

Sterling Libor transition: Loan delays

Hot on the heels of our latest [IBOR reform report](#), the working group on sterling risk-free rates has put out a statement on the difficulties encountered in transitioning the loan market. In spite of the delay, the transition should be achieved by 1Q21. Meanwhile, the focus on fallback spread adjustments intensifies



Source: Shutterstock

Loan laggards: New deadline in 1Q21

Regular readers of our Libor reform updates would not be surprised that loans are proving to be one of the slowest markets to transition.

Given the lack of public data, how slow is hard to say, but the working group on sterling risk-free rates noted key milestones in bilateral and syndicated loans referencing Sonia. The working group has already [acknowledged, at the end of March](#) that the coronavirus pandemic was affecting the shift. [The latest update](#) admits complete transition by the original 3Q20 deadline will not be feasible.

The new hard deadline for the issuance of Libor-referencing loans is the end of 1Q21 but the

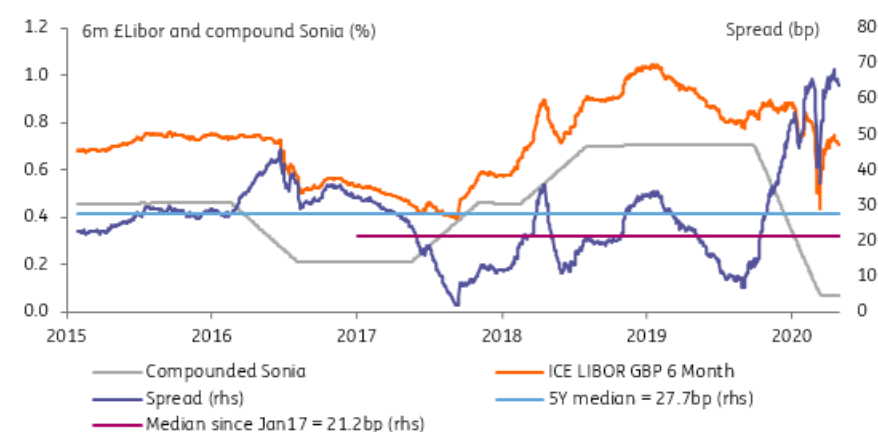
working group wants lenders to be in a position to offer non-Libor linked products by the third quarter of this year. What's more, the new deadline doesn't preclude the need to include contractual arrangements to facilitate conversion by the end of 2021 when the demise of Libor is planned.

Focus on fallback calculation

The extended timeline in loan transition does not mean progress has stalled in other areas, on the contrary. Fallback spread methodology has become a key focus after the ISDA published its members' favoured spread adjustment method, and after [respondent to the working group survey on fallbacks in cash products](#) expressed their preference an approach consistent with derivatives.

Ahead of Bloomberg publishing fallback adjustment spreads for the main currencies, we provided estimates and explanatory notes in [our latest Ibor transition report](#). We re-produce the chart below showing how the fallback spreads from 6 months Libor to Sonia will be calculated.

Fallback calculation: 5Y median of the Libor-counpounded Sonia spread



Source: ICE, BOE, ING

There is no saying where that spread will eventually settle but the length of the lookback window (the spread will be calculated as the 5-year median between Libor and compounded Sonia) and the proximity of the trigger event (by the end of 2021 we presume), means that it should not diverge too much from its value if it was calculated today.

As things stand, we think between 20bp and 25bp is a realistic estimate.