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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. (Operator Instructions) As a reminder, this conference is being recorded, October 25, 2017.

I would now like to turn the call over to Dave Cresci, Investor Relations Manager at MarketAxess. Please go ahead, sir.

David Cresci

Good morning, and welcome to the MarketAxess Third Quarter 2017 Conference Call. For the call, Rick McVey, Chairman and Chief Executive Officer, will review the highlights for the quarter and will provide an update on trends in our businesses; and then Tony DeLise, Chief Financial Officer, will review the financial results.

Before I turn the call over to Rick, let me remind you that today's call may include forward-looking statements. These statements represent the company's beliefs regarding future events that, by their nature, are uncertain. The company's actual results and financial conditions may differ materially from what is indicated in those forward-looking statements.

For a discussion of some of the risks and factors that could affect the company's future results, please see the description of risk factors in our Annual Report on Form 10-K for the year ended December 31, 2016. I would also direct you to read the forward-looking statements disclaimer in our quarterly earnings release, which was issued earlier this morning and is now available on our website.

Now let me turn the call over to Rick.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Good morning, and thank you for joining us for the third quarter earnings call. Our earnings report this morning reflects a solid quarter in a trading environment that remains challenging. Third quarter trading volumes of $347 billion were up 8% year-over-year. International client volume increased by 24% to $89 billion. And our emerging market product area experienced continued momentum with a 22% increase in trading volume.

Open Trading set a new record this quarter in client participation. Revenues for the third quarter were up 7% to $97 million. Expenses of $49.5 million were up 13% due to ongoing investments in our business and expenses related to global regulatory changes. Diluted EPS of $0.90 was up 10%. Third quarter U.S. high-grade estimated market share of TRACE increased to 17.2% from 16%.

Slide 4 provides an update on market conditions. In the third quarter, credit spreads continued to trend lower, and spread volatility remained at historically low levels. U.S. credit inflows continued to be very strong due to global investor demand for yield. Like other credit market participants, very low market volatility, coupled with investors chasing scarce funds, creates a difficult trading environment for our business. In light of these market conditions, we believe our business performed well during the quarter. Overall, TRACE high-grade market volumes in Q3 were relatively flat year-on-year while high-yield TRACE volumes were down 7%. The lack of volatility in high-yield has led to fewer trading opportunities for alternative market makers and ETF relative value players, both important client segments for our high-yield trading business. New issue activity remains strong as issuers respond to strong demand at historically low corporate bond yields. The combination of low market volatility and high new issuance increases investor focus on the new issue calendar.

Slide 5 provides an update on Open Trading. Open Trading volumes were $56 billion in the third quarter, with average daily volume up 29% from the same period last year. Approximately 155,000 Open Trading transactions were completed in the third quarter, up 45% from 106,000 in Q3 2016. Liquidity providers or price makers on the platform drove a 51% increase in price responses in the third quarter. Liquidity takers saved an estimated $21 million in transaction cost through Open Trading on the system. Participants benefited from average transaction cost savings of approximately 2.1 basis points in yield when they completed a U.S. high-grade transaction through Open Trading protocols. When compared to our Composite Price, real time mid-market estimate for corporate bonds, we believe that liquidity providers are achieving similar savings in transaction costs.

Dealer-initiated open trades reached a new high of 24% of all Open Trading volume in the quarter. Open Trading is increasingly becoming an important distribution channel for dealers in their efforts to increase trading velocity and reduce balance sheet usage. Our vast network of investors and dealers operating in Open Trading provides an additive pool of liquidity for dealers to move bonds. In the third quarter, Open Trading accounted for 37% of U.S. high-yield volume, 15% of U.S. high-grade volume and 13% of emerging market volume.

Slide 6 provides an update on our international progress. International client volumes were up 24% year-over-year, driven by a 26% increase in the number of active clients to over 600 firms. All 4 of our core products continued to show solid growth in active trading clients. Emerging markets activity was especially strong during the quarter. Overall EM volume with international clients was up 38%, and local market volumes were up 22%. We had approximately 900 firms globally trading EM during the quarter. We are encouraged by the momentum we see in EM in spite of the benign market conditions.

