

PODCAST
PRESENTATION

**NORDIC REGION
SECURITIES MARKET CONSOLIDATION**

HOST: Welcome to our podcast on securities market consolidation in the Nordic region. Joining us today is Penny Biggs, Executive Vice President, and Head of Northern Trust's Worldwide Business Development for Asset Servicing. This podcast will be of particular interest to anyone wanting to find out more about trends in the global financial markets. Penny, securities market consolidation in the Nordic region is well advanced. Could you tell us what lessons the rest of Europe can learn from the Nordic experience?

PENNY: Yes. Amidst all the frenzied transatlantic activity between European and US stock exchanges, many have said that one voice has stood out as an advocate of reason and moderation. Magnus Böcker, chief executive officer of OMX, the Stockholm-based exchange owner and operator, stated that what bothers him is that most of the discussions to date have been on shareholder value, but there has been very little focus on what is good for the customer and product development.

OMX itself has been much more than an interested bystander in the continuing story of exchange consolidation. For many, it first came to our attention in 2000, when it made an unsuccessful bid to buy the London Stock Exchange. Undaunted, it went away and began the process of building a regional conglomerate of Nordic and Baltic exchanges, which today includes the exchanges in Copenhagen, Stockholm, Helsinki, Riga, Tallinn and Vilnius. OMX says that this so-called Nordic Exchange offers access to more than 80 percent of exchange trading in the Nordic and Baltic regions.

HOST: Can the Nordic experience teach the rest of the market about the opportunities – and pitfalls – of consolidation? Is the Nordic model applicable in the broader European context, and does it deliver what market participants and regulators really want?

PENNY: Consensus, said Margaret Thatcher, is something in which no one believes and to which no one objects, but there are strongly-held beliefs and heated objections within Europe about the best path to take. Everyone, it seems, has their own view of what is required to make European capital markets more efficient, cost-effective and attractive to investors and issuers.

HOST: Could you briefly talk about any of those opposing views, Penny?

PENNY: Certainly. In February 2006 a group of four European trade associations – the French Association of Investment Firms, the Italian Association of Financial Intermediaries, the French Banking Federation and the London Investment Banking Association – issued a statement on consolidation of the European post-trade infrastructure. The statement called for action from the European Commission



to accelerate the horizontal consolidation of infrastructure providers, for example, clearing houses and central securities depositories. In making this case, it dismissed arguments in favour of continued competition and interoperability between post-trade service providers. The commission argued that competition is set to remain weak in clearing and settlement and certainly insufficient to bring meaningful price reductions and innovation for users and customers. On the contrary, further consolidation would bring significant benefits.

HOST: Penny, what is the position of the Federation of European Securities Exchanges?

PENNY: Recently, the Federation of European Securities Exchanges published its position paper on clearing and settlement, arguing strongly for interoperability, between both clearing houses and central securities depositories. It stated that the Federation welcomes the improvement of cross-border links and interoperability, the open access to post-trading services, the transparency of prices and the freedom of choice for traders. In summary, it supports the establishment of a level playing field to increase competition and the choice for investors.

HOST: Who is right – or, more importantly, who will decide who is right?

PENNY: Much as the European Commission might want to enforce a solution on the market, it must first establish that the new infrastructure satisfies the current and future needs of all participants. This, of course, is a huge challenge.

There is little doubt that the Commission is becoming frustrated by delays in reforming the system. In March 2006, it threatened the market that, if it did not make more effort to improve clearing and settlement of securities trades in the European Union, it would intervene. The Commission said they had not yet reached any definitive view on the precise measures they would propose to remedy this situation. They further stated that it is clear the present system is untenable and changes are going to have to be made. They believe the industry recognises this and encourages them to be part of the solution and not the problem.

Trying to get any kind of consensus out of the 25 member countries may be tough, especially if the Nordic experience is any guide. With three of the four Nordic countries as members of the European Union – Norway, of course is not – and a history of enlightened self-interest when it comes to cross-border co-operation, it should have been a relatively easy task to create a pan-Nordic stock market and associated infrastructure.

HOST: Would you mind talking a little bit more about how the integration started?

PENNY: The journey towards integration started in 1998, when the Copenhagen and Stockholm stock exchanges formed the NOREX alliance, which was followed the next year by the transfer of Danish and Swedish equities trading to a common platform, called SAXESS. Iceland became a partner in NOREX in 2000 and also moved its bond and equities trading on to the SAXESS platform, with Oslo Börs following the same path in 2002.

Integration moved beyond alliances in 2003, when HEX, the Finnish stock exchange operator, and OM, owner of the Stockholm Stock Exchange, joined forces to create OMX. As part of the deal, HEX brought its existing operating agreements with the exchanges in Estonia and Latvia to the new venture. Subsequently, the Danish and Lithuanian exchanges have merged with OMX.

OMX has also established a link with EDX, the equities derivatives market run by the London Stock Exchange, with the exchanges in Stockholm, Copenhagen and Oslo sharing a common order book with EDX.

