

**CONSULTATION PAPER
ON THE
RECOMMENDATIONS FOR EONIA
OF THE
WORKING GROUP ON EURO RISK-FREE RATES**

20th March 2019

*The **European Money Markets Institute (EMMI)**, formerly known as Euribor-EBF is an international non-profit making association under Belgian law founded in 1999 with the launch of the euro and based in Brussels (56, Avenue des Arts, 1000 Brussels.*

As per EMMI's statutes, its purpose is twofold:

- I. The development and support of activities related to the money and interbank markets. To that end, the association shall have the task of making an evaluation of fluctuations in the interest rates in the money and interbank markets of the euro area and of providing the results of its research to the monetary authorities and interested parties who are active in these markets.*

- II. In ancillary, the association shall also serve to support other practical initiatives fostering the integration of the European financial market such as but not limited to the improvement of the liquidity, safety and transparency of the European short term debt market by means of a harmonized framework for short-term European paper 'STEP'.*

EMMI currently provides the following two indexes: EURIBOR, the money market reference rate for the euro and EONIA, the effective overnight reference rate for the euro.

EMMI is continuously working to enhance its governance framework and to improve the quality, integrity, and transparency of its benchmarks. Moreover, EMMI strives to develop suitable benchmarks adapted to the latest regulatory requirements context.

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1 Introduction

EONIA is a major reference rate for the European money markets, as it represents the rate at which banks lend funds in the overnight interbank money markets in euro. It is a fully transaction-based reference rate, calculated on the basis of the submissions coming from a panel of 28 credit institutions (the Panel Banks), which report, on a daily basis, the volume-weighted average rate of their executed overnight interbank lending transactions, as well as the corresponding aggregated notional volume.

In 2016, seeking to enhance EONIA's governance and align its determination with the requirements of the EU Benchmarks Regulation (EU BMR),¹ EMMI launched the **EONIA Review**. As part of this programme, EMMI also intended to enhance EONIA's methodology, in view of some shortcomings that had been historically observed.

[EONIA's underlying dynamics](#)

The low underlying EONIA volumes represent the market it intends to measure. The current monetary policy environment, coupled with macro-prudential measures, does not encourage unsecured short-term lending between banks. According to the [ECB's study](#) of the size of the unsecured overnight money market based on TARGET2² data, "volumes stood on average at EUR 6 billion (...) in September 2017." EONIA's average underlying volume in that same month was EUR 7.2 billion.³

The limited market activity has reflected on the EONIA rate as an increase in the concentration of

underpinning volumes in a limited number of EONIA Panel Banks. At the same time, the number of Panel Banks which submit non-zero volumes has decreased significantly over the past few years. This trend may reflect the contraction of the unsecured money markets, also captured and portrayed more recently in the [First ECB public consultation on developing a euro unsecured overnight interest rate](#).

[The working group on euro risk-free rates](#)

On 21 September 2017 the European Central Bank (ECB), the Belgian Financial Services and Markets Authority (FSMA), the European Securities and Markets Authority (ESMA) and the European Commission announced the launch of the working group on euro risk-free rates (the Working Group or WG).⁴ On the same day, the ECB also [announced](#) its intention to publish a new unsecured overnight interest rate based on data already available to the Eurosystem, which later materialised as the euro short-term rate (€STR).

[The end of the EONIA Review](#)

On 1 February 2018, EMMI communicated on its intentions to stop efforts related to the alignment of EONIA with the requirements of the EU BMR.⁵ This decision was made on the basis of discussions with EONIA Panel Banks and other stakeholders, reflecting a non-existent support and appetite for a fully-fledged EONIA Review. At that time, EMMI highlighted how under unchanged conditions and dynamics in the unsecured segment of the euro

¹ (EU BMR) [Regulation \(EU\) 2016/1011 of the European Parliament and of the Council of 8 June 2016](#) on indices used as benchmarks

² TARGET stands for Trans-European Automated Real-time Gross settlement Express Transfer System. The euro system maintains TARGET2, which is the second generation of TARGET and is a real-time gross settlement system. Throughout this document, references to "TARGET" should be read with respect to the euro system's TARGET2 system.

