

# HKEX STRATEGIC PLAN 2016-2018

## Overview

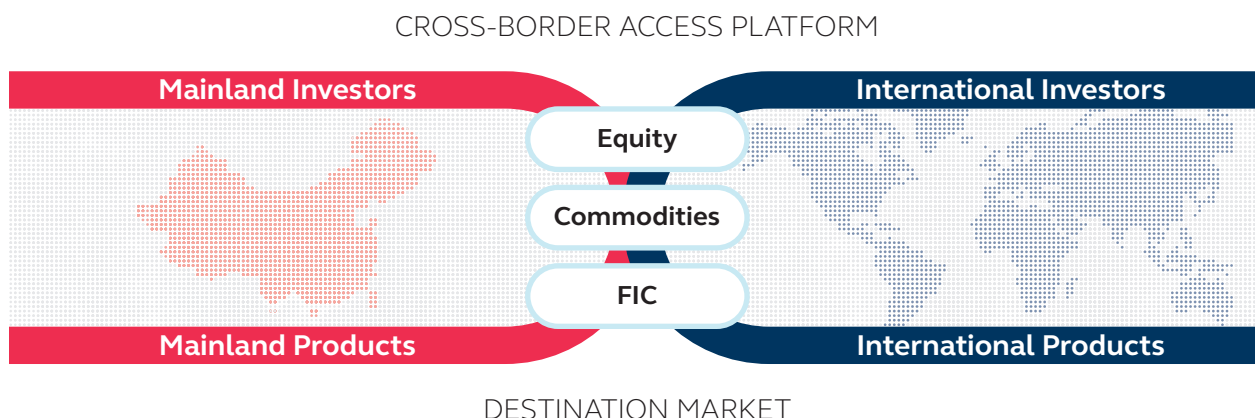
Hong Kong is entering a new phase as a leading international financial centre. The scale and depth of the world's interaction with Mainland China's markets and investors are being transformed by two-way capital flow opening, domestic reforms and RMB globalisation. While Mainland corporates begin to formulate their internationalisation blueprints, a large number of Mainland investors are starting to meaningfully enter the global financial markets for the first time, seeking investment opportunities and wealth diversification. At the same time, the Mainland markets themselves are changing, especially in commodities where an increasing need for the market to "physicalise" and internationalise has become apparent.

We believe that this new chapter in financial markets history presents Hong Kong and HKEX with a large number of compelling, even transformative opportunities in multiple asset classes. Building on our heritage as a leading cross-border access platform and as a destination market in our own right, we aim to expand and entrench this model across equity, commodities, fixed income and currency – becoming a true multi-asset platform that connects China with the world.

## Our Vision

**Connecting China with the World, we are Reshaping the Global Market Landscape.** We aim to be the global exchange of choice across asset classes both for our Chinese clients and our international clients seeking China exposure.

## Key Themes of our Strategic Plan 2016-2018



Our strategic goal in 2016-2018 is to extend and deepen HKEX's value proposition against the backdrop of Mainland China's accelerating capital market internationalisation. We see our value proposition as having two principal, inter-related facets, which will enable HKEX to:

- **Build the most effective platform for cross-border market access.** Building on the breakthrough of Stock Connect, we will seek to ensure that HKEX continues to offer the most competitive and convenient cross-border access platform for both our Chinese and international clients seeking exposure to each other's markets.

To achieve this, in 2016-2018 we will focus on expanding and scaling the "Connect" model to new asset classes; and modernising our core platforms and market microstructure to deliver an integrated trading and clearing solution that breaks down the barriers for cross-border capital flows.

- **Develop a unique destination market in Hong Kong for products with both Chinese and international relevance.** Mutual connectivity has led to the arrival of a vast group of investors from the Mainland on our doorstep along with the rising demand for a wider range of international products that they bring. At the same time, the launch of new products that provide exposure to Mainland China's development trajectory is set to attract more international investors to Hong Kong.

This confluence of international and Mainland investors and products represents, in our view, the most transformational opportunity in the 15-year history of HKEX, capable of structurally transforming the breadth, depth and global relevance of Hong Kong's markets. We see a unique opportunity for HKEX to build price discovery capabilities, benchmarks and risk management tools in fixed income, currency and commodities – asset classes in which Chinese and international liquidity will increasingly converge.

## Major Strategic Initiatives in 2016-2018

With these themes as its foundation, our 2016-2018 Strategic Plan features the following key initiatives, covering all 3 of our asset classes:

### Equity

- Grow and strengthen our core franchise as a compelling listing and fundraising venue;
- Significantly expand mutual connectivity: extend Shanghai-Hong Kong Stock Connect, launch Shenzhen-Hong Kong Stock Connect and launch "Primary Equity Connect";
- Launch new derivatives products in Hong Kong, with Mainland, Hong Kong and international underlying assets.

### Commodities

- Expand our suite of products both on the LME and in Hong Kong into adjacent commodities;
- Build a convenient channel for Asian liquidity to access the LME market and products, as a way to further "financialise" the LME;
- Develop a spot commodities trading platform in the Mainland market in order to service the real economy, with a view to producing and internationalising "Chinese benchmarks" as well as "physicalising" the Mainland commodities market using the LME model;
- Pursue cross-border connectivity with Mainland commodities exchanges and products.

