



DEUTSCHE BÖRSE
GROUP

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Financial report 2016

Excerpt: report on expected developments



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

results, many of them outside the company's control. Should opportunities, risks or uncertainties materialise or should one of the assumptions made turn out to be incorrect, the Group's actual performance could deviate either positively or negatively from the expectations and assumptions contained in the forward-looking statements and information contained in this report on expected developments.

Developments in the operating environment

Macroeconomic environment

Deutsche Börse Group anticipates that the global economy will grow moderately during the forecast period. In the case of the emerging markets, the Group expects that countries with a current account surplus will expand at an above-average rate. Due to cyclical as well as structural factors, these countries will no longer be able to match the high growth rates seen in the past. Furthermore, the Group expects the economies of industrialised nations to recover slowly following a series of challenging years in the aftermath of the financial crisis, with economic growth picking up slightly over the previous years. Looking at Europe, the Group expects an improvement of the economic situation, driven by developments in Germany and France, the two largest economies. Against this generally positive background, we are assuming that market participants will have more confidence in the capital markets compared to the previous year, which was marked events, such as the Brexit referendum and the US presidential elections. However, current uncertainties could once again unsettle the markets. These include geopolitical crises, the development of commodity prices, monetary policy moves by the Fed in the US and the ECB in Europe, or a crisis of confidence in the growth of certain emerging market countries, especially in Asia. Regarding interest rate trends, the Group does not expect to see any fundamental departure from the current low interest rate policy in Europe. While the monthly volumes of the ECB's bond-buying programme will be slightly reduced, the deposit rate is expected to remain at -0.4 per cent. Now that the positive effects during 2016 of this monetary policy on cash and derivatives markets trading volumes have largely run their course, the Group does not expect any such stimulus for 2017. The turnaround in US interest rates continued at the end of 2016, and we expect further hikes in 2017 – provided that the economy (and inflation) accelerate further.

In its economic development forecast for 2017 published in January 2017, the International Monetary Fund (IMF) predicts an increase of around 1.6 per cent in the euro zone and growth of around 1.5 per cent in Germany. Expectations for the United States are slightly higher than for the euro zone: the US economy is forecast to grow by around 2.3 per cent. The highest growth by far in 2017 – approximately 6.5 per cent – is again expected in Asian countries (and especially China), due to expected high domestic demand. Given the extremely varied estimates for the different economic regions, global economic growth is projected to be around 3.4 per cent in 2017.

Regulatory environment

Governments and central banks are currently working to enhance regulation of the financial markets so as to stabilise the financial sector and prevent future crises of the magnitude experienced. The measures planned, and in some cases already initiated, range from revising the legal framework for banking business and capital adequacy requirements through rules for clearing over-the-counter (OTC) derivatives transactions down to improving financial market supervision (for more information, please see the [“Regulatory environment” section of the report on economic position](#)). For Deutsche Börse Group's customers, the ultimate impact of these far-reaching regulatory reform projects on market structures and business models is difficult to gauge accurately at present. Deutsche Börse anticipates that this uncertainty will continue to weigh on market participants' business activities during the forecast period.

For the Group itself, the various regulatory projects will have both positive and negative consequences. Overall, however, the Group sees the changing regulatory environment as an opportunity to expand its business further; see the [report on opportunities](#) for further details.

In addition to the structural opportunities arising from regulation, the Group expects to see further debate in the forecast period on the potential introduction of a financial transaction tax. The introduction of a financial transaction tax will continue to be pursued in 2017 by a number of EU Member States, which have formed an alliance to achieve greater cooperation. The introduction of such a tax would negatively impact Deutsche Börse Group's business performance. Since the ten Member States concerned have been unable to date to reach agreement on the tax base, tax rates and technical collection and remittance methods, it is not possible to gauge the concrete impact on the Group's business.

