

Interactive Brokers Group's (IBKR)

Q2 2018 Results - Earnings Call Transcript

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Executives

Thomas Peterffy - Chairman and CEO

Paul J. Brody - CFO

Nancy E. Stuebe - Director, IR

Analysts

Chris Harris *Wells Fargo Securities*

Doug Mewhirter *SunTrust Robinson Humphrey*

Kyle Voigt *Keefe, Bruyette, & Woods*

Rich Repetto *Sandler O'Neill*

Reinhart Schmitz

Operator

Good day, ladies and gentlemen, and welcome to the Interactive Brokers Group Second Quarter Financial Results Conference Call. (Operator Instructions) As a reminder, this conference may be recorded.

I would now like to turn the conference over to Ms. Nancy Stuebe, Director of Investor Relations. Ma'am, you may begin.

Nancy Stuebe

Good afternoon, everyone. Thomas is on the call but he has asked me to present his comments on the business. Thank you for joining us to review our 2018 second quarter performance.

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

Once again, in this quarter, we set new records in our brokerage business. Just 1 year after we passed the \$100 billion mark in customer equity for the first time, we ended the quarter with \$134.7 billion. We also hit an all-time high in customer accounts, up 27% to over 542,000. Margin lending, at over \$28 billion outstanding, was also up 27% from the year-ago quarter although it did moderate somewhat sequentially.

Our growth and momentum continued to increase. The pretax margin in our brokerage business reached 64% for the quarter. DARTs this quarter were 797,000, up 19% over last year, so they were down from the very active first quarter as market volatility slowed from the high levels earlier this year. The 19% DARTs increase comes from account growth and not from making acquisitions.

It is not that we have some fundamental objection to acquisitions, but whenever we look at an opportunity, we encounter the barrier of our own extremely low pricing. Sellers hope to receive a multiple of revenues, but after transferring those accounts to our platform and our pricing, they would generate substantially lower revenues, so that we cannot justify paying for them based on the sellers' pricing. It is ultimately those customers who had realized those savings who'll eventually transfer those accounts to us anyway, we hope.

Commissions per DART were \$3.86, down slightly from last year. Commissions per DART will probably continue to decline slowly as we sign up more and more introducing broker accounts, where the brokers pay us based on their customers' combined volume and charge their customers the price we would charge them as an individual account, or possibly even more.

As it is our goal to become the largest broker in the world, we are happy with this outcome and want more and more introducing broker accounts.

On the interest income side, our low margin rates continue to attract new customers. The Federal Reserve raised interest rates 25 basis points again in June, which will benefit our net interest income in the quarters to come, and also serves another benefit for Interactive Brokers - to highlight the difference between what we pay on idle cash and what we charge for margin loans and what our competitors charge. Our U.S. rates range from 2.2% for the largest loans to 3.4% as the maximum rate on small amounts. Our competitors charge 5% as their minimum, all the way up to 10%. That is 50% to 200% more than our maximum rate. Although, we are being told by some helpful would-have-been customers that in some cases, our competitors are willing to negotiate and come close to our rates. But they cannot do that across the board because it would seriously impact their income.

Yet while our rates are, by far, the lowest in the industry, they are still quite profitable and they attract new customers and more institutions to us. Our prices are available to everyone on our platform. We believe in transparency, so we do not have negotiated rates. The prices you see on our site are what you will pay. Your performance is going to be better with us because you are not overpaying for your margin loans. We are equally transparent about what we pay to our customers on our cash balances. For qualified accounts, we pay benchmark Fed Funds, less 50 basis points, on U.S. dollars and comparable on other currencies relative to the rates of the relevant central banks and money markets.

Our clients earn 1.41% on their qualified U.S. dollar cash. Each future interest rate increase gets passed on, fully, to our customers. That is real money on cash that gets automatically credited to your account, not cash that has to be moved to and from a different account or invested into a money market fund that must be sold before the cash becomes available for investment or to reduce margin loans or for withdrawal.

