P O Box 427 Pretoria 0001 South Africa
370 Helen Joseph Street Pretoria 0002
+27 12 313 3911 / 0861 12 7272
www.resbank.co.za

SOUTH AFRICAN RESERVE BANK

File ref. no.: 11/26/18/1

Financial Markets Department

Minutes of the meeting of the Market Practitioners Group on Interest Rate Benchmark Reforms (MPG) held via MS Teams on Tuesday, 6 August 2024 at 09:00

Minutes No. 03/2024

Present:

R Cassim	Chairperson – Deputy Governor of the SARB
P Mjandana	SARB – DG Cassim's Office
J Mol	Association of Corporate Treasurers of Southern Africa (ACTSA)
R Roux	SARB: Chair – Data Collection and Infrastructure Workstream
Z Parker	SARB: Chair – Communications Workstream
A Du Toit	Chair - Risk-free and Term Reference Rates Workstream
R Klotnick	Chair – Derivatives Workstream
E Hamman	Chair - Governance and Regulatory Issues Workstream
P Burgoyne	Chair – Transition Workstream
K Tulsi	Chair – Accounting and Tax Workstream
P Mananga	SARB Prudential Authority
O Makhubela	Financial Sector Conduct Authority (FSCA)
M Phungo	Secretariat – SARB Financial Markets Department

In attendance:

B Maronoti	SARB Financial Markets Department
Z Gininda	SARB Financial Markets Department
N Hoosenmia	SARB Financial Markets Department

By invitation:

M Vilakazi	Legal Workstream member

Apologies:

G Haylett	Banking Association of South Africa
G Raine	Association for Savings and Investment South Africa (ASISA)
M Shongwe	SARB: Chair – Legal Workstream

1. **Welcome**

1.1 The Chairperson welcomed members to the third meeting of the Market Practitioners Group on Interest Rate Benchmark Reforms (MPG or Committee) in 2024.

1.2 There being a quorum present, the meeting was duly constituted.

2. **Adoption of the agenda**

2.1 The agenda was adopted as proposed, with no amendments.

3. **Confirmation of the Anti-Competitive Statement**

3.1 The Anti-Competitive Statement was noted and accepted by all members and attendees present.

4. **Approval of Minutes No. 2/2024 of the meeting held on 4 June 2024**

4.1 The minutes of the meeting held on 4 June 2024 were accepted as a true reflection of the deliberations and were approved for signature by the Chairperson.

4.2 The signed minutes would be published on the MPG page on the SARB website.

5. **Consultation on market convention for nonlinear ZARONIA-based derivatives**

5.1 Mr Klotnick indicated that the Derivatives Workstream (DWS) had finalised the white paper on market conventions for nonlinear ZARONIA-based derivatives. The paper had been reviewed by the DWS members, the International Swaps and Derivatives Association (ISDA) and traders active in the derivatives market. Members were requested to review and comment on the paper, after which it would be published as a consultation paper to solicit comments from market practitioners.

6. **Regulatory instruments to deal with tough legacy contracts**

6.1 Ms Hamman reported that, following the legal opinion of an independent senior legal counsel, safe harbour provisions would need to be housed in primary legislation. There were concerns raised regarding the process to include provisions in primary legislation as it tended to be lengthy process, and thus, it would negatively affect the Jibar transition timeline.

6.2 It was suggested that the FSCA could potentially include safe harbour provisions as part of its work on the Conduct of Financial Institutions (COFI) bill. However, the primary drawback of the COFI bill was its extensive scope, which could potentially delay consequential amendments if issues arose. An alternative option would be to process a separate bill for safe harbour provisions. The FSCA would discuss this internally to determine the best course of action

7. **Credit adjustment spread**

7.1 Mr Burgoyne presented the options for calculating the credit adjustment spread, which the Transition Planning and Coordination Workstream (TPCW) had considered for use in defining Jibar fallback arrangements. The workstream had settled on recommending ISDA's historical mean/median approach. However, they had not decided on whether the mean or the median of 5-year historical spreads between Jibar and respective ZARONIA compounded in arrears approach would be the most appropriate for South Africa. Adopting the mean approach would account for shifts in the interest rate regime and structural changes. The median approach would be more robust to outliers; however, it would not account for the idiosyncratic factors that were unique to South African markets. The five-year historical period considered in the analysis captured both periods of higher and lower spreads, thereby satisfying a broad spectrum of participants.

