Bond Dealers of America

2015 Bond Dealers of America Fixed-Income Compensation Survey

Executive Summary

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Table of Contents **Page**

Transmittal Letter from BDA

October, 2015

As the only organization dedicated exclusively to the unique interests of middle-market and regional securities dealers and banks focused primarily on the U.S. fixed income markets, the Bond Dealers of America (BDA) is pleased to present the results of the Sixth[1] Fixed-Income Dealer Compensation Survey *("Compensation Survey")*.[2] It is our hope that the BDA 2015 Compensation Survey will serve as a valuable tool to enhance and inform your compensation management, strategic planning process and decision making.

At the outset, we wish to gratefully acknowledge the leadership of the BDA Board of Directors for its continued support and advice in the development of the survey instrument and presentation of the results in this report, as well as the regional and the middle-market fixed-income dealers who participated in the Compensation Survey. Their input enables the Compensation Survey to remain a relevant document that serves the needs of the fixed-income industry, BDA members and the marketplace. I am pleased to report that this year's Compensation Survey, which is the only compensation survey dedicated exclusively to middle-market and regional fixed-income dealers. The Compensation Survey maintained a high level of participation among regional and middle-market fixed-income bond dealers as it has done in prior years and continued to add new participants. The survey definitions and methodology may be found as Annexes to the report.

Based on the success of the first five reports, there was strong agreement to continue with the series and produce the Sixth Compensation Survey report. As was the case in the each of the prior five surveys, the decision to produce the Compensation Survey report was a member-driven one. Our members communicated to us that the BDA Compensation Survey was both unique and of high value as it addresses both compensation (including salary, commission, and bonus) by position trends and broader strategic, human resources and financial management issues, as they relate to staffing and compensation policies of the middle-market fixed-income securities dealer industry.

The Compensation Survey's value extends across our membership to the industry and the marketplace. The BDA Compensation Survey is the one compensation and strategic survey specifically tailored to the needs of regional and middle-market fixed-income dealers and their managements.

The timing of each of the first five survey reports covering 2007-2013 was propitious and perhaps uniquely valuable to the middle-market bond dealer community. The first BDA Compensation Survey covered the period during which the firms began to plan for the fixed-income market recovery from the 2008 crisis. The second survey covered the strong bond market recovery from the ashes of the 2008 crisis. The 2010 into 2013 period covered in the last two surveys were generally a much stronger one for the fixed-income markets and middle-market dealers. The

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[1] The first five surveys were conducted annually from 2009-13. This sixth survey was conducted after a one-year absence in 2015.

[2] The terms BDA Regional Dealer Fixed-Income Compensation Survey and Compensation Survey may be used as substitutes for each other throughout the report.

previous survey reflected the firming up of the U.S. fixed-income markets, global economic challenges and the growth and prominence of middle-market firms. The Survey responses reflected those trends, as well as reflecting the developing uncertainty about the direction of rates after the prolonged period of the low interest rate environment.

This sixth survey period extended into a more challenging period (2014-2015) and one characterized with regulatory changes across the industry and markets. It was also a year that once again demonstrated the resiliency of the fixed-income markets and the integral role of regional and middle-market dealers in the markets. The U.S. bond markets continue to be source of strength and safety in this turbulent year. Similarly, as of this writing, the local government and taxable bond markets are showing stability and strength in the face of the evolving U.S. government debt outlook, the uncertainty about a continued low benchmark Treasury rate environment and divergent and uncertain state and local government finances. The last several years provide ample evidence that the middle-market fixed-income dealer industry will respond and flourish as the marketplace challenges and operating environment evolve.

There are indeed new sets of strategic challenges awaiting the industry today amid constantly shifting market conditions and regulatory demands. We expect this year's survey to be equally useful – if not more so – in the new emerging environment.

As we noted in previous, middle-market firms appear to be better positioned in the developing marketplace and operating environment to grow and maintain and capture market share. Within this environment, insights about compensation levels, trends and policies would appear to be valuable tools for the middle-market dealers as their securities firms develop, fine-tune and implement strategies; decide how to allocate resources; and grow and manage capital and staffing in 2015 and beyond.

