



EUROPEAN CENTRAL BANK

EUROSYSTEM

Mikael Stenström
Senior Adviser Market Operations
European Central Bank

Benchmark reform: The advent of €STR and the transition away from EONIA

Round table on the reform of interest rate benchmarks in the EU
Banque de France, Paris, 13 September 2019

Overview

- **Background:** Global reform, EU Benchmarks Regulation, EONIA and EURIBOR, and the Working Group on euro risk-free rates
- **The advent of €STR:** Main features, governance, publication and comparison between EONIA and €STR
- **Transition from EONIA to €STR:** Timeline, transition path, publication of €STR, recalibration of EONIA methodology, move from T to T+1, Working Group recommendations and EONIA to €STR Legal Action Plan + further work re EURIBOR and need for preparations by market participants

Global reform towards more robust benchmarks

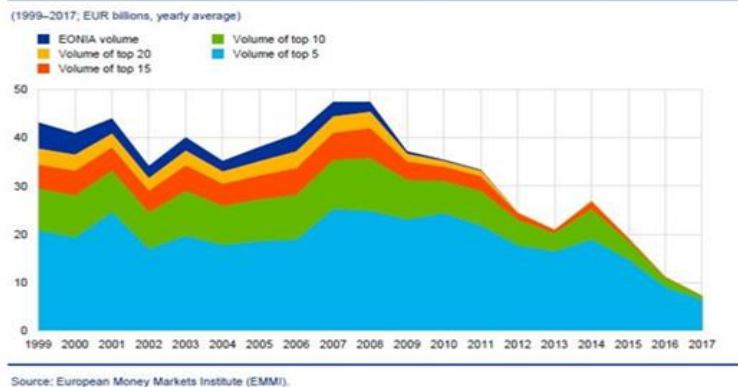
- Global reform of benchmarks to comply with international standards (e.g. [IOSCO principles](#))
 - Past incidents of manipulation
 - Decline in underlying volumes (unsecured interbank market)
 - Robust benchmarks to be ideally transactions-based, reflecting active markets
- [FSB recommendation](#): Identification of alternative (nearly) risk-free rates (RFRs) → Dedicated working groups in all major jurisdictions

Euro area

- [EU Benchmarks Regulation \(BMR\)](#): The BMR codifies the IOSCO Principles into EU law and covers the provision of a benchmark, contributions to a benchmark and the use of a benchmark. Majority of BMR provisions apply as of 1 January 2018 and will be fully phased in for critical benchmarks and third country benchmarks as of 1 January 2022.

Euro area critical benchmarks: EONIA and EURIBOR

EONIA volume and panel bank concentration



The panel of contributing banks currently consists of 18 CONTRIBUTORS.

| | |
|---|---|
| Belgium Belfius | Netherlands ING Bank |
| France BNP-Paribas - HSBC France - Natixis - Crédit Agricole s.a. - Société Générale | Portugal Caixa Geral De Depósitos (CGD) |
| Germany Deutsche Bank - DZ Bank | Spain Banco Bilbao Vizcaya Argentaria - Banco Santander - CECABANK - CaixaBank S.A. |
| Italy Intesa Sanpaolo - UniCredit | Other EU Banks Barclays |
| Luxembourg Banque et Caisse d'Épargne de l'État | |

EONIA

Not compliant with the BMR

Market activity underpinning EONIA is very low and its volume is concentrated in a limited number of panel banks

EURIBOR

Not compliant with the BMR (under its current methodology)

Quote-based methodology

Reform ongoing by EMMI: Hybrid methodology

EMMI granted authorisation by FSMA provided the reform is fully implemented

Benchmark reform in the euro area

- EONIA low underlying volumes, high panel concentration: not compliant with the EU Benchmarks Regulation in its current form.
- Given the systemic importance of benchmark rates, the ECB has announced:
 1. The production of an overnight unsecured rate: Euro short-term rate, €STR;
 2. The setup of the Working Group on euro risk-free rates, chaired by the private sector and with the ECB providing its Secretariat.
- €STR selected by the Working Group as euro RFR in September 2018 and will be published by the ECB as of 2 October 2019.
- EONIA's administrator, European Money Markets Institute (EMMI), has announced the end of reform efforts regarding EONIA and the Working Group has prepared a transition path from EONIA to €STR.
- EURIBOR reform: Following the implementation by EMMI of a new "hybrid methodology", the Belgian Financial Services and Markets Authority (FSMA) announced on 3 July 2019 that it has granted authorization to EMMI for EURIBOR.

