 2% with an EBITDA margin of 28.2% up 40 basis points compared to the prior year. Excluding the impact of currency EBITDA was up 3% and the margin was up 50 basis points compared to Q2 last year.

Our second-quarter operating profit was down 1% compared to the prior year and the margin was up 60 basis points. Again, excluding the impact of currency operating profit was up 7% and the margin was up 100 basis points.

Now there were some negative factors both last year and this year which impacted the year-on-year comparability of our second-quarter performance. As you may recall we booked approximately \$30 million of charges in the second quarter of last year which did not happen this year.

On the other hand we implemented our annual merit increases on April 1 this year or three months earlier (technical difficulty). So on balance the 100 basis point improvement in the margin I just described this quarter genuinely reflects a continuing improvement in the underlying performance of the business.

Now let me provide you with some additional color on the performance of our individual businesses starting with Legal. Demand for legal services in the US market was again up slightly, the third consecutive quarter of improvement with four of the last five quarters showing modest growth. As Jim just indicated Legal grew 2% all organic during the second quarter, slightly below the 3% increase in the first quarter as both subscription and transaction revenue growth rates were slightly lower than in the first quarter as we expected.

Transaction revenues for the quarter which are primarily services revenues and which represent 13% of the total were up 10% all organic once again driven by strong performance in Findlaw, Pangea3 and Latin America. Subscription revenues which accounted for about three-quarters of the total were up 2%, again all organic.

Turning to our profitability metrics for the quarter, the EBITDA margin was down 150 basis points while the operating profit margin decreased 80 basis points. The margin decline was primarily due to the impact of salary increases which as I just said came into effect in the second quarter versus the third quarter last year. For the full year we continue to forecast that Legal's EBITDA margin will be broadly flat compared to 2014.

This next slide shows a more detailed look at the revenue performance of the three main subsegments in our Legal business. US Online Legal Information which is 39% of total revenues was up slightly for the quarter as it was in the first quarter. So the positive trajectory continues for this business.

The continued improvement in retention for Westlaw is making a significant contribution with retention rates up 60 basis points compared to 2014. In addition, Practical Law continues to perform strongly with that business in the US now about three times the size it was when we acquired it 2.5 years ago.

US Print revenues were down 5%. Excluding the impact of US Print the rest of the Legal business therefore grew 3% organically during the quarter.

And finally this quarter's performance was once again driven by our Legal Solutions businesses which continued to grow at a solid pace. These solutions businesses consist of everything except US Online Legal Information and US Print.

In aggregate they made up 45% of Legal's total revenues in the second quarter and they grew 5% all organic. This strong organic growth performance was driven by our Legal Enterprise Solutions business which includes Elite and Serengeti and our Pangea3 legal managed services business as well as strong growth in our Investigations and Public Records business.

Now let me spend a moment on the Legal's improving growth dynamics. As you can see on this slide, in total Legal business grew 2% organically in the first half of the year as compared to flat in the first half of last year and to a 1% organic decline for the whole of 2013. This improvement is directly related to the evolution of our revenue mix and to the growth profile of the three main business segments within Legal which are depicted on this slide.

Our US Online Legal Information business has improved from minus 2% both in 2013 and in the first half of 2014 to slight growth in the first half of 2015. This is a very encouraging turnaround in what is Legal's most profitable business segment. The Solutions Businesses grew 7% organically in the first half of this year, up from 5% organic from the same period in 2014 and 3% organic in 2013.

These Solutions Businesses represent our most promising growth opportunities and they accounted for 46% of Legal's revenue base in the first half of the year. They are delivering strong and steady growth.

And finally, the decline in our US Print business appears to be stabilized at around 5% to 7%. And this business which is highly profitable will become an increasingly smaller percentage of Legal's total revenue base. So it is the combination of the improving growth performance of our US Online business as well as the increasing size of the faster growing Solutions Businesses which are driving Legal's overall growth performance.