³ The difference between these volumes is due to the fact that not all EONIA-eligible transactions settle in the TARGET2 system/Central Bank money.

⁴ In view of its role as an administrator of critical benchmarks, EMMI is a [non-voting member](#) of the Working Group.

⁵ In discussions with market participants and EONIA Panel Banks, EMMI indicated that redefining EONIA as an overnight *wholesale borrowing* benchmark would most likely allow for a more robust and representative interest rate, with a lower geographical concentration. At that time, the ECB had already indicated their intention to produce an overnight interest rate benchmark which would serve as a backstop for EONIA.

money market “EONIA’s compliance with the EU BMR by January 2020 could not be warranted.”

[Recommendations of the Working Group on euro risk-free rates](#)

Following the [recommendation of the Working Group of the ECB’s €STR](#) as the alternative euro risk-free rate (RFR) on 13 September 2018, the Working Group continued exploring possible approaches to ensure a smooth transition from EONIA to the €STR. In December 2018, the Working Group published a [report on the transition from EONIA to the €STR](#) (the Report), in which a number of transition scenarios, proposals, and recommendations to promote and facilitate this transition were laid out.

Some of the recommendations presented in the Report were addressed to EMMI. Given the systemic importance of EONIA for the financial markets, also recognised by the European Commission in June 2017, when EONIA was classified as a critical benchmark under the EU BMR, EMMI would like to consult the public on the measures proposed and [endorsed by the Working Group during its meeting on 14 March 2019](#).

Due to the dependencies between the recalibration of EONIA’s methodology and the ECB’s production plans for the €STR, which stem from the recommendations of the Working Group, the market and other users of EONIA will have to adapt to a change in the publication time of EONIA in a short timeframe. By conducting this consultation, EMMI intends to raise awareness of the implications of the suggested changes, and ensure that users of EONIA start preparing for the potential upcoming changes as soon as possible.

Responses to the questions included at the end of the consultation and feedback on the overall approach should be sent to eonia2019@emmi-benchmarks.eu. **The consultation period closes on Monday, 15 April 2019 at 5:00 p.m. CET.**

EMMI will evaluate all responses and prepare an anonymised feedback summary. **This summary will be published on EMMI’s website on Thursday, 30**

May 2019. Final details on the implementation plan will also be announced on that date.

2 The recommendations of the working group on euro risk-free rates

The following table transcribes the recommendations addressed to EMMI by the Working Group. These recommendations received [broad supportive feedback](#) from the financial sector and other interested parties. The formal endorsement of the Working Group followed a voting procedure, whose [outcome was disclosed on 14 March 2019](#).

In order to allow for an easier reading, references to each of the recommendations/paragraphs are placed throughout the consultation.

BOX 1

Recommendations of the working group on euro risk-free rates

1. The working group recommends that the European Money Markets Institute (EMMI), as the administrator of EONIA, takes the following steps before 1 January 2020:
 - a) Modify the current EONIA methodology to become the €STR plus a spread for a limited period, in accordance with Financial Stability Board (FSB) recommendations and IOSCO Principles for Financial Benchmarks to further anchor EONIA's methodology in transactions;
 - b) Engage with the relevant authorities to ensure the compliance of EONIA, under its evolved methodology, with the EU Benchmarks Regulation;
 - c) Consider and consult market participants on discontinuing the publication of EONIA under its evolved methodology, after a transition period that ensures firms can achieve transition to the €STR in a smooth manner and that pays due regard of the existing EONIA legacy book. This transition period should last until the end of 2021, which is consistent with benchmarks transitions in other jurisdictions.
2. The working group also invites EMMI to take the following considerations into account:
 - a) Consider an EONIA-€STR spread methodology based on a simple average with an observation period of at least 12 months, combined with a 15% trimming mechanism;
 - b) That the recalibration methodology and the effective determination of the spread are announced at the same time before the €STR's first day of publication;
 - c) That the recalibration date is on the first day of the €STR's publication for simplicity reasons.

