

Meeting of the working group on euro risk-free rates

held in Frankfurt am Main on Thursday, 18 October 2018, 11:30-16:00

SUMMARY

1. Welcome address by the ECB and introductory remarks by the new Chair

Cornelia Holthausen (ECB) welcomed Steven van Rijswijk as the new Chair of the working group on euro risk-free rates. Mr van Rijswijk is Chief Risk Officer at ING, and was selected by the public institutions' observers in the working group on the basis of his long-standing experience in European banking and financial markets. The current support team from ING will remain unchanged, thereby ensuring organisational continuity of the working group. The [composition of the working group](#) on the ECB's website has been modified accordingly.

Steven van Rijswijk (Chair) introduced himself to the meeting participants. He said he had accepted the role owing to the pressing need for the financial industry to tackle the challenges of interest rate benchmark reforms, and the strong commitment of ING's team to pursuing this task together with the working group members.

2. Approval of the agenda and obligations of the working group members as regards competition law

Steven van Rijswijk (Chair) asked the group members to approve the agenda of the meeting and also reminded them of their obligations under EU competition law, as described in the guidelines on compliance with EU competition law published on the ECB's website.

3. Follow-up discussion on the high-level implementation plan

Jaap Kes (ING) recalled the two requests made to European authorities to support the benchmark transition, as described in the high-level implementation plan for potential scenarios for EONIA transition and Euribor reform published on the ECB website:

- (i) an extension of the transition period for index providers of all designated critical benchmarks and for the use of those critical benchmarks by a minimum of two years;
- (ii) a request to the European Commission to designate ESTER and possibly the ESTER-based term structure as critical benchmarks, thereby ensuring the market will understand these to be the successor rate(s) to benchmark(s) not compliant with the EU Benchmarks Regulation (BMR).

Alessandra Atripaldi (European Commission) updated the working group members on the state of play of the various initiatives to possibly amend the BMR. She recalled that the European Commission's policy is not to table any further stand-alone legislative proposals between now and the European parliamentary elections in May 2019. She indicated that amendments to the Regulation would therefore have to be introduced as part of a pending legislative proposal amending the BMR – either the review of the European supervisory authorities or the low carbon benchmark proposal. The Commission will update the working group members on the progress and timing of these negotiations. Ms Atripaldi also indicated that the second request of the working group (the designation of ESTER and possibly ESTER-based term rates as critical benchmarks) could be acted on once data on the volume of contracts referencing either one of these benchmarks have been made available to the Commission.

Ms Atripaldi said that the working group's request to extend the transitional period for critical benchmarks had some support in the Parliament, but there were still concerns as to the timetable and the milestones to be achieved in the two-year period of extension. As a consequence, a positive outcome of the legislative procedure could not, for the time being, be taken for granted. Working group members expressed their strong concerns as regards the financial stability implications if no extension were agreed and recalled that the prohibition of using non-compliant benchmarks in new contracts as of 2020 could cause market disruption. Concern was also raised with regard to the language of the amendment to the BMR currently

under consideration by the co-legislators, which may introduce some conditionality and uncertainty regarding the coverage of new contracts. Ms Atripaldi said that these ambiguities would be brought to the attention of the co-legislators.

4. Issues relating to term rates

4.1. Update on the Euribor hybrid methodology

Jean-Louis Schirmann (European Money Markets Institute (EMMI)) presented the outcome of the testing exercise for the hybrid methodology for Euribor, as well as the related public consultation. The hybrid methodology is aimed at bringing Euribor into compliance with the BMR's requirements. It relies on a "waterfall approach", whereby Euribor submissions are based on three hierarchical levels: (i) transaction-based data, (ii) transaction-derived data, and (iii) expert judgment. On 17 October EMMI published the results of the test, which was carried out between May and July 2018. EMMI expects to file for authorisation with the Financial Services and Markets Authority (FSMA) by the second quarter of 2019. It will subsequently start a phased transition for panel banks from the current methodology to the hybrid methodology, with a view to finishing the process before the end of 2019.

The FSMA commended EMMI on the work done to develop and test the hybrid methodology, saying that it represented a significant step towards a BMR-compliant Euribor. The FSMA further indicated that it would make an effort to expedite the authorisation process once EMMI filed for authorisation (by the second quarter of 2019). An important prerequisite for the FSMA would be the assurance that panel banks are operationally ready and willing to contribute under the new hybrid methodology.

