GAIN Capital

Third Quarter 2014 Results Conference Call

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CORPORATE PARTICIPANTS

Glenn Stevens, *President and Chief Executive Officer*

Jason Emerson, *Chief Financial Officer*

PRESENTATION

Operator
Good morning, and welcome to GAIN Capital's third quarter results conference call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. Please note this event is being recorded.

During this conference call, management will make forward-looking statements to assist you in understanding its expectations for future performance. These statements are subject to a number of risks that could cause actual events and results to differ materially, and I refer you to the company's press release of November 6, 2014, and the company's filings with the SEC for discussions of those risks. In addition, the statements during this call, including statements related to market conditions, the acquisition and integration of City Index, changes in regulation, operating performance and financial performance are based on management's views as of today, and it is anticipated that future developments may cause these views to change. Please consider the information presented in this light. The company may at some point elect to update the forward-looking statements made today but specifically disclaims any obligation to do so.

I will now turn the call over to GAIN's CEO, Glenn Stevens. Please go ahead, sir.

Glenn Stevens
Thanks, Operator, and thanks to everybody joining our call this morning. This is our GAIN Capital Q3 earnings review, and bear with me on my shaky voice today, but I'll be aided by my CFO, Jason Emerson, so we'll try to provide a team approach on this one.

In any case, following up on an announcement that we masde last week in terms of pre-announcing some of our macro results accompanied with the advice that we had acquired City Index, creating a very material scale for us, but we wanted to go into a little bit more detail today in terms of some specifics on our third quarter and year-to-date financial results and just an overall update on our strategy as we go forward.

There are accompanying materials posted publicly on our IR site, and I'll be using a particular deck as a backdrop, so for those following along the slides, I talked about our overall strategic execution. It's good to see a particularly strong quarter for us in Q3 when market conditions improved, but there's a couple of important takeaways from this set of results. Number one, we're not shocked by it, because what we've been trying to telegraph all along is that we manage the business not for necessarily 90-day segments but more of a broader-term perspective, and sometimes it's hard to do that when trading conditions oscillate or vacillate dramatically from one quarter to the next, and when you look at the volatility doldrums that many products suffered in Q2, you create a challenging environment to produce strong financials, but, more importantly, if your underpinnings are solid and you're delivering on the customer metrics in terms of new trading accounts, new assets, a new product rollout, opportunistic M&A — if you're methodically executing on that kind of intra-quarter but underneath holding it up, then when trading conditions improve, like they did in Q3 — not dramatically, just improved modestly, then the operating leverage and the results flow. So our job as a management team is to set the stage, and make our own luck, so when the sun is shining in that respect, we're able to capitalize.

So in this case, our strong third quarter results reflect basically a successful execution of a strategic plan that's been in place for a while and will continue to be in place. It's something we keep our eyes on, and it's something we continue to tweak as we see opportunities arise. We look for organic and inorganic growth opportunities in our retail business, particularly in periods of weaker market conditions, so when market conditions improve, they'll bear fruit. Also, in our institutional business we tried to see several years ago that this is a good complement to our existing retail business, and we've tried to build that by adding scale, adding technology, and adding talent in that business.

Our expense management was something that needed to happen in simultaneous fashion. It's one thing to grow top lines in business, invest in some early growth stage businesses within GAIN, but we also need to keep our eye on the fixed operating expenses, and we have some detail there to demonstrate our responsibility on that and continue to work and stay focused on it. Ultimately — I've talked in the past about lowering the threshold at which we can be profitable and increasing the level at which operating leverage starts to kick in, and that's done particularly by keeping your fixed operating expenses to the lower end of the spectrum.We have a slide in there about navigating regulatory changes and a shifting industry dynamic. It's a mouthful, but the reality is there's a certain skill acquired over the last 15 years that GAIN has been in existence that it's not a one-size-fits-all approach, and when you look at our go-to-market retail-wise, institutional-wise, there are seven continents we operate on, and all of them have their own nuance, all of them have their own set of rules, all of them have their own set of relationships that we need to cultivate and navigate successfully to be good at this. And I think ultimately that is a — kind of an unsung hero in this business, not to be forced into making strategic or pricing or policy changes that some companies may face, in any part of the market, whether it's FX, institutional, commission basis, non-FX products. You have to be enlightened by what's going on in the market, certain trends, certain sensitivities, and I think you have to really stay on top of that process, because ultimately it can become a hindrance to your success, and we want to avoid that and actually turn it into a strength at GAIN, and I think we're demonstrating that over time.

So the M&A strategy is one that I'd like to summarize in kind of four points, and the four parts of a successful M&A strategy include — I use the word "introspection" first, where you have to look internally and say where can we be stronger, what are our weaknesses, what needs to be enhanced? And we do that on a very regular basis in a very proactive manner and say what needs to be folded into GAIN? It isn't about me and my management team having a penchant for doing deals. It's about trying to bring in complementary products and services or geographies, a customer segment approach, and try to layer those in so that we become a broader and deeper offering for our customers and for our market opportunity. So when we do that, we try to identify what might be there.

Phase 2 is to say, "Let's survey the landscape of the market, and is anything available?" Sometimes opportunities for transactions are brought to our doorstep, sometimes we go and seek them out, sometimes it's a situation where a company may be in distress, sometimes it's a win/win situation, and so we go to Phase 2 and identify opportunities and try to do our best to engage in discussions.

Phase 3 is negotiating effectively, being fair, having a solid reputation, being able to do the due diligence in a professional fashion. Those are things that we'd like to believe is a learning curve, and with every deal we do, we learn to get a little bit better at it, and so when you get to that fourth phase, you've done all the work, which means, does this make sense for us? Is this something that is an opportunity that provides value for both sides? Is it going to create some lasting value and not just kind of an overnight hit or miss?

And then the fourth part, which is just as key as the other three, is the integration piece, and that's another one that people look past. They look at the flash of a deal, they look at the released aspect of it and say, "Wow, that's great, what a deal got done," but ultimately it's how you integrate that product, it's how you create the cost synergies, it's how you superimpose a smaller shop with a small set of products onto a larger global distribution network. So in many cases, we have to do that quiet work, that quiet kind of hard work in the dark to get the integration done so that the result translates into a longer-lasting value. And so with every piece of M&A, yes, we're quite active, but we have a very talented group at building an experienced learning curve and being able to finish off with that integration piece that tees you up to identify a new set of opportunities or even weaknesses or challenges internally to say, "What do we need to plug now?"

