

# HKE<sub>x</sub> GROUP STRATEGIC PLAN 2013-2015

## Overview

Our Strategic Plan 2013-2015 builds upon the growth-oriented strategy of the past 3 years and aims to take the Group into a new phase of transformational development in the next 3 years.

### Mission

We aim to be the global exchange of choice for our China clients and our international clients seeking China exposure.

### Vision

With the continuing growth of HKE<sub>x</sub>'s core business as a foundation and with the successful acquisition of the LME Group as a catalyst, our vision is to build HKE<sub>x</sub> into a leading global vertically-integrated multi-asset class exchange and prepare ourselves for the managed but accelerating opening of China's capital account.

### Highlights

Our plan has 2 key components: business strategy, and platform and infrastructure strategy.

In terms of business strategy, we will seek to build out a horizontally integrated business across the following asset classes:

- **Cash Equity:** Continue to grow this core business line by seeking additional China and international listings and by expanding access products such as ETFs particularly in RMB; continue our efforts to achieve a breakthrough in mutual market access via partnership with Mainland counterparties;
- **Equity Derivatives:** Build on our existing business by offering new products and providing new services by ourselves or in partnership with others;
- **FIC:** This is largely new and will be mainly driven by RMB internationalisation and global regulatory changes; and
- **Commodities:** Leverage the acquisition of the LME Group to build an extensive commodities platform.

Within each asset class, we also seek to achieve vertical integration from products through trading to clearing.

In terms of platform and infrastructure strategy we will seek to consolidate and further modernise our currently diverse trading and clearing platforms, and to build greater connectivity with local, Mainland and international market communities.

## Background

### Recap of Strategic Plan 2010-2012

The 2010-2012 Strategic Plan aimed to enhance our global competitiveness and capture opportunities from the continuing opening of Mainland market. It had 3 main themes:

- **Core Strategy:** These initiatives aimed to strengthen our existing business by enhancing efficiency and improving the market structure. Key achievements included: being ranked the world's number one IPO market by funds raised in 2010 and 2011, streamlining the listing process, successfully implementing new trading hours, and strengthening risk management capital adequacy.

- **Extension Strategy:** Under this strategy, our objective was to build a platform for higher performance. We achieved key components of this strategy, including: the introduction of AMS/3.8, the completion of the TKO Data Centre, and the offering of Hosting Services.
- **Expansion Strategy:** This prepared us to enter new asset classes and geographies. Key milestones achieved included: offering RMB products, establishing the BRICS Exchanges alliance and the Mainland equity derivatives joint venture, the CESC, launching our new clearing house for OTC derivatives, and crucially, successfully acquiring the LME Group.

### Historical Trend of Our Development

We view the Group's development as a story in 3 chapters.

- **Chapter One:** This chapter is the listing of Mainland enterprises in Hong Kong to raise capital from international investors. This chapter is continuing but is relatively mature.
- **Chapter Two:** Anticipating the continued relaxation of Mainland capital controls, in this chapter we attract Mainland investors by providing an array of RMB-denominated products that will give them currency neutrality. We expect the growing presence of Mainland investors over time to increase the level of trading in our market and attract a wider range of international companies to list in Hong Kong. Chapter Two has already commenced and is gradually building, driven by the pace of the capital account opening.
- **Chapter Three:** We have at the same time begun Chapter Three, in which we attract a broader range of Mainland and international players to deal on the Group's trading and clearing platforms, not only in equity but extending into fixed income, currency and commodities. Our acquisition of the LME Group is a key catalyst for this Chapter and, by accelerating RMB internationalisation and Mainland capital account opening, could in turn further facilitate the development of Chapter Two.

### Strategic Outlook

#### Continuing Mainland Opening

Looking at the next 3 years, we remain confident in the structural opportunities arising from the opening of the Mainland economy. Historically, since the mid-1990s, our growth has been fuelled by the Mainland's economic growth and its increasing utilisation of Hong Kong's equity capital markets. As the Mainland's growth continues to evolve, we expect the Mainland's needs to shift increasingly from capital formation to investment diversification and risk management across all asset classes, reflecting the country's transformation from an importer of capital to an exporter of capital. A presence in multiple asset classes will position us to serve the Mainland economy across a broad front during this evolution.