Future development of results of operations

Given its diversified business model and multiple sources of revenue, Deutsche Börse Group continues to consider itself very well positioned and expects to see a positive trend in its results of operations over the medium and long term. This expectation is based on, among other things, the growth opportunities that the company intends to exploit over the same period. The Group expects net revenue to increase further in the forecast period. This assumption is based on two main factors. Firstly, a further slight increase in economic growth could improve investor confidence, and motivate US investors to return to European markets. Against the background of the UK's exit from the EU, the general elections to be held in a series of European countries, and the development of US policies, we anticipate elevated stock market volatility in 2017, at least temporarily. Both of these factors, i.e. returning US investors and elevated equity market volatility, would have positive effects on trading volumes in equities and equity index derivatives. Moreover, market speculation on interest rate developments in the US and Europe may boost trading activity in interest rate derivatives at Eurex derivatives exchange – whilst higher, or increasing US interest rates could lead to a further increase in net interest income from the banking business in 2017. Secondly, the Group expects a further increase of the contribution from its structural growth initiatives as well as from new growth opportunities being explored within the scope of its “Accelerate” growth programme launched in 2015 (for details, please refer to the [report on opportunities](#)).

Depending on developments in the operating environment, the impact of both cyclical and structural growth drivers and the success of new products and functionalities, Deutsche Börse Group expects net revenue to increase by approximately 5 per cent to 10 per cent during the forecast period. Net revenue growth expected during the forecast period is based on net revenue of around €2,389 million achieved in 2016.

Even if, contrary to expectations, the operating environment turns out to be worse than described above, and clients were to scale back their business activities, particularly in the Group's business divisions which depend upon trading, Deutsche Börse Group believes it is in a position to continue to do business profitably thanks to its successful business model and its cost discipline.

Within the scope of its “Accelerate” growth strategy, in 2015 Deutsche Börse Group introduced principles for managing operating costs. The core element of these principles is to ensure the scalability of the Group's business model. To this end, the Group continuously manages operating costs adjusted for non-recurring effects relative to the development of net revenue. Accordingly, the lower end of the net revenue growth range during the forecast period and the following years, of approximately 5 per cent, would imply stable operating costs compared to the previous year. If net revenue reaches the upper end of the

growth range, at around 10 per cent, operating costs would be permitted to rise by up to 5 per cent per annum during the period under review and the following years – for instance, for the purpose of increasing investment in growth initiatives. Operating costs expected during the forecast period are based on adjusted operating costs of €1,174.2 million in 2016.

Essentially, the Group achieves the necessary flexibility in managing operating costs through two different initiatives designed to enhance operating efficiency. Firstly, the Group has implemented a continuous process to improve operating efficiency by focusing even more on client needs in order to further enhance quality and efficiency of the services offered. At the same time, Group-internal processes are simplified, generating costs savings. Secondly, the Group resolved a series of structural cost reduction measures during the reporting period, and has already commenced implementation. For instance, we started to reduce the number of external service providers. This included the shift of tasks from external to internal staff, or the hiring of external service providers as internal staff. As at the publication date of this combined management report, the company expects that operating costs will be affected by non-recurring effects of some €80 million. The majority of these is due to mergers and acquisitions (excluding performance-related components) but also due to efficiency measures and costs incurred in connection with criminal proceedings against Clearstream Banking S.A. in the US.

Given the expected increase in net revenue of approximately 5 to 10 per cent, with operating costs rising by between 0 and 5 per cent as a result, the Group anticipates a growth rate of between approximately 10 and 15 per cent (excluding non-recurring effects) for net profit for the period attributable to Deutsche Börse AG shareholders during the forecast period. This assumption is based on an adjusted figure of €810.8 million for 2016.

With regard to the cyclical environment and structural growth initiatives, Deutsche Börse AG's expected business development is based on the same factors that influence the expected business development of Deutsche Börse Group as a whole. These are described in this report on expected developments. For 2017, the company expects sales revenue to be above the 2016 level (2016: €1,300.2 million) and to rise by approximately 5 to 10 per cent depending on how the factors described above develop.

Given the expected increase in sales revenue of approximately 5 to 10 per cent, with operating costs rising by between 0 and 5 per cent as a result, the Group anticipates a growth rate of between approximately 10 and 15 per cent (excluding non-recurring effects) for adjusted net profit for the period attributable to Deutsche Börse AG shareholders (2016: €553.2 million) for the forecast period.

