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VIRT - Q1 2016 Virtu Financial Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Virtu Financial first quarter 2016 financial results earnings call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will be given at that time. (Operator Instructions) As a reminder, this call maybe recorded. I would now like to introduce your host for today's conference, Mr. Andrew Smith, Head of Investor Relations. Please go ahead.

Andrew Smith - *Virtu Financial, Inc. - Head of IR*

Thank you. Good morning. As you know, our 2016 first quarter results were released this morning and are available on our website. Today's call may include forward-looking statements, which may represent Virtu's current belief regarding future events and are therefore subject to risks, assumptions and uncertainties, which may be outside the Company's control.

Our actual results and financial condition may differ materially from what is indicated in these forward-looking statements. It's important to note that any forward-looking statements made on this call are based upon information presently available to the Company and we do not undertake to update or revise any forward-looking statements as new information becomes available. We refer you to disclaimers in our press release.

In addition to GAAP results, we may refer to certain non-GAAP measures, including adjusted net trading income, adjusted net income, adjusted EBITDA and adjusted EBITDA margin. We believe these non-GAAP measures are more reflective of our operating and core business performance. You'll find a reconciliation of these non-GAAP measures to the equivalent GAAP terms in the earnings materials with an explanation of why we deem this information to be meaningful, as well as how management uses these measures.

Speaking and answering your questions today are Mr. Douglas Cifu, our Chief Executive Officer; and Mr. Joseph Molluso, our Chief Financial Officer. They will begin with prepared remarks and then take your questions.

Now, I'd now like to turn the call over to Doug.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Thank you very much, Andrew. Good morning and thank you for joining our call to discuss Virtu's first quarter 2016 results. On our last earnings call in early February, I noted that the environment in early 2016 had been favorable. I stated that the sustained elevated volatility and corresponding volumes in the beginning of 2016 in the US equities market in particular showed promising early results for Q1 and we're trending better than the fourth quarter of 2015. While comparisons to Q1 2015 are difficult given the Swiss Bank's surprise de-pegging event in January 2015 and the subsequent sustained broad-based market volatility, Virtu's first quarter 2016 results reflect the improved market conditions in several of our markets as compared to the fourth quarter of 2015.

Our adjusted net trading income of $117.3 million reflects Virtu's diversification across asset classes and geographies. We saw particularly strong performances in our Americas equities and global commodities categories. Our $117.3 million of adjusted net trading income was up 9% versus the fourth quarter of 2015. We continue to perform well versus selected industry volume benchmarks. As we have mentioned in the past, Virtu's facilitation of risk transference thrives in periods of high volumes and sustained volatility as bid offer spreads widen. We review benchmark metrics in terms of total volume, shares or contracts traded as well as the notional value traded.

For example in Q1 2016, the average daily volume of shares traded increased 21% versus the prior quarter while the average daily notional US dollar of consolidated US equities traded was up 12% versus the prior quarter. Our Americas Equities adjusted daily net trading income during the period was up 17% versus Q4 2015, certainly in line with the share and notional dollar value traded increases during the same period.

Continuing to look at the individual categories versus select market benchmarks, our business performed well. European equity volumes were up 20% versus Q4, while notional euro values were up 16% and our European equities category was up 15%. Tokyo Stock Exchange volumes were up 17% versus Q4, notional yen values were up 7% and our APAC equities category was up 16%.

CME energy contract volumes were up 25% versus Q4 and our Global commodities business was up 44%. FX volumes showed mixed results versus Q4 2015. CME FX futures volumes was up 21%, notional dollar values traded increased 17%. However, spot FX volumes were mixed, Hotspot was up 25%, Reuters FXall was up 18% but EBS was down 13%. Our global currencies category was up 6% versus Q4 2015 as compared to the Composite Index Spot FX being up 10% over the fourth quarter. Comparisons to the first quarter of 2015 will naturally be less favorable in particular for global currencies and European equities given the Swiss National Bank's de-pegging in January of 2015 and the subsequent impact on currency volumes and European equities that persisted throughout the first quarter last year. Overall, we are very pleased with the financial performance in Q1. Our normalized adjusted EPS of $0.31, again, reflects a very profitable and high margin company. We realized $81 million of adjusted EBITDA, maintaining an adjusted EBITDA margin of 68%.

