



ICE Swap Rate based on SONIA - Consultation feedback

June 16, 2020



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Executive Summary

ICE Swap Rate™ (ISR) is recognised as the principal global benchmark for swap rates and spreads for interest rate swaps. ICE Swap Rate is used as the exercise value for cash-settled swaptions, for close-out payments on early terminations of interest rate swaps, for some floating rate bonds and for valuing portfolios of interest rate swaps.

It represents the mid-price for interest rate swaps (the fixed leg) and swap spreads (the applicable mid-price minus a corresponding specified government bond yield), in USD, GBP and EUR in various tenors at particular times of the day. The floating leg is [ICE LIBOR](#) (LIBOR™) for USD and GBP and [EURIBOR®](#) for EUR.

In January 2020, ICE Benchmark Administration Limited (IBA) published a [Consultation](#) on specific aspects of the implementation of ISR GBP rates based on SONIA in light of the growing volumes in SONIA Swaps. IBA subsequently updated the paper and extended the consultation period in two steps to May 22, 2020.

IBA is very grateful for the feedback received.

All respondents were supportive of IBA's proposed introduction of ISR GBP SONIA rates and a summary of the comments received is included in this paper.

The main feedback points were that ISR GBP SONIA rates should be introduced as soon as possible, and by no later than the end of 2021, using:

- The same Waterfall Methodology as for ISR GBP LIBOR rates;
- The same tenors as for ISR GBP LIBOR rates; and
- The SONIA Swap conventions: Actual / 365 day count and Overnight (O/N) SONIA compounded annually; and
- The existing collection window, publication days and publication times for ISR GBP LIBOR rates.

In conjunction with the ICE Swap Rate Oversight Committee, IBA will work on the introduction of ISR GBP SONIA rates and will announce in the coming months when the new rates will be made available.

IBA is planning to introduce ISR GBP SONIA rates on a test basis in advance of their being made available by IBA as benchmarks to be used in financial instruments and financial contracts or to measure the performance of investment funds.



Proposed ISR GBP SONIA rates

Introduction

ICE Swap Rate (ISR) is recognised as the principal global benchmark for swap rates and spreads for interest rate swaps. It represents the mid-price for interest rate swaps and spreads (the fixed leg), at particular times of the day in three major currencies (USD, GBP and EUR) and in tenors ranging from 1 year to 30 years. The floating leg is 3M ICE LIBOR (LIBOR™) for USD, 3M and 6M LIBOR for GBP, and 3M and 6M EURIBOR® for EUR.

ISR is used as the exercise value for cash-settled swaptions, for close-out payments on early terminations of interest rate swaps, for some floating rate bonds and for valuing portfolios of interest rate swaps.

The movement away from GBP LIBOR™ to SONIA is expected to lead over time to diminishing volume in the existing ISR GBP benchmark as the transition progresses and as the demand for SONIA-based swaps increases.

IBA is looking to introduce a suite of ISR tenors with SONIA as the floating leg. This will be done alongside the existing GBP LIBOR™-based benchmark for as long as necessary and/or possible.

In the recent [Consultation](#), IBA sought feedback on aspects of the introduction of ISR GBP SONIA rates, as set out below.

Methodology

In the Consultation, IBA asked for feedback as to whether the same waterfall approach should be used for ISR GBP SONIA as for ISR GBP LIBOR, which is summarised below:

- Each published ISR benchmark rate is calculated using eligible prices and volumes for specified interest rate derivative products, provided by trading venues in accordance with a “Waterfall” [Methodology](#);
- The first level of the Waterfall (“Level 1”) uses eligible, executable prices and volumes provided by regulated, electronic, trading venues;
- If these trading venues do not provide sufficient eligible input data to calculate a rate in accordance with Level 1 of the Methodology, then the second level of the Waterfall (“Level 2”) uses eligible dealer to client prices and volumes displayed electronically by trading venues;
- If there is insufficient eligible input data to calculate a rate in accordance with Level 2 of the Methodology, then the third level of the Waterfall (“Level 3”) uses movement interpolation, where possible for applicable tenors, to calculate a rate; and
- Where it is not possible to calculate an ISR benchmark rate at Level 1, Level 2 or Level 3 of the Waterfall, then the [Insufficient Data Policy](#) applies for that rate.

