



DEUTSCHE BÖRSE  
GROUP

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# Financial report 2016

Excerpt: report on opportunities



## Outlook

The Group continually assesses its risk situation. Based on stress tests, on the required EC, which was calculated, and on the risk management system, Deutsche Börse AG's Executive Board concludes that the available risk cover amount is sufficient. Furthermore, it cannot identify any risk that could endanger the Group's existence as a going concern.

In 2017, the aim is to further strengthen Group-wide risk management. For instance, the Group plans to concentrate on the digitisation of information in order to improve quality and efficiency. In addition, the data made available with these efforts will be used to identify risks and opportunities, and to improve our services. Moreover, the Group launched an initiative aimed at a streamlined cooperation between the different control functions through the Group-wide standardisation of documentation and control processes. The Group also plans to extend its business continuity measures in the event of emergencies (or crises), to include additional functions over and above business-critical units.

## Report on opportunities

### Organisation of opportunities management

Deutsche Börse Group's opportunities management aims to identify, evaluate and assess opportunities as early as possible and to take appropriate measures in order to transform opportunities into business success.

Deutsche Börse Group evaluates organic growth opportunities both on an ongoing basis throughout the year in the individual business areas and systematically at Group level as part of its annual budget planning process. Suggestions from the Group's business areas for new products, services or technologies serve as the starting point. The process begins with a careful analysis of the market environment: this considers both customer wishes and factors such as market developments, competitors and regulatory changes.

Ideas for growth initiatives are developed further using uniform, Group-wide templates and subjected to a profitability analysis. Qualitative aspects are documented in a business plan, and expenses and revenues are projected in detail for multiple years.

Once a business plan and profitability analysis have been prepared for a specific growth initiative, the Executive Board of Deutsche Börse AG decides on its implementation. This decision is taken as part of the annual budget planning process. The initiatives that, after taking into consideration the associated risks, add the most value and that can be financed from the budget allocated are selected by the Executive Board and included in the budget.

Budgeting for growth initiatives involves reserving a full-year budget comprising expenditures and expenses for each selected growth initiative included in the investment portfolio. The Group Project Committee (GPC) monitors progress of growth initiatives throughout the year, checking and overseeing projects on a regular basis. In this context, the GPC focuses on whether defined milestones have been reached, on the potential impact of changes in the competitive environment on commercial performance, and on the utilisation of budgets compared to planning.

Where budget adjustments are required during the course of the year, project management must first submit a corresponding application to the GPC. Following a discussion of the application, the GPC will submit a recommendation for a resolution to the Group Management Committee (GMC), which also comprises the members of Deutsche Börse AG's Executive Board. On this basis, the GMC will decide upon whether to increase the budget. The GPC may also recommend adjustments to full-year budgeted funds, to bring them into line with general business developments. Where needed, this also provides for the opportunity to approve new growth initiatives during the course of the year.

Furthermore, supervision of growth initiatives is supported by regular reporting. GPC and GMC receive a monthly report on the status and progress of initiatives that are currently being implemented. This report is coordinated by central functions and created in cooperation with the individual projects from the business areas and compares planned costs with actual budget utilisation. In addition, the financial planning is adjusted, forecasts are updated and changes to the scope of the project are made transparent. Checks are made to establish whether milestones have been reached and project-specific risks, and the countermeasures taken are described.

### **Organic growth opportunities**

When assessing organic growth opportunities, Deutsche Börse Group makes a basic distinction between structural and cyclical opportunities. Structural opportunities arise, for example, as a result of regulatory changes or new customer requirements, and can be influenced directly by the company. Cyclical opportunities, which cannot be influenced directly by the company and are driven by macroeconomic changes.

### **Structural growth opportunities**

The focus of Deutsche Börse Group's structural growth potential is on product- and service-driven initiatives designed to satisfy new client needs as well as regulatory requirements. In order to ensure the Group is optimally positioned and in order to explore new opportunities, the Group has gradually realigned its organisational structure since announcing the "Accelerate" growth programme in 2015. Moreover, it regularly examines options for growth in high-potential asset classes, products or services – organically or through external acquisitions and cooperations.