Working group members enquired about certain technical details of the suggested methodology, relating to volatility, the proportion of expert judgment and the scope of transactions.

Working group members also raised the issue of the representativeness of the Euribor panel and its stability. In response, the FSMA reiterated that mandatory contributions to Euribor were a feasible, although last resort, option. Working group members were reminded that participation in the Euribor panel was still open to voluntary contributors, as an enlargement of the panel would obviously be the best way to address these concerns. Finally, working group members were strongly encouraged to respond to EMMI's public consultation on the features of the hybrid methodology.

4.2 Update by Subgroup 2 on the identification and recommendation of a term structure based on risk-free rates

Patrick Chauvet (BNP Paribas) recalled the context (including regulatory guidance, ongoing consultations by the International Swaps and Derivatives Association (ISDA) and the sterling risk-free rate working group as well as the process of transition from EONIA to ESTER) and the related uncertainties for the discussions and work of Subgroup 2. Against this background he outlined the main discussion topics and agreements reached by the Subgroup since the last working group meeting: agreement on selection criteria, agreement on working hypotheses underlying a public consultation document on term rates methodologies and a proposal for narrowing the scope of the public consultation.

4.2.1. Presentation of the scorecard for the assessment of term rates methodologies

Alberto Covin (UniCredit) gave additional insights into the way Subgroup 2 had further refined the selection criteria for the benchmarking of the term rates methodologies. He explained that the bundling of these criteria into more suitable categories eventually resulted in them being linked to three International Organization of Securities Commissions (IOSCO) principles, related to data sufficiency, benchmark design and transparency of benchmark determinations (principles 7, 6 and 9). The working group approved the three retained IOSCO principles as scoring criteria for the assessment of term rates methodologies.

4.2.2. Presentation of the composite methodology

Neil McLeod (Erste Bank) subsequently presented an analysis of a "composite methodology", combining quotes and actual transactions in the overnight index swap market for the possible construction of term rates. The methodology allows transactions to be used where possible and may help the transition from a

quote-based methodology to a transaction-based methodology until sufficient transactions become available. A composite approach is, though, both methodologically and operationally complex.

In addition, Mr McLeod gave an update on the backward-looking methodology, which was seen as the only viable option in a “tail risk” scenario where the use of the Euribor also became restricted owing to its non-compliance with the BMR.

4.2.3. Update on the public consultation on the term rates methodologies

Carlos Infesta (Santander) outlined the proposal for a public consultation on term rates. A number of generic assumptions on the shape and liquidity of an ESTER derivative market would set the background for the public consultation. The public consultation would concentrate on forward-looking methodologies, as backward-looking approaches would in any case be available and the challenges of their use by different users with different products would be analysed in more depth by Subgroup 2 in early 2019, also taking into account the outcome of the ISDA consultation on benchmarks fallbacks ^[1]. The target of the consultation would be to recommend a single forward-looking methodology to be proposed to an administrator. Based on the previous overview of methodologies, Subgroup 2 could propose one of them as the focus of the consultation.

In the absence of any objections, the working group agreed on the assumptions-based approach for the public consultation as well as on expressing a preferred forward-looking methodology as part of the consultation. The public consultation document will be submitted for approval by the working group at the latest at the latter’s meeting on 19 December 2018.

5. Update by Subgroup 4 on the EONIA transition: presentation of the draft report and proposal on the next steps

Carlos Molinas (Crédit Agricole) updated the working group on the progress of Subgroup 4 and on the proposed next steps.

Subgroup 4 is currently drafting a report, expected to be finalised by the beginning of December and to be presented for endorsement at the 19 December 2018 working group meeting, which will propose either one or two transition paths from EONIA to ESTER to be endorsed by the working group members. The drafting of this report is progressing according to the planned timeline.

In this context Mr Molinas also presented the defining characteristics of the transition approaches: (i) the independent or dependent nature of EONIA vis-à-vis ESTER beyond 1 January 2020, (ii) the parallel publication or not of EONIA and ESTER beyond 1 January 2020, (iii) the existence or not of a non-zero spread, (iv) the existence or not of a parallel discounting regime for EONIA and ESTER, and (v) the limitation or not of time for the use of EONIA as reference or discounting rate. When applying these defining characteristics, Subgroup 4 identified additional transition paths that will be described and analysed as part of its report. Subgroup 4 plans also to elaborate a set of criteria for evaluating the different transition options in order to give its recommendation.