This year's survey had higher participation from smaller firms and thus, lower median FTE (full-time equivalent employment) and fixed-income revenue levels than the prior Compensation Survey. Nearly 60% of the responding firms' employment – full-time equivalents or FTEs – increased in 2014. Fixed-income revenues increased at two-thirds of the participating firms but with some distinctions among the market sectors. The participating firms indicated a general expectation of rising employment and fixed-income revenues in 2015.[3]

When appropriate, the Compensation Survey results are presented (1) nationally and segmented by primary geographic region, revenue level and Full-Time Equivalent (FTE) staff size peers groups and (2) compared to previous years. We are collecting the same information as in the last three surveys, indicative of the survey maturity, which enhances year-over-year trend comparisons. There are no changes in the questions asked.
That we are asking the same questions as last year reflects the success of the format and that the survey questionnaire has achieved stability and critical mass. It also indicates that BDA member firms appear to be satisfied with the questions and data requested and the results reported. The participation and survey structure stability also speak to the fact that the industry finds value in

[3] Year-over-year comparisons should be evaluated with some caution of there are invariably some entries and exits from the survey, although the middle-market survey population is generally relatively stable. These comments hold for this year's Compensation Survey

the BDA Fixed-Income Compensation Survey and reported results. Of course, as the industry and markets evolve and change, we are looking to further enhance the BDA compensation product in future years based on input from the fixed-income market participants, the BDA membership.

The results are divided into 12 topical areas within six report sections summarized below. We encourage you to read the methodology and definitions annexes at the end of the report in conjunction with the tables and results. By doing that, you will have a fuller understanding of our approach, the definitions used in the tables and how we arrived at the reported data.

- **Compensation by Position:** 48 positions including executive management; and compliance, trading, sales, investment banking, public finance, operations and technology, research, risk management and accounting. Within each department, compensation results are separated between senior, mid-level and junior positions, generally defined by level of responsibility and seniority.
    - Averages, medians, maximums, minimums and medians are provided by position, including total 2014 compensation, and by bonus (2013 and 2014), salary (2014), commission (2014), and sum of commission, salary and bonus (2014).
    - Data were presented nationally and by region (four regions – West, Midwest, South and East), full-time equivalents or FTE (two peer groups, up to 83 and above 83 as of the end of 2014) and annual fixed-income revenue (two peers, above $48 million and below $48 million in 2014 fixed-income revenue) peer groups.
    - Comparison of median bonus levels by position from 2007 to 2014 and base salary 2008 to 2014.

- **Trader Compensation by Market:** Average, median, maximum, and minimum salary, commission, bonus and total compensation for municipal, agency and government, securitization, corporate bond and money markets for senior, mid-level and junior trading professionals nationally. Averages are presented for trading by market sector depending on whether sufficient responses were received by FTE (2 groups, above and below 69.5) and fixed-income revenue (2 groups, above and below $37 million annually[4]) peer groups. This section was incorporated to provide more detailed breakdown for trader compensation among market sectors than is provided in the general compensation tables.

[4] The difference between the broader compensation by position and trader compensation fixed-income revenue groups reflect the fact that a few firms responded to the general compensation by position question but not the trader compensation tables.

- **Compensation Policies**
  - **Payout Trends:**
    - Sales: Percentage payout of all net transaction revenues and for primary market and secondary market transactions segmented by market sectors – municipal, corporate bond, Treasury/Federal agency and securitization. As appropriate, the responses are divided between the retail and institutional sales segments.
    - Municipal Market/Public Finance Banking and Underwriting and Trading: Percentage payout for primary market and, as appropriate, broken out between negotiated and competitive sales.
  - **Sales professional compensation structure; and Bonus payment frequency:**
    - Whether sales professionals are paid by commission only, salary/bonus only or commission and salary/bonus.
    - Whether traders are paid bonus in equity, cash or other form, and frequency of compensation (quarterly, semiannually or annually). Results are presented in percentage terms.
  - **Bonus Criteria:**
    - Whether based on objective quantitative basis, subjective basis, or combination of subjective and objective factors.
    - Responses are divided by trading – traders and trading desk managers; sales – sales professionals and managers; investment banking and public finance.
  - **Retirement/Deferred Compensation Programs**
    - Whether the firm has a deferred compensation program.
    - Whether the program is based on a formula or fixed amount and the basis of the formula.

