Interactive Brokers Group, Inc.
Q1 2013 Earnings Conference Call
April 17, 2013 4:30 PM ET

Executives

Thomas Peterffy - Chairman & Chief Executive Officer
Paul Brody - Chief Financial Officer
Deborah Liston - Director of Investor Relations

Analysts

Chris Harris - Wells Fargo
Rich Repetto - Sandler O'Neill
Chris Allen - Evercore Partners
Sean Brown - Teton Capital
Niamh Alexander – KBW
Sameer Murukutla - Macquarie Capital
Justin Hughes - Philadelphia Financial

Operator

Good day everyone and welcome to the Interactive Brokers, first quarter 2013 earnings results conference call. This call is being recorded.

At this time for opening remarks and introductions, I would like to turn the call over to Ms. Deborah Liston, Director of Investor Relations. Please go ahead.

Deborah Liston - Director of Investor Relations

Thank you operator and welcome everyone. Hopefully by now you've seen our first quarter press release, which was released today after the close of market, which is also available on our website.

Our speakers today are Thomas Peterffy, our Chairman and CEO and Paul Brody, our Group CFO. They'll begin with some prepared remarks about the quarter and then we'll take some questions.

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

I'd now like to turn the call over to Thomas Peterffy.

Thomas Peterffy - Chairman & Chief Executive Officer

Thank you for joining us on our earnings announcement afternoon. The most important thing to know about our first quarter is that the earnings number gives you a misleading picture about the current state of our business and our future prospects, which have become ever brighter.

This has been a fantastic quarter for our brokerage business, in which we sailed past almost every one of our previous records earning $111 million. This is great performance, even if it is overshadowed by our poor showing in Market Making which earned only $32 million and our currency hedging position, which lost $92 million.

Of this $92 million loss, $61 million is applied against Market Making profits resulting in a net loss of $29 million in Market Making and the remaining $31 million is reported below the line as other comprehensive income.

As you know, we maintain our net capital of nearly $5 billion in a basket of 16 currencies we call the GLOBAL. As a globally diversified enterprise doing business in 27 countries and we found this to be a prudent approach to reduce our currency risk on the long-term.

It is true that quarter-to-quarter this approach contributes a great deal of volatility to our earnings as reported in U.S. dollars, but we believe that it will smooth out over the long-term. We feel more secure that we'll be holding something of value even if some of these currencies in the basket are basically zero.

This quarter the Japanese yen, the euro and the British pound wreaked havoc in our currency basket. But we must not lose sight of the fact that the U.S. is printing more money than all the others combined. The GLOBAL lost 1.9% against the U.S. dollar during the quarter. At the end of the quarter, 41% of the GLOBAL was comprised of U.S. dollars and Hong Kong dollars, which have a fixed ratio.

Now returning to our favorite topic, our brokerage business, produced a profit of $111 million, a 33% increase from the year ago quarter and a profit margin of 57%. Our long-term strategy is validated, and by long-term I do mean long-term. We entered into the brokerage business as a sideline to Market Making exactly 20 years ago.

The idea was that we would make available to others our already existing global automated network to exchanges, our existing systems to execute ,clear and settle, to borrow and lend shares and to pay and receive funds in different currencies, to conduct daily business at very low additional cost. That we could pass on to our customers the bulk of the savings and that coupled with our expertise in getting the best prices, it would be a compelling offer to professional traders and investors.

We also warned during our IPO six year ago that while our Market Making business was thriving at the time there was no barrier to entry to that business, while an efficient brokerage platform required a great deal of system resources and automation that takes a long time to develop. So it is with great satisfaction that we see our brokerage business finally taking off in a big way, just as our Market Making business is fading.

To give you some numbers our cleared customer accounts increased by 12% year-over-year. Institutional customers now comprise 40% of our accounts and nearly 60% of our customer equity. This is reflected in the growth of customer equity, which has increased at the rate of 32% year-on-year to $35.6 billion, while our margin balance has increased 23%, boosting net interest income by 27%.

Equity in the average customer account grew by 10% year-on-year to $164,000. DART for the quarter were 465,000 up 9% on the year, but there were larger trades resulting in average commissions of $4.61 per trade, up 15%.

