EUROPEAN CENTRAL BANK

EUROSYSTEM

Summary of feedback

Public consultation on €STR-based EURIBOR fallback rates

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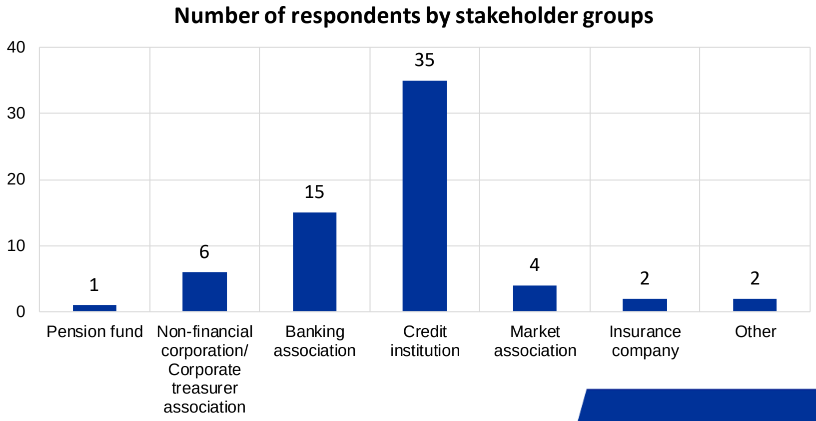
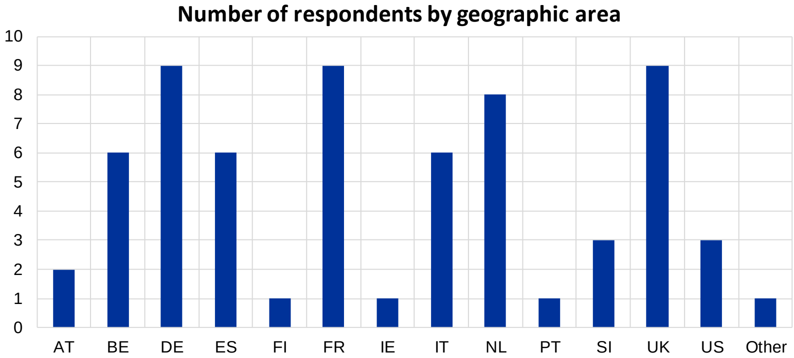
Feedback coverage

65 respondents: appropriate geographic coverage and considerable interest mainly from the banking industry





Criteria used in the analysis (Q1 & Q2)

78% respondents agreed with the **criteria identified by the WG**

Appropriate, exhaustive, comprehensive and robust

86% respondents agreed with the **analysis and conclusions of the WG** on the evaluation of the €STR-based term structure methodologies according to the criteria

Deep, accurate, rigorous, fair and well-balanced

- *Minimising the value transfer in the transition*
- *Methodological transparency*
- *Information content*
- *Market innovation opportunities*
- *Possibility of competent authorities to adjust regulation*

20% respondents pointed at additional criteria

10% respondents disagreed on the evaluation of several criteria

- *The evaluation "availability" factor of the robustness/availability criteria has been insufficiently considered*
- *The acceptance of the last reset methodology should be slightly downgraded*
- *The introduction of different types of rates would lead to a more complex transition and increase risks*

Use cases feedback summary (Q3 – Q12)

Products	Corporate lending	Retail mortgages/ consumer loans/ SME loans	Current accounts	Trade finance products	Export and emerging markets finance products		Debt securities	Securitisations	Transfer pricing model		Investments funds (benchmarking)
Fallback methodology recommended for the first level of the waterfall	BWL lookback 58%	FWL 81%	BWL p. delay 57%	FWL 84%	For most: FWL 69%	For some: BWL lookback 58%	BWL lookback 77%	Depending on the underlying assets 79%	Corporates and some financials: FWL 55%	Most financials BWL lookback 46%	FWL 50% BWL lookback 42%
Fallback methodology recommended for the second level of the waterfall (if needed)	N/A	BWL last reset 61% BWL Lookback 32%	N/A	BWL last reset 75%	BWL last reset 53%		N/A		BWL last reset 46%		BWL lookback 50%

