

Minutes of LIBOR Trade Association Working Party meeting
held on 26 April 2023
via teleconference

Present

ACT
AFME
APLMA
ICMA
ISDA
LMA
LSTA
TACT

1. Introduction

The purpose of the meeting was for the trade associations to provide updates on any developments in respect of LIBOR transition since the last meeting.

2. TACT update

In relation to US dollar LIBOR, TACT is particularly involved with securitisation, and has been tracking the transition progress with respect to securitised products and CDOs. The process for collating transaction data on the performance and rate switch of such products involves compilation of a standard form. TACT added that this has generally been hard to follow because the relevant deadlines have not approached yet.

TACT has also been working on the transition of sterling LIBOR deals. TACT noted that it had recently heard of a few deals that were going to get caught by the discontinuance of 1- and 6-month synthetic sterling LIBOR on 31 March 2023, but that these transitioned just in time. Some reasons for the delay in transition include a combination of flaws in the system, for example, notices not getting to noteholders and custodians not passing them on.

Further, TACT is aware of deals that will need to be updated in light of the US dollar LIBOR deadline. In order to get past the finishing line, TACT will be urging noteholders to carry on with the transition as US legislation on its own will not suffice in transitioning outstanding contracts.

3. LSTA update

The LSTA noted that it had three main updates in respect of US dollar LIBOR transition to share with the other trade associations: (i) overall progress of legacy transition; (ii) use cases for synthetic dollar LIBOR; and (iii) the update to the ARRC's term SOFR scope of use recommendations.

In relation to US dollar LIBOR transition progress, it was noted that leveraged loans transition has picked up considerably together with amendment fallbacks activity. The LSTA expects this to continue in the coming weeks as the June 2023 deadline approaches. The latest data show that over 50% of leveraged loans are now linked to SOFR, and that over a third of the outstanding ones are linked to hardwired fallback language. In terms of credit adjustment spreads, a range of approaches are being seen, including 10bps flat across all tenors and also the ISDA spreads as set out in the ARRC fallback language.

On synthetic US dollar LIBOR, the use cases for this in the US market are not very wide – it will have only limited application. There is some confusion in the US loan market on this, notwithstanding the fact that most remaining LIBOR-referencing loans have fallback language

embedded which triggers on non-representativeness, which means that most contracts will not need to resort to a synthetic methodology. Therefore, the LSTA is continuing its efforts to educate market participants on the limited application of synthetic US dollar LIBOR.

In relation to Term SOFR use cases, the ARRC published a summary and update of its term SOFR scope of use recommendations. The LSTA noted that this represents a positive development for the hedging space. There has been a large build-up of hedges, as dealers have assisted clients in hedging term SOFR loans and so assumed term SOFR risk they need to unload. While inter-dealer trading continues to be prohibited, the ARRC's update will now permit term SOFR-SOFR basis swaps between dealers and non-dealer market participants, even when the market participant does not hold term SOFR cash assets that they are seeking to hedge.

However, the LSTA noted that the update could also potentially constitute less of a positive development for loans. The reason for this is that in the process of updating its term SOFR use case recommendations, the ARRC also updated the definition of "business loan" and clarified that a business loan is one which is not classified as a public security under rule 144A. The LSTA noted that while this would seem logical, there is also a case (*Kirschner v JPM*) currently being heard in the US debating whether Term Loan Bs are securities and, if so, subject to federal securities laws. If the case decides that Term Loan Bs are securities, this would mean that they would not fall within the ARRC's definition of business loans and would mean they fall outside the use case for term SOFR.

4. LMA update

The LMA noted that it has not yet received much feedback in relation to the ARRC's update on its term SOFR scope of use recommendations and its impact on hedging. On the FCA's decision on synthetic US dollar LIBOR, the LMA has also not received much feedback from members, although the general consensus is that the decision has been helpful. It was added that the LMA will hold a Developing Markets Conference on 24 May 2023, where it will be interesting to gather views and comments from emerging market participants in relation to legacy transition. LIBOR transition in the emerging markets continues to be a key area of focus for the LMA giving the continuing need for education.

The LMA noted that it published a note on EURIBOR fallbacks for its members. The note follows a meeting of the Working Group on Euro Risk-free Rates in December 2022, where concerns about the loan market not adopting robust fallbacks to EURIBOR were expressed. The note seeks to remind members that LMA documentation provides options for robust fallbacks mechanisms, and that there are also term rates available to users.

The LMA is also engaged in the transition of other IBORs globally, and members have an interest, for example, in the Canadian, Polish and South African loan markets. On the South African front, the LMA is continuing to give its support on the South African Rand transition. It was noted that the LMA is part of a JIBAR transition working group that is currently producing two separate consultation papers for transition rates, namely one aimed at loans and one for bonds.

5. ISDA update

ISDA noted that the LSTA and the LMA covered all the recent market updates that are also applicable to derivatives, i.e. the ARRC's update of its term SOFR use cases and the FCA's decision on synthetic US dollar LIBOR. It was further noted that the last few weeks have overall been positive for US dollar LIBOR transition, with further clarity and also an increase in queries.

