



Edited Transcript of ASX FY 2010 Analyst Briefing

19 August 2010

Chris Williams – UBS

I have two questions; both pick up on comments in your own report within the ASX Group and your report. The first one is around clearing, and you allude to a restructuring of clearing fees perhaps being introduced in alignment with the margining framework that you are introducing in cash equities as I believe that is being introduced in the next six months or so with the encouragement of the Reserve Bank so that is the first question if we could get some detail on that.

Robert Elstone - Managing Director & CEO ASX Ltd:

I will just jump in there and correct you on the timeframe. I think the consultation papers on the introduction of margining are indicating late 2011 for implementation so not the next 6 months.

Chris Williams:

Sure and the second question I had was that you go on to talk about data services in the market in particular the provision of consolidated data in a competitive market environment. I just want to understand the risks and the opportunities around that and whether you are referencing potentially a market wide consolidated tape similar to the US structure or whether perhaps its just a Canadian model that has synchronisation of trading systems across multiple market operators, so just understanding the risks and opportunities around that as well as again the fee structure and margining framework in clearing.

Robert Elstone:

I will take the clearing question and I will flick the data question to Peter to respond to. Just clarifying that the timeframe we are aiming at for the eventual introduction of margining of cash equities will be late 2011. My forward looking statement in my written words released an hour or so ago were really to indicate that we are likely to initiate and hence you are likely to observe something of a rerun or an unbundling of our clearing and settlement service offering and hence an unbundling of our fee structures for clearing and settlement pretty much along the lines of what has begun to happen with our trade execution service offering. Clearly we have started to differentiate from a one size fits all trade execution fee into more of a tiered pricing model to accommodate the style of trade execution. I think very similar thinking is being applied, that's the full extent of the comments I will make on that and clearly, the timing of the introduction of any unbundling and greater differentiation of our clearing and settlement service offering may or may not coincide in a timing sense with the introduction of cash margining for equities but clearly there will be a lot going on in that clearing and settlement space, probably not in the next 6 months but probably in calendar 2011 so second half of the current new financial year and first half of the next one. Peter do you want to field the data question?

Peter Hiom - Deputy CEO ASX Ltd:

Thanks Rob. Chris I think its one of those answers which is really watch this space. I think we wait for the market integrity rules to be, or at least that discussion, to begin with the market around how the settings across a range of issues become finalised because there are so many questions that we don't know the answers to in terms of what data is going to be consolidated, how would it be disseminated, what are the revenue arrangements going to be around that consolidated tape if indeed there is one. So I think it is just too early to call as to what the implications are. Rob just mentioned the disaggregation of the clearing service, I think it is just going to be more of the same there that you are going to see what is currently one market point product which has in it everything that you might want to have as a market user, anything from trading halts to index data to trading information both in depth and at the top of the book. I just think you are going to see that become disaggregated and made available at different speeds depending upon what customers want for different prices. But ahead of knowing what the market integrity rules state about consolidated tapes and best execution, beyond that it is really speculation as to what that is going to mean.

Andrew Hills - Wilson HTM:

Firstly, a broad question on expenses and then a number of specific questions. On expenses; at the beginning of 2008 and also 2009 you guided everyone to growth in line with inflation, expenses in both of those years fell. You have done that again. What sort of assurance can you give us that expenses will actually grow by 3% or so?

Robert Elstone:

I guess if you are asking for an apology Andrew I don't think I will give you one. I think those statements back in 2008 and 2009 and the one we put out this morning are our genuine honest best assessment. The fact that we have beaten our own expectations, I am not going to get into derivatives of forward looking statements so we will be doing our best to contain our cost base. I think the FY10 year we have just finished was an aberration because it was very unusual to have no fixed remuneration pay increases care of the GFC. We continue Andrew to put out the guidance in the most honest way that we can so that we are not trying to in anyway deceive or set the bar higher when we know we can jump it easily. I have said each year and I will restate it again now that we set out to achieve increases to or within overall CPI inflation, I don't think you should take the trend of the last 2 years as systemic pattern of behaviour.

Andrew Hills - Wilson HTM:

Can you please give me your view on the flash crash that occurred in the US on 6 May and also what your view would be of the impact on the Australian market of multi venues and also maker taking pricing?