Use cases – vast support to WG's proposal

Mortgages, consumer & SME loans

First level waterfall	Second level waterfall	Potential impediments
81% support to WG's proposal: **FWL**	61% support to: **BWL last reset (up to 3 M)**	• Issues related to the SPPI testing, client acceptance, potential litigation and legal issues; introduction of conduct risk • Main impediment: introduction of potentially non-hedgeable interest rate risk
	32% support to: **BWL lookback period**	• Legal impediments linked to consumer protection laws and client acceptance • Potential increase of delayed interest payments by less sophisticated users • IT systems not technically ready yet – demanding implementation

- Easier acceptance and transition - similarity with EURIBOR
- Provides more certainty for retail and SME clients

Use cases – vast support to WG's proposals

Trade finance

First level waterfall	Second level waterfall
84% support to WG's proposal: **FWL**	75% support to WG's proposal: **BWL last reset (up to 3 M)**

- Known in advance
- Conceptually closest to EURIBOR
- Consistency across jurisdictions

- Appropriate to add a backstop given the current lack of FWL rates
- Also known in advance, which is crucially important for trade finance products

Use cases – vast support to WG's proposal

Debt securities

77% support to

WG's proposal:

BWL

lookback period

A minority of 16% respondents preferred the **FWL** methodology

- Consistency with derivatives, which are frequently used in hedging securities
- Consistency across jurisdictions

- To better align with fallbacks for other financial products
- Some suggested the use of the BWL lookback on the second level of the waterfall

Use cases – vast support to WG's proposals

Securitisations

83% support to WG's proposal:

BWL

lookback period

for securitisations of assets where this methodology has been already identified as the most appropriate fallback

75% support to WG's proposal:

FWL

for securitisations of assets where this methodology has been already identified as the most appropriate fallback

- Alignment between the fallback used for the securitisation and its underlying asset would avoid basis risks arising between them

Use cases – (significant) support to WG's proposals

Export and emerging markets finance products

For the majority of export finance and emerging markets finance products

First level waterfall

69% support to

WG's proposal:

FWL

- Some respondents noted that FWL should only be used for products that need to know the rate well in advance
- 12% respondents preferred the BWL

Second level waterfall

53% support to:

BWL last reset

(up to 3 M)

- Known in advance but it comes with drawbacks
- 16% respondents preferred the BWL lookback

For those that involve sophisticated counterparties and developed markets

58% support to

WG's proposal:

BWL lookback period

- Consistency with derivatives is more relevant as these products are more likely hedged
- Sophisticated clients can handle a shorter period between the rates calculation and the payment
- 25% respondents preferred the FWL for consistency across the asset class and difficulty to disentangle sophisticated and non sophisticated clients

Use cases – support to WG’s proposal

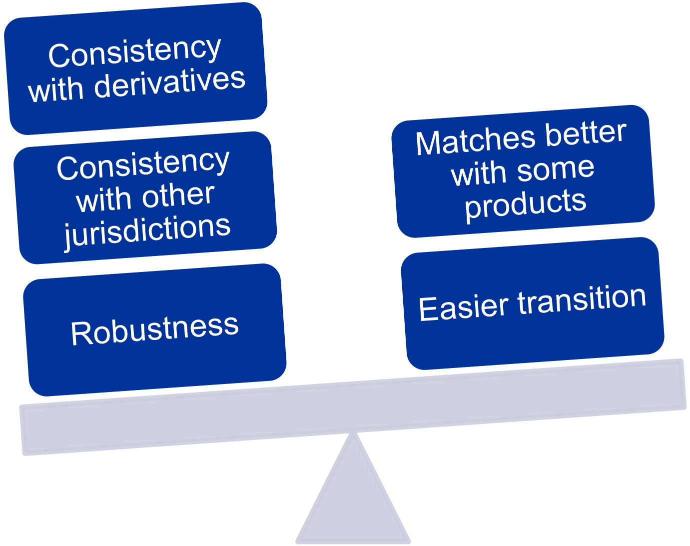
Corporate lending

“Should be planned well in advance as it is demanding in terms of IT implementation and resources”.

