

INNOVATION AND DIVERSIFICATION

# SeDeX - The Certificates and Covered Warrants Market



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# SeDeX - The Certificates and Covered Warrants market

## Introduction

**SeDeX is the Borsa Italiana market dedicated to the trading of certificates and covered warrants, collectively defined as securitised derivatives.**

This electronic market uses a highly efficient technological infrastructure, allowing investors to electronically trade thousands of listed instruments on a continuous basis and in real time.

SeDeX is a regulated market, subject to *CONSOB* supervision and disciplined by a set of clear and non-discretionary rules designed to protect investors.

### INNOVATION

*A constantly evolving market*

The SeDeX market has always been open to change and product innovation. The issuers systematically expand their offer range to include new underlyings, new structures or different versions of existing instruments. The flexibility and versatility of the certificates at the time of their structuring allow the issuer to propose new products embodying investment strategies that adapt to changing market conditions or instruments that take advantage of a particular underlying's propitious phase.

### DIVERSIFICATION

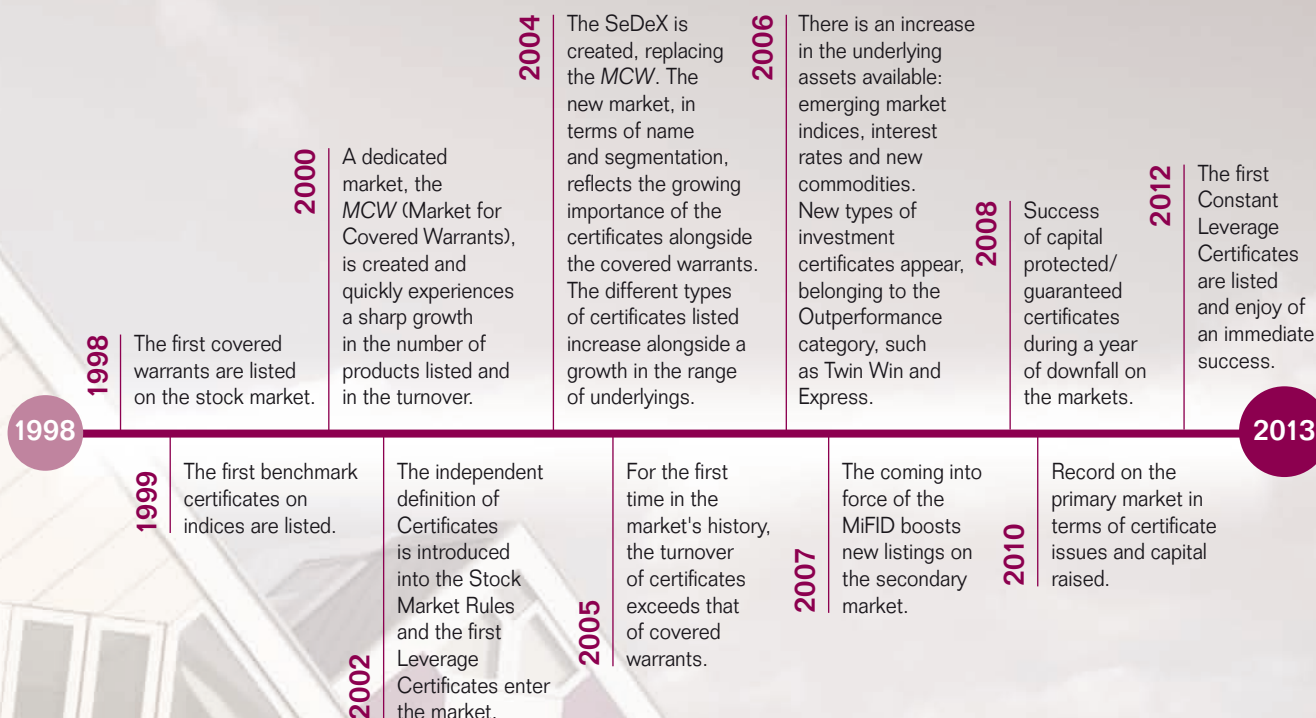
*Large variety of listed instruments*

SeDeX offers a wide selection of listed instruments, with an official list comprising several thousand products. The products listed vary according to the different investment strategies, the range of underlying assets available and the various issuing banks. Moreover, included within each category of certificates are variations on the certificate's standard version.

The many different combinations obtainable by putting together these various elements provide a range of products such as to satisfy a wide assortment of investment requirements.

