



## MEMORANDUM

ICMA ERCC Committee

Repo market best practice with respect to the transition from EONIA to €STR

July 2, 2019

---

### Background

On March 14 2019, the ECB supported private sector Working Group on euro risk-free rates published [recommendations](#) on transitioning from the euro overnight index average (EONIA) to the euro short-term rate (€STR). The Working Group's recommendations include the following:

- (i) market participants should gradually replace EONIA with €STR for all products and contracts, making €STR their standard reference rate once the period of transitioning to the €STR ends at the end of 2021;
- (ii) EONIA's administrator, the European Money Markets Institute, should modify the current EONIA methodology to become €STR (plus a spread)<sup>1</sup> for a limited period of time, allowing market participants sufficient time to transition to €STR; and
- (iii) market participants should make all reasonable efforts to replace EONIA with €STR as a basis for collateral interest for both legacy and new trades with each participant's counterparties (clean discounting).

The ECB further [announced](#) that it will start publishing the €STR as of October 2 2019, reflecting the trading activity of October 1 2019.<sup>2</sup> Additionally, the ECB is ready further to support private sector efforts in the transition away from the euro overnight index average EONIA and will provide the computation of a one-off spread between the €STR and EONIA, which was requested by the Working Group on Euro Risk-Free Rates. This [spread](#) (published on May 31 2019) has been calculated by the ECB according to the methodology publicly recommended by the Working Group on Euro Risk-Free Rates.

Perhaps the most significant consideration from a repo market perspective, in the case of EONIA-based transactions, is the timing of the publication of €STR. Unlike the publication of EONIA today,<sup>3</sup> €STR will only be published the following day of the contributing transactions (no later than 09:00 CET).<sup>4</sup> This is because the MMSR Regulation specifies that data shall be transmitted once per day to the ECB between 18:00 CET on the trade date and 07:00 CET on the first TARGET2 settlement day after the trade date. The complete dataset is therefore only available for the computation of the €STR after 07:00 CET on the following TARGET2 day. There is a provision for the rate to be amended up until 11:00 CET in the event of an error.

---

<sup>1</sup> On May 31 2019 the ECB [confirmed](#) that this spread will be 0.085%

<sup>2</sup> Note that this means that there will be no published rate on October 1 2019.

<sup>3</sup> Currently EONIA is published on the same day, between 18:45 and 19:00 CET.

<sup>4</sup> EONIA, represented by €STR + the calculated spread, will be published by EMMI by 9:15 CET.

This ‘T+1’ publication creates potential challenges for transacting and settling €STR-based repo, since the final rate to be applied in calculating the final repo interest will not be known until the actual repurchase date, which may be too late to send settlement instructions to the (I)CSD in time for settlement

It should also be noted that the use of EONIA-based repo is largely limited to transactions in French government securities.<sup>5</sup> According to the most recent ICMA ERCC European Repo Market Survey (December 2018), the floating-rate repo portion of the overall market is 13.1%.

#### Recommendation for market best practice

The practicalities of the EONIA/€STR transition for non-cleared repo market have been discussed at length by the ICMA ERCC and the ERCC Operations Group. The ERCC has agreed on the following recommended best practice to be followed from October 1 2019:

- The Interbank market should transact purely on a fixed-rate basis (“classic repo”) and should no longer use floating rate repo.
- In the case of non-interbank transactions (such as dealer-to-client), where firms agree to transact on a floating-rate basis (using EONIA or €STR), best practice will be to apply the fixing of the penultimate accrual date of the transaction to the final (repurchase) date (i.e. “crystalizing” the penultimate fixing into a fixed rate for the final business day). This will allow for parties to send timely settlement instructions for the repurchase leg of the transaction.
- Where parties transact on a floating basis, using the crystallization methodology, this will create discrepancies between the repurchase price calculated and settled by the parties and the repurchase price that would have applied had it been possible to instruct after the final fixing. In this instance, the disadvantaged party can elect to claim the differential from the advantaged party, so long as the differential is equal to or greater than an agreed threshold per transaction (the exact amount to be determined by the ERCC in the coming weeks following further discussion).
- Any claim should be made immediately (ideally on the repurchase date, once the final fixing is known), and any reimbursement should be made on the business day following the repurchase date. Ideally, any claims or reimbursement made with respect to the same day should be made in aggregate. In any event, any claims or reimbursements should be made no later than 30 days after the repurchase date.

It should be noted that the recommended best practice for floating-rate (EONIA or €STR) repo is largely similar to current market best practice for overnight-index (OI) based repo in the event that the

---

<sup>5</sup> This is very much a legacy, market specific practice that pre-dates the introduction of the euro.

publication of the OI fixing is too late to send settlement instructions to the (I)CSD in time for settlement.<sup>6</sup>

### Other considerations

#### *Averaging vs compounding*

Currently, market practice for EONIA-based repo is to apply the average rate over the life of the trade, rather than compounding, even though daily compounding is used in the EONIA swap market. The ERCC agreed that this practice should continue in the case EONIA or €STR repo, noting that it is also possible for parties to agree to a compounding methodology.

#### *Reference to EONIA in GMRA annexes*

While none of the GMRAAs reference EONIA, it is understood that some bilaterally negotiated annexes may make reference to EONIA with respect to interest payable on cash collateral. Where this is the case, firms will need to update these bilateral annexes to reference a suitable alternative benchmark. While ICMA cannot do anything directly to assist firms in identifying or updating any bilateral contractual arrangements that may be impacted, in coordination with the ERCC it will look to raise awareness of the issue so that affected firms can take the steps necessary to prepare for the discontinuation of EONIA.

---

<sup>6</sup> See paragraphs 2.72, 2.73, and 2.76 of the [ERCC Guide to Best Practice in the European Repo Market](#)

### About the ERCC

The ICMA European Repo Council (ERC) was established in December 1999, to represent the cross-border repo market in Europe. In 2015, the ERC's name was changed to European Repo and Collateral Council (ERCC) in recognition of the increasingly intimate relationship between repo and collateral and the group's substantial focus on collateral.

The ICMA ERCC is today the main industry representative body for repo and collateral markets, developing consensus solutions for issues arising in a rapidly evolving marketplace and consolidating and codifying best market practice. The Council also plays a significant role in nurturing the development of the repo market and supporting its wider use in Europe and globally by providing educational courses and market information, such as the bi-annual survey of the European repo market which has become established over the past two decades as the authoritative indicator of market size and structure and the dominant trends.

The ICMA ERCC Committee is the governing board of the ERCC which is elected on an annual basis by all ERCC member firms.

Membership of the ERCC is open to ICMA members who transact repo and associated collateral business in Europe. The ICMA ERCC currently has around 100 members, comprising the majority of firms actively involved in this market.

For more information on the ICMA ERCC [download the ERCC brochure](#) or contact [ercc@icmagroup.org](mailto:ercc@icmagroup.org)