Eurex segment

In the past year, cyclical factors (see the [“Future development of results of operations”](#) section for details) led to an overall rise in derivatives trading volumes. Higher stock market volatility since the end of 2014 resulted in a significant rise in trading volumes, especially in equity index derivatives. Deutsche Börse Group believes that structural growth factors will remain the dominant feature over the long term, and that they will positively influence trading volumes in all product segments (see the [report on opportunities](#) for further details). In the short term, a positive economic environment would result in increasing trading volumes, in particular for equity index derivatives – whilst the present direction of monetary policy, especially in the US, would have positive effects on interest rate derivatives trading.

Eurex will continue to invest systematically in expanding its product offering in the forecast period in order to take advantage of structural factors, such as regulation or changing customer needs. The focus of our efforts will be on the acquisition of new business, which is currently not settled through an exchange or

clearing house. We are expecting positive developments along these lines due to regulatory requirements determining that OTC derivative transactions must be settled via central counterparties. This requirement has entered into force during 2016. Consequently, the Group expects this initiative to deliver additional net revenue for the first time in the 2017 financial year, and significant net revenue in the medium to long term. Looking at the once again very positive development of EEX group's trading volumes during the year under review and the continued positive market environment for trading in power and gas products, the Group expects further structural growth in business activity during the forecast period, e.g. by gaining additional market share at the expense of OTC energy markets. Moreover, the Group expects rising demand for multi-bank platforms to further boost business activity at the foreign-exchange (FX) platform 360T[®]. In addition, we plan to include clearing services in the value chain of fully electronic FX trading during the 2017 financial year, in order to realise the revenue synergies projected in the context of this acquisition.

Xetra segment

As in the past, net revenue in the Xetra cash market segment will continue to depend heavily on stock market cyclicality and volatility. Trading volumes could rise during the forecast period, driven by a gradual improvement in economic growth as well as a rise in investor confidence. Furthermore, the company expects stock market volatility to increase, at least temporarily, making further positive contribution to business development.

As well as enhancing its cash market offering, the company will continue to closely track changes in the competitive environment for the European cash markets. As in the past, it considers itself well positioned to retain its status as the market leader for trading German blue chips and to offer its customers across the globe an attractive range of products and services for cash trading in German and European equities, and for equities clearing. However, the stronger competition in the cash market means that further shifts in the market shares of all competitors cannot be ruled out.

Clearstream segment

The Clearstream segment's main net revenue driver is the settlement and custody of international bonds – a business that is much more stable than the trading business and only subject to less significant capital market fluctuations. The Group anticipates a structurally driven increase in demand for collateral and liquidity management services due to regulatory requirements. In the medium to long term, Clearstream expects its attractive collateral and liquidity management and its strong position in the TARGET2-Securities (T2S) network to result in increased business activity and hence in significant additional net revenue. As Clearstream did not migrate to T2S until February 2017, the Group anticipates only a moderate contribution to net revenue for 2017. Another factor to impact Clearstream's business in the forecast period will be central bank monetary policy, as it has been in the past. Transaction activity is expected to increase in the medium term, as a result of the ECB's ongoing commitment (at least for 2017) to the programme for purchasing government and corporate bonds. At the same time, however, the continuation of the programme could have a dampening effect on securities issuance and liquidity management. If, contrary to expectations, monetary policy becomes more restrictive, this would have positive consequences for securities issuance, the use of collateral and liquidity management services, as well as for net interest income in the banking business. As a significant portion of customer balances are denominated in US dollars, the turnaround in US interest rate policy – initiated at the end of 2015 and continued in December of 2016 – will cause a rise in net interest income in 2017, at steady cash balance levels.

With regard to its customer structure, the company continues to expect that consolidation in the financial sector will persist and that customers in Clearstream's domestic and international business will merge. These larger customers would benefit from greater discounts, which would lead to a decline in average fees.

Although Deutsche Börse faces especially intense competition in the settlement and custody of international bonds, the company does not expect this to have a major impact on its net revenue or to result in a loss of market share during the forecast period.