Our preparations for MiFID II are on schedule, and we have reached multiple milestones to support our clients in meeting their regulatory obligations. MarketAxess subsidiary, Trax, has been granted approval by the U.K. FCA to operate as an APA for trade publishing and as an arm for transaction reporting. MarketAxess was also recently approved by the Monetary Authority of Singapore to operate as an RMO. This not only demonstrates our continued investment in the region, but also addresses client demand by providing a new trading platform with a regulatory structure that meets the needs of our clients in Asia prior to MiFID II implementation. We expect the MiFID II reporting, transparency and best execution obligations to drive greater demand for electronic trading and market data solutions. We have made significant investments in all 3 areas to help our clients with the upcoming regulatory changes.

Now let me turn the call over to Tony for more details on our financial results.

Antonio L. DeLise - *MarketAxess Holdings Inc. - CFO*

Thank you, Rick. Please turn to Slide 7 for a summary of our trading volume across product categories.

Our global volume increased 8% in spite of the continued lackluster market environment. Global trading volumes surpassed $1 trillion on a year-to-date basis, up $132 billion year-over-year. U.S. high-grade volumes were $201 billion for the quarter, up 13% year-over-year, primarily due to an increase in estimated market share. Volumes in the other credit category were up 9%, while estimated aggregate market volumes for emerging markets, high-yield and eurobonds was down 5% year-over-year.

There's been a fairly consistent pattern over the past 3 quarters with strong growth in emerging markets trading on our platform and lower-than-average growth in high-yield and eurobonds. For the first time, municipal bonds traded on the platform exceeded $1 billion in the quarter, and over 50% of the trading volume was through Open Trading.

Recent news kept light on micro-lot trading in U.S. high-grade bonds. Our trading volume and market share in micro-lots has grown significantly over the past 5 years. Our estimated market share of trading volume under 250,000 in trade size was 23% compared to the aggregate of all retail ATS trading platforms of 21%. With 5 important trading days remaining in the month, high-grade and high-yield market share are tracking below third quarter levels, while overall average daily volume is tracking similar to the third quarter.

On Slide 8, we provide a summary of our quarterly earnings performance. Quarterly commission revenue and overall revenue were up 6% and 7%, respectively, and are fairly consistent with the overall growth in trading volume. Information of post-trade services revenue increased by 14%, driven by higher data revenue. Operating expenses were up 13% year-over-year, leading to a 2% increase in income before taxes. The effective tax rate was 28% in the third quarter and reflects excess tax deductions of approximately $3.8 million relating to the new standard for share-based compensation accounting adopted effective January 1, 2017. The full year effective tax rate is trending towards the lower end of our 26% to 28% guidance range. The discussions around tax reform has heated up now that the Senate has passed the budget bill. While it's too early to speculate on the outcome, at 2017 earnings level and business mix, we estimate that a 10 percentage point reduction in the U.S. Federal corporate income tax rate would increase EPS by approximately $0.40 and drop the effective tax rate by 7 percentage points. Our diluted EPS was $0.90 for the quarter on a stable diluted share count of 38 million shares.

On Slide 9, we have laid out our commission revenue, trading volumes and fees per million. Total variable transaction fees were up 2% year-over-year as the 8% increase in trading volume was offset by a mix shift and the impact of our new high-yield fee plan. U.S. high-grade fee capture was up $7 per million on a sequential basis, mainly due to a roughly half-year increase in years to maturity on bonds traded over the platform.

The percentage of volume in our tier-sized buckets didn't vary much from the second quarter. Our other credit category fee capture was down $22 on a sequential basis. In addition to the typical swings in fee capture resulting from fee mixes on products and protocols, the third quarter other credit fee per million also reflects the impacts from the new high-yield fee structure implemented effective August 1.

At this time, we have 10 dealers participating in the distribution fee plan, which amounts to $1.5 million in monthly distribution fees and a variable transaction fee per million for all of high-yield bond trading post implementation has been roughly $350. We expect fourth quarter distribution fees will be approximately $1.5 million higher than the third quarter.

Slide 10 provides you with the expense detail. Sequentially, expenses increased by 4% as higher professional and consulting fees, mainly associated with various regulatory-related initiatives and Brexit, along with nonrecurring lease costs, were offset by a decrease in marketing and advertising expenses. September year-to-date expenses were up 8% and full year 2017 expenses are expected to land in the lower half of our original guidance range of $192 million to $208 million. Overall, headcount is tracking close to our original plan and is up 44 from year-end 2016 level. The majority of the expense variance versus the midpoint of our guidance range results from lower-than-anticipated variable incentive compensation.