Now turning to Tax & Accounting, that business had another good quarter with revenues up 6%, of which 5% was organic. Recurring revenues, about 80% of the total was up 7% organically in the quarter which is in line with the first quarter. From a profit standpoint EBITDA was down 8% in the quarter with the margin declining 270 basis points.

Now the margin was negatively impacted by three factors this quarter: first, the decline in revenue in our Government business which is small but fairly volatile; second, the timing of our annual salary increases; and third, investments we continue to make in selected high growth opportunities. These three negative impacts were partially offset by currency which had a positive impact on margins in Q2. For the second quarter operating profit was down 3% with the margin down 80 basis points for the same reasons that highlighted EBITDA.

As you can see on this next slide, our Professional and Corporate segments which represent 70% of the business maintained the strong performance they recorded in the first quarter with organic growth rates of 10% and 11% respectively. And our Knowledge Solutions segment return to growth in the second quarter.

As I just mentioned our smaller segment, the Government business, had a challenging quarter with revenue down significantly due to timing-related items for some contracts. Although Government is a small percentage of the total business its weak performance had an impact of 170 basis points on revenue growth this quarter. So if you were to exclude Government, Tax & Accounting's revenue growth would have been closer to 8%.

Revenues for the Government business are less predictable in nature and so from time to time we do see results such as this in a given quarter. However, we continue to expect Tax & Accounting to deliver another strong performance for the full year, both on the top- and bottom-line levels.

IP & Science is where 1% for the quarter, again a bit disappointing but slightly better than the first quarter. This performance was primarily the result of growth in subscription revenues partially offset by a lower number of transactional deals compared to the prior-year period. More on that in a moment.

The EBITDA margin and the operating profit margin were down 120 and 130 basis points respectively also driven in large part by the timing of the annual salary increases. Subscription revenues, which make up about three-quarters of the total, continued to perform well and were up 4% all organic during the second quarter. Transaction revenues declined 8% all organic due to softer sales in the academic segment.

And as you can see on this slide the results for the first half of the year are similar to the second quarter as we have seen very similar trends for transaction revenues throughout the first half of the year. As we always remind you, small movements in the timing of revenues and expenses can impact margins in any given quarter for the IP & Science business and therefore full-year results are more reflective of the segment's underlying performance.

Now turning to our Financial & Risk business second-quarter revenues were down 6% on a reported basis with currency once again having a significant impact. If you exclude currency revenues were up 1% for the quarter all organic. This is the first time the business has posted organic revenue growth since Q4 of 2011.

As Jim mentioned a moment ago, this represents a 400 basis point improvement compared to the prior year. For the balance of the year we expect the decline in Recoveries revenues to accelerate as more third parties move to direct billing. Due to this projected decline in Recoveries, which to remind you are relatively low margin revenues, we are not expecting to see incremental improvement in the growth rate of F&R for the remainder of the year.

Once again net sales were positive in all regions and both the Americas and Asia showed positive organic revenue growth for the quarter with Europe flat. The EBITDA margin for the quarter was up 200 basis points due to the simplification actions we took in 2014. Before the impact of currency from both periods and adjusting for the impact of the charges we took in Q2 of last year the margin was up 110 basis points to 28.7%.

As we mentioned last quarter, we continue to incur some dual running cost as we work to migrate and close the real-time network. We do expect to complete this migration in the latter part of the year at which time we expect to see a more pronounced improvement in the margin.



As Jim mentioned the platform migration is very much on track with about 90% of our clients now installed on the new network and about 85% of those clients running solely on the Elektron platform. As we've said before we need to migrate 100% of our customers onto the new platform in order to enjoy the full cost benefit of this migration. We continue to expect to get there in the fourth quarter.

Operating profit was up 3% with the margin up 160 basis points for the quarter. And again excluding the impact of currency and charges the margin was up 120 basis points.

