

AFGG'S RESPONSE CONSULTATION

TRANSITION FROM EONIA TO ESTER

Report by
the ECB working group
on euro risk-free rates

6 February 2019



The Association Française de la Gestion financière (AFG) represents and promotes the interests of third-party portfolio management professionals. It brings together all asset management players from the discretionary and collective portfolio management segments. These companies manage at end 2017 €4,000 billion in assets, including €1,950 billion in French funds and €2,050 billion in discretionary portfolios and foreign funds.

The AFG's remit:

- Representing the business, financial and corporate interests of members, the entities that they manage (collective investment schemes) and their customers. As a talking partner of the public authorities of France and the European Union, the AFG makes an active contribution to new regulations,
- Informing and supporting its members; the AFG provides members with support on legal, tax, accounting and technical matters,
- Leading debate and discussion within the industry on rules of conduct, the protection and economic role of investment, corporate governance, investor representation, performance measurement, changes in management techniques, research, training, etc.
- Promoting the French asset management industry to investors, issuers, politicians and the media in France and abroad. The AFG represents the French industry – a world leader – in European and international bodies. AFG is of course an active member of the European Fund and Asset Management Association (EFAMA), of PensionsEurope and of the International Investment Funds Association (IIFA).

41 rue de la Bienfaisance - 75008 Paris - Tél. +33 (0)1 44 94 94 00
45 rue de Trèves - 1040 Bruxelles - Tél. +32 (0)2 486 02 90
www.afg.asso.fr - @AFG_France

Report by the working group on euro risk-free rates on the transition from EONIA to ESTER

1. Do you agree with the working group's recommendation that the preferred transition path is the time-limited recalibration approach with spread and clean discounting? (Yes/No/No opinion)

Yes

2. If not, what would be your preferred option and why? (Please choose from the other options presented in the report)

Please provide the reasons for your preferred option

The AFG is in line with the analysis of the working group on the transition path and therefore agrees with the time-limited recalibration approach with spread and clean discounting.

First, this path seems to be the best option to guarantee legal certainty and stability for contracts referencing EONIA, which is a prerequisite for a smooth transition. From an asset manager perspective, the continuity of contracts issue arises not only on the instruments referencing EONIA used by asset managers but also on funds referencing EONIA.

Therefore, the changeover from EONIA to the recalibrated EONIA shall be accompanied by extensive communication from the recalibrated EONIA administrator and public authorities so as to reduce litigation risk and avoid mandatory communication from asset manager to each investor in these funds.

Besides, from an economic perspective, the time-limited approach with spread and clean discounting seems the most appropriate option to create an ESTER derivatives market whilst reducing the risk of abrupt termination. This could be reached only as long as all the participants play the game in good faith. Vigilance is needed regarding the risk pointed out by the working group of a creation of an EONIA-related instruments parallel market for non-EU participants not subject to BMR. This approach would also reduce value transfer thanks to the use of the spread.

We agree with the working group as regards clean discounting based on ESTER. This seems to be the best option to avoid market fragmentation and the best incentive for market participants to move from EONIA curve to ESTER curve.

3. Do you agree that a publication deadline for the recalibrated EONIA of end-2021 is sufficient for a smooth transition under the recalibration approach with spread and clean discounting path? (Yes/No/No opinion)

Yes

4. Do you have any other ideas to accelerate the transition of the derivatives market to ESTER? (Yes/No)

Yes

Please elaborate.

We think that in addition to a publication deadline for the recalibrated EONIA of end-2021, the plan should schedule an assessment at end-2020 of the state of play of the transition from EONIA to ESTER. Depending on the results of this assessment, public authorities should be empowered to take appropriate measures, such as the extension of the transition period for the recalibrated EONIA.

5. Do you see any benefit in the new recalibrated EONIA to be authorised and supervised until its publication deadline? (Yes/No)

Yes

Please elaborate.

Authorisation and supervision of the new recalibrated EONIA are critical in our point of view to ensure a continuity for contracts and funds referencing EONIA. This is an essential step for a smooth transition as this should reduce the litigation risk emerging from the move to the new EONIA. As stated in question 2, the switch to the recalibrated EONIA shall be accompanied by intense communication from public authorities and the recalibrated EONIA administrator. Asset managers shall not have to notify each unit or shareholders of funds referencing EONIA.

6. Do you agree with a spread methodology based on a 1-year pre-ESTER historical data period, calculated as an average with a 15% trimming? (Yes/No/No opinion)

Yes

Please elaborate.

We agree with the one-year Pre-ESTER observation period to get an accurate view of the banks' short-term refinancing conditions. It is simple to understand and to implement, while allowing to exclude outliers thanks to the trimming mechanism. That said, the period between December 2017 and March 2018 should not be taken into account in our views since the spread increased noticeably.

7. If not, what would be your preferred option and why? (Please choose from the other options presented in the report)

8. How much time do you think would be the minimum to make your systems ready for ESTER T+1 publication? (Number of months)

20

Please provide the reasons for your time estimation.

As stated in the WG report, asset managers are particularly concerned with the ESTER T+1 publication, first with regards to MMFs whose success is due mainly to same day settlement. The AFG had the occasion to ask the ECB for an earlier publication of the ESTER in its response to the previous consultation. If this option is not considered by the ECB, then we estimate that the valuation process, the risk management and documentation will be impacted by a T+1 publication.

This transition implies new IT developments in our members' systems which are carried out through specific projects. These projects require approvals of all the different departments impacted by the project, not to mention the various steps of setting-up a team, assessing the needs, selecting external providers and implementing the solution. This takes at least 20 months.

Our members would also like some clarification on the following. EONIA is currently published on T and is used on T+1. With the publication of the recalibrated EONIA on T+1, in the light of the lines just above, our members are likely to be confronted to operational issues once the recalibrated EONIA will be published. Furthermore, the difference of the time of publication between EONIA and the recalibrated EONIA may induce litigation risks for existing contracts. What is the view of the Working Group on these points?