UK FINANCE

LIBOR TRANSITION READINESS SURVEY

August 2020

UK Finance

UK Finance is the collective voice for the banking and finance industry.

Representing more than 250 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation.

We work for and on behalf of our members to promote a safe, transparent and innovative banking and finance industry. We offer research, policy expertise, thought leadership and advocacy in support of our work. We provide a single voice for a diverse and competitive industry. Our operational activity enhances members' own services in situations where collective industry action adds value.

At the request of UK Finance's members, a dedicated project team was created in January 2020 to support the industry on LIBOR transition across all UK Finance Product and Service Streams. Access to UK Finance's LIBOR transition project is open to all members. UK Finance members who are not engaged in our LIBOR transition project work can contact the team at liborcoreteam@ukfinance.org.uk.

FOREWORD

The transition away from LIBOR before the end of 2021 is a significant undertaking across the financial services industry and its clients. For both the industry and its customers this is a major undertaking, being driven in the sterling market by the Working Group on Sterling Risk-Free Rates (the 'RFR Working Group') to coordinate this in a timely and smooth manner. There is a widespread recognition that the transition is fundamental and it is critical to respond to the unsustainability of LIBOR for the long term and move across to more robust rates.

The transition impacts a significant proportion of UK Finance's diverse membership across different segments, operating models and products. A key facilitator of transition is transparency across the market, particularly in products which have had less public visibility and where there is significant work to do to be ready for the end of 2021. UK Finance members are working intensively to ensure that they and their customers are ready.

In producing this detailed survey of sterling LIBOR transition status, we hope to provide our members with good visibility across the market and selected products so that they can assess the status of their transition plans compared to the overall state of readiness across the industry. The survey will also assist UK Finance to identify areas in which further work and support may be necessary. Individually and collectively, we hope this will help ensure that we achieve the RFR Working Group's milestones, even where this requires an acceleration of efforts in the short term. We also hope the report published will give stakeholders a better understanding of the remaining barriers to the transition and the different pictures between products.

The discontinuation of LIBOR (and the move to risk-free rates) is an initiative led in the sterling market by an industry working group, the RFR Working Group, supported by the Bank of England and the Financial Conduct Authority (FCA). More information on the RFR Working Group and all of its publications can be found **here**. UK Finance is actively engaged in the RFR Working Group and several of its subgroups. For the avoidance of doubt, while UK Finance is a member of the RFR Working Group, this publication is not in any way an RFR Working Group publication, nor does it necessarily reflect the group's views, though it is intended to help inform the group with a diverse evidence base from across UK Finance's membership.

Finally, we also note that there is an increasing wealth of guidance for firms on how to consider their own LIBOR transition plans. This report does not seek to replicate these. Our intention is to provide a picture of the status of readiness across UK Finance's membership to support all relevant stakeholders in ensuring that the transition away from LIBOR can be completed as promptly and as smoothly as possible.

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Notes on methodology and objectives

Around 90 members from across all segments of our membership are currently engaged with LIBOR transition. This survey was provided to all firms and achieved a completion level of over 70 per cent spread across a wider range of the membership including all large UK clearing banks. This highlights the importance of the issues relating to LIBOR transition to our members and the wider market.

The total number of respondents was 64 firms.

All responses are weighted equally which is particularly important to note for questions involving readiness status and future plans.

The survey was run in June 2020 and reflects responses at this point in time. We anticipate running the survey again in Q4 2020. We expect it will reflect the significant progress anticipated in the RFR Working Group's roadmap for the remainder of 2020, as amended to accommodate Covid-19 disruption.

1) EXECUTIVE SUMMARY

Part one of this report covers the overall findings from UK Finance's members on their LIBOR transition readiness and planning as of June 2020. This is intended as a high-level snapshot survey and is not a complete or detailed assessment of transition across the sterling market.

There is a high level of awareness of the importance of LIBOR transition and the RFR Working Group's roadmap. Progress across the financial services industry has demonstrated action underway to achieve this. The development of products referencing alternative rates has started for most respondents across all the different product ranges. Over half of all firms expect their LIBOR exposures to reduce in 2020. However, at this stage many respondents reported an intention or necessity of relying on tactical solutions this year to offer alternative rates and are waiting for progress on market conventions and it was clear the pace would increase with some key enablers.

