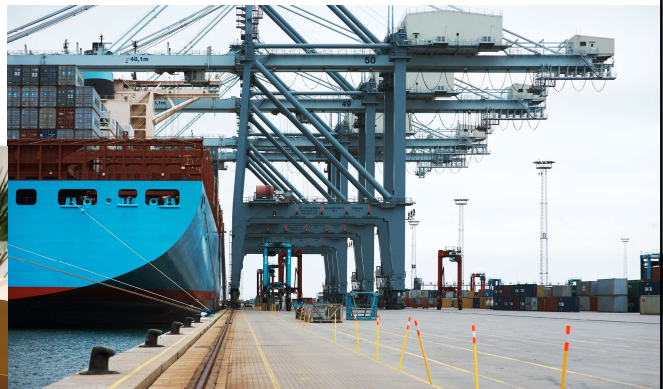


The new CHF Risk Free Rate - SARON



ICMA Switzerland and Liechtenstein Regional General Meeting
Martin M. Bardenhewer, 16 July 2020



13

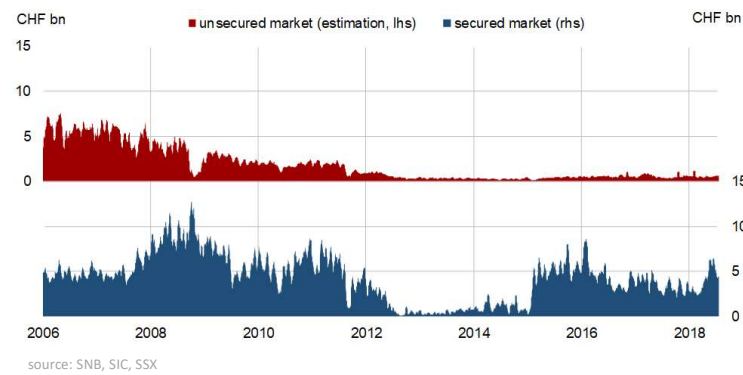
Bye Bye LIBOR

CHF LIBOR is not expected to exist after 2021 –
Announcement might come as early as late 2020

Money market has moved away from LIBOR long ago

150 JAHRE
Zürcher
Kantonalbank

CHF money market O/N turnover



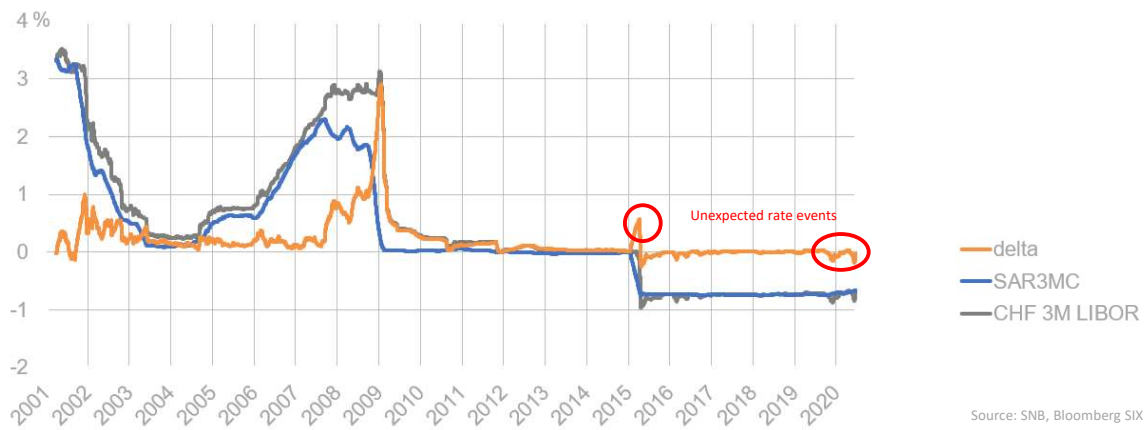
LIBOR submission quality



Source: ICE LIBOR weekly report, 22 June – 26 June 20

Compounded SARON is (slightly) below LIBOR

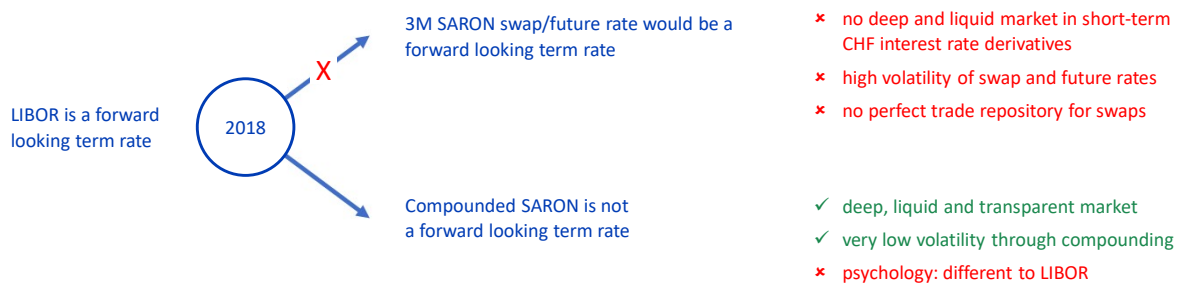
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Why the NWG did not recommend a derivative-based term rate

