

**ABA Policy Advocacy Committee Meeting**

# **From Interbank Offered Rates to Risk-Free Rates - Update**






**Position Paper by Erste Group Bank AG**

Taipei, 28 March 2021

## NOTE

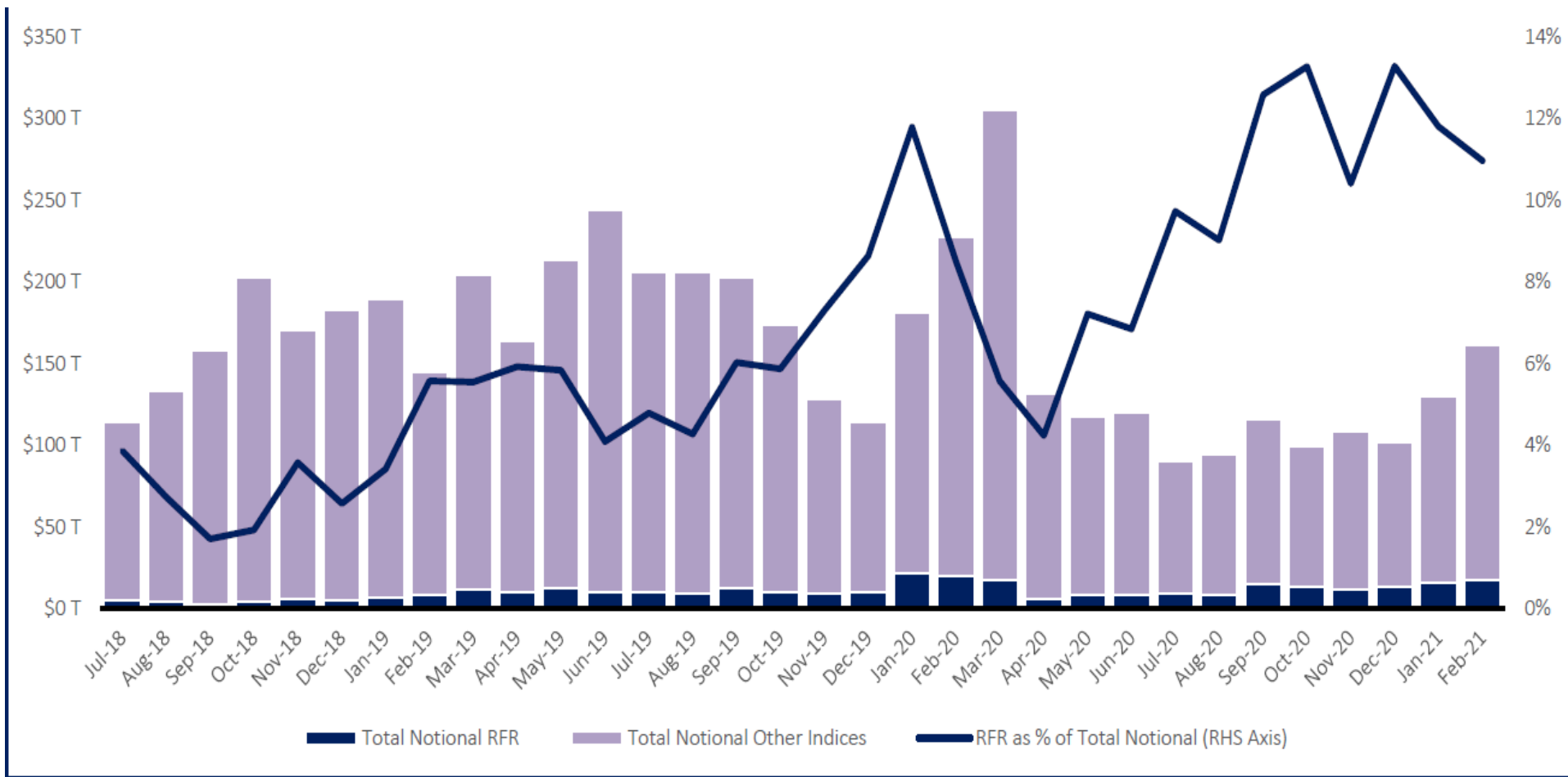
- The following presentation is an update to the previous ABA Policy Advocacy Committee Position Papers dated 14 November 2019 and 13 November 2020
- Please refer to these previous papers for basics, such as Fundamental Problems with LIBOR, Key Differences between IBORs and RFR, How to use RFR in Cash Products, etc.