Our average stock trade contained 1,400 shares at a commission of $2.36. Average option trade contained 11 contracts of $7.44 commission and 3.6 contracts to the average future trade of $6.30 commission. Please keep in mind that these numbers include exchange fees and are averaged over some 100 exchanges, many of which have very different fee structures.

Equity capital in our brokerage subsidiary increased by 21% year-on-year and now stands at $2.1 billion. Our Standard & Poor's rating of A minus with a stable outlook, is better than that of Goldman or Morgan Stanley, which both has negative outlooks, and much better than other non-bank brokers like Jefferies or Raymond James.

I think with this quarter we have entered into a new growth phase for our business and we'll continue to see faster growth in customer accounts, equity, DART's and margin loans. Our plan is to continue to develop our systems and to provide better execution prices and generally better services in more products and market centers at the lowest cost and we are committed to doing that.

Market Making continues to underperform. Besides the usual complaints about low volatility with an average VIX of 13.5 and a low actual versus implied volatility ratio and tight competitions in bid offer spreads, we must admit to an ever increasing disadvantage.

As more and more institutional traders are coming to the option market, we find ourselves making dumb two-sided markets to people, who are acting upon thoroughly researched and timely predictions. They know when news is going to break and set up their positions for quick bounces in volatilities and having been prepared they react ever faster and more correctly than we could adjust our markets.

In other words, we provide two-sided quotes to anyone who comes to market with the idea that we are straddling the most probable equilibrium price and are likely to earn part of the difference between our bid and offer. However, the unfortunate fact is that we find ourselves accumulating positions on the wrong side of the market more and more often than we used to. This means that our estimate of the equilibrium price is off and our trading counterparts have a better one than we did. While our markets were more volatile and spreads were wider and our counterparties less sophisticated, we could make up for these disadvantages, but we now see that we are holding the wrong end of the stick more often.

In response we have widened our dealing spreads in several products and decreased our trading volumes. We think that other market makers must be in similar positions, so that in the near future we expect to see a widening of spreads, either as a result of others following suit or leaving the business altogether.

You may remember that we paid out a $1 special dividend last year and that we continue to pay $0.10 regularly quarterly and both of these come out of our Market Making capital, diminishing it substantially as we follow along with periods in which Market Making does not earn sufficient profit to make up for the dividend expense. As a result our worldwide Market Making capital is now down to $2.7 billion.

Should the circumstances continue along the same lines, you will see a gradual transformation of Interactive Brokers into a pure brokerage firm. I know that you like that transformation and you would like it to happen faster, but we are still not convinced, so please do not rush us; let us take our time. Thank you.

Paul Brody will give you the financials.

Paul Brody - Chief Financial Officer

Thank you Thomas. Thanks everyone for joining the call this quarter. As usual I'll review the summary results first and then talk about some segment highlights before we take questions.

In the first quarter we saw the continuing trend of robust growth in our brokerage business and weakness in the Market Making segment; that revenues this quarter were driven by rising brokerage commissions and net interest income partially offset by declines in trading gains, which were exacerbated by translation losses on the strength of the U.S. dollar relative to other currencies.

For those of you who may not be familiar with our financial presentation, our financial statements include the GAAP accounting presentation known as comprehensive income. Comprehensive income reports all currency translation gains and losses, including those that reflect changes in the U.S. dollar value or the company's non-U.S. subsidiaries, which is known as Other Comprehensive Income or OCI. These are reported in the statement of comprehensive income.

In light of the strengthening of the U.S. dollar against a number of other currencies, adding OCI to net income decreased our reported earnings per share by $0.08 for the quarter.

Overall operating metrics for the latest quarter were mixed. Volumes were up in futures and stocks and down in options versus the year-ago quarter. Average overall daily trade volume was just over 1 million trades per day, up 9% from the first quarter of 2012.

Electronic brokerage metrics showed healthy increases in a number of customer accounts and customer equity. Total and cleared customer DART's were both up from the year-ago quarter and sequentially. Orders from cleared customers who clear and carry their positions and cash with us and contribute more revenue accounted for 91% of total DART, holding fairly steady with recent quarters.

