BBVA

Corporate &
Investment Banking

IBOR Transition

Creating Opportunities

IBOR TRANSITION

Some interest rate benchmarks such as LIBOR and EONIA have been reformed or are currently undergoing a transition to alternative risk-free rates (RFRs). If you have any financial products that reference these rates or if you use reference to these rates for any other purposes, this information is relevant for you.

What are interest rate benchmarks?

Interest rate benchmarks are interest reference rates that are periodically and publicly accessible. They are a useful reference for all kinds of financial contracts such as loans, mortgages, account overdrafts, and other more complex financial products. Interest reference rates are calculated by an independent body, in order to reflect the cost of funding for different markets. For example, they might reflect how much it costs for banks to borrow from each other or how much it costs banks to obtain funds from other sources, such as pension funds, insurance companies and money market funds.

This means that these interest rate benchmarks play a key role in the financial system, the banking system and the economy overall. Examples of these interest rate benchmarks are the London Interbank Offered Rate (LIBOR) and for the Euro, the Euro Interbank Offered Rate (EURIBOR) and Euro Overnight Index Average (EONIA), which are generally referred to as IBORs.

What is the IBOR Transition? Why are these interest rate benchmarks being reformed?

For more than 40 years, a series of interest rate benchmarks, have been key tools in the daily life of the global financial services industry. In this context, changes in interbank funding markets have meant that interest rate benchmarks were based less on observable transactions and more on expert judgment. In 2014, the Financial Stability Board (FSB) recommended enhancing existing interest rate benchmarks and the development and adoption of alternative risk-free rates (RFRs).

Authorities in many jurisdictions have been driving initiatives to: (i) reduce the financial system's dependence on interest rate benchmarks such as the IBORs, (ii) reform key interest rate benchmarks to make them more reliable and robust and (iii) transition to appropriate RFRs.

What does the European Benchmark Regulation (BMR) entail?

The European Parliament and Council approved a Regulation "on indices used as benchmarks in financial instruments and financial contracts" (Benchmarks Regulation or BMR), which was published in June 2016 and applicable as of January 1, 2018, with transitional provisions until January 1, 2022.

The BMR introduces a regime for benchmark administrators, contributors and users, in order to ensure accuracy and reliability of indices used as benchmarks in financial instruments and contracts, or to measure the performance of investment funds in the EU.

It also requires that more robust fallback language exists in certain relevant contracts and agreements. The purpose of fallbacks is to define the steps that will be taken to identify and agree an alternative benchmark in the event that the original benchmark ceases to be available or materially changes and what happens if an alternative cannot be agreed.

What are the RFRs and when will transition take place?

RFRs are based on executed transactions, which removes expert judgement from the submission process and reduces the direct conduct risk. The underlying overnight markets also contain greater liquidity and transaction volumes than most benchmark interest rates tenors.

Some of the interest rate benchmarks have been already reformed, like EONIA and EURIBOR that have evolved their methodologies to accomplish BMR. On the other hand, it is possible that some other interest rate benchmarks may be discontinued in the near future.

The following table summarizes the key aspects of each IBOR and RFR by jurisdictions as identified by the relevant public-private sector RFR working groups:

Jurisdiction	Benchmark rate	Administrator	Alternative RFR	Alternative RFR administrator	Overnight rate	Secured / Unsecured	Rates published	Cessation
EU	EONIA	European Money Markets Institute (EMMI)	€STR (Euro Short Term Rate)	European Central Bank (ECB)	Yes	Unsecured	October 2019	January 3, 2022
	EURIBOR	European Money Markets Institute (EMMI)	To be determined[1]					No discontinuation is foreseen
UK	GBP LIBOR	ICE Benchmark Administration (IBA)	SONIA (Reformed Sterling Overnight Index Average)	Bank of England	Yes	Unsecured	23 April 2018	No longer guaranteed from end 2021
US	USD LIBOR	ICE Benchmark Administration (IBA)	SOFR (Secured Overnight Financing Rate)	Federal Reserve Bank of New York (FRBNY)	Yes	Secured	3 April 2018	No longer guaranteed from end 2021
Switzerland	CHF LIBOR	ICE Benchmark Administration (IBA)	SARON (Swiss Average Rate Overnight)	Swiss National Bank (SNB) and SIX Swiss Exchange	Yes	Secured	25 August 2009	No longer guaranteed from end 2021
Japan	JBA TIBOR / EuroYen TIBOR	JBA TIBOR Administration	TONAR (Tokyo Overnight Average Rate)	Bank of Japan	Yes	Unsecured	1996	No discontinuation is foreseen
	JPY LIBOR	ICE Benchmark Administration (IBA)	TONAR (Tokyo Overnight Average Rate)	Bank of Japan	Yes	Unsecured	1996	No longer guaranteed from end 2021