Robert Elstone:

On the flash crash itself, this is something that Peter and I and all of the resources that we have available to us internal to the organisation have focused on and obviously we believe ASIC and other regulators are quite correctly focusing on what lessons can be learnt. I think what is disturbing Andrew is not so much the events themselves but the three/four months that have elapsed since, where we still don't have, the world doesn't have, an accurate incident report of the underlying cause. There's been a lot of speculation around fat finger type of behaviour that caused the problem but I think it's such a multi dimensional issue. The clear takeaway that I think most people outside of the US agree is that you must have universality of market rules i.e. rules based competition will open up systemic risks for price discovery and I think I am quite emphatic in my response there. I think it is fine to introduce competition for market services and to see competition on price, to see it on technology performance, to see it on functionality offering, but if regulators allow rules based competition they are risking the

stability of the entire price discovery process so you can tell from the tone of my voice this is a subject that has my, and our undivided attention. The fact that the regulators, the SEC, have not been able to produce a clear cut incident report on cause and why it was as complex to discover what actually happened is extremely troubling. I think it's simple to jump to simplistic solutions like market wide circuit breakers will fix everything, they will fix some things, and they will also have some other unintended consequences. So that is our take on what happened, clearly I have made comments in previous results presentations, I think one got written up substantially 6 months ago when I made reference to the technological arms race that the introduction of competition for market services has kicked off and that got written up profusely by the media and I will no doubt get more questions on that today but I can't understate how profound that impact is. The ability of regulators, market watchers generally, to keep pace with the pace of technological innovation is extremely limited so I think what's important is that we do have, we don't have rules based competition, we have universal market rules and at least we minimise the prospects of reruns of what happened there.

The second part of your question seemed to link to, you mentioned maker taker pricing. What was the first part of the second part of your question?

Andrew Hills - Wilson HTM:

Yes just your view on the impact of maker taker pricing on the Australian market given that Chi-X are proposing this pricing model and Pure Match will be offering maker taker pricing in the future also.

Robert Elstone:

Well that's yet to be finally determined. The second part of your question was as to what pricing model we will use on Pure Match, that decision is not finally taken. On maker taker pricing generally I put it almost in the same category of high frequency trading so I don't want to be on the record as being pro or con high frequency trading. I think the threshold issues here are what purpose is the market there to serve and emphatically I would say it's there to serve the interests of listed companies issuing capital and it's there to serve the interests of genuine long term investors. It is not there as a plaything for people with high performance software to use the market to extract profits. So whilst high frequency trading and the attendant maker taker pricing model that seems to go with it is seen through one prism to be welcomed because it can provide liquidity. I suspect, generally, that events like the flash crash in New York or the London and Toronto outages show that a lot of high frequency trading tends to be like a fair weather friend - in the sense that when you have a problem, that's normally the first style of trading activity which exits the market. I don't think maker taker pricing is inherently evil but I do think it is at that end of the ledger because it can, particularly during periods of high volatility, have the potential to actually exacerbate volatility and cause stocks to trade away from fair value and I don't know what market purpose that is actually serving so I think again you can tell from my tone that I think this is an area of imperative for ASIC and other regulators around the world. My comments here are not Australian specific, to look at extremely seriously because I cannot see an intellectual argument for a pricing mechanism that causes stocks to trade away from fair value so that so called liquidity providers can get to the top of the book and get a rebate from the market operator. I think I have answered your question adequately.

Russell Gill – JP Morgan:

Two questions, firstly on the market data centre. Can you talk us through the decision to spend the \$30 million capex on that rather than necessarily outsourcing those services? It is a bit of a different strategy to the rest of the core trading infrastructure across the rest of your business. And secondly a bit of colour on the recent business

initiatives you have put forward, just a bit of an update, I know it is early days particularly in relation to Volume Match and also Centre point orders.