Our focus on expense and overhead management and capital deployment remains key to our overall strategy. I've mentioned on prior calls, our intention to leverage Virtu's multi-asset class technology platform. Part of this effort is to offer a Virtu's superior order routing technology to select buyside institutions. I'm happy to report that we've executed our first trades as part of this offering in early April. It is still early days and we do not expect a meaningful contribution in terms of revenues in Q2, but we are excited that this vision has resulted in a tangible outcome. We have seen significant inbound interest from major institutional investors, and we remain excited about these relationships.

We believe there are additional opportunities for us to leverage our global technology asset and we are actively exploring these ideas. On the regulatory front, while we continue to monitor and participate actively in proposed reforms and improvements in market structures, Q1 did not see any material developments that would negatively impact our business. We continue to believe that as one of the most efficient scale providers of two-sided prices to over 230 markets globally, Virtu will benefit from enhanced transparency and competition in modern evolving markets.

As we continue to focus on the long-term growth of our business and remain excited at the prospect of Virtu in 2016, I want to conclude with some remarks regarding Q2 thus far. While the slower pace of March continued through most of April, we saw more robust activity at the end of April, and we continue to be very optimistic about the rest of the year.

Also given the geopolitical environment, global interest rate uncertainties and concerns over a possible Brexit, we are optimistic that this more robust pace will continue.

Now we'll turn the call over to our Chief Financial Officer, Joseph Molluso to review the financial results. Joe.

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

Thank you, Doug. Focusing on our continuing theme of driving revenue growth, maintaining strong expense discipline and operating efficiency and returning capital to shareholders, let me review a summary of our results and point out some financial highlights before we open it up to you for questions. Consistent with the financial presentation in our S-1 registration statement and recent quarterly results, we will provide non-GAAP financial information to supplement our presentation. For the first quarter of 2016, our adjusted net trading income was $117.3 million and total non-GAAP net revenues were $119.4 million. Our GAAP net income before attribution to non-controlling interest was $51.4 million. On a non-GAAP basis, our normalized adjusted net income excluding mainly the impact of stock-based comp, and investing in the stock-based awards granted at the IPO as well as other one-time items, was $56.2 million.

Assuming a normalized tax rate to fully converted shares outstanding, this translates to $0.31 per share in adjusted EPS for the quarter. Compared to Q4, 2015, our average daily adjusted net trading income increased 14% to $1.92 million per day. Our adjusted net trading revenue outpaced expenses as our net income margin expanded from 47.6% to 49.3% versus Q4 of 2015.

On the expense side, our first quarter results continue to exemplify our disciplined approach to cost. We consider our core fixed expenses to be communications data processing, employee compensation, operating and administration expense and depreciation and amortization. In terms of people costs, our fully loaded compensation expense, which excludes IPO-related items and other vesting as well as severance, but includes stock-based compensation accruals was 18% of adjusted net trading income and 25% of adjusted EBITDA in a range consistent with prior quarters and full year 2015.

We continue to retain and competitively compensate talented professionals at Virtu by keeping headcount at appropriate levels via automation and efficiency. Non-compensation core expenses were down versus the fourth quarter of 2015. So in total, our core expenses are up 3% versus Q4 of 2015, consistent with the guidance we had given around anticipated overall growth in core expenses.

Our focus on expense discipline has allowed us to achieve superior margins. Our margins remained strong in the first quarter with adjusted net income margins and adjusted EBITDA margins of 49.3% and 67.9% respectively. Consistent with our policy of returning free cash flow to our shareholders, our Board of Directors has authorized a regular quarterly distribution of $0.24 per share payable June 15 to shareholders of record on June 1. Finally, looking at our company as a fully taxed C-Corp with all of the Class C and D shares converted to the public company Class A and B shares, our fully taxed adjusted net income would have been $42.7 million or $0.31 per share for the first quarter, assuming 140 million shares outstanding.

Now I will turn the call back to the moderator for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Rich Repetto, Sandler O'Neill.

Rich Repetto - *Sandler O'Neill - Analyst*

I guess my questions first on the unallocated bucket, I guess in the net trading income, so it had almost $5.5 million negative adjustment, if you could just give us some color and explanation. That seems like the highest negative adjustments it's been before?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Thanks. It's a good question, Rich. I will do my best to answer. Joe, if I butcher it please jump in and save me. But yes, roughly $5.5 million, $6 million, it's really composed of two things. These are not true economic losses, but unfortunately this is how GAAP requires us to reconcile our financials. So as you know, and everyone on the phone knows, we trade across geographies. So if we put on a position, an European ADR against a US ordinary stock, for example, we lock in that spread or that profit, if you will, at 11:30 New York Time, because that's when the European markets will close.

