ISDA Safe, Efficient Markets

Benchmark Strategies Forum

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Opening Remarks

Scott O'Malia, ISDA Chief Executive

Hello everyone, and welcome to ISDA's Benchmark Strategies Forum. I'm delighted this important series has returned to an in-person format, and I'd like to thank CME Group for supporting us once again. We held a great event in New York earlier this month and I'm sure today will be equally successful.

The dust has now settled on the much-anticipated end-2021 deadline, when 30 LIBOR settings either ceased publication or became non-representative. Everyone should take credit for the huge amount of planning and preparation that allowed this milestone to be reached without significant market disruption. Removing such a widely used reference rate from financial markets is no small task, and the success of the transition so far is testament to the collaborative efforts of policymakers and market participants over many years.

But we can't afford to rest on our laurels. There is now just over a year to go until five US dollar LIBOR settings are scheduled to cease publication at the end of June 2023. These rates were given an extra 18 months to allow the large volume of legacy LIBOR exposure to roll off naturally, but there is still work to be done to ensure the mid-2023 deadline passes successfully. To achieve this, rigorous preparation and proactive transition will be needed.

In my remarks, I'll start by setting out the progress we have seen in recent months in transitioning away from US dollar LIBOR. I'll then describe the essential tools that are available to market participants to prepare for a smooth transition.

Since mid-2021, we have seen a very promising increase in the trading of interest rate derivatives referenced to SOFR. There's no doubt the 'no new LIBOR' strategy employed by regulators since the start of this year and the SOFR First initiative devised by the Commodity Futures Trading Commission's Market Risk Advisory Committee have played a big role here.

Introduced last year, the SOFR First initiative changed trading conventions in the US interdealer market for linear US dollar swaps, cross-currency swaps and non-linear derivatives from LIBOR to SOFR.

In the first six months of 2021, just 5.9% of cleared OTC and exchange-traded US dollar interest rate derivatives DV01 was referenced to SOFR, according to analysis by ISDA and Clarus. This percentage has risen every single month since SOFR First was launched, from 7.4% in July 2021 to 50.1% in May 2022.

But despite this impressive increase, I'm afraid we can't afford to relax and declare the job done. While the vast majority of OTC trades in the US interdealer market are referenced to SOFR, we need to think about how to encourage participants in other market segments and geographies to switch from US dollar LIBOR as well.

The exchange-traded market is one area where transition has been a little slower, but I'm pleased to say there has been recent progress here. Last month, CME Group launched SOFR First for Options, which will implement specific measures to boost liquidity and trading in SOFR options. These include a market-wide fee waiver for SOFR options in June and July, as well as certain market-making incentives.

This kind of initiative will go a long way to enhancing liquidity in SOFR options. It follows strong growth in SOFR futures at CME, which rose to an average of 80% of Eurodollar futures volumes at the exchange in April. As we enter the final straits of the transition, these proactive transition efforts will be vital in switching the market away from US dollar LIBOR.

Our panel this afternoon on remaining challenges will explore some of these issues, including a progress update on the SOFR First for Options initiative.

For market participants, the coming year will be all about prioritizing the transition of any remaining US dollar LIBOR exposures. For new business, multiple regulators have made clear that regulated entities in their jurisdictions shouldn't enter new US dollar LIBOR transactions from the end of 2021 except in limited circumstances, so using SOFR or another alternative reference rate is now the only real option in many cases.

For those firms that may prefer to reference an alternative to overnight SOFR compounded in arrears, forward-looking SOFR term rates are also available for certain transaction types. The Alternative Reference Rates Committee formally recommended CME Group's offering last July, while ICE Benchmark Administration launched its own term rates in March.

When it comes to managing legacy exposures to US dollar LIBOR, the necessary tools are now in place to manage the risks associated with those trades. We would certainly encourage firms to talk with their counterparties and negotiate a switch to an alternative rate proactively, but robust contractual fallbacks are also available as a safety net for derivatives that continue to reference US dollar LIBOR.

More than 15,200 entities across the globe have now adhered to ISDA's 2020 IBOR Fallbacks Protocol, which allows firms to incorporate the fallbacks into existing non-cleared derivatives. This widespread adoption meant viable alternatives based on risk-free rates automatically took effect for most non-cleared LIBOR derivatives affected by the end-2021 deadline, helping to ensure a smooth transition. These fallbacks also formed the basis for the central counterparty conversions of cleared LIBOR derivatives last year.

We expect the ISDA fallbacks to play a similarly important role in the transition from the remaining five US dollar LIBOR settings. The 2020 IBOR Fallbacks Protocol remains open for adherence, and I'd strongly encourage you to consider adhering if you haven't already.

For those tough legacy contracts that are too complex to proactively transition, I'm very pleased that we now have a robust legislative solution in place. Most recently, US federal legislation was passed in March that will allow US dollar LIBOR in certain legacy contracts governed by US law to be replaced with an alternative rate if no workable fallbacks exists. This legislation was another big transition milestone that will significantly reduce the legal and operational risks associated with tough legacy LIBOR exposures.

I started these remarks by reflecting on the need to maintain momentum as we enter the final year of US dollar LIBOR. Having outlined the initiatives that have already been adopted to boost SOFR trading, as well as the tools that are available to market participants to manage their legacy exposures, it is clear that a robust framework is in place to achieve a successful completion of the LIBOR transition.

We know from experience over recent years that outreach and education are critical in making sure this framework is properly understood so market participants can be fully prepared. It is through events like these that we are able to achieve this. I'd like to finish by once again thanking CME Group, as well as all of our speakers and delegates. I hope you find the event helpful and enjoyable.

Thank you.