DEUTSCHE BÖRSE
GROUP

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Financial report 2015

Excerpt: report on expected developments

Report on expected developments

The report on expected developments describes Deutsche Börse Group's expected performance in financial year 2016. 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 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. Moreover, the Group predicts that economic growth in the industrialised nations will continue to recover after a number of difficult years following the financial crisis. However, growth is likely to be lower than expected in 2015, mainly reflecting lower growth than expected in the US, due to the stronger US dollar. With respect to Europe, the Group is also forecasting a slight improvement in the economic situation, in particular because southern European countries such as Spain have shown a marked recovery. In view of this essentially positive situation, the company expects participants to place confidence in the capital markets at a level similar to that of the previous year. However, current uncertainties could unsettle the markets again. These include geopolitical crises, the development of the commodities prices, the monetary policy adopted 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. In December 2015, the ECB announced an extension of its bond-buying programme until March 2017 and a deposit rate reduction to –0.3 per cent. This additional capital market liquidity should continue to have a positive effect on trading volumes on the cash and derivatives markets. The turnaround in US interest rates materialised at the end of 2015, as expected. Given the slowdown in economic growth, the company does not expect any further hikes for the time being.

In its economic development forecast for 2016 published in January 2015, the International Monetary Fund (IMF) predicts an increase of around 1.7 per cent in the euro zone and growth of around 1.7 per cent in Germany. Expectations for the United Kingdom and the United States are slightly higher than for the euro zone: the UK economy is forecast to grow by around 2.2 per cent in 2016 and the US by around 2.6 per cent. The highest growth by far in 2016 – approximately 6.3 per cent – is again expected in Asian countries (and especially China), due to 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 2016.

Regulatory environment
Governments and central banks are currently working to enhance regulation of the financial markets so as to further 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 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 2016 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, cyclical conditions, especially stock market volatility, have improved significantly since the end of the third quarter of 2014 and are having a positive effect 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 Exchange, whilst higher US interest rates could lead to a slight increase in net interest income from the banking business in 2016. Secondly, the Group expects a further increase of the contribution from its structural growth initiatives as well as 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 functionality, Deutsche Börse Group expects net revenue to increase by approximately 5 per cent to 10 per cent annually during the forecast period and the following years. Net revenue growth expected during the forecast period is based on pro-forma net revenue of approx. €2,423 million achieved in 2015. The figure comprises reported net revenue of €2,367.4 million, plus approx. €56 million to annualise the effects of full consolidation of the APX power exchange (part of EEX group), effective 1 May 2015, and of 360T Beteiligungs GmbH (360T), effective 1 October 2015.

Even if, contrary to expectations, the business 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 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 range of 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. Operating costs expected during the forecast period are based on pro-forma operating costs of €1,296.0 million in 2015. The figure comprises reported operating costs of €1,248.8 million, plus €47 million to annualise the effects of full consolidation of APX Holding group, Indexium AG and 360T Beteiligungs GmbH.

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 will be simplified, generating costs savings expected to amount to roughly €5 million during the reporting period. Aggregate savings are targeted to rise to €50 million by 2018. Secondly, the Group resolved a series of structural cost reduction measures during the reporting period, and already commenced implementation. To this end, the Group's management structure was streamlined by removing hierarchical levels, in order to boost decision-making speed and agility. Operating efficiency will be further enhanced through a merger of functions into competence centres, and further improvements in purchasing and procurement. The Group is looking to generate savings of approximately €50 million during the forecast period. Overall, the Group will thus create €100 million in additional investment capacity by 2018. As at the publication date of this combined management report, the company is expecting that operating costs will be affected by exceptional items of some €75 million. One half is due to efficiency measures and costs related to criminal proceedings against Clearstream Banking S.A. in the US. The second half is related to mergers and acquisitions, in particular to the integration of companies acquired in 2015.

Given the expected increase in net revenue of approximately 5 to 10 per cent, with operating costs rising by between zero and 5 per cent as a result, the Group anticipates a growth rate of between approximately 10 and 15 per cent per annum (excluding non-recurring effects) for EBIT and consolidated net income during the forecast period and the subsequent years.