And as far as Virtu is concerned internally if we made $10 or $100 or $1,000 on that position, British Airways against British Airways ADR, we internally think we've made $1,000 and indeed we have, because we kind of stop trading at 11:30. Unfortunately that's not what GAAP requires you to do, you have to mark that price to our New York-based firm to the New York settlement price, which would be 4:00 PM. And so as a result, if that position "moves against you" that's distortion, if you will, of that price. It's not really a true economic loss. But for GAAP, GAAP doesn't recognize that profit. So that's about $3 million of that and we've talked about that in the S1, there's a footnote on it, and it really is ultimately just a timing issue, Rich. And so this quarter, it was material, it was around $3 million. The other $2.5 million of that is we have our European unit, our Irish subsidiary, that marks its books in the euro, obviously, because it's located there and is registered with the Central Bank of Ireland. Again when we reconcile that to GAAP, we have to use the US dollar value. And so if you look on the balance sheet, Joe, what's that category called?

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

It's called other comprehensive income, and other comprehensive income is positive in the net income statement, this quarter of $2.49 million.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Right. So the euro rallied and so it looks like we made $2.5 million less out of our European business, if you will. Not to give away state secrets, but, obviously, that is not how we hedge. We don't hedge our internal P&L, waiting for the end of the month and hoping that the euro didn't go up or down. So again, that doesn't represent a cash or true P&L for the firm but unfortunately I don't make the rules and that's not what GAAP requires. So if you kind of back in those two adjustments in our adjusted net trading income, again, this is not a GAAP number, would have been $5.5 million more roughly $123-ish million.

Rich Repetto - *Sandler O'Neill - Analyst*

Understood. That's very helpful. And I guess I am sure there is going to be lot of questions on the individual buckets but I'll leave them to follow-up calls. Doug, when you talked about 2Q to date April, so volatility has come down, but you seem pretty optimistic about not only the quarter but going forward. So I'm just trying to get a little bit more depth on how April looked given that the metrics that we see from a macro standpoint are relatively softer than 1Q.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

I guess I'm an optimistic guy by nature. We are running a great firm, I am blessed to have great people work for us in the firm, continues to perform very, very well. I mean, you're right, the first, if you will, 21 trading days in April, the first 18 were pretty light, it picked up a little bit towards the end, so I was kind of reflecting that. But certainly, look the metrics don't lie, Rich, the volumes in April, and I know you've all covered the exchanges and I see what they put out in CBOE and what not and so we can only react, if you will, to the volumes that are out there. But I was probably more reacting to the last couple days of April where we did see some pick up and, obviously, I'm an optimistic guy and I am hopeful that investor confidence will come back, maybe with the Presidential election coming in the future, people will have more conviction and start moving portfolios back and forth again.

Operator

Alex Kramm, UBS.

Alex Kramm - *UBS - Analyst*

Maybe just following up on Rich's question here for a second on April. Can you also talk about the quarter a little bit, different slices or different periods, I mean it looked like it was a fairly consistent quarter in the first couple of months and then March looked a lot different, so any color you can give us in terms of the different NTI that you saw in those different environment, anything else that stands out? Thanks.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes, I forgot exactly what day we did our last call, but it was probably middle of February to early February. Certainly at that point, Alex, you're exactly right. I mean, it was almost like a tale of two cities the quarter, the first two months were pretty robust, we obviously don't disclose our monthly adjusted net trading income. But certainly, January and February exceeded March fairly significantly just on an average basis, unfortunately March, if you guys see these numbers from the exchanges and from everybody else, March volumes, I don't want to say they fell off the cliff, but there were certainly materially lower than what we saw in January and February. So had the trend continued, I think we would have been talking about, obviously, I would have been talking about a much different type of quarter. That being said, I think we know we performed well given the opportunity and given the question, Rich, asked about some of the unallocated adjustments to adjusted net trading income, we would have come in at something in the neighborhood of $122 million, $123 million, $124 million, which, given our historic capture rates for quarters where there isn't some extreme exogenous event like Swiss de-pegging or August 24 frankly would have been in my mind right in line. So I think we performed consistent with capture rates and volumes and volatility for periods where you didn't have one or any other extreme kind of exogenous events.

