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LENDERS TEST TRANSACTIONS ON LIBOR SUCCESSOR SOFR

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State Bank of India (SBI) and ICICI Bank recently executed a couple of transactions after the Reserve Bank of India (RBI) wrote to banks in August last year to sensitize them about the transition. RBI also asked banks to identify exposures linked to Libor. India’s exposure to borrowings linked to the benchmark is estimated to be around $331 billion.

Both SBI and ICICI Bank have executed interbank money market deals through their Hong Kong branches with SOFR, launched by the New York Federal Reserve in 2018. SOFR is based on transactions in the US Treasury repo market and is being widely used as a substitute for Libor in dollar-denominated loans and derivatives across the world.

SBI has formed a committee to ensure a smooth transition from Libor to alternative reference rates. “A working group has been created, and a steering committee is overseeing the transition. We are also assessing the size of the total book to Libor. It is not just loans but derivatives, too, and not just assets but liabilities, too, where the bank has borrowed from others," said Chalasani Venkat Nageswar, deputy managing director (international banking group), SBI.

Experts pointed out that the transition might not be mandatory by the end of this year. According to Anant Narayan, associate professor of SP Jain Institute of Management and Research, regulators are keen that there should be minimal disruption on account of this change. “Nevertheless, the market is preparing for Libor transition as eventually inevitable," said Narayan.

Indian banks are, of course, not alone in this and the frenzy in global banks is much greater. Similar to SBI, global banks have formed large teams working actively on this transition. “It is almost like a mini-Y2K moment for them," said Narayan.

The transition became necessary after it was discovered that banks were manipulating the rate in 2007-08 that sparked an investigation by Britain’s Financial Services Authority (FSA). Libor rates over tenors are calculated as averages of rates polled by major banks and used for pricing debt instruments and derivatives like currency swaps and interest rate swaps.

In August 2020, RBI issued a ‘Dear CEO’ letter to all commercial banks sensitizing them about the need to be prepared for the Libor cessation. Then, in November, governor Shaktikanta Das said that Indian Banks’ Association has been working with market participants to facilitate the transition.

“Most of the banks are trying to do these trades to check internal systems and to understand the client journey by executing a few transactions. The clients also will be able to assess the risk management required in the new transitioned hedging environment," said Ashhish Vaidya, head of treasury, DBS Bank.

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