Looking at the Financial & Risk revenue in a bit more detail recurring revenues which were 76% of the total were up 1% during the quarter all organic. Recoveries, about 11% of the total were down 1% for the quarter and as I just mentioned we expect the decline to accelerate in the second half of the year and into 2016 as some of our third-party partners moved to a direct billing arrangement with our customers.

Finally transaction revenues, which is 13% of the total, were up 3% all organic. Our FXall, Tradeweb and BETA businesses all contributed to this growth for the quarter. However, we saw some softness in our FX matching transaction revenues with lower volume than in prior year.

During the first half of this year we have seen a bit of decoupling between volatility and volume in the foreign exchange markets. Volumes have been lower despite higher volatility due to the fact that market makers appear to be less willing to risk trading capital. We are not yet calling this a trend but it's something that we are closely watching.

Now you can see on this slide how the Financial & Risk business mix has continued to evolve as Feeds and Non-Desktop products have become a greater proportion of total revenues. In the second quarter of this year these two businesses made up 36% of the Financial & Risk revenue base as compared to 32% in 2013 and they grew organically at 6% and 5% respectively. So we had about a third of our Financial & Risk business growing mid single digit in Q2.

Desktop revenues have improved their growth rate significantly since 2013 as a result of a far better product and improved retention rates. I should also remind you that Desktop revenues in the third quarter of 2015 were impacted by the migration activity with the resulting lower price realization.

Excluding the negative impact from these migrations Desktop revenue would in fact be growing slightly. That means that the vast majority of our Desktop revenues are slowly getting back into growth territory.

So the return of our Financial business to growth is driven by factors that are quite similar to what I just described when I discussed our Legal business. First, we need the higher growth target part of the business Risk, Feeds and hopefully Transactions to continue to grow and become a bigger percentage of the total revenue base.

And second as we complete the migration of our legacy Desktops to Eikon we are seeing a meaningful improvement in the growth performance of that business from minus 6% decline in 2013 to minus 3% in the second quarter of this year and into positive territory once we complete the commercial adjustments associated with the remaining product migrations.

Finally let me review Financial & Risk's progress relative to their EBITDA margin target as we do every quarter. As was the case in Q1 currency had a significant impact on the second-quarter results. On this slide we have excluded the impact of currency and the negative impact of the charges we took in Q2 last year and that gets us to the underlying margin number.

The second quarter reflected the impact of the annual salary increases for employees. But even taking this into account F&R's EBITDA margin increased by 110 basis points versus last year.

Now turning to our consolidated results, let me start with our free cash flow performance for the first half of the year and working from the bottom to the top of the slide. You can see that free cash flow for the first six months of the year was \$644 million compared to \$517 million in the prior-year period. This included \$54 million of cash payments related to our Simplification programs as compared to \$159 million in the first half of 2014.



Free cash flow excluding the impact of the Simplification charges was \$698 million, \$22 million higher than the prior-year period. As an important aside, cash taxes for the first six months of this year were \$72 million higher than the first half of last year which was largely timing-related. So the trend in our underlying free cash flow performance continues to be very strong if you adjust for that factor.

As a reminder in the second quarter we completed the \$1 billion buyback program we announced last July and this May we announced a third \$1 billion which we expect to complete by the end of 2016. As Jim mentioned we continued to execute on the capital strategy program which we announced in October 2013 and we have now returned over \$3.8 billion to shareholders in the form of share buybacks and dividends over that period.

Now turning to our earnings per share performance, second-quarter adjusted EPS was \$0.52 per share, a \$0.01 better than a year ago. Foreign currency had a \$0.06 negative impact on a year-on-year basis. So before currency EPS improved by \$0.07, about half of which represented better operating performance and the other half was lower charges.

So to wrap up, we are pleased with our start of the year. And based on the first-half's results we are reaffirming our outlook for the full year.

With that let me turn it back over to Frank.

