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Investing in rural people

Update on Interbank Offered Rates (IBORs) Transition: Impact on IFAD and next steps

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For: Information



Update on Interbank Offered Rates (IBORs) Transition: Impact on IFAD and next steps

LIBOR Transition: relevance for IFAD

The USD 6-month LIBOR rate will cease on 30 June 2023

No new contracts referencing LIBOR should be issued from 1 January 2022, as global markets prepare for the cessation

Impact on IFAD

Amendments needed

1. The pricing of IFAD's **ordinary loans** denominated in USD and in SDR is linked to USD 6-months LIBOR
2. Some of the **swaps** in IFAD's investment portfolio are linked to USD 6-months LIBOR
3. Some **financial instruments** are measured and reported based on interest rate curves derived from 6-month LIBOR

No amendments needed

1. IFAD's **financing agreements** generically refer to IFAD's reference rate therefore they do not need to be amended
2. IFAD's **billing cycle** is semi-annual ex-post and will not be amended

Background information on LIBOR Transition



IBOR Benchmarks: LIBOR, EURIBOR, EONIA

Play an important role in financial markets and act as reference rate for loans, derivative products, bonds and other financial products



Reasons for the reform

LIBOR has been subject to manipulation, scandal, and methodological critique, making it less credible today as a benchmark rate

New principles for financial benchmarks by International Organization of Securities Commissions (IOSCO)






- Benchmarks should be robust, reliable and resilient
- Alternative reference rates are globally decided and will apply to every financial institution after cessation of existing IBORS
- Alternative Reference Rates Committee (ARRC) in 2017 recommended to replace USD LIBOR by a risk free rate (RFR), called Secured Overnight Financing Rate (SOFR) <https://www.newyorkfed.org/arrc/sofr-transition>
- Also other IBOR rates, like GBP LIBOR, CHF LIBOR will be replaced. EURIBOR is not scheduled to be discontinued

The survival of LIBOR in its current form “could not and would not be guaranteed”.

— Andrew Bailey, The Future of LIBOR. Speech delivered by the FCA chief executive at Bloomberg, London. 27 July 2017

Transition from existing benchmarks to alternative reference rates

Country

	Currency	Existing reference rate	Alternative reference rate	Administrator	Transaction based?	Nature of transition
	USD	USD LIBOR	SOFR (Secured Overnight Financing Rate)	Federal Reserve Bank of New York	Yes	Replacement by Dec 2021 for 1w and 2m Replacement by June 2023 for all other tenors
	EUR	EONIA	€STR (Euro Short Term Rate)*	European Central Bank	Yes	Replacement by 2021
		EURIBOR	EURIBOR with new hybrid methodology	EMMI**	Partly	Reformed
	GBP	GBP LIBOR	SONIA (Sterling Overnight Index Average)	Bank of England	Yes	Replacement by 2021
	JPY	JPY LIBOR	TONAR (Tokyo Overnight Average Rate)	Bank of Japan	Yes	Replacement by 2021
	CHF	CHF LIBOR	SARON (Swiss Average Rate Overnight)	SIX Financial Information AG	Yes	Replacement by 2021

From USD LIBOR to SOFR



LIBOR

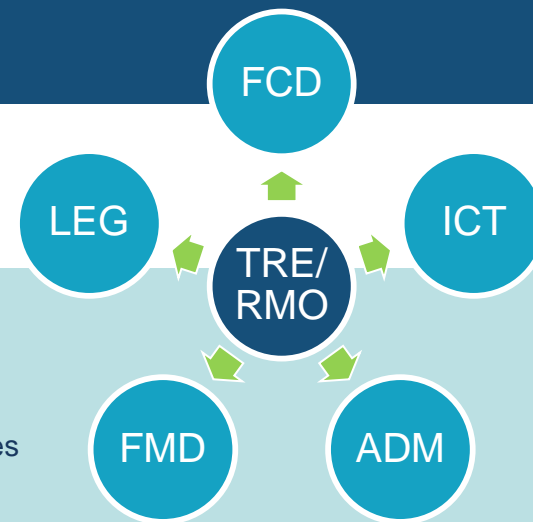
- Is based partially on market-data and partially on expert judgement
- Measures the cost of uncollateralized borrowing in the interbank market and incorporates a built-in credit-risk and liquidity component
- A forward-looking rate, published daily, with term rates from 1 day to 1 year

