P.R.I.M.E. Finance
Panel of Recognized International Market Experts in Finance

Benchmarks Update

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Economic Issues

- Replacement of IBORs by RFRs can give rise to "value transfer" in which one party to a transaction is advantaged economically to the disadvantage of another party
- Term Structure
  - ➢3 month LIBOR and 6 month LIBOR are term rates whereas RFRs are overnight rates
  - ➢Derivatives solution: determine/compound daily, calculate in arrears
  - ➢Does this work in other markets (e.g., loan market)?
- Spread
  - ➢LIBOR is a rate that incorporates bank credit risk
  - ➢RFRs are "risk free" rates
  - ➢To make RFRs "economically equivalent" to LIBOR, a spread needs to be added to the RFR (e.g., 3 month USD LIBOR = SOFR+0.25%)
  - ➢A spread determined by reference to an historical average will depend on the historical period from which the spread is determined
- Bank Funding Costs
  - ➢With RFR+fixed adjustment spread, lenders may lose the ability to pass along higher funding costs to borrowers

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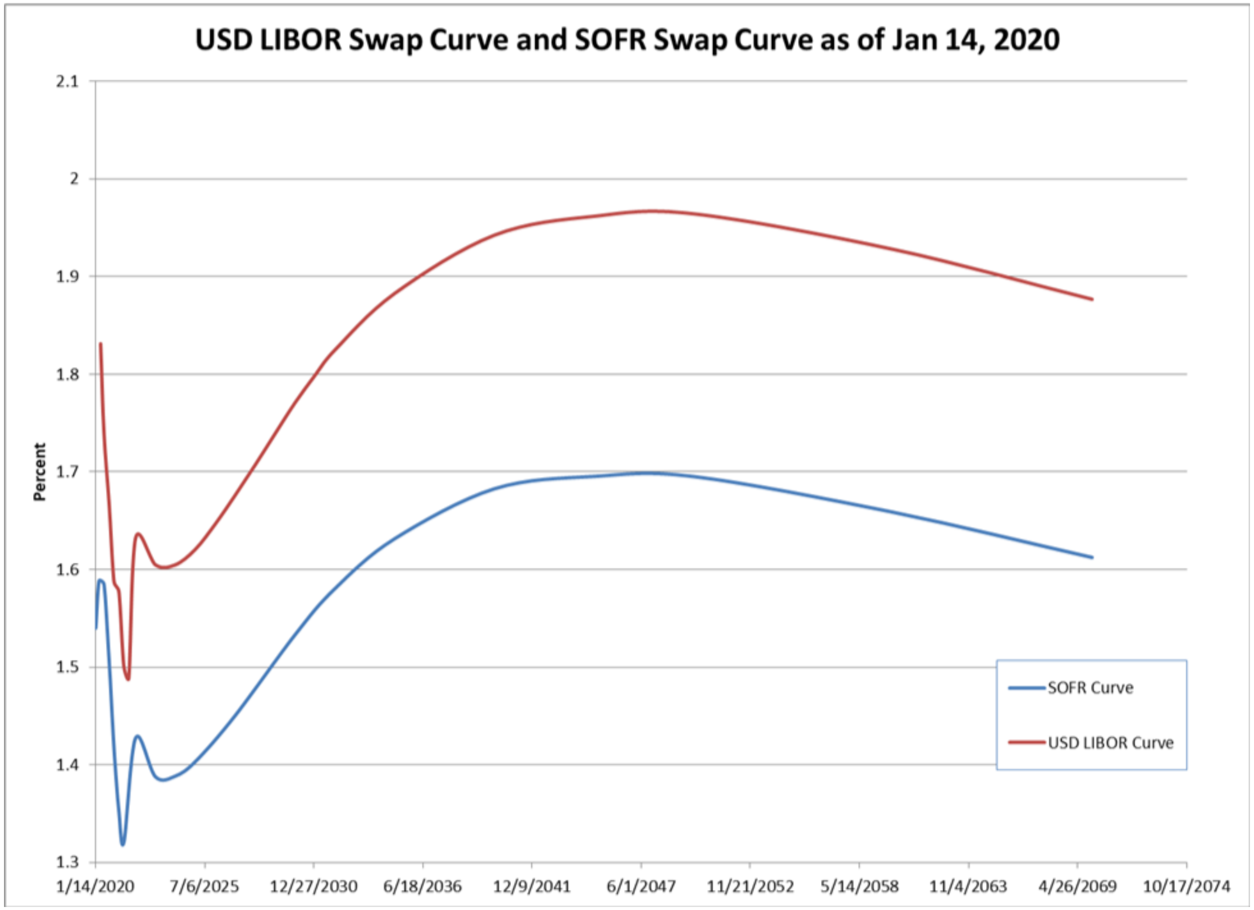
USD LIBOR Swap Curve and SOFR Swap Curve as of January 14, 2020