Frank Golden - Thomson Reuters Corporation - SVP, IR

Thanks very much Stephane and that concludes our formal remarks on the quarterly results. Now I'd be happy to open the call for questions. So if we could have the first question, operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Toni Kaplan, Morgan Stanley.

Patrick Hoff - Morgan Stanley - Analyst

Good morning everyone. This is actually [Patrick Hoff] filling in for Toni this morning. You know, lapping quarters of positive net sales in F&R, can you give us a sense whether the third quarter will be a tougher comp than 2Q for net sales?

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

I would say what's really important, it's hard to look at it from quarter to quarter, what's really important is to look at the trajectory. The trajectory on net sales performance has been very clear.

It's obviously going in the right direction. So it's hard to predict what one quarter will be relative to another one but we would expect, frankly, that it would not be a massive divergence from the trajectory that we've seen recently.

Operator

Drew McReynolds, RBC capital.



Drew McReynolds - *RBC Capital Markets - Analyst*

Thanks for a much and congrats on the organic revenue growth. Jim, just now that you have a stronger footing clearly under each of the four businesses and it sounds like there's still a cyclical tailwind out there, just wondering if and when there's any change to your acquisition versus organic growth focus as we move into 2016, do you intend on revisiting things now that you're potentially focused on things internally? Thank you.

Jim Smith - *Thomson Reuters Corporation - President & CEO*

I don't think we're less focused on things internally right now, frankly. I think we've still got a lot of work to do over the balance of the year and over the coming year in terms of building what I'd talked about and turned that platform that supports our sustainable growth in the future.

Frankly when we turn our attention externally right now we're looking at markets and customers and opportunities for organic growth and I found that very, very refreshing. If you look at the underlying activities that have driven the growth in the second quarter they have been positive changes in core products and new products and new services and those are incredibly sustainable developments inside the business. So we're going to look first at growing the businesses that we have before turning to acquisitions.

So I don't see any real change in focus based on where we are today. That doesn't mean we don't always have our eyes open and we aren't always evaluating opportunities as they present themselves. We just find more attractive opportunities today inside our business and inside the customers and markets that we're serving right now.

So I'm sure there will always be some level of tactical acquisition activity. But we're still focused on executing right now and serving our customers.

Operator

Manav Patnaik, Barclays.

Greg Bardi - *Barclays Capital - Analyst*

Hi, this is actually Greg calling on for Manav. I just wanted to ask about your pricing and reference data business. I know I've seen a couple of headlines out about you adding intraday pricing but I guess more broadly just want to hear about your strategy in that business and where you think you fit in the competitive landscape.

Jim Smith - *Thomson Reuters Corporation - President & CEO*

We can both tag on that, that's been a very strong growth business for us and I think we have a very strong business there. We've been investing behind adding capability there and we see it as a very, very important plank underpinning our risk offering and the services and products that we sell to the Financial community. We think we're very strongly, we've seen solid growth there and we continue to invest behind that business.

Operator

Vince Valentini, TD Securities.

Vince Valentini - *TD Securities - Analyst*

This is Vince for Vince. Two questions on potential problem areas. So Europe, there's obviously been some economic challenges there.

Anything changing in her conversations with your major customers there? And then secondly Global Growth plus 6% is a bit less than what we had been seeing in prior periods where that had been getting up closer to double digits. Are you seeing some challenges there in some of those emerging markets starting to decelerate a little bit? Thanks.

Jim Smith - Thomson Reuters Corporation - President & CEO

Sure. I would point first to Europe. Encouraging net sales were positive in Europe again for the second consecutive quarter and so we're encouraged by our performance in Europe.

Even with all the volatility of macroeconomic certainty in Europe our performance in Europe has been pretty good of late and we're encouraged there. And the conversations with our key customers in Europe are as strong as they have ever been, in fact stronger than they have ever been. So we're encouraged by our position there, currency fluctuations notwithstanding.