So with that, we've kind of demonstrated that by being able to clearly be successful in the M&A piece. We've closed four acquisitions in 2014, but there is a method behind the madness, if you will, with a broader strategic overview to say, "Look at these opportunities," be able to successfully negotiate and close a deal, and then work towards integrating it to create lasting value from a cost synergy part and from a revenue synergy part. So it's got to happen on both sides, and, we don't consider ourselves asset strippers, we don't consider ourselves as, I said, kind of serial deal makers. The threshold goes up every time you do a deal. Every time you plug a hole, you have a higher threshold that says, "What makes more sense now for the next — for the next steps?" and it's supposed to, in our minds, complement the organic part of the business, which is staying focused on our customer, building the metrics with customer assets, traded accounts — again, customer segment served, products delivered, and across the board.

So with that, I'll turn it over to Jason, and share — he can share some of the specific financial results from Q3, and we'll move on from there. Jason?

Jason Emerson
Great. Thanks, Glenn. Third quarter financial performance is the direct result of our ability to execute on our strategic plan of building an industry-leading global online trading company through a combination of organic initiatives and acquisitions on the back of improving trading conditions. GAIN delivered record net revenue of $103.7 million for the quarter, up 71 percent compared to the third quarter of 2013, driven by performance of the retail OTC business, coupled with the continued growth of our commission-based businesses. As a result of the collective performance across all businesses, we delivered strong earnings and operating leverage.

Revenue for the quarter was up 49 percent, while total expenses were up only 7 percent relative to last quarter, yielding an adjusted EBITDA of $27.5 million, net income of $15.3 million, and adjusted EPS of 37 cents per share, all significantly higher than the results from last quarter.

During the second quarter earnings call, we spoke about our ability to deliver strong earnings and operating leverage as a result of our success in growing our key operating metrics when trading conditions exhibited modest improvement. Our team continued to execute on building the strength of our operating metrics across our retail OTC and commission-based businesses during the quarter. Our retail volumes of $605 billion were up 53 percent relative to the same time last year, reflecting the combination of building our customer base through acquisition and our organic efforts to attract new customers, coupled with the increased client engagement from improved trading conditions.

Institutional volume delivered solid growth of 31 percent relative to the third quarter of 2013. Volumes from our GTX business have been driven by double-digit growth of our unique users trading on the platform as well as increased activity by our agency sales team.

The Sales Trader business acquired as part of the GFT transaction has been a significant contributor to the year-over-year growth of the institutional volumes. Our exchange-based futures business executed more than 1.8 million contracts in the quarter, up 39 percent, driven by the growth of our legacy introducing-broker business acquired in 2012, coupled with recent acquisitions of Daniels Trading and Top Third, which closed earlier this year.

Let’s take a look at our performance for the year, moving to the next slide. During the second quarter earnings call, we reported results for the first half of the year that reflected the decline in market conditions of the retail OTC business from Q1 that accelerated throughout Q2 and based on where we stand now, looks to have bottomed out in early — in the third quarter. As a result, the third quarter results have had a significant contribution to our year-to-date performance.

Total revenue of $254.8 million for the year is up from $183 million for the same period in 2013, due predominantly to the combination of the GFT acquisition as well as the growth of commission-based businesses, including recent acquisitions made this year. Adjusted EBITDA and net income and EPS for 2014 through the end of the third quarter reflect the challenging market conditions that faced the retail business in the first half of the year, combined with the strong performance experienced in the third quarter. In addition, we are in the first stages of realizing the reductions in the core fixed operating expense base in the first half of 2014 compared to where we stood at the end of the third quarter, where we have nearly achieved the full synergy capture from the GFT transaction and expect to see the target run rate benefit by the end of the fourth quarter of this year.

You can see our operating metrics remain robust year to date, with double-digit gains in retail, institutional, and futures volumes as well as a 25 percent increase in funded accounts. This shows the strength of our client engagement as market conditions improved in the third quarter.

Let’s move to the next slide and take a closer look at our results for the quarter. Our retail OTC business delivered strong performance for the quarter on the backdrop of improving market conditions, which drove client engagement. We experienced a range of trading conditions in the quarter, from the lows of July, where revenue per million was below the bottom end of our trailing 12-month average of $80, to September, which was more than 40 percent greater than the top end of our trailing 12 months of $120. As a result, the third quarter retail OTC revenue of $64 million was up significantly versus last quarter and 26 percent higher than the third quarter of 2013.

Our retail OTC business is well positioned to deliver operating leverage from the powerful combination of our solid operating metrics as well as our ability to successfully integrate the GFT business and achieve our annual run rate reduction of $35 [million] to $45 million in the fixed operating expenses as market conditions improve towards more normal levels relative to the trailing two years.

In addition to the strong performance of the retail OTC business, the commission-based businesses delivered $35 million of revenue, up 8 percent versus last quarter and nearly three times the third quarter of 2013. As a result of the improving trading conditions of the retail OTC business, coupled with the growth of the commission-based businesses, adjusted EBITDA for the quarter was $27.5 million, yielding a margin of 27 percent. This is significantly higher than the adjusted EBITDA loss of $1.6 million last quarter and the adjusted EBITDA of $12.1 million in the third quarter of 2013.

Net income for the quarter was $15.3 million, or 33 cents per diluted share. Adjusting net income for restructuring- and acquisition-related expenses, we get a figure of $16.3 million, or 37 cents per diluted share, for the quarter. We are now presenting cash EPS to highlight the cash generation performance of the business. For the third quarter, this was 42 cents per share.

Revenue diversification efforts continue to progress with the retail OTC business as well as through the growth of revenue from commission-based businesses. Trading in non-FX products, which are predominantly CFDs and indices, equities, and commodities by our retail OTC customers, grew to 27 percent of volume in the third quarter compared to 13 percent a year ago. Additionally, the percentage of revenue from the commission-based businesses was 34 percent, up from 21 percent a year ago. Our efforts to grow the commission-based businesses are yielding tangible benefits as can be seen by the year-over-year revenue of $97.2 million, up significantly from $37.7 million for the same time in 2013. The strategic goal of expanding into the commission-based businesses is to generate more stable revenue and reduce the volatility in earnings of the firm overall. We are successfully executing on that strategy.