- **Revenue & Staffing Growth Trends**
    - Whether staffing will change and in what direction it will change in 2015 by department (compliance, sales, trading, investment banking, research, operations).
    - Whether revenues changed in 2014 and are expected to change in 2015 and in what direction (increase, stay the same and decrease) by market sector (Treasury or government sector, Federal agencies, municipal bonds, corporate bonds, and securitization).
    - Composition (percentage) of fixed income revenues by market sector
      - Market sectors include agency, Treasury, corporate bonds, MBS/ABS and municipal bonds.
      - Average responding firm percentage fixed-income revenue distribution by market sector.
      - Maximum percentage of trading revenues generated from a particular sector.

- **Technology & Operations Expense Ratios**
    - Operational expenses as a percentage of fixed income revenues: Total non-interest operating expenses, technology expenses, Bloomberg terminal and other data service expenses, presenting the minimums, maximums, medians and averages at the national level.
    - Whether technology and operations functions are outsourced.

- **Annexes provide detailed explanations about the methodology and definitions used in the survey.**

We hope you find the information useful. We welcome any comments, questions or suggestions for future surveys.

Sincerely,

Michael Nicholas
Chief Executive Officer, Bond Dealers of America

I. *Executive Summary*

COMPENSATION POLICY HIGHLIGHTS

- **Compensation Data for 48 Positions from Senior Executive to Entry-Level Provided**
  Data on 48 positions are provided including medians, averages, maximum and minimum levels of compensation across departments at the national level, and by middle-market fixed-income dealer primary geographic region, FTE (full-time equivalent) and fixed-income revenue peer groups to the extent there were sufficient responses to tabulate meaningful compensation statistical trends. The following compensation measures are included: 2013 bonus, 2014 bonus, 2014 salary, 2014 commission, 2014 total compensation and comparison of median salary and bonus by position, when available, from 2007 to 2014 for bonus data and 2008-2012 and 2014 for base salary, respectively. With year-over-year fluctuations, bonus and salary levels have grown since the depths of the financial crisis in 2008.

- **Chief/Senior Fixed-Income Business Executive Total Compensation (Compensation by Position Section III)**
  As described above, compensation metrics are provided for positions within twelve departments at middle-market fixed-income dealer businesses including sales, trading, compliance, operations and technology, research, risk management, public finance, investment banking and accounting as well as compensation for executive "C-suite" positions. Median executive level total compensation in 2014 was $904,000 for the head of the broker-dealer, or senior broker-dealer executive (maximum of $5.5 million), $1.4 million for the head of fixed-income (maximum of $2.4 million), and $378,300 (maximum of $955,500 million) for the chief financial officer (CFO).[5]

- **Average Bonus Trends Up from 2013, Higher than 2007 Pre-Financial Crisis Year Levels. Trends Reflect Market Conditions, Revenue Trends, Industry Profitability (Bonus Trends by Position, 2007-2014 Section III-A); Higher Fixed-Income Revenues Expected in 2015 After a Mixed 2014 Dependent on Fixed-Income Market Sector, Likely to Affect 2015 Bonus**
  Bonus trends from 2007 to 2014 are presented for all positions to the extent that the statistical comparison was meaningful. Reflecting business conditions, the average median bonus across departments decreased by 33% from 2007 to 2008, increased by 16% from 2008 to 2009 and 63% higher between 2008-2014 (51% by position) and 9% between 2007-14 by department (4% by position). It is the second consecutive BDA Compensation Survey where the average bonus was higher than the pre-crisis 2007 in the six survey history. Between 2013 and 2014, the average median bonus rose in every department except one and increased in 31 positions, declined in 7 and 4 virtually unchanged where such comparisons are meaningful. The average departmental bonus rose in 2014 compared to 2013, as well as on a position-level basis regardless of department, by over 17% recovering from 2013. Taking into account the 2012-13 declines, the departmental average median was lower by 8% 2012-14.

