ISDA Safe, Efficient Markets

Benchmark Strategies Forum
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Opening Remarks
Scott O'Malia, ISDA Chief Executive

Hello everyone, welcome to the third part of the Benchmarks Strategies Forum. We've had more than 4,800 people register over the course of this series, showing the value of a regular forum that allows regulators and market participants to share knowledge and best practice during the critical period before LIBOR's demise. I'm extremely grateful to CME Group for making this possible by supporting these events.

It's now just 108 days – a little over three months – until 30 LIBOR settings either cease to exist or become non-representative. A huge amount has already been achieved to prepare for this moment – from the promotion of alternative rates, to the implementation of robust contractual fallbacks, to the development of legislative solutions to fix tough legacy contracts. It has involved exceptional levels of cooperation and coordination between regulators, legislators and market participants across the globe. But, as we approach the final three months, we all need to make a last push to get us across the line.

There's still work to do when it comes to transitioning legacy LIBOR contracts to alternative rates ahead of the end-of-2021 deadline. Trading in some risk-free rates (RFRs) also continues to lag activity in LIBOR. It means there are still a lot of late nights and long days ahead of us in order to get this done.

But there are reasons to be optimistic, especially when it comes to derivatives. I'll briefly outline three reasons why in my remarks: increasing trading activity in risk-free rates; upcoming milestones for the transition of legacy portfolios; and recent progress in legislative solutions.

First, trading activity in derivatives linked to alternative rates has been steadily climbing in recent months, and we expect that to continue as we get nearer to the end-2021 deadline. The transition milestones set by regulators and the various national working groups will undoubtedly help.

For example, a 'SOFR first' strategy, similar to the approach taken in the UK, is now being rolled out in the US. Under a plan developed by the Commodity Futures Trading Commission's (CFTC) Market Risk Advisory Committee, trading conventions switched from LIBOR to SOFR for linear US dollar swaps in the interdealer market from July 26, with cross-currency swaps following this month and non-linear derivatives and exchange-traded derivatives expected later in the year.

Following the introduction of this initiative, analysis by ISDA and Clarus shows trading activity in SOFR reached 12.5% of total cleared US dollar interest rate derivatives DV01 in August versus 7.4% the previous month.

We're delighted to have acting CFTC chairman Rostin Behnam with us today, who I'm sure can give us an update on the impact of SOFR first.

A similar approach has also been adopted in Japan for TONA. Following the formal launch on July 26, trading in TONA jumped from 6.9% of total cleared yen interest rate derivatives DV01 in June to 49.5% in August – a very big step in the right direction.

Our second panel today will look at the impact of these 'RFR first' strategies and consider whether additional steps are needed to bolster liquidity.

Turning to the transition of legacy portfolios, while there's undoubtedly more work to do here, several important upcoming milestones should spur progress. For one thing, the Working Group on Sterling Risk-Free Reference Rates has set a target of the end of this month for firms to complete active conversion of all legacy sterling LIBOR contracts expiring after the end of 2021 where viable.

Then, in December, the major central counterparties will convert all existing cleared swaps linked to euro, sterling, Swiss franc and yen LIBOR to RFR overnight index swaps. This will, at a stroke, eliminate a vast amount of legacy LIBOR exposures.

For those non-cleared derivatives that remain, robust fallbacks will automatically take effect in the vast majority of cases if firms don't complete their transition efforts in time. So far, more than 14,500 entities across nearly 90 jurisdictions have adhered to ISDA's IBOR Fallbacks Protocol, which incorporates the fallbacks into existing non-cleared derivatives.

The fact that so many entities have adhered to the protocol – which will result in LIBOR exposures falling back to a spread-adjusted RFR following cessation or non-representativeness – means there is, in effect, trillions of dollars in RFR exposure already out there.

That ISDA protocol remains open for adherence, and I'd strongly encourage you to consider adhering if you haven't already.

Finally, there has been good progress on legislative solutions for tough legacy exposures. The UK Financial Conduct Authority (FCA) has already completed a consultation on its policy framework for the development of a synthetic LIBOR for certain settings, and is shortly expected to consult on the specifics of who will be able to use synthetic LIBOR for six sterling and yen LIBOR tenors.

I'm looking forward to hearing from the FCA's Anne-Laure Condat later today to get an update on this timetable.

Meanwhile, progress is being made on a US federal bill aimed at resolving tough legacy positions tied to US dollar LIBOR, following the passing of the bill by the House Financial Services Committee on July 29. This comes in the wake of similar New York state legislation passed in April.

Of course, five of the most popular US dollar LIBOR settings will continue to be published until mid-2023, giving firms a little more wiggle room to deal with legacy US dollar LIBOR trades. However, a number of regulators across the globe, including the Federal Reserve, have said they will restrict new use of US dollar LIBOR from the end of 2021, except in limited circumstances.

We're delighted to have Michael Held from the Federal Reserve Bank of New York with us today, who I'm sure will talk more about regulatory expectations for US dollar LIBOR and use of SOFR.

Let me finish by reiterating that there are reasons for optimism. But, with only 108 days left, there's also no room for complacency. We must use the remaining time wisely to ensure everyone is ready for a future without LIBOR.

Thank you.