Lastly, on the bottom right, we highlight our retail revenue per million over the trailing 12 months as well as our capture rate for the quarter of $106.

I'll turn the presentation back over to Glenn for an update on our strategy and business performance.

Glenn Stevens
Thanks, Jason. Again, the focus overall is to try to continue to build the underpinning — the underpinning drivers that can put you in the right situation, so when market conditions improve, it's hard for us to gauge what overall volatility will do in short periods of time. We've seen that already in 2014 as a poster child for kind of a Jekyll and Hyde scenario where, Q2 was at nearly decade or beyond decade lows in currency volatility, Q3 showed a little bit of life, in terms of some of the volatility creeping back in - in currencies, and so regardless of where we believe the next several quarters will be in terms of volatility, it would be nice to believe that we're going to have an extension of coming out of the doldrums. But, beyond that, even if we don't, the idea is to expand the basis of our revenue. The idea is to expand the customer set that's driving that revenue. The idea is to expand the services we can provide, whether it be an institutional ECN that's commission driven for large participants or it's an advisory service or it's non-FX. And so that's really the crux of the — of the strategy here, and from a quarter-to-quarter basis, there's still exposure to overall market volatility, and it's hard to get away from that completely, but you can build a broader base.

So if you look — again I'll mention that, our third quarter results are really focusing on our strategic plan, and in this case, they were highlighted as the operating leverage kicks in when you're able to scale and keep your arms around the fixed operating expenses. Revenue streams can be diversified in multiple ways. You can do it across geographies, you can do it across products, you can do it across being direct or indirect, or you can do it across where that revenue is derived from in terms of — in terms of commission or market making. And in this case, the first highlight is scaling your retail business, and on Slide 8, we talk about up and to the right is really the charts and the way we hope they want to be able to come out, and in just about every single case, that's been the result, and so if you look across the period over the last call it two years, from Q3 of '12 through Q3 of '14, take a look at our client assets, take a look at our trading volumes, take a look at our number of funded accounts, and all of those are pointing to the direction that we've been trying to work towards, and it's pretty dramatic. Take away customer assets, for example, and you are able to look at a move of a CAGR of over 41 percent in that two-year period. In Q3 of '12, we had $427 million of customer assets, and that number stands at Q3 at $850 million, and so commensurate results out of funded account and out of daily retail volume works the same way.

In terms of the revenue streams, we've added new business lines, and, the idea is to piece together some of the story that doesn't always link up intra-quarter or even quarter over quarter. I'll just take an example of the GTX as a business line, and we launched that in 2010, and in 2013 acquired in the GFT transaction, we brought in the Sales Trader business. Those were both focused on clients much larger than our traditional retail client that we served in earlier years at GAIN. And if you look at the total revenue coming out of that, it was 22 percent that came out of that business in Q3, 22 percent of our revenue compared to 10 percent two years earlier. And it's important to realize that that's in a rising total revenue environment, so it's not just — that percentage didn't just go up because other revenues went down. In a growing pie, we were able to more than double the contribution coming from that customer segment.

The futures business is another example. Now it's kind of a three-stepper. In 2012, in Q3 of 2012, we closed on a technology platform introducing broker business, called Open eCry, from Schwab, and we took in a little less than $100 million of customer assets on that. Those customer assets now stand at over $200 million, and with the closing of Daniels Trading and Top Third earlier this year, we were able to complement that existing trading platform in technology with an outbound sales group and a marketing group and essentially create a unit that made sense. Now the goal is to say, "Let's take that collective group of technology and marketing and sales and see what we can do about doing a better job of superimposing it on our global distribution and in our global brand. So it's a process, right? It's a three-step process in this case, where you identify a need, you are able to either in-house build it, or, in this case, acquire a skill set and technology, and then broaden the offering and use GAIN's global brand and global distribution to drive even more value out of that business than when it was independent. And, again, it ends up in a win/win situation.

In terms of the product diversification, a key takeaway there is to look and see that for Q3, the trading volume from FX products was 73 percent of total volume versus — that number was 92 percent two years ago. Again, it's not de-emphasizing it in FX, but in a growing-volume environment, we've been able to bring in non-FX volume so that we can, create a broader and deeper foundation, not just for our revenue dependency but also for the customer experience and so we can have a stronger relationship with them.

In terms of that diversified revenue stream, go to the next slide, on number 10, and, when you look at institutional business as an example, , with the retail, we've been able to ramp that, but, again, the focus there was to bring that in as a complement to our retail business and say, hey, how do we — how do we leverage some of the strength we've established over the years there, and what can we do for institutional clients, what can we offer as a real solid alternative to that market, and does it mean you've divorced yourself from market volatility? No, institutional users are subject to market volatility the same way that retail customers are, but in this case, you're able to set up a more sticky, deep relationship, and we continue to build new users on that platform because of service, because of execution quality, and because of technology and because we're able to compete with the largest providers in that field, and we expect nothing but great things in terms of growth. The nice thing there is we've only scratched the surface, and we see a lot of upside in that business.

Those are some examples of doing organic and inorganic. The next slide talks a little bit about executing on our M&A strategy, and, again, there's a quite large arrow in the illustrative [sic] on that one, and that's certainly to the right and up, but we tried to point out some of the methodology behind this. And so on the bottom is the trend of client assets, overall from 2008 at $124 million to as of the proforma close of the City Index that we announced earlier this week, client assets of $1.2 billion, so if that looks like a 10X, that's because it is, and the reality is that that's a good demonstration of our ability to keep building the scale and keep building the opportunity, if you will, in our business overall. But with a little more granularity on the topside, you look at where does that come from, and it comes from different types of opportunities, whether it be buying retail assets from a provider that's pulling back out of the business, it might be build our institutional business through acquisitions like GFT and City Index, through product enhancements with Daniels and Top Third, and even examples of Galvan Research as an advisory business out of the UK that's got a strong brand advising clients, particularly in non-FX opportunities, particularly in the UK and Europe, and so that's a great business the way it was operating, and we saw an opportunity to team up with them, bring them into the fold. I

t's been a great addition for them and for us, and the situation there is that they were doing quite well by themselves, but we were able to have a discussion and build a partnership so that we can take their products, take their expertise, and provide broader and deeper distribution, so the results flow to them and the results flow to us, and ultimately we end up with a complementary service that can build a stronger relationship with our clients and broaden the scope of geography, or broaden the scope of type of clients there, so that's just one example of how we try to do strategic M&A, right? It's not just willy-nilly M&A, it's strategic M&A.

