

FLOW ■ TRADERS

Flow Traders Q3 2024 Results

Thursday, 31st October 2024

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Operator: Hello, and welcome to the Flow Traders Q3 2024 Results Conference Call. My name is Jess, and I'll be your coordinator for today's event. Please note this call is being recorded. And for the duration of the call, your lines will be on listen-only. However, there will be the opportunity to ask questions. This can be done by pressing star one on your telephone keypad to register your question at any time. If at any point you require assistance, please press star zero and you'll be connected to an operator.

I will now hand over to your host, Eric Pan, to begin today's call. Thank you.

Eric Pan: Thank you, Jess. Good morning, and thank you for joining Flow Traders' third quarter trading update call. As you will have no doubt already seen, we released our results first thing this morning. I am joined here on the call by Flow Traders' CEO, Mike Kuehnel, as well as Global Co-Head of Trading, Coen van Sevenhoven, who will run through this results presentation. Afterwards, we will be happy to take any questions you have.

Before we begin, let me draw your attention to the disclaimer on page two. Please be advised that if you continue to listen to this presentation, you are bound by this disclaimer. Also, please note that the results we will discuss in this presentation are unaudited.

With the formalities out of the way, I would now like to hand over to Mike for his opening remarks.

Mike Kuehnel: Thank you so much, Eric, and good morning to everyone.

The third quarter of 2024 as a whole saw increased activity in the market trading environment, while volatility levels in the quarter were also elevated. Flow Traders ETP value traded tracked relatively in line with the market as it increased by 9% in the quarter compared to the same period last year and by 5% when compared to the last quarter.

Total value traded increased by 17% year-on-year and 5% quarter-on-quarter. Flow Traders value traded across each of our three asset classes in the quarter saw corresponding movements that were largely in line with the market, with crypto seeing the largest increase year-on-year but decreased when compared to last quarter.

Fixed income value traded saw a decline compared to a year ago as we allocated our limited trading capital towards other asset classes with better opportunities.

Total income came in at €114.6 million for the third quarter, a 69% increase compared to the same period a year ago. Net trading income came in at €107.3 million, plus other income of €7.2 million. As a reminder, the other income line reflects the unrealised gains and losses of our strategic investment portfolio.

With the return of volatility in the quarter, we were able to generate €15.5 million in EBITDA, a fourfold increase compared to the third quarter of last year. Net profit for the period amounted to €37.5 million with a basic EPS of €0.87, a nearly sixfold increase compared to the same period last year. We also completed our €15 million share buyback programme in the quarter.

The strong results this quarter set as a further validation of our growth and diversification strategy and the trading capital expansion plan that was announced last quarter, which helped increase our capacity to capture the opportunities that arose in the quarter.

I will now hand it over to Coen, our Global Co-Head of Trading, to review recent ETP market dynamics on the next slide.

Coen van Sevenhoven: Thanks, Mike, and good morning, everyone.

As shown at the top left-hand side of this slide, ETP market value traded increased by 16% in the third quarter compared to the same period a year ago, and by 7% compared to the second quarter. Implied volatility in the quarter, as represented by the VIX, increased by 13% when compared to the same period a year ago and by 20% compared to the second quarter.

Total ETP assets under management increased by 8% in the quarter to over €13 trillion, given the strength of the overall market and record fund inflows into ETPs. ETP velocity was relatively flat in the quarter compared to both last quarter and remained below the levels seen last year.

In summary, market activity increased in the period when compared to the same period last year as well as last quarter, while the secular industry trend across the ETP universe continues to be strong.

I will now move into the dynamics within the fixed income and crypto markets.

As shown on the top left of the slide, trading volumes in the investment grade and high-yield bond markets increased when compared to the same period a year ago, while investment grade increased compared to the second quarter.

Volatility increased slightly compared to the second quarter but remains below the level seen last year. Trading volumes in digital assets saw a slight increase in the third quarter compared to last quarter and remained significantly higher than the same period a year ago. Volatility was down slightly in the quarter compared to last quarter but remains higher than the same period a year ago.

Global crypto ETP market value traded remained elevated when compared to the same period a year ago, but declined by about 20% quarter-over-quarter, given the slowing of fund flows into the US spot Bitcoin ETFs in the quarter.

On slide six, we present an overview of some of the key performance indicators for the third quarter on a regional basis. As Mike mentioned earlier, market ETP value traded improved in the third quarter when compared to the same period a year ago as well as last quarter, despite the third quarter being the slowest quarter of the year traditionally.

In Europe, we maintained our position as a leading liquidity provider in ETPs amidst increased market activity and heightened levels of volatility in the quarter. Our robust and comprehensive trading capabilities put us in the position to capture opportunities that arose in European and Asian markets from the substantial asset rotation in early August. Given the greater levels of price dislocations that we saw in equity in Europe and Asia and the limited trading capital base, we shifted capital to these regions and asset classes to capture those opportunities.

