



BM&F BOVESPA

The New Exchange



BM&F BOVESPA S.A.

- **Demutualization and International Trends**

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June/2008

SUMMARY

- **Trends since the 90's and their Consequences**
- **An Overview of the Capital Market in the World**
- **The Demutualization Process**
- **Perspectives for the Capital Market in Latam**
- **The Brazilian Case**





Trends since the 90's and their consequences



Trends since the 90's

GLOBALIZATION

Overseas competition for listing and trading

CLIENTS' DEMANDS

Liquidity, trading efficiency, new products and lower costs

EXCHANGES

TECHNOLOGICAL ADVANCES

Algorithms and Program Trading
Outcome: commissions reduction

ALTERNATIVE TRADING SYSTEMS

Trading through ECNs and internalization of orders



Consequences

CONVERGENCY

Cash Market
and Derivatives in the
same stock exchange

ELETRONIC TRADING PLATAFORMS

Replacement of the
Open-Outcry trading scheme

EXCHANGES

DEMUTUALIZATION

Transparency and
Strategic flexibility

CONSOLIDATION

Challenges: valuation
expectation and anti-trust
issues

REGULATION

Conflicts: jurisdiction and
self-regulation

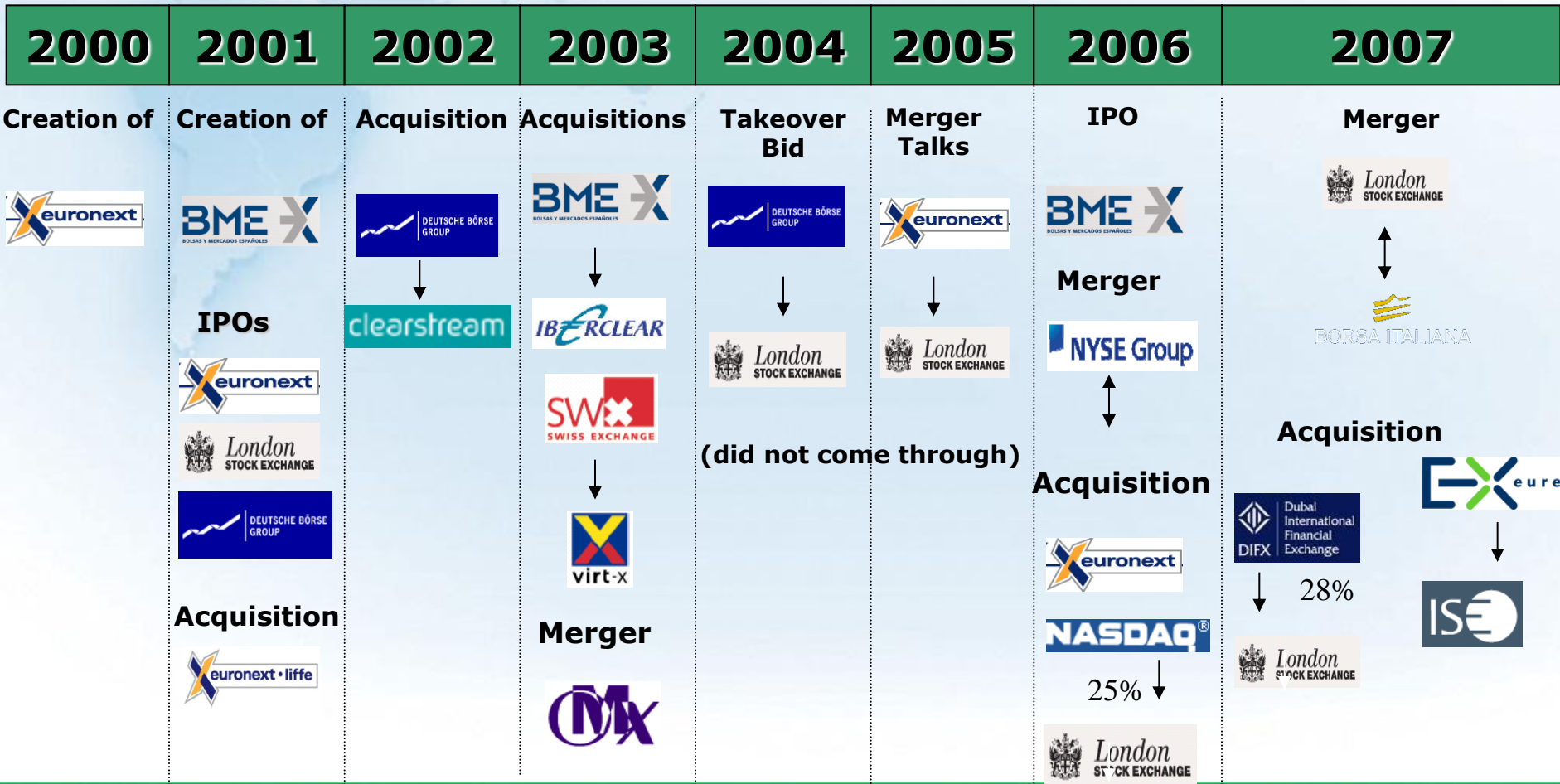




An Overview of the Capital Market in the World

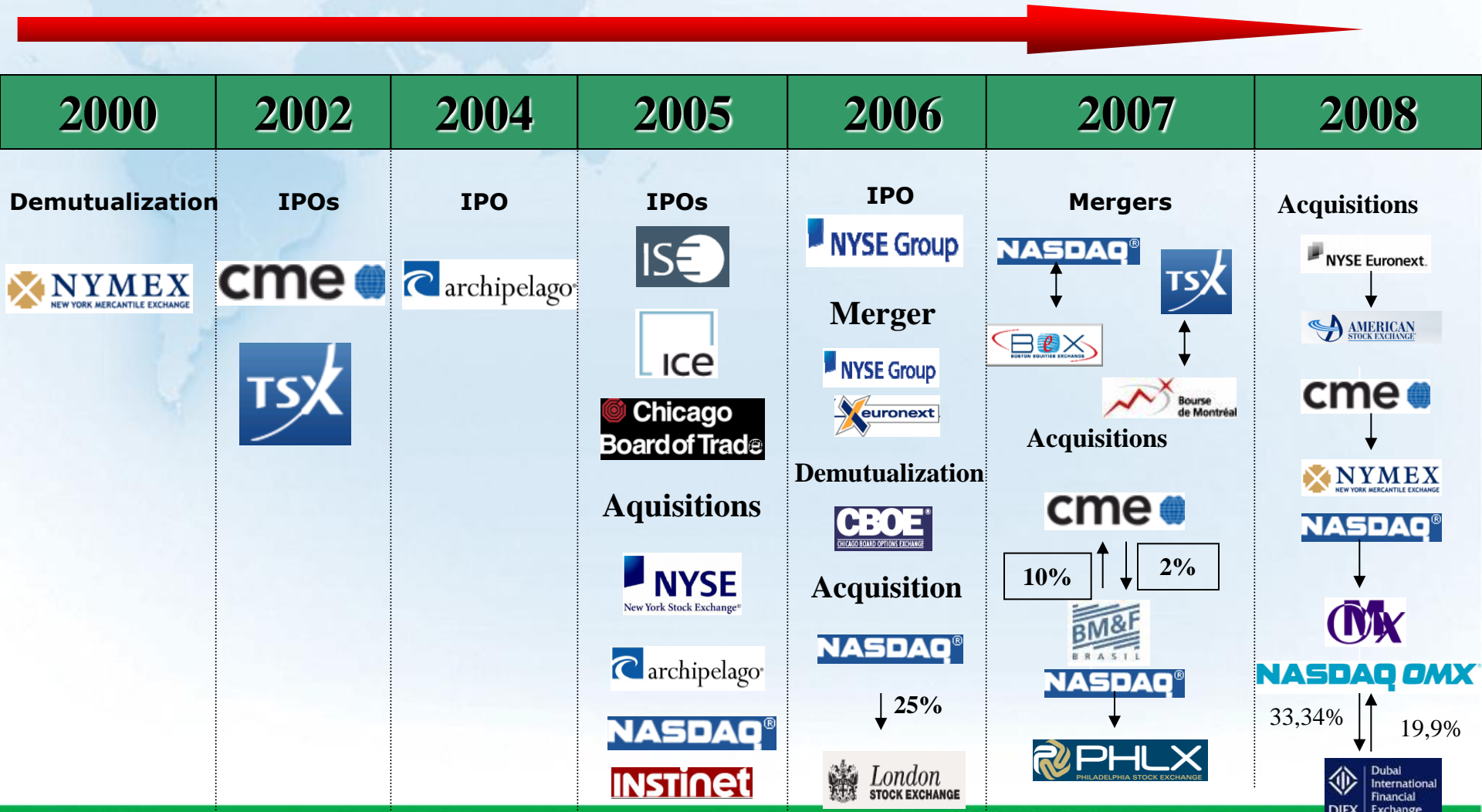


European Landscape Mergers, Demutualization and IPOs



