21 August 2020

To: Sub-working group for Market standards and fallback solutions
From: Sub-working group for Establishing an OIS (Overnight Index Swap) market in NOK
Subject: Response to Consultation paper - Market Conventions for Financial Products Referencing NOWA, June 2020

To whom it may concern,

The sub-working group for *Establishing an Overnight Index Swap (OIS) market in NOK* has discussed the **Working Group on Alternative Norwegian Krone Reference Rates Consultation: Market Conventions for Financial Products Referencing NOWA, June 2020** and prepared the below response.

In order to establish an OIS market in Norway, the sub-working group believes it is important that interdealer OIS market conventions in Norway mirror as closely as possible the interdealer OIS market conventions in major global markets. This is particularly important to ensure fungibility between cross-currency OIS derivatives, the FX swap market and single-currency OIS derivatives, which will be the key building blocks in the interdealer market for derivatives referencing NOWA. Our responses the questions posed in the consultation are listed below. Please note that our views are limited strictly to the conventions used in the interdealer market for derivatives referencing NOWA. We make no comment as to the conventions to be used for derivatives in dealer-customer or customer-customer trades, nor in any other markets that use NOWA as a reference rate (e.g. floating rate notes, loans etc).

Question 1:
Does your institution support the recommended day count convention? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

We support the recommended ACT/365 day count convention for interdealer derivatives referencing NOWA.

Question 2:
Does your institution support the recommended modified following, adjusted, as the business day convention? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

We support the recommended modified following, adjusted, as the business day convention for interdealer derivatives referencing NOWA.

Question 3: Does your institution support backward-looking interest rate calculation as the convention for contracts referencing NOWA? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

We support backward-looking interest rate calculation as the convention for interdealer derivatives referencing NOWA.

Question 4:
Does your institution support compounded average as the convention for contracts referencing NOWA? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

We support compounded average as the convention for interdealer derivative contracts referencing NOWA.

Question 5:
Does your institution support the shifted observation period as the convention for contracts referencing NOWA? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

No. We prefer the use of the delayed payment convention for interdealer derivative contracts referencing NOWA. This is to align NOK OIS conventions with the conventions used in global OIS markets and to facilitate the fungibility of cross-currency and single-currency OIS derivatives.

The two most relevant overseas markets for NOK are EUR and USD, which use payment delays of T+1 and T+2 in their respective interdealer OIS markets. We also refer to Recommendations for Interdealer Cross-Currency Swap Market Conventions paper published in January 2020 by the Market Structures Working Group of the Alternative Reference Rates Committee in Cooperation with other National Working Groups and Associations.[1] This paper identifies the alignment of payment dates as an important principle in order to limit unnecessary credit risk and, thereby, promote more robust liquidity. Given the vast majority of interdealer cross-currency basis swaps in NOK are traded versus USD, we recommend the use of a T+2 payment delay in the interdealer derivative market for contracts referencing NOWA.

[1] https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/Recommendations_for_Interdealer_Cross-Currency_Swap_Market_Conventions.pdf , 3-5

Question 6:
Does your institution support a 2 business day notification period as the convention for contracts referencing NOWA? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

We support a two day payment delay for all interdealer derivatives referencing NOWA (see our response to question 5 for more detail).

Question 7: 12 Does your institution support adding the margin to the compounded NOWA (i.e. not compounding the margin) as the convention for contracts referencing NOWA? If not, please explain why this is not your preferred solution, and suggest an alternative solution.

We support adding the margin to the compounded NOWA (i.e. not compounding the margin) as the convention for interdealer derivatives referencing NOWA.

Additional Notes

The two major building blocks for all interdealer trades referencing NOWA will be vanilla OIS (which may be traded outright, or as a spread to FRAs or IRS referencing Nibor), and cross-currency basis (which will be traded against either a foreign currency risk-free-rate or foreign currency LIBOR rate). Our suggested conventions for these products are outlined below.

Interdealer Vanilla OIS vs NOWA

Parameter	Fixed Leg	Float Leg: NOWA
Start date	Spot (T+2)	
Frequency	Annual	
Averaging	N/A	Daily compounding, exclude spread
Day count convention	ACT/365	
Business day convention	Modified Following, Adjusted	
Payment delay	2 days	

Interdealer NOWA-RFR Cross-currency Basis Swap

Parameter	Float Leg 1: NOWA	Float Leg 2: Foreign CCY RFR
Start date	FX Spot date for relevant currency pair	
Exchange of notional principal cashflows	At start and maturity dates	
Frequency	Quarterly	
Averaging	Daily compounding, exclude spread	
Day count convention	ACT/365	Day count convention used in relevant single currency OIS market
Business day convention	Modified Following, Adjusted	
Payment delay	Adjusted in order to achieve alignment of payment dates of principal*	
Reset of notional principapals	Quarterly*	

- Note that ARCC outlines different options for both payment lags and quarterly resets of notional principals in their aforementioned paper, Recommendations for Interdealer Cross-Currency Swap Market Conventions.[2] As yet it is unclear which of these will become market standard in global markets, but the sub-working group supports the principle of aligning payment dates of principal, as well as the principle of quarterly resets of notional principals for interdealer RFR-RFR cross-currency basis swaps where NOK is one of the reference currencies.

Interdealer NOWA-IBOR Cross-currency Basis Swap

We support the recommendations made by ARCC in their aforementioned Recommendations for Interdealer Cross-Currency Swap Market Conventions:[3]

[2] https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/Recommendations_for_Interdealer_Cross-Currency_Swap_Market_Conventions.pdf, 3-5
[3] Ibid. 7

Potential conventions for an RFR-IBOR dealer-to-dealer cross currency basis swaps

1) Conventions for the RFR leg
As a standard, the RFR conventions in the RFR-IBOR cross currency basis swap market should match RFR accrual conventions which develop in the RFR-RFR cross currency market and which are discussed in the previous section.

2) Conventions for the IBOR leg
As a standard, the IBOR leg of the RFR-IBOR cross currency basis swap market should match the conventions developed in the related IBOR currency swap market.

3) Alignment of settlement dates
Although in general the Group believed that standard OIS or RFR conventions could be used for each respective leg, respondents to the consultation noted that it may be useful to align settlement conventions if, for example the standard IBOR settlement date (T) diverged from the standard OIS settlement date (T+2). Recognizing the importance of aligning principal payment dates in mitigating credit risk, the group agreed that alignment of payment dates of principal could be recommended as a standard

4) Aligning Accrual Conventions with Cash Products
In certain circumstances, RFR accrual conventions may develop to include lookback periods or lockout periods. Such conventions would facilitate alignment of principal and interest and alignment with conventions in cash markets. As a matter of convenience, these may also be adopted in cross-currency swap conventions, although there currently is insufficient information upon which to assess how this will develop. Note, however, that because IBOR is a forward looking rate and overnight RFRs are based upon realized rates, incorporating certain current conventions in the RFR leg might lead to additional basis or convexity.