We continue to assist our trading partners in the digital asset space in the quarter and participated in the spot Ethereum ETF launches as a lead market maker, reflecting the long-term commitment to support the continued evolution of crypto and digital assets.

The continued improvement in regulatory sentiment and increased institutional adoption of digital assets around the world affirms our long-term investment strategy in the asset class.

And last but not least, we continue to see increased contribution from our China operations in the second year following the receipt of our QFII license.

I will now hand it back to Mike for the next slide.

Mike Kuehnel: Thank you, Coen. After a few years of rapid expansion, we continue to focus on operational efficiencies while implementing our growth strategy at the same time. And as this slide shows, fixed operating expenses in the quarter and year-to-date declined slightly, while our NTI increased by 59% or 38%, respectively, year-over-year.

We achieved strong margins in the quarter as an upturn in NTI delivered a 44% EBITDA margin compared to 18% in the same period a year ago. We ended the quarter with 646 FTEs, the same as of the end of the fourth quarter 2023. We expect headcount to remain roughly flat for the remainder of the year, given expected efficiency gains while we continue to bring on board additional talent in growth areas.

Our guidance on fixed operating expenses remains unchanged as the firm remains fully focused on operating and cost efficiencies across the business while implementing our growth and diversification strategies.

On slide eight, we take a look at the historical NTI growth of the company since the IPO. As you can see in the chart on the left, the company has delivered structural NTI growth over the last few years with higher highs and higher lows given the investments we have made in our trading capabilities across different regions and asset classes.

Our growth and diversification strategy has enabled the company to capture opportunities wherever they arose. This positions the company to deliver solid and consistent results during periods of muted market activity, while periods of high volatility provide strong upside.

On the chart on the right, you can see the strong and healthy through-the-cycle average EBITDA margins of over 40% over the years given the highly cash generative nature of our business, of which our flexible compensation philosophy plays a large role. Given our fixed versus variable compensation structure and the firm-wide bonus pool, employee compensation tracks in line with the profitability of the company and aligns the interest of employees with that of our shareholders.

Moving to the next slide. Trading capital is the lifeblood of any trading firm, as highlighted before. And bolstering our trading capital is a strategic priority for the Board. Given the strong 75% average historical return on trading capital, the Board took the decision last quarter to accelerate the expansion of our trading capital base with the suspension of the dividend and the pursuit of external debt.

As a result of this major decision, we were able to boost our trading capital by 7% in the quarter to €668 million at the end of the third quarter, the second highest level in the company's history. Shareholders' equity also increased significantly to €666 million at the end of the quarter, the highest level in the company's history. It's worth noting that shareholders' equity will now track closer to our trading capital, given the retention of 100% of company's net profits for reinvestment in the business.

The strong third quarter results serves as validation of the firm's trading capital expansion plan and the continued expansion of our diversified set of existing and newly emerging trading strategies. We continue to believe that with the additional capital, we can deliver significant

returns and further strengthen our company's role as a leading global trading firm, providing liquidity and efficiency across a wide range of financial markets.

Moving to the next slide, I will discuss market trends and our strategy.

On slide 10, you can see that the supportive megatrends, which underline the firm's strategic goals and strategy remain very much intact. These four key megatrends continue to shape our market environment, acting as tailwinds to our business and offer increased opportunities. Crucially, these trends all feed into and reinforce each other. Particularly relevant to our core business is the ever increasing acceptance of ETPs and growth in passive investing.

Total industry's ETP AUM is expected to increase from today's US\$14 trillion to US\$25 trillion by 2030 and underscores the strength and importance of the ecosystem we are a key part of. Electronification of trading is critical for all of our activities, but in particular, it is within the fixed income asset class where this is a key structural trend in corporate credit and emerging market sovereign bonds.

Increasing adoption of electronic trading ties into our core technology-enabled competency set. As highlighted in the fixed income white paper we published last year, credit algos, for instance, have comprised almost 50% of executed volumes in Euro credit in the last two to three years, particularly in the sub-1 million ticket sizes.

Fixed income ETF AUM is projected to triple from US\$2 trillion to US\$6 trillion by 2030. With the recent regulatory developments regarding digital assets, there is growing institutional interest in this asset class, and total assets invested in cryptocurrencies more than doubled from the second quarter of 2023 to more than US\$2 trillion today. With the regulatory approval of the spot Bitcoin and Ethereum ETFs in the US to the first exchange listed options on crypto ETFs, we do anticipate growing investor demand for digital assets.

The asset class remains a long-term growth opportunity with the underlying technology expected to drive significant transformation across global financial markets in the coming years.