## UPDATE RISK-FREE RATES (RFR)

CURRENCY	ARR	ADMINISTRATOR	NATURE	DATA SOURCE	O/N RATE AVAILABLE	TERM RATE AVAILABLE	WORKING GROUP
 EUR	€STR	European Central Bank	Unsecured	MMSR transactions	✓	✗ Under consideration	Working Group on Euro Risk-Free Rates
 GBP	SONIA	Bank of England	Unsecured	Unsecured overnight sterling transactions negotiated bilaterally and brokered in London by WMBA	✓	✓ Published, Term SONIA testing complete	Working Group on Sterling Risk-Free Rates
 USD	SOFR	Federal Reserve Bank of New York	Secured	Tri-party repo, FICC GC repo, FICC bilateral treasury repo	✓	✗ Planned for 2021	Alternative Reference Rates Committee (ARRC)
 CHF	SARON	SIX Swiss Exchange	Secured	CHF repo transactions in the interbank market	✓	✗ Not recommended	National Working Group on Swiss Franc Reference Rates
 JPY	TONAR	Bank of Japan	Unsecured	Data provided by money market brokers	✓	✓ Published, TORF in test phase	Cross-industry Committee on Yen Interest Rate Benchmarks

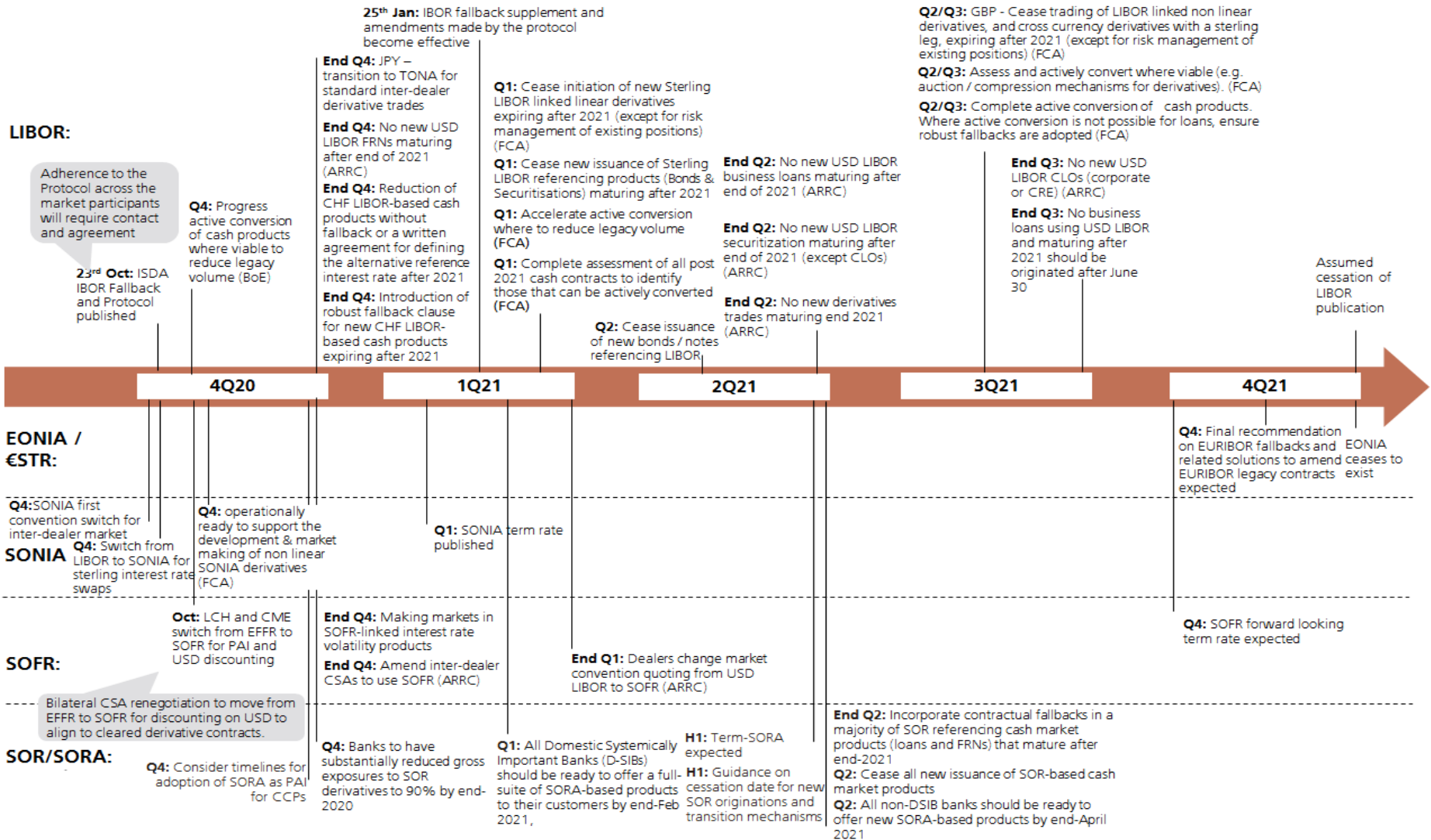
**Note:** A number of key Asian benchmarks are derived by applying a Forward FX curve to the USD LIBOR curve, notably SOR (Singapore), THBFIX (Thailand), MIFOR (India), and PHIREF (Philippines). Replacement rates also will need to be identified here