SOFR

- Relies entirely on transaction data from over \$700 billion in daily repo transactions
- Measures the cost of collateralized borrowing overnight based on interbank trades and secured by US Treasury securities
- A backward-looking rate, published daily

IFAD LIBOR Working Group

The LIBOR Working Group (WG) was established in May 2021
co-led by TRE and RMO



ToRs of the WG

- Assess impact of USD LIBOR Transition on all of IFAD's operations/ divisions
- Define steps to be undertaken so as to be prepared for cessation
- Coordinate steps and ensure communication of relevant information among parties
- Share market developments and trends

Decision

IFAD will stop using USD LIBOR as reference rate from 1 April 2022. SOFR will be the new reference rate

Summary of key issues identified

- Pricing of ordinary loans
- Communication with borrowers
- Billing cycle
- Financial instrument measurement and Reporting
- IFAD's swap documentation
- Other corporate documents



Impact on IFAD

Pricing of Ordinary Loans denominated in USD and SDR

- IFAD will continue following IBRD's loan pricing elements and, if approved by the Executive Board in December and endorsed by GC in 2022, apply IFAD maturity premia
- For Ordinary loans denominated in USD and SDR: from 1 April 2022 onwards, IFAD will use the daily compounded SOFR as new reference rate and continue applying the other pricing elements of IBRD
- For Ordinary loans denominated in EUR: Euribor 6m will not be discontinued so it will continue to be applied for EUR denominated loans

Transition to SOFR

Elements of pricing for loans denominated in USD

Example

Variable, market based	Libor 6 m	Daily compounded SOFR
Variable, based on IBRD	IBRD funding cost over Libor	IBRD funding cost over SOFR
Fixed	IBRD contractual spread	IBRD contractual spread
Fixed	IBRD maturity premium	IFAD maturity premium



The transition from LIBOR to an RFR-based rate should avoid any transfer of economic value between the parties

Impact on IFAD

Communication with borrowers

From 1 April 2022 onwards, IFAD will publish the quarterly spread for ordinary loans at the beginning of each quarter to be applied over daily compounded SOFR

IFAD will roll out a communication plan to the replacement of USD LIBOR, that involves

- Official communication to borrowers that USD LIBOR will be replaced by SOFR
- Updating IFAD's website
- Creation of FAQ for borrowers in line with practice of other IFIs



- Updating the versions of the interactive toolkit and the Guidelines for IFAD Financing Terms and Conditions available on IFAD's website
- Holding clinics and seminars upon request by the borrowers

Impact on IFAD

Billing cycle, financial instruments, reporting and Swaps



Billing cycle

The billing cycle remain unchanged. IFAD will continue billing every six months ex post. Preliminary tests on IFAD's system show that they can support the upload of daily SOFR rates. IT impacts are under testing and so far not foreseen



Financial Instrument measurement and Reporting

As of 2022, measurement of financial instruments denominated in USD or SDR will be based on zero coupon curves applied for various NPV calculations will be derived from swaps against the SOFR rate; curves are already published by financial data providers



Swaps documentation

All IFAD swaps entered into on or after 25 January 2021 incorporate the 2006 ISDA definitions and the fallback clauses introduced in January 2021 with ISDA's IBOR Fallbacks Supplement apply automatically to these swaps. For seven legacy swaps entered into traded before 25 January 2021, IFAD is liaising with its derivative counterpart amend these trades in order to incorporate contractual fallbacks



Other corporate documents to amend (minimal changes)

- IFAD's General Terms and Conditions for procurement contracts
- The General Conditions for Agricultural Development Financing, the Policies and Criteria for IFAD Financing and the recent Framework on IFAD Financing Condition



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**THANK
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