In response to a question, the administrator of EONIA, EMMI, confirmed that it stands ready to support the market and facilitate the transition from EONIA to the identified risk-free rate, within the limits established by the BMR. EMMI also indicated that, even if maintaining EONIA after 2020 with a modified methodology to track ESTER were deemed the favoured option by the market, it should be clearly understood that EONIA’s existence should be limited in time.

With regard to the next steps, working group members and observers expressed their willingness to hold a public consultation on the choice of an EONIA transition path so as to ensure broad involvement of the EONIA users. The exact modalities of such a consultation will be decided in the weeks to come. As a follow-up, a small group of members, including ING, Crédit Agricole, EMMI, ESMA and the ECB, will reflect on possible ways to ensure greater transparency in the follow-up work and at the same time adhere to the tight time schedule for the deliverables of Subgroup 4 and the objective of a smooth EONIA transition before 1 January 2020.

[1] See: <https://www.isda.org/2018/07/12/isda-publishes-consultation-on-benchmark-fallbacks/>

6. Update by Subgroup 3 on contractual robustness

José Manuel González-Páramo (BBVA) introduced the update on the work by Subgroup 3 on contractual robustness with a brief summary of the work conducted so far with regard to (i) the legal analysis and fallback recommendations, and (ii) the legal considerations on the EONIA transition paths.

Regarding the Eonia transition, the subgroup representative also presented the next steps with regard to the legal analysis of the EONIA transition paths under the subgroup's consideration. Subgroup 3 is preparing its legal input into Subgroup 4, commenting on the legal soundness of the various EONIA transition paths. Subgroup 3 plans to present its findings to Subgroup 4 in the coming weeks, which should enable these legal considerations to be taken into account by Subgroup 4 and, subsequently, by the working group when recommending (an) EONIA transition path(s).

7. Other business

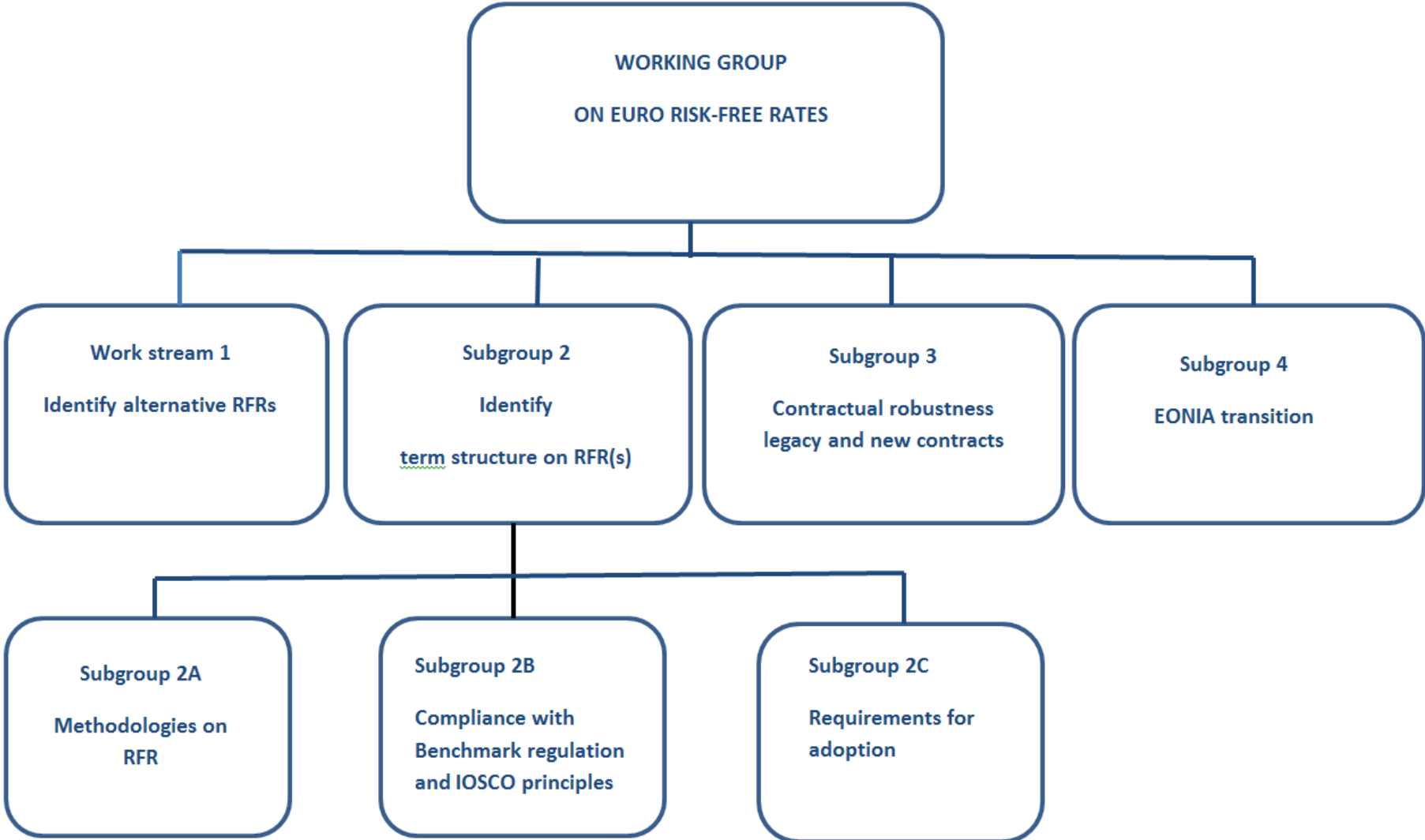
7.1. Information on the communication events of the working group members