#### Commodities as a Breakthrough

We view commodities as the asset class most likely to see a breakthrough in this transformation. This is because of the Mainland's continuing structural demand for raw materials, its extensive experience in the international trade of commodities and the growing need to reform its existing capital control regime which is increasingly constraining the further development of Mainland commodity markets. LME will spearhead the Group's efforts in this asset class. We will respond to emerging opportunities, and seek to extend the resultant benefits across other asset classes. In this process we expect to deepen our relationships with the Mainland exchanges and clearing houses, moving towards partnership and eventually mutual market access.

In order to support business development flowing from the above opportunities, as well as to forestall any competitive threats, we will continue to invest in infrastructure and technology. We will aim to deliver a highly competitive suite of systems and platforms across our business lines. We will also ensure that our market microstructure adapts to evolving market conditions.

## Business Strategy

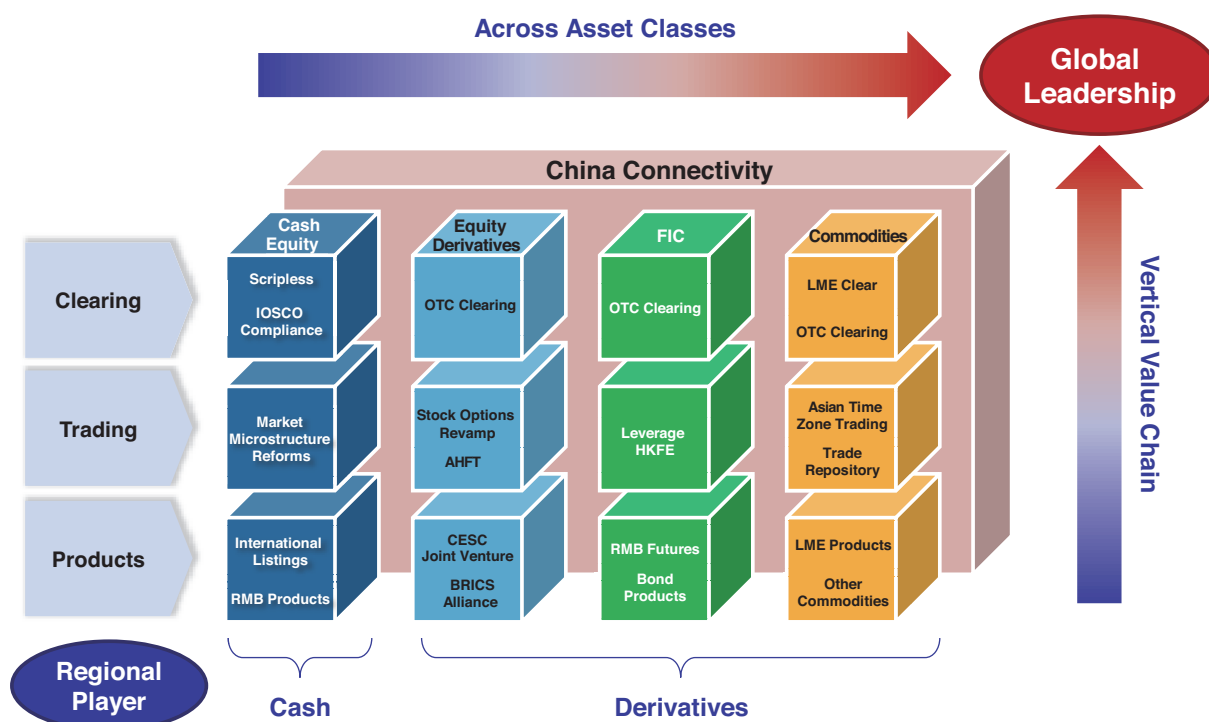
Our business strategic concept encompasses 2 dimensions of integration: horizontal integration across asset classes, and vertical integration through the value chain.

