

## **Benoît Cœuré: Reforming financial sector benchmarks**

Welcome remarks by Mr Benoît Cœuré, Member of the Executive Board of the European Central Bank, at the annual meeting of the Money Market Contact Group, Frankfurt am Main, 27 September 2016.

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Ladies and gentlemen,

I am pleased to be with you and very much appreciate having an opportunity to discuss with you issues of importance to the money market.

There is a topic that in the last few years has drawn the attention of regulators, of legislators, of market participants but also of the general public, namely financial benchmarks.

I hardly need to convince any of you of the relevance of benchmarks such as EURIBOR, LIBOR or EONIA. Indeed, I only need to quote the European Commission, which recently declared EURIBOR to be a “critical” benchmark in the light of the vast number of contracts which use it as a reference – more than €180 trillion of derivatives contracts and more than €1 trillion of retail mortgages.

Indeed, benchmarks have over the years become an essential part of the infrastructure of our economy. They are indices that are used to determine the level of payment in a financial contract, whereby neither party to the contract has any control over their setting. Their value and their credibility are derived from the fact that they are considered impartial, representative, and therefore fair. If the impartiality of a benchmark is compromised, confidence in any contractual relationship based on that benchmark will be, as a result, seriously undermined.

Therefore, following the scandals involving some of the biggest benchmarks, regulators and legislators, in coordination with private sector, identified market shortcomings and designed a framework that would guarantee the integrity of reference rates.

And a lot has been achieved so far:

1. The private sector has played an important role in improving the benchmark-setting process by designing new codes of conduct, by enhancing transparency and visibility, by launching private initiatives reflecting market needs, and by identifying alternative benchmarks.
2. The public sector has contributed to this process as well. Since 2013 the FSB and the International Organization of Securities Commissions have worked to reform benchmarks, supporting and steering the efforts of private market participants to define more robust and reliable benchmarks and related “best practices”. In addition, the public sector has adopted a dedicated regulation.

As benchmarks are an important part of the global financial system and an essential tool in the transmission mechanism of monetary policy, they matter to the ECB as well. We have been committed to improving the relevant benchmarks for the euro, as have other central banks in respect of their currencies.

While the ECB has always stressed that financial benchmarks should be private initiatives tailored to private needs, we have also helped the private sector by shaping some of the benchmark reform initiatives. For example, we have been following closely the reform of EURIBOR from a quote-based to a transaction-based index. Moreover, together with the EURIBOR administrator, we launched a data collection back in 2013 to analyse the feasibility of transaction-based alternatives. And indeed it was this group, the Money Market Contact Group that was asked to participate to at least 100%. And you delivered.

The EURIBOR reform has now reached an important stage. The transition to the transaction-based methodology is foreseen for 2017 and the administrator is planning a pre-live verification exercise to ascertain the feasibility of the proposed methodology under current market conditions. For the pre-live verification – and eventually for the EURIBOR reform – to be a success, broad market representation has to be achieved. Therefore, not only should current panel members participate but also other banks in the euro money market.

A lack of participants might seriously threaten the completion of the pre-live verification and ultimately the reference rate itself. Therefore, in view of the tremendous importance of benchmarks such as EURIBOR, the ECB would like to see banks take responsibility for the benchmark in two ways. Firstly, by participating in the pre-live verification and secondly, by eventually joining the panel of contributors to EURIBOR with the launch of the new calculation methodology.

Banks are among the biggest users of EURIBOR. As such, they would also incur the biggest costs and losses if it came to an abrupt end. It is therefore up to the banking industry as a whole to support this benchmark. But the burden cannot only be shouldered by the current panel banks, which have indeed shown their sense of responsibility. Despite the related costs and perceived risks, they have remained in the panel and helped to prevent any disorderly dismantling of EURIBOR.

But there are other examples. In some cases, banks that are among the largest institutions in their jurisdiction, and therefore rely hugely on the benchmark to price their products, have chosen to leave the panel. This is a worrisome development.

Some members left because of the perceived elevated risks related to the usage of expert judgement while contributing to EURIBOR. Since their departure, however, there have been a couple of important changes. Firstly, a new regulation has been adopted in Europe, establishing rules guiding the process of setting a benchmark and therefore contributing to greater regulatory certainty. Secondly, the envisaged reform of EURIBOR, aimed at anchoring the benchmark in transactions, will eventually remove the expert judgement and therefore the subjective element in contributing to EURIBOR.

Some banks also saw as an impediment for their participation in the envisaged transaction-based index the costs they will incur for transaction reporting. But the incremental costs for joining the EURIBOR pre-live verification and for contributing to a benchmark with transaction data may actually be limited for those banks, which already report under the ECB Money Market Statistical Reporting Regulation. This is because these banks have already set up systems in order to extract and report transaction data.

In conclusion, I hope that banks will indeed take the opportunity to create better, more robust and representative benchmarks, which will better suit the needs of end users.

And I also hope that banks will continue to participate in the panel – or decide to join or re-join it – so as to ensure that EURIBOR as well as the other reference rates continue to play their critical role in the European economy.

Thank you.