In September 2019, the Hong Kong Stock Exchange (HKEX) made an out of left field bid to acquire the London Stock Exchange (LSE). The GBP 32 billion offer by the Hong Kong bourse – which saw the LSE's shares priced in at GBP 83.61 a piece, representing a 23% premium over the shares' daily price[1] – was reportedly set off by a surprise visit by HKEX CEO Charles Li Xiaojia 李小加 to the LSE[2]. The HKEX's original pitch was a mix of cash and equity. However, the bid was almost immediately rejected by the LSE[3].

In early October this year, the HKEX's dream of acquiring the centuries-old LSE was shattered. The LSE proposed a 20% increase from the original offer and asked for cash to comprise a larger portion of the offer[4]. Such a demand rendered the HKEX unable to proceed with a new offer, as some HKEX shareholders expressed dissatisfaction with the LSE's proposal[5].

While the economic interests of such a merger are obvious – a merger between two of the world's largest bourses would give the struggling Hong Kong economy a much needed boost – the underlying motivations become increasingly mysterious when examining the LSE's initial rejection of the bid. In its September 13th "Rejection of Conditional Proposal from HEXK", the LSE highlighted – among many other variables such as serious regulatory hurdles to overcome – that "We value our mutually beneficial partnership with the Shanghai Stock Exchange which is our preferred and direct channel to access the many opportunities in China"[6].

The above statement reveals a number of changes in the global economic landscape, as well as a possible ruse by the Chinese government. For one, the LSE's statement shows that while Hong Kong will remain a gateway to the Chinese market in the short term, its position is dwindling. This is, of course, due large in part to economic and political uncertainty in Hong Kong, but also the recent waves of financial and banking liberalization in China, which has clearly caught the attention of major global players. If the LSE is to be believed, the long-term global economic landscape may see the extinction of Hong Kong.

On a more interesting note, however, could the HKEX bid simply have been a sleight of hand play by the Chinese government? According to an article published by the *South China Morning Post* on October 5th, the decision to make the offer was reached in September 2018 at a meeting of the HKEX directors – the bid for the LSE was seen as a strategy to diversify the HKEX's business model, which has mostly comprised providing mainland Chinese firms a channel to go public on the international stage[7]. However, the HKEX sat on its bid for a year, and pursued it at the peak of anti-government protests – why?

Let us be clear, an offer of this size must have been reviewed and approved by the central government. A merger which has a significant impact on the mainland Chinese economy – via Hong Kong – could not have simply been a decision made by the HKEX's board of directors. As such, given that the timing of the bid coincided with strong anti-government protests, we here at Cercius Group believes that the HKEX's bid for the LSE was a play by the central government.

The play is sophisticated: a struggling economy hit by anti-government protests is sliding into recession, and its bourse makes a bid for a competitor in an attempt to revitalize economic sentiments. Taken at face value, the bid makes sense. However, the fact that the LSE stated that it preferred Shanghai provided a hint to the true nature of the bid. When seen from the perspective of the central government, this bid proved the declining value of Hong Kong as an economic conduit, and that its recent financial and banking reforms have started to yield dividends in the form of investor confidence. Shanghai, then, is slowly being seen as an alternative – and an attractive alternative at that – to Hong Kong. Therefore, for the central government, the HKEX's bid – which would have been approved by the central government – was aimed at testing the international waters to see if Hong Kong's value as a conduit was still there, and if its recent financial and banking liberalization policies have attracted any attention.

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[1] https://www.economist.com/finance-and-economics/2019/10/10/hong-kongs-pursuit-of-the-london-stock-exchange-ends-in-tears
[2] https://www.bloomberg.com/news/articles/2019-09-11/lse-may-have-plenty-of-defenders-in-fending-off-hong-kong-bid
[3] https://www.lseg.com/resources/media-centre/press-releases/rejection-conditional-proposal-hkex
[4] https://www.scmp.com/business/companies/article/3031499/some-lse-investors-call-hong-kong-exchanges-and-clearing
[5] https://www.scmp.com/business/companies/article/3031598/hkex-shareholders-against-raising-bid-lse-after-some-investors
[6] https://www.lseg.com/resources/media-centre/press-releases/rejection-conditional-proposal-hkex?accepted=acfb844a83f45fa1f5248d5758ebf498
[7] https://www.scmp.com/business/companies/article/3031625/why-hong-kong-wanted-london-stock-exchange-so-badly-and-how-its

In fact, the bid was a win-win play. Not only did it allow the central government to gain a better understanding of how the global community views Hong Kong versus the mainland – as economic nodes – but had the bid gone through, it would have consolidated Hong Kong, and by extension, the mainland's economic interests.