So just kind of an overview there with continuing to march forward. The offset to all that is managing fixed operating expenses, and I'll have Jason walk through that, because that's the — that's the flip side of the same coin to make this machine work properly.

Jason Emerson
Great. Thanks, Glenn. Let's spend some time looking into our efforts to manage our fixed operating expenses. Our ability to successfully execute on our strategy of building an industry-leading retail OTC business while expanding into commission-based businesses through a combination of organic and acquisition-related activities has a multifaceted impact on our expense base. With that said, limiting the fixed operating expense base is a focus for GAIN, even as we scale our business.

Looking to the retail OTC business, part of our strategy is to build scale in terms of our key operating metrics of customer assets, funded accounts and volumes, through acquisitions and delivering operating leverage by lowering the combined fixed expense base where synergies exist. Our ability to successfully target, acquire, and integrate in this space can be measured by progress we've made with GFT acquisition, which we closed at the end of September in 2013. Within 12 months of closing, we've largely completed a lion's share of integration activities, which have allowed us to successfully capture the annual run rate reduction of $35 [million] to $45 million and the combined fixed expense base of the core gain in GFT businesses when compared to 2012. As we can see, core fixed operating expenses, adjusting for variable expenses as well as direct expenses related to new businesses through the end of the third quarter in 2014, of $97.9 million are down $21 million and $37.3 million relative to the same period in 2013 and 2012.

Since closing on the acquisition, the operating metrics of the customer base we acquired from GFT are strong, while we forge ahead on integration activities. This is a key part of our integration approach to preserve the customer experience and retain revenue while methodically reducing the fixed expense base to deliver operating leverage. Third quarter results demonstrate the earnings potential when we returned to more normal trading conditions on top of our ability to execute on this strategy.

The recently announced acquisition of City Index Holdings will further our ability to scale the retail OTC customer assets, funded accounts, and volumes, while diversifying revenue across geographies and products. This, coupled with our ability to reduce the combined fixed operating expense base of GAIN and City Index by $45 [million] to $55 million relative to the trailing 12 months ending September 30, sets the foundation to deliver operating leverage as market conditions revert back to the average levels we've seen over the past two years.

Alongside the growth of our retail OTC business, we've made investments in new businesses that are part of our larger strategy to diversify revenue, products, clients, and geographies. We've aligned direct — outlined direct expenses related to these new businesses over the past few years to isolate their impact on the total expense base and highlight our ability to achieve the GFT synergies as well as to present some information on the expenses related to these new businesses added to GAIN over the past three years. During the quarter, we performed additional cost reductions above and beyond the GFT synergies, aimed at lowering our fixed expense base in the event trading conditions of our retail OTC business fall below the low end of our revenue-per-million range of $80. These actions included a reduction in force that will reduce the compensation and benefits line by at least $4 million annually, which will partially benefit fourth quarter results. In addition, we made other changes that will reduce trading expense, communications, tech, as well as G&A,that will result in additional reduction of expenses of $4-plus million annually. A significant portion of these savings will flow into the fourth quarter results and more fully in the first quarter of 2015. We continue to work on efforts to lower our overall fixed operating expense base to maintain profitability when we experience challenging trading conditions in the retail OTC business as well as deliver operating leverage when trading conditions revert back to historic levels.

Moving to the next slide, GAIN will distribute its quarterly dividend of 5 cents per share on December 22 for holders of record as of December 12. We did not make any purchases under the approved buyback plan during the quarter but are prepared to opportunistically buy back shares.

Moving to concluding remarks, in summary, the third quarter results reflect a successful execution of our strategic plan buoyed by improved market conditions. Our continued focus on growing fundamental operating metrics in our retail OTC business was a significant contributor to performance in the quarter. Our rapidly growing institutional business was a major contributor to results, and we continue to deliver on expense management, with over 20 percent reduction in core fixed operating expenses year over year and are on target to achieve the $35 [million] to $45 million reduction of annual fixed operating expenses compared to 2012, resulting from the GFT transaction. Our clear and demonstrated M&A strategy to increase scale and diversify product offerings as well as revenue streams is contributing to our bottom line results.

Thank you for attending our third quarter earnings call, and we'll now turn the call over to the operator for the question-and-answer session.

QUESTIONS AND ANSWERS

Operator
We will now begin the question-and-answer session. To ask a question, you may press star, then 1 on your touchtone phone. If you are using a speaker phone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then 2. At this time, we will pause momentarily to assemble our roster.

The first question comes from Rich Repetto of Sandler O'Neill. Please go ahead.

Rich Repetto
Yeah, good morning, Glenn. Good morning, Jason.

Glenn Stevens
Hey, Rich.

Jason Emerson
Hey, Rich.

Rich Repetto
Hi. So you gave us more color on the intra-quarter results as you promised, and a little astounding, I guess, if I did my math right. So if you said September was 40 percent better than the high end of the $120 top-end range, so I'm — calculates up to about $170 revenue per million. I'm just trying to see if that's accurate. And then the next question would be, certainly volatility and volumes across asset class has picked up further in October. Can you give us any, color on where that number might be, even just a general range, maybe not specifically in October?

