

Emerging opportunity

HKEx builds a leading international marketplace in Hong Kong, Mainland China and Asia.

Hong Kong's handover to China in 1997 was a window of opportunity for Hong Kong Exchanges and Clearing Ltd. (HKEx). Today, the economy on the Mainland is growing exponentially as the disposable income of China's 1.3 billion consumers continues to rise. In addition, the Chinese government is liberalizing the country's financial markets in compliance with its WTO commitment.

To capture the ensuing demand for investments, HKEx needs a reliable, robust, scalable technology platform. While the exchange's cash market trading and clearing runs on proprietary systems, HKEx uses NASDAQ OMX CLICK XT™ and SECUR™ to support derivatives market trading, clearing and settlement. "This is very fundamental to our entire derivatives market," says Alfred Wong, CTO and head of the information technology division at HKEx. "Virtually all our derivatives products now run on this NASDAQ OMX platform."

Prior to the handover, HKEx mainly listed companies incorporated in Hong Kong. In the nineties, the exchange began listing H-shares, equities in companies incorporated in Mainland China. It also began listing Red Chips, equities in Mainland China-based companies incorporated in Hong Kong or Bermuda. Nowadays, the lion's share of cash market trading in the major Mainland equities is done on HKEx. The exchange's core derivatives products are the financial index futures and options on the Hang Seng and H-share indexes. It also offers individual stock options and futures on the major Mainland blue chip equities.

HKEx's ambitious growth strategy is to expand its product range and geographic reach, and HKEx is depending on

NASDAQ OMX's rock solid technology platform and its 24x7 dedicated support services to turn this vision into reality.

According to Gerald Greiner, chief operating officer at HKEx, introducing new products is risky business, and only about one quarter of new derivatives contracts succeed. For instance, the H-share futures and options, launched in 2003 and 2004 respectively, have done fabulously well and stock

options on some of the major Mainland company listings were a hit from day one. However, the FTSE Xinhua China 25 futures and options have not been as successful; nor have the exchange's fixed income derivatives.

HKEx has identified several potential areas for expansion. For starters, HKEx is now assessing the potential of trading commodity and carbon emissions contracts. Mainland China is among the largest commodities producers and users in the world, and the exchange is assessing whether it can add value by creating a commodities exchange in the region.

HKEx also has a marketing plan to entice Asian based overseas companies to list in Hong Kong. The favorable tax environment and

modern IT infrastructure as well as the close proximity and cultural relationship with Mainland China are an attraction for many companies. Although it is now part of China, Hong Kong has an established rule of law based on the common law of the UK, which is well understood by the financial services industry.

In order to be listed, companies must come from a jurisdiction that has investor protection mechanisms broadly comparable to those in Hong Kong. "We've been looking at

Challenge: Expand its product range for equity derivatives to generate new business in Asia and, in particular, Mainland China, and to be ready to meet future demands for these products in the region.

Solution: Create a consistent platform for all derivatives products using NASDAQ OMX technology for trading, clearing and settlement. Prepare for future growth by working closely with NASDAQ OMX to establish a roadmap for capacity planning and upgrades.

other countries to find this broadly comparable set of investor protection mechanisms,” says Greiner. “We’ve cleared Australia, Canada and Taiwan, and we’re just starting to try to clear additional jurisdictions such as Thailand, South Korea and India to support this effort.”

The third area of expansion will be the launch of depository receipts. Some Asian companies are prohibited from listing their shares in an overseas jurisdiction but they would not be so constrained if they could do it through a depository receipt. HKEx is now working to finalize its rules and arrangements to make this possible.

With all this new business in the pipeline, NASDAQ OMX is helping HKEx with capacity planning. HKEx’s derivatives business is smaller than its cash market business, but it has grown substantially in recent years. HKEx constantly reviews its system capacity to ensure it can satisfy market demands. In anticipation of continued growth, HKEx has asked NASDAQ OMX to help establish a roadmap for capacity planning and upgrades.

“Trading volumes on the HKEx can be quite unpredictable, and we get sudden surges. On the settlement date, trading volumes can be double the average,” says Wong. “For this reason, we need to ensure our systems have the capacity to support three times the historical peak activity.”

HKEx views NASDAQ OMX’s dominant position in the global exchange systems market as a big plus. By using NASDAQ OMX systems, HKEx can benefit by sharing the cost of development with many exchanges around the world.

HKEx constantly tries to improve its equity derivatives business by ensuring it has the right products, expiry months and market making mechanisms as well as adequate capacity to cope with ever-rising volumes. HKEx depends on NASDAQ OMX’s expert advice on how to expand the capacity of its software, hardware and network. Over time, it has become a partnership based on trust.

“Without NASDAQ OMX, we would be hard pressed to address system problems on our own, which just highlights the importance of the relationship,” says Greiner. “NASDAQ OMX is always there as a partner to help us.”

Fact Box - HKEx

Hong Kong Exchanges and Clearing Ltd. (HKEx) is the operator and frontline regulator of the central securities and derivatives marketplace in Hong Kong. HKEx was formed in 2000 when Hong Kong’s stock and futures exchanges merged with the clearinghouse to create a multi-asset class

trading and clearing facility. Today, its mission is to be a leading international marketplace for securities and derivatives products focused on Hong Kong, Mainland China and the rest of Asia.