

Banks Pick New Reference Rate to Replace U.S. Dollar Libor

Broad-based Treasury repo rate is chosen; phasing in expected to start next year

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Fifteen banks voted Thursday on a replacement for the U.S. dollar London interbank offered rate, the besmirched interest-rate benchmark that some of them were accused of rigging in an industrywide scandal a few years ago.

Banks participating in the vote had settled on two likely candidates as of last year and decided on a rate derived from a broad set of borrowing transactions secured by U.S. Treasuries, according to a statement from the Alternative Reference Rates Committee. The individual vote tally wasn't disclosed, a spokesman for the committee said.

Phasing in the new rate is expected to start next year on a voluntary basis, after the committee publishes a report on its work.

Getting U.S. financial firms to migrate to the new benchmark won't be like flipping a switch. Libor has been deeply embedded in financial markets for decades and is used to set rates for hundreds of trillions of dollars of derivatives and other borrowings, including loans to consumers, companies and governments.

In May, the U.K. announced an alternative reference rate to Libor for Sterling-based derivatives and other financial-market contracts.

In the U.S., the committee has "got to have a plan to encourage the market to adopt it," said David Duffee, partner at law firm Mayer Brown.

The banks that voted Thursday were brought together in 2014 by the Federal Reserve Bank of New York and the Fed Board of Governors in Washington, D.C., [after certain banks were alleged](#) to have manipulated Libor. Banks collectively paid billions of dollars to settle those investigations.

At the time the committee was formed, neither of the U.S. alternative rates had been created. Even now, the preferred rate selected has to go through a round of public comment and won't be published [until later this year or 2018](#).

The rate the banks decided on is based on short-term loans known as repurchase agreements or "repo" trades, backed by Treasury securities as collateral. The New York Fed has proposed publishing the rate in cooperation with the Office of Financial Research.

The chosen rate consists of transaction data from across the repo markets, including some provided by [Bank of New York Mellon](#) Corp. and others settled by a unit of the Wall Street-controlled utility Depository Trust & Clearing Corp. But it excludes trades struck one-for-one between firms that aren't processed by third parties, as well as repo trades [conducted with the Fed](#).

The runner up in the vote, the so-called Overnight Bank Funding Rate, is [an overnight gauge of unsecured bank funding costs](#) composed of transactions from the federal-funds market and Eurodollar trading. That rate has at times been beset by slumping trading volumes.

Asset managers, including BlackRock and Pacific Investment Management Co., were consulted as part of [an advisory group](#) formed in November 2016 but didn't vote on Thursday. A significant majority of them had expressed a preference for the Treasury repo rate, ARRC said. Four financial market utilities also provided feedback.

Last May, a Treasury group convened by the New York Fed recommended that industry participants [use benchmarks](#) that comply with new international financial-market standards. Those standards have been promoted by the International Organization of Securities Commissions.

Sandra O'Connor, a [J.P. Morgan Chase & Co.](#) executive who chairs the ARCC, said in a statement following the vote that by selecting an alternative to Libor, the industry "took an important step to strengthen the financial system."

Fed governor Jerome Powell said in a separate statement he was confident the new rate is "based on a deep and actively traded market and will be highly robust."

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