Alex Kramm - *UBS - Analyst*

Great, that's helpful and then just secondly, I guess a dig into some of the business bucket, I mean, FX obviously is still a big attention grabber, I think you gave some good color at the beginning between spot and futures, but generally speaking, I mean what updates can you give us on the secular opportunities here. Are you still seeing new marketplaces you can sign up for, are you seeing more competition in some of these marketplaces, what are you seeing from the banks and any incremental color because I think a lot of us expected this to be a nice new opportunity to focus on and it hasn't really played out yet. So any updated thoughts would be great, thanks.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes, it's a great question obviously, look I'm not satisfied with the results and no one here is, and I don't want anyone to think we're not redoubling our efforts and we will get better there. I am 100% positive of that. I think look from a longer-term perspective, which is, obviously, how I've always looked at Virtu, I liked what I saw in the first quarter in the sense that we continue to be engaged by big financial institutions that want to do business with us. We've increased the number of counterparties that we're transacting with, we're a significant player in non-G7 currency, so emerging market pairs and NDF. And I think the regulatory regime and the opportunity set with respect to making markets in NDFs is only getting better. I think it is important when people look at - this is one category where it's very, very difficult to pick one, proxy or one index and look at it and say, okay, well, how should they have performed? Right. If you look at like EBS's numbers, they may present an increase, but really have to dig through it and see what are their spot volumes doing during the quarter, I'm not picking on them, but just giving you an example. So I think Hotspot puts out a composite spot index between that and the CME futures. That's probably like the best comparison that we could use. But again, as I've said on prior calls, and I'm not going to talk about specific pairs, we are stronger in certain pairs than another pairs. So if in a quarter X, Y and Z pair volumes are down significantly, that might more materially impact what we do in FX than if those pairs are doing better. So we do well in emerging market currencies. If there is a lot of volume in countries that you could probably think of, that's going to be better for our FX business than if it's in one of the major pairs. So all in all long-term there is not a fundamental problem with our business. I know people are disappointed, they view this as a significant growth opportunity and we will get better. But overall, I still like the way where we are positioned with the low cost most efficient provider. We're making markets in over 80 pairs, we're doing it 24 hours a day. We're adding counterparties that want to do business with us and everybody on this phone is aware that the big banks, the big broker dealers are having a real difficult time both because of regulatory and capital constraints, but frankly also because of the efficiency of price. The one thing I will say and I've said it over and over again, this firm does better when markets get more efficient. So I'm not concerned that somehow competitors are squeezing us out of the market and I think the long-term trend of further efficiency in this market and in the fixed income market is a strong positive for Virtu.

Operator

Alex Blostein, Goldman Sachs.

Alex Blostein - *Goldman Sachs - Analyst*

Bigger picture question around the order routing business you guys are trying to execute upon. Doug, can you just give us your thoughts on, I understand it's not going to be needle mover I guess in the near-term, but bigger picture what you envision this business to be for Virtu, and I guess more importantly, in the past you guys have talked about one of the advantages of the business model is the fact that you don't quite have customers and that allows you to do certain things other people can't. So how do you balance the two? And just help us understand the vision for the business line?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

It's a great question. And look, I mean, we kind of stumbled into this business. I think people are aware of the history. After the events of 2014, we kind of can opened the kimono and showed a lot of buyside folks, regulators and you guys what our business was all about. We did some live trading demonstrations and then people said, hey, you've got a pretty robust system here and it works really well. Would you ever consider routing orders for us and candidly, obviously, I thought about it, but it didn't seem to me to be something that was consistent with our headcount and our infrastructure et cetera. When it became clear to me that we could do it and I think I called it a velvet rope last quarter, we could do it in a Virtu way, in other words we were not going to add personnel, we were not going to add headcount, and we could frankly have a smaller number of high-end clients, if you will, that really understand market structure and really want to get great execution and understand the benefits of working with a, I'll call them, non-conflicted efficient broker that this could be a nice business for us. And so we were fortunate enough to add a gentleman named Steve Cavoli from Morgan Stanley who knows this business real well and is very well regarded by institutional investors and so we launched into this foray. We have not added a single person. We have used our existing infrastructure. We've used our existing algorithms, if you will, that we're very good at mitigating risk for our own portfolio and our own positions. And so we're doing it in the Virtu way and it'll be a Virtu high margin type of business where it ultimately leads and how material it is to us, it's really difficult for me to say right now, I'm not trying to skirt the issue or be intentionally vague, we're working with one particular institutional investor, right now, we're getting very positive feedback from them and we have been solicited and there's been a lot of inbound calls and outbound calls to another group, a very, very important significant, very sophisticated high-end institutional investors.