Given the diversity of firms responding to the survey, which included all UK clearing banks through to international, smaller and challenger banks as well specialist and non-bank finance providers, responses were understandably mixed. It should also be noted that for some respondents (and some of the non-respondent members) LIBOR transition is relevant to a very small number of customers. In other cases, LIBOR transition impacted only the lender itself, i.e. its own funding or liquidity was LIBOR linked, but it does not have to transition individual customers or offer LIBOR-linked products.

A number of firms noted not only the disruption that Covid-19 has posed to transition, but also the very significant implications this has in the UK on business borrowing. Recent months have seen four major government lending schemes launched, including the Bounce Bank Loans Scheme (BBLS), the Coronavirus Business Interruption Loan Scheme (CBILS), the Coronavirus Larger Business Interruption Loan Scheme (CLBILS) and the Covid Corporate Financing Facility (CCFF). The industry believed that the priority was the successful delivery at pace and scale of the CBIL and CLBIL schemes, which in in some cases required the flexibility for these to be on a LIBOR-linked basis for a number of lenders. UK Finance data on **business lending** and data on the government lending schemes can be found at **https://www.ukfinance.org.uk/data-and-research/data**. However, amongst CLBILS and CBILS, it was reassuring to note that firms had LIBOR transition as a key consideration in mind as well as the RFR Working Group's milestones.

Legacy exposure will be mostly transitioned from Q1 2021 across a wide range of products and we expect future iterations of the survey will begin to show this starting at scale.

Part two of the report provides a detailed cash product by product summary of responses. These unsurprisingly show a different picture of transition status as well as current and anticipated plans. The results by product, including preferred replacement rate, do not constitute any UK Finance view on the appropriateness of such rates but simply seek to factually report aggregated views received. For many firms, their transition plans only feature a small number of products and, as was evident from responses, particularly in mortgage products, transition was more of a legacy question than a current new lending one. Across all products the different direction and pace of travel still involves a timely move away from LIBOR.

There is clearly significant progress underway across the industry over all products. The coming months will see a number of crucial and anticipated transition enablers, in particular from the RFR Working Group, which will clearly assist firms in accelerating the transition away from LIBOR. UK Finance will continue to work to provide visibility to the industry and its customers on this progress so that everyone can be ready for a world without LIBOR after 2021.

2) PART 1 – OVERALL FINDINGS ON LIBOR TRANSITION READINESS AND PLANNING

A. A transition working in line with the RFR Working Group expectations

Our survey revealed broad awareness of the RFR Working Group's milestones and the appropriateness of these. The flexibility provided on some of the shorter-term milestones in the immediate aftermath of Covid-19 disruption was welcome.

The majority (57 per cent) of the industry expects LIBOR exposures to reduce through the remainder of 2020. The RFR Working Group has stated that by Q1 2021 there should be a significant reduction in the stock of contracts referencing LIBOR, and various regulatory statements have suggested that the UK official sector will keep a close eye on the market and individual firms' exposures with an expectation that these would start to decrease as we progress towards end-2021.

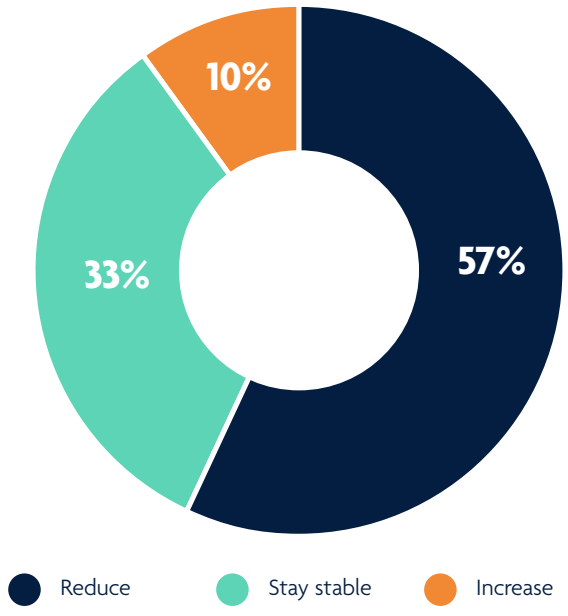
A significant part of the industry think exposure for this year will remain stay stable (33 per cent). Only ten per cent expect to see an increase.