Market Making trade volume was up 10% from the prior year quarter, mixed across the product types. Option and contract volume was down 10% of futures contract volume and stock share volume were up 54% and 40% respectively.

Net revenues were $216 million for the first quarter, down 29% from the year-ago quarter. Trading gains were $19 million for the quarter, negatively impacted by currency translation effects. While our trading gains compare to the year-ago quarter decrease by 86%, excluding the currency translation, trading gains would have dropped 42% from the year-ago results.

Commissions and execution fees were $120 million, up 19%. Net interest income was $58 million, up 22% from the first quarter of 2012, and brokerage produced $54 million and Market Making $4 million of the net interest income.

Other income was $20 million, up 9%. Non-interest expenses were $134 million, down 13% from the year-ago quarter. Within the non-interest expense category, execution and clearing expenses totaled $60 million, down 8% from the year-ago quarter, as significantly lower Market Making fees partly offset increases in brokerage fees.

Compensation expenses were $46 million, a 26% decrease from the year-ago quarter. This decrease reflects two factors; first, a reduced accrual for bonus compensation in the Market Making segment. And second, the 2012 comparative period included a special one-time stock incentive plan grant to employees.

At March 31 our total headcount was 888, an increase of less than 1% over the year-ago quarter and a slight decrease from the prior year headcount. As a percentage of net revenues, total non-interest expenses were 63% and out of this number, execution and clearing expense accounted for 28% and compensation expense accounted for 21%. Our fixed expenses were 34% of net revenues.

Pre-tax income was $82 million, down 45% from the same quarter last year. For the quarter, brokerage accounted for all of the income, partially offset by the loss in Market Making. Ex-currency effects, brokerage represented 78% and Market Making represented 22% of pre-tax income from the two segments.

For the first quarter our overall pre-tax profit margin was 38% as compared to 49% in the first quarter of 2012. Brokerage pre-tax profit margin was 57%, up from 52% in the year-ago quarter. Market Making pre-tax profit margin was negative 123%, including the translation effect and 38% without translation effect.

Comprehensive diluted earnings per share were $0.06 for the quarter as compared to $0.33 for the first quarter of 2012. On a non-comprehensive basis, which excludes OCI, diluted earnings per share on net income were $0.14 for the quarter, as compared to $0.27 for the same period in 2012.

Turning to the balance sheet, as a result of the growth of our brokerage business and the withdrawal of capital from our Market Making operations through a regular and special dividend, brokerage continues to account for over two-thirds of our balance sheet assets. From the year-ago quarter, cash and securities segregated for customers rose 13% and secured margin lending to customers rose 32%, while positions and securities held by our Market Maker units were paired back by 27%.

As Thomas mentioned, our regular quarterly dividends will continue to reduce the capital related to the Market Making segment unless higher profitability returns. Nonetheless our balance sheet remains highly liquid with low leverage. We actively manage our excess liquidity and we maintain significant borrowing facilities through the securities lending markets and with banks.

As a general practice, we hold an amount of cash on hand. It provides us with a buffer should we need immediately available funds for any reason. We also continue to maintain over $2 billion in excess regulatory capital in our broker-dealer companies around the world. Long-term debt at March 31 remained at zero, and our consolidated equity capital at March 31 was $4.83 billion.

The segment operating results are summarized in the earnings release and will be more fully detailed in our quarterly 10-Q report, so I'll just highlight some noteworthy items. Starting with electronic brokerage, customer trade volumes were up across all product types. Cleared customer options and futures contract volumes were up 25% and 27% respectively and stock share volume was up 18% from the year-ago quarter.

Customer accounts grew by 11% over the total of March 31, 2012, and by 3% in the latest quarter. Total customer DART's were 465,000, up 9% from the year ago quarter and 14% from the fourth quarter of 2012. Our cleared customer DART's, which generate direct revenues for the brokerage business were 422,000, up 8% on the year-ago quarter and 12% sequentially. The average number of DART's per account on an annualized basis was 496, down 3% from the 2012 period, but up 9% sequentially.

