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ITG - Q4 2016 Investment Technology Group Inc Earnings Call

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CORPORATE PARTICIPANTS

JT Farley *Investment Technology Group Inc - Managing Director IR & Corporate Communcations*

Frank Troise *Investment Technology Group Inc - President and CEO*

Steve Vigliotti *Investment Technology Group Inc - CFO*

CONFERENCE CALL PARTICIPANTS

Christian Bolu *Credit Suisse - Analyst*

Ken Worthington *JPMorgan - Analyst*

Rich Repetto *Sandler O'Neill & Partners - Analyst*

Chris Allen *Buckingham Research Group - Analyst*

PRESENTATION

Operator

Good morning and thank you for joining us to discuss ITG's Fourth Quarter 2016 results. My name is Drew, and I will facilitate the call today. After the speaker's remarks, there will be a question and answer period.

(Operator Instructions)

I would now like to turn the conference call over to JT Farley of ITG.

JT Farley - *Investment Technology Group Inc - Managing Director IR & Corporate Communcations*

Thank you, Drew, and good morning.

In accordance with the Safe Harbor regulations, I would like to advise you that the forward-looking statements that we will be making this morning are subject to a series of risks and uncertainties that may cause actual results to differ materially from those statements. These forward-looking statements speak as of today, and you should not rely upon them as representing our views in the future. While we may elect to update these forward-looking statements in the future, we undertake no obligation to do so. I advise you to read about the risk factors that may affect forward-looking statements in this morning's press release as well as in our SEC filings.

During the call, we will also discuss non-GAAP financial measures adjusted to exclude certain specified items. Reconciliations of these non-GAAP financial measures to the most comparable GAAP measures are available on our website. Press releases and the PowerPoint slides which accompany this presentation are available for download in the Investor Relations section of ITG.com. Speaking this morning are ITG's CEO and President, Frank Troise, and CFO, Steve Vigliotti.

To start, I would like to turn it over to Frank.

Frank Troise - *Investment Technology Group Inc - President and CEO*

Thank you JT, and good morning, everyone.

Today I will review progress and updates for the fourth quarter. I will also provide an update on the execution of our 10 quarter Strategic Operating Plan now its second quarter of implementation. Then I will share additional steps we have taken to sharpen our focus and increase operating efficiency. Steve will then review financial results; and finally, Steve and I will address your questions.

First and most important, during the Fourth Quarter, ITG returned to profitability. This progress is attributable to strong improvements in market share across all regions, boosted by higher levels of trading activity in the wake of the US election. We were break even on an operating basis in October and profitable in November and December despite the usual seasonal slowdown in trading at year-end.

Results were strong around the globe. Europe had the best quarter of 2016, hitting a new record for market share. Canada posted strong revenue growth, easily outpacing the increase in local market activity and set a new quarterly record for revenue in MatchNow, our broker neutral dark pool. Asia-Pacific had its best quarter of the year, the second most profitable quarter ever, and we reached a new record for POSIT alert activity.

In the US, our market share grew in each month of the quarter resulting in average share of 2.05%. That is up 30 basis points from our share in the third quarter of 2016. Our goal is to improve on that share in the first quarter of 2017. US business is the core engine of growth for ITG; and through these market share gains, we intend to move to a profitable run rate in the region by the end of June 2017, absent any drop in market-wide trading activity.

Our focus is on improving operational efficiency, reducing costs, and better allocating our resources to the highest priority areas. As we said on the last call, we've identified a total of $10 million in annual cost savings in the third and fourth quarter of 2016 which will help offset the investments we are making in our strategic operating plan. About 90% of these savings are reflected in the fourth quarter 2016 expense run rate.

We continue to look for cost efficiencies across our business even as we execute on the strategic operating plan. As part of that effort, we are discontinuing corporate access services by the end of the first quarter. Corporate access is not a material operation. This is another step toward sharpening our focus on core liquidity, execution, analytics and workflow technology capabilities.

While we work to build on the momentum in our business and execute against our plan, we are determined to eliminate legacy matters as demonstrated last month with our final settlement of the pre-released ADR matter with the SEC. This settlement is now behind us. It highlights the importance of risk management and the fostering of a strong culture of compliance across the entire organization. Now, as before, our focus is delivering best-in-class client solutions with the highest level of service, all while operating with integrity.