Our commitment to low rates on borrowing and high rates on cash has helped grow our overall business. We are frequently asked why we feel the need to be priced so much better than our

competitors. Customer accounts are very sticky, and we must be able to make an overwhelmingly compelling case to our prospective customers to get them to move their accounts.

Our pretax profit for the quarter was \$271 million. Adding back the \$18 million for this quarter's unfavorable currency impact, net of Treasury mark gain, gives us \$289 million, for a 62% pretax margin. Brokerage was \$280 million of this and achieved a 64% pretax margin. Our public competitors have pretax margins that are 10%, 20% or even 30% below ours.

Now for the breakdown by customer of how our brokerage business is evolving. Once again, in all our customer segments, we saw strong growth in accounts, client equity and commissions.

For the second quarter, hedge funds and proprietary trading firms were 4% of our accounts, 20% of our client equity and 26% of our commissions. Our hedge fund business alone saw a 35% jump in customer equity as our low margin rates and high cash interest give more institutions reasons to move their assets to us to improve their return.

For individual customers, accounts grew 18% and represent 50% of our total accounts. Individuals are 36% of our customer equity, up 29%; and 49% of our commission, up 19% for this customer segment. Commissions benefited from higher volatility in this year's second quarter versus 2017, especially internationally.

Also, investors are becoming more aware of the practice of brokers selling their customers' orders to high-frequency traders, a practice that gives investors lower prices on their sell orders and forces them to pay higher prices on their buys. These customers are increasingly attracted to a brokerage platform that dynamically seeks out the potentially best prices at any moment among the many different trading venues - as these prices, not wanting to push this market away, are often hidden.

Registered investment advisers and introducing brokers are the other two client segments. They represent 17% and 29% of our customer accounts, 23% and 21% of our customer equity, and 17% and 8% of our commission income.

Our introducing brokers segment continues to benefit from two major trends, the increasing regulatory burden worldwide and the growth of a new investor class in developing countries.

First, in developed and developing markets around the world, there are thousands of brokerage firms, some just being newly formed. For a new firm, it is almost impossible in terms of time, knowledge and money, to create the compliance processes and technology needed to be in business. For an existing firm, new, more onerous regulations constantly come up, so an existing broker must either increase its personnel and regulatory costs significantly to comply, or come to us. In both cases, the broker's optimal choice is to outsource their account opening, order routing and back-office functions - to us. That means our platform will be used for the introducing broker's trading, clearing and custody, so what the broker's customers see is a front end with the broker's logo.

Second, in developing countries, investors new to the securities markets prefer to use a local broker for investment guidance. That broker will white brand our platform so he can focus on marketing and building his business and not spend time on processing and compliance. The broker does what he does best, customer acquisition and client service, while we do what we do best, provide state-of-the-art technology, trade processing and detailed billing and reporting, all at low cost.

We continue to roll out new products and services this quarter. We released our new integrated cash management, which adds the variety of financial transactions you can do, including trading multiple products in multiple currencies from a single Interactive Brokers account. We now offer our recently introduced Debit MasterCard, our new Bill Pay function and will soon be introducing Payroll Direct Deposit. This means our customers will have less and less reason to leave our platform to transact any of their financial business.

Another recently introduced feature, our Insured Bank Deposit Sweep Program, gives our customers up to \$2.75 million in SIPC- and FDIC-insured deposits. Participation continues to grow and passed \$1 billion this quarter.

We have the opportunity to accelerate our growth even more. Interactive Brokers' success comes

not from maintaining our platform, it comes from what we do all day long, create additional capabilities. We want to remain in the forefront as the best broker with the best technology. This is what we will continue to do to maintain our edge and our growth.

Our growth comes from existing customers adding to their accounts and from new customers. New customers come to us from big banks and wirehouses and from the large online brokers, who, in turn, may get those customers from the wirehouses as well before these move on to us, and from people opening brokerage accounts for the first time.

More than half of our new accounts come from international customers who appreciate the global access, seamless trading in multiple product classes across multiple currencies and our best-in-class pricing. In the U.S., new accounts often come from sophisticated individuals and institutions who recognize the technology we offer at low cost and our superior trade execution.

