

Establishing an OIS market in NOK

Mandate

Background

Reference rates play a critical role in the financial system. The value of various financial products and loan agreements linked to these rates is very high. In early 2018, a working group on alternative Norwegian krone reference rates (hereinafter referred to as the ARR working group) was established by Norges Bank, in consultation with the financial industry. The main objective of the group's work is to establish a reference rate for the Norwegian krone as an alternative to Nibor. In September 2019, the ARR working group recommended Nowa (Norwegian Overnight Weighted Average) as an alternative Norwegian krone reference rate. The work on alternative reference rates is now moving into a new phase and will focus on how to transition to using Nowa as a reference rate.

Use of interest rate derivatives in Norway

A well-functioning interest rate derivatives market is important for market participants wishing to hedge against interest rate risk. Interest rate derivatives are also widely used by participants wishing to speculate on changes in market yields.

The interest rate derivatives market in Norway uses Nibor as a reference rate. A key reason for this is that a very large number of loan and bond agreements in Norway are agreements with floating interest rates based on Nibor. In other words, market participants' interest rate risk will be linked to Nibor, which in turn generates demand for interest rate derivatives with Nibor as a benchmark.

Nowa is likely to be increasingly used as a benchmark for financial products in Norway. Greater use of Nowa as a benchmark in financial contracts will likely also lead to greater demand for interest rate derivatives linked to Nowa. An OIS (overnight indexed swap) market in Norway linked to Nowa will be useful for market participants entering into contracts with Nowa as a benchmark and for participants wishing to speculate on the general level of market yields without being exposed to bank risk.

Sub-group for establishing an OIS market in NOK

Norway is currently one of few countries without any form of OIS market. Other countries have also chosen overnight rates as alternative reference rates for their respective lbor rates. Derivatives linked to overnight rates are likely to play an increasing role in global derivatives markets in the years ahead. The working group has decided to establish a sub-group to explore the possibilities for establishing an OIS market in Norway linked to Nowa.

Objectives:

The sub-group is to

- Prepare an official report with proposals for how to facilitate the establishment of an OIS market linked to Nowa.
- The report should include specific recommendations for how an OIS market linked to Nowa can be established and a plan for carrying out the recommendations.
- The report should include recommended measures for increasing interest in derivatives linked to Nowa.

Administration and work structure

- The sub-group comprises market participants from various parts of the private and public sectors.
- The chair of the sub-group is to be one of the voting members of the working group. The chair is selected by the ARR working group.
- Each member of the sub-group represents his or her own institution.
- Each institution has one vote. Norges Bank will have observer status without voting rights.
- Norges Bank will perform the secretariat function. This will be a coordinating role. The secretariat will, in collaboration with the chair or other members, convene meetings, draw up the agendas, write minutes and coordinate the writing of reports.
- The mandate, participants, agendas, minutes and reports will be published on the ARR working group's web page on Norges Bank's website.
- Non-members may be invited to make presentations or participate in some of the work of the sub-group. The sub-group can also establish sub-groups to examine more closely certain themes if deemed appropriate. Establishment of new groups must be cleared with the ARR working group in advance.
- The sub-group shall draw on relevant parties for input into the group's work.
- In collaboration with the ARR working group, the sub-group may assume tasks associated with communicating the group's work to users of reference rates.
- The sub-group must coordinate its work with the sub-group examining market conventions and fallback solutions for Nowa products.
- The sub-group shall regularly update the ARR working group on its work. The ARR working group shall be presented with a consultation report and a final report prior to publication and shall give its endorsement to what is published.

Indicative timeline

The sub-group aims to publish at least one official report by the end of 2020. The report will contain specific recommendations for how to proceed with facilitating an OIS market linked to Nowa.

Confidentiality

All information provided, discussions and statements during the meetings of the sub-group are subject to a duty of confidentiality, if the sub-group has not approved public disclosure of

such information. However, this does not prevent participants from conducting internal consultations in the institutions they represent.