Source: [Report on the transition from EONIA to the €STR, 2018](#).

3 Recalibration of EONIA’s methodology

EONIA’s Benchmark Specification

The EONIA Governance Framework defines EONIA’s **underlying interest** as the rate at which banks of sound financial standing in the European Union and the European Free Trade Area (EFTA) lend funds in the (unsecured) overnight money market in euro. The underlying interest represents the more fundamental element of EONIA’s specification, as it defines the market or economic reality that it seeks to measure.

The **determination methodology of EONIA**, in turn, describes how the underlying interest is to be measured. To derive EONIA from the data contributed by the EONIA Panel Banks (which are to be understood as a *sample* of the total population of *banks of sound financial standing in the EU and EFTA*), EMMI aggregates the individual contributions in a volume-weighted average, which gives rise to EONIA.

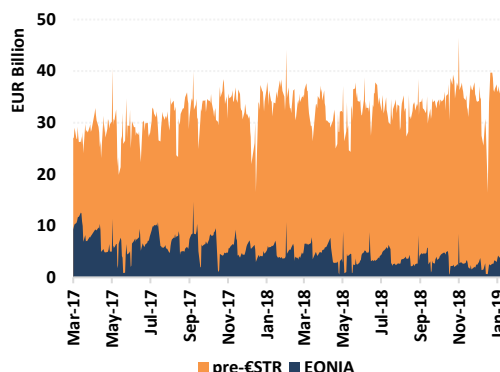
The choice of this calculation method reflects the characteristics of the unsecured overnight interbank money market at the time of the creation of EONIA, when overnight interbank lending activity was plentiful and more proportionately and homogeneously distributed across Panel Banks than nowadays.

The proposed change in EONIA’s methodology (WG’s recommendation 1.a))

The €STR is the euro short-term rate, administered by the ECB. In September 2018, it was identified by the Working Group as the rate recommended to replace EONIA as the risk-free rate (RFR) for the euro. The €STR seeks to reflect the wholesale euro unsecured overnight borrowing costs of euro area banks.

In the Report, the Working Group recommends to modify the current EONIA methodology to become the €STR plus a spread, further anchoring EONIA’s determination in executed transactions.

Chart 1 (Underlying volume)



Source: EMMI, ECB

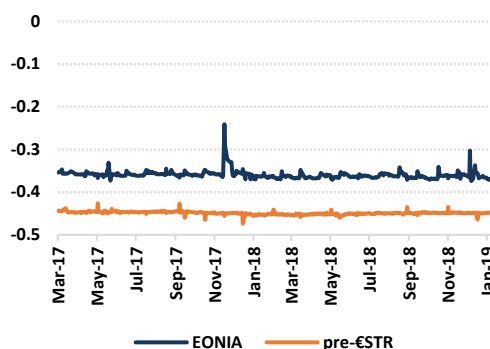
The proposed recalibration of EONIA’s methodology intends to overcome some of the methodological shortcomings discussed in the Introduction which prevent EONIA from being considered as EU BMR compliant under the current methodology.

EMMI understands from the Working Group Report and its recommendation that the suggested spread between EONIA and the €STR (discussed below) is a measure of the economic difference between the underlying interests of the two benchmarks (interbank lending rate vs wholesale borrowing rate). To this extent, **EMMI considers that the economic value that EONIA seeks to represent is not altered by the change in methodology.**

EONIA-€STR spread (WG’s recommendation 2.a), b))

The Working Group highlights that the objective of the EONIA-€STR spread would be to mitigate potential value transfers between market participants. As the spread would measure the

Chart 2 (EONIA vs. €STR)



Source: EMMI, ECB

observed differences between the two benchmarks, it would provide a stable framework to facilitate a smooth transition to the €STR, as the recommended euro RFR.

To this end, the Working Group recommended EMMI the use of a spread which is

- a) fixed over the period that EONIA will be calculated using this methodology; measured using evidence coming from historical data from both pre-€STR⁶ and EONIA;
- b) communicated at the same time the final decision on the implementation of the methodology is announced to the market, and before €STR's first day of publication.