Finally, good word-of-mouth is an important source of new accounts. Because our pricing is the lowest in the industry, the only reasons potential clients may not have an account with us are that they either do not know of us, do not believe that our pricing is for real or they do not trust our offerings. As more and more people come on to and trust our platform though, they spread the word that our company and pricing are for real, which contributes to stronger account growth.

Now Thomas would like to say a few words. Thomas?

Thomas Peterffy

As you are well aware, the stock price has come down substantially in recent weeks, and people often ask me why that is.

I can think of two reasons. First, people may think that the tariff negotiations may have an unfavorable impact due to our international client base, especially in China. This is very possible, although so far, we have not experienced any change. Approximately 16% of our accounts come from China.

Second, our currency exposure. Shareholders often ask why we carry foreign currency balances. When the dollar goes down, our reported earnings rise, but we do not get rewarded for it. While when it goes up, the earnings fall and we get penalized.

To answer this question, I would like to take this opportunity to once again explain our business model.

IBKR is a highly automated global electronic broker. Wherever you are, whether you are a hedge fund, a proprietary trading firm, a financial adviser, a broker or an individual investor or trader, wherever you want to invest around the world, in whatever product, using whatever currency, you can do so on the IBKR platform, at any time of the day or night, and custody your assets with us at lower cost than any of your alternatives.

This is the concept we started out with, and this is the technology we have been building for at least 25 years.

Electronic exchanges, so-called Fintech companies, and many new regulations have grown up in our tracks all around us.

What this meant for us is that we had to set up locally-registered, wholly-owned brokerage entities in addition to the U.S. - in the U.K., Hong Kong, Japan, India, Australia, Canada - and become remote exchange members in many other countries in Europe, the Middle East, Latin America and Asia, where we execute and custody our customers' positions. This build-out is still in process and it will continue for quite a while, until our customers will have immediate access to any trading anywhere around the world, no matter how minor.

All these different entities, our subsidiaries, are running on IBKR technology, but they must comply with local regulations that are often very different than U.S. regulations. These include the requirement to maintain customer funds and regulatory capital in local currencies, so that we must have those currencies on hand. This is the reason for maintaining 30% of our capital in a basket of different non-U.S. currencies. It also has the side benefit that if in the very remote case the U.S. dollar ever went to 0, we will still remain a viable enterprise.

Even before and ever since we went public 11 years ago, this has been our business model. We keep on building it and automating it, competing on technology and price and expecting to continue to grow at double-digit rates. Nothing has changed, and if anything does, we will let you know.

And now Paul Brody will take you through the numbers. Paul?

Paul Brody

Thank you, Thomas, and thanks, everyone, for joining the call. As usual, I'll review our results, put our numbers into context within the current environment. You may be happy to know that this quarter, my comments will follow the format of the earnings release and hopefully leave more time for Q&A.

Operating metrics reflected reasonably active trading in a moderate volatility environment.

Volatility, as measured by the average, VIX, rose to 15.4 this quarter, up 34% from 11.5 last year. While this quarter's average is closer to the historical norm, and represents a meaningful increase over last year, the VIX has retreated to lower levels after an unusually volatile February and March.

This increased volatility led to a rise in derivatives trading volumes. Customer trade volumes rose 13% in options and 21% in futures, while falling 5% in stocks. Foreign exchange dollar volume was down as well.

Total accounts reached 542,000, up 27%, which contributed to customer equity growth of 29% to \$134.7 billion at quarter end. The trend toward attracting larger customers including hedge funds and financial advisers has continued. This has led to our average account size growing to \$249,000, up 2% over 1 year and up 21% from 2 years ago. Growth in introducing broker accounts has also been robust, and although these accounts are of a smaller average size, we're happy to take them on in bulk.

With the continued tailwind from new account growth, our quarterly total DARTs were up 19% versus last year, and our overall average cleared commission per DART fell 4% versus last year

to \$3.86 on a product mix that featured smaller average trade sizes across the board.