## RFR VOLUMES STILL SMALL



**Calculation:** Total traded notional per month across all IRD products split by RFRs (including OTC and ETD) and all IRD products referencing other indices.

# RECENT AND REMAINING MILESTONES



# FCA ANNOUNCEMENT ON 05 MARCH 2021



## FCA announcement on future cessation and loss of representativeness of the LIBOR benchmarks

05 March 2021

1. This statement announces the future cessation or loss of representativeness of the 35 LIBOR benchmark settings currently published by ICE Benchmark Administration (IBA), an authorised administrator, regulated and supervised by the FCA.
2. IBA notified the FCA, following the completion of its recent [consultation](#) and notice of future departure received from the majority of the panel banks for each LIBOR setting, that it intends to cease providing all LIBOR settings for all currencies, subject to any rights of the FCA to compel IBA to continue publication.
3. We have completed our assessments of the effect of panel bank departures on LIBOR's ability to represent the underlying market, and of how IBA intends to cease providing LIBOR, as required by the UK Benchmarks Regulation (BMR). We have decided not to require any panel banks to continue to submit to LIBOR beyond the date from which they have notified their departure, or to require IBA to continue to publish LIBOR on the basis of panel bank submissions beyond such date. We have no intention to use our proposed powers to compel IBA to continue to publish any of the following 26 LIBOR settings as "synthetic" LIBOR (as described below). Therefore, these 26 LIBOR settings will permanently cease as we set out below.
  - Publication of all 7 euro LIBOR settings, all 7 Swiss franc LIBOR settings, the Spot Next, 1-week, 2-month and 12-month Japanese yen LIBOR settings, the overnight, 1-week, 2-month and 12-month sterling LIBOR settings, and the 1-week and 2-month US dollar LIBOR settings will cease immediately after 31 December 2021.
  - Publication of the overnight and 12-month US dollar LIBOR settings will cease immediately after 30 June 2023.
4. We will consult on requiring IBA to continue to publish the 3 remaining sterling LIBOR settings (1-month, 3-month and 6-month) for a further period after end-2021 on a changed methodology (also known as a "synthetic") basis using the proposed new powers the government is legislating to grant us under the BMR. Using our proposed powers in this way would be intended to protect consumers and market integrity by reducing disruption in markets where it is unlikely to be feasible to convert certain outstanding contracts that reference LIBOR to alternative reference rates.
5. We will consult on requiring IBA also to continue to publish the 1-month, 3-month and 6-month Japanese yen LIBOR settings after end-2021 on a synthetic basis, for one additional year. This proposed use of our powers would be intended primarily to protect market integrity by allowing more time for transition away from Japanese yen LIBOR to complete. We do not envisage using our proposed powers to compel IBA to continue to publish any Japanese yen LIBOR settings after end-2022, and publication of these settings will consequently cease permanently immediately after a final publication on 30 December 2022.