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[5] Year-to-year comparisons are meaningful but qualified by the fact that the responding firms may differ year over year, that is, some of the firms that responded in 2015 survey may not have participated in the prior (2013) Compensation Survey and *vice versa.* The majority of the firms that participated in 2015 also participated in the prior (2013) BDA Fixed-Income Dealer Compensation Survey.

With a forecast of stronger revenue trends across sectors in 2015 according to the BDA Compensation Survey, it is reasonable to expect a directionally similar bonus performance in executive-level bonus trends in next year's survey covering year-end 2015. Keep in mind that the survey responding firms may change slightly from survey to survey year and this is the sixth year of the BDA Compensation Survey. [6]

As would be expected, salary trends were less volatile than the more discretionary bonus, flat in 2014 compared to 2012 on an annualized basis by department and 2% up by position after 16% over the last three years (5% on an annual basis). The average median salary by department increased in 8 of 12 departments surveyed in 2014, declined in one and virtually unchanged in the other 3 departments.

- **Senior Trader Salary is Slightly Higher on Average Than Bonus Across Fixed-Income Asset Classes, Reversing a Recent Trend But With Disparity Among Fixed-Income Market Sectors; municipal traders highest have highest total compensation among fixed-income sectors, (National Bonus Trends by Positions Trader Compensation – Section IV)[7]**

  The average median 2014 salary across fixed-income asset classes was $178,745 (above the $140,375 in 2012, $112,000 in 2011, $120,142 in 2010, $129,000 in 2009 and the first year's survey of $125,000) and bonus $170,047 (lower than the $278,397 in 2012)[8] for all senior traders. There was dispersion above and below that bonus average depending on the market sector – municipal, corporate, money market, securitization and Federal agency/government - from over $250,000 for municipal traders to $125,000 for agency traders. Where sufficient data were available for the market sector, data were provided for mid-level and entry level traders, as well. There was sufficient reporting to compute data for most sectors at the mid-level trader classification, and for entry-level municipal traders by compensation type and for municipal, agency and money market entry-level traders,

  For the fourth consecutive survey, a statistically meaningful number of firms reported paying traders commissions as well as bonus and salary. The average median senior trader level commission across markets among the firms that paid commissions was $181,662 compared to 263,574 in 2012, $361,151 in 2011 and $240,507 in 2010). Frequently, firms paying commissions did not pay salaries. (Note that only firms paying a commission were included in the trader commission metrics, and not all firms were included in the commission statistical calculations.)

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[6] Note that any discrepancy between the multi-year table bonus comparison (Section III-A) and this year's Compensation Survey (Section III) results would reflect differences in 2013-14 bonus data as reported in this year's Compensation Survey, and the Section III-A which reflects bonus data from the entire survey history period encompassing the four previous surveys. The multi-year comparisons are based on Section III-A table results. The same comment holds for the multi-year salary table found in Section III-B.

[7] There may be a small number of firms that provided aggregate trader compensation by position data but did not provide a response to this section in which trader compensation is segmented by market sector, which would explain any small discrepancies in trader data between the two sections (Sections III and IV).

[8] Comparisons between this year and previous years' survey results should be made with care. The survey populations (or firms responding to the survey among years) differ slightly year-to-year. That is, a small number of some firms that participated this year did not participate last year and *vice versa*.

Average median total senior level trader compensation (sum of salary, bonus and commission) across sectors for senior traders was $439,740 ranging from $316,148 for money market traders, to $579,278 for senior municipal traders to compared to $441,000 in 2012 ranging from $267,500 for money market traders to $500,000 for MBS/ABS traders. Average median total senior level trader compensation in 2011 was $394,090, ranging from $176,000 in the money market sector to $447,759 in the municipal sector in 2012. Average median total senior level trader compensation in 2010 was $495,688, ranging from $240,000 in the money market sector to $685,000 in the ABS/MBS sector in 2012.[9] (See Methodology Annex for the definition of "total" compensation.)

