

# Benchmarks



## Differentiating IBOR Benchmark Initiatives

### IBOR Transition

- Led by the Risk Free Rate Working Groups (Public sector-Private sector)
- Selection of nearly risk free rate (RFR) as alternative to IBOR
- Voluntary transition process during the lifetime of IBOR
- For any amendment of legacy portfolio only, spread may be required to compensate for lack of IBOR-style bank credit premia in RFR
- On-going debate on whether term products need developing for the RFR

### IBOR Fallbacks

- Led by ISDA at request of the FSB OSSG
- Improve contractual robustness of derivatives referencing an IBOR
- ‘Emergency’ provisions that continue to reference IBORs, triggered by the permanent discontinuation of the relevant IBOR
- Fallback to a nominated alternative RFR plus a credit spread and subject to adjustments to address term fixings (as applicable)
  - Spread designed to compensate for lack of IBOR-style bank credit premia in alternative RFR.
  - Need to address lack of IBOR-style forward-looking term structure in alternative RFR.

### Article 28(2) European Benchmark Regulation

- Led by ISDA for derivatives
- Implementation of IOSCO principles in EU law
- Requires supervised users to plan for cessation or material change of any benchmark (large or small across all products) and reflect in contracts
- Nomination of alternative rates where feasible and appropriate
- Uncertain scope at present: only if traded on venue or if similar to instruments on venue? What if similar instruments are subsequently traded on venue? Novations into EU?

Interaction of the IBOR Fallbacks and EU Fallbacks under discussion

## ISDA is working on an initiative to implement fallbacks for certain key IBORs in derivatives documentation

- **FSB OSSG Mandate.**

At the request of the FSB OSSG, ISDA is leading an initiative to determine fallbacks for certain key IBORs that would apply if an IBOR is permanently discontinued. The selected fallbacks would be written into derivatives contracts that reference those key IBORs

- **Selection of Fallback Rates.**

The fallback rates are expected to be the RFRs selected by the public-private sector working groups

- **Triggers.**

Whether the IBOR is permanently discontinued would be based on objective pre-defined triggers (eg, a public statement by an IBOR administrator that it will cease publishing the relevant IBOR permanently or indefinitely, and there is no successor administrator)

- **New Trades vs Legacy Trades.**

The fallbacks will apply to trades entered into after the fallbacks are incorporated into the ISDA definitions for the relevant IBORs. ISDA is also considering mechanisms that would allow market participants to efficiently incorporate the fallbacks into existing contracts that reference IBORs

- **Identify impediments to successful implementation of fallbacks.**

## ISDA Fallback Working Groups in co-ordination with the FSB OSSG

ISDA GBP/EUR/CHF Benchmark  
Working Group

ISDA JPY Benchmark Working  
Group

ISDA APAC Benchmark Working  
Group (AUD/SGD/HKD)

ISDA USD Benchmark Working  
Group

ISDA Benchmark Fallbacks  
Spread Calculation and Term  
Fixing

## ISDA Working Group Objectives

Identify triggers for  
fallback

Identify alternative rates  
and other fallback  
mechanisms

Identify strategy for  
successful fallback  
implementation

Amend the 2006 ISDA  
Definitions so that  
fallbacks will be  
incorporated into new  
trades

Create a protocol to  
incorporate the fallbacks  
into legacy trades

## Issues to be resolved

- RFRs that do not yet exist
- Credit Spread
- Term Fixings
- Basis risk between products (e.g. swaps, loans, bonds)
- Basis risk between derivative products (cleared vs non-cleared, linear vs non-linear)
- ISDA intends to conduct broad market outreach for education and decision-making before implementing fallbacks for derivatives

## Potential Credit Spread Methodologies

### Credit Spread Criteria:

- Eliminate or minimize value transfer at the time the fallback is applied
- Eliminate or minimize any potential for manipulation
- Avoid distortion due to market stress at the time the fallback is applied.

### Potential Credit Spread Methodologies:

Various possibilities being examined (further suggestions welcomed) break down into two basic types:

- Spreads derived from the forward curve at or around the time of cessation
- Spreads based on historic mean values

### Other issues:

Questions to be answered include the identity of a vendor to calculate and publish the credit spread and sources of data to be used

### Term Rate Issue

- ISDA WGs have been asked by the OSSG not to wait for forward-looking term reference rates that might be developed by the RFR Working Groups – the fallbacks need to be implemented as soon as possible
- Limited number of alternatives identified, such as compounding the overnight rate for the relevant period in arrears. Alternatives identified to date may be problematic for some derivatives users. Further suggestions welcomed

ISDA, AFME, ICMA, SIFMA and SIFMA AMG are working on a comprehensive study that will propose potential solutions to identified challenges in transitioning from IBORs to RFRs

- The Trade Associations have begun a comprehensive project to analyze how IBORs are currently used across financial markets, including markets for derivatives, loans, mortgages and bonds. The analysis will inform and support transition planning
- The IBOR transition project has three parts:
  - A benchmark transition **roadmap** that outlines how the IBORs are used, describes the reform efforts to date and outlines preliminary challenges to transitioning away from IBORs
  - A global **survey** of buy- and sell-side institutions and infrastructure providers to gather input on transition planning readiness and to gauge how firms are approaching the various challenges across a range of products and functional areas. The survey will also ask for input on potential solutions to these challenges. The survey will launch on February 26<sup>th</sup>
  - A final **report** will analyze the survey results and propose potential solutions for market transitions from IBORs to RFRs. It is expected to both build on and inform the ongoing work of the public-private sector RFR working groups