

Supplementary Information on “London-Hong Kong Connect”

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Hong Kong Exchanges and Clearing Limited (HKEx) Group proposes to build “London-Hong Kong Connect” to link the commodities markets in Hong Kong and London.

1. What is “London-Hong Kong” Connect?

“London-Hong Kong Connect” is an innovative mechanism to link different markets following HKEx’s successful launch of Shanghai-Hong Kong Stock Connect in November last year.

Under the proposal, a trading link between Hong Kong Futures Exchange Limited (HKFE) and the London Metal Exchange (LME), and a clearing link between HKFE Clearing Corporation Limited (HKCC) and LME Clear Limited (LME Clear) would be established separately.

If implemented with all necessary regulatory approvals and rules in place, “London-Hong Kong Connect” will enable HKFE’s eligible Exchange Participants to trade LME products, and HKCC’s eligible Clearing Participants to clear those trades.

2. Why “London-Hong Kong Connect”?

The proposed “London-Hong Kong Connect” makes sense to users in Hong Kong, Mainland China as well as other international markets.

The LME is the world centre for industrial metals trading, and the world’s metal community uses the LME to trade futures and options contracts of 11 base metals including copper, aluminium, tin, nickel, zinc and lead. Prices are discovered on the LME and used as the global reference.

After the successful acquisition of the LME in December 2012, HKEx has carried out business consolidation, built LME Clear and reformed the warehouse system, with the vision to link China with the world by leveraging the LME platform.

China is the biggest importer of commodities in the world and a growing number of Mainland companies need to hedge their risks through the financial futures market.

Furthermore, China’s implementation of the Belt and Road Initiative is expected to bring tremendous opportunities to the commodities market.

The Belt and Road Initiative covers more than 60 countries. Some expect it could bring over US\$2.5 trillion in trading with China in the next ten years and the majority of the trading volumes would be related to commodities.

For Mainland China, how to effectively manage the fluctuations in commodities prices will have direct impact on the implementation of the initiative.

The LME is the world centre for risk management in the global metals industry with more than 80 per cent of global non-ferrous metals business conducted on its trading platforms. The LME network has more than 700 warehouses across 38 locations in 14 countries and regions, with over 500 of them across 26 locations along the Belt and Road countries and regions.

However, due to trading costs and other barriers, China remains under-represented and under-hedged on the LME relative to its size in global production and consumption.

The proposed link will lower the trading costs and barriers, and help Chinese companies and investors to better manage their hedging risks through LME products. Mainland Chinese investors will also benefit from a broad variety of investment opportunities, enabling them to internationalise their asset allocation.

“London-Hong Kong Connect” could also enable Mainland companies and investors to trade commodities on Hong Kong’s trading platforms, which they are more familiar with. They could use the proposed link to participate in the international price-setting ecosystem, with the aim to influence the price setting process.

Hong Kong would also see benefits from the proposed link. It facilitates Hong Kong brokers to directly access LME products for their clients in a low cost way, clearing in Hong Kong will enhance capital efficiency, and increased liquidity in the Asian time zone will help develop Hong Kong into a commodities trading hub. Overall, it enhances Hong Kong’s strategic role as the primary risk management and wealth management centre for Chinese and other Asian investors will be further enhanced by the proposed link.

After the implementation of “London-Hong Kong Connect”, HKEx intends to roll out more RMB-denominated futures and commodities products to promote RMB internationalisation and further enrich investment products in the offshore RMB market.

3. When will “London-Hong Kong Connect” be launched?

Implementation of the trading and clearing links is subject to regulatory approval in Hong Kong, the United Kingdom and the European Union. No formal agreement has been entered into and HKFE, HKCC, LME and LME Clear will discuss the types of products to be included, the operational model, the system requirements and other related issues with the relevant regulators, and update market participants in due course.