

LIBOR TRANSITION AND ADOPTION TO ALTERNATE REFERENCE RATE



Background



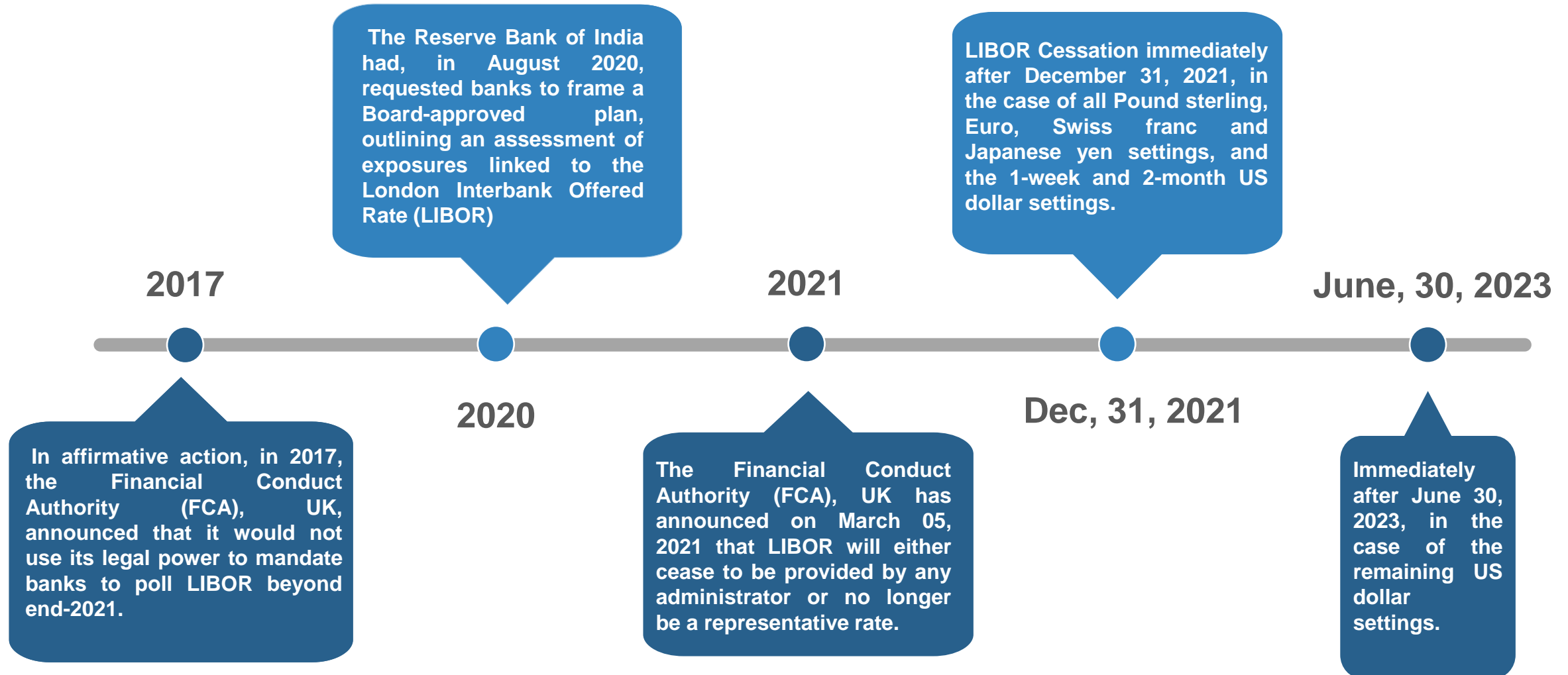
In International markets, lending and borrowing happens on an interest rate on a mutually accepted benchmark rate referred to as reference InterBank Offered Rates, or IBORs, with the London InterBank Offered Rate (LIBOR) being the most widely used IBOR. There are many such benchmark rates such as EURIBOR in Europe, HIBOR in Hong Kong, and MIBOR in India. However, LIBOR is the most preferred benchmark across the world.