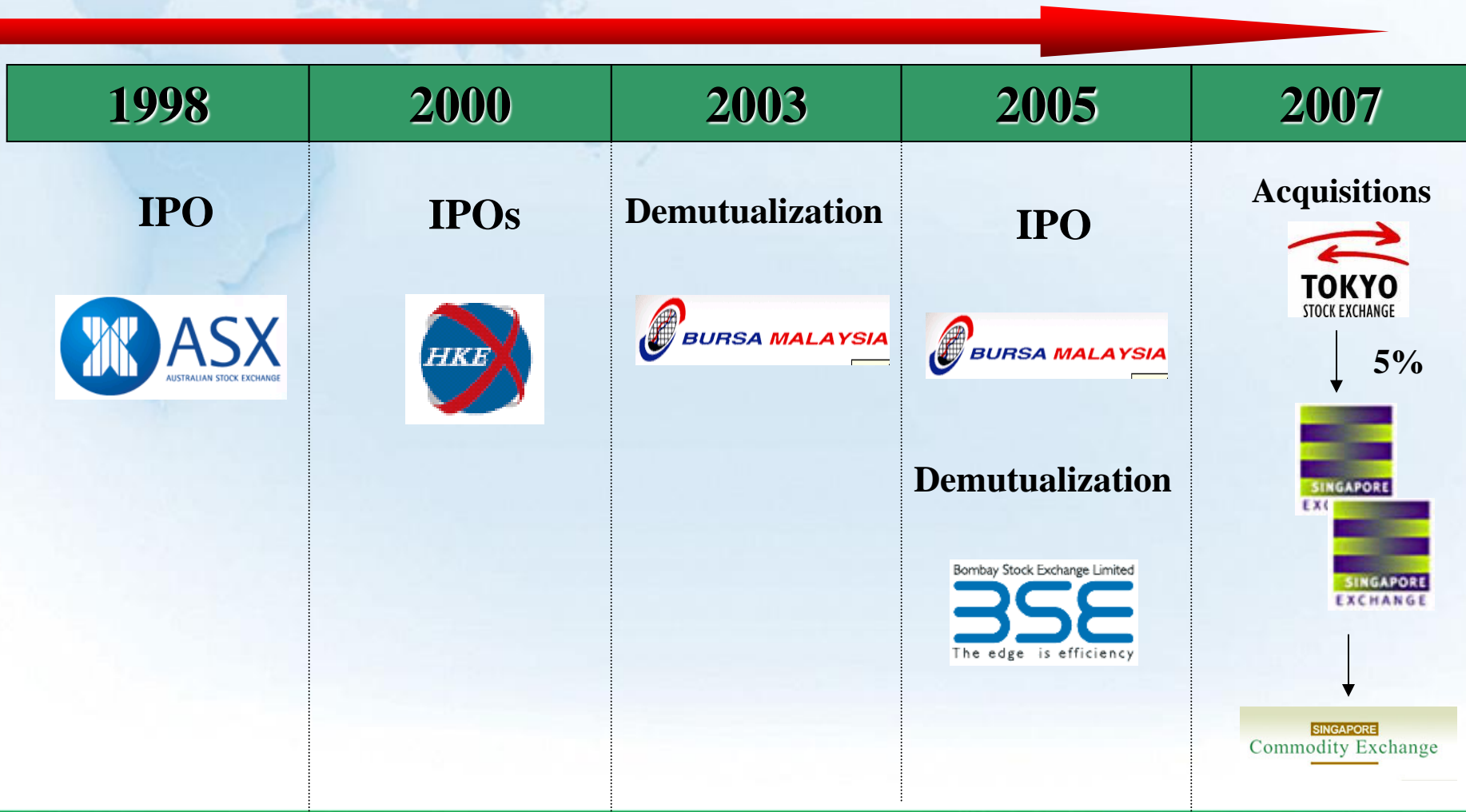
North-American Landscape

Mergers, Demutualization and IPOs



Asian Landscape

Mergers, Demutualization and IPOs



Probable Listings on the way...

North America

- ✓ NYMEX
- ✓ CBOE
- ✓ New York Board of Trade

Asia

- ✓ Bombay Stock Exchange
- ✓ Korea Exchange
- ✓ Tokyo Stock Exchange

Shares' Price Evolution of Listed Exchanges

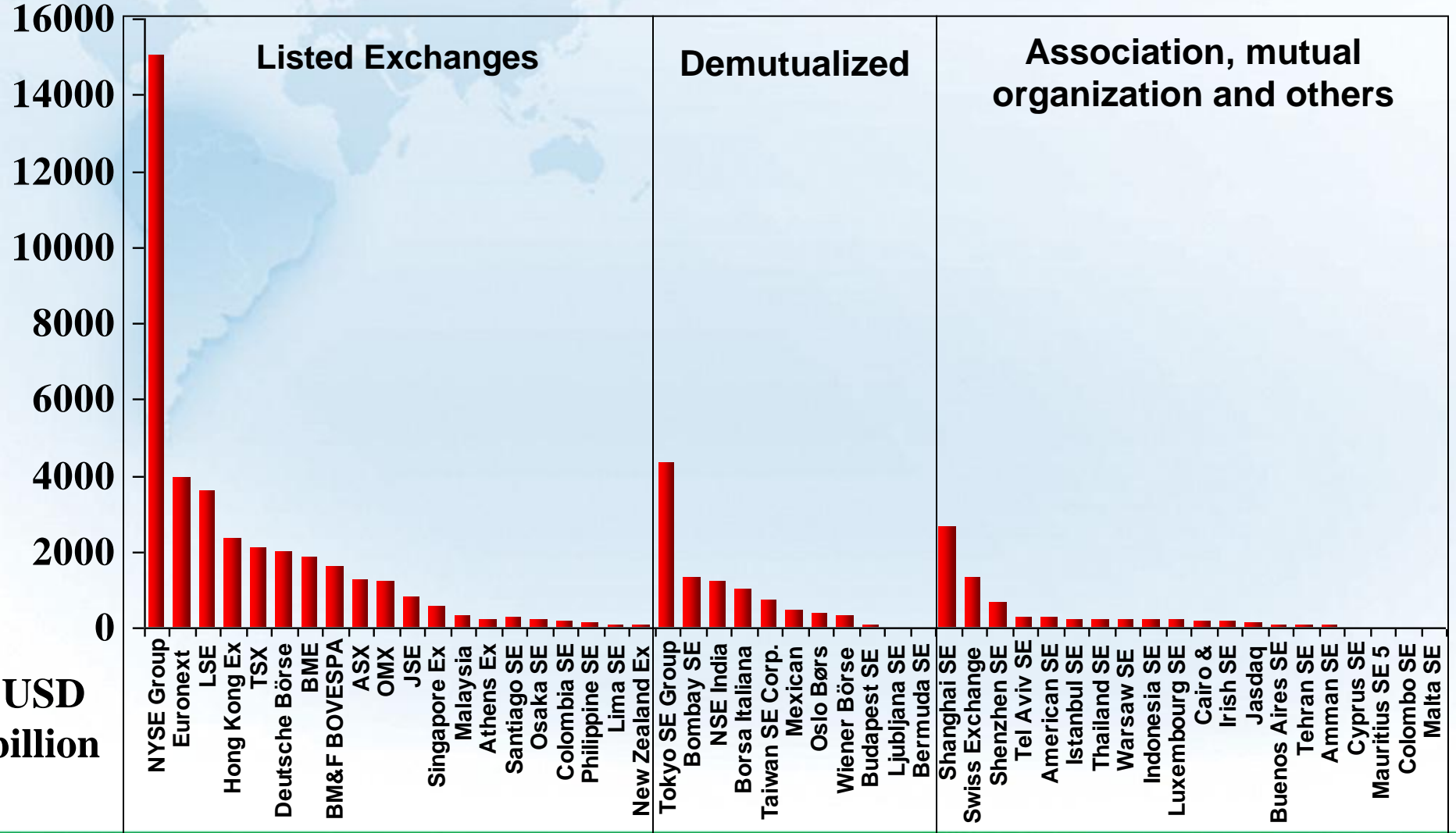
Period: From the IPO day to June/25/2008 –
(USD)