Organisational measures supporting the Group's growth ambitions include the global coordination of sales activities, as well as cross-divisional product development. In addition, Deutsche Börse AG realigned the distribution of responsibilities in its Group Executive Board at the beginning of 2016 – placing client focus at the heart of its organisation, as announced upon the launch of "Accelerate". With the steps taken, Deutsche Börse Group has bundled related areas in Executive Board portfolios, thus accelerating process flows and simplifying them – in the interest of the Group's clients. Within the framework of "Accelerate" and the related organisational changes, the Group anticipates realising potential for additional new business – especially through bundling Group-wide product development as well as sales activities. These opportunities will develop over time, which is why they have not been quantified in expected additional revenue.

Overall, the Group anticipates the strongest revenue increases in its Eurex segment. Besides the initiatives of the “Accelerate” programme, this includes clearing of over-the-counter (OTC) derivatives and further growth in the trading of power and gas products. 360 Treasury Systems (360T) will also provide a contribution to net revenue growth in this segment. In the Clearstream segment, the focus is on developing the investment funds business, cross-border securities settlements via TARGET2-Securities (T2S), as well as collateral and liquidity management. The growth focus in the MD+S segment is on the expansion of the index business. While building its business in growth regions, Deutsche Börse continues to focus on Asia; developments there will impact all reporting segments. The business potential of the above-mentioned initiatives are described in more detail below.

### **Clearing of OTC derivatives**

The liquidity problems experienced by major market participants during the financial crisis were triggered by the failure to settle bilateral OTC transactions that were mainly entered into on an unsecured basis. In light of this, the leading industrialised nations (G20) agreed to create an effective regulatory environment to make off-exchange derivatives transactions more transparent and more secure. In response, the European Union developed the European Market Infrastructure Regulation (EMIR), which is aimed at regulating OTC trading in derivatives. EMIR includes the following regulatory requirements:

- an obligation to clear standardised OTC derivatives transactions using a central counterparty
- special risk management requirements for transactions in non-standardised derivatives
- an obligation to report the transactions to a trade repository

The obligation for market participants to comply with EMIR requirements kicked in on 21 June 2016, with the first of four phases. Preparing for mandatory clearing, Eurex Clearing AG has developed a central counterparty to clear OTC derivatives. The offering, which may later be extended to other asset classes, is aimed primarily at institutional customers and the interest rate swaps they enter into. It especially focuses on security and efficiency, allowing customers to gain the full benefit of Eurex Clearing’s risk and collateral management services for their OTC transactions as well. The majority of transactions entered into by these clients has been subject to mandatory clearing since the start of phase 2 on 21 December 2016.

### **Trading and clearing of power and gas products (EEX)**

With the acquisition of a majority stake in the European Energy Exchange AG (EEX), based in Leipzig, Deutsche Börse Group expanded its product range to include trading and clearing of spot and derivatives contracts on power and gas as well as emission certificates – in order to benefit from markedly higher demand for energy trading and clearing services. The double-digit growth rates which the Group has achieved since then have been the result of external growth but also reflect structural organic growth which Deutsche Börse Group has been able to exploit, thanks to its good position. For instance, EEX has evolved into the central marketplace for energy, energy-related and commodities products in Continental Europe; its product range includes the markets in Germany, France, the Netherlands, Belgium, Italy and Spain. EEX also generated organic growth, especially in the power and gas business. Whilst this growth momentum is based on the changing importance of renewable energy sources – wind power in particular – for power generation, the resulting gains are difficult to predict, also due to the strong fragmentation of

the European energy market, and the fact that market participants predominantly trade off-exchange. Given this high degree of fragmentation, as well as the inefficiency of OTC markets, demand for on-exchange trading and clearing solutions for such transactions has been growing over recent years. Whilst OTC trading clearly continues to be the bigger market, EEX was able to significantly increase market share, to around 30 per cent in 2016. EEX continues to anticipate strong demand for efficient trading and clearing solutions for the energy markets, and resulting structural growth.