ECB involvement

Euro short-term rate

- ECB to develop a daily euro unsecured overnight interest rate
- Based on data already available to the Eurosystem through the ECB's MMSR
- Reflects wholesale borrowing costs of the Euro area financial institutions

WG on euro RFRs

- Set-up of an industry working group together with other European institutions, i.e. the European Commission, ESMA and the FSMA
- Chaired by ING
- Membership: 21 EU credit institutions as voting members, 5 non-voting members (associations, benchmarks providers), 2 invited institutions and 4 observers
- The ECB provides its Secretariat

Mandate of the WG on euro RFR: (i) identifying alternative euro RFRs, (ii) identifying best practices for contract robustness, (iii) developing an adoption plan and, if necessary, (iv) creating a transition plan for legacy contracts referencing existing benchmarks.

Main features of €STR

Scope: unsecured overnight deposits to measure borrowing costs

Calculation: weighted average, trimming 25%

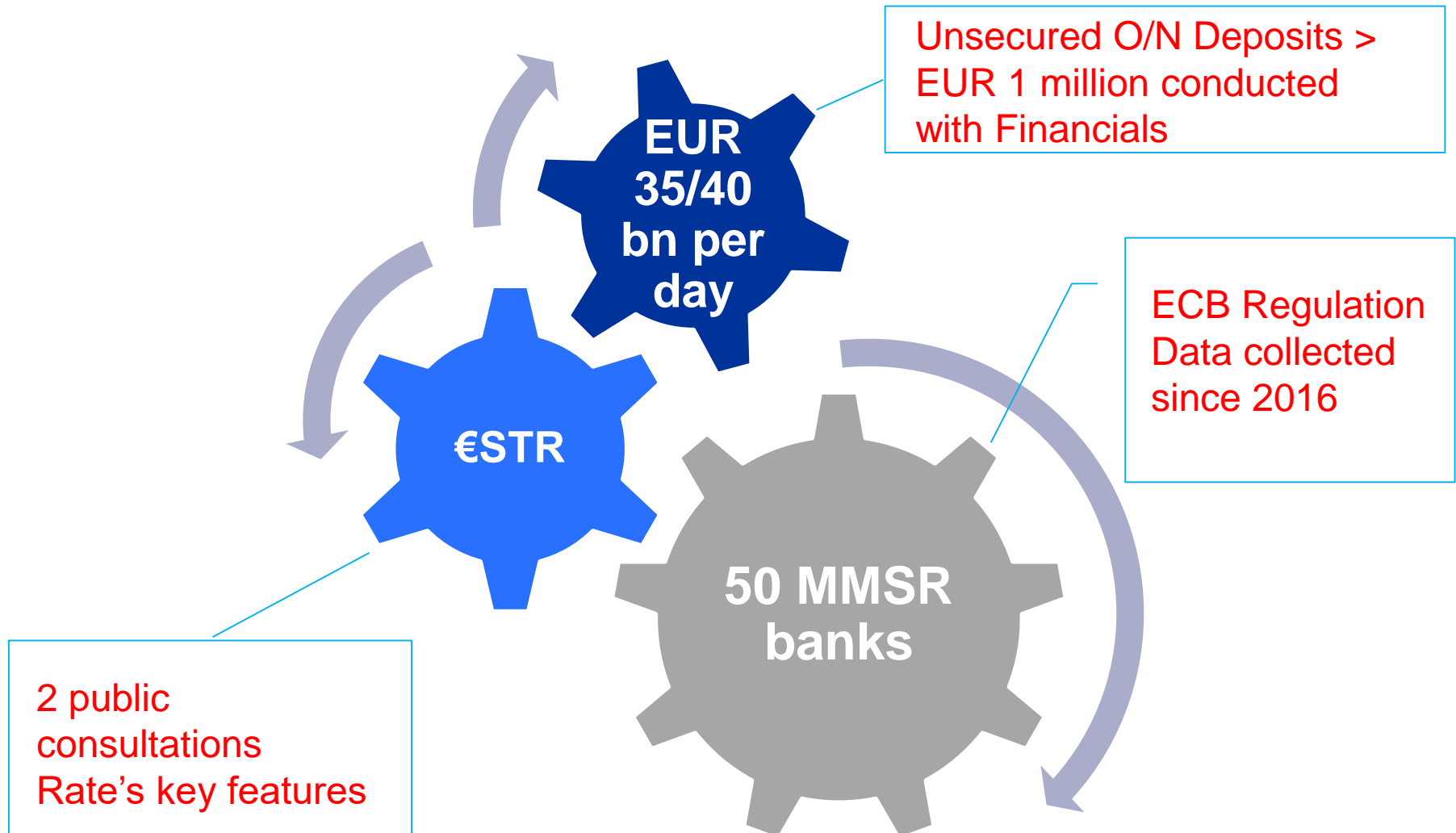
Data sufficiency policy: contingency triggers (20 banks, 75% top 5 banks' concentration ratio)