Of those who do not expect a reduction this year, one of the key reasons cited is client demand for LIBOR, and limited customer awareness of the alternatives. Market liquidity for alternative rates also came up as a concern. Beyond these fundamentals which the RFR Working Group is seeking to address currently, further work on infrastructure and systems being required was reported by many firms, with some noting that this has slowed down efforts to reduce LIBOR exposure.

For smaller banks and lenders in particular, Covid-19 has also created challenges, including a redirecting of resources towards different priorities in supporting customers on a more immediate basis with more limited resources. In some cases this has also delayed the intended launch dates of alternative product suites.

However, overall the industry has maintained progress, with the RFR Working Group welcoming the "first syndicated loan that will link to SONIA and SOFR, the first bilateral loan referencing SONIA in the social housing sector, and another successful consent solicitation to convert a legacy LIBOR referencing bond".[1]

Chart 1. Chart showing respondents' expected change in LIBOR exposure in 2020



1. https://www.bankofengland.co.uk/-/media/boe/files/markets/benchmarks/rfr/rfrwg-further-statement-on-the-impact-of-coronavirus-on-timeline-for-firms-libor-transition-plans.pdf

Respondents' views on the updated RFR Working Group milestones

Across the industry, development of new products in the cash markets referencing alternative rates is underway and picking up pace.

31 per cent of respondents plan to offer exclusively alternative rate linked products from the end of Q3 2020. A significant part of the market is moving into Q4 2020 looking to offer exclusively alternative rates to LIBOR. 44 per cent plan to continue to include LIBOR with pre agreed conversion mechanisms, aligning with the revision to the Q3 milestone in which lenders may now continue to offer new and re-financed LIBOR-linked loan products provided they 'include contractual arrangements ... to facilitate conversion ahead of end-2021, through pre-agreed conversion terms or an agreed process for renegotiation, to SONIA or other alternatives'.[2] This is primarily the case for corporate and commercial lending where LIBOR is still a prevalent reference rate as at July 2020. The scale of the challenge for corporate lending is significant. Within the survey around a third of respondents reported LIBOR corporate loans books over £500million – with a total exposure of over £10 billion the rationale to develop alternatives for new lending is clear. The RFR Working Group's guidance and expectations for LIBOR offering post Q3 2020 has been well noted by the industry. However, there is an indication that RFR Working Group messaging on milestone changes may not always filter through, with some examples of outdated references to the 'milestone' of cessation of any LIBOR lending beyond end Q3 2020.

The lack of awareness of clients about the transition is cited again by many respondents as one reason for continuing to offer LIBOR. Clients may also be reluctant to switch rates, considering LIBOR the most familiar and therefore still preferable option, until they see a visibly significant proportion of the market shifting to alternative rates. Knowledge and experience of SONIA amongst many clients remains low, impacting both demand and readiness. Some respondents, particularly smaller and specialist lenders, noted they have closed books and therefore the issue of offering new products will not be relevant to them.

Chart 2. Have you started developing new cash products referencing alternative rates?