Glenn Stevens
So, yeah, we're trying to respond to the calls for more granularity and more detail, so as a good reporter, Rich, you got more and you're asking for even more, so you're doing your job, and that's a good thing, but in terms of getting too specific on even proforma numbers or as the ink is just drying on the previous month, I think the safest thing to say is that the increase in volatility that we saw intra-quarter for Q3 seems to be holding to some degree. I alluded a little bit to that earlier in my talk about saying that we don't know — if Jason used the words defined a trough. You know, he's not making a definitive statement obviously, or he says, "That's it. That was the bottom of volatility," because involved traders would start calling him on a daily basis, but I do think it's something that we know we can't control, but we want to be able to manage and be receptive too, so, yeah, it's so far, so good in terms of the quarter, in terms of where overall trading conditions are, and generally speaking, we are poised to do better, I mean, which is the whole point of our pitch here, is to say that you have to build the business to be prepared to — sorry to use the cliché — make hay while the sun is shining, and, it rained for about 40 days and 40 nights for a while there in parts of Q2, and, look, we've seen that before. 2012 was pretty soft for a protracted period. We got seven months into 2014, but to be fair, part of the reason also for diversifying our product mix, meaning non-FX, growing some of that capability and

different types of customer segments, growing those businesses, we hope will help soften the waves, when they come, either on the negative side — and so, yeah, we've seen, I think just by looking at the cold numbers in terms of entry dates, your average daily trading ranges, seeing the majors still move around with euro and yen and obviously the dollar, and so someone asked me in last quarter, "Hey, I saw the ruble move a lot, and we saw the Argentine peso move a lot." It's helpful, but the truth is the volumes and the focus and the customers' activity in those kinds of products is small. In this case, we're seeing a shift in some of the, more highly volume — high-volume products move around, and that's a good thing. So I guess I'll stop short just by saying that we have seen some continuation in that respect do well, but it's pretty hard to be in the predicting mode.

Rich Repetto
Okay. Maybe I could rephrase it just slightly, and, again, I don't want to spend any more time than what we have, but the — just from the metrics that you see, and I put this to another CEO in a different industry, but the metrics that you see, would you expect directionally that you performed as you'd expect from the public metrics that we can see, higher —

Glenn Stevens
Fair enough. So a couple of things. Again, trying to — and it's hard to do, but trying to push the broader perspective, I think when Jason highlighted the $96 trailing revenue per million on the retail business, I think we've been pointing to that for a while, saying, Fortunately, we've seen that hover around $100 in the one-year, two-year, three-year, four-year trailing averages. That doesn't mean that intra that you can have 25 percent on either side of that, and we've shown that. We've shown — we just showed periods of $125, $130, we've shown periods of $70, $75, so when you have a whole quarter at $75, the results aren't particularly stellar. When you can come in at $125, as long as your business is set up with fixed operating expenses and other things, then you should reap the benefits.

So I'm not trying to be dodging of your thing, but I guess what I'm saying is that from a modeling perspective, from an expectation perspective, over the longer period, it's actually been pretty consistent, if you will, between $95 and $105 on the narrow, and it doesn't mean you can't have periods of 20 percent outside of that, but you have seen a decent — not a super high coefficient of causation there but a pretty decent correlation between higher volatility and higher opportunity, and that continues to remain intact. So, yeah, I think that, if we can maintain levels of market activity, it's kind of a double whammy, Rich, because it's not just straight translation into high volatility brings you higher revenue. It also means it's easier to engage clients. It also means clients care about their account to want to be active in it and at a higher level of engagement and listen to the advisory that you're selling or listen to the services that you're offering, and if your market is in doldrums, it just puts demands on your marketing, on your sales, on your conversion, and on your - things that are built around activity and client engagement and attracting customer assets. So it's really across the board. It's not just — it's not just the volatility piece.

So I guess what I'm saying is I try to orient you guys in general to say if you can look beyond the quarter and look into multiple quarters, this is — this Q3 is another example of a bit of a regression to the mean, and the mean is actually pretty healthy as long as you can be wary of getting too caught up on some of those quarters where it's in the doldrums, and on this one, we didn't even see a particularly strong three-month quarter. The quarter continued to strengthen as it progressed, and we're seeing an extension of that, which is great, but it does have, particularly in shorter periods, whether it's 30 days, 90 days, or 120 days, you can see periods of overgoodness and overbadness.

Rich Repetto
Got it. Understood. That's helpful, Glenn. And I guess to turn the subject — or change the subject on expense, Jason, I caught some of it, but I didn't catch it all, but you — what I thought you said — you basically achieved a $35 [million] to $45 million in, you know, integration cost savings from GFT, and you went beyond that by $4 million. Is that correct? And so, I guess, to verify the numbers and how they're going to play out in the coming quarter, that's one part. And the other part is is there any offset of investment spending, either 4Q or next year, to take against these, good reductions that you're pulling out of the PIC [phonetic] space?

Jason Emerson
So, Rich, in terms of highlighting the capture of the GFT synergies, by the end of — we say — I mentioned we captured it — we basically made the decisions, and we'll see the full impact of the annual reduction in fixed operating expense run rate in the fourth quarter, so it is the midpoint of approximately $10 million relative to 2012 combined fixed expense base. So in relation to the additional effort — so we made headcount reductions, which on an annualized run rate basis, will reduce the comp and ben line item by $4 million, and then — so that's, effectively $1 million a quarter. We'll see a meaningful portion of that in Q4 but just because of the way benefits and some other things will run off, we'll see the full effect of $1 million per quarter in Q1, and then we made other changes across various and other initiatives to reduce fixed expenses and trading expense, G&A, coms and tech and so on, that look to achieve at least a $4 million-plus annual reduction in fixed expenses, and some of that will come into Q4, and the remainder of that in terms of — call that $1 million a quarter, and then the remainder of that we'll see in Q1. So we should see effectively around a $2 million reduction in fixed expense base by Q1 based on those initiatives.

Rich Repetto
Okay, and there's no offsetting plan that you see right now — investment spending that could potentially bring up, offset some of that?

Jason Emerson
Yeah, as we highlighted, the direct expenses from new businesses, those are businesses that we continue to invest in to grow the business, but generally it's —that's related to, operating those new businesses we've added, but there should be no significant, investments other than, the normal operating costs related to those businesses, so barring any, tuck-in acquisition or anything of that nature.

Operator
The next question comes from Niamh Alexander of KBW. Please go ahead.

Niamh Alexander
Hi, thanks for taking my questions, and congrats again on such a strong quarter. And just a few things for the model, if I could. The other revenue, $4½ million, that was a lot above what we're used to seeing, so is this kind of a new revenue line with some of the acquisitions that we should model going forward?

