LIBOR: Be prepared!





The Financial Conduct Authority (FCA) announced that the LIBOR interest rate benchmark is to be phased out as of 31 December 2021.

Consequently,

Management Companies and Asset Managers should start assessing potential impacts on their products and operating models.

- Since 2014, **regulatory working groups** across the globe have been working to **identify alternative benchmark rates**, based more firmly on transaction data, and develop transition plans to these new rates
- However, the transition roadmaps across regions remain unclear and inconsistent
- LIBOR and Reference Rate Reform will have a significant commercial and operational impact on financial firms, including challenges around pricing, funding, risk management, contract management and many others areas/fields
- Besides LIBOR (London Interbank Offered Rate), other IBORs (Interbank Offered Rates) exist in the market, such as EURIBOR (European Interbank Offered Rate) and TIBOR (Tokyo Interbank Offered Rate)

| Existing IBOR rate(s) | Proposed alternative benchmark | Borrowing Type | Regulatory working groups |
|-----------------------------|--------------------------------------|-------------------|--------------------------------------------------------------------------------------|
| GBP LIBOR | Reformed- SONIA | Unsecured | Bank of England's Working Group on Sterling Risk Free Reference Rates |
| USD LIBOR | SOFR | Secured | Alternative Reference Rates Committee (ARRC) |
| EUR LIBOR, EURIBOR | ESTER | Unsecured | European Working Group |
| CHF LIBOR | SARON | Secured | National Working Group on Swiss Franc Reference Rates |
| JPY LIBOR, TIBOR | TONAR | Unsecured | Japanese Study Group on Risk Free Reference Rates |

LIBOR Reform timeline



Challenges for the Luxembourg based asset management industry and services

Tax, Accounting and other impacts

- Identify tax impact due to reforminduced portfolio re-allocations (e.g. closing & opening of derivatives positions)
- Identify accounting impact (e.g. due to valuation changes, principles such as hedge accounting)
- Analyse impact on cash balances w/3P providers (e.g. custodian, collateral manager, clearing broker, FX hedging)

Product and Fund Strategy

- Define catalogue of funds/ products that provide exposure to Reference Rate Reform
- Assess potential remediation options for these funds/products (e.g. with respect to overall investment strategy, set up of new products)
- Identify options for new products and services

Valuation and Risk Models

- Analyse economic impact on valuations solely from switching to new reference rates
- Define approach for minimising adverse economic impacts or windfall profits for legacy positions
- Analyse functional guidance from existing systems in the course of Reference Rate Reform (e.g. in risk systems)
- Ensure **availability of data access** to required time-series

Performance & Benchmarks

- Assess performance impact of portfolios having exposures to products being affected by the IBOR reform
- Analyse impact on existing performance calculation techniques/methodologies
- Identify required benchmark changes of funds (e.g. when benchmark refers to LIBOR + "x" bps)



Reference Rate Reform transition challenges

Contract Discovery and Remediation

- dentify all contracts with direct (LIBOR indexed) or indirect provisions (e.g. deal contracts, lease contracts)
- Define a proper legal wording (including transition clauses) and evaluate existing fallbacks/provisions (e.g. side letters)
- **Define timeline** for amending identified contracts
- **Leverage industry efforts** for consistent remediation

Guidelines and Fund Documents

- Identify required guideline changes and align with PM, CAM, and Legal on relevant amendments
- Establish timeline for incorporating guideline changes in compliance systems
- Identify fund documents that require amendments (e.g. fund prospectus, KIDs) and determine relevant timelines

Market Liquidity

- Monitor liquidity levels of relevant IBORs in the course of their phase-ou
- **Conduct liquidity impact analyses** of portfolios with "new" reference rates (incl. hedging relationships)
- Align timing of migration of funds/ holdings to new reference rates and phase in trading at new rates

Market Outreach

- Develop engagement approach and negotiation strategy across entities and regions
- Coordinate client outreach across entities and regions (e.g. when portfolio impact is identified)
- Monitor political & regulatory developments, and liase with local institutions
- Set up **Q&A database** and **education** material

Project Approach



Scoping

Define the project and mobilise the organisation:

- Training and awareness of stakeholders
- Review scoping, definition and prior work
- Identify the key stakeholder by service
- Kick-off and workshops with stakeholders

Impact assessment

- a. Identify the area / services that might be impacted
- b. Conduct gap analysis between current setup and requirements
- c. Analyse impact on asset/ portfolio value and subsequent impact on fee structure
- d. Perform documentation analysis to identify necessary changes

Prioritisation and roadmap

- a. Prioritise the required changes and implementation needs from the easiest to the more complex
- b. Develop a project approach for the implementation phase
- c. Present results to senior management

Governance

Stakeholder education

Project Steering & Management

Stakeholder Management & ad-hoc support Provide guidance and insights from regulators, associations & market developments

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