Commission revenue rose on a product mix that featured larger average trade sizes across options, futures and stocks. This resulted in an overall average cleared commission per DART of $4.61 for the quarter, 15% higher than the year-ago quarter, 11% higher sequentially.

These numbers reflect our success in attracting institutional customers who trade in larger size. Customer equity grew to $35.6 billion, up 23% from March 31, 2012 and up 8% sequentially. These changes took place during periods in which the S&P 500 index rose 11% over the past year and 10% over the last quarter.

The source of this growth continues to be a steady inflow of new accounts and customer deposits. In addition, our favorable financing rates have allowed us to attract customer margin borrowings. After falling to lows in the fourth quarter of 2011, margin debits have been building steadily to $11.1 billion, 32% over the quarter end level a year ago.

Customer credit balances, which increased 20% over the year-ago quarter also continue to grow progressively, though spread compression, especially in certain foreign currencies persist in restraining interest income. Higher options and futures trade volumes resulted in top line revenue from commissions and execution fees of $120 million, an increase of 19% from the year-ago quarter and 16 % sequentially. These revenues are spread mainly across options, future stock and foreign exchange.

Net interest income rose to $54 million, up 26% from the first quarter of 2012 and 11% sequentially. Low benchmark interest rates, which continue to compress the spreads earned by our brokerage units have been offset by steadily higher customer credit balances in each successive period, and our aggressive lending rates have boosted customer margin borrowing.

Our fully paid stock yield enhancement program continues to provide an additional source of interest revenue that is shared with our participating customers. As a result, our net interest income as a percentage of net revenue rose slightly to 27%.

Execution and clearing fees expenses increased to $36 million for the quarter, up 19% from the year-ago quarter and 5% sequentially, in line with the volume increases. Fixed expenses increased to $48 million, up 6% on the year ago quarter, primarily due to higher employee compensation-related expenses and pre-tax income from electronic brokerage was $111 million for the first quarter, up 33% on the year-ago quarter and 27% sequentially.

Now turning to Market Making, trading gains from Market Making for the first quarter of 2013 were $19 million, down 86% from the year-ago quarter. Currency translation effects negatively impacted the first quarter's reported earnings by $61 million, while the year-ago quarter's reported earnings were reduced by only about $1 million.

Our overall equity as measured in U.S. dollars was reduced by the strengthening of the U.S. dollar against certain currencies. More specifically, we measured the overall loss from our strategy of carrying our equity in proportion to the basket of currencies we call the GLOBAL to be about $92 million for the quarter. Because the $31 million translation loss is reported as other comprehensive income, this leaves the loss of $61 million to be included in reported earnings. To summarize this, if we eliminated all currency effects, pre-tax income from Market Making for the first quarter of 2013 would be about $32 million.

Execution and clearing fees expenses decreased to $23 million for the quarter, down 33% on the year-ago quarter, driven by lower trading volumes and options. Fixed expenses decreased to $29 million, down 30% from the year-ago quarter, primarily due to lower accruals for bonus compensation, commensurate with the lack of profitability. And pre-tax loss from Market Making was $29 million for the quarter without adjusting for OCI. Taking into account the $60 million shift and the currency effect, the year-over-year decrease in pre-tax income from Market Making would be about 52%.

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

Question-and-Answer Session

Operator

(Operator Instructions). We'll take our first question from Chris Harris. Please go ahead Chris.

Chris Harris - Wells Fargo

Hey, good afternoon guys.

Thomas Peterffy - Chairman & Chief Executive Officer

Hello.

Chris Harris - Wells Fargo

So first question I want to kind of get out is the topic of kind of gradually morphing into a pure play broker and just curious if you guys have ever thought about or entered into any discussions with any other parties about potentially selling the market maker. And the reason I ask that, even if you had to take a substantial discount on that sale, it seems like you could unlock a lot of value. So curious to see what you guys thought about that. If it's anything you've ever explored.

Thomas Peterffy - Chairman & Chief Executive Officer

By discount you mean discount to the cash we have in the business?

