

Merge or bust for local bourses

Asia-Pacific exchanges must expand across borders, argue **Ivan Png** and **Chi-Wo Cheng**

June has been a momentous time for financial exchanges. On June 1, Euronext, which operates the Amsterdam, Brussels, Lisbon, and Paris stock exchanges, and the Liffe derivatives exchange, accepted a €7.9 billion (\$13.4 billion) offer from the New York Stock Exchange.

On June 6, the Treasurer approved the takeover by the Australian Stock Exchange of SFE Corporation. Yesterday, following investor pressure, the ASX announced SFE chief executive Robert Elstone would assume the merged entity's top post. SFE shareholders will vote on the proposed merger on July 5.

The ASX-SFE merger should be considered as just the first step towards international consolidation. Besides the NYSE-Euronext merger, Nasdaq has bought 25 per cent of the London Stock Exchange, and Euronext itself is negotiating to acquire Borsa Italiana.

The consolidation of financial exchanges is being driven by the substantial fixed costs of technology. Exchanges can reap economies of scale and scope by spreading these fixed costs over larger trading volume, more share listings, and more financial products such as derivatives.

The organisation of financial exchanges is subject to another trend — vertical disintegration. Buying and selling shares, derivatives, and other financial instruments on an exchange actually involves three services — trading, clearing, and settlements.

Traditionally, exchanges provided all three services in a vertically integrated "silo". Owing to fixed costs of technology, exchanges are tending to specialise in trading, while other entities specialise in clearing and settlement.

In 2003, Liffe and Euronext merged their clearing services,



Huge markets like the NYSE, which recently merged with Euronext, may suck our region dry of issuers and traders.

Photo: AP

London Clearing House and Clearnet, to form LCH.Clearnet, now Europe's largest clearing house. LCH.Clearnet's ultimate goal is a single pan-European clearing house.

Euronext specialises in trading, while outsourcing clearing to LCH.Clearnet, and custody and settlement to various national depositories. The LSE has recently proposed to let traders choose to clear

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with LCH.Clearnet or SIS x-clear.

By contrast, the Asia-Pacific region seems quiet. The ASX-SFE merger is national rather than international in scope. Further, the ASX-SFE and other exchanges in this region still follow the vertically integrated model of operation.

Yet Asia-Pacific exchanges

confront the same economic imperatives as European and US exchanges. Exchanges face competition in listings. The ASX may have a monopoly over listings in Australia, but it doesn't have a monopoly over listing of Australian companies. News Corporation is listed on the NYSE and ASX. BHP Billiton is listed on the LSE and ASX.

Exchanges face competition in trading as well. Traders in US-listed shares may deal directly with one another, or indirectly through "over the counter" brokers, or new intermediaries. More than half of trading in Britain and Germany-listed shares takes place outside the respective exchanges.

Should Asia-Pacific exchanges merge to reduce the cost of providing trading systems? Should they establish a regional clearing house — which would lower the costs for trading throughout Asia?

It is time for exchanges in our region to address these issues. The

barriers are high — besides plain protectionism, laws and regulations differ substantially.

Yet to do nothing would be very short-sighted. Mammoth markets like the NYSE-Euronext may suck away issuers and traders, leaving Asia-Pacific exchanges to become regional backwaters.

The ASX has been a pioneer in restructuring. In 1998, it was the first exchange in the region to demutualise and list its shares on itself. After the SFE merger, it will be well placed to lead on international consolidation and specialisation.

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Change is difficult but necessary

John Pesutto

Labor's proposal to abolish Australian workplace agreements (AWAs) would impede terms and conditions and deprive individuals of choice. It is being pitched to a public seen as nervous about change.

Under such conditions, fear is not easily allayed nor anger assuaged. Crucially, many may overlook the mechanisms in place to protect rights and preserve balance.

Why abolish AWAs when they are subject essentially to the same protections as non-union employee collective agreements under the Work Choices legislation? If the debate is really about the adequacy of employee protections, let's look at just some.

Under Work Choices, employers, employees and their unions can agree to remove protected award conditions such as overtime, penalty rates and annual leave loading.

It is said that the ability to remove these award conditions, albeit only by agreement with employees (and their unions), betrays an intention to undercut pay and conditions. This fails to recognise provisions that protect existing employees who refuse to sign workplace agreements removing these award conditions.

Take an employee who refuses to sign an AWA. Let's say the

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employer decides to allocate shifts, otherwise attracting penalty rates, to those who have signed away penalty rates for a higher hourly rate of pay in their AWA. Assume the employer decides to reallocate to the employee opposed to the AWA shifts not otherwise attracting penalty rates. Suppose the employee is upset at the prospect of losing normal hours that had attracted penalty rates.