All but one respondent agreed with using the current Waterfall Methodology for ISR GBR SONIA rates.

The firm which disagreed favoured combining Central Limit Order Book (CLOB), Dealer to Client (D2C) and Request For Quote (RFQ) data at all times.

Tenors

In the Consultation, IBA asked whether ISR GBP SONIA should be published in the same tenors as ISR GBP Rates 1100, which are 1 year (1Y); 2Y; 3Y; 4Y; 5Y; 6Y; 7Y; 8Y; 9Y; 10Y; 12Y; 15Y; 20Y; 25Y and 30Y.



Respondents were unanimous in agreeing that IBA should publish ISR GBP SONIA in at least the same tenors as ISR GBP Rates 1100.

Some respondents recommended publication of additional tenors, as follows:

- 40Y and 50Y were suggested by two respondents;
- 3M and 6M by one respondent; and
- 1M, 3M, 6M, 12M, 18M, 40Y and 50Y by one respondent.

IBA will consider publication of the 18M, 40Y and 50Y tenors, but not the short tenors which should be covered by Term SONIA Reference Rates (TSRR).

Day counts and interest rate basis

Market participants were asked about the day counts and interest rate basis that should be used for the underlying interest rate swaps for ISR GBP SONIA.

The consensus was that the SONIA Swap conventions should be used: Actual / 365 day count and Overnight (O/N) SONIA compounded annually.

Publication time and days

Market participants were asked whether they agreed that ISR GBP SONIA should be based on a collection window from 10:58 to 11:00 London time, which is the same as for the existing ISR GBP. Respondents were unanimous in their agreement.

One respondent said that it would also be comfortable with a shorter data collection window if the methodology included broader liquidity (such as in the Waterfall Methodology which was recently introduced by IBA). Another respondent suggested a wider window in times of low CLOB liquidity.

IBA proposed that the GBP SONIA-based benchmark should be published on all London business days (and not on bank holidays in England and Wales - see <https://www.gov.uk/bank-holidays>). Respondents were unanimous in their agreement.

Implementation

Market participants were asked to suggest when IBA should introduce ISR GBP SONIA.

Almost all respondents supported introduction of ISR GBP SONIA rates as soon as possible. One respondent considered that implementation should be delayed due to the Covid-19 implementation.

The rationale for early introduction included that it would be a pre-requisite for significant volumes of SONIA swaption trading, that it would help build liquidity in SONIA swaption trading and that it would facilitate the transition away from LIBOR™.

General Feedback

IBA also welcomed more general feedback. Additional comments included suggestions that IBA should:

- Specify the clearing house choice as part of the input data specification;
- Combine Term SONIA Reference Rates (TSRR) with SONIA-based ISR; and
- As well as providing clarity on its commitment to publishing ICE SONIA Swap Rates, provide clarity as soon as possible on its intentions with regard to other Risk Free Rates (RFRs).



Publication of Completed Questionnaires

IBA stated that it would publish completed questionnaire unless confidentiality was requested. All respondents requested confidentiality in respect of their completed questionnaires, other than as part of aggregated feedback.



Next Steps

IBA is very grateful for the stakeholder feedback and will consider all of the feedback and suggestions in conjunction with the ICE Swap Rate Oversight Committee.

IBA will announce in the coming months when the new rates will be made available.

IBA intends to introduce ISR GBP SONIA rates on a test basis in advance of their being made available by IBA as benchmarks to be used in financial instruments and financial contracts or to measure the performance of investment funds.

IBA will also closely monitor the liquidity in other RFRs and assess the potential for a similar implementation in due course for other currencies.

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