On Slide 11, we provide balance sheet information. Cash and investments as of September 30 were $376 million, and trailing 12-months free cash flow was approximately $147 million. During the quarter, we paid a quarterly cash dividend of $12 million and repurchased 64,000 shares also at a cost of $12 million. In September, the existing share repurchase program was terminated, and our board approved a new $100 million program. Repurchases under the new program began on October 2.

Consistent with the expired plan, the primary intention of the new repurchase program is to offset dilution from employee equity grants. Based on the third quarter results, our board has approved a $0.33 regular quarterly dividend.

Now let me turn the call back to Rick for some closing comments.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Thank you, Tony. In spite of extremely difficult trading conditions, we are pleased with the growth we are seeing in many aspects of our business. We are investing more than ever in technology solutions for our clients to meet their regulatory and trading needs. The future opportunity in electronic tradings for credit markets remains large, and our competitive position has never been stronger.

Now I would be happy to open the line for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from the line of Patrick O'Shaughnessy from Raymond James.

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

So with yesterday's news of BondPoint selling to ICE for $400 million, how do we evaluate the potential competitive threat that ICE would pose at some point in the future? And do you see it as any different from when Tradeweb acquired BondDesk in 2013?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Yes, thanks, Patrick. To date, the retail segment has largely remained separate and apart from the institutional business that we operate. And we don't really see any changes to that dynamic. And Tradeweb's acquisition of BondDesk 4 or 5 years ago was an example of where that business, to this day, remains largely a retail business without much intersection into the institutional business. We have great respect for Jeff and his team at ICE and what they've been able to accomplish, and we are sure that they've been thoughtful about the acquisition. I think our calculation and thought process, for a variety of reasons, was a little bit different. And as Tony pointed out, we're very active in that segment of the market already. Our share has been growing very rapidly in $250,000 and under trade sizes. And when we look at it today, our share of those trade sizes is greater than all of the retail ATS systems in the aggregate. And what probably is less well known is that all of the retail market participants are now active on the MarketAxess system. The retail liquidity providers have been here for a long time, given the micro-lot institutional trading opportunities that we create for them. And increasingly, the retail brokerage firms and wealth advisers are finding us. And so a component of that business that's been growing in [$250,000] and under is coming from retail market participants. And in our view, we continue to believe that there are 3 key things to driving a successful marketplace: the liquidity providers and a vast network of available liquidity, order flow from liquidity takers and technology. And we feel very comfortable with our assets in that space. And the one change that we would need to make to have a more focused effort on retail is really on providing responses through streaming prices as opposed to RFQ today. But we're very comfortable with where we sit in that part of the market. And the beauty of our platform is that there are no boundaries. And we do see an increasing presence with retail clients on the MarketAxess system.

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

All right. That's very helpful. And then as a follow-up to that, if we were to see more competition in the institutional space, what would I guess concern you more? Would it be if somebody entered with an aggressive pricing strategy, if somebody had new trading protocols? Is there anything out there that somebody could do that you'd say, "Hey, this would really kind of concern us and would look different from everything we see in the past"?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

I think we've seen a lot, Patrick. As you know, you've been following us for many years. But we've seen various competitors come with new pricing schedules, including 0 pricing in some cases. We've seen them come with new protocols and new approaches. But what has proven to be the case through time is that our 17 years of very heavy investment in building our technology platform with a variety of trading protocols that are relevant to institutional investors and building the broadest network of liquidity providers and clients on our system has made it difficult for new entrants to come into the space. And there is no sign of that changing. I think all the competitive data that we picked up again during the third quarter demonstrates that we continue to be the strongest e-trading platform in credit markets and that our growth rates are extending that lead. And I think what would worry us is if we were not investing, if we were standing still and hoping to maintain our share based on what we've done in the past, I think that would be an enormous mistake. The reality is we think we're investing more than anyone in this space by a wide margin. So we continue to add client segments, we continue to add new products to our trade system, we continue to add new trading protocols. And importantly, we're investing very heavily in data tools for our clients. And to me, that investment is what gives me confidence that we can continue to extend our competitive lead.

Operator

And our next question comes from the line of Conor Fitzgerald from Goldman Sachs.