Lastly, regulation continues to support our business in terms of creating a level playing field from the aspect of execution transparency. We continue to work with the regulators around the world to drive the increase of transparency and improve liquidity across all markets and asset classes.

Now moving to the last slide. On this slide, I outline the firm's four key strategic pillars to grow, strengthen and accelerate the business. The first is to optimise our core and grow capital. This means building an increasingly resilient and efficient business model through dedicated optimisation of the firm's trading core, while simultaneously growing the firm's capital base to accelerate the monetisation of all existing and new trading strategies across asset classes and regions.

The second is to expand and enhance our trading capabilities. We will leverage our proprietary infrastructure, capabilities and expertise to expand into adjacent products and enhance existing trading strategies.

Third is technology and innovation. We will further adopt emerging technologies and increase the utilisation of data insights within trading to improve our own pricing competency as well as internal hedge and execution efficiencies.

And last but not least, diversify our business model and revenue streams. We will continue to invest in adjacent business propositions as well as in connectivity, platforms, data and tokens via dedicated partnerships to accelerate innovation across financial markets and to diversify existing revenue streams.

I will now hand back the call to Eric.

Eric Pan: Thanks, Mike. This concludes the formal part of our presentation. We would now like to open up the floor for any questions you may have. Operator?

Questions and Answers

Operator: If you would like to ask a question, please press star one on your telephone keypads. Please ensure your line is unmuted locally as you will be advised when to ask your question. So once again, that's star one if you would like to ask a question. Our first question comes from the line of Julian Dobrovolschi from ABN AMRO-ODD BHF. Please go ahead.

Julian Dobrovolschi (ABN AMRO-ODDO-BHF): Good morning, gentlemen, and thanks for taking my questions. I think it was a good print. So congrats on that. I have a couple of questions. Maybe to start with the first one. Hello, good morning, do you hear me?

Mike Kuehnel: Yes, we hear you.

Julian Dobrovolschi: Hello.

Mike Kuehnel: We hear you. Can you hear us?

Julian Dobrovolschi: Can you hear me?

Mike Kuehnel: Yes, we can hear you.

Eric Pan: Yeah, loud and clear.

Julian Dobrovolschi: Yes, likewise. Okay, sorry for that. Yeah. Again, good morning. Thanks for taking my questions. I have three. I think there is a big delay, so I hope I can still shoot my questions.

Mike Kuehnel: Yes, fine. Go ahead.

Julian Dobrovolschi: All right. I have three. Then to start with the first one. Is it possible for you to unpack a bit more about the other income line. So that's €7.2 million in the third quarter. I think this is the highest one that we've ever seen so far since you launched the corporate ventures versus VC unit. So can you kind of talk a bit about that? And what kind of expectations should we have going forward on this line on the P&L?

The other one is on the ETP volumes. So if you look at the growth in Flow value trade ETPs, that's about 9% year-over-year, but the market grew at 16%. And even if you kind of try to isolate region by region, it still kind of grew across all the regions below the market expectations on the ETP side. So I was wondering how should we read that. Is it a bit of a kind of, let's say, indication that now you're trying to be less keen on trading ETPs overall and structurally move into other asset classes or let's say, products? Or is this just kind of a bit of a result of you chasing higher yielding trades, which clearly were not in the ETP space in the third quarter?

And then the third question is on the APAC trading performance. I was wondering if you can quantify how much of an uplift did you get from, let's say, the aftermath of the yen credit trade stuff that happened in Japan in the third quarter?

Mike Kuehnel: Thank you so much, Julian. Maybe best if I take the first question, and the second and third, Coen can jump in.

So on the first question, a large part of the other income in Q3 was related to a one-time lift with certain investments due to a change in the valuation methodology we applied, more commonly used in the market. So in a way, it was a technical adjustment in line with market standards. And maybe the second point to highlight in this piece, and this relates more than to the expectation going forward. So we do continue to invest, and given our business footprint, also see a rising amount of opportunities.

I think two points to highlight in this context. The kind of continued strategic focus on that line is important to us as it very much benefits our core. So the investments we seek are actually very much related to market-making or liquidity provisioning opportunities, not exclusively, but that's what we see as a core.

The second point is that I think the expectation we have is that there will be mid to long-term significant, let's say, market uplift opportunities in, for instance, digital assets, where we see that more institutional adoption leads to more predictability and rising market prices of underlying assets.

So I'm not giving a specific guidance, but the addition of the investments portfolio to our core business is still a high priority. But very specifically to Q3 was related more to a technical adjustment.

Maybe handing over to Coen for question two and three.

Coen van Sevenhoven: Hi, Julian. Thanks for your questions, and I think I will answer them in a combined fashion. I think ETPs are still very much at the core of our trading activity in the core of the firm. I think it's important to note that we don't optimise our strategies for market share. We don't work with market share targets. And especially as Mike very often alluded to, we have a limited capital base.