Jason Emerson
Hi, Niamh, this other revenue has to do with us being a global company and having jurisdictions outside of the U.S., where the functional currencies in those other entities are not U.S. dollars, and so there is a result of —during the quarter, with currency movements, we saw an increase in the fluctuations and the translation of those other assets that resulted in —

Glenn Stevens
And the thing is, Niamh, part of it's with scale. We've been managing — you're absolutely right, we were managing that intra-quarter or quarter-by-quarter amount to a somewhat lower number as — and as the business scales, I think it's interesting, if you look at one of the other larger participants in this — in this market, I think they announced north of $200 million in FX-related revenue. So we're never going to approach that kind of scale, but, for us, if we were in kind of the 1-to-3 range, this is well within where we could see it moving, but it is something that we can put kind of — kind of guardrails on, but it does have to do a lot with being truly multinational now and having to dollarize everything for reporting. I don't want to use the word noise, but it is something that we can — we can manage and we are managing. It's just that from an administrative perspective, trying to manage it down to zero, by the way, has its own costs, and so that's kind of why in this case you had some pretty strong movements. Obviously, in the — in Q3, you had some pretty demonstrative movements in the euro and the British pound and in the dollar-yen, and we — guess what, we operate in all those locales, and as our customer asset base goes bigger and our P&Ls are bigger, it sometimes can bring higher up other revenue.

Niamh Alexander
So some of that goes through the OCI and the balance sheet, and then some of it ends up kind of in trading. Is that it, kind of trading revenue with the translation?

Jason Emerson
Correct.

Niamh Alexander
Yeah, okay, fair enough.

Jason Emerson
And other revenue, not trading revenue, other revenue [inaudible].

Niamh Alexander
Yeah, sorry, but it's kind of the trading assets that you're translating that creates that line, right?

Jason Emerson
That's right.

Glenn Stevens
That's right.

Niamh Alexander
Okay, fair enough. And then just, I guess, on the trading and the market making, the balance sheet, I mean, there's a lot in the cash at the end of the quarter versus —first of all, we've seen historically, and then the collateral, you have with other brokers dropped [phonetic]. Is that — have you been hedging less? Is that what helped the recapture so much, or, is it just coincidence that suddenly it's kind of that much higher? I'm just trying to understand, if you have kind of made the decision, you usually hedge what, about 95 percent of the open positions? Is that changing?

Jason Emerson
Yeah, so, Niamh, we made a change in presentation with relation to cash, so historically we had access, so our receivable from brokers is all cash, and a large portion of that is typically tied up in required collateral, and then we have open positions, and then we have futures, and then we have excess cash. So going forward, from Q3 forward, we will show our cash and equivalents — we'll move that excess cash out of receivable from broker and hold that in our — and move that up to the cash and equivalents.

Niamh Alexander
Oh, okay. So you have — and you're still hedging 95 percent of what you're —

Glenn Stevens
Yeah, no change in model, Niamh. Again, I think what was — what we tried to do is move the cash depiction to a clearer methodology. It was raising more questions than providing answers in the receivables from brokers just because, I guess, the traditional nomenclature with that kind of was different than the actual cash that it is, and so, we're able to view our brokerage liquidity providers and our bank liquidity providers — they're one and the same in terms of protection and value and the whole bit, but when you start breaking them out, it kind of creates confusion, so from an operational model, from a hedging perspective, nothing's changed.

Niamh Alexander
Okay. That's important, because, then I have to start thinking about maybe more capital intensive, but as long as you're hedging the same level, that's good. And then — I'm sorry, just on the model as well, just the tax rate, was a lot lower this quarter. Is this kind of part of the diversification, or, is there something unusual in there?

Jason Emerson
No, so, Niamh, from the perspective of our growing global operations and implementation of our transfer pricing for this year, for 2014, we saw a reduction — we'll see a reduction in our tax rate on kind of a year-over-year basis as a result of the differential, so I would expect, from your modeling perspective, I think we used to say between 29 and 30 percent. It's probably better to, model it in kind of the 25 to 28 percent. We should see a couple of hundred basis points come off, at this point, and then clearly as we go forward and close on the acquisition of the City Index, we'll provide further guidance at that point, because we will, definitely have had a change at that juncture.

Glenn Stevens.
Kind of a positive byproduct, Niamh, on the globalization of our business, again, moving to more non-U.S. revenue opportunity and putting in some of the structural improvements over the last couple of years. They obviously pay more dividends when you make more money than when you don't.

Niamh Alexander
Okay, fair enough. All right. I'll get back in line. Thank you.

Jason Emerson
Yeah.

Operator
The next question comes from John Dunn of Sidoti & Company. Please go ahead.

John Dunn
Morning. I wanted to switch to the institutional side for a minute. Can you just talk about some of the market share gains you're making on the institutional side and what's going on with some of the bigger guys?

Glenn Stevens
I think, John, in that business overall, that it's a fairly narrow spate of providers. It's not nearly as crowded as revenue providers are geographically. It appears that on the institutional side, it's focused more on global players. I mean, there's still some pretty strong regional players on the retail FX piece and CFD business, but on the institutional FX piece, it's a — it's a fairly global business. If you look at ICAP's CBS [phonetic] unit, if you look at KCG's Hotspot unit, if you look at Reuters FXO, I mean, those have been preeminently the biggest providers in this business, and so, it's our job to see how we can fit in.

We all have our niches in terms of who we can serve. I think if you look at our average trade size and you look at the increasing number of participants that we've been adding, it's helpful to see that our business continues to gain traction on that side. We have a real strong group of talent that works in that group. We continue to add to that. We announced last quarter of acquiring the full intellectual property for that business, so it's an asset internally for us on our balance sheet, which means we can grow. We successfully launched our SEF to be able to be right up in the forefront in terms of regulatory applicability there, so across the board, I think it's no big bang there.

It's having strong technology, providing great service, having longstanding experience and skill set in that group and leadership there, and being able to deliver. And as far as we're concerned, we think that's a business we can continue to grow, not just by hope but by having industry-leading technology. By having the focus of being able to be flexible, we can get in there and not say, "Hey, here's how you have to do business with us," but more about, "How can we do business with you?" And whether that's bespoke liquidity pools or whether that's different types of products, NDFs, metals, or certain types of solutions that can be branded or be used as an in-house platform, there's lots of ways for us to continue to grow that business, so — and given, frankly, where our market share is in mid-single digits, I feel like it gives us a tremendous amount of upside without having to have, 50 percent of the market.

John Dunn
Gotcha. And then could you just, post [unintelligible] and the election, some of the factors, you know, over the next six months that you might point to as being able to sustain volatility?