As far as emerging markets go, Stephane could probably provide some more color on that. But we're still bullish long term on that despite the fluctuations quarter to quarter. Stephane, any color?

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

Good morning, Vince. The two things I would highlight, this first this is now a business that's close to \$1.2 billion in revenue, so growing that revenue base at 6% is not a bad performance.

The other thing I would point to is that when we speak about some of the commercial adjustments that impact our Financial & Risk business these do impact our (inaudible) regions also. And so the organic growth rate is a little bit depressed if you want because of these commercial adjustments this year.

Operator

Sara Gubins, Merrill Lynch.

David Chu - BofA Merrill Lynch - Analyst

Hi, this is David Chu for Sarah. So it sounds like about half of the FX and buy side migration is complete. So when do you expect to get all 700 in revenue over to Eikon?

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

As we've said in the past we do expect it's going to happen over 2015 and 2016. I would expect the migration of our foreign exchange Desktop to be largely but not fully completed by the end of this year. So there's still going to be some leftovers if for lack of a better word if you want in the first quarter of 2016, but we should be very much done with this one by the first half of 2016.

On the buy side on the asset management side we are adopting a much more deliberate approach there, so we know that this is going to take us well into 2016 and potentially a little bit further. But I would say the vast majority of the migration, the migration is progressing very well and most of the commercial adjustments impact that we've talked about are going to essentially hit this year with a little bit still hitting us in the first quarter of next year.

David Chu - *BofA Merrill Lynch - Analyst*

Okay, and just one follow-up, so is it still fair to assume that this migration represents about a 200 basis points drag to revenue?

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

You're speaking about the impact of the commercial adjustments? I'd say it's about in that region.

I think in the quarter we said that if you were to exclude the impact of the commercial adjustments the growth for F&R would have been somewhere between 2% and 3%. I think that's exactly where it would have been also in Q2, maybe just a little bit above 2% into the second quarter.

Operator

Ato Garrett, Deutsche Bank.

Ato Garrett - *Deutsche Bank - Analyst*

Just following up on the previous question relating to pricing realization, you mentioned clearly that there is some headwind there from the buy side and FX migrations but can you talk about pricing for new customers on Desktops?

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

What we've seen is that once we move customers on the new product the pricing is much more resilient than it is on the legacy product because the product is simply much better. So this is reflected both by our ability to achieve the annual price realization on the revenue base for several years in a row now and also importantly in the improving retention rates of the business, which are really have really increased dramatically as I think we said during the remarks.

Core Financial & Risk business, our retention rate now overall is just shy of 90% and that's I think was at 89.9% in the second quarter. That's a massive improvement, 250 basis point improvement, in one year. So the new perks enables us certainly better price realization but also important much better attention which is very important in driving the improvement in net sales.

Ato Garrett - *Deutsche Bank - Analyst*

Great. And then one quick follow-up on Legal.

I wanted to get your expectations for growth for the balance of the year. Should we continue to expect the first quarter to be the highest growth for the year or do you think you might see a little bit of a bounceback in the back half?

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

I'd say what I would always recommend is looking at the trajectory of the growth rate not quarter by quarter but more on an annual basis. If you look at our legal business it was negative 1% in 2013, moved just to slight positive growth rate last year in 2015.

In the first half of this year I think it was about 2%. That's probably a good product projection for the full year, be around 2%. And then from there in 2016 and 2017 because of the mix dynamics I explained on that slide we would expect a gradual improvement in the growth rate year after year.



Operator

Bill Bird, FBR.

Bill Bird - FBR - Analyst

Good morning. I was wondering if you could talk a bit about churn, maybe you could speak to Eikon churn versus total Desktop churn and how much room you think there is for improvement?

And just secondly, you were very clear in calling out accelerating Recoveries declines. How big do you expect the upcoming headwinds to be from that in F&R? Thank you.

