The Future for European Stock Exchanges

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The Future for European Stock Exchanges

Overview

1) Business Models

2) Industry Structure

3) Linkages and Mergers

4) Examples

5) Conclusions
The Future for European Stock Exchanges

1) Business Models
Business Models

Big Markets

- Revenues in Cash Markets Limited by GDP Growth
Business Models

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- Revenues in Cash Markets Limited by GDP Growth
- High Derivatives Growth
Business Models

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- Revenues in Cash Markets Limited by GDP Growth
- High Derivatives Growth
- **Clearing & Settlement Attractive**
Business Models

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- **Strong Vested Interests**
Business Models

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- Revenues in Cash Markets Limited by GDP Growth
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- **High Regulatory Intervention**
Business Models

Big Markets

- Revenues in Cash Markets Limited by GDP Growth
- High Derivatives Growth
- Clearing & Settlement Attractive
- Strong Vested Interests
- High Regulatory Intervention
- **Small Companies Dilemma**
Business Models

Alternative Businesses: Strengths and Benefits

- Experience/Knowledge
Business Models

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- Experience/Knowledge
- Neutral Provider
Business Models

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- Experience/Knowledge
- Neutral Provider
- Market Management Expertise
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- Brand Exploitation Possible
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- Experience/Knowledge
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- **Non-Correlated Source of Revenues**
Business Models

Alternative Businesses: Difficulties and Risks

- Lack of Experience/Knowledge
Business Models

Alternative Businesses: Difficulties and Risks

- Lack of Experience/Knowledge
- Vested Interests of Members/Users
Business Models

Alternative Businesses: Difficulties and Risks

- Lack of Experience/Knowledge
- Vested Interests of Members/Users
- **Competition with Members/Users**
Business Models

Alternative Businesses: Difficulties and Risks

- Lack of Experience/Knowledge
- Vested Interests of Members/Users
- Competition with Members/Users
- **Reputational Risk**
Business Models

Alternative Businesses: Difficulties and Risks

- Lack of Experience/Knowledge
- Vested Interests of Members/Users
- Competition with Members/Users
- Reputational Risk
- **Branding Tension**
Business Models

Alternative Businesses: Difficulties and Risks

- Lack of Experience/Knowledge
- Vested Interests of Members/Users
- Competition with Members/Users
- Reputational Risk
- Branding Tension
- **Too Important to Fail?**
Business Models

New Markets

- Large Potential for New Companies
Business Models

New Markets

- Large Potential for New Companies
- Lower Cost Base
Business Models

New Markets

- Large Potential for New Companies
- Lower Cost Base
- Longer Investment Period
Business Models

New Markets

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- Lower Cost Base
- Longer Investment Period

- Where Are You?
The Future for European Stock Exchanges

2) Industry Structure
Industry Structure

Do European Exchanges face Competition?

- Single Municipal Exchange
Industry Structure

Do European Exchanges face Competition?

- Single Municipal Exchange
- Multiple Competing Municipal Exchanges
Do European Exchanges face Competition?

- Single Municipal Exchange
- Multiple Competing Municipal Exchanges
- **Single National Exchange**
Industry Structure

Do European Exchanges face Competition?

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Industry Structure

Do European Exchanges face Competition?

- Single Municipal Exchange
- Multiple Competing Municipal Exchanges
- Single National Exchange
- Multiple Competing National Exchanges
- **Multiple Competing ATSSs, ECNs, etc**
Industry Structure

Do European Exchanges face Competition?

- Single Municipal Exchange
- Multiple Competing Municipal Exchanges
- Single National Exchange
- Multiple Competing National Exchanges
- Multiple Competing ATSs, ECNs, etc
- Single Pan-European Exchange
Industry Structure

Some Key Factors affecting Competition in Trading

- **Network Externality** - Order Flow attracts Order Flow
Industry Structure

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- Economies of Scale
Industry Structure

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- Automation
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- Network Externality - Order Flow attracts Order Flow
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- Different Trading Preferences
Industry Structure

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- Network Externality - Order Flow attracts Order Flow
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- **Internalisation**
Industry Structure

Some Key Factors affecting Competition in Trading

- Network Externality - Order Flow attracts Order Flow
- Economies of Scale
- Automation
- Different Trading Preferences
- Internalisation
- **Disintermediation**
Industry Structure

Overcoming the Order Flow Externality

- Superior Trading/Routing Technology
Industry Structure

Overcoming the Order Flow Externality

- Superior Trading/Routing Technology
- New Group of Customers
Industry Structure