Conor Burke Fitzgerald - *Goldman Sachs Group Inc., Research Division - VP*

I just wanted to circle up on BondPoint again. I guess I appreciate your comments or your thought process on the deal was a little different. Maybe just a 2 parter on that. Can you talk about some of the metrics that you look at when you consider M&A more broadly? And then for this deal, specifically, did you discuss the scenario where it made sense to kind of go beyond some of those metrics, given it could have been an opportunity to keep the competitor at bay?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Well, sure, happy to answer both of those. I think as you would expect, we're very interested in acquisitions that are going to add important clients to our platform or new product capabilities or new geographies. This deal really didn't do any of those. As I've mentioned, the retail clients are already on the MarketAxess system, and we have the largest share of $250,000 and under trade sizes today. So our calculation on this one was that this is a very modest add in terms of earnings accretion for our shareholders at a very full price. And we think, as we have in the past, or in this case, by investing a bit more in technology and sales more focused organically, we can achieve much better earnings accretion for our shareholders at a much lower cost. But we're playing a long game here. We think about where we want to be 5 or 10 years from now. We are wide open to acquisitions and anything that would really add technology, products or clients to our trading system that would be beneficial to our shareholders is something that we are -- we continue to be very interested in. As we've mentioned in the past, we don't restrict ourselves to trading acquisitions either. Data and analytics and post-trade services are also very, very valuable to us. So I think those are the kind of things that we think about as we look at potential acquisitions.

Conor Burke Fitzgerald - *Goldman Sachs Group Inc., Research Division - VP*

That's helpful. And then I just want to get your updated thoughts on building your own retail trading platform now that Bondpoint is off the market.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Well, sure. I mean, like I say, without a tremendous amount of focused effort, we've been gaining a lot of traction in retail. And we're happy to put together more specific numbers. But the retail liquidity providers and, increasingly, the wealth advisers and retail brokerage firms are important part of the daily trading that takes place on MarketAxess. And that is why you see our share of $250,000 and under larger than anyone else by a wide margin. What we would need to do to compete directly with the retail ATS businesses is to convert what is now an institutional protocol, which is highly competitive RFQ into a price-based protocol, which is a pretty straightforward change and add a bit more sales focus in terms of convincing retail market participants to take advantage of the pricing that's on our system. And the reason that we have the largest share in the $250,000 and under trade segment is because we have the best prices in that space. And that is why the most price-competitive clients in the world use MarketAxess for micro-lots. And I am highly confident that as we focus more on this, we have an organic opportunity to continue to expand our retail business.

Conor Burke Fitzgerald - *Goldman Sachs Group Inc., Research Division - VP*

Got it. That's helpful. And then, Tony, just one for you on the balance sheet. You've always operated with a very clean balance sheet, cash-rich. Partly, I think that's been because M&A opportunities can come off from time to time. Any thoughts on changing your leverage position now that one potential opportunity is in the rearview mirror?

Antonio L. DeLise - *MarketAxess Holdings Inc. - CFO*

Conor, really no change in the thoughts around the balance sheet. We've always had this philosophy of having a strong balance sheet. We like the operating flexibility, and it gives us the opportunity to act opportunistically if there is some activity around M&A or around share repurchases. But really, no change in the thought around what we're doing with capital returns, around the dividend. We've been targeting about a 1/3 payout of free cash flow and earnings. We've increased that dividend 400% since we launched it in [2019]. It's kept pace with the increase in earnings and have the increase in free cash flow. And on the repurchase side, it's been -- we've had a stated policy of having a repurchase plan in place. We like that repurchase plan and sort of the primary purpose right now to offset dilution from equity grants, we're going to stay the course on that. So really, no plans, but we do have -- we have the flexibility to change that. But today, it's a bit status quo on the capital policy. And so leverage up right now. I think if there was something to do in the retail space right now, we would have levered up. And it wouldn't have been an unusual amount of leverage we would have put on the balance sheet, but that would've been an event that would've made us add some leverage onto the balance sheet.

Operator

And our next question comes from the line of Chris Shutler from William Blair.