In the horizontal dimension, we have identified 4 asset classes: cash equity, equity derivatives, FIC, and commodities. We will seek to build upon our existing core asset classes of cash equity and equity derivatives, and expand into new asset classes by using commodities as a catalyst, leveraging RMB internationalisation, and seeking mutual access across the Hong Kong and Mainland markets. Our cross asset class strategy will reap the benefits of synergy and link contiguous market communities.

Within each asset class, we also aspire to offer services along the value chain, from products through trading to clearing. We believe this vertical integration strategy, with an emphasis on clearing, will allow us to achieve the maximum degree of synergy, defend our existing businesses, and gain entry to new businesses that require clearing services and to new relations with the mainland of China.

Throughout our horizontal asset classes and vertical business segments, we seek to build the critical connectivity with the Mainland's markets in order to benefit from the accelerated opening of its capital account.

The above concept and the initiatives under each asset class (as detailed in the rest of this section) are shown in the diagram below:



### Cash Equity Strategy

Our cash equity business is relatively mature, but we believe this segment could undergo structural uplift in velocity and trading volumes as and when Mainland investors are progressively permitted to invest offshore. Our cash equity strategy is to better position us to take advantage of the expected lowering of Mainland capital account barriers.

In terms of products, as a continuation of our Chapter One strategy, we will continue seeking to attract Mainland-related issuers, positioning as their primary offshore capital formation centre. Recent developments such as B share to H share conversion and the easing of offshore listings by Mainland regulation are expected to provide renewed impetus. At the same time, to prepare for the increasing participation of Mainland investors, we will continue to reach out to international issuers and enlarge our RMB product suite. We will further develop our ETF segment as this is a potential facilitator of RMB internationalisation and mutual access with Mainland markets.

In terms of trading and clearing, we will seek further improvement in our secondary market microstructure, implement the scripless market, and ensure our clearing houses' compliance with evolving international standards. We will also explore, together with Mainland counterparties, the feasible model for mutual market access, which, as we view, will be a significant catalyst for the structural change in Hong Kong's capital market and will position us as an interface between the international and Mainland market environments.

### Equity Derivatives Strategy

In our equity derivatives strategy, we aim to offer an extensive product suite across Hong Kong and Mainland underlying securities. Leveraging the CESC, we will roll out a range of cross-market and A share-related products, including indices and derivatives. Our BRICS Exchanges alliance will also develop a range of international benchmarks.

To reap the benefit of new and existing products, at the trading level we will seek to improve volumes by launching a revamp of our stock options market, and introducing AHFT.

At the clearing level, through our OTC clearing house we will seek to tap a new asset class – OTC equity derivatives on Hong Kong, Mainland and regional underlyings. We will again seek to improve connectivity with the Mainland market via partnership and other means.

### Fixed Income and Currency Strategy

The FIC asset class is largely new to HKEx. New factors such as international regulation mandating the shift to central counterparty clearing of OTC derivatives, and RMB internationalisation, offer us an opportunity to enter this asset class.

We have a two-fold strategy. The first initiative is the launch of on-exchange RMB futures. Although trading at first will be slow, reflecting the low volatility of the RMB exchange rate, it should pick up as RMB internationalisation proceeds. We will also continue to explore other product opportunities, such as bond index products and RQFII ETFs on bonds, where appropriate in partnership or cooperation with others.

Secondly, leveraging emerging regulatory requirements, our OTC derivatives clearing house will provide clearing services, initially for interest rate swaps and non-deliverable forwards in RMB and other appropriate currencies. This initiative can be extended to other FIC products, and will lead over time to new revenue streams. It will also bring in new bank-related participant groups to whom we can provide other products and services.

## Commodities Strategy

Building on the deep liquid markets of LME, we will expand the existing business by lowering barriers for Asian particularly Mainland investors to access the LME market. Key initiatives include: facilitating easier cross-border access, developing Asian time zone trading and clearing, offering RMB clearing services, and extending LME's warehouse network into the mainland of China.

On the other hand, we will leverage the base metal platform and our proximity to the mainland of China as the largest global consumer of commodities to extend into other metals and commodities. By achieving this, we expect to build a broader commodities derivatives business.

We will also seek to realise the untapped potential in the business through commercialisation and modernisation. Key initiatives include enhancing the electronic trading platform and infrastructure, and expanding contract types.