- **Range of Payouts on Trades: Concentration in the 30% to 40% Range, More Between 35% to 40% (Compensation Policies – Section V)**

Total Trades (both primary and secondary trades)
Responses indicate a concentration of compensation practices on trade payouts to sales professionals from net transaction/trade revenues[10] between 30% and 40% in the 2015 BDA Survey, less dispersion, and a higher average payout than in the previous survey. Most middle-market firms indicated a 35% to 40% range on all trades (primary and secondary market) on institutional trades compared to most firms indicating payouts in the 30% to 35% range in the previous Compensation Survey. Retail payouts were more concentrated in the 35% to 40% in this year's survey for all trades as was the case in the prior Compensation Survey.

Secondary Market Trade Payouts
Firms reported a 25% to 50% range of institutional secondary market ("off the run") trade payouts than in the prior survey. The most typical responses were between 35% to 40% across market sectors. Both trends were similar to the prior survey results. Middle-market firms indicated retail secondary market trade payouts were evenly distributed between above 35% and below 35% across fixed-income market. In the previous survey, retail secondary market trade payouts were concentrated between 30% and 40% with taxable market payouts typically 30% to 34% and municipal trade payouts 35% to 40%.

Institutional Primary Market Trade Payouts: Taxable
The middle-market dealer firms responded to primary or new issue market retail trade payouts with a narrower range of responses than in the previous survey. The middle-market firm responses were concentrated in the 35% to 40% "bucket."

[9] More generally, apparent inconsistencies between the sum of the average commission, bonus and salary relative to average total compensation reflects the inclusion of all firms in the "total" compensation calculation but only those firms that pay commissions (bonus) in the commission (bonus) averages. As noted above, some firms will pay a bonus (more frequently) or a commission but not both a bonus and commission. See the Methodology annex for a fuller explanation.
[10] A small number of firms used alternative metrics for payout based on a firm-wide calculation of profits and individual production volume rather than on a transaction basis and are excluded from this calculation.

Primary Market Trade Payouts: Municipal
2015 Compensation Survey: About 43% reported institutional negotiated municipal bond sale payouts above 35% compared to 57% below 25% payouts (with minimal responses between 25 and 35%). In the competitive sales segment, about 50% reported institutional municipal sales 35% or more, 33% below 25% and 17% reporting between 25% and 35%. Retail primary market competitive sales payouts clustered at or above 35% while half of the responses were above (and half below) 35% in the negotiated sector.

Public Finance Banker Payouts
There was a wide range of practices regarding public finance banker payouts (less than 5% to 60%) with average higher payouts on negotiated sales with a median of 30% for negotiated municipal bond sales and 18% for competitive sales. Among firms that do not distinguish between competitive and negotiated sales, the average payout was in the 25% range with responses ranging from 12% to 33%.[11]

Trader/Underwriter Payouts
For traders/underwriters, the median payout was 5% for negotiated and 12% for competitive trades. For those firms that did not distinguish payout policies between competitive and negotiated sales, payout compensation averaged 13% (median).

- **Cash Most Common Form of Trader Bonus Pay (Compensation Policies – Section V)**
  Of those reporting such information in 2015 (this year's survey), virtually all middle-market firms paid institutional traders cash bonuses, about 28% paid an equity bonus, and 17% indicated "other". Retail trader bonuses were paid a cash bonus with none responded an equity bonus. (Fewer firms reported retail trader bonus information than institutional trader bonus information.)

- **Most Firms' Sales Professionals are Paid Commission Only (Compensation Policies – Section V)**
  Dealer firms paid their sales force on a commission only basis in 2015 at approximately 71% (compared to 62% in 2013 and 70% in 2012) of the reporting middle-market fixed income dealer firms and a combination of salary/bonus and commission is paid at 14% (15% in 2012 and 2013 as well). That is, 85% paid their sales force commissions, and 15% of the dealer firms paid their sales force salary/bonus only.

