

## **The ASX-SGX proposal – in the national interest?**

Contrary to Joe Hockey's pronouncement that the ASX-SGX deal will see an end to Australia's aspirations as a global financial centre, it may be just the opportunity Australia has been looking for to assume a major role in Asian financial markets.

As last year's Australian Financial Centre Forum (Johnson) Report points out, despite our highly skilled workforce and excellent regulatory system, Australia's imports and exports of financial services have been low by international standards. While our funds management sector is the fourth largest in the world, it manages only a small volume of funds from offshore. The integration of Australia's capital market with an Asian exchange together with the introduction of a passport package for Australian businesses should assist in correcting this "inward focus" leading to a boost in trade for financial services and further improve the competitiveness and efficiency of the financial services sector. This should translate to reduced costs for business, wider choice for consumers, increased skilled job opportunities for Australian workers and the potential development of a wider range of business support industries.

The ASX-SGX proposal is representative of an international trend in stock exchanges which has occurred in two stages. First, there has been a widespread privatisation of what were formerly mutual or government-owned exchanges. According to the World Federation of Stock Exchanges, between 1998 and 2006, the proportion of for-profit stock exchanges increased from 38% to 75%. Second, these for-profit entities have moved to consolidate internationally for competitive and scale purposes. Better know consolidations have been the OMX which owns and operates 7 exchanges based in the Nordic and Baltic countries and the Euronext, which is a merger of Amsterdam, Brussels, Lisbon and Paris stock exchanges. In addition, there has been the OMX-NASDAQ merger, consolidation between London and Milan, mergers amongst derivative exchanges and numerous within country mergers as in Japan, India and Spain.

To date there is little research into the effectiveness of these consolidations, but a recent study by Ulf Nielsson of Columbia University, soon to be published in the *Journal of Financial Markets*, explores the impact on the Euronext. Nielsson found that bigger firms and firms with foreign sales benefited from increased liquidity, noting that the latter included most firms listed on the exchange. The study also found that the merger also led to an increase in Euronext's market share at the expense of the London Stock Exchange, although there was no evidence of an increase in competitiveness with regard to attracting new listings.

On that basis one might expect advantages for the ASX, dominated as it is with large financial services firms and export-oriented resource stocks. One might also anticipate the combined strength of Singapore and Sydney, currently ranked fourth and tenth respectively as Global Financial Centres, in creating a stronger financial hub in the South Asia region to be at the expense of North Asian centres such as Hong Kong, Shanghai and Shenzhen.

From a strategic point of view, this merger would demonstrate a genuine integration of Australian and Asian financial markets and potentially reposition Australia. Despite Australia's aspirations to be a leader in Asia, the broader public perception of Australia has not been as a part of Asia but more as part of a separate classification, usually grouped together with New Zealand as Oceania or Australasia. Had the ASX merged with Toronto or London exchanges as has been explored, the vision of Australia as a leader in Asia would become even more remote.

Ideally from Australia's point of view, this proposal would have been more beneficial had it come three years ago when previously discussed. At that stage the ASX would have been the initiator of such a proposal, in more advantageous and appropriate position given that the SGX is smaller and less liquid than the ASX, and in a better position to hold the balance of power with the appointment of a Chair, CEO and Board members. One would also expect there to be some advantages in having a home-based stock exchange. Those with a long memory may remember the outcomes for the Melbourne Stock Exchange when merged into the ASX!

All of these issues and more will be explored no doubt in the regulatory impact statement that will be required to overcome regulatory hurdles such as Australian gaining government approval to lift the 15 % ownership cap on the ASX and approval of the Foreign Investment Review Board. Provided those obstacles can be overcome, further approvals will need to be sought from ASIC, under the Corporations Act, from the Monetary Authority of Singapore, from ASX and SGX shareholders, and for SGX shares to be listed on the ASX.

While the potential benefits of mergers are not always realised, there are two notable strengths in this proposal. First, the reported mutual understanding and good will between the two stock exchanges, and second the proposed and current CEO of SGX, Magnus Bocker, is formerly the head of the OMX and is therefore experienced in such consolidations.

On the other hand, the proposal would be more appealing were there a better representation of ASX interests in the appointment of management and Board. Both the proposed CEO and Chair are from the SGX and the proposed Board will have only 4 nominees, David Gonski, Russell Aboud, Jillian Broadbent and Alan Cameron. As a minority these Directors may not always be in a position to act in the best interests of Australian companies as new combined listing rules and regulations are developed.

As we are only too aware, Australia's resilience through the GFC was in no small part a direct outcome of our trading partnership with China. Forward economic projections indicate that if there is a positive economic future internationally, it revolves around the dynamic Asian economies. Critical mass and economies of scale that result from the ASX-SGX merger would potentially provide a highly efficient international capital market linked to the vibrant economies of South Asia, and provide a gateway for Australian business to Asia and the rest of the world.

This proposal ticks all the boxes in terms of the Johnson Report. It has the potential to increase the size of the market, provide more diversified funding sources for Australian business, lower costs and widen choices for consumers and business, it will still adhere to strong regulatory standards, and will promote Australia's role in the Asian region. It is therefore hard to argue that the proposed merger would not be in the national interest.

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