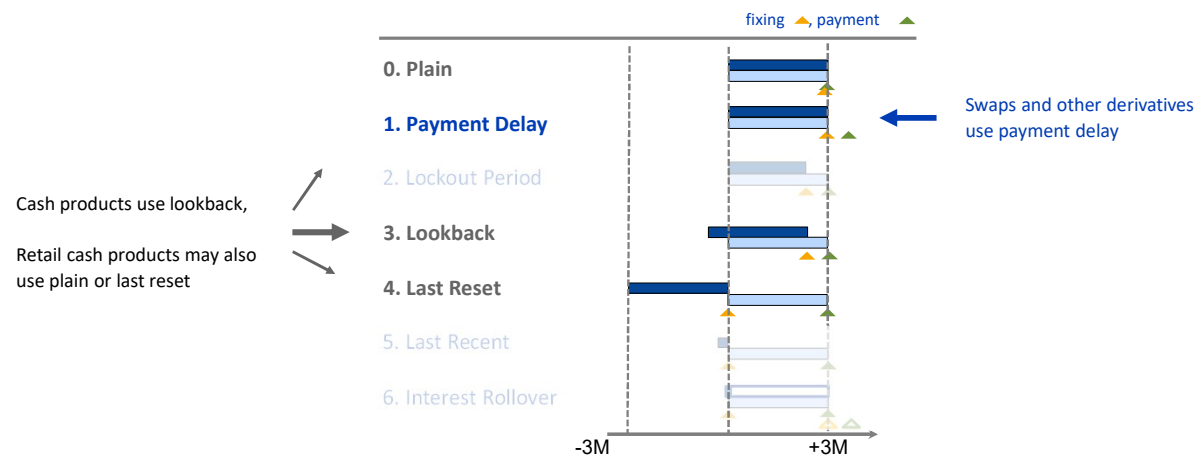


Transition will only reduce vulnerabilities if it **addresses the core weakness of the IBORs** – the lack of deep and liquid underlying markets. (FSB letter July 2018, <http://www.fsb.org/wp-content/uploads/P120718.pdf>)



5

Standards for compounded SARON



The cash markets have started with mortgages



Mortgages

GLKB	term	lookback 5 days
UBS	perp	plain
SGKB	term	lookback 5 days
Raiffeisen	term	plain
LUKB	term	lookback 2 days
ZKB	perp	lookback 2 days
WIR	term	last reset (announced)
CS	term	plain and last reset (announced)

Product differentiation without market fragmentation

Banks report **positive customer feedback**

Corporate loans

SME

Some banks offer SARON loans to SME based upon their mortgage offering.

Multinational corporates and institutional clients

NWG has recommended **lookback 5 days** for syndicated loans. This might be a standard for large bilateral loans as well

NWG liaises with other currency groups for standards in multicurrency loans

Limited number of transactions so far

CHF FRN expected to be fully implemented by end of 2020



National Working Group on Swiss Franc Reference Rates (NWG)

2 July 2019

Discussion paper on SARON Floating Rate Notes

Executive Summary

- The purpose of this paper is to evaluate interest rate provisions for SARON Floating Rate Notes (FRN) assuming that a time lag is required to address operational matters related to the timely determination of interest payments. Further, a sample fallback language is provided.
- Based on the following assessment, the advantages of the approach "Lookback" (approach 3) outweigh its small inherent economic drawbacks. Thereby a time lag between three to five days is deemed sufficient to deal with operational matters. In addition, such a time lag may obtain the largest operational acceptance, as it is already applied in FRN referencing to other alternative risk-free rates (RFR).

Background

- The National Working Group on Swiss Franc Reference Rates is the key forum for considering proposals to reform reference interest rates in Switzerland and discussing the latest international developments. The NWG is co-chaired by a representative of the private sector and a representative of the SNB. NWG recommendations are not legally binding.
- The results of this assessment were discussed at the NWG meeting on 5 February 2019.¹ The NWG concluded that there are no impediments to issuing SARON FRN and supported the preference for the approach "Lookback".² Exchanges were thereby encouraged to facilitate the listing of SARON FRN.

Evaluated approaches³

- 1) Payment delay
- 2) Lockout period
- 3) Lookback

Please refer to the appendix II for a detailed description of the approaches considered and other proposed provisions.