Chris Harris - Wells Fargo

Discount to book value.

Thomas Peterffy - Chairman & Chief Executive Officer

Now why would I? Why wouldn't I just wind it down?

Chris Harris - Wells Fargo

Yes, why not just do that then? Because…

Thomas Peterffy - Chairman & Chief Executive Officer

I told you. I try to make very, very sure that you all pay attention to the idea that I know that you want me to close this down, but I'm not so sure that this is finished. So I would like to take my time and do it slowly, maybe it will reawaken.

Chris Harris - Wells Fargo

Okay, that's fair enough. I guess the other question relates to the dividend. Thomas you had mentioned the dividend is based on what happens with the market maker. Does that mean if conditions continue to deteriorate, could you possibly be looking to cut the dividends or could you just base it or allocate capital from the broker to pay the dividend?

Thomas Peterffy - Chairman & Chief Executive Officer

We will not cut the dividend. We will continue to pay the dividend from the market maker.

Chris Harris - Wells Fargo

Right. If the market maker goes away, then I guess you don't have anything to pay the dividend with, unless you…

Thomas Peterffy - Chairman & Chief Executive Officer

Well, then we have $2.7 billion.

Chris Harris - Wells Fargo

Alright, so you could use the broker for that. All right, so last…

Thomas Peterffy - Chairman & Chief Executive Officer

No, we'll have the broker and after the market maker has gone away we'll have $2.7 billion of the market maker that is left behind, yes.

Chris Harris - Wells Fargo

Yes, okay I got it. A real quick last question then for the brokerage business, you guys are definitely getting momentum there, but I'm just kind of curious as to why growth isn't even better and I know that's kind of an unfair question to ask, because you guys are growing faster than anybody else, but it just seems like your value proposition is so much stronger. I would think that you guys would be taking even more share than you really are.

So as you talk to clients or prospective clients, what are the kind of the objections to moving more accounts or capital to your broker?

Thomas Peterffy - Chairman & Chief Executive Officer

The objections are always the same. Some people do not believe the value proposition. Some people who manage money for others say that their customers do not know Interactive Brokers and they would be worried to be exposed to us, even though we explain to them that our credit seems to be, at least by S&P, seems to be valued higher than that of Goldman or Morgan Stanley.

It's a slow push, but as you'll see we are catching on. I think the growth is quickening and I think that this is as I said, I think it's going to quicken even further. So our growth is curving up.

Chris Harris - Wells Fargo

Okay great. Thanks.

Operator

Thank you and we'll take our next question from Rich Repetto from Sandler O'Neill. One moment while we open Rich's line. Taking just a minute. There we go Rich, your line is open.

Rich Repetto - Sandler O'Neill

Yes, good evening Thomas. How are you?

Thomas Peterffy - Chairman & Chief Executive Officer

Good evening.

Rich Repetto - Sandler O'Neill

Well, so the Brokerage is setting all new records here. And I guess I'm assuming it's come incrementally more from institutional, would that be correct and any of these tools that you talked about last quarter like the Money Manager Marketplace or anything else helping you with the record growth here or the growth?

Thomas Peterffy - Chairman & Chief Executive Officer

I mean it's hard to tell what exactly that's helping, but as Chris said before, our value proposition is definitely better than anybody else in this business and slowly but surely people will begin to accept it.

Rich Repetto - Sandler O'Neill

And is it fair to say that it's come in incrementally more from the institutional side?

Thomas Peterffy - Chairman & Chief Executive Officer

That is correct, yes. Institutional accounts are growing at the higher rate and money in institutional accounts is growing as a percentage of total money and commission derived from institutional accounts are also growing higher than the overall commissions.

Rich Repetto - Sandler O'Neill

And have you grown the sales force at all or anything else. Is it still just plainly the value, the product, the value proposition rather than…

Thomas Peterffy - Chairman & Chief Executive Officer

The sales force has grown some, not a great deal, but maybe we added and we grew another 10%. So we added about three sales people in the course of the last year. So we are around 33, if I'm correct.