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6. As the transition away from US dollar LIBOR progresses, we will continue to consider the case for using these proposed powers also to require continued publication on a synthetic basis of the 1-month, 3-month and 6-month US dollar LIBOR settings for a further period after end-June 2023, taking into account views and evidence from the US authorities and other stakeholders.
7. Where we decide to require IBA to continue the publication of any settings on a synthetic basis, the methodology we would propose to require LIBOR's administrator to use it as set out in our statements of policy described below. Although this methodology provides in our view a fair approximation of what panel bank LIBOR would have been beyond the end-date for each of the panels, LIBOR settings published on this synthetic basis will no longer be representative of the underlying market and economic reality the setting is intended to measure as those terms are used in the BMR.
8. Consequently it is clear that these 9 LIBOR benchmark settings (1-month, 3-month and 6-month settings in each of sterling, Japanese yen and US dollar LIBOR) will no longer be representative of the underlying market and economic reality that such setting is intended to measure and that representativeness will not be restored, as set out below.
  - Immediately after 31 December 2021, the 1-month, 3-month and 6-month Japanese yen LIBOR settings and the 1-month, 3-month and 6-month sterling LIBOR settings will no longer be representative and representativeness will not be restored.
  - Immediately after 30 June 2023, the 1-month, 3-month and 6-month US dollar LIBOR settings will no longer be representative and representativeness will not be restored.
9. It follows that all 35 LIBOR settings will either cease to be provided by any administrator or no longer be representative immediately after the dates set out above.
10. We make this statement in the awareness that it will engage certain contractual triggers for the calculation and future application of fallbacks that are activated by pre-cessation or cessation announcements made by the FCA (howsoever described) in contracts, and in accordance with our [11 March 2020 statement](#) on LIBOR contractual triggers.
11. The exercise of our proposed new powers to require continued publication on a synthetic basis is subject to the enactment of the [Financial Services Bill](#) by Parliament. Any decision to use them to require a methodology change for LIBOR settings will take into account evidence and views from market participants and our counterpart global authorities, and will be consulted upon in due course.
12. We have also published today our [statements of policy](#) in relation to some of the proposed new powers that the government is legislating to grant us under the BMR. The statements of policy provide more detail of the policy framework which explains why we have no intention to use our proposed powers to require continued publication on a synthetic basis for 26 of the LIBOR settings, will consult on using them for the remaining 3 sterling LIBOR settings and, for one additional year, the remaining 3 Japanese yen LIBOR settings, and will continue to consider the case for using them for the 3 US dollar LIBOR settings as described above. It also confirms our intentions with regard to the methodology we would propose to use for any settings published on a synthetic basis (i.e. a forward-looking term rate version of the relevant Risk Free Rate plus a fixed

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spread adjustment calculated over the same period and in the same way as the spread adjustment implemented in the IBOR Fallbacks Supplement and the 2020 IBOR Fallbacks Protocol published by the International Swaps and Derivative Association).

13. We remind market participants that, although publication of certain LIBOR settings on a synthetic basis would be intended to assist legacy contract holders, new use of this synthetic LIBOR by UK regulated firms in regulated financial instruments would be prohibited under the BMR as amended by the Financial Services Bill currently being enacted by Parliament. Continued use by regulated firms in legacy financial instruments would also be subject to the FCA using its proposed powers to permit such use. We will consult later in 2021 on which legacy use of synthetic LIBOR might be permitted.