A couple of weeks ago, ISDA held a webinar together with Bloomberg, who publish the ISDA fallback rates and spreads, CME, LCH and Eurex. The webinar, which is available to watch on the ISDA website, went through the mechanics of fallbacks and the CCPs went through the process of transitioning away from US dollar LIBOR for cleared derivatives. ISDA added that there are some

nuances in terms of different CCPs and transition timeline of derivatives, which are explained comprehensively in the webinar. Further, ISDA is holding a weekly Q&A call with members, which is likely to increase in popularity in the next few weeks as the US dollar LIBOR deadline gets closer. Non-members can attend and recordings are available. ISDA will also be hosting a panel with David Bowman and Tom Wipf at its AGM. ISDA also published a blog post looking at the ARRC's updates to its term SOFR use cases (although ISDA is neutral on term SOFR use in the derivatives market).

Further, ISDA is also working on other IBORs globally that are key to the derivatives market, such as in Poland and South Africa. ISDA expects work on IBORs in other jurisdictions to continue for the next couple of years.

The LMA highlighted that the LMA also produces South African law documentation, which means that the JIBAR transition is a relevant development for the LMA to monitor. In addition, the LMA is also looking to update its domestic interest rate benchmark schedule in due course, and has recently published a compounded CORRA schedule.

6. ICMA update

ICMA is considering the FCA's decision on synthetic US dollar LIBOR and all the recent regulatory announcements from the bond market's perspective. Bond market participants are resigned to the end date and the announcement helps provide clarity. ICMA is working on collating data in respect of bonds impacted by the US dollar LIBOR transition and liaising with the FCA as to the size of the task ahead. It was noted that ICMA has reiterated the need to the FCA of a robust transition process. ICMA is also looking into issues around litigation risk and other residual tail risks, including the possibility that any litigation risk arising out of synthetic LIBOR will lie with the FCA rather than with bondholders. ICMA is also tracking the remaining progress of sterling LIBOR transition and what remains outstanding on the US dollar LIBOR side. Finally, ICMA is continuing to keep a watching brief on RFR conventions.

The LMA noted that data collection on outstanding loans is a rather difficult exercise for the EMEA loan market given that the market is private (and tracks issuance rather than volumes of outstanding loans). The LMA suspects there is not much transition activity on the developing markets side, and is concerned that the recent synthetic US dollar LIBOR announcement may slow the pace of transition for some market participants. The LMA added that litigation risk is also an interesting issue; whilst the UK has legislation dealing with contractual continuity, other countries may not have similar legislation in place and there may be a risk here of participants arguing that synthetic LIBOR is not LIBOR (although query the incentive for that when synthetic LIBOR is term SOFR plus the well-publicised ISDA spread).

7. APLMA update

The APLMA recently conducted a LIBOR transition survey, which did not receive many responses as APAC market players seem to have a tendency not to share data on their transition progress.

On the main trends the APLMA is observing in the APAC region, which is mainly a dollar-denominated market, term SOFR is emerging as the preferred methodology in some deals, while compounded SOFR is used in others. It was noted that overall the ARRC's LIBOR legacy transition playbook has worked well. The APLMA noted that it gathered some anecdotal evidence that some borrowers are considering waiting until synthetic US dollar LIBOR before remediating their loans. Further, the credit spread adjustment tends to be fixed in remediation deals, while it is either negotiated as separate or incorporated in the margin in new deals. It was noted that the APLMA's waterfall fallback provisions provide for either cost of funds or central bank rate. As far as the APLMA is aware, parties are using both options, with no clear preference, and noted that they differ from the fallbacks under LMA documentation.

The APLMA further commented that the existence of synthetic US dollar LIBOR will be a relief for many.

Finally, the APLMA noted that the Monetary Authority of Singapore has issued some guidelines for the Singapore loan market that recommends compounded rates (either NCCR or CCR). Singapore is a small market, but this is a different route from the one taken in the US.

8. AFME update

AFME noted that it did not have many updates to share. AFME is mainly continuing to monitor developments in the UK, such as the FCA announcements, and participates in the sterling bond market sub-group meetings. AFME has not been made aware of any concerns with regard to US dollar LIBOR transition from its members. Further, AFME will continue working on a monthly LIBOR transition update published by GFMA that contains contributions by both SIFMA and AFME.

9. ACT update

The ACT has not received much feedback from members with regard to the outstanding transition in the UK market. The feedback which has been received, however, highlights that the FCA's announcement on synthetic US dollar LIBOR has been welcomed in the UK. The ACT further noted that there is not widespread use of term SOFR in the UK market, as it is more convenient to use overnight SOFR to align with sterling transactions. The general consensus from the market is that participants are carrying on with the transition.

10. AOB

The LMA thanked members of the Working Party for their contributions and sought feedback as to whether it would be more helpful to schedule the next call before the end of June or during the second week of July. Members agreed to set the next meeting for July 2023, as it provides an opportunity to discuss any potential issues that may have arisen with US dollar LIBOR transition.

The ACT asked whether these calls should be extended beyond July, given that the transition efforts in the other IBORs around the world are likely to continue for the next few years. The LMA suggested these calls could continue for a more restricted group of people who have an interest in these markets. Members agreed to discuss this further during the next meeting in July 2023.