Moving to our net interest margin table. Our net interest margin widened to 1.61% from 1.17% in the second quarter last year. The Federal Reserve raised rates again this quarter in late June, making a total of 4 increases in the Fed funds target rate during the preceding 12 months. Due to careful management of our short duration portfolio, we recorded a modest mark-to-market gain of \$3 million on our holdings of U.S. Treasuries. As always, we plan to hold these securities to maturity, but as brokers, unlike banks, GAAP rules require us to mark them to market in our financial reporting. These rate increases, together with increased customer balances, generated more net interest income on cash balances. We believe our continued success in asset gathering should lead to larger contributions from interest-sensitive assets going forward.

Our FDIC-insured Bank Deposit Sweep Program, introduced late last year, has grown steadily to over \$1 billion.

Margin lending and segregated cash management were the most significant contributors to our net interest margin. Average margin loan balances grew 35% versus last year which, combined with higher interest rates, led to margin interest growth of 84%. Our segregated cash interest income rose 60%, primarily on the Fed hikes to U.S. interest rates.

Two factors caused the yields on our segregated cash to lag the increases in Fed funds rates. First, currently about 15% is held in other currencies; and second, given an average duration of investment in Treasuries of about 90 days, roughly 1/3 is not reinvested in any given quarter. So these amounts would not be expected to follow a Fed hike immediately. The decline in segregated cash is a function of both the increase in margin loans and customers' appetite to put more of their cash to work in the securities markets. Note also that the FDIC Sweep Program removes funds that would otherwise be included in our segregated cash balances from our balance sheet for accounting purposes.

Securities lending interest income was lower this quarter as there were fewer hard-to-borrow names that investors were looking to borrow.

And now for our estimate of the impact of the next 25 basis point increase in rates. Given the growth in our customer assets, the investment opportunities available to us, and new product introductions, we are well-positioned to maximize our net interest income. Expectations of further rate increases are typically already reflected in the yields of the instruments in which we invest. Therefore, in our calculation, we attempt to isolate the impact of an unexpected rise in rates, separate from the impact of rate hikes that have already been baked into the prices of these instruments. With that assumption, we would expect the next 25 basis point unanticipated rise in rates to produce an additional \$14 million in net interest income over the next 4 quarters, and \$16 million as the yearly run rate. That run rate includes the reinvestment of all of our present holdings at the new, higher, rate.

Turning to the segments. Electronic Brokerage turned in a solid performance, with gains in both commissions and net interest income. Net revenues were \$443 million for the quarter, up 33%. Pretax income was \$283 million, up 43%, for a 64% margin. Excluding Treasury marks, pretax income was \$280 million, up 39%, with pretax margin also at 64%. Fixed expenses in brokerage were \$97 million, up 20%, and the primary reason for this increase was the transfer of staff from Market Making, with increased legal and compliance expenses and reserves a secondary factor. Customer bad debt expense was immaterial this quarter, a reflection of the continued effectiveness of our risk management systems which limit customer default.

Market Making today consists of the customer facilitation business that we will retain as well as a few profitable markets outside the U.S. which we continue to evaluate. Net revenues were \$22 million, of which \$11 million were Trading Gains and the bulk of the remainder was net interest income. Market Making pretax income was \$9 million, and we remain at about 95% absorption of the \$40 million of expenses that were projected to migrate to Brokerage.

The Corporate segment reflects the effects of our currency diversification strategy. We carry our equity in proportion to a basket of 14 currencies we call the GLOBAL, to best reflect the international scope of our business. As the U.S. dollar strengthened against most other major currencies this quarter, we incurred an overall loss from our strategy of about \$100 million, of which \$79 million is reported as other comprehensive income and \$21 million is included in

earnings. We estimate the total decrease in comprehensive earnings per share from currency effects to be \$0.21, with \$0.02 reported in Other Income and \$0.19 as Other Comprehensive Income.