58% support to WG’s proposal:
BWL lookback

40% respondents:
FWL + BWL lookback

Most respondents: dependent on the existence of a liquid and robust FWL rate



Use cases – support to WG's proposal

Current accounts

57% support to

WG's proposal:

BWL

payment delay

- Fully represents time value of money
- Transparent
- Current accounts do not require a rate that is known in advance
- Simple to implement

Minority of respondents (17%) preferred a different methodology **but were divided on the most appropriate alternative**

- FWL for its similarity with EURIBOR
- BWL lookback for its consistency with other jurisdictions
- BWL last reset for being known in advance

26% respondents

registered

no opinion

- Several respondents noted that many current accounts are remunerated using overnight rates

Use cases –unclear response to WG’s proposals

Transfer pricing models

For non-financial companies			
First level waterfall		Second level waterfall	
55% support to: **FWL**	38% **No opinion**	46% support to: **BWL last reset**	31% **No opinion**

- Respondents repeated the arguments used for other asset categories to support the FWL/BWL methodologies

For financial companies

46% support to WG’s proposal: **BWL lookback period**

- Alignment with capital market securities and derivatives preferred to reduce basis risks
- Financial firms would be able to operationalise it

33% support to: **FWL**

- Consistency across financials and non-financials
- BLW lookback proposed as a backstop
- A few respondents requested flexibility

Use cases – Divergent views

Investment funds

A few respondents noted that investment firms might need flexibility to have different fallbacks for different investment funds (according to their funds' assets)

First level waterfall		Second level waterfall	
42% respondents: **BWL lookback**	50% support to: **FWL**	50% support to: **BWL lookback**	38% **No opinion**

BWL lookback:
- Consistency with debt and derivatives
- Consistency with other jurisdictions

FWL:
- Consistency with investment funds assets
- Easier transition & fewer changes to systems

Credit spread adjustment (Q13 – Q17)

Vast support to almost all WG's proposals

97% support **Historical mean/median methodology**	+	95% (essential/ highly desirable) **Aligned across currencies and products**	+	80% support **For each tenor (irrespective of fallback methodology)**	+	97% support **Use of EONIA fixings if €STR data insufficient**	~~+~~	25% support 1 year transition period

- Transparent approach based on widely available data and with a straightforward calculation
- Expectation that it would be broadly accepted
- Drawbacks of other methodologies

- Reduces complexity
- Avoids confusion and broadens market acceptance

- Facilitates the use of multicurrency products
- Reduces risk management costs

- Preference for a simple solution even when different approaches would be more accurate

- Transparent, easy to understand and widely accepted approach
- Acknowledgement that the lack of data becomes less relevant over time and it is unlikely that fallbacks will be trigger in the near future

- Adds complexity
- Inconsistent with ISDA's approach
- Some proposed to implement it for certain retail products

Calculation methodologies & conventions (Q18 –Q21)

Vast /significant support to WG's proposals

95% support

Published spread adjustment and /or all-in rate

- Transparent solution
- Constituent parts of the all-in rate to be published separately

87% support

Floor applied to (€STR compounded + spread)

- The proposal avoids operational complexity
- Aligned with ISDA"s methodology

90% support

Compounding the rate

- Easy to understand
- Consistent with existing practices in numerous financial markets
- Reflects time value of money

68% support

Observation shift

&

75% support

lag approach as a robust alternative

- Observation shift matches better other asset classes, notably derivatives
- Lag approach inconsistent with compounded €STR rates
- If rates are not volatile, small economic impact of both

- Consistency with other jurisdictions

Summary of responses available at

https://www.ecb.europa.eu/paym/interest_rate_benchmarks/WG_euro_risk-free_rates/html/index.en.html