So, Alex, I see it as being, I don't want to call it a niche but a more concentrated business with a couple dozen high-end institutional investors that kind of get the value of our service and if not a commoditized offering. So whether that's X or Y or Z of our ultimate results, I can't really tell you. The thing that I'm very excited about is it demonstrates to me as we previously had demonstrated with the technology services partner that we have, is that we've got a great asset here. We really are as much a technology firm as we are a trading firm. We really understand market structure. We really understand low latency architecture. We're connected to 230 venues and we've got this great multi-asset class, multi-currency platform, if you will, that manages risk and is a terrific order management system. That's a very valuable asset. As large financial institutions try to figure out, how they deal with a more competitive world, I think they're going to continue to have approach us and will continue to approach us about trading partnerships, technology arrangements and our job as a management team is to try to figure out the handful of people that will be good business partners for us going forward. So again, I'm not going to sit here and predict what percentage of our ultimate net revenues that will end up being, but I see it as a significant growth opportunity for us that frankly two years ago, I wasn't as focused on.

Alex Blostein - *Goldman Sachs - Analyst*

Got you. Understood. And just as a follow-up question around the environment over the course of the first quarter. Obviously, you've seen a lot of very volatile days a lot of funky things were happening in the market over the course of the first quarter. How have your risk systems handled days like that? And I guess, more importantly, can you comment on profitability on the basis whether MTR was positive everyday this quarter?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

With just regard to the last one. I keep bringing up the histogram even though I don't want to bring up the histogram right around profitability. So I promised myself that I would never comment again on our daily profitability. But in general, to get back to your original question on risk management, look, that was the basic foundation for this firm was we're a firm, I'll use a sports analogy, that will hit singles all day. As Vinnie says, we're picking up the scraps on the floor as the market maker. We're never swinging for the fences. We don't make bets. We try not to guess. We try very, very hard not to be directional and so we're trying to make a tick. And when it's very clear that we're not going to make a tick, we're going to get out of the position and so we're not perfect. Hubris is a horrible vice. I don't want to ever say never, but we've really constructed this firm to manage the transference of risk back and forth between buyers and sellers in a very, very efficient manner.

Again on August 24, a lot of people asked did we handle it very well and I made the mistake of saying something like "the firm was built for that day," I didn't mean because we made a Gazillion dollars. I meant because we handled the transference of risk between literally hundreds of thousands of people that wanted to get in and out of position in a very, very effective and very, very efficient manner. So in the first quarter to answer your question more directly, we performed very well. We had no hickeys, no hiccups in our risk system. We continue to perform very well and it's something that we're very, very, very focused on, we spent a lot of hours on our lock downs, on our controls, on our reconciliation procedures. We're not perfect. We strive to get better every day, but the firm performed very, very well in the first quarter and continues to perform very well in the second quarter with regard to risk management.

Operator

Ken Worthington, JPMorgan.

Ken Worthington - *JPMorgan - Analyst*

I'm going to kind of follow-up on some of the products, commodities so-so quarter at a time when oil bonds and volatility were up. There were some good metals price movements and price of gold. It wasn't the weakest quarter from an NTR perspective but it was, I would say, a weaker quarter, can you flesh out kind of the ins and outs of commodities sort of similar to what you did earlier in the ins and outs for FX?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes, I mean we were up as compared to the fourth quarter about 44% and again, it's a great question, Ken, because commodities by definition is a very, very broad category, so it includes everything from corn, sugar, cocoa and cotton to gold and silver to natural gas, gas, oil, crude, I could go on and on. Anything that kind of comes out of the ground or from livestock or whatnot is included in that category. I would say the one sub-asset or sub-class, if you will, and you guys know this very well, that continues to be a challenge is natural gas, that's really a factor, if you will, of lack of price movement and volatility and it's become a very, very obviously low priced sub-asset class, if you will. A lot of that has to - I'm not a natural gas expert, but you guys get it fracking and over supply and whatnot and all that kind of stuff. And so as a result, that continues to be a sub-asset class within this asset class that has not performed as well as it certainly did last year, or frankly the couple of years before that as natural gas prices were tumbling.