#### **Expansion into foreign exchange trading (360T)**

Deutsche Börse AG successfully explored a new asset class – foreign-exchange trading – with the full acquisition of 360T. 360T<sup>®</sup> is a leading, globally active foreign-exchange trading platform which has generated double-digit annual growth rates since its inception in 2000. The broad client base of 360T includes corporate and buy-side clients as well as banks. The acquisition of 360T by Deutsche Börse is expected to further boost the company's organic growth momentum. On a medium-term horizon, the combination offers the potential for revenue synergies in a double-digit million euro amount, with 360T using Deutsche Börse Group's international sales network and expertise for growing business, especially through the introduction of electronic trading in order to further improve liquidity and transparency. To date, regulatory obligations such as EMIR have not yet been expanded to cover the foreign exchange market. If this were to happen, Deutsche Börse Group would be able to tap further growth opportunities from its extensive portfolio of products and services it offers in the context of regulatory requirements. For instance, the Group plans to establish a foreign exchange clearing house in order to service the fundamental demand for capital-efficient solutions. Thanks to its leading position, 360T further benefits from a structural trend. Even though, at present, the vast majority of daily foreign-exchange trading volumes are executed off-exchange, demand for transparent, electronic multi-bank trading platforms such as 360T is rising. By combining the skills and experience of 360T in foreign-exchange trading with Deutsche Börse's IT competence, the Group will be able to explore the resulting revenue potential.

#### **Cross-border settlement of investment funds**

Clearstream completed the integration of the hedge fund custody business, acquired from Citco. This enables clients of Deutsche Börse Group to use Clearstream's settlement and custody services for their entire fund portfolio – covering traditional investment funds, exchange-traded index funds (ETFs) as well as hedge funds. Given that regulatory authorities demand more efficient settlement and custody solutions in order to achieve a maximum safety level for customer assets, the Group anticipates that it will acquire additional client portfolios.

#### **Cross-border securities settlement (T2S)**

Initiated by the ECB, the purpose of the T2S project is to harmonise cross-border securities settlement using central bank funds across Europe. Clearstream has undertaken substantial investments over recent years to bring its systems into line with the new settlement structure. For Deutsche Börse Group, this holds the opportunity of winning new clients for Clearstream's innovative services, such as global liquidity management. Furthermore, the Group expects higher custody volumes and new services from T2S, which can only be provided through Clearstream via its integrated international central depository (ICSD). Clearstream has been connected to T2S within the scope of the fourth migration wave in February 2017. Once this connection is in place, clients will be able to use Clearstream as a central point of access for domestic and international settlements, both in central bank and commercial bank funds. National central securities depositories (CSDs) – Clearstream in Germany and LuxCSD S.A. in Luxembourg – will offer their clients T2S settlements at ECB terms, without any mark-up. Full interoperability between national and international CSDs will enhance liquidity and collateral management.

### **Collateral and liquidity management**

Clearstream's collateral and liquidity management offering, developed as part of its Global Liquidity Hub growth initiative, helps customers cope with the structural changes they are facing, such as those resulting from the additional liquidity requirements under Basel III and the clearing obligations under EMIR which came into force in December 2015. The Global Liquidity Hub allows banks to use the assets held in custody by Clearstream on their behalf more efficiently across different platforms and countries.

### **Expansion of the index business**

Deutsche Börse Group's objective in its index business is to re-position its established European index provider STOXX with a global profile, in order to develop further indices (on top of its DAX® and STOXX® index families) and to market them on a worldwide basis. The goal is to acquire new client groups, both within Europe as well as in Asia and the Americas, through diversification. In addition, we will position our index business to better exploit the structural trend towards passive investment products (ETFs). An increasing number of private clients and asset managers now follow this trend; not only are the costs lower, but many active investment strategies have been returning under-average performance.

### **Expansion in Asia**

In addition to growth in its core markets and products, the Group is focusing on expanding its business in growth regions. A particular emphasis is on Asia, where the Group is already successfully represented by Clearstream subsidiaries in particular. Among other things, Clearstream has been operating a permanent establishment with its own banking licence in Singapore since 2009. The China Europe International Exchange (CEINEX) commenced trading in November 2015, initially with cash market products such as ETFs based on Chinese underlyings, and renminbi-denominated bonds. CEINEX is a joint venture between Deutsche Börse and the Shanghai Stock Exchange (holding 40 per cent each) and the Chinese Financial Futures Exchange (holding a 20 per cent stake). CEINEX provides international investors with access to investment products based on Chinese underlying instruments. The marketplace is the first regulated and authorised trading platform outside China for financial products denominated in renminbi, the Chinese currency. CEINEX thus offers investors new opportunities for efficiently trading Chinese securities; at the same time, it effectively promotes the renminbi's internationalisation.