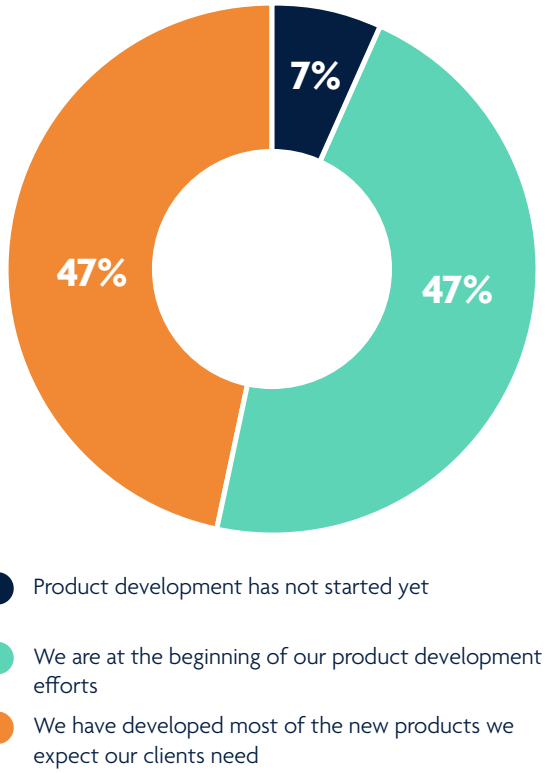


Chart 3. What are your expectations when it comes to product offerings from the end of Q3 2020?

2. https://www.bankofengland.co.uk/-/media/boe/files/markets/benchmarks/rfr/rfrwg-further-statement-on-the-impact-of-coronavirus-on-timeline-for-firms-libor-transition-plans.pdf

When providing additional comments on what informed their decisions on product offerings beyond Q3 there was acknowledgement that by continuing to offer LIBOR-linked loans after this point firms would be increasing the required legacy challenge for 2021, in terms of remediation of legacy contracts, with a noted desire to reduce this risk. Other key findings of note included fairly high LIBOR exposure in mortgages also, with both commercial and retail mortgages seeing around one in five respondents estimating exposures of over £100 million. Total LIBOR exposure in retail mortgages is estimated at over £5.6 billion and commercial mortgages over £5.5 billion.

B. SONIA compounded in arrears is the primary transition rate, but not the only one

Overall, our results demonstrated that, as the RFR Working Group has long noted, SONIA compounded in arrears will be the primary alternative replacement rate for sterling LIBOR contracts. 90 per cent of new loans by value was the estimate from the SONIA Term Rate Use Case Task Force.[3] Our results echo this as the direction of travel in firms' transition plans. However, they also highlight that SONIA compounded in arrears is not the only alternative rate being considered with some products in particular gravitating to other replacement rates which the Use Cases paper again foresaw.

Most members who responded to this question did not change their plans following the Use Cases Paper (63 per cent), which illustrates that transition towards SONIA compounded in arrears was happening already.

The transition to the Bank of England Base Rate (BoE Base Rate) will be important to consider. For our respondents, a significant part of the transition is expected to be to this rate. Part two of this report demonstrates the importance for some products such as trade and working capital products (29 per cent), commercial mortgages (55 per cent), retail mortgages (50 per cent) and Invoice Finance (50 per cent).

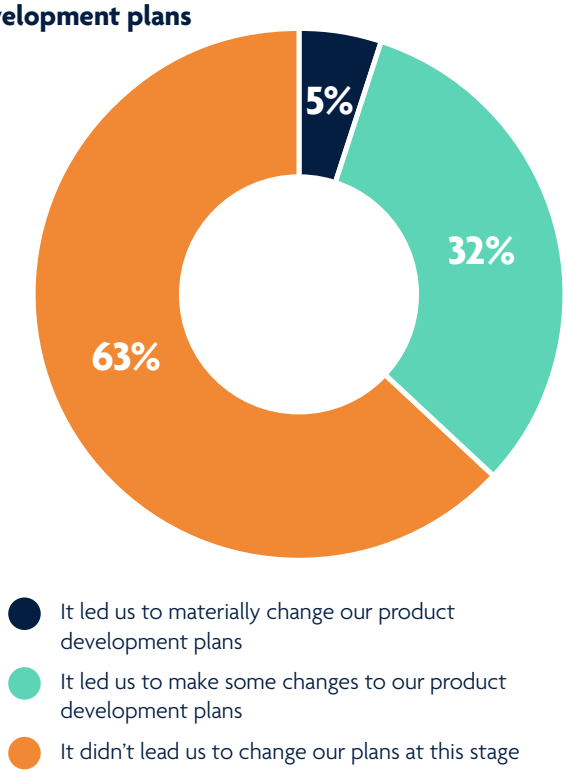
Many respondents called for the RFR Working Group to work on the calculation of spreads between LIBOR and the BoE Base Rate. This is also referenced below as an important potential enabler of active transition. Around 33 per cent of respondents said the publication of a credit adjustment spread between LIBOR and other alternative rates would be highly significant as an enabler for transitioning legacy contracts.