Source: Bloomberg

Market Capitalization*

*Up to May/08
Source: WFE





The Demutualization Process



The Reasons to Demutualization

- ✓ Strengthening before the international competition and adjusting to an integrated markets dynamic
- ✓ Higher flexibility and response velocity to the changes in the domestic and international scenario
- ✓ Capital raising to new investments
- ✓ Liquidity and valorization of the brokerage houses' (members) investments
- ✓ Strengthening the commercial focus



Demutualization Stages

- ✓ 1st. stage: Mutual Structure → Non-Mutual Structure
- ✓ 2nd. stage: Corporation → Public Corporation (optional)
- ✓ 3rd. stage: Listing in the Stock Exchange (optional)

Some Stock Exchanges carry out the 3 stages, others just do the 1st or the 1st and 2nd stages

✓ Examples:

- Demutualization: *Bolsa da Colômbia, Bombay Stock Exchange*
- Demutualization and IPO: *NYSE, Euronext, LSE, BME, BM&FBOVESPA and Bolsa Mexicana de Valores*

Changes and Needs Resulting from the Demutualization and Merges

- ✓ Separation between the “trading access” and the “decision making power”
 - The trading access and the others services provided by the Stock Exchange are, generally, separated from the ownership of shares
 - The decision-making power now belongs to the shareholders (that will not be, necessarily, the former brokerage houses or the former members)
- ✓ Corporate governance reinforcement and strategy
 - For-profit corporation, the management will be more competitive
 - Adoption of a “Business Model”
- ✓ Regulation
 - Changes in the self-regulation model after the demutualization
 - Jurisdiction conflicts in the merger process



Trading Access

Some adopted models

- ✓ Issue of trading access licenses
 - Automatically granted to the former owners of the membership certificates
 - Entrance possibility to the new intermediaries, since they are properly qualified for that
 - Ex. NYSE

- ✓ Issue of shares with different classes
 - Voting right Class
 - Trading access right Class
 - Ex. CME and NYMEX



Regulation

Issues in discussion at IOSCO

✓ Jurisdictional Conflicts

- Anti-trust issues and difficulties to conciliate the regulators' requirements in the regional and international mergers

✓ Self-Regulation Function of the Stock Exchange

- As a commercial entity, for profit organization, can a Stock Exchange keep satisfactorily its self-regulatory function?

Profits maximization

X

Fair market operating

Self-Regulation

3 Alternatives

- ✓ The Stock Exchange keeps the self-regulatory activities
 - If the stock exchange acts in a relapse way regarding its regulatory activities, it can cause damage to its commercial image
 - The stock exchange has a better display to perform the trading supervision as well as the compliance of the public companies. It is its task providing a regulated market
- ✓ Dissociation between the commercial activities and the regulatory activities inside the demutualized stock exchange
 - Launch of a non-for-profit entity to take care of the regulation activities, under the same holding, but constituted by an independent board and an independent management
- ✓ Outsourcing of the regulatory activities
 - Launch of a non-for-profit entity, fully disentailed and constituted by members that do not have entails with it or interest in the stock exchange activities
 - Regulatory activities fully attributed to a governmental body.