So we need to make choices on where we can allocate our capital and what opportunities we can pursue, which I think is also a testament to the fact that we believe we can deploy more capital if we're able to grow our capital further.

So yes, as we don't optimise for market share. But to your point, for the opportunities that are presented, yes, you will see shifts in market share across areas over time. And we will not be able to always pursue all the opportunities we see, but we will focus on the highest yielding ones as you implied.

Mike Kuehnel: Just checking, Julian. Yeah. Just wanted to check whether the audio was okay. Did that answer your questions, Julian? Might have an issue with the audio line on his side.

Julian Dobrovolschi: Yeah, clear. I mean I have another one, the last one is on the uplift to NTI and from the – I'll go on mute. Okay. It doesn't matter.

Coen van Sevenhoven: I understand the question. So yes, it's not per se like that the opportunity was only specifically to one moment cost in Japan. It's more than the overall market

environment that we saw around that period that led to opportunities in most notably the European and Asian strategies that we deploy around the period of time of 5th August. So yeah, that are typically the strategies that are really close to our core and key competencies where we were able to capture the opportunities that were presented.

Eric Pan: Operator, maybe next question?

Operator: The next question comes from the line of Reg Watson from ING. Please go ahead.

Reg Watson (ING): Good morning, all. I wanted to ask about fixed income. And I noticed in the prepared release and the remarks, you mentioned that trading volumes have increased in the US, but volatility declined. I was wondering if there was anything more to it than that in terms of competitive pressure or your initiatives to grow the market there and take share? Perhaps you could give us a bit more colour, Mike, on what's going on in fixed income?

Mike Kuehnel: Yeah. Thank you so much, Reg. I think the two points I would like to play back on the fixed income side, I mean, there are different perspectives you can take on how important capital is, but I want to come back to what I said before, running a diversification strategy globally and across asset classes also then comes down to having sufficient capital to benefit from a rising opportunities.

And specifically on the fixed income side, having an adequate capital base is a key ingredient for our success. So what has happened is that as we did see more opportunities on the equity and crypto side, there's always then with the limited nature of our capital base, a trade-off call we need to make.

And with that, I want to build a bit the foundation again why an increased capital base is important for us for all asset classes, but specifically also to capture opportunities in fixed income.

Another element on fixed income, I think, in terms of competitive pressure. It's not that we are seeing new entrants in the market, but I'm quite reflective of the fact that we need to constantly improve specifically on the algo side. And as such, we have deployed more capacity and more resourcing as a global effort actually to look into the continued and even accelerated enhancement of our underlying algos.

So I think the overarching message is that we very much still believe in our value proposition across all the asset classes and fixed income being a key component of it, but I'm also quite mindful that when you look into the last decade, for instance, we have seen spikes in fixed income where markets then offered opportunity to us that we could really capture very well. So that mindset shift on our side now is really focusing on making sure that the capital base is there over time in order to make sure that we can capture these opportunities as they arise to us. So no fundamental shift in our diversification strategy on that end.

Reg Watson: Okay. No, that's good to know. It's also good to know that the agnosticism of trading capital is working well and that the business model is performing as intended. With that in mind, I have a question about the forthcoming US election. I think if memory serves me correctly, at the last election, you benefited significantly from the vola around that. What is your take on the forthcoming election? And what are you doing to prepare for it?

Mike Kuehnel: Yes. As usual, I can't comment on any kind of NTI projection. But what I will say is that the company has meaningfully advanced in preparing ourselves for upcoming events

in the market and the US election next week is probably one of the more prominent examples for it. I think that comes in two shapes. One is global alignment in terms of strategies and resourcing. The second is capital allocation.

So we did prepare scenarios in order to really be able to act fast depending on how we will see the world turning next week. And I will say that given the fact that we performed well in this quarter, where we did see the volatility spike early August is an indication that the company is fully intact and the business value or model as such is fully intact to capture these opportunities. So I would expect that we can deploy the same approach and our capabilities than in any kind of bolus spike that might come or might not come. We'll see what happens, but I think we are well prepared for it.

Reg Watson: Okay, that's great. Thanks for Mike, and good luck.

Mike Kuehnel: Thank you.

Operator We currently have no questions in the queue. So as a reminder, please press star one if you would like to ask a question. We have no further questions in the queue. So I will turn the call back over to your hosts for any closing remarks.

Eric Pan: Thank you, operator. We would like to thank all the analysts for participating in today's call. Please note that we will host our next analyst call when we release our fourth quarter and full year 2024 results in February of next year. Details and timing for this call will follow in due course. This now ends the call. Thanks again, and have a great day.

Operator: Thank you for joining today's call. You may now disconnect your lines.

[END OF TRANSCRIPT]