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ITG Seeks To Scratch The Itch Of Stock Traders In A Shrinking World

BY VICTOR REKLAITIS
INVESTOR'S BUSINESS DAILY

Investment Technology Group's management and some analysts don't precisely see eye-to-eye on the company's recent scratching.

CEO Bob Gasser said ITG has "just scratched the surface" in the European market during a third-quarter conference call.

Meanwhile, analysts at Keefe, Bruyette & Woods wrote in a research note that ITG has "not yet scratched the surface on international opportunities."

But here's what the two sides agree on: The company should attract a growing number of overseas customers who are itching to use its products.

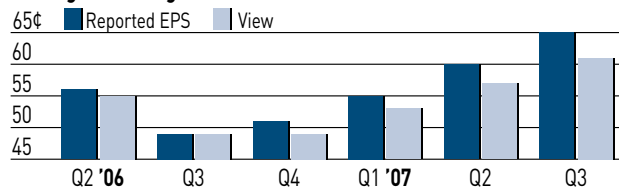
ITG makes electronic trading products that cover the whole investment process, including pre-trade analysis, trade execution and post-trade evaluation. It's poised for gains in Europe partly because of a rule change last year called MiFID, which is short for the Markets in Financial Instruments Directive.

The complicated change, which updates European regulations on investment services, is expected to bring about gradual market fragmentation. Analysts see it as one big way MiFID should benefit ITG. One of the New York-based company's main products is Posit, a stock-matching system that lets institutional investors trade with each other, basically in secret.

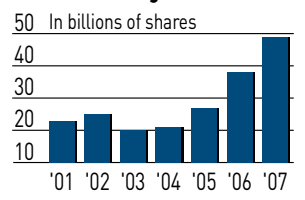
Aiming At The World

Investment Technology Group provides a range of electronic trading products, from order management to post-trade analysis. It expects more overseas growth and has worked to expand into new asset classes such as derivatives

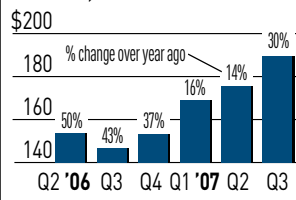
Beating or meeting views



ITG's U.S. trading volume



Revenue, in millions



Sources: Company reports, Thomson Financial

MiFID "essentially legitimizes a lot of these alternative trading venues such as ITG's Posit," analyst Niamh Alexander of Keefe, Bruyette & Woods said in an interview. "It should really help bring in and grow the volume, and encourage new customers to trade on ITG."

ITG, which is slated to report fourth-quarter results on Thursday, cites overseas growth as its current top priority. The company has been in business in the U.S. since 1987. That's when it was established as an arm of the **Jefferies Group**^{JEF}.

"It's really been all about globalizing what is a very powerful North American product suite," Gasser, the CEO, said in an interview. He said ITG is "exporting

that (suite) to Europe — clearly MiFID is a big driver there — and ultimately into Asia-Pac and Australia as well."

Besides expanding into other countries, the company also has diversified by acquiring RedSky Financial for about \$22 million in June. RedSky is now called ITG Derivatives. It specializes in electronic trading with multiple asset classes.

"It's going to add a new arrow to their quiver, in terms of providing access to derivatives markets and equity markets," analyst Michael Vinciguerra of BMO Capital Markets told IBD. "You see more and more buy-side clients today who utilize options and futures as part of their trading strategies for their equity division. I think

Investment Technology Group itg.com

Ticker	ITG
Share price	Near 46
12-month sales	\$687 mil
5-year profit growth rate	15%

IBD SmartSelect Corporate Ratings

Composite Rating	94
Earnings Per Share	73
Relative Price Strength	91
Industry Group Relative Strength	A-
Sales+Profit Margins+ROE	A
Accumulation/Distribution	B-

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that ITG adding that piece of the pie is important."

But it's the expansion into other countries that analysts usually emphasize in predicting ITG's earnings per share for future quarters. Analyst Rob Rutschow of Deutsche Bank, which owns ITG stock, wrote in a recent company report, "We continue to believe that international growth can drive double-digit EPS growth."

ITG has met or beat Wall Street's profit forecasts for at least 11 straight quarters. For the third quarter, the company said earnings rose 33% to 65 cents a share. That topped forecasts by 4 cents. Revenue grew 30% to \$189.8 million. Analysts expected \$178.6 million.

Earlier this month, the company reported average U.S. daily trading volume for December of 172 million shares. That's a 25% drop from November and about flat compared with December 2006. But ITG cited lower overall market volumes. Plus some analysts said December volume was in line with expectations. (Continued)

Customer trading volume drives ITG's business. The company relies on large mutual funds and large hedge funds for its customer base, rather than retail investors.

"Our wheelhouse tends to revolve around the largest and most sophisticated institutional investment managers," Gasser told IBD.

The company went public in 1994. Over the past 14 years, Raymond Killian has served as ITG's CEO for most of the time.

Killian briefly left the firm a couple of times over the years. But he kept coming back. So when he appeared

to retire from his CEO post for good in 2006, some investors kept a watchful eye on the new boss. Alexander, the KBW analyst, said Gasser is proving he can deliver.

"He just passed his year at the firm in October. I think that's an important milestone," she told IBD. "Investors are pretty comfortable and increasingly impressed with what Bob has accomplished while he's been there."

In addition to concerns about its new leadership, ITG also faces challenges from competitors. Its Posit product competes against

other so-called "dark pools," such as those offered by **Liquidnet** and **Pipeline Trading Systems**. In trade cost analytics, ITG competes with a number of large brokers that provide that analysis to their customers.

But analysts say the company separates itself from the competition with its wide range of products and by not engaging in proprietary trading. Gasser also cites those two factors.

"I think our largest global investment clients value and appreciate that type of one-stop shopping – and from a firm that does not compete with them for liquidity," he

said. "In other words, we don't have any principal trading or proprietary trading."

Another concern is how ITG might react to a recession. Gasser said it's "hard to predict" what that would mean for the company.

"A recession over a prolonged period of time could obviously lead to lower market volumes," he said. "In that case, we would be negatively affected like everyone else in the business. I don't think we're immune from that."

But the CEO also sounded an upbeat note: "Do I think in that context we have the ability to continue to take market share? Absolutely."