

IBOR Transition

Highlights

The London Interbank Offer Rate (LIBOR) is one of the Interbank Offer Rates (IBOR) used globally to set the benchmark rate for a wide range of financial products including loans facilities, derivatives and bonds and some of the tenors of LIBOR will be discontinued by 31 December 2021. Having regard to this discontinuation, **BOCHK Jakarta Branch will no longer issue any new LIBOR contracts after 31 December 2021.**

Furthermore, to understand more about the IBOR Transition, please see below information.

Overview

What are IBORs?

Interbank offered rates (**IBORs**) include the London Interbank Offered Rate (**LIBOR**), the Euro Interbank Offered Rate (**EURIBOR**), the Euro Overnight Index Average (**EONIA**) and certain other rates.

IBORs serve as widely accepted benchmark interest rates that represent the cost of short-term unsecured borrowing by large banks.

Over time, IBORs have grown in relevance, with some estimates suggesting they serve as interest rate benchmarks for over US\$350 trillion in financial products, including bonds, derivatives, mortgages and other loans. IBORs are used by financial institutions, corporations and governmental entities, as well as by consumers. IBORs are used not only as benchmarks in financial contracts, but also as the basis for many asset valuations.

LIBOR is used in financial products denominated in USD (US Dollar), EUR (Euro), GBP (British Pound), JPY (Japanese Yen) and CHF (Swiss Franc).

Certain currencies also use specific non-LIBOR interest rate benchmarks such as EURIBOR and EONIA for EUR, the Tokyo Interbank Offered Rate (**TIBOR**) for JPY, the Bank Bill Swap Rate (**BBSW**) for Australian Dollars, the Canadian Dollar Offered Rate (**CDOR**), the Hong Kong Interbank Offered Rate (**HIBOR**) for Hong Kong Dollars and the Singapore Interbank Offered Rate (**SIBOR**) for Singapore Dollars.

Discontinuation of LIBOR

Regulatory authorities and working groups in several jurisdictions, including the International Swaps and Derivatives Association (**ISDA**), the Sterling Risk-Free Rates Working Group, the Working Group on Euro Risk-Free Rates and the Alternative Reference Rates Committee (**ARRC**), have been discussing alternative benchmark rates to replace the IBORs. These working groups are also considering how to support a transition to alternative rates and the development of new products that refer to them.

The UK Financial Conduct Authority (FCA) has stated that after 2021, it will no longer compel banks to submit rates used for the calculation of LIBOR. This means that LIBOR will very likely be discontinued at the end of 2021, if not sooner. Regulators globally have emphasized that market participants must start transitioning away from the use of IBORs and adopt alternative benchmark rates.

Aiming for a smooth transition for the existing LIBOR contracts, ICE Benchmark Administration consulted the industry regarding the “potential extension of some LIBOR cessation dates to June 2023” in November 2020 with the result published on 5 March 2021. Following this, the FCA announced that all LIBOR settings will cease or no longer be representative, as below:

| LIBOR Currency | LIBOR Tenors | Final Publication Date |
|--------------------|---|------------------------|
| EUR, CHF, GBP, JPY | All tenors | 31 December 2021 |
| USD | 1 week and 2 months | 31 December 2021 |
| USD | overnight and 1, 3, 6, and 12 months tenors | 30 June 2023 |

IBOR Transition to Risk-free Rate (RFRs)

Regulators and working groups in several jurisdictions have identified replacement benchmarks and have developed strategies for transition. RFRs in the jurisdictions of each LIBOR currency have been judged to comply with new regulatory standards governing financial benchmarks that have been adopted since the 2008-era financial crisis.

These standards are derived from principles set forth by the International Organization of Securities Commissions (IOSCO).

RFRs are calculated based on information gathered from large volumes of actual transactions, often taken from regulated exchanges or other central clearing platforms, and do not rely on the expert judgment of panel banks. In this regard, RFRs have been judged to be more robust and transparent than LIBOR, and less susceptible to potential manipulation.

Certain jurisdictions have adopted a multiple rate approach, which sees the jurisdiction's existing IBOR being reformed and to exist alongside a new RFR for the currency in such jurisdiction. The multiple rate jurisdictions are set out in the table below, and include the Euro-zone, Hong Kong, Japan and Singapore.

Certain examples of IBORs which are either being replaced or reformed are set out in the table below.

| Jurisdiction | Currency | Multiple rate jurisdiction? | IBOR | RFR |
|--------------|------------|-----------------------------|----------------------------------|---|
| US | US Dollars | No | LIBOR <i>(being replaced)</i> | Secured Overnight Financing Rate (SOFR) |