Perspectives for the Capital Market in Latam



Some Possibilities...

- ✓ Demutualization and IPO
- ✓ Currently, the Stock Exchanges from São Paulo, Santiago, Lima, El Salvador Panama and Colombia, Mexico are listed, while the Stock Exchanges from Bolivia and Caracas are demutualized
- ✓ Mergers and acquisitions by North-American and European Stock Exchanges



Demutualization in Brazil

BOVESPA`s case

BOVESPA e CBLC announced studies to the demutualization and IPO in June 2006



The whole process, which culminated in BOVESPA's IPO, was concluded in 16 months

- *Demutualization: August 2007*
- *IPO: October 2007*

Demutualization in Brazil

BM&F`s case



- *Demutualization: October 2007*
- *IPO: November 2007*



Combined Exchange's Corporate Structure



Operating a vertically integrated exchange, offering a multiasset class exchange and the main business lines

Listing

**Equity and
Equity
Derivatives
Trading**

**Financial
Derivatives**

**Fixed
Income
Trading**

**Commodities
and Metals
Contracts**

**FX
Contracts**

**Clearing
and
Depository**

- Brazilian and International Companies
- SMEs
- Closed-End Funds
- Fixed Income Products

- Stocks
- BDRs
- Stock Options and Index Options
- Forward REITs
- ETF
- POP

- futures & options
- interest rate Ex. Rate
- USD denom. domestic yield curve
- Structured Products
- SWAPs
- Flexible Options
- sovereign debt bond
- global bond
- US Treasury Bond

- Sovereign Bonds
- Debentures
- Commercial Papers
- Mortgage-Backed securities
- Asset-backed securities (FIDC)
- NEW: Corporate Governance Bonds

- Arabica coffee
- Conillon coffee
- Sugar, Ethanol, Cotton, Corn, Soybean, Live cattle, Feeder cattle, Gold

- Exchange rate
- Dollar denominated domestic yield curve
- Interest rate x price index
- (Ppi/cpi) spread
- Price index (ppi/cpi)

- Central Counterparty
- Risk Management
- Securities Lending Program - for stocks and corporate bonds
- Final Beneficial Owner Market

THE NEWS IN THE BRAZILIAN INFRA-STRUCTURE

Preparing for the future...

- The consolidation of the Brazilian capital market infra-structure
 - May 8, 2008 – the shareholders of Bovespa Holding S.A. and BM&F S.A. approved the merger of the two companies and the creation of BM&F BOVESPA S.A.



Demutualization in Brazil

Steps taken

- Approval by the regulatory bodies
 - Securities and Exchange Commission and the Central Bank
- Corporate Restructuring
 - Approval by the members for the creation of a for-profit organization
 - Bylaws and contracts review
- Trading Access
 - Rules definition, licenses etc
- Self-Regulation
 - Restructuring of the supervision activity
- Social Responsibility
 - Future of the current projects
- Preparation to IPO
 - Adjustment to the financial statements standards and corporate governance improvements



Experienced Management Team and High Standards of Corporate Governance

- All common shares with equal voting rights
- Full tag-along rights
- Majority of board of directors composed of independent members. Very strict definition of independence including:
 - No commercial relationship with Bovespa
 - Cannot be a controlling shareholder of any company listed on the Bovespa
 - If a board member of any listed company, must be an independent director of that entity
- All board members are non-executives
- Listed in the Novo Mercado



Novo Mercado

An adequate environment for IPOs

- ✓ Launched in December 2000
- ✓ Private sector initiative, based on and enforced through a contract with BOVESPA
- ✓ Decision of joining NM is voluntary and market driven
- ✓ Set of rules over and above the Corporations Law reflecting market demands and requirements. Extensive hearing process with local and foreign institutional investors.
- ✓ Set of rules that expand shareholders rights, require greater transparency, and mandate more comprehensive disclosure



CORPORATE GOVERNANCE

The standard is set

NOVO MERCADO

– Shareholders' rights

- Only one class of shares, with full voting rights: one share, one vote
- Full tag along rights