Christopher Charles Shutler - *William Blair & Company L.L.C., Research Division - Research Analyst*

Open Trading has been 15% or so of high-grade volume now for 4 consecutive quarters. Can you just talk about why you think that has slowed? And markets are very tough right now with volatility. But I guess I'm particularly interested in how the market environment impacts the ratio of Open Trading as a percentage of total high-grade volume.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Yes. We're happy with the growing participation that we see in Open Trading, but there is no doubt that the market environment has an impact on those growth rates as it does for our overall business. And I think when the tide goes out, Open Trading is going to really show its value to our clients as we move from an environment that is heavily one way with investors, looking to add bonds, especially in U.S. credit, to a 2-way market, where investors and dealers are both looking for alternative sources of liquidity. And this is far from a normal secondary market environment that we're dealing in right now. But when we see the participation numbers continue to grow for both dealers and investors in Open Trading, we think we're positioning the business very well for the future in terms of being an extremely valuable source of liquidity when the market conditions change.

Christopher Charles Shutler - *William Blair & Company L.L.C., Research Division - Research Analyst*

Okay, great. And then on the global regulatory changes that you guys talked about, so with MiFID and everything, the expenses, can you maybe quantify what you're incurring this year and whether next year could be higher or lower? And then, any sense from a revenue perspective or an opportunity perspective just how you may benefit? I know it's tough to quantify at this point, but any broad sense?

Antonio L. DeLise - *MarketAxess Holdings Inc. - CFO*

Yes. So Chris, let me give you some sense on the expense side, and then we'll have Rick comment a little bit on the revenue side. We are incurring additional expenses this year, and it's -- there's not only what you see in the professional and consulting line, but you saw in the third quarter. The majority of that uplift year-over-year professional and consulting and the majority of the uplift from the second quarter to the third quarter had to do with planning around MiFID II and Brexit and establishing new trading venues in other jurisdictions and responding to all of these rule changes. So there was additional expenses this quarter in particular. We expect some of those expense to recur. Some will be nonrecurring, but a chunk of that will recur. I said in other piece which is more technology-related, we've had to do some things to respond to the evolving regulation that has become ARM and APA registered. And it's somewhere around $4.5 million this year that we've incurred. Now this has been capitalized. Once MiFID II goes live, we will start amortizing those costs over a 3-year period. But that's another -- in addition to the items that hit the expense line and you're also seeing about $4 million, $4.5 million in capitalized cost as well. Some of that is going to recur. Some of that will -- as the landscape changes here, and we're registered in more jurisdictions, and we're meeting client needs across the globe, you will see an increase in expenses like that.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

On the revenue side, Chris, we think we're well advantaged -- well positioned, excuse me, to take advantage of the changes taking place, primarily through MiFID II. First, of course, our Trax business should benefit from the increase in regulatory reporting obligations for both dealers and investors. And given the client adoption of Trax, the reporting mechanism, we do anticipate the reporting revenues will be higher beginning in January of next year. Secondly, our data products are doing very well, and a lot of that generated from Trax data products. As clients are really required to think more specifically about best execution and transaction costs, data is a critical component of that analysis. And then, finally, on the trading side, clearly, there are advantages for investors and dealers to trade on regulated trading venues built into MiFID II. And we would continue to expect that trading activity will grow on regulated trading venues. And we think we're already seeing signs of that as our growth rates in trading volume with European clients are currently outpacing growth rates elsewhere in the world. So we really think we will benefit from all 3 sides of our business from an increase in electronic trading adoption, from growing regulatory reporting revenue and then from a bigger base of revenue coming out of our data products.

Christopher Charles Shutler - *William Blair & Company L.L.C., Research Division - Research Analyst*

Okay. And one last one on the high-grade fee rate, Tony. It looks like October quarter-to-date that the volumes are a little more tilted to larger bonds. So is high-grade fee capture trending down a little from Q3 levels so far in the quarter?

Antonio L. DeLise - *MarketAxess Holdings Inc. - CFO*

As much as I'd like to tell you, day-to-day and month-to-month, what the high-grade fee capture looks like, or even our overall fee capture looks like, we're typically not providing that level of granularity. You are right that when you look at TRACE volume for this month in October, those larger trade sizes have ticked up a little bit. Chris, I'll tell you one thing. On fee capture, one thing to be sensitive about, going forward, is if you look at that other credit category, just remember that we didn't have the full effect of the high-yield C plan reflected in the third quarter, so you will see -- all things being equal, you would expect the other credit fee capture to go down to the fourth quarter. So just be cautious of that one. On that one, you know it's a bit of a flip between distribution fees and variable transaction fees. And on the high-yield plan, it's actually, at today's volume levels. It's actually mildly accretive. So it's a bit of geography, but just be sensitive to that fee capture line in other credit.