Rich Repetto - Sandler O'Neill

Okay. And I guess my last question Thomas is, so when you say the gradual transformation, we know you have the mechanism of the dividend and I fully understand it, and I respect the idea that this thing did earn the $1.2 billion not too long ago. The gradual mechanism, the gradual process that you are talking about, is it the same processes that we are aware of where the dividend eats into the capital or is there something else that you have in mind?

Thomas Peterffy - Chairman & Chief Executive Officer

No, it eats into capital, other things being equal. Now we could have another special dividend. I'm not saying that I'm thinking about it, but that would be a possibility and though I'm not planning it. So yes, if we completely stop the Market Making business, which I don't think we'll do, at least not in the near future, but if we did, then we would pay up with special dividends.

Rich Repetto - Sandler O'Neill

And then just the capital at the market maker, the 2.7 something. Paul, how did that change quarter-to-quarter?

Paul Brody - Chief Financial Officer

Well, in the end of the year we gave about $400 million out and then it didn't change much over the quarter, other than the fact that we paid the regular, about $40 million in the regular quarterly dividend and lost a little bit of money.

Rich Repetto - Sandler O'Neill

Got it, okay. So very last I promise. This is the last one, promise, that when the timeframe, when you say gradual and again respecting the profitability prior of this unit, so is this something that's a year, a two year process or am I thinking about it correctly or what timeframe is gradual to you?

Thomas Peterffy - Chairman & Chief Executive Officer

It all depends on what is going to happen in the next quarter and the next quarter and next quarter. We'll remain flexible, and see how it goes. We are not masochists. If it really doesn't work at all, then we'll have to think about shutting it down, but I don't think the chances are that that will happen.

Rich Repetto - Sandler O'Neill

Understood. That's all I have, thank you.

Operator

Thank you. And we'll take our next question coming from Chris Allen from Evercore.

Chris Allen - Evercore

Good afternoon guys. It's just that I'm kind of following-up on that, and Thomas it's your statement that this may not happen and it could reawaken. Are you thinking about this somewhat like the cycle that we saw post the financial crisis when new capital came in, volatility came lower and then it had to be flushed out and people pulled out of the marketing business. Are these kind of the signposts that you are thinking about moving forward?

Thomas Peterffy - Chairman & Chief Executive Officer

No. What I'm thinking about is that there are a bunch of us in this business and nobody is making a living and I think that we're a little bit better than probably most of our competitors. So I think that they will have to throw in the towel before we would and once a few of them leave, then the rest of us will have acceptable returns. Of course if the return goes very high, then people will come back, but I think that it's a business where one should be able to make about 10% pre-tax return and that would be sufficient for us to stay in the business.

Chris Allen - Evercore

Got it. In terms of I guess one of the way I was thinking about this, the capital in the Market Making business, if you had a chance to do an acquisition to bolster the brokerage business and utilize that capital within the Market Making business, would you consider that to maybe accelerate some of the shift?

Thomas Peterffy - Chairman & Chief Executive Officer

I would consider it, but it's hard for me to imagine what kind of big acquisition we could make that would bolster our brokerage business, because most other brokerage businesses are very different than ours.

Chris Allen - Evercore

Got it. Alright, thanks a lot guys.

Operator

Thank you. And our next question is from Mac Sykes from Gabelli & Co. Mac, please go ahead.

Mac Sykes - Gabelli

Good evening gentlemen. Thomas, I assume you're seeing a little bit of volatility in the commodities recently. I was wondering if you could give us some of your wisdom about what may be driving that volatility. Secondarily, are you seeing any particular stress with some of your commodities focused traders, and then if there is fallout from this down draft, what might be some of those negatives?

Thomas Peterffy - Chairman & Chief Executive Officer

I do not know. I listen to the same commentators you do, so I don't have anything special to say as to what would cause it, except that I started my business career in the gold business, and always thought that gold has no intrinsic value. So it could go to $1 an ounce, it could go to $1 million an ounce, I don't know.