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## SUMMARY

- Announcement constitutes an **index cessation event** under the IBOR Fallbacks Supplement and the ISDA 2020 IBOR Fallbacks Protocol **for all 35 LIBOR settings**
- As a result, the **fallback spread adjustment** published by Bloomberg is **fixed** as of the date of the announcement for all EUR, GBP, CHF, USD, and JPY settings (see next page)
- **24 LIBOR settings** will permanently cease immediately after **31 December 2021** (all seven EUR LIBOR tenors; all seven CHF LIBOR tenors; O/N, 1W, 2M, 12M GBP LIBOR; S/N, 1W, 2M, 12M JPY LIBOR; 1W, 2M USD LIBOR)
- **2 LIBOR settings** will permanently cease immediately after **30 June 2023** (O/N and 12M USD LIBOR)
- For the **remaining 9 LIBOR settings**, FCA will consult on requiring IBA to continue publication on a **synthetic basis** after 31 December 2021 (1M, 3M, 6M GBP LIBOR; 1M, 3M, 6M JPY LIBOR), resp. after 30 June 2023 (1M, 3M, 6M USD LIBOR). However, these LIBOR settings will **no longer be representative** of the underlying market and economic reality immediately after 31 December 2021, resp. 30 June 2023, and representativeness will not be restored
- Publication of the mentioned LIBOR settings on a synthetic basis would be intended to **assist legacy contract holders**. New use of this synthetic LIBOR by UK-regulated firms would be prohibited. FCA will consult later in 2021 on which legacy uses of synthetic LIBOR might be permitted

# FIXED SPREAD ADJUSTMENTS

LIBOR	Tenor	Ticker	Spread Adjustment (%)
CHF	Spot/Next	SSF00SN Index	-0.0551
CHF	1 Week	SSF0001W Index	-0.0705
CHF	1 Month	SSF0001M Index	-0.0571
CHF	2 Months	SSF0002M Index	-0.0231
CHF	3 Months	SSF0003M Index	0.0031
CHF	6 Months	SSF0006M Index	0.0741
CHF	12 Months	SSF0012M Index	0.2048
EUR	Overnight	SEE00ON Index	0.0017
EUR	1 Week	SEE0001W Index	0.0243
EUR	1 Month	SEE0001M Index	0.0456
EUR	2 Months	SEE0002M Index	0.0753
EUR	3 Months	SEE0003M Index	0.0962
EUR	6 Months	SEE0006M Index	0.1537
EUR	12 Months	SEE0012M Index	0.2993
GBP	Overnight	SBP00ON Index	-0.0024
GBP	1 Week	SBP0001W Index	0.0168
GBP	1 Month	SBP0001M Index	0.0326
GBP	2 Months	SBP0002M Index	0.0633
GBP	3 Months	SBP0003M Index	0.1193
GBP	6 Months	SBP0006M Index	0.2766

LIBOR	Tenor	Ticker	Spread Adjustment (%)
GBP	12 Months	SBP0012M Index	0.4644
JPY	Spot/Next	SJY00SN Index	-0.01839
JPY	1 Week	SJY0001W Index	-0.01981
JPY	1 Month	SJY0001M Index	-0.02923
JPY	2 Months	SJY0002M Index	-0.00449
JPY	3 Months	SJY0003M Index	0.00835
JPY	6 Months	SJY0006M Index	0.05809
JPY	12 Months	SJY0012M Index	0.16600
USD	Overnight	SUS00ON Index	0.00644
USD	1 Week	SUS0001W Index	0.03839
USD	1 Month	SUS0001M Index	0.11448
USD	2 Months	SUS0002M Index	0.18456
USD	3 Months	SUS0003M Index	0.26161
USD	6 Months	SUS0006M Index	0.42826
USD	12 Months	SUS0012M Index	0.71513



## KEY ISSUES

- **Spread Adjustment** – to fairly reflect the structural differences between IBOR and RFR. RFR's such as SONIA and SOFR do not include a liquidity or credit risk premium, which lenders must add when they transition away from IBOR's to maintain their interest rate return. Spreads between IBOR's and RFR's can widen substantially in times of stress, as we have seen in March 2020. Beyond 2021, the lack of credit spreads in new risk-free rates could still create a risk of high interest margin volatility for banks, as widening bank credit spreads have tended to partly mitigate falling risk-free rates in times of market stress
  - Fixed Spread Adjustments as of 05 March 2021; fallback rates in general higher than current IBOR
- **Term Rate** - IBORs are forward-looking, usually over various tenors, and therefore rates are known ex-ante. In contrast, RFR's are overnight rates and are only known ex-post, on the next day, which creates significant challenges in determining RFR term rates, in particular for cash products such as loans and mortgages
  - Term Rates published for GBP (Term SONIA testing complete) and JPY (TORF in testing phase), **but still not available for USD!**
- **Increasing Regulatory Pressure** – increased demand for ever more detailed data on IBOR-linked exposures and transition plans by regulators, deadlines for switch to RFR
  - E.g. in HK, HKMA requires banks by 30 June 2021 to cease issuing new IBOR-linked products maturing after 31 December 2021