| | | | | |
|-------------|--------------------|-----|---|---|
| Euro-zone | Euro | Yes | LIBOR <i>(being replaced)</i> | euro Short-term Rate (€STR) |
| | | | EONIA (until 3 January 2022 (when EONIA will cease), EONIA has been recalibrated to refer to €STR plus a fixed spread of 8.5 basis points) | |
| | | | EURIBOR <i>(reformed)</i> | |
| UK | Sterling | No | LIBOR <i>(being replaced)</i> | Sterling Overnight Index Average (SONIA) |
| Japan | JPY | Yes | LIBOR <i>(being replaced)</i> | Tokyo Overnight Average Rate (TONAR) |
| | | | TIBOR | |
| | | | Euroyen TIBOR <i>(may be discontinued)</i> | |
| Switzerland | CHF | No | LIBOR <i>(being replaced)</i> | Swiss Average Rate Overnight (SARON) |
| Australia | Australian Dollars | Yes | BBSW | Reserve Bank of Australia Interbank Overnight Cash Rate (AONIA) |
| Canada | Canadian Dollars | Yes | CDOR | Canadian Overnight Repo Rate Average (CORRA) |

| | | | | |
|-----------|-------------------|-----|------------------|--|
| Hong Kong | Hong Kong Dollars | Yes | HIBOR | Hong Kong Dollar Overnight Index Average (HONIA) |
| Singapore | Singapore Dollars | Yes | SIBOR (reformed) | Singapore Overnight Rate Average (SORA) |

Key differences/comparison between RFRs and LIBOR/other IBORs

RFRs are different from LIBOR in three ways:

| | | LIBOR | RFRs |
|----|--------------------------------------|--|---|
| 1. | Tenor | Available in seven tenors (i.e. overnight/spot next; 1 week; 1 month; 2 months; 3 months; 6 months; and 12 months). | Not available for any tenor other than overnight . |
| 2. | Notice of payment | Forward-looking and is known in advance of any interest payment date. Published at the beginning of the relevant observation period. | Backwards-looking and the rate applicable to any day may only be known after that day. Published after the end of the overnight borrowing period. This may pose difficulties for parties who wish to have advance notice of the interest rate before interest payment date, to raise the necessary funds for interest payment. |
| 3. | Credit and term funding costs | reflect bank credit risks or term funding costs | do not reflect bank credit risks or term funding costs |

What market participants should do

All market participants should identify their own exposure to IBORs, and the need to undertake IBOR transition in their contracts and business relationships. Certain steps to consider include:

- conducting a review of all existing contracts to identify where references to IBORs may arise;

- considering what steps need to be taken from a legal, operational, risk, compliance accounting and tax perspective to ensure readiness for transition;
- engaging with counterparties and their own customers to facilitate transition of existing contractual arrangements to include appropriate fallbacks to alternative rates;
- remaining aware of industry and regulatory developments; and
- understanding the new RFRs and considering whether and when to enter into new transactions that utilize new RFRs.

For existing transactions that extend beyond 2021, customers may have to decide whether to replace LIBOR with the alternative benchmark in advance or to use "fallback" provisions that provide a mechanism for the replacement of LIBOR with an alternative benchmark if a trigger event occurs. According to Hong Kong Monetary Authority timeline, BOCHK Jakarta Branch is not allowed to issue any new Libor contracts after 31 December 2021.

Market participants should take similar steps with respect to other IBORs.

Trigger events for these fallbacks may differ, but frequently refer to either a cessation of an IBOR or a regulatory determination that, prior to actual cessation, the IBOR does not reflect underlying financial reality or is not sufficiently representative of the market (so called "pre-cessation" triggers).

There are industry efforts to standardize approaches across jurisdictions and financial products, although fallbacks may include different provisions across products such as different trigger events or a different fallback rate. Market participants should be aware of the possibility that a mismatch may exist between fallback provisions in related assets or financial products, which may have unintended or unforeseen consequences.

What could these changes mean for customers?

The changes arising from IBOR transition may affect a number of our products and services currently used by the customer or which the customer may use in the future. The impact will depend on various factors, such as:

- which particular IBOR is referred to in a product;
- the adjustments which need to be made to reflect credit and term differences between the relevant IBOR and the RFR;
- the nature and term of the product or contract;
- the date when any changes arising from IBOR transition take effect; and
- the nature of any fallback provisions in the particular contract, if any.

IBOR transition could have a number of effects on customers. These include, for example, changes to the value of products, the need to amend existing contracts, the possibility that products may no longer serve the purpose for which they were originally intended and making changes to existing operational processes and/or systems.

There may also be tax, regulatory, legal and accounting effects depending on a customer's particular situation.

The effect of IBOR transition may also vary depending on whether the relevant benchmark is being discontinued or reformed.

For More Information

BOCHK Jakarta Branch is actively monitoring developments on IBOR transition and assessing any changes which may need to be made to existing contracts, products and transactions. BOCHK Jakarta Branch will continue to provide more information as appropriate.

This information briefly summarizes the latest developments in the reform of the interest rate benchmark. The above information is not a complete statement regarding the subject related. This information is general in nature and are not intended and should not be relied upon as legal, regulatory, financial, tax, accounting, or other advice. Bank of China (Hong Kong) Limited Jakarta Branch makes no representations regarding the accuracy, completeness or timeliness of such information. There will be no notice from Bank of China (Hong Kong) Limited Jakarta Branch if there are any changes on this related subject. In particular, the preparation of this information did not take into account the objectives, financial situation or needs of any particular contracting party. Recipients of this information should consult their own independent professional advisers and/or conduct their own investigations on the potential risks of interest rate reform and the potential impact on their transactions with Bank of China (Hong Kong) Limited Jakarta Branch.