Overcoming the Order Flow Externality

- Superior Trading/Routing Technology
- New Group of Customers
- **Conducive Regulatory Environment**
Industry Structure

Overcoming the Order Flow Externality

- Superior Trading/Routing Technology
- New Group of Customers
- Conducive Regulatory Environment
- **Inability/Lack of Incentive for Incumbent to React**
Industry Structure

Overcoming the Order Flow Externality

- Superior Trading/Routing Technology
- New Group of Customers
- Conducive Regulatory Environment
- Inability/Lack of Incentive for Incumbent to React
- **Significantly Lower Pricing/Better Service**
Industry Structure

Overcoming the Order Flow Externality

- Superior Trading/Routing Technology
- New Group of Customers
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- Inability/Lack of Incentive for Incumbent to React
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- **Incentives to Use New System**
Industry Structure

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- **Very Dissatisfied Customers**
Industry Structure

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- Very Dissatisfied Customers
- **Full Access to Clearing/Settlement**
The Future for European Stock Exchanges

3) Linkages and Mergers
Linkages and Mergers

Potential Functions to Integrate

- Listing
Linkages and Mergers

Potential Functions to Integrate

- Listing
- Information Dissemination
Linkages and Mergers

Potential Functions to Integrate

- Listing
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- Order Routing
Linkages and Mergers

Potential Functions to Integrate

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- Order Routing
- Trading
Linkages and Mergers

Potential Functions to Integrate

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- Information Dissemination
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- **Central Counter-Party Clearing**
Linkages and Mergers

Potential Functions to Integrate

- Listing
- Information Dissemination
- Order Routing
- Trading
- Central Counter-Party Clearing
- **Settlement**
Linkages and Mergers

Potential Functions to Integrate

- Listing
- Information Dissemination
- Order Routing
- Trading
- Central Counter-Party Clearing
- Settlement
- Marketing
Linkages and Mergers

Different Contractual Procedures Possible

- Linkage
Linkages and Mergers

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- Linkage
- Joint Venture
Linkages and Mergers

Different Contractual Procedures Possible

- Linkage
- Joint Venture
- **One Exchange Purchases from Other Exchange**
Linkages and Mergers

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- Third-Party Provision
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- Alternative Business Relationship
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- \textbf{Share-Holding}
Linkages and Mergers

Different Contractual Procedures Possible

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- Joint Venture
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- Alternative Business Relationship
- Share-Holding
- **Merger**
Linkages and Mergers

Potential Benefits

- **Economies of Scale**
Linkages and Mergers

Potential Benefits

- Economies of Scale
- Easier Access to More Markets
Linkages and Mergers

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- Greater Liquidity by Pooling Order Flow
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- **Greater Visibility**
Linkages and Mergers

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- Greater Visibility
- **Lower User Costs:**
Linkages and Mergers

Potential Benefits

- Economies of Scale
- Easier Access to More Markets
- Greater Liquidity by Pooling Order Flow
- Greater Visibility
- Lower User Costs: Technology
Linkages and Mergers

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- Lower User Costs:
  - Technology
  - Standards
Linkages and Mergers

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- Easier Access to More Markets
- Greater Liquidity by Pooling Order Flow
- Greater Visibility
- Lower User Costs:
  - Technology
  - Standards
  - Regulation
Linkages and Mergers

Most Linkages Have Failed

- Over-Optimistic IT Assumptions – Cost & Speed
Linkages and Mergers

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- Exchange Governance Implications
Linkages and Mergers

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- Over-Optimistic IT Assumptions – Cost & Speed
- Exchange Governance Implications
- **Lack of Credibility of Contractual Commitments**
Linkages and Mergers

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- Over-Optimistic IT Assumptions – Cost & Speed
- Exchange Governance Implications
- Lack of Credibility of Contractual Commitments
- Cross-Jurisdictional Legal Issues
Linkages and Mergers

Most Linkages Have Failed

- Over-Optimistic IT Assumptions – Cost & Speed
- Exchange Governance Implications
- Lack of Credibility of Contractual Commitments
- Cross-Jurisdictional Legal Issues
- Still Relatively Small
Linkages and Mergers

M&A: Very Difficult Both to Agree & to Implement

- Technological
Linkages and Mergers

M&A: Very Difficult Both to Agree & to Implement

- Technological
- Commercial
Linkages and Mergers

M&A: Very Difficult Both to Agree & to Implement

- Technological
- Commercial
- Legal
Linkages and Mergers

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- **Regulatory**
Linkages and Mergers