LIBOR is an interest-rate average calculated from estimates submitted by the leading banks in London. Each bank estimates, what it would be charged were it to borrow from other banks. The resulting rate is usually abbreviated to Libor or LIBOR. It is the primary benchmark, along with the Euribor, for short-term interest rates around the world.

LIBOR rates are calculated for five currencies (USD, GBP, EURO, JPY, and CHF) and are currently produced in 7 tenors (Overnight/spot next, one week, one month, two months, three months, six months and 12 months) across 5 currencies.

The need for transition from LIBOR to nearly risk-free Alternate Reference Rates (ARR) arises due to the dwindling volumes of interbank unsecured term borrowing due to the structural changes in the financial markets, especially since the global financial crisis, meant that transaction-based submissions leading to LIBOR formation has significantly reduced and what is left are estimates and the Financial Conduct Authority (FCA), UK, announcement that it would not use its legal power to mandate banks to poll LIBOR beyond end-2021.

LIBOR Cessation



Proposed Alternative



SOFR

Secured Overnight Financing Rate is **secured** overnight and transaction based encompassing multiple repo market segments.

SONIA

Reformed Sterling Overnight Index Average is **unsecured** rate that covers overnight wholesale deposit transactions.

TONAR

Tokyo Overnight Average Rate is **unsecured**, overnight and transaction based. It reflects the uncollateralised overnight call rate market encompassing multiple repo market segments.

SARON

Swiss Average Rate Overnight is a **secured** overnight rate that reflects interest paid on interbank overnight repo transactions.

ESTR

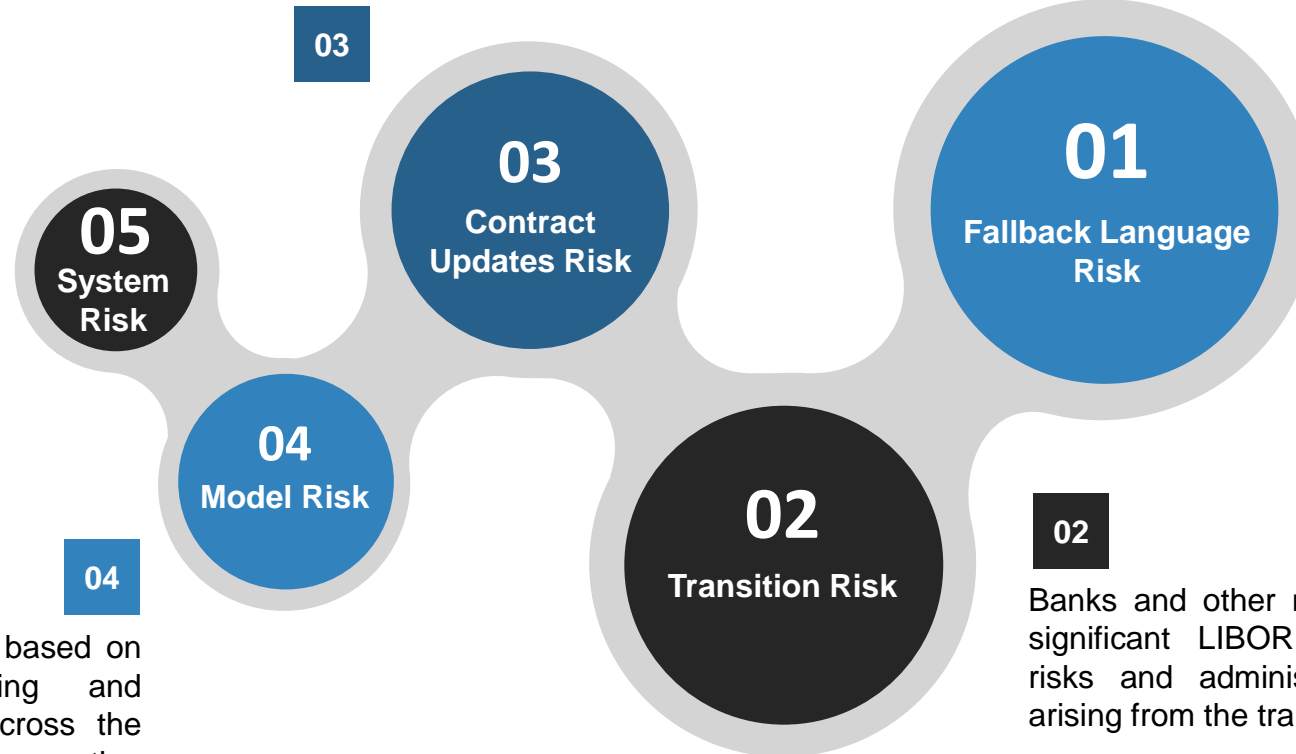
Euro Short term rate is an **unsecured** rate that captures overnight wholesale deposit transactions in the EURO area.