Turning to the income statement. Net revenues were \$445 million, up 15% over the year-ago quarter. Adding back the \$21 million loss on our currency strategy and deducting the \$3 million gain from marking our Treasury portfolio to market, results in adjusted net revenues of \$463 million for the quarter, up 28% over last year's \$361 million on the same basis. Commission revenue rose 16% on higher volume in options and futures, which tend to carry higher per unit cost than stocks, partially offset by lower average trade sizes. As we noted earlier, the decline of our overall average cleared commission per DART to \$3.86 reflected this mix. Of our \$225 million net interest income, Brokerage produced \$217 million, Market Making \$7 and Corporate, the remainder.

Other Income, which includes our GLOBAL currency strategy, Treasury marks and other fees and income we received, was \$23 million. And aside from the GLOBAL, all areas of other income - gains and fees and Treasury marks - showed modest increases.

Noninterest expenses were \$174 million for the quarter, down 5% from last year. The decline in expenses is due to lower G&A than last year when we took an impairment charge on our U.S. Market Making business in preparation for its transfer. Higher execution and clearing costs were due to stronger trading volume, and compensation and benefits increased modestly.

At quarter end, our total headcount stood at 1,310, an 8% increase over last year. We have been hiring most aggressively in the areas of client services, legal and compliance, and software development, and to this end, we have been building up our operations in India.

Pretax income of \$271 million was up 33% and represented a 61% pretax margin. Adjusted for the noncore items I mentioned previously, pretax income was \$289 million, up 45% over last year's pretax income of \$200 million on the same basis, representing an adjusted pretax margin of 62%. Diluted earnings per share were \$0.58 for the quarter versus \$0.32 for the same period in 2017. Comprehensive diluted earnings per share, which includes all currency effects, were \$0.39

for the quarter versus \$0.41 last year. Without the impact from currencies and Treasury marks, diluted earnings per share would have been \$0.59, \$0.01 higher than the reported EPS for the quarter.

Now, to help investors better understand our earnings, the split between the public shareholders and the noncontrolling interests is as follows: Starting with income before income taxes of \$271 million, we deduct \$8 million for income taxes paid by our operating companies, which are mostly foreign taxes. This leaves \$263 million, of which 82.4%, or that \$217 million reported on our income statement, is attributable to noncontrolling interests. The remaining 17.6%, or \$46 million, is available for the public company shareholders, but as this is a non-GAAP measure, it's not reported on our income statement. After we expense remaining taxes of \$4 million owed on that \$46 million, the public company's net income available for common stockholders is the \$42 million you see reported on our income statement. Our income tax expense of \$12 million consists of this \$4 million, plus the \$8 million of taxes paid by the operating companies. Finally, the \$4 million tax to the public company was relatively low this quarter due to a deduction for the annual vesting of our Stock Incentive Plan shares at a higher stock price, which resulted in tax deduction but no effect on book income.

Turning to the balance sheet, we remain consistently highly liquid with low leverage. We are extremely well capitalized from a regulatory standpoint and continue to deploy our equity capital in the growing Brokerage business. We hold excess capital in order to take advantage of opportunities as well as to emphasize the strength and depth of our balance sheet.

We continue to carry no long-term debt. And on June 30, margin debits were \$28.8 billion, an increase of 27% over last year. Our compelling margin lending rates, especially noticeable versus our peers in a rising interest rate environment, plus our customers' willingness to take on leverage and Interactive Brokers' capacity to satisfy it, have contributed to this growth. This figure may show more swings than in past years due to our success in attracting institutional hedge fund customers, who are more opportunistic in taking on leverage. Our conservative balance sheet management supports the growing margin lending business.

Our consolidated equity capital at June 30, 2018 was \$6.7 billion. \$5.2 billion of that was held in

brokerage, \$1.2 billion in Market Making and customer facilitation activities, and the remainder in Corporate.

Now I'd like to turn the call back over to the moderator, and we'd be happy to take some questions.

Question-and-Answer Session

Operator

(Operator Instructions) And our first question will come from the line of Rich Repetto with Sandler O'Neill.

