

LSEG Response to Bank of England Consultation on a new sterling money market data collection and the reform of SONIA

Background Information

London Stock Exchange Group plc (LSEG) is a financial market infrastructure provider, headquartered in London, with significant operations in Europe and North America.

LSEG operates a range of international equity, fixed income and derivatives markets, including: London Stock Exchange; Borsa Italiana; MTS Group and Turquoise; post-trade and risk management, including Cassa di Compensazione e Garanzia (CC&G), the EMIR authorised CCP; Monte Titoli, the Italian CSD; and globeSettle, a new CSD based in Luxembourg; and is majority owner of the multi-asset global CCP, LCH.Clearnet Group serving major international exchanges and platforms, as well as a range of OTC markets (with EMIR authorised CCPs in France and the UK). LSEG operates the EMIR authorised trade repository UnaVista, and offers a range of real-time and reference data products, as well as access to international equity, bond and alternative asset class indices, through the leading index providers, FTSE International Ltd and Frank Russell Company.

We have responded only to those questions which relate to the potential risk management impact on CCP operations regarding the proposed reforms to SONIA with some additional high level commentary. We have not responded to questions in section 1 of the consultation as CCPs are not covered by the data reporting regime envisaged in part 1.

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RESPONSE TO QUESTIONS

Part 3: Reform of Sonia

Q20) The Bank anticipates that publication of the reformed SONIA would be moved to 09.00 on the day after that to which the rate pertains. What problems, if any, might this create?

- **There will be a direct impact on the ability to calculate coupon amounts in sterling OIS cleared by LCH.Clearnet, leading to a risk of delay in the settlement of swap amounts.** The proposed change would represent a change to market conventions and LCH.Clearnet would want to consult with market participants as to whether they agreed with such a change and were willing to accept the accompanying delays to settlement cycles. LCH already clears US dollar denominated OIS, accommodating the publication lag set by the FRBNY, with a corresponding payment lag by market convention. There are two potential efficiency impacts:
 - I. **Payment efficiency:** A later publication time than used at present could impact the timing of the payments. It could mean either OIS payments are delayed or that extraneous cash payments would be necessary to readjust for changes in the rate from the settled amount based on an assumed rate. LCH.Clearnet expects more transactions to be cleared and expect increasing pressure to improve settlement speed, so the impact of this risk could be magnified as the industry transitions to central clearing.
 - II. **Price Alignment Interest (PAI) adjustments:** SONIA is used as the PAI rate, which is the interest rate at which cash collateral is compensated and by extension the discount rate for sterling transactions. The proposed delay to SONIA publication would lead either to delays or adjustments (meaning more transactions), both of which could impair efficiency.
- **We believe the Bank should only consider delaying the publication time once it has exhausted all avenues available for achieving its objective of broadening the number of transactions underpinning SONIA whilst maintaining the current publication schedule.** If a small number of transactions are excluded from the calculation of the rate because the data cannot be submitted on time, this may not necessarily be material for the calculation when the number of data inputs has increased significantly.

Q21) Does the outline timetable proposed for the reform of SONIA present you with any problems?

- **LSEG appreciate the desire to implement the reforms as soon as is practicable in early 2017, however the Bank should be mindful of other significant industry wide initiatives being implemented around a similar time, notably MiFID II / MiFIR.** Banks and other market participants may on account of these other initiatives therefore face significant operational and capacity challenges at the same time as the Bank seeks to implement the reform of SONIA. We therefore believe the second half of 2017 would be a more prudent timescale.

Q22) Are there any additional comments or feedback on the Bank's high level plans for the reform of SONIA you would like to contribute?

- **LSEG welcomes the Bank's work in reforming SONIA.** We make two high level points for the Bank to consider at this stage in the process:
 - I. **The Bank should remain mindful of concerns over “frustration of contract” when reforming benchmarks.** In respect of existing contracts, the implementation of methodological or other significant changes to SONIA, including systematic bias to the level of SONIA, gives rise to a degree of legal uncertainty and risk. There is a risk that parties to the contract may assert that performance under the contract had been frustrated on account of the obligations under the contract being very different to the obligations undertaken at the time of entry of the contract. For example, a clearing member disadvantaged by a systematic bias is more likely to challenge the validity of the contract, thereby threatening the CCP's matched book. Separately market participants will need to consider including appropriate fallback provisions in existing contracts referencing SONIA in anticipation of changes to SONIA/the administrator of SONIA.
 - II. **Broadening the population of data reporters may not necessarily lead to a more robust and representative rate.** Whilst in theory a larger and more diverse sample of data reporters should lead to a richer picture of activity in the sterling money market, in practice some participants are active only at certain times in the market and may cause undue short term movements in SONIA which are inconsistent with a drive to make it a more robust long term benchmark indicator of risk free interest rates. There is the potential for a stressed event or even a simply calendar event in particular sector of contributors causing an undue change in reported prices. Such a phenomenon is already present for example in the setting of EONIA, when the German Landesbanks participate on a day which is a bank holiday in other parts of Europe.