Governance and processes: €STR published at 08:00 am Frankfurt time

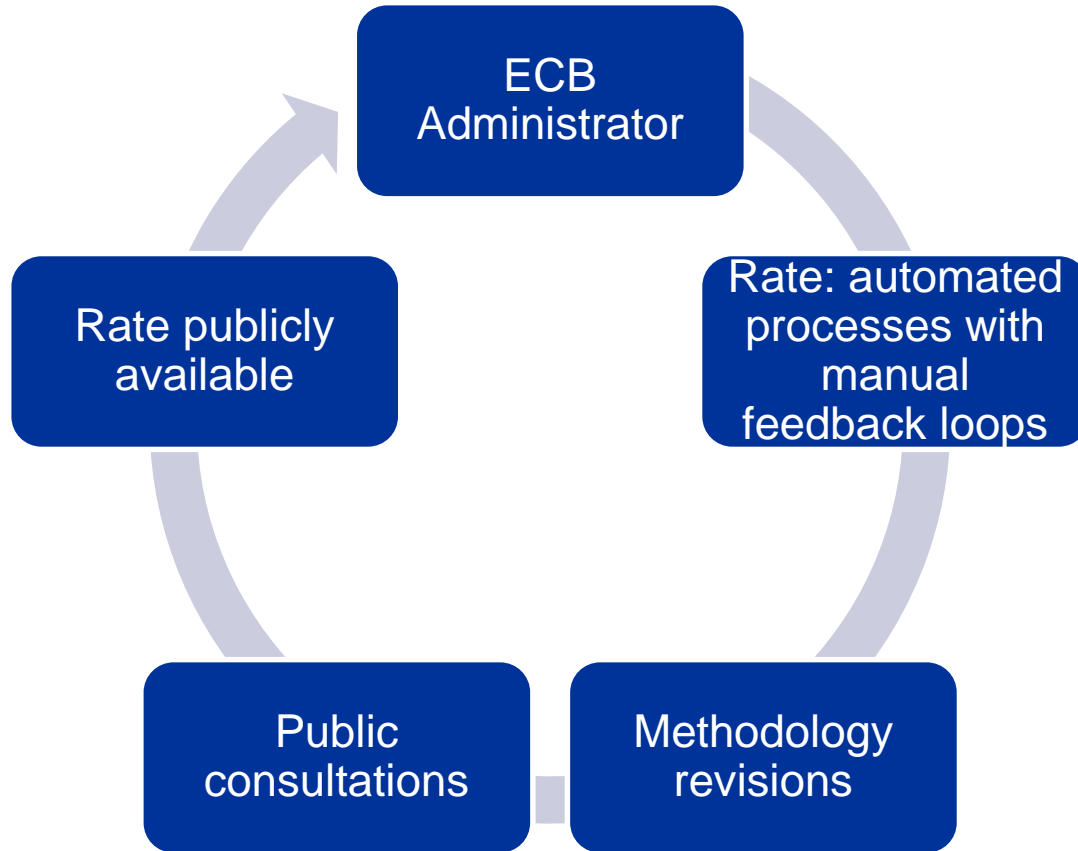
Publication policy and transparency on errors

Rate published daily from 2 October 2019
Pre-€STR publications since 28 June

€STR is fully transactions-based



Governance



€STR methodology will be re-assessed annually and

- adapted with market changes, or
- re-confirmed

Publication policy

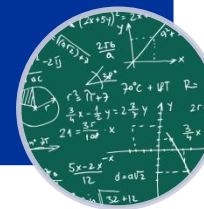
- 1) Rate, 3 decimals
- 2) Total volume
- 3) Number of transactions
- 4) Mode: normal, contingency