Challenges

Amendments to existing contracts and devising new business contracts are a big challenge.

01 Fallback language is a contractual provision that specify the trigger events for a transition to a replacement rate and the spread adjustment to align the replacement rate with the benchmark being replaced.

05 Developing and adjusting to new infrastructure as per the new rate regime.



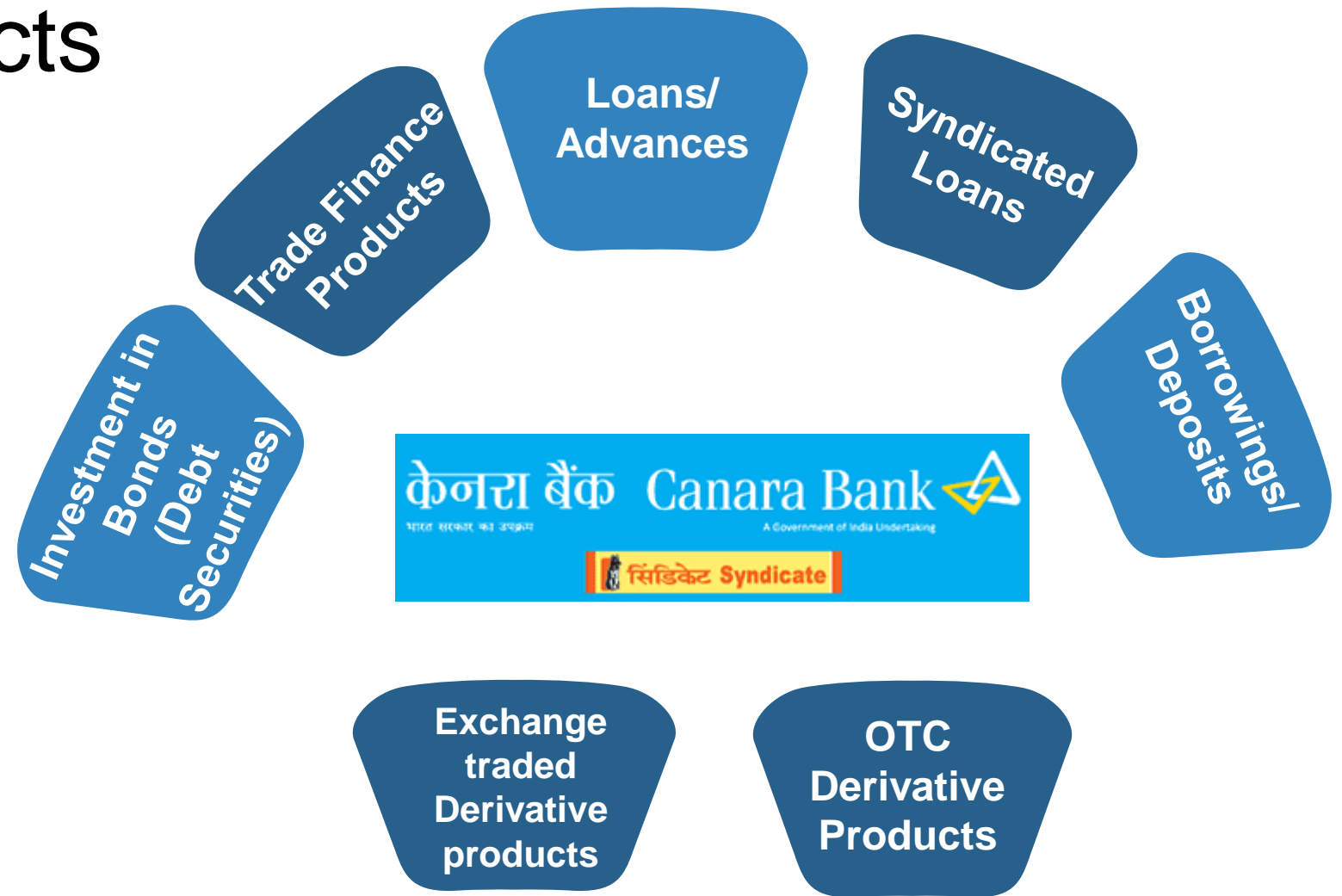
02 Banks and other market participants with significant LIBOR positions face major risks and administrative burdens (cost) arising from the transition to the new rates.