Let's turn to our strategic operating plan. To review briefly, we launched the plan on our second-quarter earnings call in late July 2016, and we are already making significant progress. We plan to invest $40 million through the end of 2018 in technology and people.

These investments will allow us to deliver world-class client service, optimize operations, and drive business scale. The investments are in flight, with the majority to be completed this year.

We plan to add at least 60 new hires over the course of our ten quarter plan in client coverage teams, product management and technology development efforts. We expect starting in 2019 that investments in technology and process improvement will yield at least $5 million in annual savings from efficiency opportunities.

Assuming no reduction in average global trading activity, the goal of this investment plan is to exit 2018 at a $600 million annual run rate for global revenues, approximately 25% higher than annualized fourth quarter 2016 revenues. Given our high incremental margins and the expected expense savings related to these investments, pretax margins are targeted to be 15% by the fourth quarter of 2018.

As a reminder, some goals of our strategic plan focus on, first, enhancing the client experience. We're developing robust account service tools to enable coverage teams to better serve clients.

Second, creating a customization toolkit for Triton and Algos. This will address client needs with greater precision and in a cost-effective manner. Third, we are investing to bolster our leadership in multi-broker transaction cost analytics and embedding them in our portfolio trading and electronic execution products.

Since our discussion last quarter, we started executing this plan. During the fourth quarter, we invested $2.9 million under the strategic operating plan and made 18 hires. Thirteen of these hires are within technology development. Ten of these hires engaged before the end of 2016.

Let us note, that with a focus on cost discipline and delayering we ended the quarter slightly down on headcount at 956 employees globally. While most of the work in the strategic operating plan is multi-quarter in nature, in the first half of 2017, we expect to roll out some new client-facing capabilities. To share a few, one of our cornerstone products is POSIT Alert. It's our global buy-side block crossing network available in 37 countries with Thailand launched last month. We are improving our user experience for Alert through enhanced indication management tools, improved trading workflow, and the addition of commission management capabilities.

Commission insight. We plan to launch a new set of tools to manage CSAs globally with features to accommodate the new the MIFID 2 regulations. In analytics, we're extending our capabilities in FX and launching a new fixed income offering. We look forward to providing updates on these capabilities and sharing our progress on the execution of the strategic operating plan on future calls.

While we are fully engaged in executing on our strategic plan, we have also centralized our leadership structure to better focus our efforts on core capabilities and clients. We announced this week that Brian Pomraning will be leading the Global Product Management Organization. Brian is responsible for our liquidity, execution, analytics and workflow technology capabilities.

Ian Domowitz assumes the newly created role of Vice Chairman. Ian will focus on the groundbreaking analytics research, cross product innovation, and client service for which he is well known.

Our advisor, Robert Ferstenberg, has joined the firm full-time as Global Head of Quantitative Research and Execution Analytics, a center of excellence for quantitative and analytical rigor across our enterprise. And we are consolidating the corporate functional areas under Steve, who will also assume the title of Chief Administrative Officer. With these changes, we have the people and processes in place to execute on our strategic operating plan and to work on growing our business.

In addition to reassigning our organizational structure, we've changed our compensation structure, increasing the mix of deferred equity grants and reducing the percentage of cash bonuses to better align our compensation with our long-term growth goals. Our focus as a firm is to provide clients with solutions for best execution, delivered with integrity and customized service. We will expand on our strength in financial market technology with investments in core liquidity, execution, analytics and workflow solutions.

To sum up, our strategic operating plan is well underway, and we are off to a good start in gaining business momentum. Our international operations are strong and our US franchise is on a path to profitability. Throughout 2016 we have had many meetings and discussions with clients, and I have found that they are taking notice of our commitment to providing best in class solutions and the highest level of service.

During the first quarter, I will be embarking on another round of outreach to ensure that we are listening to clients as we execute on our strategic operating plan. I will use the feedback from these meetings to refine our approach as we strive to create a culture of best operator in all aspects of our business.

Now, let me turn to Steve to discuss the financial results of the fourth quarter. Steve?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Thank you, Frank, and good morning everyone.

