IBOR Reform Panel Luxembourg

18:30 - 19:50

Opening of the Panel IBORs Transition: are we ready for the challenge?

Mr. Pascal Nicoloso – ECB
Team Leader for the Work on Reference Rates and Project Manager for €STER
Mr. Yassine Boudghene – EIB
Head of Division in charge of Financial Policies
Mr. Olivier Hubert – NATIXIS
Global Head Short Term Treasury BPCE / NATIXIS President ACI France
Mr. Andrea Lanzi – HSBC/ AEFMA GERMANY Vice President
Short break and drinks

Jan Eger
Introduction:
I think this going to be a very useful and interesting panel in that the participants are both from the official (Central Banks/ Regulators involved in the transition) and private sector. Very grateful for the participants for flying in to be with us. It shows the important role of the authorities in facilitating together with the private sector this particular complex transition.

I am going to start by reminding you of what we are going to be talking about today.

In July 2017 Andrew Bailey, the Chief Executive of the FCA said that the FCA would no longer intend to compel or persuade banks to submit contributions for LIBOR after the end of 2021.

In the view of the authorities, the problem with LIBOR is first of all since the financial crisis, the structure of financial markets has changed, LIBOR has become the rate at which banks do not lend to each other. Second, LIBOR is a risk to financial stability. The pricing of hundreds of trillions of USD of financial instruments rests on the expert judgment of

relatively few individuals. And third, in the period before the introduction of benchmark regulation in different jurisdictions, there was more scope for LIBOR to be manipulated.
So, to avoid these problems, the authorities want financial markets to transition away from LIBOR and the other IBORs to near risk free rates. To enable the market to move away from IBORs, three main areas of concern must be addressed:

1. Identify alternative risk-free references (RFRs) to replace LIBOR
2. In the case of these replacement rates, write fallback alternatives into contracts and specify how they will be used in any existing contracts that reference LIBOR
3. Adjust the RFRs (essentially overnight rates) to deliver a term rate representation

In all the major jurisdictions, the chosen risk-free rates are overnight rates: SONIA in the UK, SOFR in the US, €STR in the Euro-area, SARON in Switzerland and TONA in Japan.

The transition to risk-free rates is a global challenge. It will only succeed if the authorities and market participants work closely together. And to help organise the transition, the authorities have set-up a series of working-groups with market participants.

I am very pleased to welcome today senior officials working on the transition and market participants who are faced with the challenges:

To my right XXX, etc, etc
….and we're going to discuss some of the key issues affecting market firms.

First of all, the progress that has already been made with the adoption of risk-free rates so far. Secondly, the challenges ahead (and there are many of them) and third, delivering the transition. What the authorities are doing and what the authorities want the market to do and the timetable for doing it.

So this panel affects everybody in the room. So I am going to start with the ECB:
Pascal, €STER will go live from October 2019, with an indicative rate being published daily up to that date. Please explain to the audience the first of all, the progress that has already been made with the adoption of risk-free rates so far. Secondly, the challenges ahead (and there are many of them) and third, delivering the transition. What is the ECB and authorities doing are doing and what do you want the market to do and the timetable for doing it.

Then to all the other panellists

e.g.
Explain in practice how the EIB/ is experiencing the transition. Concrete messages on the experience it has and make a number of proposals. Different approach in reform between the US and UK, vs Euro area. Currently no clear pressure from the EU. Cash- and Derivative market interlinked in €STR.

What is clear and what is less clear at the moment?

What are the concrete issues you are facing? What does it mean from an AML point of view? Contingent point of risk.

Market readiness, incl. non-bank community. Bank have to be ready for 2 October but also their customers need to be ready. Some banks are very aware but others aren't. Is the customer communication taking place

Sense of urgency is it high enough? Why don't we have solutions to some of the challenges?

Talk about fall-back rates and how their calculation may be different to derivative market/ create accounting issues.

Q2) €STER & differences to EONIA. Why is €STR better?

Q3) We also see in the market the reform of existing IBOR benchmarks. Where the IBORs are being reformed, we are seeing two things.

1) *is another form of wholesale funding. These reforms are bringing in non-bank sources of funds. For instance, from insurance and pension companies to money market funds and non-financial corporates. That brings these reformed IBORs closer to CIDOR (Canada) and BBSW (Australia)- based on bills where the buyers are not banks.*
2) *Introducing waterfalls for banks to submit input data.*

Where does the panel think the market will go- the loan market, the FRN (floating rate notes) market and the derivative market? Towards hybrid reformed rates such as EURIBOR or €STR and EONIA?

Q4) We have heard the EC note the extensive retail use of Euribor as one of the reasons for the reform of the rate. How do you see the future use of EURIBOR develop in the retail space vs €STR (for mortgages, retail loans and credit cards)?

Q5) Back in the 1980s the market moved away from risk free term structures (based on T-Bills) to LIBOR because the latter actually did reflect their marginal cost of credit & the former didn't. What's different today (it's an open question really)?

Q6) There seems to be continued reliance on expert judgment (Extensive Level 3 reliance despite the Hybrid EURIBOR reform implying limited term funding by banks). What are your views on that and the

Annex:
Q6) I would like the panel to reflect on the 3rd country benchmarks / critical benchmark BMR implementation extension.

Q7) There has been some discussion of creating compound overnight reference rates based on the official RFR itself. One example is SAFR, that has been proposed in the US (based on SOFR). SIX Exchanges in Switzerland has released for illustrative purposes compound released rates based on SARON to help with the transition to the RFRs, especially for FRNs and derivatives. Does the panel see these of use for the transition from LIBOR and other IBORs?

Q8) to the EIB: What potential/ investor appetite do you see for any ESTR-based FRNs? What investor community would be interested?

Audience Q&A

Closing:
So you have heard from the four panellists about the main messages. There is a lot of information on the Risk Free Rate Working Group Website, there are also special pages on websites of associations such as the ICMA, which link in and source information from key authorities the market.

Please make use of that information. The message to take away today is the need to prepare for the transition to RFRs: in yourselves as market firms, law firms and participants – but to also speak to your clients to make sure they understand what the transition involves. So that everybody is properly prepared for something that will happen and will affect all of us and that we will need to be prepared for.

I would like you to thank the panellists for coming over today to talk to you!

Reform of Euribor owing to retail need (in contrast to official sector push in other countries from IBORs to the o/n RFRs)
Extensive Level 3 reliance despite the Hybrid EURIBOR reform implying limited term funding by banks
€STER & differences to EONIA
European views on continued usage of EURIBOR vs. migration to €STER (it's not clear)
Issues relating to lack of credit in term fixings derived from EONIA/€STER and other RFRs.