As to the impact of these last few days on customers, it hasn't been good. Customers have lost a lot of money, our customers have and I assume everybody else's has. We have taken some very small losses on certain accounts who didn't have sufficient funds in their accounts to make up for their losses, but of course as you know, we have all automated closeouts when the markets are open, so we have liquidated many accounts and as I say, our losses were, so in the total our losses are in the $100,000 range. But I assume that other brokers who do not have automated close-out policies must have taken much more substantial of it and so we basically have two fall-outs from this.

One is that, while many of our customers have lost substantial amounts. As a result our customer deposits have diminished by those mostly. But secondly, our competitors, brokers who are less automated than we are, maybe have suffered more and are therefore less likely to compete with us as vehemently they otherwise would.

Mac Sykes - Gabelli

Thank you. I've asked this before but I'm going to try again. You continue to actually keep well. Certainly on the brokerage you've highlighted that was deepest visibility on the interest revenue. Given the trajectory of the business and the visibility and the firm's discount to intrinsic value, wouldn't it make sense now to use cash flow to shrink the cap despite the slight premium to book you've talked about in the past?

Thomas Peterffy - Chairman & Chief Executive Officer

I don't understand why can't I use cash flow to change the capitalization?

Mac Sykes - Gabelli

Right, to increase share repurchases or…

Thomas Peterffy - Chairman & Chief Executive Officer

Well, they cannot do that because of our tax circumstance that we are in and we have a very small float out there. We only have 12% of the company floating, so if you took back half of it, it wouldn't make much sense.

Mac Sykes - Gabelli

Then my last question is, how much does Market Making profitability affect brokerage? In other words, assuming that Market Making did cease operations, what would be the impact on brokerage?

Thomas Peterffy - Chairman & Chief Executive Officer

Well, as you know we have systems cost, exchange connections, back office functions that are shared between the two segments. So obviously the expenses on the brokerage side would go up if the Market Making activity would go down. So that's one reason why one would go about this in a slow manner.

Mac Sykes - Gabelli

Is there any way to sort of quantify that in terms of the margin of the two, just looking at the last quarter?

Thomas Peterffy - Chairman & Chief Executive Officer

Well, we know very well what our expenses are in each segment and they are roughly 60% brokerage and 40% Market Making.

Mac Sykes - Gabelli

Thank you.

Operator

Thank you sir. And our next question is coming from Sean Brown from Teton Capital. Sean, your line is now open.

Sean Brown - Teton Capital

Yes, hi guys. Congratulations on the great brokerage performance. I just got a quick question on the non-brokerage equity or I guess the market maker equity as you guys refer to it, sort of returns on that low and declining.

So what do we need to see to accelerate the process of winding down or repatriating some of the capital? I mean I know this is a sensitive topic, but is it X number of quarters or years of sort of low pre-tax returns and low spreads. I know that it could always come back at some point, but where do we draw the line in terms of accelerating the process versus going at the current pace? Thanks a lot.

Thomas Peterffy - Chairman & Chief Executive Officer

I think this is a third or fourth time I got this question in the last half an hour. I cannot say anything more than to repeat what I said before. I cannot see into the future. You are telling me, okay, so what would we do if in the next quarter the return would be in low single digits and then the following quarter in low single digits and three quarters from now in low single digits.

Yes I mean, as long as the returns are in the low single digits we will try to work on transferring more and more of our resources and expenses into the brokerage side. If we have a fantastic quarter that will slow that process. So you should look for bad quarters in Market Making.

Sean Brown - Teton Capital

Alright. Is there any sort of maximum pace where you'd say, we don't want to load up brokerage with expenses too quickly?

Thomas Peterffy - Chairman & Chief Executive Officer

No, it is a secondary consideration. No, that's not a serious issue on it. If we only told that everybody would be better off closing down the Market Making, we will just close it down, but we do not think that. I keep repeating. We believe that although it will never return to those high flying days that we used to have, we do believe that there is a very good chance that we will be able to enjoy a roughly 10% pre-tax return on our Market Making capital in the coming years.

Sean Brown - Teton Capital

Got it. Well, you definitely know that business better than us Thomas. So thanks for being a good steward of the businesses. Thanks a lot guys.

Thomas Peterffy - Chairman & Chief Executive Officer

Thank you.

Operator

Thank you. And our next question is from Niamh Alexander from KBW.