Glenn Stevens
Well, that's a — that's a good loaded question, so I think the rule in my house was no politics and no religion at the dinner table, but in terms of that kind of stuff, look, number one, interest rate divergence is always a good opportunity to move products around, and if the U.S. can show the ability to be comfortable with a tightening rate environment, which it appears to be — and, again, I'm no expert in terms of prognosticating where rates are going. I think I joined a lot of people in being three years early, that said rates were going to go up, and we all waited a long time with money and cash instead of anything else. And so — but if you look at recent events, and you see Japan going after a more easing environment and the U.S., if they are indicating getting more comfortable with a tightening environment, what matters to us is divergence. So there's a great example of dollar-yen. It's not just U.S. rates moving or rates going higher. It's rates diverging. And rates diverging brings in new participants for hedging, for putting on the classic carry trade, for trading currencies based on future value, because rates have changed

[unintelligible]market rates have gone out, so, yeah, there does seem to be some underpinning, but I guess part of it's the rubber band theory too, to say rates were so locked in, stagnant, and globally zero, that having them move just a little bit shouldn't shock anybody, because they really were locked in the doldrums of not moving around. So in terms of that, yeah, I think we see the makings of some extended moves on that case, but it will be important to see if it goes on there too.

I guess the other thing to factor in that, outside of that, one of the reasons we've tried to continue to build our CFD presence to this point, and we'll amplify that even more as we integrate the City Index building — business, is that the equity models matter, right? And so seeing equities move around, not that the Dow is the bellwether, but 100 points a day is pretty [unintelligible] now, and so it's nice to see that, because that's good for overall, business. If you look at the DAX, the movement there, you look at the price of oil, if gold starts to, get a little flaky in its price action, these all complement that, so interest rates are a big one, absolutely, and it's been one we've been missing for a while, by the way, but there are lots of other players in that show.

Operator
The next question comes from Daniel Fannon of Jefferies. Please go ahead.

Daniel Fannon
Thanks, good morning.

Glenn Stevens
Hi, Dan.

Jason Emerson
Hi, Dan.

Daniel Fannon
I guess, Jason, just looking at Slide 12, just making sure I understand the fixed costs kind of trajectory, so the $80.7 that you're pointing to actually — or actually I should say the $30.5, the numbers you called out around both the G&A incrementally of $4 million plus the additional $4 million in other kind of cost cutting, that's really not in the Q3 run rate for fixed costs. Is that correct?

Jason Emerson
Part of it is very — a small portion. Most of it will — some of it will come into Q3, and all of it will come into, Q1. We should see more of it in Q1.

Daniel Fannon
And that's —those are some large numbers compared to where we were last quarter. I guess are there other things that you're still working on, or is this basically what you flagged last quarter as kind of what you think you can take out?

Jason Emerson
Yeah, these are the, the most immediate. As we spoke about in the last call, there are certain levers, and it takes time, and, in terms of identifying, additional costs, and also as we look to the City Index transaction and looking at the synergies there, so we're going to be mindful of, in terms of making sure we give you guys the right information in terms of adjusting the fixed cost base, so at this point, those — that's where we are. And as we dive into the integration efforts

with City Index, we'll provide, some more guidance on potentially anything in addition to the synergy numbers, between GFT, finalizing those this quarter, and then starting on with the City Index once we close, hopefully the end of the first quarter.

Daniel Fannon
Great. And then I guess on the City business and, really, I guess the CFD kind of market, is that — because I don't know that product as well, and I guess can you talk about the volatility and trading of that product and asset class and how that compares to what your traditional FX and now your institutional business looks like? Is it — does it provide a broader diversity, or is there similar kind of volatility effect to it with — that is going to result in more macro dynamics driving it, or is there a more consistency to the volumes over time?

Glenn Stevens
So, Dan, first of all, it's not a particularly new product for us in terms of understanding it. When we made the acquisition of GFT last year, they already were offering a broad spectrum of CFD products, and so on some level, the CFD business for City Index that they're more heavily focused on is more of the same. What it — what it ultimately does is continue to move more mix into a more even-based pie that isn't so dominated by FX, and so we made the point there of showing that non-FX volatility — sorry, non-FX revenue now is derived of 27 percent, whereas before it was only 8 percent. We expect that number to get even larger with City Index, because just by virtue of the fact that City Index is, 70-plus percent of CFD business, you add that to our existing business, we'll probably go 60/40 on a proforma basis. If we're 73/27 now, once that's fully integrated, we'll be more like 60/40.

So what does that mean? You asked a question about the drivers of that business. They are similar to FX in that what drives equity volatility or industry volatility or commodity volatility, interest rates, geopolitical unrest, all those kinds of things, and so generally speaking it goes back to that higher vol in those products generally translates into positive results, not just because there's an ability to capture more spread, there's more two-way interest, but it's also higher level of engagement for clients. Clients see a market opportunity when it's moving. If a market is stagnant, they don't see a client opportunity, and so they don't — they don't get into that.

So I think that, if you look at some of these businesses, then you can see that — the IG market is a good example of a UK-based shop that's got a big CFD-based business with a huge chunk of market share there — I say "there," in the UK and European markets. CFDs aren't prominent in the U.S., obviously, but it is a business that's gained a lot of traction outside the U.S. in Europe and the UK, in Asia, and it's a product we think is a perfect fit. It's this concept of providing a broader and deeper experience for the client, to give them more things to trade, give them more things to invest in. It can only make sense. When they move, it's better for business overall, so in terms of characteristics like you asked, it's got — it's got similar drivers. When it moves, you have the ability to get, clients trading with each other. You can provide a very robust market, and, by the way, then your complementary businesses, like advisory or like, your charting information or what have you, just becomes that much more appealing, because it's applying to a market that's moving. So in that case, it's very similar. For us, we're just trying to broaden the overall there.

So the one good thing is that CFD vols don't — aren't perfectly correlated with FX volatility, so we're broadening the base a little bit there by being able to say, hey, there's going to be periods where FX rates will move around, but equity markets are stagnant and vice versa. So we get a little bit of that diversification of vol reliance, if you will, by adding that product, not just from the customer side but also from the market side.