C. The transition for new contracts is starting but significant progress is required in the cash markets

As the RFR Working Group itself has acknowledged, whilst transition in the derivatives market has progressed significantly and recent developments from ISDA will assist in this regard, the 'big challenge' for 2020 was replicating this in the sterling cash market.[4][5] Progress across products in the cash market has depended on the product and this is the focus of this report.

In the cash markets, only seven per cent of firms who responded had not yet started alternative rate product development.

Chart 4. To what extent has the publication of this guidance impacted existing or upcoming product development plans



3. https://www.bankofengland.co.uk/-/media/boe/files/markets/benchmarks/rfr/use-cases-of-benchmark-rates-compounded-in-arrears-term-rate-and-further-alternatives.pdf
4. https://www.isda.org/category/legal/benchmarks/
5. https://www.bankofengland.co.uk/-/media/boe/files/speech/2020/turbo-charging-sterling-libor-transition-why-2020-is-the-year-for-action-speech-by-andrew-hauser.pdf

In terms of the dependencies cited, market conventions were noted as the number one dependency, highly significant for 36 firms. This was followed by infrastructure readiness (29 firms) and the publication of a SONIA compounded index (24 firms). We note at the time of this survey, discussions around the compatibility of the Bank of England SONIA Index and likely market preference in terms of conventions were still ongoing. The publication of SONIA term rates was also flagged by many respondents as important.

Engagement with clients has started but remains at an early stage

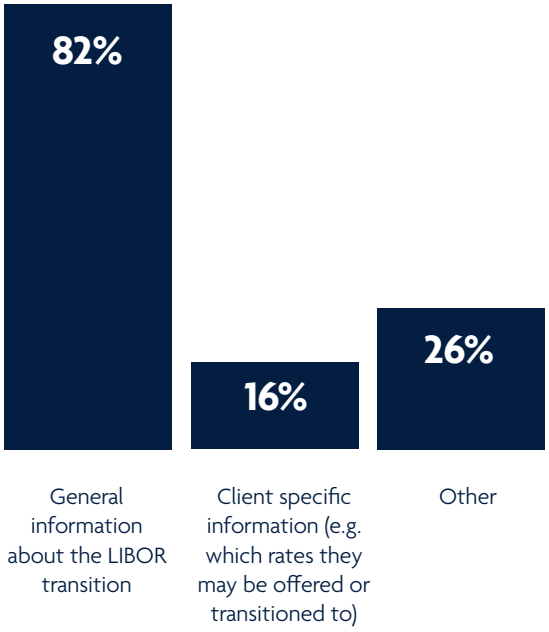
Most banks and lenders have begun engagement with their clients on the LIBOR transition, with 39 per cent of firms having engaged with either most or all of their clients. Only 28 percent of firms are still in the process of planning, with actual client engagement yet to start.

However, there is a clear need to be careful when referring to 'engagement'. To date the overwhelming majority (82 per cent) has just sent general information about the transition. Only 16 per cent have sent their client specific information, such as the rate they may be offered or transitioned to. It was noted that in a small amount of cases, client specific communication has been initiated by individual 'market aware' customers themselves, due to their concern about issues such as price difference between LIBOR and alternative rates. However, this level of market awareness amongst customers should not be relied upon as a common occurrence, with results showing that many firms are finding their customers' focus is not yet on LIBOR transition.

When asked if there were any further initiatives the RFR Working Group or other LIBOR transition stakeholders could take to facilitate greater engagement with clients, 48 firms felt additional steps could be taken. While many of these centred on general calls to drive greater transition awareness and wider transparency into areas of development (e.g. tough legacy), some more specific suggestions were also provided, for example, webinars, risk disclosure documents, check lists of what to do, have all been cited as means to explain the transition with clients. The results show a good engagement with Non-Financial Counterparties (NFCs) with 75 per cent of respondents having communicated with them.

Chart 5. Have you started engaging with your clients to explain the transition?

