

Evolving LIBOR

Managing the transition to new Risk Free Rates



LIBOR - what is changing?

Interbank offer rates ('IBORs') are systemically important benchmarks underpinning many contracts within the financial sector globally. There are estimated to be over \$370tn contracts currently referencing them from US retail mortgages to derivative contracts and corporate loans.

Following the OSSG recommendations in 2014 to move the industry towards new risk free interest rate reference rates ('RFR's') the industry has been developing proposed new reference rates. In 2017 the FCA's confirmed that it will no longer compel banks to submit data to LIBOR post 2021 resulting in a clear impetus and need to implement these alternative RFR benchmarks globally.

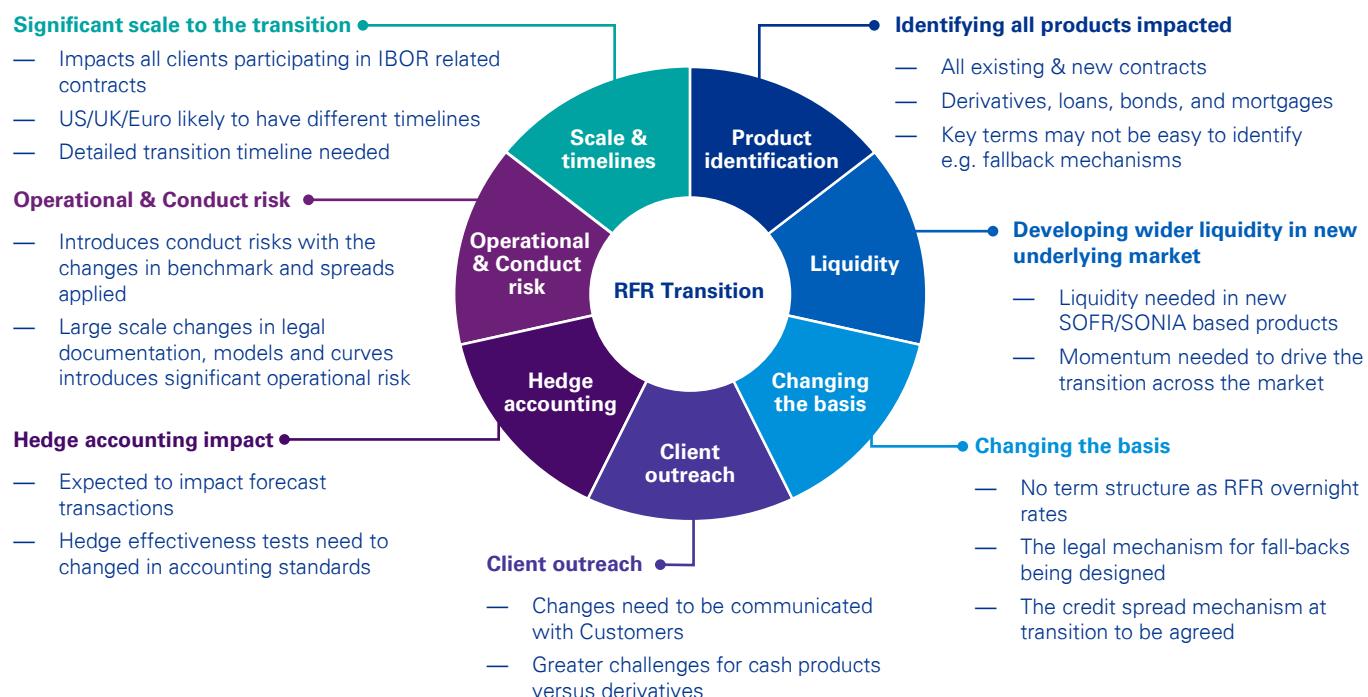


To date US, UK, Swiss and Japanese Working Groups ('WG') have developed SOFR, reformed SONIA, SARON and TONA. The EU WG is yet to finalise its RFR.



The RFR's have been designed to be based on transactions (where practical) with minimised reliance on expert judgement and are based on overnight rates.

What are the key challenges?



What do firms need to do?

Firms need to assess the impact of the transition across their products, clients and infrastructure. The impact on products will need to be considered from front to back across an organisation covering key functions: Sales & Trading, Operations, Risk & Valuations, Treasury, Legal and Compliance.