## RFR ISSUES BY APAC BANKS

Issuer Name	Ticker	Country	Coupon	Maturity	Amt Issued	Maturity Type	Currency
Bank of China Ltd/Macau	BCHINA	CN	0.98	17.10.2022	350,000,000	AT MATURITY	USD
Bank of East Asia Ltd/HK	BNKEA	HK	0.18	15.09.2021	20,000,000	AT MATURITY	USD
Commonwealth Bank of Australia/New York	CBAAU	AU	0.20	10.09.2021	150,000,000	AT MATURITY	USD
Commonwealth Bank of Australia/New York	CBAAU	AU	0.11	03.05.2021	50,000,000	AT MATURITY	USD
Export-Import Bank of Korea	EIBKOR	KR	0.31	11.03.2024	240,000,000	AT MATURITY	USD
Export-Import Bank of Korea	EIBKOR	KR	0.61	25.08.2021	100,000,000	AT MATURITY	USD
Kookmin Bank/Seoul	CITNAT	KR	0.47	03.08.2022	200,000,000	AT MATURITY	USD
Korea Development Bank	KDB	KR	0.26	09.03.2024	300,000,000	AT MATURITY	USD
Korea Development Bank	KDB	KR	0.56	21.03.2022	200,000,000	AT MATURITY	USD
Macquarie Group Ltd	MQGAU	AU	1.34	12.01.2027	1,250,000,000	CALLABLE	USD
Mitsubishi UFJ Trust & Banking Corp/New York	MUFG	JP	0.17	23.08.2021	100,000,000	AT MATURITY	USD
National Australia Bank Ltd	NAB	AU	0.15	26.04.2021	50,000,000	AT MATURITY	USD
Norinchukin Bank/New York	NORBK	JP	0.19	18.11.2021	300,000,000	AT MATURITY	USD
Sumitomo Mitsui Banking Corp/New York	SUMIBK	JP	0.16	10.09.2021	100,000,000	AT MATURITY	USD
Sumitomo Mitsui Banking Corp/New York	SUMIBK	JP	0.12	25.05.2021	130,000,000	AT MATURITY	USD
Sumitomo Mitsui Banking Corp/New York	SUMIBK	JP	0.12	14.05.2021	250,000,000	AT MATURITY	USD
Sumitomo Mitsui Banking Corp/New York	SUMIBK	JP	0.12	12.05.2021	300,000,000	AT MATURITY	USD
Sumitomo Mitsui Banking Corp/New York	SUMIBK	JP	0.15	22.07.2021	330,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.16	19.03.2021	415,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.14	13.05.2021	350,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.15	14.07.2021	350,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.21	16.06.2021	70,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.20	24.06.2021	50,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.12	10.06.2021	100,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.15	02.08.2021	100,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.15	12.07.2021	50,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.18	08.07.2021	150,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.16	09.04.2021	100,000,000	AT MATURITY	USD
Sumitomo Mitsui Trust Bank Ltd/ New York	SUMITR	JP	0.15	14.07.2021	350,000,000	AT MATURITY	USD

# CHECKLIST FOR ASIAN BANKS

No.	Topic	Key Considerations
1	Program Governance	<ul style="list-style-type: none"> <li>• Create working group to monitor market and regulatory developments and coordinate with all stakeholders, establish contact with official RFR working group</li> <li>• Senior management sponsor with decision-making powers</li> </ul>
2	Transition Management Program	<ul style="list-style-type: none"> <li>• Project management framework</li> <li>• Impact assessment</li> <li>• Resources and budget needs</li> <li>• Deadlines for stop of IBOR-linked business and switch to RFR</li> </ul>
3	Communication Strategy	<ul style="list-style-type: none"> <li>• External: clients, investors, counterparties, regulators, industry bodies</li> <li>• Internal: regular updates to all stakeholders, staff training</li> </ul>
4	Identify and Validate Exposures	<ul style="list-style-type: none"> <li>• Product exposure analysis</li> <li>• Identify and quantify IBOR-linked products maturing post 2021 and any changes needed – consider using AI tools</li> <li>• Continuous monitoring</li> </ul>
5	Develop Product Strategy	<ul style="list-style-type: none"> <li>• Timeline for offering new RFR-linked products</li> <li>• Risk and product approval requirements for RFR products</li> </ul>
6	Risk Management	<ul style="list-style-type: none"> <li>• Assess key risks from IBOR discontinuation incl. market readiness, business impacts, legal risk, operational risk, and financial risk such as accounting treatment and valuation</li> <li>• Establish processes to monitor and mitigate material risks</li> </ul>