Market Data + Services segment

This segment aims to accelerate expansion of Deutsche Börse's technology leadership and expertise in the area of market data by pooling all relevant resources within the company in a dedicated, market-driven business unit. The goal is to open up untapped growth opportunities in the medium to long term.

The company anticipates that net revenue in the Market Data + Services segment will increase slightly during the forecast period. This expectation is based on the continuous expansion of the product range in all areas and greater marketing of these products in growth regions. The Group's index business is set to benefit from this development in particular. Moreover, the Group considers the significant structural growth in the market for passively managed assets as an additional growth driver that is expected to further strengthen demand for index licences for exchange-traded funds. In addition to distributing index licences, the Group also benefits from the growing investment volumes in these products. In light of this, the Group believes it is well placed to increasingly extend the positioning of its globally focused range of indices to the Asian market as well.

Changes in pricing models

Deutsche Börse anticipates sustained price pressure in some of its business areas during the forecast period. The company's objective is to cushion this price pressure by continually improving its products and services and by offering selective incentives for price-elastic business.

Over the long term, the average net revenue per unit (e.g. trading or clearing fees per transaction, or fees for custody services) is expected to decline slightly in all areas of the Group. This is a result of laddered pricing models that lead to a decline in income per unit as customers' business activities increase.

Trends in non-financial performance indicators

Initiatives to promote the transparency and security of the markets will continue to be a key focus during the forecast period, ensuring that Deutsche Börse Group adds value to society. Against this backdrop, the company expects to maintain the availability of the different trading systems Xetra[®] and T7[®] at the very high level seen in previous years throughout the forecast period.

Responsible management that focuses on long-term value creation is of considerable importance for Deutsche Börse Group as a service company. Given demographic change and the resulting shortage of specialist staff, the company aims to continue to position itself adequately and among other things to increase the number of women in management positions. The Executive Board already set a voluntary target in 2010 for Deutsche Börse Group to increase the proportion of women in middle and senior management to 20 per cent and in junior management to 30 per cent by 2020. These targets remain in place. They relate to Deutsche Börse Group worldwide, including subsidiaries.

In accordance with the Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern an Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst (German Act on the Equal Participation of Women and Men in Leadership Positions in the Private and Public Sectors), the Supervisory and Executive Boards of Deutsche Börse AG additionally resolved to maintain the existing quotas of women on the two

management levels below the Executive Board, i.e. 6 per cent on the first and 10 per cent on the second management level. These target quotas relate to Deutsche Börse AG (excluding subsidiaries) and will be valid until 30 June 2017.

Future development of the Group's financial position

The company expects operating cash flow, which is Deutsche Börse Group's primary funding instrument, to remain clearly positive in the forecast period. The Group expects that two significant factors will influence changes in liquidity. Firstly, the company plans to invest some €150 million per year in intangible assets and property, plant and equipment at Group level during the forecast period. These investments will be included in cash flows from investing activities, and will serve primarily to develop new products and services in the Eurex and Clearstream segments and to enhance existing ones. The total amount mainly comprises investments in trading infrastructure and in risk management functionalities. Secondly, the Executive Board and Supervisory Board of Deutsche Börse AG will propose a dividend of €2.35 per share to the Annual General Meeting to be held in May 2017. This would correspond to a liquidity outflow of about €440 million. Apart from the above, no other material factors were expected to impact the Group's liquidity at the time the management report was prepared. As in previous years, the Group assumes that it will have a sound liquidity base due to its positive cash flow, adequate credit lines (see [note 36 to the consolidated financial statements](#) for details), and flexible management and planning systems.

Within the framework of a programme to optimise its capital structure, Deutsche Börse Group generally aims to distribute dividends equivalent to between 40 and 60 per cent of adjusted net profit for the period attributable to Deutsche Börse AG shareholders. In recent years (where the Group's net profit was lower), the dividend payout ratio was kept at the upper end of this range, in order to distribute stable dividends to shareholders. Given that the Group's profit targets were raised in July 2015, in connection with the announcement of the "Accelerate" growth strategy, the company aims for a dividend payout ratio in the middle of the range between 40 and 60 per cent going forward.