The Working Group made one further recommendation with respect to the precise methodology, which shall be used to calculate the EONIA-€STR spread. In particular, the Report advises **a spread based on data collected over a period of at least 12 months⁷ and calculated as a 15% trimmed mean⁸ of the observations.**

Following the recommendation of the Working Group, EMMI would agree to use the result of such a calculation for the determination of EONIA under the proposed recalibration methodology. The recommendation put forth by the Working Group indicates that the calculation of this spread is to be performed with the most updated and recent pre-€STR data at the time the final decision on the implementation of the methodology. In a [press release](#) on 14 March 2019, the ECB indicated that in order to further support private sector efforts in the transition away from EONIA, **the ECB will provide the computation of a one-off spread between the €STR and EONIA.** The resulting spread will be communicated on the day on which the change in the methodology of EONIA is announced.

Question 1. In view of the Working Group's recommendation, do you agree that EMMI implements the recalibrated methodology for EONIA, whereby EONIA will be defined as the €STR plus a *spread*? If not, please provide a rationale for your answer.

⁶ The ECB called [pre-€STR](#) the data published for market participants to assess the suitability of the new €STR rate.

⁷ The Working Group recommends that the 12 months observation period should be based on the latest pre-€STR data series available at the time of the announcement of spread.

⁸ To calculate the 15% trimmed mean the observed daily EONIA-€STR spreads are arranged in ascending order from lowest to highest. The highest and lowest 15% of these observations are discarded and the final *spread* is obtained as the simple average of the remaining numbers.

4 Discontinuation of EONIA

The use of the recalibration methodology proposed by the Working Group should be understood as a temporary solution to facilitate and ensure that the market and users can achieve a transition to the €STR in a smooth manner.

[Publication of EONIA until 3 January 2022](#)
(WG's recommendation 1.c))

The Working Group recommends EMMI to continue providing EONIA defined as the €STR plus a spread during a *transition period* of approximately two years in order to incentivize users to transition from EONIA to the €STR. EMMI accepts this recommendation, as it understands it will give counterparties enough time to either let their EONIA legacy books lapse, or to renegotiate their existing contracts to move to the €STR.

Considering the discussion in Section 6 on the change of the time of publication of EONIA upon implementation of the recalibrated methodology, **EMMI proposes that the last publication of EONIA calculated with the methodology proposed by the Working Group is 3 January 2022**, as it will represent the market on 31 December 2021.

Question 2. Do you consider that the discontinuation of EONIA on 3 January 2022, allows for and promotes the orderly transition of the market away from EONIA to the €STR? If not, please provide a rationale for your answer.

5 Implementation of EONIA's recalibrated methodology

As discussed above, the Working Group recommends **the first day of EONIA publication under the recalibrated methodology to coincide with the first day of publication of the €STR**. The Working Group justifies this recommendation as a way to avoid any possibility of arbitration. In addition, the parallel publication of €STR and EONIA under the current methodology would not act as an incentive for market participants and users of EONIA to transition to, and finalise arrangements for the full adoption of, the €STR in their contracts, products, and procedures.

The implementation date of EONIA's recalibrated methodology
(WG's recommendation 2.c))

The ECB has recently [announced](#) that the first day of publication of the €STR will be 2 October 2019. As a result, and following the recommendations of the Working Group, **EMMI will plan for the first publication of EONIA under the recalibrated methodology on the same day, i.e. 2 October 2019.**

Question 3a. Do you agree that EMMI should avoid the continued publication of EONIA under the current methodology once the €STR starts being published? Please provide a rationale for your answer.

Question 3b. Do you foresee any issues arising from the projected implementation date of EONIA's recalibrated methodology on 2 October 2019? Please provide a rationale for your answer.

6 Moving EONIA’s publication from T to T+1

EONIA is currently published by 7:00 p.m. Brussels time every day on which the TARGET2 system is open. The calculation relies on transactions executed by Panel Banks on the same day of publication, before markets have closed (day T).

