

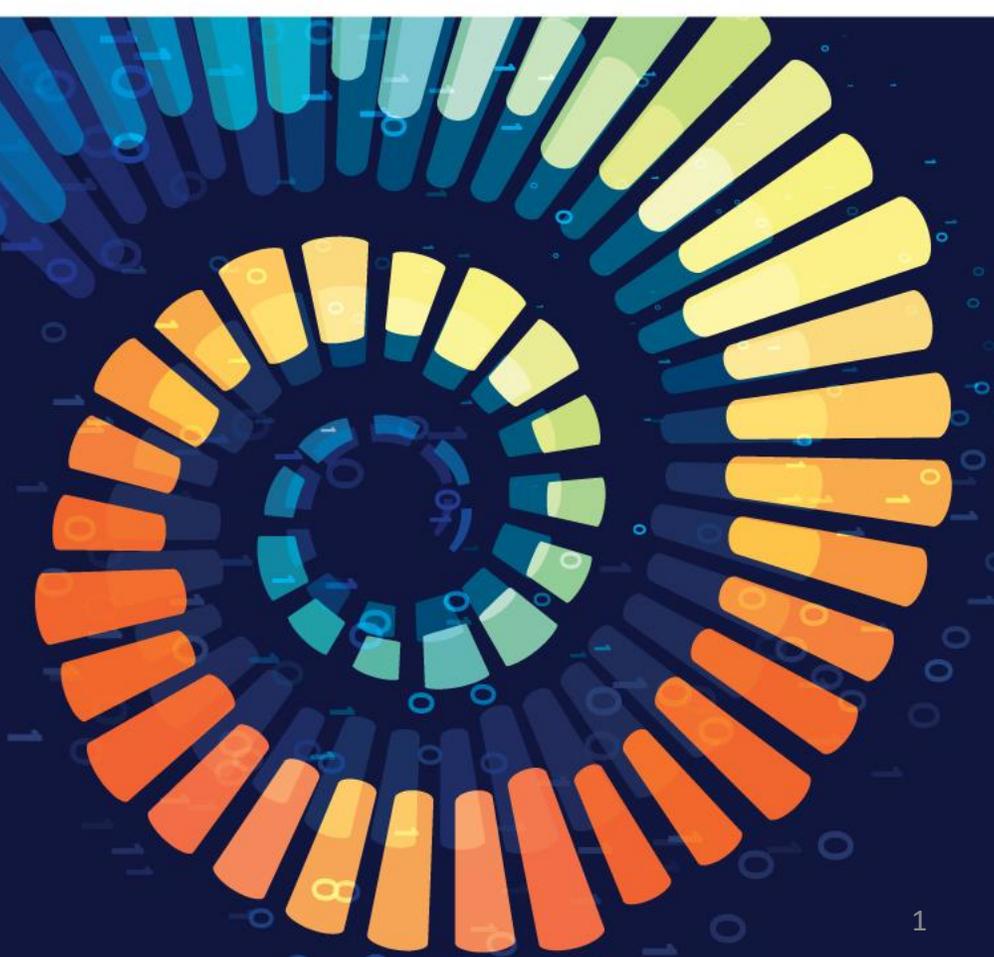


香港銀行學會

The Hong Kong Institute of Bankers

INNOVATION & TRANSFORMATION

A BRAVE NEW WORLD OF BANKING



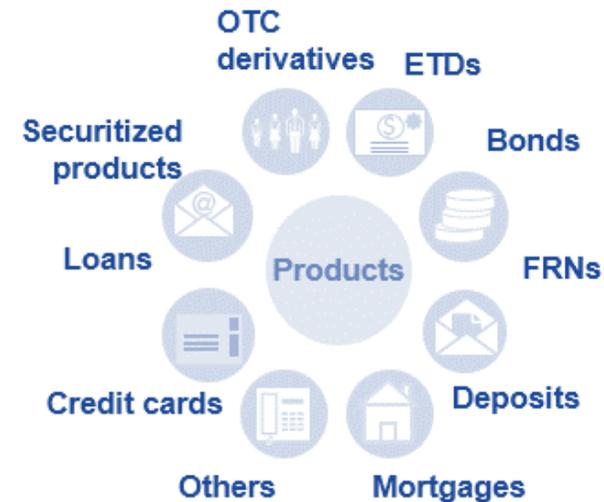
Introduction

The rate and its uses

LIBOR (London interbank offered rate): The rate offered in the London interbank market. LIBOR underpins financial contracts globally, with estimated exposures totaling USD350tn globally on a gross notional basis.