# Historical evolution and current segmentation

SeDeX was created in 2004 as the Borsa Italiana market dedicated to the trading of Certificates and Covered Warrants, collectively referred to as securitised derivatives (thus the name SeDeX, acronym for Securitised Derivatives Exchange). However, the first covered warrants made their initial appearance on the stock market in 1998, followed shortly afterwards by the first certificates.



## DISTRIBUTION BETWEEN MARKET SEGMENTS

Covered warrants and certificates are derivative financial instruments, in other words their value depends on the performance of another financial asset. Securitised derivatives are normally issued by banks. The financial instruments listed on SeDeX are divided into 4 segments:

### PLAIN VANILLA COVERED WARRANTS

These are options which give the holder the right to receive at the date of exercise, in the case of a call CW, the difference – if positive – between the value of the underlying and the strike price (vice versa in the case of a put CW).

### STRUCTURED/EXOTIC COVERED WARRANTS

These covered warrants are a combination of two or more call and/or put plain vanilla options or exotic options.

## SeDeX

### LEVERAGE CERTIFICATES

Class A: certificates that replicate with leverage effect the performance of the underlying; Class B: certificates that replicate with a constant leverage the performance of the underlying.

### INVESTMENT CERTIFICATES

Class A: instruments which replicate in a linear manner the performance of the underlying asset; class B: instruments which embody a particular investment strategy.

# Regulated market and requirements for admission to listing

## Safeguards and guarantees in favour of investors

SeDeX is a regulated market, meaning that it is authorised to operate under the supervision of public authority *CONSOB*.

*CONSOB* approves the market regulation – the set of operational rules – having first ascertained their compliance with EU directives, law and their suitability for ensuring market transparency, the orderly course of trading and investor protection.

The publication of prospectuses for the offering and listing of financial instruments is also subject to authorisation by *CONSOB*. Based on European legislation, it is possible to use listing prospectuses that have been approved by the authority of another EU member state and recognised in Italy (passporting).

### Main requirements for admission to listing

#### Admissible issuers

One of the principal requirements for admission to the market is that the companies issuing (or guaranteeing) securitised derivatives must be subject to prudential supervision. Their supervisory capital must amount to at least 25 million Euro. Regarding new issuers, Borsa Italiana performs an admissibility analysis based on the last 2 audited annual reports.

#### Admissible underlying assets

Admission to listing is allowed for covered warrants or certificates that have as their underlyings the following financial assets:

- Italian or non-Italian shares of issuers other than the issuer of the securitised derivatives, that are traded in regulated markets in Italy or in another country and satisfy high liquidity requirements;
- bonds or other debt securities (including government securities), that are traded in regulated markets and satisfy high liquidity requirements;
- official interest rates or those generally used on the capital market;
- currencies whose exchange rate is recorded on a continuous basis by the authorities and competent bodies;
- commodities for which there is a reference market characterised by an ongoing and updated availability of information on the prices of the traded assets;
- indices or baskets featuring transparent methods of calculation and dissemination;
- derivatives contracts for which a liquid market exists, characterised by availability of updated information on the prices of the contracts in question;
- units/shares of open-end CIUs, including ETFs.



### **Instrument admissibility characteristics**

Borsa Italiana also envisages a series of other requirements as regards the characteristics of the instruments, designed to facilitate comparability between similar products:

1. The maturity of the covered warrants must not exceed 5 years. This latter condition may be departed from by Borsa Italiana upon reasoned request from the issuer and where there is sufficient information to determine the price;
2. If the underlying is an Italian share, the parity must be equal to 0.1 in the case of a plain vanilla covered warrant and 1 in the case of Leverage Certificates. If the underlying asset is the FTSE MIB index or another index managed by Borsa Italiana or by companies with whom Borsa Italiana has entered into appropriate agreements, in the case of plain vanilla covered warrants, leverage certificates and class A investment certificates, the parity must be equal to 0.0001.
3. The settlement price must reflect a significant quantity of volumes traded of the underlying asset. More specifically, for securitised derivatives with Italian shares as underlying, it must correspond to the reference price for the

day prior to maturity, in the case of exercise at maturity, and to the reference price for the day of exercise, in the case of early exercise. For securitised derivatives based on indices managed by Borsa Italiana, the settlement price must correspond to the opening price of the constituent securities at the time of maturity, in the case of exercise at maturity, otherwise on the trading day following the day of exercise, in the case of early exercise (with the exception of Investment Certificates - class B and exotic/structured CWs).

