Friday, December 14, 2018 6:44 AM ET

Libor administrator may continue use of tainted benchmark after 2021

By Jon Rees

Finance companies that use the benchmark interest rate Libor to underpin contracts are being asked for information which could see the controversial measure remain in use after its supposed 2021 cut-off date.

Libor, or the London interbank offered rate, has been used for decades to set the interest rate on millions of derivatives, bonds, credit cards and loan contracts worldwide.

The Financial Conduct Authority and the Bank of England have repeatedly told the market that Libor was on borrowed time.

It is set by a panel of banks that provide information on interest rates for unsecured wholesale bank borrowing. But there are relatively few of these transactions and the absence of active underlying markets raises a "serious question" over the future use of Libor, according to the FCA. The regulator has said that from 2021, banks will no longer be required to submit the daily rates which together make Libor.

Regulators want companies to stop using Libor by the end of 2021 after a series of attempts to fix the rate involving numerous banks and traders were revealed, which saw banks fined and traders jailed. The FCA has said continued use of Libor is a risk to financial stability and has demanded that banks and insurers provide a board-approved summary of their plans to mitigate the risks of moving from Libor by Dec. 14.

However, the ICE Benchmark Administration, which administers Libor, has now issued a survey to all users of the rate and said it would use the results to work with banks to continue to publish Libor rates after 2021. These could be used for Libor-linked contracts which cannot make use of any other benchmark rate, it said. The survey closes in February 2019.

Banks' support

"[The] IBA will use the results of the survey to inform its work in seeking the support of globally active banks for the publication of certain Libor settings after year-end 2021. The primary goal of this work would be to provide those Libor settings to users with outstanding Libor-linked contracts that are impossible or impractical to modify," the survey said.

The survey asks finance firms for information on which Libor currency and length of contract they use most and why and for which they want the IBA to work on agreement with banks to continue to publish Libor settings after 2021. The IBA noted, though, that regardless of the results of the survey there is no guarantee that any Libor settings will continue to be published after 2021.

Alternative benchmarks favored by the regulators are making little headway, however.

Sonia, or the sterling overnight interbank average rate, is one of the leading alternatives to Libor. It has been available since 1997 but was reformed by the Bank of England in April 2018.

It is based on transactions reported to the BoE providing representative coverage of the market. The central bank said in its most recent financial stability report that although there had been a pickup in the volume of Sonia futures contracts traded the total was still "negligible" compared with Libor contracts. The U.S. Federal Reserve has undertaken a similar process to the Bank of England and identified SOFR, the secured overnight financing rate, as the preferred risk-free rate for dollar markets.

The International Swaps and Derivatives Association said Sonia accounted for just 3%, or $5.9 trillion, of the $179 trillion interest rate derivatives traded to the end of the 2018 third quarter. In contrast, Libor underpinned 55% or $98.45 trillion of interest rates derivatives contracts.