The implementation of the changes in the EONIA methodology, as recommended by the Working Group, requires EMMI to defer the publication of EONIA until after the €STR has been published. Unlike EONIA today, the €STR will be published on the day following the execution of trades (day T+1).

Other overnight benchmark reform efforts have also undergone these changes in publication times, in order to guarantee the processing of all input data. Most notably, the Bank of England changed the publication time of the reformed SONIA to the morning of the day following the day of execution of underlying transactions, in order to guarantee the correct processing of data.

The Working Group highlighted the implications of the move of publication from the end of day T to the morning of T+1 in their Report, advising all EONIA users to not underestimate the impact in IT and valuation systems that this change in publication time could have, and encouraging all parties to make the necessary changes to guarantee a smooth transition to a T+1 EONIA publication.

Question 4. Do you foresee any impediments for the preparation and implementation of changes in IT or valuation systems prior to the first publication of EONIA under the recalibrated methodology on 2 October 2019? Please provide a rationale for your answer.

Envisaged transition calendar

The following table summarises EMMI’s proposed approach for the move of publication of EONIA from day T to day T+1, which takes into consideration the first day of publication of the €STR (as announced by the ECB) and the

recommendation of the Working Group to not allow for the parallel publication of EONIA under the current methodology and the €STR.

Monday 30 Sept 2019	Tuesday 1 Oct 2019	Wednesday 2 Oct 2019
Day before move	Day of move	Day after move
T_{M-1}	T_M	T_{M+1}
EONIA is calculated under the current methodology.	No EONIA rate is published.	EONIA is calculated under the recalibrated methodology at 11:00 a.m. CET.
EONIA published on day T_{M-1} reflects the market on day T_{M-1} .		EONIA published on day T_{M+1} reflects the market on day T_M .

Question 5. Do you foresee any challenges in the calendar proposed by EMMI to transition EONIA from the current to the recalibrated methodology proposed by the Working Group? Please provide a rationale for your answer.

Envisaged publication time on day T+1

The change in EONIA’s methodology proposed by the Working Group makes EONIA dependent on the publication time of the €STR, as it is the main input for the determination of the recalibrated EONIA.

The [€STR methodology and policies](#) indicate that the ECB will publish the €STR no later than 09:00 a.m. CET on each TARGET2 business day. In addition, the ECB contemplates a republication policy that indicates that, in case errors are detected following standard publication that affect the published the €STR by more than 2 basis points, the €STR will be revised and republished on the same day, no later than 11:00 a.m. CET.

In order to minimize operational burden, EMMI proposes to publish EONIA under the recalibrated methodology at or shortly after 11:00 a.m. CET, in order to guarantee that errors derived from potential errors in the standard publication of the €STR do not impact the EONIA determination.

Question 6. Do you agree with EMMI's proposed publication time for EONIA under the recalibrated methodology? Would a publication at or shortly after 11:00 a.m. CET pose a challenge in your use of EONIA? Please provide a rationale for your answer.

7 How to respond to the Consultation

Throughout the text, EMMI has placed a number of questions for which we would welcome the market's feedback.

It is crucial for EMMI to obtain the largest number of responses possible, with a preference for full responses, in which the rationale behind each answer is fully elaborated.

For the readers' convenience, a .doc file has been made available on EMMI's website to for respondents to provide us with their feedback.

EMMI kindly asks respondents to submit their answers by e-mail to eonia2019@emmi-benchmarks.eu specifying "EONIA Consultation" on the subject line.

EMMI welcomes and encourages additional views or considerations regarding any issue discussed in this consultation paper, even if explicit questions are not included in the text.

The consultation period closes on **Monday, 15 April 2019 at 5:00 p.m. CET.**

Together with their responses, EMMI kindly asks respondents to submit the following minimum information:

- » Full name of respondent;
- » Position;
- » Organization and country;
- » E-mail address;
- » Contact telephone.

EMMI will evaluate all responses and prepare an anonymised feedback summary. **This summary will be published on EMMI's website on Thursday, 30 May 2019.** Final details on the implementation plans will also be announced on that date.