Jim Smith - Thomson Reuters Corporation - President & CEO

Why don't I take the first part of that and then let Stephane deal with the second part of that. We've seen a significant improvement in churn, I assume you're talking about retention, with a over 200 basis point improvement in our overall retention rates where we got new modern Eikon platforms in place.

In fact you look at some of the other Desktop businesses that we have, the remaining ones that are sitting in wealth management or matching where we have very solid and in fact better retention rates there, and I think we reported for this quarter we were approaching 90% now in terms of retention rates on those Eikon platforms. So we have seen improvement there.

I can tell you that internally we are targeting increased improvement. And we see that based upon customers sat, we see it with the product on improvements in customer service that we have and so we continue to improve that.

The good news about those improved retention rates is they do bring down that customer churn and then obviously it is far more profitable to keep an existing customer than to go out and try to win a new one. So we're focused on that. We've seen marked improvement over the last two years in our retention rates and we think there's room to improve it even further.

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

And Bill, on your question regarding recoveries it's really hard to predict exactly how much of a headwind it will be because it depends upon the timing with which our third-party partners are moving to that direct billing arrangement with customers. But in the first half the rate of decline of recoveries was in the area of like 1% and we would certainly expect that to accelerate to mid to high single-digits decline in the second half of the year.

Again, what's important is that this is not really highly profitable revenue for us. So it doesn't have any impact, this change in direct billing arrangement has no impact on the growth rate of EBITDA or free cash flow or operating profit. It's really just a contractual change in terms of how we do the billing with our customers.

Operator

Paul Steep, Scotia Capital.

Paul Steep - Scotiabank - Analyst

Thanks. Just for Jim and Stephane, both, maybe you could talk about where the investment is going in terms of the CapEx spend that's been out there this year and how we should think about major platform refreshes, particularly I guess I was thinking Legal, we're about five years into WestlawNext. How you're thinking about redeploying the capital and how we should think about in the 2016 and 2017 in terms of big refreshes. Thanks, guys.

Jim Smith - Thomson Reuters Corporation - President & CEO

Why don't you start Stephane?

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

Okay. Let me start with good morning. I would say that where the investments are going right now there are two clear priorities.

The first one is investment in our highest growth areas. So that would be areas like global trade management, KYC and Risk in general or Legal Solutions business and the like. That's where we're making a fair bit of investment.

And also I think as we look next year and the year after we need to continue to make investment is make sure that we keep improving the stability of our platforms and really make sure that we have one of the strongest infrastructure that we can have because that's absolutely the backbone of our Company. So that's really where I think investment will be going going forward.

But as we've always done and you've seen us doing that for the next four or five years we can really do that and we think we can really manage the cycle of product refreshment investment in growth and reinforcement of the stability of the infrastructure, we can do that within the what we call the spending envelope that we have. And we will continue to do that very much.

Jim Smith - Thomson Reuters Corporation - President & CEO

I have very little quantitatively to add to that. But qualitatively I would note that we've made a lot of progress.

And a lot of that's down to both the finance teams inside our business and our technology teams inside the business are doing a very good job of shifting resources from those maintenance of ongoing legacy systems toward things that are going to drive growth in the future. And that's the approach we'll continue to take as Stephane said, trying to manage within the envelope that we have but just be smarter about how we deploy that.

Operator

Peter Appert, Piper Jaffray.

Peter Appert - Piper Jaffray & Co. - Analyst

Thanks, good morning. So Jim at the risk of oversimplification it sounds like the fourth quarter is a pretty big inflection for F&R in terms of growth and profitability, the pricing reset done as the migrations completed the cost down with the elimination of the duplicate network. So I'm wondering if, one, that's a fair assessment, and, two, more importantly does it suggest that perhaps you're more confident that you can get to the 30% margin in 2016?



Jim Smith - Thomson Reuters Corporation - President & CEO

I think that's probably a fair view of the situation. If we can continue to execute over the balance of this year, 2016 looks very encouraging.