Rich Repetto

I guess the first question is on, actually, the shares that the brokerage customers traded. We know the DARTs and you preannounced them and we've already done the accounting, but I think it was about 49 million shares traded in the quarter. And that seems like it's the lowest it's been in a year plus. And I know I've talked to you a little bit about this, Thomas, but could you just go in -- is that less of the trading of low-priced stocks reflected because -- can you just give us some color?

Thomas Peterffy

So that's correct. The SEC does not like the newly registered shares or -- which are generally low-priced shares. So yes, that's that. While our higher-priced shares, so to say, the volume increased, the low-priced shares decreased much more substantially.

Rich Repetto

And was that just market conditions or what? I'm trying to see whether that was something regulatory or not.

Thomas Peterffy

Well, it's -- so we are scared to have -- as you remember, at your conference when Chairman

Clayton came on, I asked him about that, because we are getting more and more pushback from the SEC on taking on orders in these low-priced shares. And if you remember, he said that there is a great deal of pump-and-dump activity and other bad stuff going on. And so we have to -- even though we don't know of any that came through us - we had to curtail the activity.

Rich Repetto

Understood. And then another question, you talked -- the prepared remarks that Nancy did -- talked about where another broker -- a potential acquisition of another broker, sort of hits a stumbling block because of the price of your highly competitive pricing. And I guess, is this from scenarios you went through more recently with companies that are out there? Or is -- just trying to see what is -- whether there's been activity in the space. Is this something that's occurred over the last...

Thomas Peterffy

So yes. Since we have looked at two opportunities, and when we tried to model what the thing would look like if we tried to incorporate those customers into ours, they were not as profitable to be able to justify the price the seller was asking, even though based on their pricing, they are reasonable.

Rich Repetto

And would this be more sizable acquisitions for you, or small?

Thomas Peterffy

We're not talking about that, but - good try.

Rich Repetto

One last question is, the margin loan balances, Thomas, would you expect them to continue to grow? They were down a little bit quarter-over-quarter, but still outpacing everyone else year-over-year. Would you expect that growth rate -- anything more to what might have occurred this quarter? Would you expect the margin loan balance to rebound?

Thomas Peterffy

We think that if margin loans in the industry hold steady, ours will grow because we are charging so much less - about 1/3 of what other people charge. And if the industry grows, then our margin loan balances will grow even faster. So unless margin -- unless the market crashes and the people who trade on margin substantially shrink their margins, ours will grow.

Paul Brody

I think I'll just add a little color to that, if I could. So you -- when you look at the period-end balances, sequentially they were down a little bit. The average debit balances for the quarter actually increased, and that's what we earn are based on. It increased about 4%, but you don't see that because the average is not there. And then the other relevant thing is we talked about opportunistic larger clients who put on yield-based positions. And with the yield curve flattening and so forth, those opportunities fluctuate. And so by the end of the second quarter, they were simply lower than they were at the end of the first quarter. Without that reduction, our base margin debits actually increased a few percent.

Operator

And the next question will come from the line of Doug Mewhirter with SunTrust.

Doug Mewhirter

I just have one question. I heard you talk in the opening remarks about hiring in India. I know that in the past, on past calls, you had said that India had not been growing as fast as other Asian countries like China or Hong Kong or Singapore, and so have you made sort of a breakthrough in India? Do you expect growth would improve there?

Thomas Peterffy

So our hiring in India has nothing to do with the location of the growth in the business. We hire in India because we get relatively well-trained, well-educated people at a relatively low cost.

Doug Mewhirter

Okay. I see. So it's more of a -- the technology customer service than direct brokerage in India. I

get it.

Thomas Peterffy

That's right.

Operator

The next question will come from the line of Chris Allen with Compass Point.

Chris Allen

In the prepared remarks that Nancy read, she mentioned opportunities to accelerate growth. I wonder if you could just give any incremental details around that, if there's any specific opportunities you're pointing to. Or is this more just continuing the same story, blocking and tackling from here.

Thomas Peterffy

It's generally the same going forward that we have been doing until now.