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As Frank noted, during the fourth quarter we returned to profitability with strong improvements in market share across all regions. Our European and Canadian operations increased profitability during the fourth quarter, while in Asia-Pacific, we posted our second highest quarterly profit on record. In the US, market share gains throughout the quarter helped us significantly narrow the loss from the third quarter.

In the fourth quarter, we generated revenues of $119.6 million and GAAP net income of $5.7 million or $0.17 per share. These results compared to revenues of $104.2 million and a GAAP net loss of $0.73 per share in the third quarter of 2016, and GAAP revenues of $224.2 million and GAAP net income of $2.40 per share in the fourth quarter of 2015.

On slide 9, we detailed non-operating items that were included in our GAAP results. Fourth quarter 2016 results include, first, a charge of $3.6 million pretax or $0.09 per share after taxes, representing the amount by which the final ADR settlement exceeded the reserve we established in the third quarter of 2016 as well as related professional fees.

Second, a restructuring charge of $5.3 million pretax, or $0.10 per share after taxes, to delayer our management structure and eliminate positions. Third, a charge of $600,000, or $0.02 per share after taxes, for the contractual up-front awards granted to our CEO. These charges were offset by a tax benefit of $7.3 million, or $0.22 per share, related to a reduction in tax reserves covering several years. Excluding these items, we earned net income of $5.3 million, or $0.16 per share.

Slide 9 also breaks out the non-operating items in the third quarter of 2016 and the fourth quarter of 2015. The remainder of this discussion all references to results, revenues, and costs will be on an adjusted basis excluding the items listed on slide 9.

Slide 10 presents consolidated results along with separate breakdowns of results from North America, Europe, and Asia-Pacific operations, as well as our corporate activity. As a reminder, corporate activity includes investment income and other gains as well as costs not associated the operating ITG's regional and product-based business lines. As compared to the third quarter of 2016, consolidated revenues were up $15.4 million while consolidated expenses were up $2.6 million.

As we noted in this morning's news release we have increased the proportion of deferred equity in our full-year 2016 incentive compensation program. This reduced costs by $2.4 million in the quarter, or $0.05 per share after taxes, and lowered our compensation ratio. This move will better align employees with our long-term growth objectives. Going forward, this shift to be spread out over each quarter and will be offset over time by increased expense for the deferred awards.

Our consolidated pretax margin was 6.1% up from negative 5.3% in the third quarter 2016 and from negative 2.6% in the fourth quarter of 2015. The effective tax rate on our consolidated pretax income was 27%.

Our North American businesses posted net income of $0.02 per share on revenues of $72.2 million. Our combined European and Asia-Pacific businesses posted net income of $0.24 per share in the fourth quarter and revenues of $47.1 million. Corporate activity lowered net income by $0.10 per share.

On slide 11, you can review the year-over-year impact exchange rates had on the financial results of our foreign subsidiaries. The overall currency rate changes reduced our profitability by $300,000 when compared to average exchange rates in the third quarter of 2016. Currency changes increased our profitability by $400,000 when compared to rates in effect in the fourth quarter of 2015.

As a reminder, the foreign currency exposure for our European operations is split amongst multiple currencies including British pounds and euros. The weakening of the British pound has little impact on our bottom line since revenues and expenses that originate in that currency largely offset each other.

On slide 12, we separate North American operations between the US and Canada. During the fourth quarter of 2016, we generated revenues of $56 million with a pretax margin of negative 3.3% in the U. S. This compares to $48.8 million in revenues with a pretax margin of negative 17.5% in the third quarter of 2016.

Commission revenues rose 21% sequentially due to gains in market share as well as higher market wide trading activity. Our percentage of sell side volume rose sequentially from 52% to 53% while our average US revenue per share held study at 41 mills.

Recurring revenues were down $300,000 from the third quarter of 2016 and$ 8.2 million from the fourth quarter of 2015. The year-over-year drop primarily reflects the investment research divestitures in May 2016 and December 2015.