Source: BBVA and www.gfma.org

(1)*The alternative RFR that has been chosen in the European Union is the €STR and it will be introduced as the basis for a reliable fallback rate for EURIBOR, as soon as possible.*

What are the fundamental differences between the IBORs and RFRs?

There are some fundamental differences between IBORs and RFRs which may be summarised as follows.

- Tenor: RFRs are available for an overnight tenor only. By contrast IBORs are published for different tenors (e.g. ICE LIBOR is published for 7 tenors ranging from overnight to 12 months).

- Currencies: Each RFRs is published for a specific currency amounts only whilst, by contrast, ICE LIBOR is published for amounts denominated in euro, Japanese yen, sterling, Swiss francs and US dollars.

- Historic or predictive: RFRs are backward-looking, in that they report the rates paid yesterday on the relevant transactions. By contrast IBORs report the rate at which funds are made available today for the relevant tenor.

- Economic concept measured: RFRs are designed to be nearly risk-free rates. As a consequence they do not incorporate any credit or liquidity premium. By contrast most IBORs are designed to provide an indication of the average rates at which submitter banks could obtain wholesale unsecured funding for set periods and incorporates both a credit premium (to reflect term bank credit risk) and a term liquidity premium (to reflect the risk inherent in longer-dated funding).

Due to the structural differences between the benchmark interest rates with a term structure and RFRs, certain adjustments to RFRs are needed to ensure that contracts referencing IBORs will continue to function if fallbacks referencing the RFRs take effect.

As a BBVA client, what is the industry recommending you to do now?

The industry (e.g. Working Group on Sterling Risk-Free Reference Rate) has given some guidance in respect to IBORs reform:

1. Understand for which products and contracts you have exposure to benchmark interest rates and to understand what will happen to these contracts if these benchmark interest rates are no longer available.

2. Check your contract terms. You will need to check the fallback terms, what that means for your financial products and whether these need to be amended. If needed you should ask for professional advice in this regard. In case of contracts with BBVA, we will provide you with the information you need, clearly and completely, in order to understand the fallback terms.

3. Familiarise yourselves with the alternative Risk Free Rates (RFRs) that have been selected by the relevant public-private sector RFR working groups.

4. Contact your bank(s) to understand more on the preparations that your banks are taking and the impact of those preparations on your own operations.

The IBORs reform may impact products and services in a number of ways and the information above cannot be, and is not, exhaustive. You should contact your professional advisors on the possible impact of the IBOR reforms on the financial products and services you use or may use in the future.

What does BBVA do to support you through the transition?

BBVA`s priority is to engage with and support our clients through all aspects of this transition; this includes, continue to provide products and services to our clients.

The information on this site is not intended to be a complete or exhaustive overview. We are monitoring industry developments regarding the IBOR transition process, however please reach out to your BBVA sales representative or relationship manager for any further questions. Our BBVA representatives are available to support you in this context in relation to BBVA products and services.

We highly appreciate and value your business and we are confident that we will continue our partnership and that we will continue to serve your needs during these times of change.

Related links

- **New York Federal Reserve (USD): Alternative Reference Rates Committee (ARRC)**
- **Bank of England (GBP): Working Group on Sterling Risk-Free Reference Rates**
- **Swiss National Bank (CHF): National Working Group on Swiss Franc Reference Rates**
- **European Central Bank (EUR): Working Group on Euro Risk-Free Rates**
- **Bank of Japan (JPY): Study Group on Risk Free Rates**
- **Financial Conduct Authority (FCA)**
- **US Commodity Futures and Trading Commission (CFTC)**
- **Financial Stability Board (FSB)**
- **International Swaps and Derivatives Association (ISDA)**
- **Loan Market Association (LMA)**

BBVA SUPPORT

BBVA SA is committed to support our clients and counterparties through the IBOR transition.

Contact for any queries
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For further information please visit our website www.bbvacib.com

Please feel free to contact your BBVA banker for any further IBOR transition queries in relation to BBVA products and services