HOST: Could you elaborate on OMX and its recent actions?

PENNY: Yes. OMX plans to replace the current exchange list structures for Sweden, Denmark and Finland with the so-called Nordic list. This will be organised in three segments: Large Cap for companies with market capitalisation

of not less than €1 billion; Mid Cap for companies with a market capitalisation of between €150 million and €1 billion; and Small Cap for companies with a market capitalisation of less than €150 million. In addition, the companies on the Nordic list will be organised by industry sector to facilitate comparisons by investors. The indices will be harmonised and extended, with an all-share index, benchmark index, industry index and trade index.

Jukka Ruuska, President of OMX Nordic Marketplaces said they are in a unique position to make something good work even better. He stated that within the Nordic region, OMX can truly create a larger and more efficient home marketplace, so everyone who is doing business in this region will be better off. They are all relatively small countries and are realising that there is a lot to gain from working together. Co-operation is in their culture.

HOST: Is there really support for the Nordic market concept from within the region?

PENNY: Yes, there certainly is support. Johan Wennerberg, head of relationship management for Handelsbanken Asset Management, says that it is a work in progress and that OMX is taking a leading role in creating a single Nordic market. OMX hasn't yet seen the full effects and benefits of the project, which will take time to come through.

Wennerberg also believes that the continuing independence of Oslo Börs is not an obstacle and that in fact Oslo Börs wants to be part of the Nordic market and has always been a participant in NOREX and uses SAXESS as its trading platform.

HOST: And what about the post-trade infrastructure?

PENNY: Well, there is less clarity around that. OMX is enthusiastic about the prospects for an integrated clearing and settlement platform for the Nordic and Baltic markets, but not all of the existing providers have demonstrated that they are willing to participate. Some progress has been made: in 2004, VPC and APK, the Swedish and Finnish central securities depositories, did merge to create a depository that handles nearly three quarters of all Nordic settlement volumes. Following on from this merger, the combined entity now operates under the Nordic Central Securities Depository brand or NCSD.

HOST: Were there any recent actions that came out of that merger?

PENNY: NCSD has issued a consultation paper on its proposed clearing and settlement model for the region. But, although the project undoubtedly has merit, there are serious doubts about the enthusiasm of either VP, the Danish depository, or VPS, the Norwegian depository, to do more than agree to some form of interoperability.

And in Denmark, VP has extended the reach of its operations, acquiring the shareholder register businesses of both Nordea and Danske Bank, suggesting that it is primarily concentrating on the expansion of its commercial activities. Similarly, VPS in Norway has bought the financial derivatives clearing operations of Imarex/NOS Clearing, which takes it into the clearing business for the first time.

VP has acknowledged the drive towards consolidation, although it stopped short of committing itself to anything more than cooperation.

HOST: Is there any debate about a central counterparty?

PENNY: Perhaps surprisingly, there is currently very little debate about the establishment of a Nordic central counterparty, an issue that was specifically omitted from the NCSD consultation paper.

HOST: What communication is coming out of the Nordic region?

PENNY: The message coming out of the Nordic region is that integration is much tougher than some regulators anticipated. OMX has made considerable progress, with the Nordic Exchange now Europe's fifth largest equities exchange in terms of transaction volumes. But, as OMX chief executive Magnus Böcker admitted at the firm's AGM this year, there is more to do and the Nordic financial market remains more a sum of the markets than an integrated, well functioning and uniform market.

As OMX and other market service providers in the Nordic region push for further connectivity and integration, they could do worse than measure themselves against the future criteria for any exchange's success identified by Jim Gollan, chief executive officer of virt-x, the cross-border stock exchange.

HOST: Could you tell us what Mr. Gollan identified?

PENNY: He identified four criteria:

- First, a pan-European focus, not simply a group of national exchanges, but an exchange offering trading in a variety of stocks across Europe under a single rule book and on a multi-currency basis;
- Second, a provision of post-trade services that give users choice and flexibility;
- Third, it had to be customer-centric, the long-term needs of the users of exchanges must be at the heart of all decision-making processes, as opposed to being driven by the more short-term desires of shareholders that may or may not be exchange users;
- And fourth, he said a commitment to innovation was key; in this rapidly developing environment, only those that adapt will succeed.

HOST: Penny, do you have any final thoughts on what we have seen taking place in the Nordic region?

PENNY: Yes, the Nordic experience has vital lessons that can and should inform the broader debate over European harmonisation. Nordic market players have followed a pragmatic path to ensure that, with relatively limited resources they remain competitive and continue to attract international investors. The rest of Europe is watching their progress with a healthy degree of self-interest.

Northern Trust in particular is very focused on these developments given our commitment to the Nordic region – the result of our very substantial and market-leading client base across Norway, Sweden, Finland and Denmark.

HOST: Thank you Penny. For more information on securities market consolidation in the Nordic region, please visit northerntrust.com/Europe.

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