

Minutes of the Meeting of the Working Group on Sterling Risk-Free Reference Rates
Friday 14 October 2016
Barclays' offices – Canary Wharf

Obligations under competition law

1 The Chairman reminded all members of the Group of their responsibilities in relation to compliance with competition law and the importance of taking their own independent competition law advice. He made clear that this was particularly relevant as the work of the group progresses to the making of practical recommendations in relation to Sterling Risk-Free Reference Rates.

The Reform of SONIA

2 The Bank – in its capacity as the SONIA benchmark administrator – provided a summary of the consultation on the reform of SONIA that it had issued on 10 October.¹ The reformed SONIA rate would be based on data capturing 95% of overnight unsecured sterling money market transactions, by including bilateral as well as brokered deposits. This change would result in a 3 to 4 times increase in volumes, with average daily volumes around £36 billion. The concentration of data reporters in reformed SONIA would be lower than for current SONIA.

3 The Bank noted that bilateral transactions in the available sample tended to occur at slightly lower rates than brokered transactions, on average. Related to this, it was proposed that the calculation methodology for reformed SONIA would change to a volume weighted median, from a volume weighted mean currently. This would help to ensure that the reformed rate was consistent with the existing measure of SONIA, given the change to the data inputs; and is robust to outliers and unrepresentative trades. There was a 1 to 2 basis point spread between reformed SONIA and current SONIA over the sample period, and daily changes in the proposed rate had tracked changes in current SONIA closely over the sample period.

4 The Bank explained that it anticipated the transition to reformed SONIA would be a point-in-time switchover from current SONIA to reformed SONIA: a 'seamless transition'. SONIA reforms were expected to be implemented in 2017 Q4, with a more precise date to be communicated in early 2017.

5 The Bank outlined that, under international regulatory best practice – including the EU Benchmarks Regulation² and the IOSCO Principles for Financial Benchmarks³ – benchmark administrators are expected to have in place procedures for the evolution of benchmarks, or the cessation of benchmarks, for example in the event of structural change in the underlying interest. Accordingly, the Bank had proposed that the definition of SONIA be separated into a definition of the underlying interest (an enduring statement of the economic concept that the benchmark seeks to measure) and a statement of the methodology (how it is currently to be measured) that might if necessary change in response to market developments that undermined the current methodology. That would facilitate the smooth evolution of SONIA if required, allowing for greater contractual certainty/continuity.

¹ www.bankofengland.co.uk/markets/Documents/soniareformcp1016.pdf

² Regulation (EU) 2016/1011 on indices used as benchmarks in financial instruments; see eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016R1011&from=EN.

³ See www.iosco.org/library/pubdocs/pdf/IOSCOPD415.pdf

6 The Group discussed the Bank's proposals for re-defining SONIA. Whilst recognising the greater contractual certainty provided by the Bank's proposed approach, some members of the Group felt that the proposed broad definition of the underlying interest of SONIA might lead to uncertainty as to the potential timing and scope of any future evolution, and that this uncertainty had the potential to discourage usage of SONIA as an RFR. An alternative approach would be to define the underlying interest of SONIA more narrowly, reducing the scope for future uncertainty about the input data, but increasing the chance that any material future changes in the underlying market could necessitate a transition to an alternative benchmark. The risks of such a transition were obvious, although they could be mitigated through a common approach to contractual fall-back provisions.

7 It was suggested that a clear and transparent process and governance around the evolution of the benchmark would be desirable. In this regard, the Bank had highlighted in the consultation that any evolution process would involve, where possible, consultation with end-users of SONIA.

8 The Group deliberated the impact of moving publication of SONIA to the following business day. The ISDA representative noted that the Rates Market Infrastructure Group has been considering the impact on the calculation of the floating-leg payment of sterling OIS. In particular it is examining whether settlement can still occur on the maturity date of the swap, as is current practice, or whether firms would prefer to defer settlement to the following day. Feedback to date has been split between these two positions. Some Working Group members felt that deferring settlement procedures in the sterling swap market to align better with market practice in other currencies may be preferable, noting that the timeframe for settlement in Asia would otherwise be compressed. ISDA expects a consensus to be reached in 2017.

9 The Group also discussed the Bank's proposed approach to transition: a switch from current SONIA to reformed SONIA on one specific day. The Bank noted that trade repository data showed 70% of existing SONIA-referencing swap contracts had a residual maturity of less than nine months, so the majority of existing contracts at the point of switchover will have been agreed with knowledge of the final details of the reforms.

10 As noted in its Interim Report, the Group had previously considered the discontinuation of SONIA as a means to stimulate transition of the sterling OIS market to reference a secured rate.⁴ Since the Bank viewed the existence of an unsecured benchmark as important for the transparency of unsecured money markets, an implication of this approach was for reformed SONIA to have been introduced as a new benchmark. In the Bank's view as the administrator of SONIA, the introduction of a reformed unsecured rate and the discontinuation of SONIA would have been warranted only if the reformed rate were a materially different benchmark to current SONIA. In fact, as the analysis in the consultation showed, this was not the case.

11 The Bank emphasised that the key priority for the Group was to select the near risk-free reference rate that had the highest chance of widespread adoption as an alternative to Libor, and that the Bank would support the implementation of whichever rate was chosen by the Group.

⁴ See www.bankofengland.co.uk/markets/Documents/sterlingoperations/rfr/2016/rfrwgintrep16.pdf

Voting governance and future meetings

12 The Chair proposed a plan for future meetings. The present meeting had focused on reformed SONIA, while the following meeting would focus on candidate secured rates, including a discussion of how a transition of the sterling OIS market to reference a secured rate could be achieved. Subsequent meetings would revisit the Group's initial selection criteria and then proceed to a vote for a recommended rate. The Group would then engage in a consultation process with broader market participants on their recommended rate in early 2017 prior to a final recommendation being made.

13 The Chair's office confirmed that, after the next meeting, only voting members and the authorities would be present, to avoid the perception of a conflict of interests for private sector non-voting members. The Chair proposed electronic voting via a secure email to the Bank; the Group agreed this was a sensible approach.

14 Consistent with previously outlined best practice for Group members' governance,⁵ the Chair detailed some recommended minimum governance requirements for Working Group members.

⁵ See www.bankofengland.co.uk/markets/Documents/sterlingoperations/rfr/2016/minutes22jan16.pdf

Private sector attendees

Nick Sagers	Bank of America-Merrill Lynch
Francois Jourdain	Barclays (Chairman)
Andreas Giannopoulos	Barclays (Chair's office)
Nick Hallett	Barclays
Bruno Chauviere	BNP Paribas
Adrian Averre	BNP Paribas
Alain Verdickt	Citigroup
Stephen Randall	Citigroup
Arif Merali	Credit Suisse
Michael Graham	Goldman Sachs
Christophe Rivoire	HSBC
Charles Bristow	JP Morgan
Christophe Coutte	Lloyds
Freddie Napier	Morgan Stanley
Mike Curtis	Nomura
David Bradley	Royal Bank of Scotland
Andrew Cross	Santander
Stephane Cuny	Société Générale
Chirag Dave	UBS
Catherine Farrer	ISDA (Observer only)
Phil Whitehurst	LCH.Clearnet (Observer only)

Official sector attendees

Tim Taylor	Bank of England
Will Parry	Bank of England
Rob Harris	Bank of England
Renée Horrell	Bank of England
Jan Lasik	Bank of England
Ben Morley	Bank of England
Harriet Hunnabell	Financial Conduct Authority
Devid Mazzonetto	Financial Conduct Authority