With regard to the cyclical environment and structural growth initiatives, Deutsche Börse AG's 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 the report on expected developments. For 2016, the company expects sales revenue to be above the 2015 level (2015: €1,182 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 p.a. (excluding non-recurring effects) for adjusted EBIT and adjusted net profit attributable to Deutsche Börse AG shareholders for the forecast period and the subsequent years.

Eurex segment

In the past year, cyclical factors (see the "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). However, it is also of the opinion that, in the short term, positive cyclical effects on the business environment will lead to an increase in trading volumes, especially in the area of equity index derivatives and – depending on the US and European monetary policy – interest rate derivatives.

Eurex will continue to invest systematically in implementing its technology roadmap and expanding its product offering in the forecast period. Its investment focus will continue to be on risk management. For example, all listed derivatives will be processed exclusively through the new C7 clearing architecture. Among other things, these new features are being implemented to further enhance the attractiveness from a customer perspective of clearing services for OTC derivatives trading. In the medium to long term, the company expects this initiative to deliver significant additional net revenue. Since the new regulatory requirements for settling OTC derivatives transactions via a central counterparty will finally enter into force in the course of 2016, the Group does not yet anticipate any material additional contribution to net revenue for 2016 from these investments. Looking at the 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. Moreover, the Group expects rising demand for multi-bank platforms to further boost business activity at the foreign exchange platform 360T®, acquired in 2015. As for the cyclical business drivers in the Eurex segment, persistently high stock market volatility could continue to boost business activity. Stock market volatility at the level seen in the last months before the publication of this report would have a significant positive impact on trading in equity index derivatives. Furthermore, market speculation on central banks' monetary policy, triggered by the US Federal Reserve's interest rate hike at the end of 2015, might lead to higher trading volumes in interest rate derivatives.

Xetra segment

As in the past, net revenue in the Xetra cash market segment will continue to depend on equity market trends and equity market volatility in the future, as well as on structural and cyclical changes in trading activity.

Stock market volatility increased significantly since the end of the third quarter 2014 and led to increased trading volumes in the cash market, in some cases significantly so. As at the date of preparation of this management report, the company expects stock market volatility to remain high in 2016. In addition, the ECB's persistently expansive monetary policy is expected to have a continued positive effect on demand for equities. As a result, a slight year-on-year increase in net revenue can be assumed compared to the year under review.

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 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 minor capital market fluctuations. The Group anticipates a structurally driven increase in demand for collateral and liquidity management services due to regulatory requirements. In addition, Clearstream will make further preparations for TARGET2-Securities (T2S), the European Central Bank's future central settlement platform, during the forecast period. In the medium to long term, Clearstream expects its attractive collateral and liquidity management and its strong position in the T2S network to result in increased business activity and hence in significant additional net revenue. However, since the new partners can only be connected consecutively and Clearstream itself will not be linked in to T2S until 2017, the Group initially anticipates only a moderate contribution to net revenue for 2016. The central banks' monetary policy in the forecast period will continue to have an impact on Clearstream's business. Transaction activity is expected to increase in the medium term as a result of the programme for purchasing government and corporate bonds launched by the ECB in March 2015 and expanded during the course of the year. At the same time, however, this 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. Given a steady level of cash balances, the reverse of the US interest rate policy at the end of 2015 will cause a rise of net interest income in 2016, because a significant proportion of the Group's customer balances are denominated in US dollars.

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 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 CR

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 of 2016.

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 upper management to 20 per cent and in lower 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 zur gleichberechtigten Teilhabe von Frauen und Männern an Führungspositionen (German Act on the Equal Representation of Women and Men in Executive Positions), the Executive Board 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 the trading infrastructure and risk management functionality. Secondly, the Executive Board and Supervisory Board of Deutsche Börse AG will propose a dividend of €2.25 per share to the Annual General Meeting to be held in May 2016. This would correspond to a liquidity outflow of €420.1 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 July, 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 – as implemented in 2015, with the acquisition of STOXX Ltd. and 360T Beteiligungs GmbH.

To maintain its strong credit ratings at Group level, the company aims to achieve a ratio of interest-bearing gross debt to EBITDA of no more than 1.5. The Group expects to reach or slightly exceed this figure in 2016, 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 partially 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 EBIT and 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 and the following years. 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.

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