THE EUROPEAN ASSOCIATION OF CORPORATE TREASURERS

18 February 2019,

Third country benchmarks and EU non-financial corporates' ability to hedge
Extension of transitional provision of the Benchmarks Regulation for third country benchmarks

EACT fully supports the objectives of the European Benchmark Regulation (BMR) to build reliable and transparent indices for financial transactions – indeed as corporate treasurers, the integrity of the benchmarks we use is paramount.

We are however concerned that corporate treasurers' ability to hedge their FX risks could be negatively impacted if a number of 3rd country benchmarks can no longer be used by EU counterparties by 31 December 2019 – given those 3rd country Benchmark administrators are not on the path to be recognised as equivalent in that timeframe.

Expected impact on EU corporates

Should the transitional period for the use of third country benchmarks not be extended (i.e. aligning it to what is planned for EU critical benchmarks)– a detrimental impact would be felt for corporates with global activities hedging the following foreign currencies : Indian Rupee INR, Chinese Renminbi CNY, Korean Won KRW, Russian Rubble RUB, Nigerian Naira NGN, Brazilian Real BRL, Argentine Peso ARE, Philippine Peso PHP, Taiwan Dollar TWD, Indonesian Rupiah IDR.

Whilst it may represent rather small volumes in comparison to the global FX market, the actual impact on each European company with some business exposures and/or investments planned in those countries will be important.

Indeed, as these currencies are not fully deliverable, corporate exposures to these currencies are hedged with "non-deliverable forwards" (NDFs) whose price settles according to a reference quote.

It is our understanding that the administrators of most of these reference quotes will not try to obtain equivalence with IOSCO principles in the near future and would therefore not be eligible for recognition, endorsement or equivalence via the EU BMR's third country framework by the 31 December 2019.

If European corporates are no longer able to refer to those 3rd country reference quotes, it will lead to a reduction of the liquidity and added transaction costs for some of the products used by non-financial corporations to hedge their exposures to foreign exchange risks. This worsened liquidity and higher transactions costs will be the results of:

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- EU corporates no longer being able to transact NDFs on multilateral trading facilities and being forced to revert to the bilateral OTC space; and
- Even if bilateral trading were possible, the current marked-standard benchmark might be deemed non-compliant and market participants could be forced to use bilateral references, which would comply with significantly lower transparency standards. This would – in our view – run contrary to global efforts to bring more transparency to financial indices for the benefits of the end-users.

Suggested way forward

In light of this anticipated impact on non-financial corporates, we would suggest the current transitional period for third country benchmarks to also be extended by a period of two years until 31 December 2021.

We would be happy to provide further details on this issue if it could be useful in the context of the ongoing trilogue discussions on low-carbon benchmarks.

Yours sincerely,

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Chair
European Association of Corporate Treasurers

As background, the EACT brings together 13 000 treasury professionals active in 21 countries and working for around 6500 individual companies. Corporate treasurers are the finance professionals of the real economy.

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