### **Other structural growth opportunities**

In addition to these initiatives, the Group has identified a number of other structural factors that should have a positive impact on its business success.

- In January 2014, agreement was reached at a European level on the MiFID II Directive: among other things, OTC derivatives transactions will in future have to be settled via organised trading facilities, a requirement that is expected to benefit Eurex. In addition, a decision was taken to limit the volume of equities traded in dark pools. The Group expects this restriction to have a positive impact on the volumes traded on Xetra®. The Group will apply MiFID II as from January 2018.
- Risk management is becoming more important in the wake of the financial crisis. The company expects market participants to make greater use of Eurex Clearing's clearing services to net out transactions in different asset classes and hence to eliminate counterparty risk.
- In line with the European legal and administrative framework governing certain undertakings for collective investment in transferable securities (UCITS V), the company expects that traditional investment funds will increasingly include derivatives in their portfolio strategies. This could result in additional business for the Eurex segment.
- With respect to Clearstream's post-trade activities, the company anticipates a long-term increase in capital raising through equity and debt financing on the capital markets. This ties in with the higher capital and liquidity requirements for banks and the resulting negative impact on the total volume

of available credit. For Clearstream, this could have a positive effect on custody volumes, especially in the international bond segment. In addition, given the growing internationalisation of the capital markets, the company is continuing to expect a sharper rise in the bond volume issued internationally compared with national bond issues.

### **Cyclical opportunities**

In addition to its structural growth opportunities, Deutsche Börse Group has cyclical opportunities, for instance as a result of positive macroeconomic developments. Although the company cannot influence these cyclical opportunities directly, they could lift Deutsche Börse Group's net revenue and net profit for the period attributable to Deutsche Börse AG shareholders significantly in the medium term:

- In the cash and derivatives market segments (Xetra and Eurex), sustained positive economic development, a lasting rise in investor confidence in the capital markets leading to a renewed rise in risk appetite among market participants and a sustained increase in market volatility could again stimulate trading activity by market participants and boost trading volumes.
- The volumes of interest rate derivatives traded on the Group's derivatives markets could rise if speculation on trends in long-term yields on German and other European government bonds grows, and if the spread between the various European government bonds continues to narrow.
- While the company does not expect the ECB to change its low interest rate policy during the forecast period, the US Federal Reserve could incrementally continue to raise interest rates. Among other things, this would positively impact Clearstream's net interest income from banking business as some 49 per cent of its daily cash balances are denominated in US dollars. A rise in key interest rates of one basis point affecting all customer cash deposits could lift income by some €100 million.
- In the market data business, an increase in the number of employees at companies active on the financial markets could lead to growing demand for data packages.

### **External growth opportunities**

In addition, the company regularly explores external growth opportunities, which are subject to the same kind of stringent analysis as its organic growth initiatives. For this reason, only a small number of the opportunities analysed are ultimately realised. Examples of external growth in the past few years include the takeover of Citco's hedge fund custody business, the majority interests in EEX and Pownext, the full acquisition of the joint ventures STOXX including Indexium, as well as the full acquisition of 360T. Furthermore, the planned merger with London Stock Exchange Group plc was pursued in 2016 (see the [☞ "Planned merger with London Stock Exchange Group" section](#) for details).

### **Report on expected developments**

The report on expected developments describes Deutsche Börse Group's expected performance in financial year 2017. It refers to the Group's standalone business operations. It does not refer to either the new HoldCo established in the context of the merger with London Stock Exchange Group (LSEG), nor does it refer to Deutsche Börse AG as a subsidiary of the new HoldCo. It contains statements and information on events in the future and is based on the company's expectations and assumptions at the time of publication of this corporate report. In turn, these are subject to known and unknown opportunities, risks and uncertainties. Numerous factors influence the Group's success, its business strategy and its financial

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