The employer may be liable under the act to a penalty and to pay compensation for discriminating against that employee because his employment is covered by an award.

The consequences for employers who refuse to recognise unions are just as serious. These protections exist not only in respect of workplace agreements, but also in the area of freedom of association.

Employers must allow unions an opportunity to confer with the employer about a workplace agreement. If employers fail to provide the prescribed information to employees asked to sign an AWA, they commit a breach. The information covers matters such as the right to be represented by a union.

Employers can face serious financial penalties if they breach the new act. They have many new opportunities to consider, but as many obligations to remember.

Change is difficult. It might have been easier for the government to defer major reform in workplace laws at a time of general economic wellbeing and avert the political costs. But leaders whose incumbency defines the history of their time respond as well to prosperity as to adversity. Their purpose and urgency, more than just the course of events, fashion the circumstances of their leadership.

Leaders who stand still will not trip; but nor will they cultivate an enduring legacy.

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An emission of fact on nuclear energy

I am an engineer who has worked on almost every way of generating electricity: alternative energy, nuclear energy, black and brown coal, gas and hydro. From my standpoint all these forms of generating electricity can be adequately safe and there are well-established ways of dealing with their wastes. The only exception to this is carbon dioxide emission, which has not been resolved.

Nuclear generation was, until a few weeks ago, not on the list in Australia. A Nuclear Activities (Prohibitions) Act, which forbids everything to do with nuclear power and the nuclear fuel cycle including exploring for uranium and thorium, was passed in Victoria in 1983 and in NSW in 1986. Other states have similar legislation.

It's hard to remember the situation in 1983. The concept of global warming due to greenhouse gases was not on the political agenda. Governments at the time probably envisaged a future of cheap coal-fired plants.

By the 1990s the discussion had changed. As a consequence of the new understanding of greenhouse gases, the future for fossil fuel stations became less clear. Growth since that time has been covered by operational improvement and new

The cost of reducing greenhouse gases works against the existing generating groups, argues **John Price**.

natural gas stations, but this period of relaxed decisions is ending.

Australia faces the prospect of having to add another 10 gigawatts to 12 gigawatts in the next 10 years. The bulk sources of energy available for electricity production are natural gas, coal and, if permitted, nuclear.

The new entrants must deal with two issues, emissions and cost.

One comparison of carbon emissions is an International Atomic Energy Agency Bulletin paper in 2000 by Joseph Spadaro, an environmental engineer, using a unit — grams of carbon equivalent emissions per kilowatt hour (kWhr) of electricity. New brown coal technology produced 228 units, new black coal produced 206 units, new natural gas (combined cycle) produced 106 units. Nuclear was the lowest at 2.7 units including enrichment and reprocessing.

Additional technologies have arrived for coal, in particular integrated gasification combined cycle (IGCC). The Australian consortium, Coal 21, suggests a further reduction of 50 per cent is possible with IGCC, which will bring coal carbon dioxide emissions into the range of natural gas emissions.

These technologies increase cost but also increase efficiency and may be economic without significant subsidy.

Then there are zero emission concepts. These involve separating the oxygen from the air, a process involving quite a large factory in its own right, and then burning the coal or gas in pure oxygen (a process called oxy-fuel burning). The resulting nearly pure carbon dioxide flue gases are sequestered. Sequestration involves injecting carbon dioxide under pressure into permeable strata underground or perhaps into cold sea layers.

This group of technologies increases costs and reduces efficiency so that perhaps twice as much fuel must be burnt. When sequestration is a long way from the power station there will be high pumping costs.

The annual market average price in NSW is 3.76¢ kWhr ranging to 2.83¢ kWhr in Queensland and this price is dominated by coal-burning power stations.

The power stations are reportedly scarcely making a profit, let alone an attractive return on capital. New coal entrants will be required to add

emission reduction equipment, which will depend on regulatory requirements. Economic evaluation of these technologies is not available. In any case, costs are highly site specific and will depend on the permitted emission levels.

A large factor in cost estimates for new entrants is the rate of return required by the investors. According to recent studies, the generating cost for nuclear power goes from 4.3¢ a kWhr if a discount rate of 5 per cent is used to 10¢ a kWhr if a discount rate of 12.5 per cent is used. In a Danish paper about wind power the costs go from 8.6¢ to 12¢ when the discount rate changes from 5 per cent to 10 per cent.

Having looked at this data it seems that nuclear power could fit into Australia's future energy mix and may be important for low-cost base load supplies.

Until site specific opportunities are made available for comparative bids we will not know what technologies are competitive, what their emission burdens are and what market guarantees are required. If no action is taken, Australia will build mainly natural gas-fired plant.

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