Moreover, until 2012 the company distributed a part of freely available funds to shareholders, via share buy-backs. Since 2013, these funds have been used predominantly to support the company's development, as well as to fulfil credit rating and regulatory capital requirements. Against the background of the growth strategy announced in 2015, the company anticipates that in future, freely available funds will increasingly be applied not only to support the Group's organic growth, but also to complementary external growth options.

To maintain its strong credit ratings at Group level, the company aims at a ratio of interest-bearing gross debt to EBITDA of no more than 1.5. The Group expects to reach or slightly come below this figure in 2017, depending on net revenue developments.

The parent company, Deutsche Börse AG, plans to invest some €30 million in intangible assets and property, plant and equipment during the forecast period.

Overall assessment by the Executive Board

The Executive Board of Deutsche Börse AG believes that the company continues to be in a very good position compared with the international competition thanks to its comprehensive offering along the securities trading value chain and its innovative strength. Against this background, it therefore expects to see a

positive trend in its results of operations in the long term. The purpose of the measures resolved – and mostly implemented – in 2015, as part of the “Accelerate” programme, is to further accelerate the Group’s growth. In this context, the Group aims to act in a more agile and effective manner, and with increased client focus, to turn Deutsche Börse into the global market infrastructure provider of choice, being top-ranked in all its activities. However, for the forecast period, the uncertainty as to how capital market participants will react to the economic and regulatory situation makes it difficult for the Executive Board to make a specific forecast. Deutsche Börse Group’s goal for the forecast period is to ensure the scalability of its business model. To this end, the Executive Board will actively manage operating costs in a way that net profit for the period attributable to Deutsche Börse AG shareholders will grow at a stronger rate than net revenue. Specifically, annual growth rates of approximately 10 to 15 per cent (excluding non-recurring effects) are projected for the forecast period. Overall, the Executive Board assumes on this basis that cash flow from operating activities will be clearly positive and that, as in previous years, the liquidity base will be sound. The overall assessment by the Executive Board is valid as at the publication date for this combined management report.

Deutsche Börse AG (Disclosures based on the HGB)

In contrast to the consolidated financial statements, the single-entity financial statements of Deutsche Börse AG are not prepared in accordance with International Financial Reporting Standards (IFRSs) but with the German Commercial Code (Handelsgesetzbuch, HGB) and the supplementary provisions of the German Stock Corporation Act (Aktiengesetz, AktG).

Deutsche Börse AG compiled its annual financial statements for the 2016 financial year pursuant to the Bilanzrichtlinie-Umsetzungsgesetz (German Accounting Directive Implementation Act, BilRUG), which called for changes in particular to the definitions of revenue and other operating income. To ensure comparability, the BilRUG has also been applied to the previous year’s figures for these two items as reported in the following.

Business and operating environment

General position

Deutsche Börse AG is the parent company of Deutsche Börse Group. Its business activities primarily comprise its cash and derivative markets as well as IT and Market Data + Services. The performance of the Clearstream segment is primarily reflected in Deutsche Börse AG’s business performance via the profit and loss transfer agreement with Clearstream Holding AG. In view of this, Deutsche Börse AG’s business and operating environment is essentially the same as that of Deutsche Börse Group. These are described in detail in the [“Macroeconomic and sector-specific environment”](#) section.

Deutsche Börse AG’s course of business in the reporting period

Revenue for the 2016 financial year remained within the company’s guidance. At the same time, total costs increased only slightly, thanks to continuous enhancements in operating efficiency due to the “Accelerate” programme launched in 2015. Net profit increased significantly, due, among others, to the divestment of International Securities Exchange Holdings, Inc. (ISE), and exceeded the company’s expectations. Against this background, Deutsche Börse AG’s Executive Board considers the company’s performance during the 2016 financial year as satisfactory. The 2016 financial year was largely characterised by plans for the merger of Deutsche Börse with London Stock Exchange Group (LSEG).

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