Operator

And our next question comes from the line of Kyle Voigt from KBW.

Kyle Kenneth Voigt - *Keefe, Bruyette, & Woods, Inc., Research Division - Associate*

Just, I guess, a follow-up on MiFID II. You just outlined that it could accelerate electronification of the corporate debt market, or your belief that it's going to accelerate electronification in the market. But in the quarter, we saw MarketAxess and other trading platforms in Europe draft a letter to ESMA, stating that MiFID II could drive business away from Europe. So I'm just trying to understand if you could -- or you could help us understand this dynamic or this potential risk.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Sure. Our concern is that the regulatory reporting requirements are so onerous that any client that does not need to be captured within the MiFID II environment will choose to operate outside of it. And you see some signs of that already with client segments that are not directly in the EU. So I think that's the view that we express. I don't think it necessarily changes the amount of trading that clients will do within European fixed income or emerging markets, which are very active within the European region. But any client that can avoid the obligations that are built into MiFID II is working pretty hard right now to do so. The point of letter is the reporting obligations, in our opinion, are excessive. To have trade-by-trade reporting requirements of 75 fields is something that we have never seen. And we're working very hard at Trax to make that as easy as possible for our customers, but I think anyone would acknowledge that, that is a significant burden for institutional investors that have thousands of transactions per day in many cases.

Kyle Kenneth Voigt - *Keefe, Bruyette, & Woods, Inc., Research Division - Associate*

Okay. And then I guess one more on MiFID. Just any color on what you're seeing in terms of change in behavior at this point for MiFID II? I know you said Europe growth is outpacing the U.S. growth. But are you having discussions with some of your global asset managers about their entire business, including the U.S.? Or is this really going to be isolated to the European business, in your view, with the U.S. trying to stay out of a lot of these regulations?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Well, that's an open question, right? I think global asset managers are grappling with that right now. If they run a global portfolio and a portion of it is in Europe, do they need to adopt MiFID II standards for the entire portfolio or just for the component that's in Europe. And I think every firm is -- has a slightly different view and opinion on that. But I think it's safe to say, it is having implications beyond just Europe. And one of the -- the primary areas of focus right now is not an area we deal directly in, but it's the whole area about dealer research. So there is a ripple effect going on beyond Europe. Most of the activities that we're involved in is within Europe, as clients get ready to comply with the new reporting requirements, the new best-exit requirements and fulfill all of their obligations that are built into MiFID II.

Kyle Kenneth Voigt - *Keefe, Bruyette, & Woods, Inc., Research Division - Associate*

Okay. Just one more for me. Really, there's a recent article in the journal written regarding the increase use of algos and automated trading by dealers in the U.S. corporate debt market. I think that's an opportunity that you've mentioned in the past, but just wondering what the impact could be to your business. Are you seeing increased adoption of algos by dealers on your platform? And just wondering if you think this could increase hit rates on your platform, over time?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

We have, and it's part of the growing success that we're having in small ticket sizes is that the growth in algos is significantly increasing the price responses for smaller trades. And most of that activity that is fully electronic from the algos is in $500,000 and under trade sizes in corporate bonds. But we've definitely seen an increase in the number of algos that are live and at work on the MarketAxess system, and we're aware of more that are coming. And I think it's a very positive development for the small ticket business in corporate bonds because the clients will see more pricing and more competition on the back of those investments.

Operator

And our next question comes from the line of Rich Repetto from Sandler O'Neill.

Richard Henry Repetto - *Sandler O'Neill + Partners, L.P. - Principal*

I don't think your operator likes me here, but anyway. So my first question is, Rick, you talked about in this other credit that emerging markets, the growth has outpaced high-yield in eurobonds. And certainly, that's the case year-over-year. But if you look more recently, it's probably a lot more mixed. So I guess if you could -- I don't know whether there's any different, any insight you can add to the growth rates of -- in that bucket, the other credit bucket between high-yield, emerging markets and eurobonds. Like what's going on there that caused -- now emerging market looks like it's dropping off quarter-over-quarter and so forth.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

You mean the growth rate is slowing, is your point, Rich? It's not dropping off. You mean, the growth rate is slowing?