One standard recommended by NWG

Fully specified template:

- Interest rate calculation: lookback [3/4/5] days
- SARON fallback language



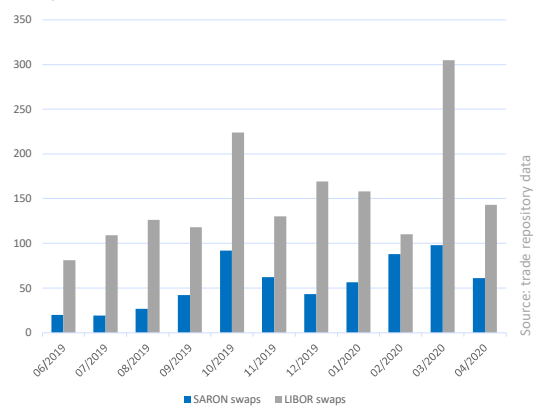
NWG has asked SIX to implement the standard **by end of 2020**

SARON swap market accelerates, but still has to take off



Last 12 months

Monthly traded volume in CHF bn.



Next 12 months

Revised **ISDA documentation** for new and legacy transactions expected for summer and for taking effect in November 2020. Swiss master agreement will follow shortly thereafter

Growing market for **SARON cash products**

Banks are expected to change their **FTP curves** from LIBOR swap to SARON swap within the next months



Tipping point in the swap market in Q4/20 and Q1/21

Don't get confused



Index
(initial peg of 100)

SARON Index
available since 2009

SONIA Compounded Index
available from August 2020 on

SOFR Index
available since 2 March 2020

Averages
(period compounded)

SARON Compound Rates
1-, 3- and 6-month

available since 25 March 2020

SONIA Period Averages

placed on hold after consultation

SOFR Average
30, 90, 180 days

available since 2 March 2020

Most products will reference the formula as defined in the SIX rulebook and implemented in a forthcoming calculator on SIX website

10

Tough legacy



The problem

For some legacy positions a transition before the end of LIBOR is unfeasible because of **missing robust fallback language** and other features like product complexity or large number of counterparties, investors or customers

Sorry, no loophole: So far only a very small amount of tough legacy in CHF is expected

The magnitude

Only limited tough legacy issues identified in CHF so far.

Significant issues for other currencies, e.g. in the bond markets

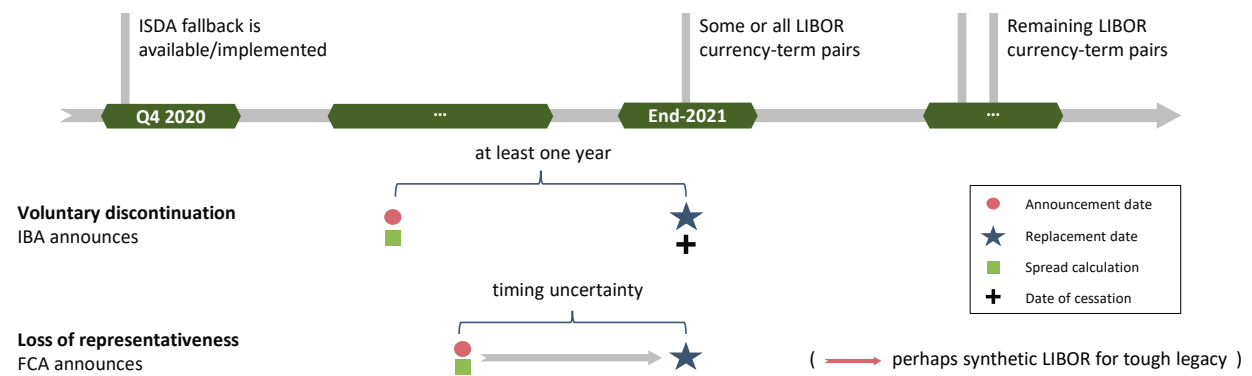
Remedy

The USD ARRC has proposed **legislative relief** under NY state law.

The GBP RFRWG has issued a tough legacy paper. Subsequent UK government has announced to update the UK **Benchmark Regulation** (BMR) to empower FCA to introduce methodological changes to deal with tough legacy. This might be a way forward for EU BMR, too.

LIBOR end game – how it works

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On 22 June, FCA stated that announcements could come as early as November or December this year

12

Minor spread adjustments in CHF (if any)



Compounded SARON is (slightly) below LIBOR



Spread LIBOR to compounded SARON is calculated as **5-year historical median at announcement date**

Current values:

1.3bp for 3M
8.6bp for 6M

Little change expected for final values due to short time to announcement and the median

Spreads will be applied under ISDA master agreement and are expected to be the standard for all cash and derivative products globally.

Need for information? Sharing know how? Any remarks?



Libor Starter Pack medium level	nwg@snb.ch Share, ask, discuss, sign-up for newsletter	NWG protocols expert level	ARRC and UK WGRFR all levels
Swissbanking.org insight 2/20 entry level	ICMA quick guide really good	martin.bardenhewer @zkb.ch happy to get in touch	SIX definitions & data from the administrator

14