Chart 6. Where your engagement with clients has started, what type of communications have you shared with them?



Most client communication programs impacted by Covid-19 will have been resumed by Q3 2020, with less than ten per cent of firms thinking it will take longer than this. 37 per cent of firms have already resumed these communications.

Very few clients are ready to transition, which appears to be the single biggest barrier to transition in the medium term. The only firm who responded that they felt their clients were ready noted that this was because their LIBOR exposure did not lie in client products and therefore they would not have to tackle this issue of communication. A majority of respondents said their clients were progressing towards it (49 per cent).

Around a third of respondents felt their clients are currently not focusing on transition, which is a concern we expect will be addressed in forthcoming communications from the RFR Working Group to corporates. The Outreach and Communications subgroup of the RFR working group had plans for an outreach push in early 2020. These were put on hold due to Covid-19, but there is awareness that this should start to resume, with education for firms with both sophisticated and limited financial expertise remaining a central focus of the group's objectives. Similarly, the UK Finance guide for business customers on Discontinuation of LIBOR, originally published in November 2019, was due to be relaunched to reflect developments at the beginning of 2020.[6] This will be published shortly as the expectations for corporates and the revision of interim milestones continue to become clearer.

Next steps in client communications

Our survey across the industry demonstrated a consistent recognition of the collective and individual effort required to raise awareness on the transition and the material needed to support client education.

At the start of 2020, the RFR Working Group in conjunction with the Association of Corporate Treasurers and the CBI published an education document called **Calling time on LIBOR: Why you need to act now** aimed at businesses.[7] This was followed in March 2020

Chart 7. If you have begun to communicate with clients, which have you engaged with so far?

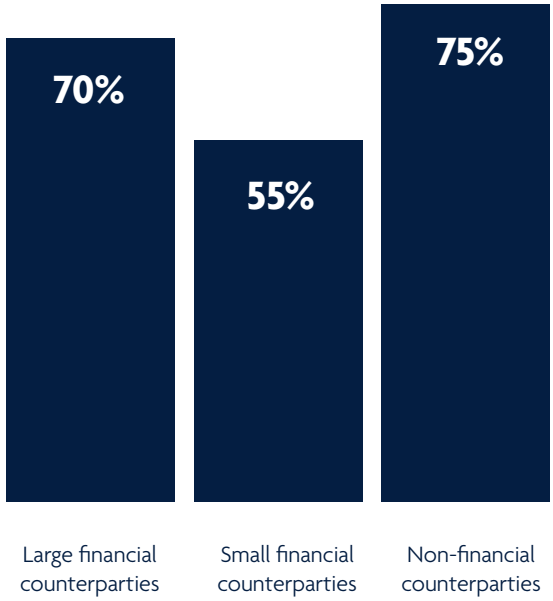
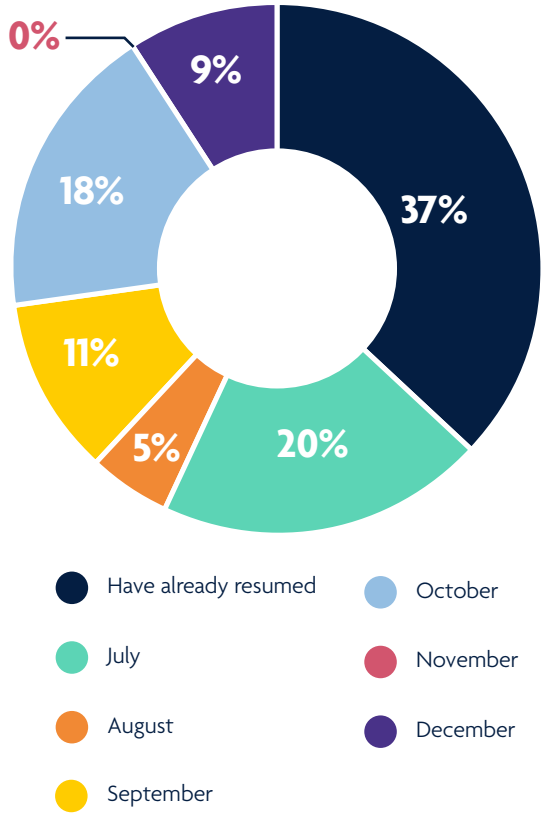