7.2 It was clear the SARB's migration to the surplus system for implementing monetary policy, the use of Gold and Foreign Exchange Contingency Reserve Account (GFECRA) funds, and the SARB's policy rate adjustments had affected the behaviour of spread. As such, it was preferable to adopt the mean as it would incorporate all these idiosyncratic factors, unlike the median which would treat them as outliers and exclude them completely. Nonetheless, using the mean would be a departure from the methodology applied in most jurisdictions. The workstream would engage ISDA and Bloomberg to determine whether they would consider this minor deviation, such that they would continue to include the credit adjustment spread so determined in the definition of the fallback for Jibar in the ISDA protocol and publish indicative credit adjustment spreads on Bloomberg.

7.3 Members considered the risks related to forfeiting the use of the ISDA protocol. While it was theoretically possible to renegotiate contracts bilaterally without relying on the protocol, the Legal Workstream argued that renegotiating all Jibar legacy contracts without a fallback protocol would be impractical. It was argued that the protocol allowed for bulk amendments of contracts, eliminating the potential of such contracts becoming tough legacy contracts after Jibar is discontinued.

7.4 The SARB had received data from the London Clearing House (LCH), showing that their Jibar-related exposure amounted to circa ZAR104 trillion as at 30 June 2024 – an amount that was significantly higher than the domestic Jibar-related exposure as the regular ‘quantitative survey’. Given the significance of the international exposure to Jibar, it would be beneficial to adhere to the ISDA methodology as much as possible. The LCH data would be shared with all MPG members to ensure they had a comprehensive understanding of the exposure landscape.

7.5 In conclusion, it was noted that the credit spread adjustment was crucial for market participants, and ensuring its accuracy was even more important, even if it required deviating from the ISDA methodology. Its use would extend beyond the ISDA protocol to include determining economic equivalence in cash instruments and for tax purposes. The workstream would collaborate with the SARB to determine the most appropriate course of action. Should a deviation be pursued, the Legal and Governance and Regulatory Issues Workstreams would be engaged to assess the potential implications.

7.6 The workstream aimed to study Turkey's transition, as they deviated from the ISDA methodology. Furthermore, it would use the MPG conference to solicit market practitioners' initial impressions. A discussion paper would be distributed to attendees ahead of the MPG conference.

8. Annual MPG conference

8.1 Mr Gininda presented the agenda for the annual MPG conference, which was scheduled to take place at The Maslow, Sandton, on 21 August 2024. The conference would provide a platform to discuss the opportunities and risk that market participants needed to be aware of in terms of the Jibar transition.

8.2 The agenda would entail a keynote address by the Chairperson, followed by a panel discussion with selected MPG members. The recent publications of the MPG and its workstream would form the content that would be discussed at the conference. As such, the topics would include, among others, the updated MPG's Jibar transition plan, managing interest rate and liquidity risk during the Jibar transition, minimising the risk of economic value transfer in legacy contracts and modernising market infrastructure. Furthermore, it was envisaged that there would be a breakaway session to allow for an in-depth discussion by derivatives market practitioners. They would be provided an opportunity to expand on the content of the white paper on market conventions for ZARONIA-based non-linear derivatives.

8.3 Panel discussants were requested to provide pictures and short bios of themselves, which would be included in the conference pack. They were also advised that the whole conference would be recorded and posted on YouTube in due course as the format of the conference would only allow for in-person attendance. It was noted that any comments on the agenda should be submitted promptly, as the finalised agenda was expected to be distributed to conference attendees on 13 August 2024. Furthermore, the affected workstream chairpersons were required to finalise and submit discussion documents by 14 August 2024. These documents included the ZARONIA First initiative, the methodology for the credit adjustment spread (CAS), and the paper on non-linear derivatives. A presentation template would also be provided to allow members to submit their presentation slides on 19 August 2024.