Peter Appert - Piper Jaffray & Co. - Analyst

And maybe just as a follow-on to that, I'm wondering in the context of that whether you think better than 30% is potentially achievable on an intermediate-term basis?

Jim Smith - Thomson Reuters Corporation - President & CEO

Well we're -- let's get to 30% first and then we'll talk about that. I think in all honesty if you look at where our margins are and you look at where some competitor margins are there's clearly opportunity for us to continue to be more efficient inside the business. And once we get to the 30% margin what we'll have to do is weigh the trade-offs between improving the margin and investing in things that will drive growth.

My goal is not a margin number. My goal is a profit growth number. I'm looking for the maximum sustainable rate of profit growth and growth in free cash flow that we can generate.

If we're in a position where we can drive that by top line I'd much rather drive it by top line than bottom line. But in an environment like we've lived through in the past few years you've got to be certain that the top line will come if you make that investment.

So that will be a trade-off as we put together our 2016 plan, 2017 plan and I suspect the constant tension inside the business. There are opportunities for us to be more efficient and there are opportunities for us to continue to drive bottom-line growth and we will just manage that in real-time as opportunities present themselves.

Operator

Doug Arthur, Huber Research.

Jim Smith - Thomson Reuters Corporation - President & CEO

Doug, are you there? Operator, we'll take the next question.

Operator

Aravinda Galappathige, Canaccord Genuity.

Aravinda Galappathige - Canaccord Genuity - Analyst

Thanks for taking my question. With respect to the FX exposure at the free cash flow level, Stephane I was wondering if you can give us a bit of color? Once you factor in the forward contracts in the hedges that you have, how much of the FX impact that we're seeing at the EBITDA level is offset?

Stephane Bello - Thomson Reuters Corporation - EVP & CFO

Sure, happy to take that question. At the EBITDA level if you look at it in absolute dollar terms I think the impact here today is about \$100 million or so.



Now let the free cash flow level there are two important upsets, there is some upset in working capital movement and there is the biggest upset which is the hedges that we have on the book. So the foreign exchange impact, the currency impact on free cash flow this year it's much lesser than \$100 million. It's about \$30 million.

Aravinda Galappathige - *Canaccord Genuity - Analyst*

Okay, great. That's really helpful.

Just lastly with respect to the IDN bond platform, any idea or can you give us some color around what the potential margin uptick would be as we get that behind us? Are we talking something in the range of about 150 basis points? Thank you.

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

I'd say this. I would say the dual cost running in the second quarter were in the area of \$10 million, plus or minus. So you can extrapolate from that and get a sense of where our margins would have been or could be once we don't have two dual running cost anymore.

And as you can see from the progress we're getting dangerously close on that 30% margin target which obviously makes us feel very good. And that's actually a pretty good performance given that if we are able to get there as by the end of the year if we are able to get to an exit rate of 30% as we end the year we would have done that in spite of facing much, much higher headwinds from a transactional revenues than what we were expecting over the period that elapsed since we set that target out.

So it's a good result. But there's still as I said the bond platform, the migration is certainly going to help the margin in the fourth quarter.

Aravinda Galappathige - *Canaccord Genuity - Analyst*

Okay, sorry Stephane, the \$10 million per year in dual running cost, is that a quarterly number?

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

Yes, that's a quarterly number.

Operator

Tim Casey, BMO.

Tim Casey - *BMO Capital Markets - Analyst*

Thanks, good morning. Given the volatility on foreign exchange markets, obviously that's having an impact on your reported results but are you getting any benefits on the transactional or any of the other FX platforms you have from a revenue point of view? Like is the increased volatility helping you on some of the trading platforms, are you seeing any benefits in business that way?

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

That's a very good question and you've seen what we've reported in terms of transaction revenue growth this quarter, it was like 3%. That's lower than what we would've expected it to be given the volatility that we've seen in the markets. And so as we mentioned on the call what we're seeing is a little bit of a decoupling between high volatility in high volumes.