Rate
determination



- 1) Number of banks
- 2) Share volume by largest 5 reporting banks
- 3) Rates at 25th and 75th percentiles

Additional
information

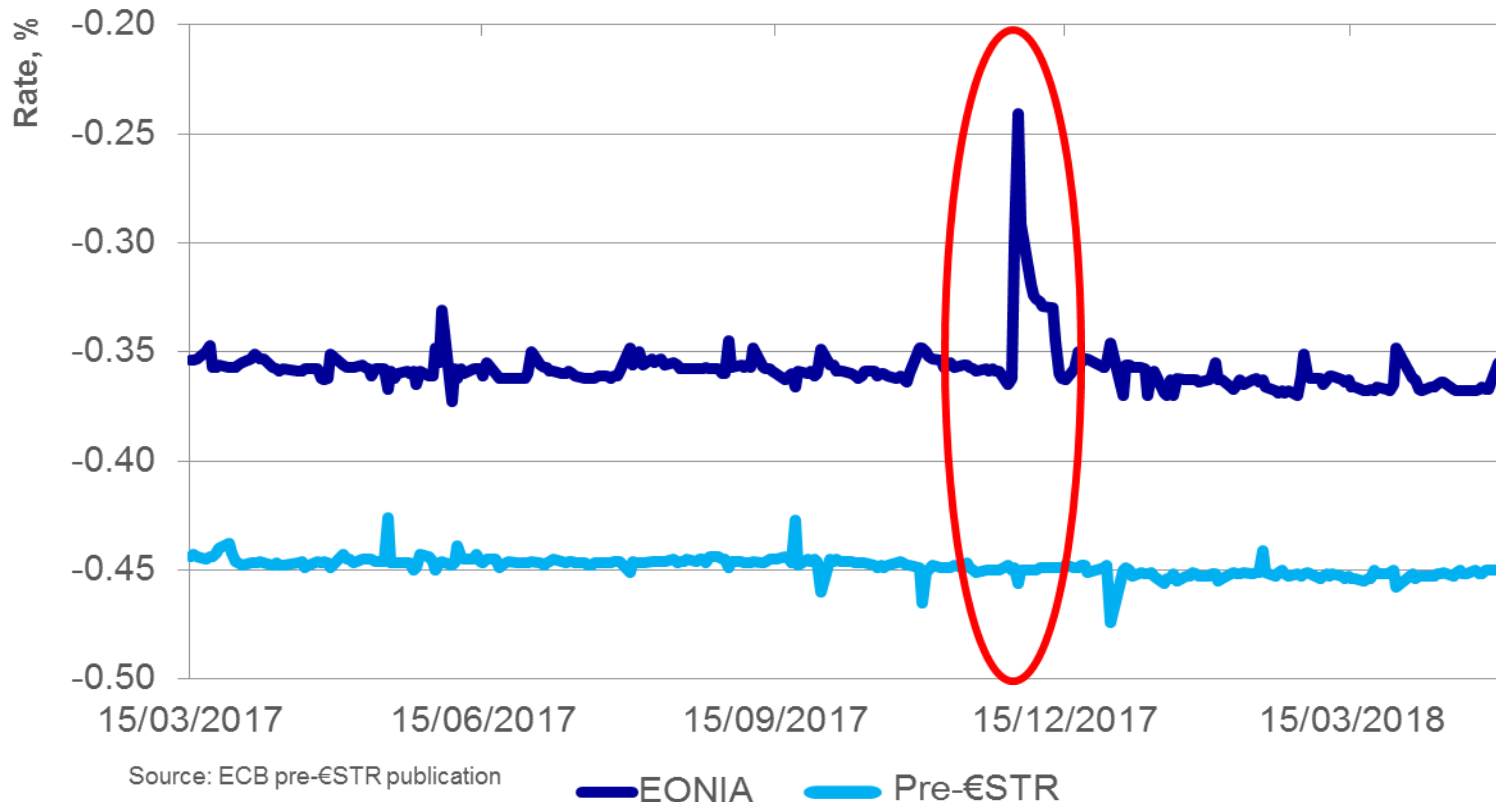


Rate is well explained to the markets and the public

EONIA vs. €STR: a comparison

| EONIA | Euro short-term rate |
|--------------------------|--------------------------------|
| EUR | EUR |
| Overnight | Overnight |
| Unsecured | Unsecured |
| Transaction Based | Transaction Based |
| Unstable Panel | Stable reporting sample |
| Interbank | Wholesale |
| Bank Lending | Bank Borrowing |
| Published on T | Published on T+1 |