## CHECKLIST FOR ASIAN BANKS CONT'D

No.	Topic	Key Considerations
7	Transition of Contracts	<ul style="list-style-type: none"> <li>• Legal review of contracts maturing post 2021</li> <li>• Check for adequate fallback language in existing contracts and amend/renegeotiate/replace/terminate if necessary</li> <li>• Incorporate adequate fallback language in all new contracts (or switch to RFR right away)</li> <li>• Check adherence to ISDA 2020 IBOR Fallbacks Protocol</li> </ul>
8	Operational and Technology Readiness	<ul style="list-style-type: none"> <li>• Check if systems can accommodate RFR mechanics – KONDOR+ has new functionality for IBOR replacement</li> <li>• Incorporate new market data sources and calculation methodologies into IT system</li> <li>• Testing and readiness of material operations and technology vendors</li> </ul>
9	Accounting and Reporting	<ul style="list-style-type: none"> <li>• Identify impact on fair value, impairment, P&amp;L, credit allowances</li> <li>• Identify changes needed to be made to current finance systems, operations, and control environment</li> <li>• Update financial disclosures</li> </ul>
10	Taxation	<ul style="list-style-type: none"> <li>• Identify tax implications and update tax documentation</li> <li>• Determine tax reporting requirements and jurisdictions</li> <li>• Review amendments to existing contracts</li> </ul>

# USEFUL LINKS

## **RFR Working Groups:**

EUR: [https://www.ecb.europa.eu/paym/interest\\_rate\\_benchmarks/WG\\_euro\\_risk-free\\_rates/html/index.en.html](https://www.ecb.europa.eu/paym/interest_rate_benchmarks/WG_euro_risk-free_rates/html/index.en.html)

USD: <https://www.newyorkfed.org/arrc>

GBP: <https://www.bankofengland.co.uk/markets/transition-to-sterling-risk-free-rates-from-libor>

CHF: [https://www.snb.ch/en/ifor/finmkt/finmkt\\_benchm/id/finmkt\\_reformrates](https://www.snb.ch/en/ifor/finmkt/finmkt_benchm/id/finmkt_reformrates)

## **RFR Calculators**

SIX for SARON: <https://www.six-group.com/en/products-services/the-swiss-stock-exchange/market-data/indices/swiss-reference-rates/saron-calculator.html>

IHS Markit: <https://rfrcalculator.ihsmarkit.com/> (recommended)

ICE Benchmark Administration: <http://www.theice.com/iba/rfr-portal>

NatWest: <https://www.realisedrate.com/>

## **New RFR's**

### SONIA

<https://www.bankofengland.co.uk/boeapps/database/fromshowcolumns.asp?Travel=Nix&ShadowPage=1&SearchText=sonia&SearchExclude=&SearchTextFields=TC&Thes=&SearchType=&Cats=&ActualResNumPerPage=&TotalNumResults=12&XNotes2=Y&C=5JK&ShowData.x=41&ShowData.y=34>

SARON (license required!)

[https://www.six-group.com/exchanges/indices/data\\_centre/swiss\\_reference\\_rates/values\\_de.html](https://www.six-group.com/exchanges/indices/data_centre/swiss_reference_rates/values_de.html)

### SOFR

<https://apps.newyorkfed.org/markets/autorates/SOFR>

## **Erste Group Bank AG – Update on LIBOR**

<https://youtu.be/RyB6RRGnh84>

# SOURCES

- Erste Group Bank AG
- Working Group on Euro Risk Free Rates
- Alternative Reference Rate Committee (ARRC)
- International Swaps and Derivatives Association (ISDA)
- Asia Securities Industry and Financial Markets Association (ASIFMA)
- European Central Bank (ECB)
- Standard & Poor's (S&P)
- Bloomberg
- Moody's
- UBS

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