M&A: Very Difficult Both to Agree & to Implement

- Technological
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- Regulatory
- **Political**
Linkages and Mergers

M&A: Very Difficult Both to Agree & to Implement

- Technological
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- Political
- Cultural
Linkages and Mergers

M&A: Very Difficult Both to Agree & to Implement

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**But Still More Likely to be Successful than Linkages**
Linkages and Mergers

M&A: Lessons

- **Anticipated Technological Efficiencies take Time**
Linkages and Mergers

M&A: Lessons

- Anticipated Technological Efficiencies take Time
- Regulatory Efficiencies Difficult to Achieve
Linkages and Mergers

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- Retention of National Identities Possible
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- Politics of Mergers Critical
Linkages and Mergers

Increased National Political Intervention

- **Vested Interests face More Economic Competition**
Linkages and Mergers

Increased National Political Intervention

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- Trading Consolidation Brings Power Agglomeration
Linkages and Mergers

Increased National Political Intervention

- Vested Interests face More Economic Competition

- Trading Consolidation Brings Power Agglomeration

- Competition and Consolidation is more International
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4) Examples
Examples

Overview

- 3 Large Exchanges: Deutsche Börse, Euronext, LSE
Examples

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- 3 Large Exchanges: Deutsche Börse, Euronext, LSE
- Perceived Competition
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- Instability of Troika
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Examples

Overview

- 3 Large Exchanges: Deutsche Börse, Euronext, LSE
- Perceived Competition
- Instability of Troika
- Other National Silos
- **NOREX seen as a Model for Regionalization**
Examples

NYSE-Euronext Merger: Rationale

- Euronext: LSE Competition
Examples

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- Euronext: LSE Competition
- Euronext: Deutsche Börse Potential Strategy
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- **Euronext: Continued Role in Europe**
Examples

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- **NYSE: Domestic Growth Limited**
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- **NYSE: Escape Sarbanes-Oxley**
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- Euronext: LSE Competition
- Euronext: Deutsche Börse Potential Strategy
- Euronext: Continued Role in Europe
- NYSE: Domestic Growth Limited
- NYSE: Escape Sarbanes-Oxley
- **NYSE: Diversification into Derivatives**
Examples

London Stock Exchange

- 6 “Bids”
Examples

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- **Success of London Independent of Success of LSE**
Examples

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- 6 “Bids”
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- Investment Banks’ Regrets
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- **Shareholder-Determined**
Examples

London Stock Exchange

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- Shareholder-Determined
- Management’s Good Fortune
Examples

Deutsche Börse-ISE Merger: Rationale & Aspects

- Entry into the US
Examples

Deutsche Börse-ISE Merger: Rationale & Aspects

- Entry into the US
- Reinforced Position of Strength in Derivatives
Examples

Deutsche Börse-ISE Merger: Rationale & Aspects

- Entry into the US
- Reinforced Position of Strength in Derivatives
- Limited Number of Major Exchanges Left to Buy
Examples

Deutsche Börse-ISE Merger: Rationale & Aspects

- Entry into the US
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- Risks of Options Market
Examples

India

- NYSE-Euronext 5% Purchase of National SE:
Examples

India

- NYSE-Euronext 5% Purchase of National SE: Investors Taking Profits
Examples

India

- NYSE-Euronext 5% Purchase of National SE:
  Investors Taking Profits

- Deutsche Börse 5% Purchase of Bombay SE:
Examples

India

- NYSE-Euronext 5% Purchase of National SE:
  Investors Taking Profits

- Deutsche Börse 5% Purchase of Bombay SE:
  Mandated Demutualisation
Examples

India

- NYSE-Euronext 5% Purchase of National SE: Investors Taking Profits
- Deutsche Börse 5% Purchase of Bombay SE: Mandated Demutualisation
- Opportunistic Cheap Diversification
Examples

India

- NYSE-Euronext 5% Purchase of National SE: Investors Taking Profits
- Deutsche Börse 5% Purchase of Bombay SE: Mandated Demutualisation
- Opportunistic Cheap Diversification
- **Benefits for Indian Exchanges?**
The Future for European Stock Exchanges

5) Conclusions
The Future for European Stock Exchanges

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- Large Exchanges will Dominate Trading
The Future for European Stock Exchanges

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- Some Small Niche Markets will Survive
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- Cooperative Projects Can Work - but Most Don’t
- Mergers Difficult – but Easier than Linkages
- **Politics is Inescapable**

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