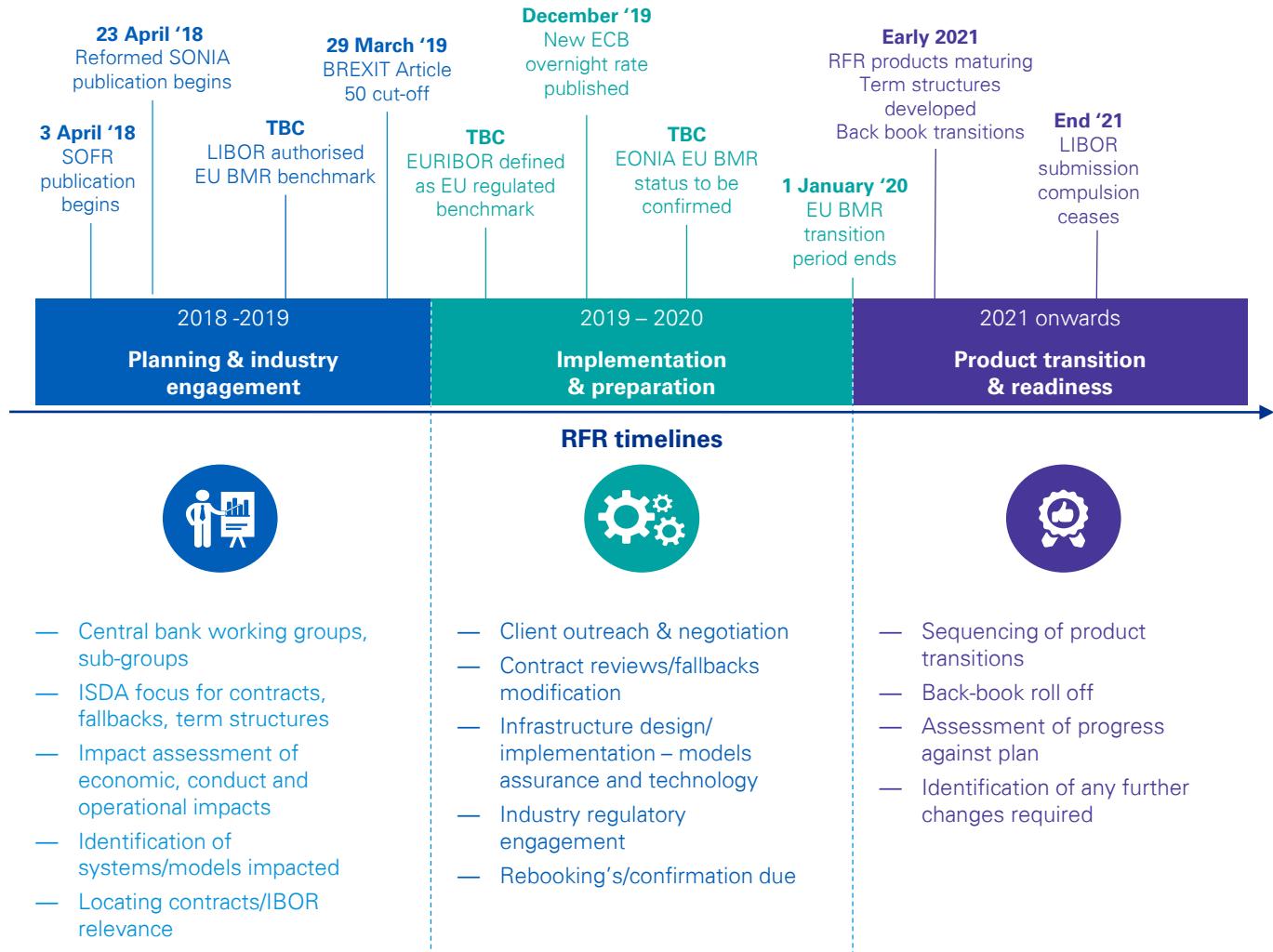
The differences in approach and timing across the US, UK and Europe will require a well coordinated programme of activities to ensure changes are joined up.

RFR Transformation Programme	RFR Governance & Oversight
	<ul style="list-style-type: none">— Project management/governance control of all workstreams ensuring delivery of RFR transformation programme— Wider impact assessment across the organisation → prioritisation— Managing diverse timelines (Geography/Asset/Product Class)— Manage external stakeholders e.g. regulators/customers



Developing a clear timeline?

There is a clear impetus to make the change up to 2021. Timelines are being developed, but there are going to be variations across jurisdictions.



Outstanding industry building blocks

Clear & detailed industry timeline	A clear timeline and approach has not been defined for an industry transition. Need to bring in all regions, products and industry in line (big bang).
Regional approaches	There are clear differences by RFR region – US, UK, Europe, Japan, Switzerland taking slightly different approaches and are at slightly different stages of implementation
Liquidity	Organisations need to maintain and implement liquidity to used new RFRs e.g. industry created RFR products need hedging.
Education	Bring wider market participants, industry and end clients up to speed.
Technical issues (fallback, tenor & credit spread)	The new RFR's are overnight indices and currently have no term structure unlike IBOR's. Whilst term structures potentially rebuild for new products, a mechanism is needed to ease back book adoption.
Market infrastructure	The exchanges and clearing houses are starting to build out RFR products and services in certain jurisdictions.

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