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Transition to SORA: New Timelines to Cease Issuance of SOR Derivatives and SIBOR-linked Financial Products and Others

Introduction

To reinforce the shift to a Singapore Overnight Rate Average ("**SORA**")-centered SGD interest rate landscape and provide additional guidance on cessation timelines, the Steering Committee for SOR & SIBOR Transition to SORA ("**SC-STS**") published a report on 31 March 2021 ("**Report**") announcing the following new timelines for financial institutions ("**FIs**"):

1. FIs to cease usage of Swap Offer Rate ("**SOR**") in new derivatives contracts by end-September 2021 and recommend FIs to cease usage of Singapore Interbank Offered Rate ("**SIBOR**") in financial products by end-September 2021;
2. SC-STS to retain the original end-2024 end-date for Fallback Rate (SOR) despite SOR now set to be discontinued later in mid-2023 and that a Fallback Rate (SOR) publication period of three years is not necessary. The Fallback Rate (SOR) was designed as an interim fallback solution for residual contracts which are unable to transition to SORA in time; and
3. FIs to aim to substantially reduce their SOR exposures (both cash and derivative) to corporates to 20% by end 2022. All contracts that continue to reference SOR as at end-2022 should minimally incorporate appropriate contractual fallbacks.

These new timelines are in addition to the earlier timelines announced by SC-STS in October 2020 for shifting new cash market use away from SOR into SORA. The earlier timelines include:

- By end-February 2021, all Domestic Systemically Important Banks ("**D-SIBs**") should be ready to offer a full-suite of SORA-based products to their customers; and
- By end-April 2021, all non-DSIB banks should be ready to offer new SORA-based products to their customers, and all lenders and borrowers must cease issuance of SOR-linked loans and securities that mature after end-2021.

For details, please refer to our November 2020 Client Update "*Transition to SORA: Key Timelines to Cease Issuance of SOR-Linked Financial Products & Market Guidance*" (available here).

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The new timelines announced in the Report are in response to significant progress and developments globally and locally that have critical implications on SC-STS' transition roadmap and timelines. In this Update, we provide a summary of the above three key implications for FIs set out in the Report.

Recent Developments and Significance to FIs

In December 2020, there have been various significant developments globally and locally with implications for the industry benchmark transition to SORA. In brief, these include:

- **Discontinuation of key USD London Interbank Offer Rate ("LIBOR") tenors in mid-2023.** Among other things, all LIBOR settings would either cease to be provided by any administrator or be no longer representative: (i) immediately after 31 December 2021, in the case of all GBP, EUR, CHF and JPY settings, and the 1-week and 2-month USD settings; and (ii) immediately after 30 June 2023, in the case of the remaining USD settings.

- **Discontinuation of the 6M SIBOR on 31 March 2022, the 1M and 3M SIBOR by end-2024**. In December 2020, the Association of Banks in Singapore and the Singapore Foreign Exchange Market Committee (ABS-SFEMC) and SC-STS published a joint response to feedback received from the July 2020 consultation on SIBOR Reform and the Future Landscape for SGD Interest Rate Benchmarks. Among other things, the response paper highlighted: (i) broad public support for the proposal to discontinue SIBOR and shift towards a SORA-centered interest rate benchmark; (ii) plans to discontinue all remaining tenors of SIBOR in a few years, starting with the 6M SIBOR on 31 March 2022, and the 1M and 3M SIBOR by end-2024; and (iii) SC-STS' intention to announce a clear timeline to cease the use of SIBOR in new contracts. In setting this timeline, SC-STS would consider the state of readiness of SORA markets, particularly the usage of SORA in retail and small and medium-sized enterprises (SME) loan markets where SIBOR is widely used. SC-STS would provide the market with advance notice of at least six months from the date of announcement to the date of cessation of SIBOR usage in new contracts.

- **LIBOR discontinuation.** In February 2021, LCH confirmed its intentions to automatically convert or replace outstanding LIBOR derivatives contracts with corresponding RFR-referencing contracts, at or before the expected discontinuation of the relevant LIBOR benchmark.

Three Critical Implications on SGD Benchmark Transition Timelines

We highlight below three main implications of recent developments on SC-STS' guidance on timelines for the SOR and SIBOR transition to SORA.

1. **New timelines on stopping new usage of SOR/SIBOR early by end-September 2021, in addition to earlier announced timelines.** Aligning with the global trend to cease usage of USD LIBOR in new cash market contracts, SC-STS remains committed to the earlier announced timelines for shifting new cash market use away from SOR and into SORA. Specifically:

- By end-April 2021, all FIs and their customers should cease usage of SOR in new loans and securities that mature after end-2021.
- To support this, most D-SIBs have started to offer a full-suite of SORA-based products to their customers from February 2021, while all non-DSIB banks should be ready to offer new SORA-based products by end-April 2021.

SC-STS has also set out further implementation guidance on how banks could approach limited situations where SOR loans have been signed or agreed on before end-April 2021, but where disbursements may occur only after end-April 2021. For details, please refer to Annex A of the Report.

Additionally, SC-STS has introduced new timelines for FIs and their customers to cease new usage of SOR/SIBOR. Under the new timelines:

- ***All FIs and their customers cease usage of SOR in new derivatives contracts by end-September 2021***, except for specified purposes relating to the risk management and transition of legacy SOR positions to SORA. For details on exemptions, please refer to Annex B of the Report. This complements existing industry timelines to reduce the stock of outstanding SOR products ahead of SOR's discontinuation in mid-2023, including to cease usage of SOR in new cash market products by end-April 2021, and for all banks to substantially reduce their gross exposures to SOR derivatives by end-September 2021.
- ***SC-STS recommends that FIs and their customers cease usage of SIBOR in new contracts by end-September 2021***. This is consistent with the preparation for the discontinuation of the less widely used 6M SIBOR by March 2022, and the widely used 1M and 3M SIBOR benchmarks by end-2024. There is no immediate impact on existing SIBOR loans. Banks will reach out to their customers at the appropriate time and provide sufficient notice for customers to consider switching these loans to other alternative loan packages. SC-STS and ABS will launch a public education campaign in the middle of 2021 to increase public awareness and support wider adoption of retail SORA products.