US expenses were down year-over-year due primarily to the investment research divestitures, but they were up slightly on a sequential basis due to higher transaction processing costs associated with increased trading activity. Our compensation ratio in the US was 43% in the fourth order of 2016 as compared to 52.3% in the third quarter of 2016 and 49.2% in the fourth quarter of 2015. The improved ratio reflected the full-year impact of the increase use of deferred stock, our cost-reduction measures, and higher commission revenues.

Canadian revenues were up both sequentially and year-over-year driven by solid market share gains and a new quarterly revenue record for our Match Now dark pool.

On slide 13 is a breakdown of our European and Asia-Pacific businesses. Our European team posted strong results with revenues up both sequentially and year over year thanks in large part to a new quarterly record for market share. Asia-Pacific posted its second best quarterly profit on record driven in part by increased electronic trading by buy-side clients including a third straight record for POSIT Alert in terms of both revenues and value traded. This was the fifth consecutive quarter where we saw growth in value traded and market share in the region.

On slide 14, we offer supplementary information on revenues for our product groups and investment income which we categorize as corporate. Execution services revenues rose sharply versus the third quarter for 2016 due to market share gains and our trading businesses globally and increased market activity. They were also up year-over-year despite the impact of the investment research disposals and business closures.

Workflow technology revenues rose modestly versus the third quarter of 2016 and the fourth quarter of 2015 due in part to increased commission share revenues. Analytics revenues were up modestly on a sequential basis but down year-over-year due in part to reduced levels of project margin.

On slide 15, we present supplementary pretax income information for our three product groups and for corporate activity. Margins were up both sequentially and year over year in execution services and workflow technology reflecting higher commissions from trading activity and lower fixed costs. Analytics profitability was flat versus the third quarter but down versus the prior year due to lower revenues and higher expenses as we expand our multi-asset TCA capabilities.

The corporate loss increased sequentially and was nearly unchanged versus the fourth quarter of 2015. As a reminder, our corporate expenses will vary from quarter to quarter as we work through litigation, regulatory, and other corporate matters.

Slide 16 presents US volume and rate capture statistics. Our average daily executed volume was up 25% versus the third quarter of 2016 and up 16% versus the fourth quarter of 2015. Overall revenue capture per share was unchanged on a sequential basis but down year-over-year. This drop was due to a lower average sell-side rate per share and the impact of reduced high-touch trading.

We ended the quarter with $278 million of cash. This was up from $260.9 million at the end of the third quarter. This increase reflects, in part, a reduction in cash tied up in European settlements due to the seasonal activity decline in late December.

Excess cash at December 31 over and above what is needed for required regulatory capital and other compensation liabilities was approximately $55 million. This is up from $50 million at September 30, reflecting our free cash flow and the suspension of our share repurchase program in the fourth quarter.

Regarding capital returns, with the settlement of the SEC ADR matter, we expect to resume share repurchases this quarter. We intend to repurchase shares over the course of the year in an amount sufficient to offset any dilution from the vesting of stock awards. We may purchase additional shares on an opportunistic basis depending on factors including market conditions and competing needs for our excess cash.

Looking forward, let me make a few closing observations. Our US average daily volume in January was 139 million shares with average revenue per share lower than our fourth quarter 2016 average. The average revenue decline was due to an increase in the percentage of volume from sell side accounts. While that overall volume level reflects a market share decrease as compared to December, it is flat month over month if you factor out the significant rebalance activity we previously noted in December.

Going forward, we are targeting US market share improvements on a quarter-by-quarter basis, noting that it will fluctuate from month to month due to events such as index rebalances. Combined average daily commissions in January in our Canadian, European, and Asia-Pacific businesses were down approximately 2% in US dollar terms compared to the fourth quarter of 2016.

With that, I would like to turn it back to Frank.

Frank Troise - *Investment Technology Group Inc - President and CEO*

Thank you, Steve.

Before we answer your questions, let me briefly recap our remarks. We are executing on our strategic operating plan and are off to a promising start. Based on discussions with clients and recent market share improvements, we see that our plan is gaining traction. Our market share in the US was 1.75% in the third quarter of 2016. It rose to 2.05% in the fourth quarter.

We are relentless in our ambition to grow our market share in the coming quarters and are encouraged by our momentum. With disciplined investment and a commitment to excellence we will continue to work towards our goals.