### FIC

- Launch new exchange-traded derivatives in Hong Kong on RMB and onshore interest rates;
- Offer a broader product suite in OTC Clear, delivering tangible benefits to market users;
- Explore mutual market access with the Mainland in the institutional cash bond market through a "Bond Connect" scheme.

The following section elaborates on our asset class strategy.

## Business Strategy

We classify our business into 3 asset classes: Equity, Commodities and FIC. While our capabilities in each asset class are at different stages of development, they share an important advantage. We believe that our biggest strength – and the ultimate driver of our success – is our ability to deliver cross-border access between the Mainland and international markets, backed by a strong suite of investment, financing and risk management products that provide a unique blend of Chinese and international price discovery and risk management.

### Equity

In cash equity, we have already taken significant steps towards achieving this vision. In November 2014, we delivered a cross-border connectivity breakthrough, launching Shanghai-Hong Kong Stock Connect. Going forward, this gives us a tremendous opportunity to not only expand Stock Connect itself, but also to enhance our historically strong Hong Kong cash and equity derivatives franchise with new products that fulfil the needs of both our established international clients and relatively new pool of Mainland clients.

### Key Equity Initiatives

- Our core equity market is strong and remains a major engine of our business. To grow and strengthen our core listing franchise and retain our competitiveness as a world-leading fundraising venue, we will seek to implement reforms that will strengthen our listing regime and help us attract a wider range of issuers from more diverse economic sectors.
- In order to extend and enhance mutual connectivity, we will firstly seek to enhance the functionality of Shanghai-Hong Kong Stock Connect, launch Shenzhen-Hong Kong Stock Connect, and add ETFs, listed bonds and convertible bonds to the two Stock Connect schemes. Secondly, we will work with regulators in Hong Kong and the Mainland to relax trading restrictions including quotas, eligible securities, eligible investors, holiday trading, and stock borrowing and lending. Our third area of focus will be to enable investors to subscribe to primary market offerings using a “Primary Equity Connect” structure, which we believe will fundamentally change Hong Kong’s proposition as a listing venue for international issuers, and offer new diversification opportunities for our Mainland investors.
- Finally, to help cross-border investors better manage their risks, we will seek to expand our derivatives suite, covering Mainland China, Hong Kong and international underlying. This will include listing A-share index benchmarks, adding sector-specific products, and exploring international benchmark derivatives in Hong Kong.

### Commodities

In Commodities, our goal is to reinforce and extend the global price benchmarks that we own today through the LME, and to draw additional liquidity into those products from both the international and Mainland markets – especially from new participants outside of the physical metals value chain.

At the same time, we will pursue a breakthrough in the Mainland commodities market. To do this, we will focus on the physical foundations of the market, where our strengths position us well to address market needs by developing stronger domestic benchmarks and, ultimately, cross-border access with the international commodities markets.

## Key Commodities Initiatives

- Firstly, we intend to expand our Commodities product complex in London and Hong Kong into contiguous areas where we see significant market demand, including precious and ferrous metals, as well as value chain products in the base metals delivery chain and in the steel complex. We also plan to expand LME Clear's service into the large and important OTC-traded market.
- To bring untapped Asian liquidity to the LME, we will list LME products in Hong Kong in various forms in the near future. In the medium- to long-term, we are undertaking preparatory work for "London-Hong Kong Connect", a scheme that connects the LME and HKFE more directly. Initially, the scheme will focus on "Westbound" trading and clearing of LME products for HKFE Participants. This will facilitate access to the LME for Mainland QDII2 investors, as well as Asian corporates seeking to manage their international metals exposure.
- In the Mainland market, we will explore the creation of a Mainland spot commodity trading and financing platform as a service to key stakeholders, including investors, warehouse operators, physical producers and consumers, and financing banks. With the trusted status of HKEX and the unique expertise of the LME in the physical metals market, we anticipate being able to develop credible and internationally relevant onshore benchmarks that are firmly grounded in the physical market.
- After the linkages are in place for "London-Hong Kong Connect", we plan to extend its scope at a subsequent stage by establishing a mutually beneficial Mainland-Hong Kong "Commodities Connect" mechanism that expands the bridge between the two markets and makes onshore commodities derivatives accessible to Hong Kong and international participants.

## FIC

In FIC, the internationalisation of the RMB has given us a unique opportunity to entrench Hong Kong as a gateway for cross-border fund flows and as a risk management venue. As international investors look to increase their exposure to RMB assets, we believe they will naturally demand interest rate and currency derivatives to manage their risk, and we expect Mainland investors coming out into the international markets will want the same kind of products. Our aim in 2016-18 is therefore to build the platform and product suite that facilitates these interactions as the Mainland FIC market continues to open up.