I think the other thing is we did very well in crude during the quarter, but as the price of crude goes down, you have to imagine that the capture rate probably goes down as well, right, because the notional size, the notional volume of what's being transacted will naturally compress. So look, overall, I was very happy with the quarter. We were up, as I said, Joe is showing here about 44% from Q4. And if you look at the indexes, the CME contracts were up around like 17%-ish. CME and ICE and crude and whatnot. So I think as a comparison basis, I'm pretty happy with where we ended up. But again, it's a broad category. For competitive reasons, we're not going to sit there and say, here's what we did in softs, here's what we do in metals, here's what we do in the various energy products. So by definition, it's going to be a little vague and lumpy. But overall, I was pretty pleased with how we performed.

Ken Worthington - *JPMorgan - Analyst*

Thank you. And just maybe a little more color there. How big is energy in terms of global commodities for you versus the ag and other stuff, I don't need the ag and other stuff. But is energy the majority, is it less than the majority, like where does that fit in the complex?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes. I mean, it is the majority of the complex. It's not a vast majority but it's more than 50% of that complex. Don't forget we trade a lot of metals products and we do that globally. These are global businesses. So we're trading while we're all sleeping in New York, we're making markets in TOCOM and in Dubai and other places where precious metals are transacted and base metals as well. We trade a lot of copper and some other base metals. And then, of course, there's all the various soft products, which tends to be a smaller commodity and a little more US or our time zone kind of centric, but it's probably in that kind of cascading order, I would say, the energy complex, metals complex and soft complex are kind of one, two and three within the commodities category.

Operator

William Katz, Citigroup.

William Katz - *Citigroup - Analyst*

Can we sort of come back to the unallocated for just a moment? I appreciate your disclosures, very simple. But if you still look at the swings over the last couple of quarters and this is, as you mentioned, a bit on the higher side, what changed this particular quarter that made it such a wide negative relative to the last couple of quarters?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Well, two things, and Joe will jump in. And one is, it really just depends what the size of the positions are and how the currencies are moving or how the settlement prices are moving. So we could have a large hedge position in a bunch of ADRs because we saw value in that spread. And it just so happens on March 31 that the price in London versus the price in United States or frankly as you know we trade in Asia, so maybe the price in Japan as compared to the price in New York, 12, 13 hours later changes materially, is complete and utter happenstance, it's non-economic. It's not how I would look at the firm from a kind of internal database P&L perspective, but as I said, we are rule followers and that's what GAAP says. Joe, did I answer it correctly?

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

The clock strikes midnight for GAAP when it does and that's what we need to do to mark settlement prices. And as Doug said, depending on the size of the position, depending on time zones, depending on which way things are going, it has nothing to do with the way we traded it. It is no different than anything else we do. It's just literally, as the footnote says, that we wrote, it's just really deferring our accelerating revenue from one day to another or one reporting period to another as the case may be. So it's completely non-economic as Doug says.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

And look, just to be clear, I'm not whining and complaining about it, it could cut either way. All I'm suggesting is if you all want to get a true perspective internally as a management team how I and Joe and the others here are looking at our performance, I don't look at - of course, I look at our GAAP P&L, I shouldn't say that, but I look at our internal database P&L, which is literally on my screen second by second and then I compare it to the metrics and opportunities. So I look at the quarter and I say, "hey, we did very, very well." I mean one of you all, I forgot who it was, put out a research report in the last couple of days, where someone had the number and I smiled and said to myself, well, they really kind of hit it right on the head. I forgot which one of you all put that out. But again it's something that's going to vary quarter by quarter. It's a GAAP thing, there's sort of nothing we can do about it.

William Katz - *Citigroup - Analyst*

That's helpful. Sorry to belabor the point.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

No, not at all.

William Katz - *Citigroup - Analyst*

Lot of my big picture questions were already asked. But just as you look on the expense dynamic on a go forward basis, assuming January/February type volatility would not persist, and then you have a couple of longer dated expense initiatives underway. How are you thinking about comp, I know you mentioned in your prepared remarks you're still within your range. So how you think about that may be tactically as we look out the next couple of quarters and longer term about the long-term margin in the franchise?