Now, we will answer your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Christian Ballou of Credit Suisse

Christian Bolu - *Credit Suisse - Analyst*

Good morning, guys. So thanks for all the color. Just some expenses. Factor in the feral expense reduction initiatives, plan investment spend, maybe could you just help us think about how -- what 2017 expenses growth maybe land, and then any color on the cadence through the year?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Sure. Let me start. As you know, we are embarking on and have embarked on our strategic operating plan which calls for the investment of $40 million over the course of a ten-quarter period which began, really, in the fourth quarter of this year. We expect the majority of those investments, roughly 55%, to be made in 2017. Those investments should take our costs up by roughly around 10% -- excuse me, $10 million over the course of 2017. Having said that, we did implement some cost-saving measures throughout the second half of last year, about 90% of which was realized in the fourth quarter run rate. So a little bit more to go there. And of course, going forward, we're going to continue to look for operating efficiencies in our model.

Christian Bolu - *Credit Suisse - Analyst*

Okay. So I should think of it as roughly 10% over 4Q run rate?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

No. Sorry. I misspoke. It was $10 million of expenses from the strategic operating plan over the course of 2017.

Christian Bolu - *Credit Suisse - Analyst*

Okay. Got you.

Just a bigger question here in 2018 targets, as we see pretty weak market volumes here to start the year, just maybe talk through your confidence level in being able to hit targets and any other drivers or any other levers you have to the extent we stay here in terms of where market volumes are.

Frank Troise - *Investment Technology Group Inc - President and CEO*

So we remain confident in hitting the $600 million exit rate in 2018. The market opportunity is there. We're investing in the core business. It's up to us to capture it. The plan has been put together over several months in 2016, it is a thoughtful investment plan. And I have seen firsthand the impacts that technology and process improvements can have on revenues and market share. We can't control market volumes. We can control our engagement with clients and our market share growth. I'm confident that this level investment and our energy and intensity will deliver the results.

Christian Bolu - *Credit Suisse - Analyst*

Okay.

Then a couple questions just on the international side of things. So as we are fast approaching the implementation here, can you give us any insights into the conversations you are having with clients, and if you are beginning to see any concrete evidence that some of that $8 billion paid for bundled execution and research could ultimately accrue to ITG. And then the second part to that question is in Asia, obviously you've launched the initiative into POSIT in Thailand. So just remind us again how you're thinking about your opportunity set in Asia, kind of any targets you have as to how much that region could ultimately contribute to our your business and then any key milestones we should be watching out for.

Frank Troise - *Investment Technology Group Inc - President and CEO*

Sure. Let me start with the question on European Regulatory Change MIFID 2.

We view MIFID 2 as a clear tailwind for our business. We've had many conversations with clients. Client feedback indicates that unbundling of execution from research is going to extend well beyond Europe. We're a leading provider of best execution tools and commission management solutions. Both of these set us up well to capitalize on the change. So we do view this as a tailwind. We view that there is upside. The conversations are beginning to happen in reality and practicality with clients.

In Asia today, we have about 1% market share. Asia, to me, is a developing market with respect to electronic execution. All indications from third-party research, from client conversations indicate that there will be more and more electronification of execution in Asia which positions us well given our cornerstone product POSIT Alert, in the region as well as our Algo capabilities and smart order routing.

Christian Bolu - *Credit Suisse - Analyst*

Okay. Thanks for taking my questions.

Operator

Ken Worthington of JPMorgan.

Ken Worthington - *JPMorgan - Analyst*

Hi. Good morning.

Frank, I'm sorry I missed this, but I think you said by the end of June 2017 was it the US business you thought would be back to profitability?

Frank Troise - *Investment Technology Group Inc - President and CEO*

That's correct. We intend to drive the US business back to profitability in the second quarter of this year, by the end of June.

Ken Worthington - *JPMorgan - Analyst*

Okay. So if expenses are going up, and I assume a lot of the expenses are going up in the US, what sort of is the path that you are taking to get revenue to go up a pretty reasonable amount in a fairly short period of time here to get you back to profitability? It feels like a big goal in a very short period of time. Can you take us down the path? It sounds like it's more than just, like, market share, but it's like new products being successful. Anyway, more details would be helpful.