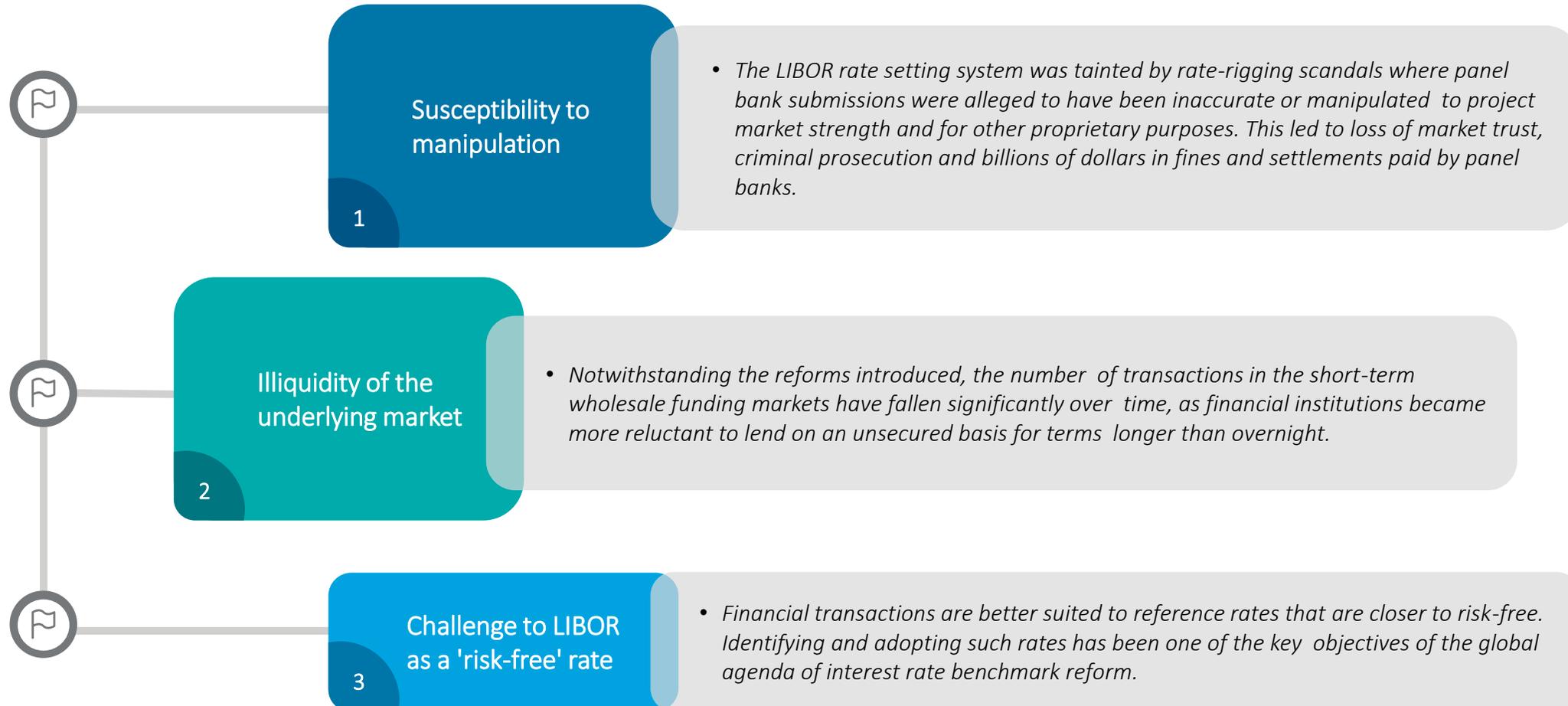
LIBOR is widely used in a variety of loans and financial instruments, including consumer and syndicated loans, structured products, securitisations, short term instruments, bonds such as floating rate notes, over-the-counter derivatives and exchange-traded derivatives, as well as in corporate contracts, accounting, tax, and valuation methods.