04 All present systems are based on LIBOR rates, adopting and changing the system across the globe is a big risk for transaction as well as risk models.

Impact on Products

•Deposit Products viz., FCNR(B)/ RFC deposits, Credit Facilities like PCFC, FCLR, etc., and OTC Interest rate derivatives are likely to be impacted by the transition.

•The transition from LIBOR to RFRs shall have cascading effect on Accounting, P&L, Tax, Infrastructure, etc., which may likely affect the LIBOR based products.



RBI has advised to cease using the Mumbai Interbank Forward Outright Rate (MIFOR), a benchmark which references the LIBOR, as soon as practicable and in any event by December 31, 2021. In this context, Financial Benchmarks India Pvt Ltd (FBIL) has started publishing daily adjusted MIFOR rates from June 15, 2021 and modified MIFOR rates from June 30, 2021 which can be used for legacy contracts and fresh contracts respectively.

What Customers can expect?

1. PRICING

1. Changes in pricing as it is normally based on the source of funds of matching maturities and matching Benchmark with additional spread. It is also depending upon the rates offered by other India based peer Banks/Prime Banks in that center.

2. SELECTION OF BENCHMARK RATE

2. Selection of benchmark rate (alternative Risk free reference rate) and the spread should be mutually agreeable to the Bank and counterparty/borrower while ensuring the yield on advances/return on assets/cost of borrowing remain at the level linked to LIBOR.

3. DOCUMENTATION

Legacy Contracts

3. Amendments in legacy contracts. Suitable examination and necessary amendments shall be incorporated in legacy contracts to mitigate any conduct risk and legal risk and to reflect new regulatory and International Swap and Derivatives Association (ISDA) guidelines.

4. DOCUMENTATION

New Contracts

4. Linking of any new contracts necessarily to new benchmark rate reflecting new regulatory and International Swap and Derivatives Association (ISDA) guidelines.



Our Readiness



Our Bank has a transition plan in place to address/ mitigate the risks and a roadmap has been designed with tentative dates of transition plan duly considering the risks.

We have also formed a working group to monitor the timelines for transition and to strengthen the preparatory work in smooth transition of LIBOR benchmark. As a part of our obligation towards our customers, we are fully committed in identifying and addressing potential impact on existing and future transactions on account of LIBOR transition.

This advisory is published for information purpose with an objective to reach out to our constituents who have foreign currency exposure (deposits, viz., FCNR(B)/ RFC deposits and Credit Facilities like PCFC, FCLR, etc.) linked with LIBOR as the benchmark reference rate. This publication is intended to establish an outlook of the transition process with relevant challenges and the readiness of the Bank in addressing the same and ensuring a smooth transition to Alternate Reference Rate.

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