To support the above initiatives, we will initially build a London-based clearing house to achieve self-clearing for base metals and extend this to enable Asian time zone clearing, RMB clearing, and clearing of other products relevant to Asian markets. We will also extend further along the value chain to provide OTC clearing and trade repository services for commodity derivatives.

## Platform and Infrastructure Strategy

The Group inherited a collection of different platforms, reflecting the history of its formation through merger. These platforms differ by application – from market data distribution to trading, clearing, risk management and depository – and by asset class. They vary greatly in terms of functionality, capacity and performance level, and some have support dependency on external parties. The aim over time is to develop next-generation platforms that fully meet global standards and converge onto a single technology platform for each application across asset classes. At the same time, in-house support capability will be strengthened through source code licensing arrangements and knowledge transfer with third-party platform vendors where applicable. However, given the life-cycle of the Group's platforms and market impact during transition, this process of consolidation and strengthening will take place over time.

The Group's TKO Data Centre will continue to play a key role in improving connectivity – not just within the Hong Kong market, but between the international environment and the mainland of China, and between the London and Hong Kong. The connectivity will be leveraged to facilitate implementation of the Mainland Market Data Hub in Shanghai for more efficient distribution of market data generated in Hong Kong and London to Mainland-based investors.

With TKO Data Centre facilities, consolidated trading and clearing platforms and improved connectivity with the mainland of China and internationally, the Group will be positioned to support business diversification and growth across asset classes.

## Conclusion

Building upon the strong foundation established under the previous strategic plan, over the coming 3 years we aim to consolidate recent investments, fill out HKE<sub>x</sub>'s capabilities as a vertically-integrated multi-asset class exchange of global reach, and begin to harvest the fruit of these efforts.

In our equity business, we expect to deepen Hong Kong's role as a leading listing market for Mainland and international companies and prepare ourselves for the greater participation of Mainland investors. In equity derivatives, we expect to establish new benchmarks with Mainland and international underlyings and leverage them for trading and clearing. In FIC, we expect to establish a solid base of business and participant community around our on-exchange RMB-related and OTC clearing initiatives. And in commodities we aim to enhance the existing LME business and make significant progress in the China dimension. These four pillars of achievements would transform HKE<sub>x</sub> into a comprehensive platform and consolidate its leading position among world exchanges.

## Key Initiatives

We have identified the following key initiatives under Strategic Plan 2013-2015:

Business Strategy
<b>Cash Equity</b> (1) Improve framework for and continue to attract international listings (2) Further improve quality of listing (3) Develop critical mass of products trading in RMB (4) Improve Cash Market microstructure (5) Implement scripless market (6) Explore feasible model for mutual market access via partnership with Mainland counterparties
<b>Equity Derivatives</b> (1) Leveraging the CESC joint venture, introduce further A share-related products (2) Launch stock options revamp (3) Introduce AHFT (4) Launch Phase 2 of the BRICS alliance (5) Explore potential to clear OTC equity derivatives
<b>Fixed Income and Currency</b> (1) Launch and establish OTC clearing business (2) Build out RMB derivatives and bond-related product suite (3) Explore other potential opportunities to enter the FIC space
<b>Commodities</b> (1) Establish LME clearing house in London (2) Introduce Asian time-zone price-discovery and clearing (3) Launch OTC commodity derivatives trade repository and clearing (4) Expand Mainland participant base (5) Seek to establish LME-licensed warehouse network in China (6) Explore potential to extend LME's product suite into Hong Kong market
Platform and Infrastructure Strategy
(1) Fully establish the TKO Data Centre operation and hosting business (2) Implement Genium platform for equity derivatives trading, clearing and risk management (3) Develop and roll out the OMD system (4) Implement necessary infrastructure to facilitate connection of market platforms and corporate systems between Hong Kong and London (5) Fully establish Mainland Market Data Hub (6) Develop and roll out the OCG system (7) Define requirements for and commence development of the OTP system, initially to support cash trading as replacement of AMS (8) Conduct feasibility study for and commence implementation of Next Generation Clearing and Risk Management Systems