Richard Henry Repetto - *Sandler O'Neill + Partners, L.P. - Principal*

Yes.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

I think relative to anything you see in the trading space, any growth right now is good growth. It's not a normal environment by any means. And I think you can look back at previous periods and see when credit spread volatility is this benign, you do get flatter growth rates than when credit spreads are more active, and especially when they're rising. And we've reached a level in credit spreads where I would suggest that the next big move is going to be wider spreads because we are now at levels that -- where spreads do not normally go any lower. The key question is when that starts to happen. But on EM, these are great growth rates in this kind of environment. And as I've mentioned in the past, what's so exciting about it is we're putting a unique global EM marketplace together that includes all major currencies and markets, external debt and local markets. Clients are embracing the platform in all regions. We've had great growth this year and new clients coming onboard in Asia, new clients coming onboard in Latin America. And technology on MarketAxess has no boundaries. So the ability for EM market participants around the world to trade with each other is not only creating efficiency, it's lowering transaction costs. And I think when you look around your community, Rich, are the companies that you cover and compare our EM growth rates this quarter to everything else that's going on, we look exceptionally good. And the nice thing is it's only the beginning because by our reckoning, when we try to patch together the market opportunity in EM as well as we are doing, we still think we're high single digits in overall market share of what takes place in EM. So there's a tremendous opportunity there, and the breadth of client participation, the activity that we're seeing, the breadth of markets that are being traded on the system all give us great confidence that this is going to be a long-term growth area for MarketAxess.

Richard Henry Repetto - *Sandler O'Neill + Partners, L.P. - Principal*

That's fair, Rick. That's fair. I guess one last question on BondPoint. The way you explained it, Rick, that you have a lot of the customers, you have a lot of retail, you have a lot of small-order liquidity. And I guess, you'd expect, given your liquidity, your match rates, I would assume, be much higher, except for this, what you've pointed out, the streaming quoting capability. So I guess my question is, how fast could you build that? And is that --

if that's the case, why -- like why do people even use BondPoint, if you have all the liquidity other than the streaming capability, how fast could you build it? And is it a question of allocation of investment or capital and so forth?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

It absolutely is. It's clear, given the adoption of the retail client segment on our platform that there's more reason for us to invest in those modest technology changes now than ever before. But you're right, it's all about prioritization, right? And when you look inside the retail market in U.S. credit and you look at TRACE, Rich, what you will see is that the total market share of TRACE in $250,000 and under trades is about 5% of TRACE. So we've been focusing on the 95% of the market. The retail community is operating in the 5% of the market space. Furthermore, when you look at the retail ATS business today, it is almost entirely D2D business. These are retail brokerage firms and retail market makers trading with each other. So it's in the D2D space. And if you look at $250,000 trade sizes and under, D2D, you're down to about 2% of TRACE volume. So that is why our priorities have been building and investing technology for the larger part of the market and for our institutional clients. But because our liquidity is so good in $250,000 and under trades, the retail client segment has been increasingly finding MarketAxess and trading on MarketAxess. So the pricing here is here, and it's a matter of us converting that into what retail brokerage firms are used to, which is price-based trading rather than spread-based trading, and we are optimistic that those are changes that we can make and grow our participation in that segment even further.

Operator

(Operator Instructions) And we do have a follow-up question from Patrick O'Shaughnessy from Raymond James.

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

Yes. A follow-up on your micro-lot market share. How much of that market share gain has been a function of your effort to build up share with some of the retail wealth managers and market makers? And how much just comes from ETF market makers that tend to trade in smaller lots?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

I think the majority of it is the former. We have always been an important venue for the retail market makers because of the micro-lot trading that our institutional investors cannot conduct on the platform. So there are many, many trading opportunities for those market makers throughout the day on the platform, and that has been a key source of liquidity for us in small tickets. The ETF ARMs are increasingly getting involved in that space, and it's been a growth area over the last year or 2. But I would say that there's a much bigger participation today on the platform in those trade sizes from traditional retail market makers.