Chris Allen

Okay. And then at the Sandler conference, Thomas, you had mentioned that you saw the potential for competition in China, specifically a year or two from now. Your comments around the -- around trade, the impact there, are positive. Just what -- like when you're thinking about the competition, is it larger U.S. competitors that are moving overseas or is it domestic competitors? Any color on that?

Thomas Peterffy

No, I was mostly talking about domestic competitors. So there are more and more firms -- more and more new firms that are getting into the electronic brokerage business in relatively complex ways because the number of brokers that are authorized by the mainland Chinese authorities are fixed, at something like 290-something. I don't know the exact number. But it is -- so these companies are trying to basically compete without a brokerage license, just like we do not have

ourselves. We do not have a brokerage license in mainland China, so we are not there. But to the extent we get customers from there, that's what's happening.

Operator

And the next question comes from line of Chris Harris with Wells Fargo.

Chris Harris

Yes, with respect to your introducing brokerage relationships, when you guys onboard a new broker to your platform, is there a specific screening process that's involved?

Thomas Peterffy

Of course, there is a screening process for all customers.

Chris Harris

Yes, can you talk a little bit about...

Thomas Peterffy

I mean, introducing brokers have to be registered and licensed in a credible locality as a broker.

Chris Harris

Okay. And so...

Thomas Peterffy

You have to be a licensed credible broker in order to come onto our platform as an introducing broker.

Chris Harris

Got it. No, I totally understand. And we don't have to get into exact numbers. I'm just wondering qualitatively, when you think about the growth you've had in this channel, what percentage of those relationships do you think are coming from brokers that were formed, I don't know, within the last, like, 5 or 10 years?

Thomas Peterffy

So I really -- I...

Chris Harris

Is it a high number, you think? Or...

Thomas Peterffy

I really don't know.

Operator

(Operator Instructions) And the next question will come from the line of Kyle Voigt with KBW.

Kyle Voigt

Just a couple for Paul. Just one on the customer credit balances and the yield paid there. It looks like the yield increased from 42 bps to 53 bps, so roughly 11 basis point difference sequentially. I think the average Fed fund rate increased 25 bps sequentially, and I know you're above that 50 bps hurdle. I'm just wondering, is that a good ratio to use as assumption going forward if we're modeling in Fed increases? I guess I'm trying to get to -- like, do you have a percentage of the credit balances that are held in U.S. dollar? And then I know that some of the balances are obviously not being paid rates and we can kind of back into that, but I just wanted to make sure that, that kind of ratio, that 11 bps for every 25 bps increase, is that a good ratio to use?

Thomas Peterffy

That -- it will slowly diminish.

Paul Brody

Right. You've identified the right components, Kyle, as far as the non-U.S. dollar and balances in interest tiers that don't earn interest.

Kyle Voigt

Do you have an approximate breakdown of the percentage of the credit balances that are held in U.S. dollar?

Paul Brody

We do, but we haven't published that information specifically. But you can sort of -- you can backtrack it from seeing -- I mean, there's a number of factors, but those are the major factors. The portion that won't follow along with the Fed funds increases because they're either in foreign currency or they're not earning interest to begin with.

Kyle Voigt

Okay. And I guess just one on the low tax rate in the quarter. I guess, should we just look at 1Q as kind of a more normalized tax rate, is that fair?

Paul Brody

That's probably fair, yes. The second quarter generally, each year, will have a tax deduction when our Stock Incentive Plan shares vest, as it has in the past, but it is a function, obviously, of what the current stock price is because the more relative difference between the current price and the historical price at which those shares are granted, then the bigger the tax deduction.

Kyle Voigt

Okay. And then probably the last one for me is actually just on the Market Maker profitability in revenue. I think it's the second quarter with similar revenue and profit dynamics. Is this a good run rate for that business? Or is there remaining, kind of, further pullback that's yet to come?

Thomas Peterffy

That probably -- it will probably -- it certainly will not become higher. It's more likely to become lower. In other words, there are certain localities where we still carry on doing this, but it's not -- so we'll keep constantly looking at those and be done.