Chart 8. If your customer communication has been impacted by Covid-19, as it currently stands when to do you expect to broadly start/resume your communication



6. https://www.ukfinance.org.uk/system/files/LIBOR-Guide-for-Business-Customers-FINAL_1.pdf
7. https://www.bankofengland.co.uk/-/media/boe/files/markets/benchmarks/rfr/factsheet-calling-time-on-libor-why-you-need-to-act-now.pdf

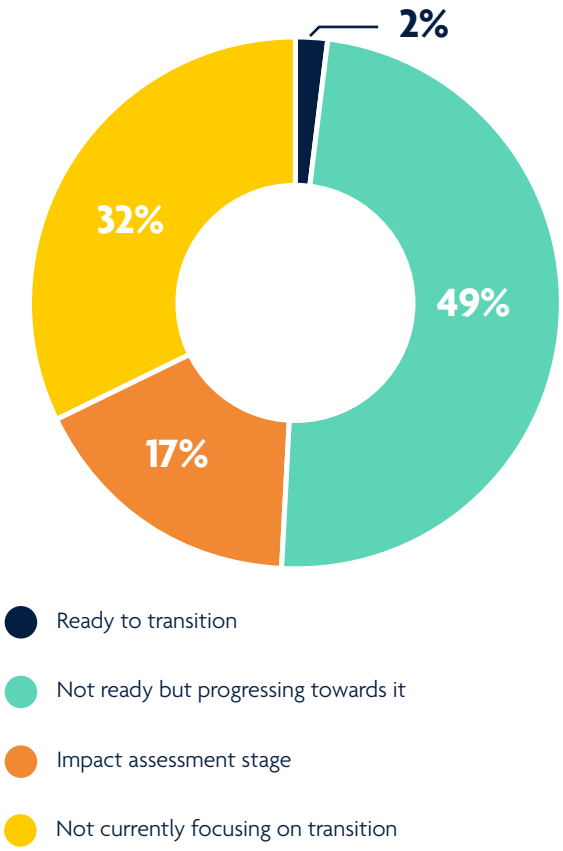
by a letter from the authorities to trade associations representing businesses addressing the **Next Steps on LIBOR Transition** and encouraging them to ensure their memberships were engaged with the transition and recognised the importance of it for them.[8] Clearly the RFR Working Group has publicly acknowledged the immediate disruption Covid-19 posed to end user engagement. However, despite reflection of the short-term disruption within the milestones proposed by the RFR Working Group for 2020, the end-2021 date for cessation of LIBOR means that customers must now be engaged and engage themselves in the transition's implications. This was identified by a significant number of lenders as a key dependency for ensuring the RFR Working Group goal of a significant reduction in the stock of GBP LIBOR referencing contracts can be achieved, with over half the firms who expect their LIBOR exposure to increase or stay stable in 2020 (see Chart 1.) citing a lack of customer engagement and demand as a contributor to their limited progress.

While there is a broad recognition of the importance of firms ensuring communication with their clients is appropriately timed and detailed, some firms cited the benefit of collective communication to end users of LIBOR.

The Outreach and Communications subgroup of the RFR Working Group has a key role to play and UK Finance and a number of our members are actively engaged in this group. A number of respondents considered what further tools this group could use. Examples included webinars on technical issues which lenders could reference within, or use to supplement, individual lender communications. Many larger banks have produced extensive collateral for use with clients and customers, which was not always possible or feasible for smaller lenders.

It is in everyone's interest that the LIBOR transition is treated as a two-way process and that client businesses of all sizes, including SMEs, engage with the transition, even where lenders are taking a leading role. The remainder of 2020 will need to see a concerted step-up in engagement across a wide range of stakeholders.

Chart 9. From engagement to date, how ready do you feel your firm's clients are for transition?