The ECB Secretariat said it plans to hold an exercise in the next few weeks to gather information on the working group members' benchmark reform-related communications (conferences, speeches, interviews, news articles). This information-sharing exercise will be made on a voluntary basis.

7.2. Update on the Roundtable on euro risk-free rates (agenda and participation)

The working group members were invited to share their comments on the agenda of the Roundtable on euro risk-free rates which will take place on 9 November 2018 at the ECB.

The next meeting of the working group will take place at the ECB on Thursday, 19 December 2018.



List of meeting participants

Participant's organisation	Name of participant
Chair	Steven van Rijswijk
ING	Johanneke Weitjens
Voting members	
Bank of Ireland	Barry Moran
Barclays	Sascha Weil
Barclays	Joseph McQuade
Bayerische Landesbank	Harald Endres
BBVA	José Manuel González-Páramo
BBVA	José Carlos Pardo
BNP Paribas	Patrick Chauvet
BNP Paribas	David Gorans
BPCE/Natixis	Olivier Hubert
BPCE/Natixis	Sophie Asselot
CaixaBank, S.A.	Juan Cebrian
CaixaBank, S.A.	Sergio Castella Quintana
Crédit Agricole	Carlos Molinas
Crédit Agricole	Florence Mariotti
Deutsche Bank	Juergen Sklarczyk
DZ Bank	Michael Schneider
DZ Bank	Philipp Nordloh
Erste Group Bank AG	Neil McLeod
Eurobank - Ergasias SA	Theodoros Stamatiou
HSBC	Pierre Jenft
ING Bank	Jaap Kes
ING Bank	Marjolein de Jong-Knol
Intesa Sanpaolo	Maria Cristina Lege
KfW Bankengruppe	Markus Schmidtchen
LBBW	Jan Misch
Santander	José Manuel Campa
Santander	Carlos Fernandez Infesta
Société Générale	Olivier Balpe
Société Générale	Stéphane Cuny
UniCredit Bank	Alberto Covin

Non-voting members

European Money Markets Institute	Jean-Louis Schirmann
European Money Markets Institute	Alberto López Martín
European Fund and Asset Management Association	Agathi Pafili
International Capital Market Association	David Hiscock
International Swaps and Derivatives Association	Rick Sandilands
Loan Market Association	Kam Mahil

Invited institution

European Investment Bank	Yassine Boudghene
--------------------------	-------------------

Observers

European Central Bank	Cornelia Holthausen
European Central Bank	Holger Neuhaus
European Securities and Markets Authority	Michele Mazzoni
Financial Services and Markets Authority	Rik Hansen
Financial Services and Markets Authority	Timothy de Meester
European Commission	Alessandra Atripaldi

Secretariat

European Central Bank	Anne-Lise Nguyen
European Central Bank	Stephanie Broks
European Central Bank	Philippe Molitor
European Central Bank	Pascal Nicoloso
European Central Bank	Yasmina Santalla Perez
European Central Bank	Michael Stenström
European Central Bank	Vladimir Tsonchev