Frank Troise - *Investment Technology Group Inc - President and CEO*

Sure.

We are driving to profitability in the US through market share growth and cost effectiveness. Market share growth will come from the intensity of engagement with clients, the rollout of some of the capabilities I spoke about in my comments, and cost-effectiveness. I mentioned also that we'd be exiting a non-material corporate access operation. So as I mentioned in my comments, we gained 30 basis points in the fourth quarter over the third quarter of 2016, and we're relentless in our pursuit of market share growth in engagement with clients. Based on our capabilities, the capabilities that we intend to roll out and client feedback, we believe that it's achievable.

Ken Worthington - *JPMorgan - Analyst*

Okay. And I know I can probably do this after the call, but any guess on how much market share you will need to get by the end of June to kind of get back to that breakeven or profitability metric?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Yes. Obviously that's going to depend a lot on overall market activity, as well as the client mix of our business; but when you can look at the fourth quarter activity, market activity and our share of 2.05%, and see that we posted a pretax loss of $1.8 million. So you kind of do the modeling probably from there.

Ken Worthington - *JPMorgan - Analyst*

Okay. Given the delayering in the business, how are you thinking about margins on incremental revenues? So it kind of used to be -- or maybe the rule of thumb used to be for ITG, 50% incremental revenue would fall to the bottom line; but again, you've delayered in I would say X investment. How should we think about the margins on incremental revenue today?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

I think the guidance from where we are right now, obviously, a lot of the measures we took are reducing our fixed-cost base. And then going forward from here, I would still guide the incremental revenues would drop us somewhere north of 50% to our pretax line.

Ken Worthington - *JPMorgan - Analyst*

Okay. Then maybe two more.

Can you tell us about details on the changes you made, like what was the old policy and what is the new? And I assume -- I think you said $2.7 million was the impact in 4Q. I assume that's proportional US versus non-US?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Was that the deferred comp you were mentioning?

Ken Worthington - *JPMorgan - Analyst*

Yes.

Steve Vigliotti - *Investment Technology Group Inc - CFO*

So the impact in the fourth quarter, Ken, that was a full-year decision we made. So for the full year of 2016 incentive compensation program, we decided to pay a little more of that in equity. Made that decision in the fourth quarter as a result of the entire impact in the fourth quarter, which was $2.4 million.

So, looking out on a quarter-by-quarter basis going forward, that would be about a $600,000 per quarter impact; and going forward, that would be largely offset by the fact that we're now going to be expensing these higher -- these increased awards that we just issued on a going-forward basis.

Ken Worthington - *JPMorgan - Analyst*

Is this vesting over a three-year period, four-year period, five-year period? Is it the same invest as it used to be as we think about how the amortization kicks in, in forward years?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Yes. Three years, correct, same as usual. Yes.

Ken Worthington - *JPMorgan - Analyst*

Okay. And then one more tiny one.

Steve, you mentioned the recurring was down year-over-year due to the divestitures of research. It was also down a bit sequentially, so that wouldn't have been impacted by the divestitures. Why was that down?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

It was also research driven as well, right, just part of our sale of the energy business a year ago. We had a research distribution agreement that began to wind down towards the second half of this year. So we did continue to generate some recurring research revenue from our -- from the distribution services we're providing in the first half of the year. That wound down now towards the end of this year.

Ken Worthington - *JPMorgan - Analyst*

So is that completely -- was that completely out of the fourth quarter or is there more --

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Yes.

Ken Worthington - *JPMorgan - Analyst*

Okay. Awesome. Thank you very much.

Steve Vigliotti - *Investment Technology Group Inc - CFO*

They'll be out in the fourth quarter, yes.

Ken Worthington - *JPMorgan - Analyst*

Okay. Thanks.

Operator

Rich Repetto from Sandler O'Neill.

Rich Repetto - *Sandler O'Neill & Partners - Analyst*

Good morning, Frank; and good morning, Steve.

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Good morning, Rich.