## Key FIC Initiatives

- Building on our existing USD/CNH Futures contract, we plan to launch more benchmark derivatives with China relevance in Hong Kong, including additional RMB currency products as well as derivatives on onshore interest rates.
- To complement our listed derivatives offering, we also plan to launch a number of new products and services in OTC Clear, including deliverable foreign exchange forward and swap contracts, cross-currency swaps, OTC currency options and client clearing.
- We believe that stimulating cross-border capital flows in the underlying RMB cash bond market is an important prerequisite for our long-term success in FIC derivatives. To facilitate these flows, we will explore the creation of a "Bond Connect" scheme to provide cross-border cash bond trading and settlement connectivity with China's major onshore bond market infrastructures, with a focus on the institutional bond market.

## Platforms and Capabilities

We will support our Business Strategy by developing a strong client relationship management culture throughout the Group and rolling out targeted platform upgrades and enhancements. On the market microstructure front, we will continue to pursue enhancements that help improve efficiency for our market participants, ease access and reduce risks.

### Client and Marketing Services

To better understand and cater for all of our market participants, we are developing a comprehensive client relationship management function. As part of this, we will also undertake a review of our market maker and other incentive schemes to ensure that we are achieving the best value for our investments and optimising the provision of liquidity, particularly in connection with new products.

### Platform Enhancements

In Hong Kong, we are undertaking two major projects to upgrade the core systems in our Cash Market. Firstly, the Orion Trading Platform will be introduced to replace the current securities trading system, thus complementing the Orion Market Data and Orion Central Gateway systems as the final building block of our Cash Market trading infrastructure upgrade. Secondly, we will commence the phased replacement of the current system for cash clearing, starting with its clearing, risk and collateral management elements, before replacing the central securities depository function with a new system.

Following the opening of our new primary data centre in Hong Kong in 2012, we plan to consolidate our back-up data centres to provide the necessary capacity for our future business needs. We will also further leverage the capabilities of our recently launched Mainland Technology Centre facility to support IT development across the Group. Information security remains a key focus for our business, and we will invest to ensure that our capabilities in this regard are up to date and fit for purpose in both Hong Kong and London. In addition, we are in an era of rapid advances in technology, and these advances are capable of dramatically reshaping the financial industry. We will invest to stay on top of emerging trends in financial technologies to protect our core competitiveness.

Finally, to fully align our evolving platform capabilities with the delivery of our business strategy, we have created a dedicated Platform Development Division that will consolidate our development resources, providing us with greater agility and efficiency going forward.

### Market Microstructure and Regulation

In the area of market microstructure in Hong Kong, a number of initiatives are already under development following market consultation, including the Closing Auction Session and Volatility Control Mechanism. Initiatives we intend to pursue in 2016-2018 include new capabilities in pre-trade risk management, stock borrowing and lending, remote Participantship, a new hedge exemption regime for derivatives position limits, and new after-hours and holiday trading arrangements.

In London, we intend to explore measures to further enhance access to the LME and improve transparency. We also plan to continue delivering the LME Liquidity Roadmap.

Across our clearing houses in both London and Hong Kong, we will continue to review our risk management measures to ensure an optimal balance of market security and capital efficiency for our Participants. In our Cash Market, we will continue to review our existing margin model with a view to implementing dynamic and product-specific margin requirements. In our Derivatives Markets, we will continue reviewing our margin and collateral arrangements, seeking to widen the range of collateral we accept. We will also explore portfolio margining in selected product suites.

On the regulatory front, we will continue to adhere to international regulatory requirements emanating from regulatory authorities in the US, Europe and other relevant jurisdictions, as well as local regulators in our markets.

## Conclusion

Over the past several years, we have progressively prepared ourselves for Mainland China's accelerated opening of its financial markets and the internationalisation of the RMB by expanding our asset class reach and consolidating our vertically integrated business model. Those achievements now enable us to pursue a number of ambitious but important initiatives which will shape HKEX's future.

In our Strategic Plan 2016-2018, we intend to:

- Build the most effective platform for cross-border market access, facilitating capital flows into and out of Mainland China across multiple asset classes; and
- Develop a unique destination market in Hong Kong for products with both Chinese and international relevance, focusing on a compelling product suite that serves the needs of our expanding client base.

In our Equity business, we will focus our efforts on strengthening our listing regime, growing and entrenching Shanghai-Hong Kong Stock Connect, launching Shenzhen-Hong Kong Stock Connect, exploring "Primary Equity Connect" and introducing new derivatives in Hong Kong that are actively traded by both Mainland and international investors.

In Commodities, we believe that true cross-border linkages between the Mainland and international commodities markets require closer alignment between physical and financial market participants. We are therefore planning to pursue initiatives to further "financialise" the LME, and will explore developing a Mainland spot commodities platform capable of "physicalising" Mainland market benchmarks.

Finally, in FIC we are preparing a suite of derivatives focusing on China-related currency and interest rates as a valuable tool for investors looking to hedge their growing exposures in both areas. We will also seek to achieve a cross-border breakthrough in cash bond trading through "Bond Connect".

We believe that these initiatives will build on HKEX's achievements to date, and position us for continued leadership among global exchanges during this historic time in the world economy.