# Frankfurt intends to "go it alone" in creating pan-European stock exchange

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The "strategic alliance" between the London Stock Exchange and its German counterpart, Deutsche Börse, announced 17 months ago has broken down, with the latter's announcement that it intends to create its own pan-European exchange.

The joint venture was initially planned to start from January 1999, to coincide with the launch of the euro. It was to begin by trading Europe's top 300 shares. The move was hailed by British and German finance centres as ending the war between the two exchanges for supremacy in Europe's rapidly converging financial markets. The *Financial Times* described the alliance as marking "a giant step towards the creation of a single European stock market", whilst *Das Handelsblatt* wrote that it would create the "kernel for building a unified European stock market".

However, earlier this month Deutsche Börse announced that it intended to go it alone by converting into a public company and becoming a pan-European exchange under the new name, Euroboard.

Although Deutsche Börse said it hoped to "quickly establish a single European cash market together with the exchanges of the European Exchange Alliance", the decision apparently came as a surprise to other European exchanges, which had not been notified about the plans.

The combined exchange was motivated by the need of European capital to compete more effectively against the United States. At a market capitalisation of £2.03 trillion, the combined London-Frankfurt exchange was to be second only to New York, at £6.05 trillion. It was also aimed at forcing the smaller European bourses into line with the new exchange, or risk losing out completely.

The new trading platform was subject to severe competition from other exchanges, especially from New York, and the growth of new electronic communications networks (ECNs), which have cut the cost of share trading.

London and Frankfurt agreed earlier this year to synchronise their trading hours as part of creating a single Euro-stock market. The move was almost immediately matched by the New York exchange signalling its intent to open earlier to trade European stocks.

The Deutsche Börse decision was undoubtedly hastened by last month's announcement by Nasdaq, the US hi-tech exchange, that it would launch a European stock exchange, based in London, within 18 months. This meant that disagreements inside the alliance of European exchanges undermining Frankfurt's position could no longer be tolerated.

The alliance had always been subject to the competing interests of its two prime movers. London is almost twice as big as Frankfurt, but its decision to enter an equal partnership was dictated by its concern that, outside “euro land”, London would be left behind in single currency trading.

For Frankfurt, the alliance with London would give it international standing. According to its web site, Frankfurt is "the largest and financially strongest European exchange organisation", and "it is already the leader in transactions on the European capital markets, in both the cash market and the derivatives market".

Although the smaller bourses in Amsterdam, Brussels, Madrid, Milan, Paris and Zurich eventually came around, the plans for a grand alliance of all Europe's stock markets had been criticised for months for proceeding too slowly and being subject to too many disagreements between its eight competing exchanges.

Plans to set up a joint company to control the venture also ran into problems of how ownership of the new market would be divided. Deutsche Börse is 80 percent controlled by Germany's banking sector, whilst the London exchange is owned equally by its members. Disagreements over the technology to be used in the new exchange also divided the European alliance. The London-Frankfurt exchanges had suggested using Xetra, Frankfurt's existing trading system, as the technology for the pan-European exchange, but the six other exchanges rejected the proposal on the grounds that it would mean them having to replace their own systems and hand Frankfurt a competitive advantage.

In September, Deutsche Börse Clearing (DBC), a subsidiary of the exchange, merged with the Luxembourg cross-border clearing house Cedel. The two then invited the French clearing house Sicovam to join, but as an unequal partner. Unable to get agreement, Sicovam went into a rival alliance in November with Euroclear, Cedel's main competitor. By November, the alliance announced that its single trading platform objective would be downgraded to linking trading systems into a "virtual exchange".

Deutsche Börse has clearly decided that its ability to play a leading role in any pan-European venture can be secured only by striking out alone. Whilst sceptical of Frankfurt's success, financial analysts have warned that, with the European Central Bank located in Frankfurt, and Germany the economic engine of the entire single market project, the plan should not be dismissed. London should be especially concerned over the end of the European alliance, the *Financial Times* warned on December 6. Quoting financial expert Fields Wicket-Miurin that "The end-game is European domination," it opined, "there has been little sign of London devising an aggressive alternative, as its German partner has done. Without such an alternative, London's place in the pan-European stock market of the future is in doubt".