2. **Limiting usage of Fallback Rate (SOR) in view of the end-2024 end-date for Fallback Rate (SOR).** The Fallback Rate (SOR) was designed only as an interim fallback solution for residual contracts which are unable to transition to SORA in time, and not intended to be used in new contracts. Previously, it was announced that Fallback Rate (SOR) would be published for a period of about three years following the expected discontinuation of SOR after end-2021 (i.e. till end-2024). With SOR now set to be discontinued later in mid-2023, more existing legacy SOR transactions would be able to mature and the need for extended Fallback Rate (SOR) arrangements would be much lower. Therefore, SC-STS has decided to retain the original end-2024 end-date for Fallback Rate (SOR).

3. **Active transition of SOR contracts to SORA as soon as practicable.** While SOR remains available till mid-2023, liquidity in SOR derivatives markets has started to decline and this trend will likely accelerate with the new cessation timeline on the use of new SOR derivatives. SC-STS

strongly encourages all market participants to actively explore converting or replacing outstanding SOR cash market contracts with SORA contracts. Taking into account the expected trajectory of the SOR-SORA basis markets, banks should aim to substantially reduce their SOR exposures (both cash and derivative) to corporates to 20% by end 2022. Where it is not possible to fully exit from gross exposures to SOR derivatives, FIs should aim to reduce their net risk exposures to centrally cleared SOR derivatives across the entire curve. All contracts that continue to reference SOR as at end-2022 should minimally incorporate appropriate contractual fallbacks.

For a summary of the updated SC-STS transition timelines, please refer to Annex C of the Report.

Concluding Remarks

FIs are strongly encouraged to accelerate operational and system changes, staff training and client outreach, and implement the necessary changes to transition SOR exposures to SORA. The key timelines detailed in the Report provide a clear and prudent path towards mitigating financial risks from the eventual SOR discontinuation, and ensures continued access to key funding markets beyond end-April 2021, when usage of SOR in new cash market contracts will effectively cease.

For more details, please refer to the SC-STS Report on "Timelines to Cease Issuance of SOR and SIBOR-Linked Financial Products" and previous publications (link here).

If you have any queries on the transition to SORA, how it may impact your business, and/or require any assistance to manage the transition, please feel free to contact our team members below who will be happy to assist.

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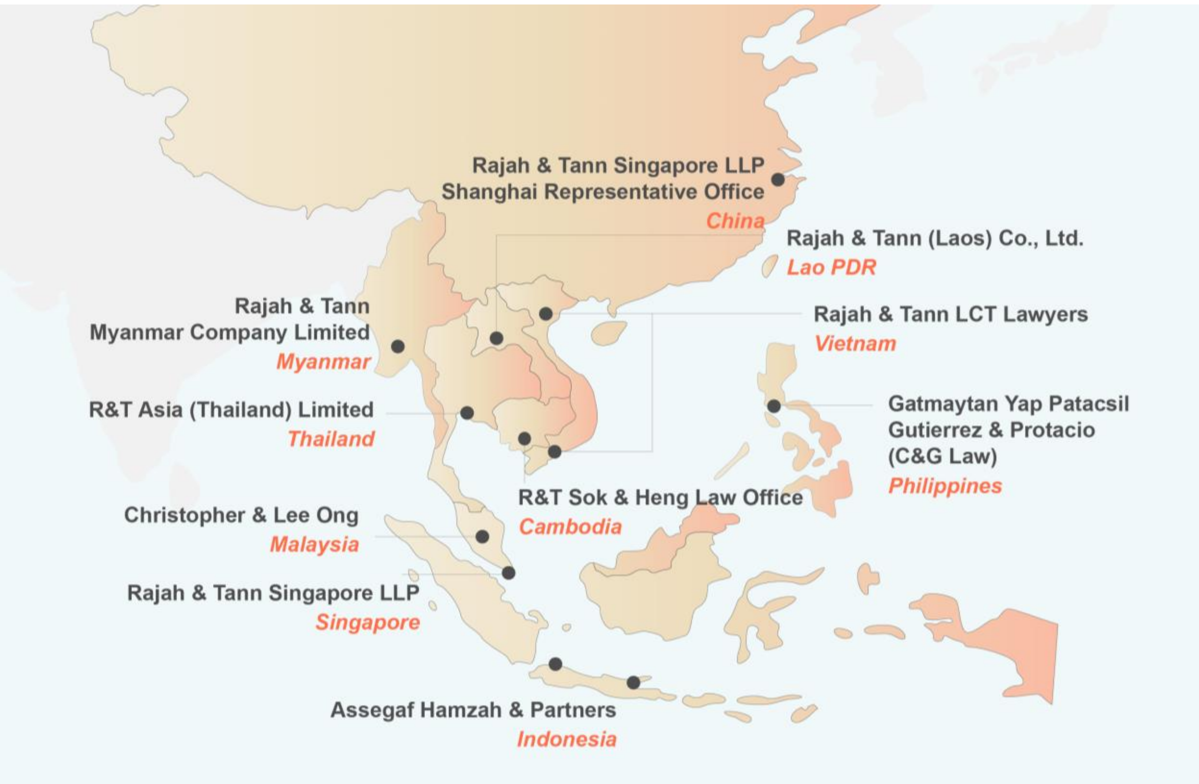

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