9. **Updates from MPG workstreams**

9.1 The Derivatives Workstream had been collaborating with market makers to secure their commitment to launching the market, setting up pricing structures and accelerating inter-dealer market making. Furthermore, market makers had been quoting basis swaps, specifically focusing on the basis swap between ZARONIA and Jibar to help establish a basis market. The workstream had also engaged inter-dealer brokers and offshore markets; and included the Emerging Markets Trading Association as an attendee to the workstream to broaden communication channels, particularly with offshore traders and banks.

9.2 Regarding the ZARONIA First initiative, the workstream had conducted an in-depth study on the United States and United Kingdom markets and their respective Secured Overnight Financing Rate (SOFR) First and Sterling Overnight Indexed Average (SONIA) First initiatives. It was observed that trading and clearing in the cash market instruments and swaps referencing SOFR and SONIA were well established prior to the implementation of their derivatives-first initiatives. However, delays were noted in certain areas, such as cash market trading in overnight instruments, the availability of swap clearing, and engagements via Dear CEO letters, primarily due to the impact of COVID-19. Furthermore, the ISDA protocol was in place before these initiatives were launched.

9.3 Questions were raised regarding the development of a basis swap market, specifically whether the workstream had considered the timeline and the limited period in which the basis swap market would operate. Furthermore, the interaction between the basis market and the CAS was noted, particularly in terms of how it would align with the experience in international markets, where the basis market typically coalesces around established credit adjustment spread prices.

9.4 While discussions on the basis market were still in the early stages, the DWS recognised the significance of these issues and emphasised the urgency of reaching consensus on the pricing dynamics for the basis market. Regarding the CAS, trading would continue until a clear consensus was reached on the appropriate level of the CAS. Alternatively, market activity could proceed at levels that diverge significantly from the eventual agreed-upon CAS, reflecting uncertainty in the interim.

9.5 Furthermore, Mr Gininda inquired about the steps that should be taken to stimulate market activity in the period leading to the implementation of ZARONIA First initiatives in February 2025. While market makers had been posting prices for interest rate swaps, there had been no significant market activity locally. Building liquidity would depend on banks' ability to mitigate risk. If the market was predominately one sided, it would limit the banks' ability to provide substantial liquidity.

9.6 The Cash Market Workstream (CMW) was scheduled to meet with LCH and Strate Pty Ltd to discuss trade repository requirements. Furthermore, SA Home Loans had requested an impact analysis to be conducted because of the long-dated nature of their mortgage loan portfolios. SA Home Loan was one the retail segments that continued to offer Jibar-linked products, making the analysis crucial for assessing the potential effects of the transition. It was agreed that the CMW would engage the TPCW to determine the way forward.

9.7 The Legal Workstream had planned to provide support on measures for dealing with tough legacy legislation in collaboration with the Governance and Regulatory Issues Workstream (GRIW). The workstream would also provide support to the TPCW in determining the credit adjustment spread methodology. This decision would affect the use of the ISDA protocol if an alternative methodology was chosen, necessitating collaborative efforts between the TPCW, GRIW and the Legal Workstream.

9.8 Mr Burgoyne presented the revised Jibar transition roadmap, which reflected an announcement of the ZARONIA First initiative in November 2024, postponing its implementation from November 2024 to February 2025. Furthermore, the Dear CEO letters would be distributed in September 2024. This extended timeline would allow market participants more time to familiarise themselves with the new instruments and the proposed conventions, facilitating a voluntary transition without the soft power typically associated with the ZARONIA First initiative. These updated dates would also be announced at the MPG conference.

10. **Date of the next meeting – 10 October 2024, 09:00 AM**

11. **Closure**

1.1 The Chairperson thanked everyone in attendance for their contributions, and there being no further matters for discussion, the meeting was closed.

Rashad Cassim

27-Nov-2024

DG R Cassim **Date**

Chairperson:

Market Practitioners Group on the Interest Rate Benchmark Reforms