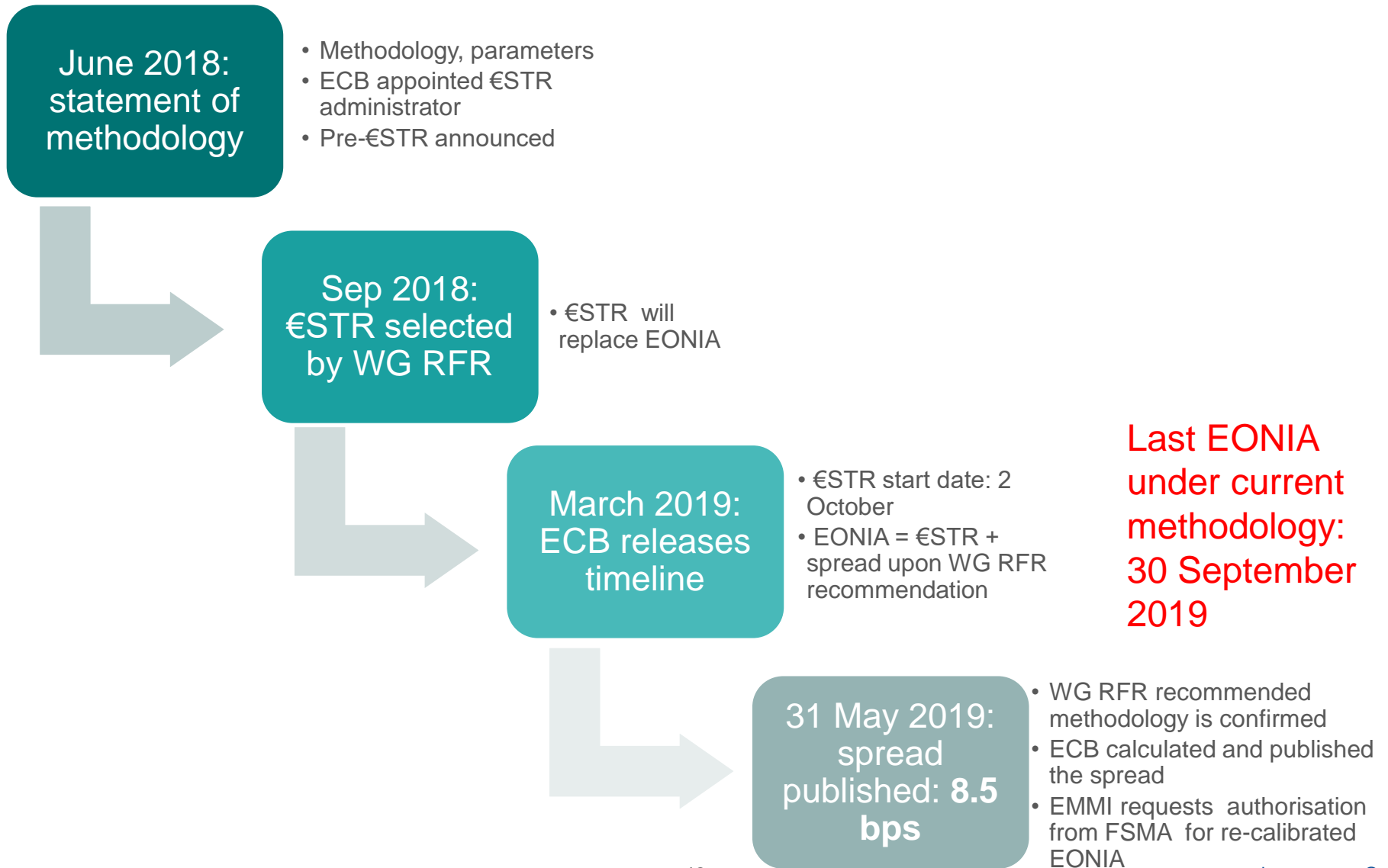
Trimming: outliers filtered out



- Rate reacts to market factors (Excess Liquidity, rate falls at quarter-ends)
- While being less vulnerable to outliers
- Pre-€STR (post corrections) very similar to €STR (based on 7:00 data)