Niamh Alexander - KBW

Hi, thanks for taking my question. I just have one at this point. If you could Thomas, what can you share with us about the growth in the brokerage business and are you seeing kind of outsized activity maybe in FX? It seems like you really are sending a message to the market that institutional is really getting the traction and bringing up the commissions as well as the activity.

But what about international? What can you share in terms of what's coming from the international mix and any particular markets that are stronger than the others where you might see more growth or more of a ramp up from here?

Thomas Peterffy - Chairman & Chief Executive Officer

Yes. More than 50% of our new accounts are outside of the United States and the fastest growing region for both, for new account growth and customer deposits and commission revenues is Asia. Asia is growing faster, Europe is holding steady and America, including Canada and South America are shrinking as far as the relative percentage of their import in the total mix.

Niamh Alexander - KBW

That's wonderful. Thanks Thomas and then just lastly on that and what's the mix of say of retail versus institutional. So in the Asia market, which is the biggest growth market here right now, is that mostly institutional or is it more retail?

Thomas Peterffy - Chairman & Chief Executive Officer

I'm sorry, we haven't analyzed it carefully enough, so I cannot tell you.

Niamh Alexander - KBW

Okay. Thanks for taking my questions.

Operator

Thank you. And our next question is from Sameer Murukutla from Macquarie Capital. And Sameer, your line is now open.

Sameer Murukutla - Macquarie Capital

Good afternoon guys. I had a question regarding the employee compensation, which came in below my expectations and it seems like lowest levels since like 2010. I was finding a slight increase based on maybe bonus payments and just increase in payroll tax. Is this a new normal run rate that we should be expecting going forward, assuming the market maker continues to remain sluggish?

Paul Brody - Chief Financial Officer

We have adopted a sort of new accrual policy to bring those bonus expenses in the Market Making and in line with the profitability. So if it remains sluggish than the accruals, the bonus expense will remain low.

Sameer Murukutla - Macquarie Capital

Thank you.

Operator

Thank you. And I'm showing another question from Justin Hughes, Philadelphia Financial. Justin, please go ahead.

Justin Hughes - Philadelphia Financial

Good afternoon. I just wanted to ask, how do you arrive at the 10% targeted return in the market maker, evens if it's like 10% pre-tax, because for us public investors that actually have to pay tax, it's only 6% after-tax return and that's just not adequate return for the risk in the volatility that we see and that's not even what we're targeting now. You are saying someday maybe we can get back to a 6% after-tax return on equity. I mean that's just not enough for us public investors.

Thomas Peterffy - Chairman & Chief Executive Officer

I understand. That's why public investors value the market maker book.

Justin Hughes - Philadelphia Financial

But we're valuing at a book, because it's not a good use of capital?

Thomas Peterffy - Chairman & Chief Executive Officer

That's right.

Justin Hughes - Philadelphia Financial

I mean, I know people are asking – some people are saying just shut it down, but why not just increase your payout out of that business and return capital rather than just having to say we're in it or we're not in it. Maybe just increase the payout ratio to more like 15% or 20%. Maybe if you right size the capital, it's still an attractive business?

Thomas Peterffy - Chairman & Chief Executive Officer

But you are telling me to do it faster. I hear you.

Justin Hughes - Philadelphia Financial

Okay. But don’t you think it would be fair to weigh public investor’s return requirements over time, not just this quarter or next quarter, the quarter after that, but over time to target higher returns for public shareholders?

Thomas Peterffy - Chairman & Chief Executive Officer

I don’t agree with you that our – if the market maker were making 10% and the broker were making 25%, that the total mix would be not acceptable.

Justin Hughes - Philadelphia Financial

Okay, thanks.

Operator

Okay, thank you. And I’m showing no further questions in the queue. I’d like to turn the conference back to your host for any concluding remarks.

Deborah Liston - Director of Investor Relations

Thanks everyone for participating today. And just a reminder, this call can be available for replay on our website shortly. Thanks again for your time and have a great evening.

Operator

Ladies and gentlemen, this does conclude your conference. You may now disconnect and have a great day.