Market footprint



Limitation of LIBOR

The global financial crisis in 2008 exposed several crucial limitations and weaknesses inherent to LIBOR. The key limitations can be summarized as follows:



The End of LIBOR

In 2017, the Financial Conduct Authority (FCA) announced that it would not require panel banks to support LIBOR beyond the end of 2021. Recent announcements from the have introduced a number of other timing considerations for LIBOR transition plans.

For ALL LIBOR currencies, the FCA would neither “persuade nor compel” LIBOR submissions after December 31, 2020.

UK – LIBOR transition milestones The FCA, Bank of England (BOE), and the Working Group on Sterling Risk-Free Reference Rates (RFRWG) issued a statement at the end of April 2020 recommending that:	US – LIBOR transition milestones The Alternative Reference Rates Committee (ARRC) released this recommended timeline in April 2020 for market participants transitioning away from USD LIBOR business.		HK – LIBOR transition milestones HKMA issued a circular on 23 July 2020 to provide guidance to FIs’ as well as transition milestones recommending that:
	Product	Target for Cessation of new use of USD LIBOR	
<ul style="list-style-type: none"> By end of Q3 2020, lenders should have non-LIBOR linked products available. 	<ul style="list-style-type: none"> Floating Rate Notes 	<ul style="list-style-type: none"> December 31, 2020 	<ul style="list-style-type: none"> FI’s Should be in the position to offer products referencing the LIBOR ARR’s from 1 January 2021. On 1 January 2021, fallback provisions should be included in all newly issued LIBOR-linked contracts that will mature after 2021. FI should cease to issue new LIBOR-linked products that will mature after 2021 by 30 June 2021.
<ul style="list-style-type: none"> After Q3 2020, all new and existing GBP LIBOR loans should include pre-agreed conversion terms or have an agreed arrangement for renegotiation. 	<ul style="list-style-type: none"> Business Loans Consumer Loans 	<ul style="list-style-type: none"> June 30, 2021 Mortgages: September 30, 2020 	
<ul style="list-style-type: none"> By end of Q1 2021, lenders should stop issuing any new GBP LIBOR loan products. 	<ul style="list-style-type: none"> Securitizations Derivatives 	<ul style="list-style-type: none"> CLOs: September 30, 2021 Other: June 30, 2021 June 30, 2021 	

Note: Despite the disruptions caused by the COVID-19 outbreak, the central assumption that firms cannot rely on LIBOR being published after the end of 2021 remains unchanged.

Replacing LIBOR

In order to achieve the FCA's target of replacing LIBOR, Alternative Reference Rates (“ARRs”) have been identified for each of the five LIBOR currencies therefore reducing the need for expert judgement by basing the ARR on robust underlying transactional data.

Currency	Selected Rate	Working Group	Administrator	Type
Pound Sterling, GBP	Sterling Overnight Index Average (SONIA)	Working Group on Sterling Risk-Free Reference Rates	Bank of England (BoE)	Unsecured
US Dollar, USD	Secured Overnight Financing Rate (SOFR)	Alternative Reference Rates Committee (ARRC)	Federal Reserve Bank of New York	Secured
Euro, EUR	Euro Short-Term Rate (€STR)	Working Group on Risk-Free Rates	European Central Bank (ECB)	Unsecured
Swiss Franc, CHF	Swiss Average Rate Overnight (SARON)	National Working Group on CHF Reference Rates	SIX Swiss Exchange	Secured
Japanese Yen, JPY	Tokyo Overnight Average Rate (TONAR)	Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks	Bank of Japan (BoJ)	Unsecured