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

I don't think it will change at all. I think the first quarter accrual was - it's consistent with, as I said, what we did last year on a full year basis, it's within a range. As I said in the past, our compensation expense will behave, much more like a fixed cost than a traditional variable cost that you may see in an investment bank. It will look more like compensation expense at one of the exchanges that you cover. And, obviously, it will fluctuate within a band but it should not change. There is nothing that we have underway in any of the initiatives that we've talked about that would cause that philosophy to change, or would cause the way we account for it or accrue for it to change

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Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes, I think the important thing and we've said this over and over again, this firm is, again, we've got wonderful people here. They are very, very talented. And every one of them owns equity in the firm and everyone is totally driven to produce results. But this firm is really ALL about automation and making the markets more efficient, and you see - I was asked a couple of years ago when our headcount was 140-something, "what's your headcount going to be in two years?" And I said, "around the same and perhaps maybe a little bit lower," and everyone kind of scratched their head, and said, "how could possibly be?" This is not a firm where we need 200 to 300 people to accomplish our mission. We are at a good size right now. It's just a question of getting more efficiencies out of the business and having our people effectively grow and mature and continue to work hard and produce. And we've built that culture. It's much more of a technology style culture, if you will, than it is a trading firm culture and I see no reason why we would ever change that.

Operator

(Operator instructions). Ashley Serrao, Credit Suisse.

Ashley Serrao - *Credit Suisse - Analyst*

I guess, first question. Can you just talk about your aspirations in electronic fixed income? I know there's been some press. What segment of the market do you think you can effectively compete in, what segments would not be a match for your style? Any color there would be appreciated.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes. I think it's a great question. I mean, as we've always said, and I said in my remarks and I wasn't specifically referring to fixed income but this is an asset class where we need transparency. Right now, the SEC and CFTC and Treasury, as I'm sure you're well aware of are kind of circling around, do we have trades for treasuries, do we have real-time reporting? Obviously, as compared to fully electronic, central clearing, central order book-style firm, we are big believers in real-time disclosures of data and prices and what-not. Everybody on Wall Street doesn't agree with that statement, but I think it's the right thing for the marketplace. And we are essentially involved in that discussion. We put in comment letters. We've got representatives in Washington including myself who goes down there and we try to lobby for those things because we do think it's the right thing for the market. And so we think it's a good thing ultimately for Virtu. So if you had a number of competitive platforms, where, for example, US Treasury is another cash government instruments were traded in a fully electronic manner, that's a good thing for our business. So that segment of the marketplace we think we can be very, very competitive in.

The same thing with interest rate swaps that are now transacted to some extent on various swap execution facilities. As the marketplace continues to evolve and the buy-side insists on real-time execution in a fully disclosed transparent manner, that's going to be a good thing for our business and then we think we can be significant market makers and players in that. You've seen some of our competitor firms and the Citadels of the world have already made that push and are doing frankly a very, very good job in that area. Areas where we will not likely be competitive and not participate are corporate bonds. There are millions and millions of corporate issuers out there that have issued bonds that really either trade by appointment or trade a handful of times a day. And frankly the skills, if you will, and the technology and the efficiency that we provide to the marketplace really aren't needed there. That's more of an RFQ style of market or maybe it's a voice and IM type of market and will continue to be, and there is no reason that that marketplace shouldn't be segmented.

I would probably throw CDS into that bucket as well because it's not really as in vogue as it was eight years ago and there is not enough volume. Maybe there are some indices of those products. You might have a corporate bond index or something like that, or an ETF that trades in a more transparent, more rigorous kind of way. But otherwise I think you'll see, Ashley, some segmentation of that marketplace, and obviously we will gravitate much more to the fully transparent, more efficient part of that market. So I think the addressable opportunity in fixed income will only grow, if you imagine a pie and maybe 5%, 10% of it is addressable by us right now. As that marketplace continues to electronify, how much of that pie will be addressable by us? It's difficult to say. Again, I've said this to various people privately and I'll say it publicly. JPMorgan did a great investor deck, I think it was in January or February of this year. And in it, they talked about electronification of markets. And Jamie Dimon and Matt Zames are two very brilliant, wonderful gentleman that know a lot more about markets than I do. And in that they talked about each of the various asset classes and how they are becoming electronified. And so to me that was really - I actually said to Matt, we should use that as our investor presentation because it was really like a roadmap for where I think Virtu is going over the next 12 to 36 months.

Ashley Serrao - *Credit Suisse - Analyst*

And then moving on to FX, just curious how your customized liquidity offering is faring. Any color on the growth, what's in the pipeline? And then can you also remind us for spread differential, if there is any between transacting directly on Reuters and EBS and White Labeling's liquidity?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Yes, that's a great question. The answer is, look, I'm very bullish about it because to me it's just a - remember our model, we've got one basic product which is a two-sided price and we don't have customers in a traditional sense. So we have to disseminate that price through intermediaries either they are exchanges, they are dark pools or they could be brokers, technology providers. And then the FX market largely because it's highly unregulated and because there is a history of taking a single bank fees and multi-bank fees, folks are more than happy to take our prices directly.