Kyle Voigt

Okay. And then one more, I guess, on -- just on the hiring comments and the headcount growth.

Can you just talk about specifically what specific function you're trying to improve? Is it mostly customer service for the financial adviser community? Is that a lot of the headcount that you're adding is to support growth in that area? Or is there some other segment that you're...

Thomas Peterffy

Well, we're hiring -- we're trying to hire in 3 areas: customer service, compliance and technology development.

Kyle Voigt

And is the technology hiring picking back up now? I remember you had said that as you migrated some of the technology folks from the market maker to the broker, headcount would maybe flatline for a few quarters, but is that starting to pick back up again now?

Thomas Peterffy

Yes, it's back up again, and our dreams are greater than our abilities to get them done.

Operator

And the next question will come from the line of Reinhart Schmitz.

Reinhart Schmitz

My name is Reinhart Schmitz. I'm German, located in Luxembourg. We met two years ago at the annual shareholder meeting. So I bring in a more European point of view. First of all, let me say, I love the ads, what you are currently running. I think this is high-impact advertisement, and I would like to actually see that in Europe if plans show that people can get 1.42% on cash in Europe. I mean, they get nothing or negative.

Thomas Peterffy

What currency are you talking about?

Reinhart Schmitz

Yes, okay. I know it. I know that it is dollars, but Euro is not so strong. People might think about

it.

Thomas Peterffy

Yes, but you can -- if you deposited dollars or you convert your Euros to dollar, yes, you can get 1.41%. But on Euros, we cannot give that to you.

Reinhart Schmitz

I know that, but I think people should know in Europe that this is existing. I would think it would make a high-impact, I guess. So I do my best to bring people to IB and to the platform, and they are astonished to see what is possible, Europeans, I mean. So that is the one thing. The other thing is what I actually have a problem with, is one month ago, we got a new regulation, this PRIIP. And this -- although I trade broad-based market ETFs for more than 10 years, now I cannot do that because I'm European, and the European authorities want to protect me.

Thomas Peterffy

That's right.

Reinhart Schmitz

Thanks. Thanks to the Europeans. The funny thing is, it is my understanding, please, you can give me some explanation maybe, it depends on this KID, this KID document, yes? And...

Thomas Peterffy

That's correct. As long as you're not an institutional investor. So if you have more money and put it into the account that is with us, maybe you rise to the level of an institutional investor and you can take whatever you want.

Reinhart Schmitz

Yes, I opened a ticket and I got papers and I signed them and I fulfilled all 3 criteria and so on, but still I cannot do that, what I did 10 years ago, for more than 10 years. And the funny thing is, my local bank, which is a bank, let me say, a size of 20 billion, they let me trade SPY ETFs. I mean, I will not do that because the commission is too high, yes? I cannot trade with such a bank,

but it is possible. They have these papers. And the question is, is there a difficulty that IB have not these papers?

Thomas Peterffy

Well, you see, we all pick and choose what laws we abide by. We are more stringent than most other folks, apparently more stringent than your local bank.

Reinhart Schmitz

Well, are you -- I do not understand the answer correctly because of the line. Are you in process to get these papers available?

Thomas Peterffy

No, there is nothing we can do about this situation. Sorry. It's your laws, and we have to abide by them.

Reinhart Schmitz

Yes, I understand fully that it is -- the ball is not in your -- on your side in this issue. The -- can you say about something that -- it happened very surprisingly 4 weeks ago.

Thomas Peterffy

Yes, I'm very sorry about this. So maybe you can send me an e-mail, but I don't want to hold everybody up -- else up with this issue. Please send me an e-mail, okay?

Operator

Thank you. And I'm showing no further questions at this time. I would now like to turn the call back over to Ms. Nancy Stuebe for any further remarks.

Nancy Stuebe

Thank you, everyone, for participating today. As a reminder, this call will be available for replay on our website, and we will be also posting a clean version of our transcript on the site tomorrow. Thank you again, and we will talk to you next quarter-end.

Thomas Peterffy

Thank you.

Operator

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