Consequences for other IBORs

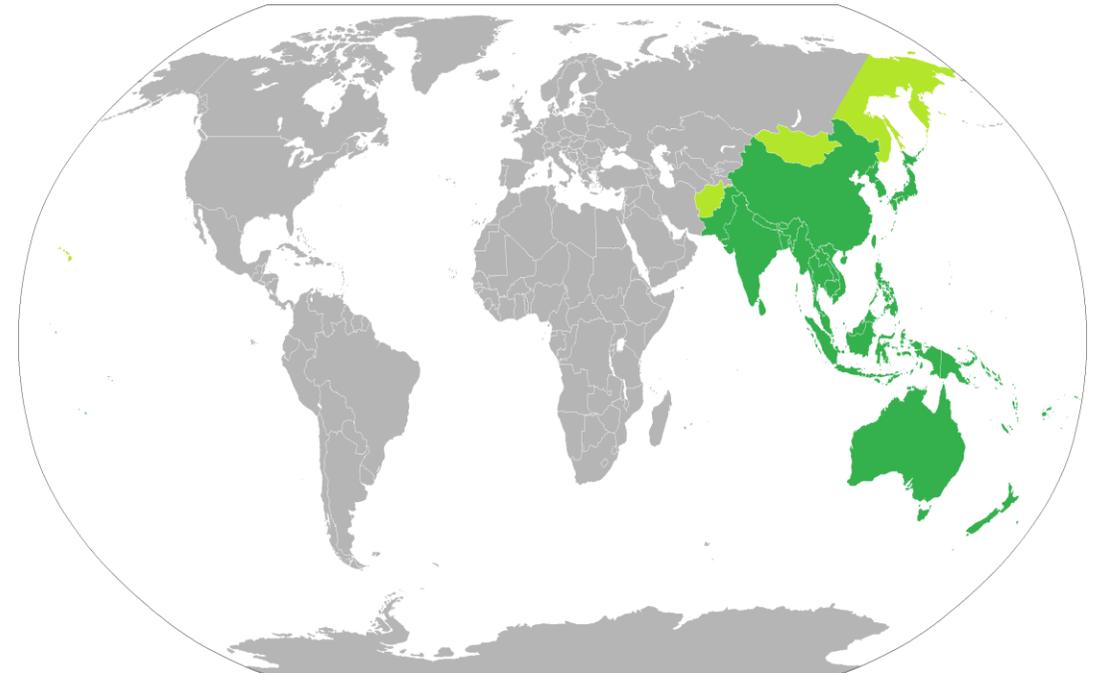
Key Asian Benchmarks

A number of key Asian benchmarks are synthetic benchmarks derived by applying a forward FX curve to the USD LIBOR curve. When USD LIBOR is no longer available after the end of 2021, the sustainability of these benchmarks is in doubt.

Key benchmarks are: **SOR** (Singapore); **THBFIX** (Thailand); **MIFOR** (India) and **PHIREF** (Philippines).



Planning for the cessation of LIBOR is underway by the respective administrators of these benchmarks. Some have replacement rates for new transactions identified and transition timelines in place (**SOR** and **THBFIX**), whereas others are yet to identify the replacement rates. As a result, any organization planning for the cessation of LIBOR should also consider its exposure to any of these four affected IBORs.