- **Dealer Firms Indicate Bonus Metrics Trends Focused on a Combination of Objective and Subjective Criteria, a Shift From More Diverse Practices Across the Middle-Market Firms Weighted Towards Objective and Measurable Criteria (Compensation Policies – Section V)**
  The majority of firms pay bonuses across professions in the sales, trading, investment banking and public finance groups based on a combination of measurable objective criteria and subjective criteria in 2014. Compared to the prior survey, there was a shift away from basing a bonus on only quantifiable/objective criteria or subjective criteria. The trend marked a significant move away from subjective criteria. It should be kept in mind that, while the

[11] There were insufficient responses to report results on the taxable investment banking side.

survey responding middle-market firms are generally year-over- year, certain firms enter and exit the survey population from year to year.

In this year's survey, 83% base bonus compensation on a combination of objective and subjective criteria across all professional categories, e.g. sales, trading, public finance etc. The highest percentage of firms reporting bonus based on objective criteria was for public finance bankers (50%). The highest percentage of firms reporting bonus based on subjective criteria was for public sales managers (14%).

- **Most Firms Have Deferred Compensation Programs (Deferred Compensation/Retirement Programs – Section V)**
  Most firms, approximately 85%, (91% in 2011, 2012 and 2013) have deferred compensation retirement programs and those that do not have such programs generally offer profit sharing. The deferred compensation is generally based on a formula rather than a fixed amount. This year the formulas were typically (but not always) tied to employee contribution levels (e.g. 50% or 100%), generally up to a maximum employer contribution level. These responses were consistent with the prior survey.

- **Staffing Growth for 2015 (Revenue & Staffing Growth Trends – Section VI)**
  Unlike some other sectors of the financial services industry, middle-market fixed-income dealer staffing reported either increasing or flat staffing across market functional and departmental areas in 2015. These trends are consistent with the reported average higher FTE levels among survey respondents in 2015 compared to 2014. Despite reported financial staffing cuts especially at some large global banks, the majority of the dealer firms expected the staffing level to stay the same for 2015. The survey responses indicated the greatest proportion of planned staffing increases in revenue generating areas or profit centers, institutional sales (43%) and trading (43%) followed by public finance (33%). Reflective of the increased regulatory requirements, 28% of the firms expect compliance staffing increases. Also, 28% expect an increase in the market strategist and research function. There was no indication of a net decline in any department among the survey participants.

- **Revenue Trends: Firms Reported Weaker Revenue Across Most Sectors in 2014; Higher Revenues Expected in 2015 (Revenue & Staffing Growth Trends – Section VI)**
  Although the revenue mix diverges among the middle-market firm participants and reporting total fixed-income revenue increases for 2014, the firms' average response was that the municipal bond, government and securitization product sectors had revenue declines in 2014, while there was an equal distribution among, increased revenue, decreased revenue and no change responses for the corporate bond market sector. These 2014 revenue trend responses may help explain a decline in average trader bonuses across market sectors noted above.

  Firms had a much more upbeat view for 2015. The majority of the firms reported revenue increase expectations across fixed-income product sectors in 2015 by wide margins.

  The municipal market accounted for nearly half of the firms' trading revenue (45%), followed by corporate (26.5%) and agencies (9.5%) based on the median response. There were variations among the firms' trading focus as reflected in the maximum revenue by sector percentage response.

- **Operations and Technology Expenses Trending Lower Longer Term (Technology & Operations Expenses – Section VII)**
  Middle-market firms have generally reduced operating expenses significantly as a percentage of fixed-income revenues between 2007 and 2014 though with some year-over-year fluctuations, according to most of the Compensation Survey's statistical measurements. Operating, technology and Bloomberg expense ratios were much lower with "other data providers" higher. In 2014, operating expense ratio was flat, Bloomberg expense lower, and technology slightly higher and other fixed income data ratios more significantly higher. Most firms (80%+ in 2015 and 90+% in prior years) do not outsource the technology function.