Source: Bloomberg

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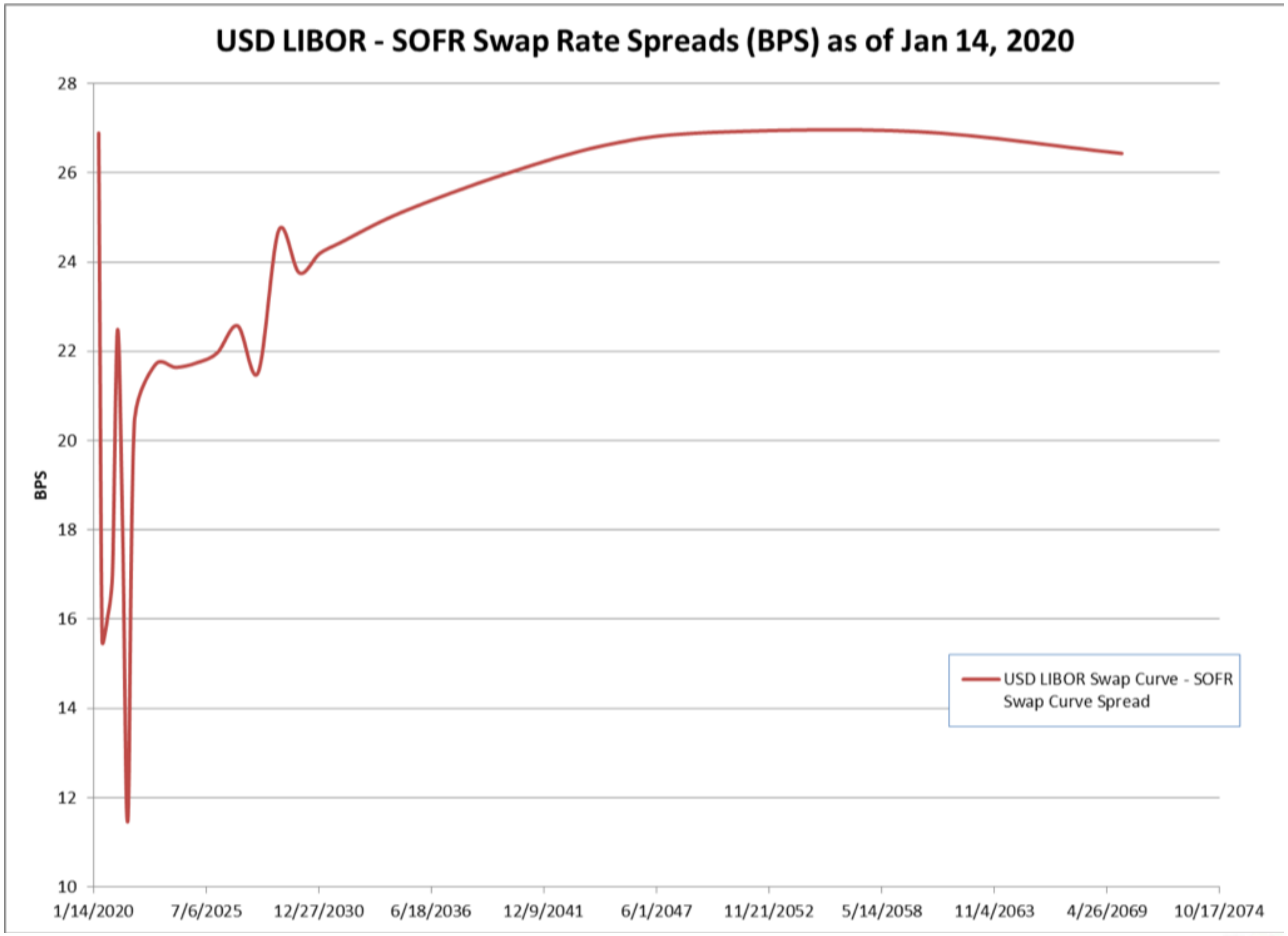
USD LIBOR Swap Curve and SOFR Swap Rate Spreads as of January 14, 2020



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Potential for Disputes

- Triggers – has one occurred?
- Fallbacks – are they economically equivalent?
- Continuity of contract if no fallback or if fallback is nonsensical
- Disputes regarding spreads and appropriate compensation payments, if any
- Can transition be "gamed" or manipulated?