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

Got it. And then one more question, if I could. Obviously, still early days on your new high-yield pricing strategy, and we can see what the market share has done. In your conversations with liquidity providers in the high-yield space, do they seem more inclined to provide more liquidity now that their variable costs are going to be lower?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

I think the answer to that is, yes. We were very pleased to get 10 major high-yield dealers embracing the new fee plan. It's obviously a fee model that scales well for them and incents them to do more volume on the system. And anecdotally, that's the feedback that we are getting. And the new fee plan obviously includes benefits for our clients and liquidity takers as well because the variable fee is roughly half of where we had been prior to the change. So we think it's a better fee model all around, and there's no doubt in our mind that the major dealers are happier with this plan and willing to support future growth in high-yield. The quarter in high-yield, the big difference is it doesn't really have anything to do with traditional institutional investors or major dealers. It's just that the players that thrive on high-yield volatility are very quiet right now. And so all of the ETF ARMs that are very active trading the shares versus the bonds, those trading opportunities right now are very limited, and you can see a significant dropoff in their activity not just here. But, Patrick, if you look at ETF share trading in the major high-yield funds, ETF funds, you will also see significant dropoffs in HYG and JNK share trading. And that's really the story this quarter of our high-yield business.

Operator

And we do have a follow-up question from Chris Shutler from William Blair.

Christopher Charles Shutler - *William Blair & Company L.L.C., Research Division - Research Analyst*

Two real quick ones. In eurobond, I know it's small today, but just given the market share declines over the last couple of quarters, do you see any need to adjust pricing? And then secondly, in block trading, can just give us the market share numbers and how that changed year-over-year?

Antonio L. DeLise - *MarketAxess Holdings Inc. - CFO*

So Chris, on the eurobond side, you'll recall, in the second quarter earnings call, we had some comments that we were probably going to revisit a couple of elements of the fee grid. And there were some concerns that some of the dealers had raised on some very specific components. We did -- in September, we did make some adjustments to some very specific components sort of around euro high-yield. We actually reduced the fees, it looks consistent with our mark-up fee in our new high-yield plan in the U.S. We also made some changes to long-dated paper where we weren't seeing a lot of traction. So we have made those changes. Again, what Rick said on high-yield, just the macro environment is sort of dominating the landscape right now. So it's hard to say that they've had an immediate impact, but we do expect that these changes have eliminated some of that noise around specific components irrelevant to the plan.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Just a follow-up on that, Chris, is that I think what you see in our European business is indicative of what's going on more broadly. On the back of the ECB quantitative easing that is now -- that has, over the last 18 months, included corporate bond purchases, eurobond spreads are at all-time low levels, and European institutional investors are trading more in EM and U.S. credit than they are in euros. So what you see for us, overall, is that the European business is growing very well, but the products that are in vogue and trading actively because of the demand for yield among European investors are EM and U.S. credit products, not euros. And it's quite possible that tomorrow might signal the beginning of a change in ECB quantitative easing policies. The market is awaiting their announcements of they intend to do, but it would be a significant change if the ECB stops buying corporate bonds and storing them away on their balance sheet in terms of more trading opportunities going back to the private market and to institutional investors versus what we've been dealing with over the last 18 months.

Christopher Charles Shutler - *William Blair & Company L.L.C., Research Division - Research Analyst*

That's real helpful, Rick. And then on the block market share.

Antonio L. DeLise - *MarketAxess Holdings Inc. - CFO*

Oh yes, I'm sorry. On the block market share, it was very consistent with what you saw in the second quarter, which was right around 9%. So -- and you'll recall, we talked about this on the second quarter all, it was around 7% last year for the full year, 8% Q1, and last 2 quarters have been right around 9%.

Operator

And we do have a follow-up question from Rich Repetto from Sandler O'Neill.

Richard Henry Repetto - *Sandler O'Neill + Partners, L.P. - Principal*

Rich, just one follow-up. On your relationship with BlackRock and the Aladdin platform, is that exclusive? Can Aladdin hook up, or are they already hooked up to other people, or is it exclusive?

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

They are totally hooked up to other people. That is a broad trading risk and analytics solutions, not just for BlackRock, but for all of their Aladdin clients. And so they are connected to many different trading venues. And as you would expect, they are serving their clients by ensuring that they're making best efforts to always find the best price for their clients. And as you know, we're highly confident that when it comes to global credit products, that they continue to believe that MarketAxess is delivering great liquidity, great pricing and efficient integration with the Aladdin system.

Operator

Thank you, and this concludes today's Q&A session. I would now like to turn the call back over to Rick McVey for closing remarks.

Richard M. McVey - *MarketAxess Holdings Inc. - Founder, Chairman & CEO*

Thank you for joining us, and we look forward to talking to you next quarter.

Operator

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