– Higher disclosure Standards

- Annual financial statements in IFRS or US GAAP
- Improved Quarterly Reports (ITRs), including an English version, consolidated financial statements and cash flow statements
- Related party transactions
- Trading and ownership of the company's shares by the management and the controlling shareholders

– Other listing requirements

- Delisting: tender offer at a price based, at least, on the economic value
- Board of directors: a minimum of 5 members, maximum two years terms
- 25% minimum free-float and adoption of special procedures in public offerings to enhance the dispersion of the company's shares
- Adhesion to an arbitration panel (dispute resolution)

SPECIAL LEVELS OF CORPORATE GOVERNANCE

– Nível 1 (level 1)

- Higher disclosure standards of Novo Mercado

– Nível 2 (level 2)

- Higher disclosure standards of Novo Mercado
- Must comply with all the requirements of the Novo Mercado
- Exception:
 - May continue to issue non-voting, « preferred » shares (PN), but these « preferred » shares will have voting rights in exceptional circumstances



CORPORATE GOVERNANCE

Supporting Companies Growth

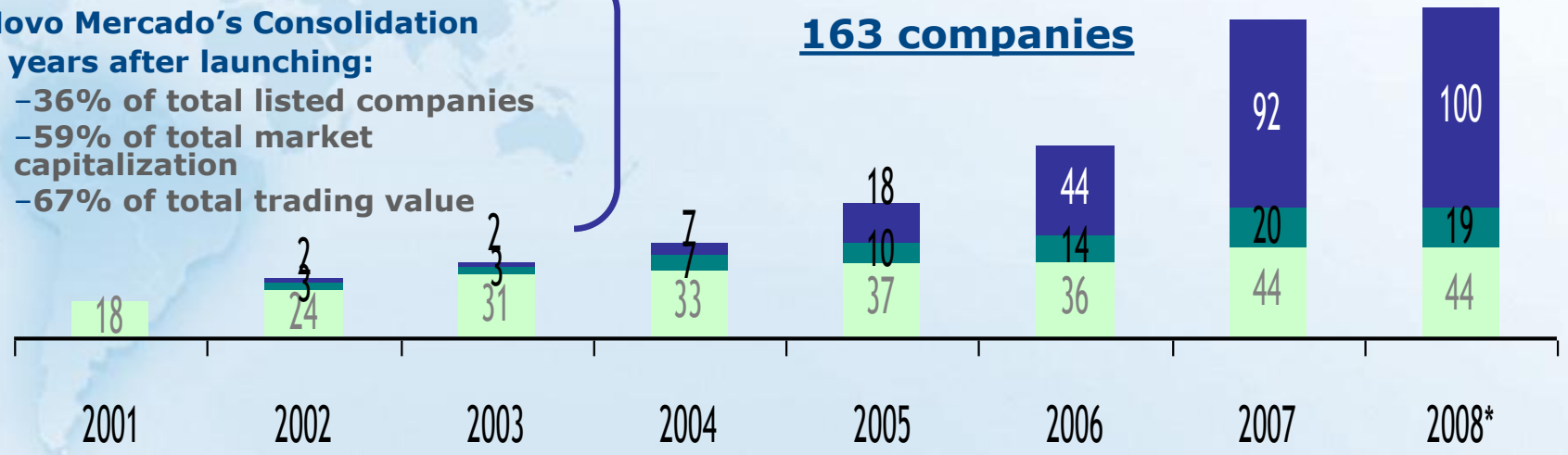
Source: BOVESPA

*Up to June 13

Novo Mercado's Consolidation
7 years after launching:

- 36% of total listed companies
- 59% of total market capitalization
- 67% of total trading value

163 companies



follow the regulation

regulation + more disclosure

Level 1 + shareholders rights

Level 2 + only common shares

adapted rules for companies that look for gradual access

Basic Segment

NÍVEL 1
BOVESPA BRASIL

NÍVEL 2
BOVESPA BRASIL

NOVO MERCADO
BOVESPA BRASIL

BOVESPA MAIS
BRASIL



Demutualization and International Trends in the Stock Exchange Market

Nora Rachman
June, 2008