The transition from EONIA to €STR

Timeline



Transition path and evolved EONIA methodology

- 14 March 2019: WG recommendations re transition path from EONIA to €STR
 - EONIA methodology to become €STR + fixed spread until the end 2021
- 31 May 2019: EMMI consultation results
 - EMMI published results from consultation on the change of EONIA's methodology, confirming WG recommendations
 - ECB published a press release announcing the fixed spread of 8.5 bps calculated on the basis of WG recommended methodology
 - ECB updated €STR webpage and €STR Q&A

Next steps

- 2 October 2019: €STR publication
 - Start of €STR publication and change in EONIA methodology
 - EONIA publication to [move from T to T+1](#)

The transition from EONIA to €STR

The move from EONIA in T to €STR in T+1

**30 September by
19:00 CET**

Last EONIA
published under
current methodology

2 October at 8:00 CET

€STR based on 1
October transactions

**2 October at or shortly
after 9:15 CET**

re-calibrated EONIA

1 October:



No overnight rate
published

The transition from EONIA to €STR


WG recommendations re transition from EONIA to €STR


Preparation phase

Recommendation: Market participants to:

-  (i) gradually replace EONIA with €STR as a reference rate for all products and contracts,
-  (ii) make all reasonable efforts to replace EONIA with €STR as basis for collateral interest for both legacy and new trades with each of its counterparties.

Recommendation: EMMI to:

 modify current EONIA methodology to become €STR + spread (8.5 bps) from first publication date of €STR until the end 2021.

 Following public consultation, EMMI announced EONIA's change of methodology as of 02/10/2019 until 31/12/2021.

EONIA modified to be published on T+1 at or shortly after 9:15.

Last EONIA publication: 03/01/2022.

Adoption phase



Following public consultation, on 16 July WG published final recommendations on the EONIA to €STR legal action plan

WG published a report by end-July incl. recommendations re **cash and derivatives** on:



- (i) T to T+1
- (ii) closing out legacy EONIA exposure
- (iii) details on the new discounting regime
- (iv) use cases for €STR in cash products



WG sent a **letter to the IASB** mid-July to inform of the status of the euro benchmarks reform agenda and flag the need for some urgent clarifications / possible relief on IFRS 9 and IAS 39.



WG continues working on:

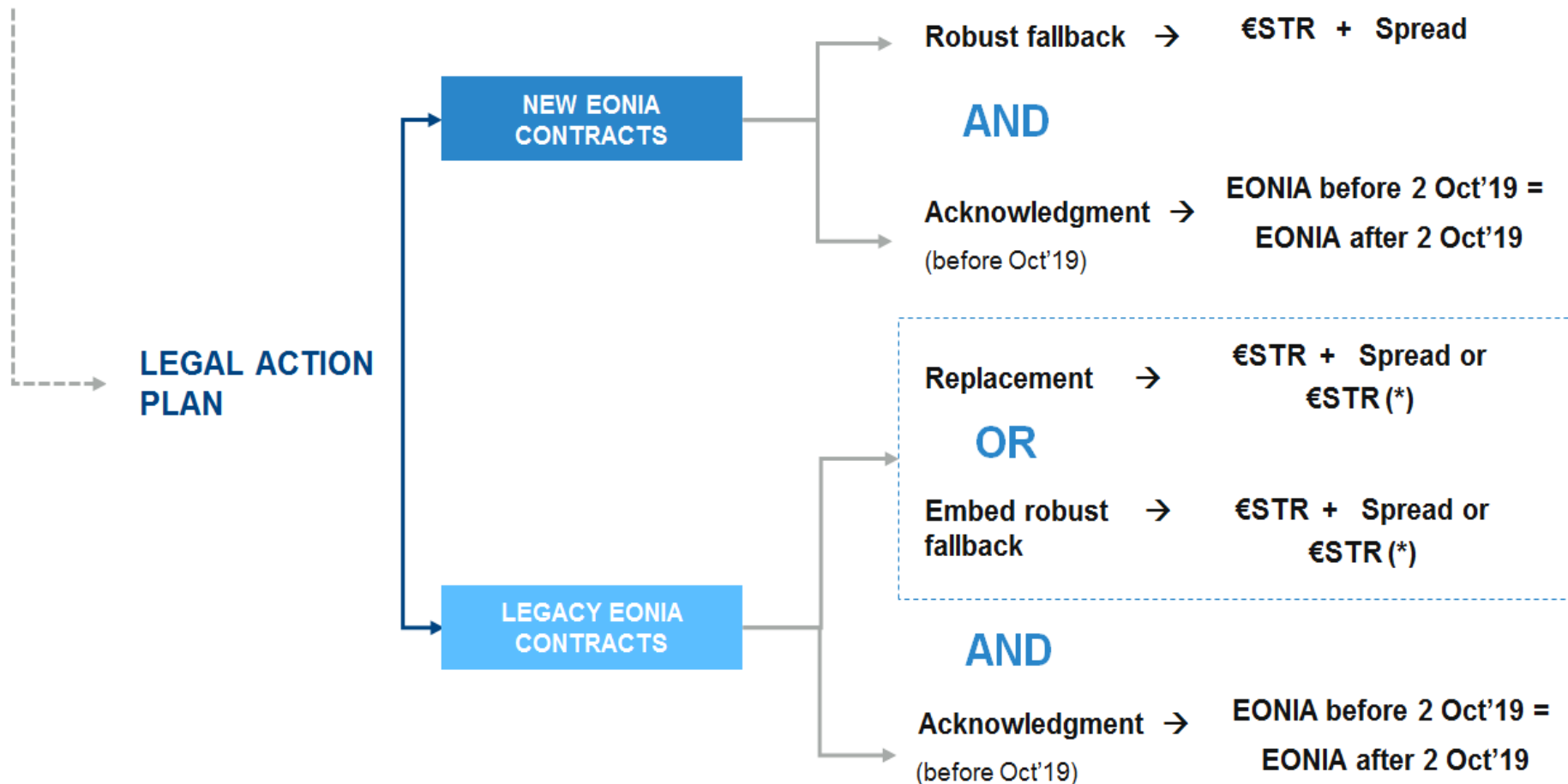
- (i) establishing a liquid €STR derivatives market;
- (ii) financial accounting & risk management issues.

The transition from EONIA to €STR

WORKING GROUP
RECOMMENDATIONS AND EONIA
TO €STR LEGAL ACTION PLAN

Use €STR in new contracts and products as soon as possible

EONIA fallback rate → €STR + Spread



EONIA to €STR Legal Action Plan

€STR plus a fixed spread of 8.5 basis points as EONIA fallback rate for all products

New contracts: Market participants, whenever feasible and appropriate, should avoid entering into new contracts referencing EONIA, in particular new contracts maturing after 31 December 2021.

New contracts signed before October 2019 should ideally include clarification that the EONIA methodology is expected to change as of 2 October 2019 and that references in contracts to EONIA shall be understood to be references to EONIA as changed.

Legacy contracts: For existing contracts maturing after December 2021, market participants should replace EONIA as a primary rate as soon as possible or embed robust fallback clauses.

EURIBOR and €STR-based fallbacks

Base case for the Working Group: EURIBOR reformed, BMR compliant

EMMI

(EURIBOR's
administrator)

- Currently phasing-in of the hybrid methodology of EURIBOR
- "Hybrid methodology" aims at better anchoring the banks contributions in real transactions

FSMA

(EMMI's competent
authority)

- 3 July 2019: EMMI authorised as administrator of the EURIBOR by the FSMA, i.e. EURIBOR compliant with BMR

WG working on identifying €STR-based fallbacks for EURIBOR:

- Fallback provisions as required by Article 28 of the BMR.
- Forward looking methodologies, including expectations.
- Backward looking methodologies based on calculations over realised rates.

The transition from EONIA to €STR

Preparations by market participants necessary

Processes



- Use the new rate
- Systems: new timing
- Dealing, hedging

Documentation



- Procedures
- Contracts, fallbacks
- New products

IT setup for €STR:

ISIN: EU000A2X2A25

German WKN: A2X2A2

FISN: ECB/EUR EURO SHORT-TERM RATE IR