Daniel Fannon
Okay, and I guess just one last question on the income statement. It's small, but the bad debt provisions picked up and it's not a big number, but I guess is that just a function of activity levels and the pickup that you saw in the quarter, or is there something else?

Jason Emerson
Yeah, Dan, you're spot on there. The majority of that is related to the pickup in the retail OTC business, with, a little bit on the futures side as well.

Daniel Fannon
Okay. Thank you.

Glenn Stevens
Thanks, Dan.

Operator
Again, if you have a question, please press star, then 1 on a touchtone phone. The next question comes from Zach Arrick of Senvest. Please go ahead.

Zach Arrick
Hey, guys.

Glenn Stevens
Good morning.

Jason Emerson
Hey, Zach.

Zach Arrick
Nice quarter. Glenn, in your opening remarks, you mentioned that you didn't think the conditions improved dramatically, something along those lines, and so I'm kind of wondering where do you — what would be a dramatic increase? Where do you think kind of like a — excluding City — and just on your business now, kind of what do you think business looks like when interest rates start moving around and it's more of a new normal?

Glenn Stevens
So one of the benefits or pitfalls, I guess depending on how you look at it, of having as much experience in this market as I do in terms of watching it, is that it gives you a perspective that doesn't go back six months or a year. It can go back ten, and so I guess I'll answer your question by saying, okay, so what is the normal? If you go back to 2008 and you look at kind of our measure or an index of volatility, then let's use the CVIX, for example, as an example like that. And so you look at the CVIX back in 2008, it got as high as almost 25, and then when you look at in the beginning of 2014, it was as low as 5, so just in a simple five-year or four-year parameter there, what was right, 5 or 25? So I'm not saying that it was — that it was 25. I guess what I'm saying is that there's lots of opportunity to see it around 10. For many of those years in-between there, you could argue that if we're currently, in the kind of mid-67-ish number, then you could — why couldn't you be a 10 for the same period? Unfortunately, we could just as easily be hanging around back at 5, and if we were at 15, great. And, by the way, it's not

linear. It's not perfectly correlated, right? I've said a bunch of times on the one end, there are periods of volatility that customers don't like. If average daily trading ranges are so nasty, people sometimes recoil from a market and say, "I'm confused. Let me wait. Let me let the dust settle." In other cases, you have this volatility over a period, but it's very methodical, so you don't get two-way participation.

So in trying to answer your question, yeah, I guess what I was trying to show was that we — what I've been saying for a while is we don't need a doubling or a tripling of the doldrums — we were down there at 5, using the VIX as one example as a proxy. We didn't need a tripling of that to see some positive results come out. An improvement would be helpful, and it was, and I guess what I'm saying here is that if it goes up, fantastic. If it stays here, let's hope we can continue to position the company accordingly, but I was trying to make the point to say that we saw an improvement, but it wasn't like we saw a whole step function order of magnitude change that said, okay, volatility is back at 2008 levels. That was the point I was trying to make.

Zach Arrick
Got it. Thanks.

Glenn Stevens
Sure.

Operator
The next question comes from Albert Jones of Jones Capital Management. Please go ahead.

Albert Jones
Nice quarter, gentlemen. I'm new to this story, so forgive me if I ask something that might be known by others. Are the October metrics going to be released in the next week or so? It looks like you have the trend of doing that.

Jason Emerson
Yes, Albert, we're going to be releasing our monthly operating metrics on Monday.

Albert Jones
Okay. Great. As far as City, would you say that their business has trended the same way as yours? Here in the last eight weeks or so, it looks like FX and IG and all those guys have seen, volumes come up quite a bit, so is it safe to say that City has seen the same trend?

Glenn Stevens
Yes, I think we showed some proforma financials and operating metrics with City during that release, and so, even in this [unintelligible] we've seen similar curves, if you will, in terms of their responsiveness to increases there. The one slight translational difference is, if you will, in our retail part of GAIN'S business, we are more heavily weighted towards FX. City is more heavily rated towards CFDs, and so if there was a distinct divergence of volatility between FX and CFDs, that might affect our outcomes different. Again, it folds into our diversification story, but separate, looking at that, I think you saw a pickup in volume, both equity CFDs and also FX, so in this case, they generally mirrored each other, but there could be cases where they'd diverge if they were separate businesses.

Albert Jones

Okay. Thanks. Could you just give me a quick overview of the collar on the purchase of City and whether there's some variables there, if City hits certain metrics, in the timeframe before you close, whether anything changes or not?

Jason Emerson
So the collar was established that goes from $720 to $925 based on the trailing 20 days, I believe — I don't have the details right in front of me — prior to the close. And if the closing price is above $925, that would be the conversion price.

Glenn Stevens
So ultimately there aren't alternative metrics driving value there. The collar was put in and the details are in our queue in terms of filings, but — okay, sorry. But the point there is that it was put in more to manage for the lag time between when we announced the deal and when we close the deal. We have to finish up regulatory approvals globally, so it won't, to answer your question, be driven by market performance directly. It will be driven by the prevailing gain stock just to provide some smoothness, if you will, for that process.

Operator
This concludes our question-and-answer session. I would like to turn the conference back over to Glenn Stevens for any closing remarks.

CONCLUSION

Glenn Stevens
Thanks, Operator. So thanks again for joining us today. We're real happy to announce a strong quarter. We don't want this to be a standout quarter. We want this to be a regular event for us, and so what we'll do to manage that is continue to build the foundation and build the underpinnings, and then we're hopeful we'll get some market capitulation in terms of cooperating on the vol side and continue to go down that road.

We didn't focus too much on our recently announced acquisition of City. It's not because we aren't super excited about the opportunities there. We provided the details as recently as last Friday, and, more importantly, we're really encouraged by what the upside is in terms of integrating that business over the coming months; however, we don't stand —kind of view it as a standalone end result. We just see it as another example of using strategic M&A to build our revenue base and to continue to diversify that revenue base, and you heard me say this, but establish a broader and deeper customer experience. I think what's really important here is staying focused on the customer, and we have to be able to do that — that internally we integrate and extract value on the cost synergy side. We showed that with our acquisition of GFT but also on the revenue synergy side and building the business, not creating siloes that don't cooperate and communicate but building a linked business and an integrated business.

So, overall, real pleased to present these results for Q3 but frankly, even more excited about future quarters. So thanks for joining and have a good day.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.