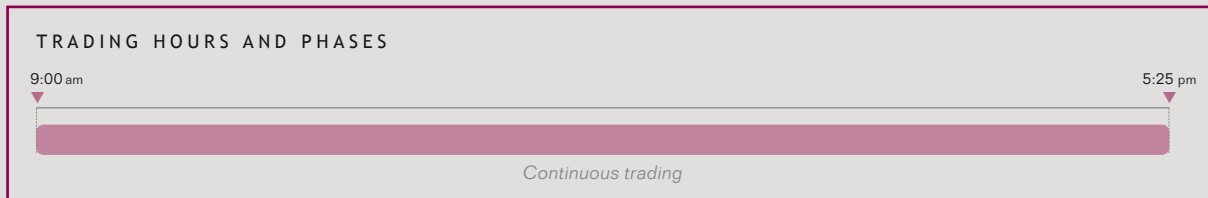
4. Exercise is automatic at maturity, if the securitised derivatives mature 'in-the-money', namely with a positive value. The listing prospectus must envisage the possibility for holders to waive automatic exercise at maturity.

To date, all instruments listed on SeDeX provide for cash settlement at maturity. At regulatory level, it is possible to provide for settlement via the physical delivery of the underlying asset, exclusively in the case of financial instruments listed on Borsa Italiana.

# Trading procedures and order types

## Trading procedures

Trading on SeDeX takes place in a single continuous trading phase, from 9.00 a.m. to 5.25 p.m.. There is no opening or closing auction. During the continuous trading phase, the orders entered are executed automatically with those present on the book, based on a principle of price/time priority.



### CHARACTERISTICS OF THE MARKET MODEL

<b>Multilateral</b>	access to the market is permitted for all requesting intermediaries, who are able to meet regulatory requirements
<b>Order-driven</b>	price formation is driven by all market participants through the automatic matching of orders
<b>Specialist</b>	the liquidity of all listed instruments is guaranteed by the presence of a specialist
<b>Settlement</b>	in Monte Titoli, the third trading day following the conclusion of trades. Settlement follows the Straight-Through-Processing mechanism from the matching of orders up to final settlement
<b>Delisting date and maturity date</b>	the securitised derivatives continue to be tradable until four days prior to their maturity date

## Order types

An order represents a commitment to trade based on specific conditions concerning price and quantity, according to particular trading procedures laid down by Borsa Italiana for each market. The main elements comprising an order are:

### THE INFORMATIVE CONTENT OF ORDERS

<b>Price</b>	this must be a multiple of the minimum trading tick applicable to the instrument
<b>Quantity</b>	this must correspond to at least the minimum trading lot and at most to a multiple of the minimum lot defined by Borsa Italiana
<b>Transaction type</b>	buy or sell
<b>Terms of execution</b>	validity parameters

Orders that can be injected are the 'price limit orders', that can only be carried out at a price equal to or better than the specified limit. "Orders with no price limit", also referred to as 'market orders', are disabled on SeDeX.

Orders with partially displayed quantities, or 'iceberg orders', may also be entered.

Cross Orders and BTFs (Block Trade Facilities), two types of orders aimed to execute pre-arranged trades between two counterparties, may be entered.

The orders on SeDeX are entered anonymously, apart from the specialist who is identifiable. Specialists support the liquidity of the market by using a specific type of order, the quotes, which are couples of buy and sell named orders.

#### VALIDITY PARAMETERS

<b>Fill or kill</b>	the order can be executed immediately, but only in its entirety. If the requested quantity is not available on the book, the order is cancelled
<b>Fill and kill</b>	in cases where the order is partially filled, the unfilled portion is automatically cancelled
<b>Good till cancelled and good till date</b>	on SeDeX, these orders in any case have a maximum duration of one day and are automatically cancelled before the next session

**Reference Price:** this is determined by Borsa Italiana at the close of the market based on a significant number of best buy and sell orders present on the trading book during the session, giving greater consideration to the most recent. If there are no orders on the book, the reference price corresponds to the previous day's reference price.

**Static Price:** this corresponds to the price of the first trade concluded during the session.

**Dynamic Price:** this corresponds to the price of the last trade concluded during the session.

For the purpose of automatic control of the regularity of trading, the following categories of price variation limits have been established, as set out in the table below:

- maximum limit on order price variation with respect to the static price;
- maximum limit on contract price variation with respect to the static price;
- maximum limit on contract price variation with respect to the dynamic price.