And we think that's due to the fact that some of the largest players, particularly on the sell side, are essentially staying a bit more on the sidelines than we've seen them in the past as there are a number of investigations going on. So what we think is happening is that they just want to make sure that operationally they are completely compliant from a trading perspective and then they reenter the market.

But we'll have to see. Time will tell, but at this point in time your point is a good one. Given that the increased volatility and currency we would have expected to see more volume.

We are not seeing about volume. And it's not just on our platform, I think it's a little bit across the board on the foreign exchange side.

The only area where we've seen good continued growth is on our FXall platform. So treasurers and buy side continue to have a very healthy level of trading activity. But the biggest chunk of trading and volume is probably not as high as what we would have expected given currency volatility.

So a little bit of benefit from transaction bollards were up 3%. But as I said on the call we would have expected that transaction volume to be up by more given the volatility we see in the market. So that's a bit of a disappointment.

Tim Casey - *BMO Capital Markets - Analyst*

And would you characterize that level of activity, is that a high-margin revenue piece or is it relatively --

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

No, that's very high-margin. Transactions are very high-margin.

Frank Golden - *Thomson Reuters Corporation - SVP, IR*

Operator, I think we have one final question and I'm happy to say I think we have found Doug Arthur. So Doug over to you.

Doug Arthur - *Evercore ISI - Analyst*

Can you hear me now?

Frank Golden - *Thomson Reuters Corporation - SVP, IR*

Yes we can.

Doug Arthur - *Evercore ISI - Analyst*

Okay great. I just wanted to go back to Legal for a second. The 39% of revenues that's Online Legal, can you refresh our memory in terms of what are the main components that are keeping the growth from turning more positive? Thanks.

Stephane Bello - *Thomson Reuters Corporation - EVP & CFO*

So that's what we very much what we refer to as our Westlaw business and also Practical Law. This is really the two products that in our US online business.

And that's core legal research into the US. And I think what's impacting the core legal research in the business is general demand for legal services. So that's where we give you our Peer Monitor Index which gives you a sense of what the market demand is for legal services and that one has been just marginally positive for now a number of quarters.

So I would say its market demand is not very robust at this point in time. And that's the primary driver of the growth in that business given that they are really like two primary players in that business, LexisNexis and Westlaw. So these two players will grow most likely in line with the overall market demand.

Doug Arthur - *Evercore ISI - Analyst*

And do you still see sort of a tension between large legal firm demand and small- and medium-sized firms or is it all sort of going in the same direction?

Jim Smith - *Thomson Reuters Corporation - President & CEO*

Let me jump in. I think we've been surprisingly encouraged in both sectors over the past I would say six to eight quarters. And with the dynamic that's played out there you think about it Practical Law has been growing very fast, is a small part of the mix.

Westlaw is obviously and Westlaw in the US particularly is the big gorilla. And as you know we have a lot of price competition from Lexis in the marketplace. We were very disciplined about selling on value not on price and that appears to have been a successful, though painful, path to take and frankly we're seeing, what we saw was the downturn of Westlaw for a temporary period offset some of the growth in Practical Law.

We saw that stabilize and now Westlaw itself get back in growth for the quarter, which was highly encouraging. And we've done on the back of quality wins in the face of pretty stiff price competition. So I think if you're looking at the damper on that growth it's been price competition against Westlaw primarily from Lexis.

Frank Golden - *Thomson Reuters Corporation - SVP, IR*

That was our final question and we'd like to thank you all for joining us to review our second-quarter results. Speak to you again next quarter. Thank you.

Operator

Ladies and gentlemen, this conference will be available for replay starting at 1030 a.m. this morning and running through August 5 at midnight. You may access the AT&T executive playback service at any time by dialing 1-800-475-6701 and entering the access code of 363082.

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That does conclude our conference for today. We thank you for your participation and using the AT&T executive teleconference. You may now disconnect.



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