Rich Repetto - *Sandler O'Neill & Partners - Analyst*

The first question is, I'm just trying to understand, to me, it appears a little bit selective when you exclude the award for the CEO and then include the benefit of the deferred comp. Can you go through the rationale on why you would exclude one and include the other, because they are both one time?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Well, the -- we're obviously calling out. We're trying to be pretty transparent here with the shift to more deferred stock for this year. A lot of companies in our space will vary that percentage from period to period. Again, I thought we were being pretty transparent in calling out. And, quite frankly, we're going to be expensing that going forward now. We're not going to be calling out the extra expense on that going forward.

Again, we just wanted to point it out because it had a disproportionate impact on the fourth quarter, but it's very common with what a lot of companies do when they decide their year-end compensation programs. With respect to the upfront comp, as you know, that was a pretty sizable number in the fourth quarter, most of that to replace awards that Frank walked away from to come work here. And we continue that on through the remainder of the year, and that will discontinue come beginning of next year.

Rich Repetto - *Sandler O'Neill & Partners - Analyst*

Okay. I guess the next question is, there's been a couple questions on the breakeven -- you know, the market share. That's predicting volumes I guess. Can you just even tell us what breakeven volume is? We're calculating around 160 million a day. Is that a reasonable estimate, 160 million to 165 million?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Again, it'll depend on the mix of business. I don't want to necessarily want to -- we haven't typically provided guidance, but you can kind of see what our rate was and our volume in Q4, and where that left us with a $1.8 million pretax loss. I think that's a reasonable base to model off of.

Rich Repetto - *Sandler O'Neill & Partners - Analyst*

Okay. But if we don't have any other -- there's other moving parts. We don't have one thing, whether it's market volumes or market shares. And we don't know which way the rate's going or expenses, et cetera.

But anyway, I guess the last question is, just a follow-up. Frank, you've talked about -- several quarters ago about the number of clients that had reengaged that hadn't -- fully reengaged, some partially and some that hadn't at all. Can you revisit those numbers and sort of give us an update on -- obviously the numbers have improved, but more qualitatively, have you surveyed that again?

Frank Troise - *Investment Technology Group Inc - President and CEO*

So, Rich, we look at that as a bit of a stale analysis at this point. We're beyond Omega at this point, and we're in the steady-state pursuit and engagement with clients.

Rich Repetto - *Sandler O'Neill & Partners - Analyst*

Okay. Thanks.

Operator

Chris Allen with Buckingham Research.

Chris Allen - *Buckingham Research Group - Analyst*

Morning, guys. I was wondering if you could give us a little bit more color on the capture rate pressure that you're seeing in January relative to the fourth quarter, and maybe if you could talk about any seasonality with buy-side versus sell-side flow in if that's impacting it.

Steve Vigliotti - *Investment Technology Group Inc - CFO*

This is Steve.

So the mix we talked about being 53% in Q4 is picking up to around 56% in January. So that's shaved about 5% off our average commission rate.

Chris Allen - *Buckingham Research Group - Analyst*

Got it. Okay.

And then just on the investment spending for the SOP in2017, I think, Steve, you mentioned $10 million of impact in the expense line, but 55% of the 40 is $22 million or so. Is the rest being capitalized? I just want to be clear on that.

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Yes, that's correct, Chris. In addition to hardware purchases that are obviously capitalized, part of the comp that we expend for, development time and efforts to build new product is also capitalized.

Chris Allen - *Buckingham Research Group - Analyst*

Okay. Just to kind of think about compensation moving forward and kind of the comp to revenue ratio, any kind of color now just in terms of maybe what the base fixed level is of compensation and how to think about the comp-to-revenue ratio moving forward from a quarterly perspective?

Steve Vigliotti - *Investment Technology Group Inc - CFO*

Yes. I mean, the full year was around 40%. I think that's what we'd probably guide for the first half of this year; and as you know, our ratio tends to move a little bit lower as revenues grow. So we'd expect that to improve towards the latter part of the year.

Chris Allen - *Buckingham Research Group - Analyst*

Got it. That's it for me guys. Thanks.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Frank Troise, CEO, for any closing remarks.

Frank Troise - *Investment Technology Group Inc - President and CEO*

Thank you for your questions. We look forward to discussing our continued progress on our first-quarter call in May, and thank you again for joining us this morning.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.