TABLE OF MAXIMUM PRICE VARIATIONS\*

Price (EUR)	Maximum order price variation with respect to static price	Maximum contract price variation with respect to static price	Maximum contract price variation with respect to dynamic price
Less than, or equal to 0.003	-	200%	150%
0.0031 – 0.3	900%	70%	50%
0.3001 – 1.5	500%	50%	30%
1.5001 – 3	300%	50%	25%
3.0001 – 30	150%	50%	10%
30.0001 – 70	50%	30%	5%
70.0001 – 100	30%	20%	5%
100.0001 – 300	25%	15%	3.5%
Greater than 300	20%	10%	2.5%

\* check for subsequent revisions to the table in the "Guide to the parameters for trading" available on the website [www.borsaitaliana.it](http://www.borsaitaliana.it) (path: Borsa Italiana/Rules/Instructions and Guides).



# The specialist

## Market liquidity and the role of the specialist

The liquidity of the market is guaranteed by the role of the specialist who ensures the liquidity of the listed instruments, undertaking to comply with a series of listing obligations. The presence of the specialist enables investors to always find on the market a price at which to trade securities.

There are three types of listing obligation:

### 1. Obligation to continuously display bid and ask prices

The specialist constantly displays on the book both bid and ask prices. This ensures that investors can always find an up-to-date valuation of the instrument in which they are interested and have the possibility to close or increase a position. In the case of a hit on the specialist's book, he is required to restore the quotes within 5 minutes.

### 2. Obligation to display a minimum quantity

Each price of the specialist is linked to a minimum quantity in terms of number of instruments corresponding to a value of 2,500 Euro. The minimum quantities are recalculated at least 4 times per year based on the revised prices of the instruments.

### 3. Maximum spread obligation

As regards plain vanilla covered warrants, leverage certificates and class A investment certificates (benchmark certificates), the specialist is also required to observe maximum spread obligations, as set out in the table below. The spread obligations vary according to the instrument's reference price. These obligations do not apply to instruments listed in the class B investment certificate and structured/exotic covered warrants segments.

## Bid-only specialist

For certain certificates, admitted to listing on the Stock Exchange as a result of a public offering, the specialist may ask to be present on the book only on the bid side. This service allows subscribers of the security to sell the certificates acquired and therefore to close their position at any time. It is possible to purchase the certificate or increase the number of instruments held in portfolio by interacting with other market participants.

## Market Surveillance

Compliance with obligations is carefully monitored by Borsa Italiana, specifically by the Market Surveillance unit, which may intervene in the event of non-compliance, also by inflicting sanctions on specialists who fail to observe their obligations. In verifying compliance with obligations, consideration is given *inter alia* to a synthetic indicator, epsilon, calculated on a monthly basis, which measures the observance of the three above mentioned obligations.

MINIMUM TICK AND MAXIMUM SPREAD*		
Reference Price (EUR)	Minimum tick	Maximum spread
Less than, or equal to 0.003	0,0001	180%
0.0031 – 0.3	0.0005	50%
0.3001 – 1.5	0.001	20%
1.5001 – 3	0.005	15%
3.0001 – 30	0.01	7.5%
Greater than 30	0.05	3.5%

\* check for subsequent revisions to the table in the "Instruction accompanying the Borsa Italiana Rules" available on the website [www.borsaitaliana.it](http://www.borsaitaliana.it) (path: Borsa Italiana/Rules).



## Other market features

### Trading participants

The SeDeX market counts a high number of participants who are connected directly or via interconnection, including representatives of the most important Italian banking groups, on-line banks and leading international banking institutions.

All market participants are subject to participation requirements as regards the organisational and technological structure used to access the markets and their ability to settle the trades concluded.

### Trading platform

SeDeX is a fast, efficient and high performance electronic market. Borsa Italiana has always invested in technological infrastructure, with a view to offering its customers a modern trading platform that can guarantee rapid times for order entry and the automatic execution of trades, despite the thousands of instruments traded and the hundreds of thousands of orders entered.

### Disclosure to the market of transparent and up-to-date information

SeDeX guarantees clear, exhaustive and promptly updated information on the instruments traded.

The issuers undertake to report in good time all events that are relevant for the listed instruments. For such purpose, a provision is required at regulatory level for adjustments to be carried out whenever extraordinary events affect the underlying asset. The adjustments must be based on generally accepted methodologies and serve to counteract as much as possible the distortive effects of the event. In this way, the information recorded for the securitised derivatives is always up-to-date and correct.



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