So you tend to have in the all-to-all market, the EBSs and the Reuters and the Hotspots and their all-to-all platforms, you tend to have - obviously, it's an anonymous market, but you tend to have wider spreads and there is lack of accountability and people complain about the high frequency traders and blah, blah, blah, all the other stuff that I'm sure you're very familiar with.

When you've got more directed feeds either through - we can stream directly through our own API, or we can do it through a technology provider or we can do it through FXall or EBS Direct and some of these other platforms, we will show a tighter spread and, obviously, we'll be fully disclosed to the counterparty, so they understand price impact and what-not, and we have to put our money where our mouth is, if you will, and actually show them a good product. So that offering is very competitive in the highly transacted payer, so dollar/euro and dollar/yen and things like that, you are going to see a lot of providers that are providing that stream, including the big broker/dealers. When you go further down the food chain to some of the more obscure crosses and some of the emerging market pairs, I think we could be more competitive because we are more than happy to provide those prices. So it's hard to over-generalize the marketplace. I've kind of given you like a 20,000 foot view. Again, I continue to be very, very bullish about that business. I think it plays very well into our strengths because you have got a very diverse, very somewhat over-fragmented marketplace. And as NDFs and other emerging pairs move from being opaque and traded bespoke to being traded in a pseudo or somewhat electronic fashion, that's only going to be good for our business. So again I'll use the sports analogy. We are not in the first inning but we are certainly not in the eighth inning in terms of electronification of those marketplaces. And so I think there is a lot of room to grow there. I would also point out that that model of streaming bespoke prices works with US Treasuries. We are now doing that as well, and it works with precious metals. We have counterparties where we are streaming metals prices too. So we are all about taking our product and disseminating it. We are happy to do it through an exchange, although I would say we are cheaper. We're happy to do it through a broker and we are happy to do it directly if that's what the counterparty wants.

Operator

(Operator instructions). Ian Johnston, Prudential.

Ian Johnston - *Prudential - Analyst*

Since going public, could you maybe explain your tax bases? I'm trying to figure out the cash taxes and I'm comparing it to the provision for taxes, and it looks like a relatively low effective tax rate. So I'm just trying to understand how we should factor that in going forward and how we should provide for that?

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

Yes, sure. This is Joe, I'm happy to handle that question.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

You don't think I can handle it, Joe?

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

You can.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Okay. Go forward, Joe.

Joseph Molluso - *Virtu Financial, Inc - CFO, EVP*

The public company owns around 27% of the partnership unit, so the actual cash taxes that we pay reflects that kind of low cash tax number that you're coming up with. So the provision for income taxes in Virtu Financial Inc. just reflects the amount of income that Virtu Financial Inc. gets from the partnership. We all assume that as an investor, as a research analyst, you want to look at the company as if it were a fully taxed C-Corp and that's why we use the fully loaded effective corporate tax rate.

But you're correct in that our actual cash taxes are much lower on an actual corporate level. So when you look at our GAAP income statement, you see the cash taxes are above the line and then we look at GAAP EPS after that.

Ian Johnston - *Prudential - Analyst*

And I believe I read recently that Virtu purchased a very large piece of real estate in Brooklyn of the order of about $100 million or so. Anything to that?

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

No. In fact, the headline was 100% wrong and Virtu is not in the real estate business. Our Chairman and Founder, Mr. Viola obviously from time to time makes his own personal investment decisions that has absolutely 100% nothing to do with Virtu Financial. Vinnie is the Chairman of Virtu Financial. So Mr. Viola makes personal investments and occasionally, big surprise, reporters screw up and assume it's Virtu doing all these things. I can assure you we are not in the real estate business and have no plans or intentions to get into the real estate business.

Operator

Thank you. And that does conclude today's Q&A portion of the call, I'd like to turn the call back over to CEO, Doug Cifu for any closing remarks.

Douglas Cifu - *Virtu Financial, Inc. - Chief Executive Officer*

Well, thank you very much everybody for participating today. We really appreciate the questions and all the great feedback. Again, we continue to be very excited about our business and optimistic. We continue to run a very efficient business, we think, that is providing wonderful value and efficiency to the marketplace in the form of our two-sided prices into over 230 marketplaces. So we look forward to continuing our conversations with you in the near future and we'll talk to you all soon. Thank you very much.

Operator

Thank you, ladies and gentlemen, that does conclude today's conference. You may all disconnect. Everyone have a great day.