Practical Implementation Checklist

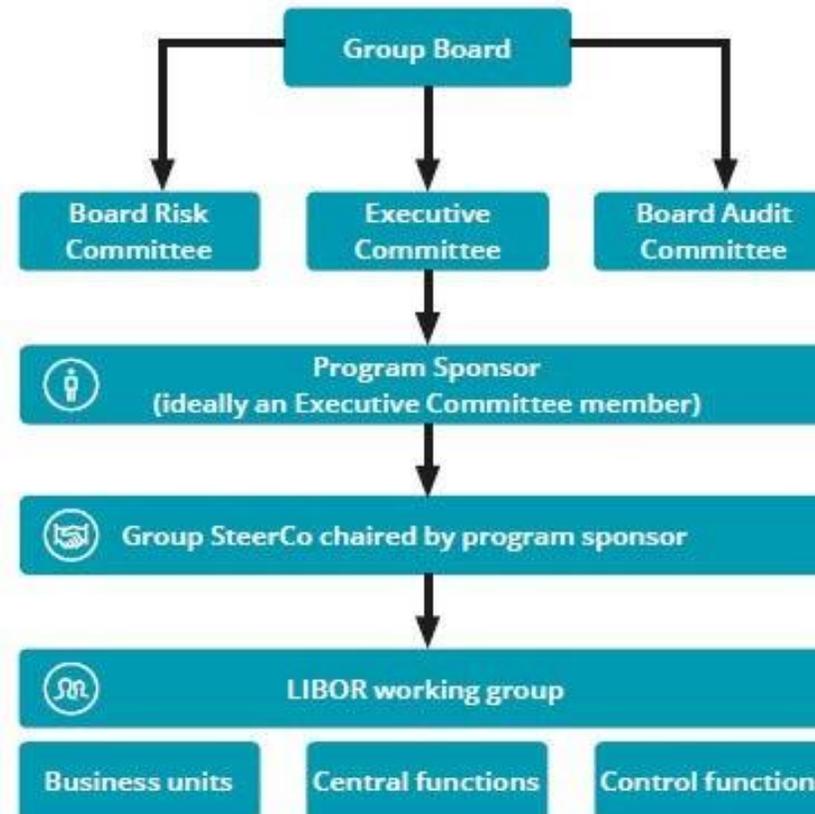
Drawing upon a combination of practical experience from organizations that have initiated transition programs, as well as emerging guidance from the regulatory community, FIs can make reference to the following key considerations when performing their own assessment of the impact from benchmark rate reforms:

Key Steps



1. Program Governance

Key Considerations



IBOR Transition Program Governance Structure
(For illustration purposes only)

Practical Implementation Checklist

Drawing upon a combination of practical experience from organizations that have initiated transition programs, as well as emerging guidance from the regulatory community, FIs can make reference to the following key considerations when performing their own assessment of the impact from benchmark rate reforms:



Key Questions to Consider in LIBOR Transition

- What is the financial exposure to LIBOR?
- What are the differences between LIBOR and ARR?
- What are the Legal & Contractual Implications?
- What are the operations and technology impact to the FI?
- Who is responsible for developing and providing internal training as well as client communications?
- How is conduct risk being monitored?

Consequences of Inaction

- Operational implications of being unable to book new rates when approached by clients to transition existing contracts
- Conduct and legal risk of continuing to sell LIBOR linked products to clients
- Uncertainty over payment obligations and even legal status of LIBOR-linked contracts
- Issues with hedge effectiveness should the organization not be ready to transition its hedging relationships

Contact



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Key Resources

- Financial Conduct Authority: [Conduct risk during LIBOR Transition – Questions and answers for firms about conduct risk during LIBOR transition](#)
- Alternative Reference Rates Committee: [Practical Implementation Checklist for SOFR Adoption](#)
- Alternative Reference Rates Committee: [Buy-Side/Asset Owner Checklist](#)
- Alternative Reference Rates Committee: [Recommended Best Practices for Completing the Transition from LIBOR](#)
- The Working Group on Euro Risk-Free Rates: [Checklist on the transition from EONIA to the €STR](#)
- The National Working Group on Swiss Franc Reference Rates: [Checklist: Operational Readiness](#)

Other relevant websites include:

- <https://www.newyorkfed.org/arrc/index.html>
- https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/WG_euro_risk_free_rates/html/index.en.html
- https://www.snb.ch/en/ifor/finmkt/finmkt_benchm/id/finmkt_reformrates
- https://www.boj.or.jp/en/paym/market/jpy_cmte/index.htm/
- <https://www.bankofengland.co.uk/markets/transition-to-sterling-risk-free-rates-from-libor>
- <https://www.fsb.org/work-of-the-fsb/policy-development/additional-policy-areas/financial-benchmarks/>
- <https://www.fca.org.uk/markets/libor>
- <https://www.bot.or.th/Thai/FinancialMarkets/Pages/ReferenceInterestAndEndOfUseLIBOR.aspx>
- <https://www.abs.org.sg/benchmark-rates/about-sora>
- https://www.tma.org.hk/en_market_LIBOR.aspx
- https://afma.com.au/ibor_transformation_working_group
- <https://www.isda.org/2020/05/11/benchmark-reform-and-transition-from-libor/>
- <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/benchmark-reform/>