JONES DAY

COMMENTARY

MARCH 2019

IN SHORT

The Situation: The updating of the Euro Interbank Offer Rate ("Euribor") to align it with the EU Benchmark Regulation 2016/1011 ("EU BMR") is in full swing. Under the EU BMR, only EU and third country BMR compliant benchmarks may be used by supervised users in new financial instruments or financial contracts as of January 1, 2020 (or any other extension to the transitional deadline to be granted by the EU Parliament and the Council, the "Extension").

The Result: The European Money Markets Institute ("EMMI"), the administrator of Euribor, recently published stakeholder feedback on its consultation on a hybrid methodology for Euribor and a blueprint for the methodology underlying the determination of Euribor.

Looking Ahead: In Q2 2019, EMMI will file for authorization of a new hybrid Euribor with the Belgian Financial Services and Markets Authority and then start transitioning panel banks to the hybrid methodology before the end of 2019.

EMMI is reforming Euribor because the EU BMR and international guidelines require benchmarks to be based on a robust calculation methodology using arm's length transactions when possible to meet the underlying interest (market economic reality) that Euribor covers, which conditions are likely not to be satisfied by the current quote-based methodology used by EMMI.

In October 2018, EMMI issued a Second Consultation Paper ("CP") on a hybrid methodology that could be used to measure Euribor's underlying interest (i.e., the borrowing rate at which funds can be obtained by credit institutions). The CP, which presented its findings after a testing phase, is part of EMMI's overall commitment to deliver a reformed and robust methodology for Euribor. While a quote-based methodology is currently used for Euribor, the proposed methodology is called "hybrid" because it would rely on both real transaction data (whenever available) and other related market pricing sources reflecting the average rate of borrowing by the panel banks over the preceding TARGET day (when necessary).

The hybrid Euribor determination methodology follows a hierarchical approach. Each day, each panel bank's contribution, for each defined tenor, will be determined on the basis of one of three levels, depending on the volume and type of underlying transactions that such panel bank has undertaken over the reference period:

- Level 1 contributions are based solely on eligible transactions in the underlying interest at the defined tenor (i.e., one week, one month, three months, six months, and 12 months), subject to agreed maturity date windows;

- Level 2 contributions are based on transactions from panel banks across the money market maturity spectrum, using a defined range of formulaic calculation techniques supported by linear interpolations of Level 1 contributions for adjacent tenors, transactions at nondefined tenors, or transactions from prior dates; and

- Level 3 contributions are based on an appreciation of the funding cost for the panel banks using as proxies transactions in the underlying interest and/or other data from a range of markets closely related to the unsecured euro money market (including futures, FRAs or OIS), using modelling techniques and/or the panel bank's judgment.

> While a quote-based methodology is currently used for Euribor, EMMI proposes a determination methodology to measure the underlying interest (i.e., the borrowing rate at which funds can be obtained by credit institutions).

On February 12, 2019, EMMI published a summary of the stakeholder feedback received from a range of respondents during the consultation period. Key aspects of the market participants' feedback on the proposed hybrid methodology focused on:

- The aggregated anonymized indicators to be published by EMMI upon implementation of the hybrid methodology as part of a transparent Euribor determination process;
- The eligibility criteria for contributors' transactions to be considered as input for Level 1 contributions: in particular, eligible transactions should exclude transactions with nonfinancial corporate counterparties and transactions whose amount is less than €20 million but could include floating rate trades against the unsecured euro overnight interest rate;
- Some of the calibration parameters of the second level of the hybrid methodology.

Pursuant to EU Benchmark Regulation (“BMR”), benchmarks that do not meet the requirements provided by BMR cannot be used after 1 January 2020 (or, after any Extension).

THREE KEY TAKEAWAYS

1. Market participants contributed to the significant progress to establish a new hybrid methodology for determining Euribor after January 1, 2020 (or, after any Extension), in line with EU BMR.
2. It remains unclear whether, without any further action, a new hybrid Euribor will simply replace the existing Euribor and, from January 1, 2020, onwards (or, after any Extension), reference in existing transaction documents to EURIBOR would actually refer to the new hybrid Euribor.
3. Market participants need to monitor the developments in this space and prepare for an outcome where there is no automatic replacement mechanism if the existing Euribor becomes unavailable on January 1, 2020 (or, after any Extension), and if the new Hybrid Euribor is considered a completely new benchmark.


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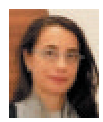
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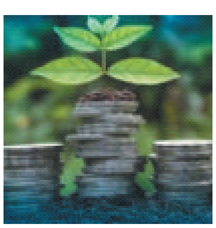
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