Robert Elstone:

I will flick the second question to Peter and I will deal with the data centre question and Peter can speak to the new functionality. On the strategy part of the data centre decision, it's a little bit out of alignment, I tend to agree with the way you have toned your question Russell. It's a little bit out of alignment with our historic strategy not to build our own proprietary applications or build our own data centres. But I think universally it is probably in alignment with the global trend, particularly for the incumbent exchanges, to want to own and operate their own data centres as opposed to building themselves and there are several precedents in the last 12 months which you know only too well being a good researcher. Hong Kong's announcement, NYSE'S commitment to go forward with their Basildon commitment in Essex to service their London aspirations and Singapore's announcement on establishing not only new data centre facilities in Singapore but to actually leverage them into foreign platforms. I think ours is about the same size in terms of capital commitment as Toronto's. The strategy behind it is we actually see that owning and operating our own data centre, both from a business continuity planning point of view and from a co-location scalability point of view is an absolute strategic imperative for us to own those facilities and to the fullest extent we can determine our own destiny. I think data centres are the future, in the exchange space we will stop being core data centres and they will look and feel more like liquidity centres in terms of the network affect that goes with them. So yes a bit of a step out from our historic IT strategy but not when you step back and look at it in a global context. We are very much in line strategically with what the other major incumbent exchanges, we are as we are on many fronts going to Andrew's question on costs, we are at the low end of the spend profile. If you look at Singapore's commitment, certainly look at NYSE's commitment, they are spending vast volumes of dollars compared to our commitment and as Ramy said in his comments, clearly it gives rise to that spike for a year or so in our capex profile, but we do expect that to settle down once the facility is built and it will revert to its normal range of more like 25 to 30 million which is what we have delivered for the last 3 years. Peter do you want to respond on the functionality?

Peter Hiom:

Russell I think in terms of operational performance and liquidity provision we are very satisfied with the first few weeks and bearing in mind we are talking about only a 6 or 7 week period that the functionality has been in place. I think its too early to call on progress, notwithstanding we obviously have more work to do in terms of developing the liquidity of that platform but it is really too early for us to make any calls on how its performing, albeit to say we are very satisfied with how things are tracking to date. I think it is also worth mentioning though that this is really only the beginning of the change in the way that our business operates in the way in which we price different parts of the trade execution offering so you can expect there to be more order types with different fees attached to them. I don't think you should be expecting any time soon for us to be reporting on an order by order type basis in terms of that transactional volume and probably one other point to note is that our participants themselves are really only just beginning to adjust to that environment as well, they have the ASX trade platform to be implemented, new order types, we are changing the fee structure, so one size fits all fee structure at the broker level is being broken down as well as us adjusting our fees and I think that's yet to fully flush its way through the system.

Mike Wiblin – Macquarie:

A quick question on introduction of competition, any views on when that is likely to be and also any views on any potential change in the approach in the event that the current government is not re-elected?

Robert Elstone:

We would have no idea on when because we are not the party making the decision. I think all I can reference there Michael is the current or the incumbent minister's statement before the caretaker government set in that he would need to be satisfied with the bedding down of the supervisory transfer. As Peter alluded to, there is hopefully a robust consultation period for the review of the market integrity rules and then there is a raft of other issues around the state of technological readiness of the entire trading clearing and settlement participant community before any new license operability becomes an issue. So beyond not wanting to get drawn, I don't need to get drawn to give you a date because it won't be ASX that's making the decision and we have no inside knowledge.

Change of approach, if there were to be a change of government we basically are financiers we are not political commentators and I think that is all I would say on that front.

Mike Wiblin:

A follow up on Chris's question around the unbundling piece around clearing and settlement, is that fundamentally in preparation for competition in that space or just the rationale around at the moment?

Robert Elstone:

I think there are probably 2 or 3 parts to the rationale. As Ramy's numbers when he was quoting you the pre, during and post GFC period on not only what's happened on volatility but on the level of collateral balances we carry, we have seen a longer term trend towards shorter and shorter so lower duration open positions in derivatives trading, not only during the GFC when open interest actually fell but the rate of turnover in open interest since the GFC recovery period. There is clearly a market trend towards lower positions being carried, that has long term implications for how the clearing houses price their risk profile, then there's probably other factors outside of the obvious one of competition. I think just understanding our clearing and settlement users and what it is they are actually looking for and what it is they value, more than a complete one size fits all service offering and then thirdly I think there is obviously the possibility of competition in that space as well but I don't think its just all about the third item. I think there has been enough change in patterns of trading behaviour and duration of open position carrying to stimulate the kind of thinking that Peter and his team are now doing anyway.

There are no questions from the phones.