8. https://www.bankofengland.co.uk/prudential-regulation/letter/2020/next-steps-on-libor-transition

D. Transition for legacy contracts

Transitioning legacy contracts will be a key focus of next year

While significant advancement has been made in the development of non-LIBOR product offerings, the transition of legacy contracts is a critical focus of the next steps for progress as end 2021 moves nearer. The government and the FCA have both made clear that all parties should continue to work to actively transition legacy contracts and highlights this is the best way for lenders and borrowers to have certainty and maintain economic control of this action. This is clearly also recognised by the RFR Working Group and the industry as a whole. The results of this survey align with Andrew Bailey, Governor of the Bank of England, referring to the transition of legacy contracts in a recent speech as 'the endgame', with the majority of firm's identifying 2021, particularly post-Q1, as the year of transitioning legacy contracts across product segments (see part 2).[9]

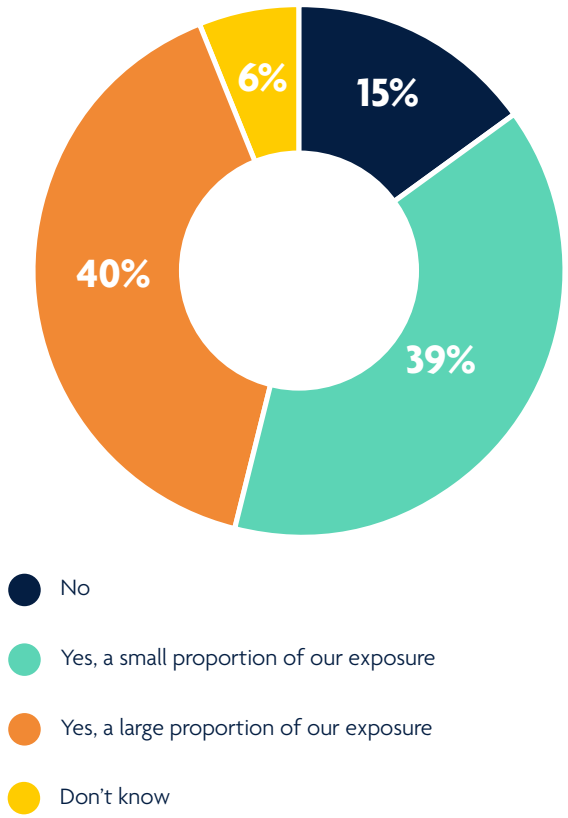
A number of firms recommended increased cross-industry engagement with less sophisticated corporates, in particular those identified by the Use Cases paper as counterparties for which SONIA compounded in arrears was not appropriate. Many respondents called for greater external engagement on market conventions and the finalisation of this process for all alternative rate options before their plans for legacy contract transition can be determined.

The expected publication of a Cash Legacy paper from the RFR Working Group will help advance this with guidance on active transition. A number of UK Finance members articulated the benefit of a consistent methodology for calculating a spread for legacy contracts as a key transition enabler.

Equally, as evidenced in part 2 of this report, the transition away from LIBOR will involve the migration to a number of replacement rates, with the BoE Base Rate important for many. A transition to BoE Base Rate in place of LIBOR will require an appropriate credit spread adjustment to be determined. We are not aware of any collective consideration yet having been undertaken to develop that methodology. A common methodology would considerably reduce conduct risk in the market, providing assurance that would speed up the transition in segments of the markets where SONIA compounded in arrears may not be the most appropriate. While SONIA and BoE Base Rate are more closely aligned than other rates, using the same credit spread adjustment as the one used to transition from LIBOR to SONIA may not be adequate.

It is clear from the survey results that 2021 will require significant steps to actively transition contracts where possible. Additional enablers could help this and reduce the reliance on potential legislative solutions, which the RFR Working Group has been clear should be only for contracts that cannot be dealt with in any other way.

Chart 10. Do you have any outstanding legacy exposure that has not been amended to include appropriate fallbacks?



9. https://www.bankofengland.co.uk/speech/2020/andrew-bailey-speech-as-part-webinar-hosted-by-the-boe-and-the-frb-of-ny-libor-entering-the-endgame

Legislative support on tough legacy contracts is welcome

The provision of market input on the issues of tough legacy contracts, those which cannot be converted or amended to include fallbacks ahead of LIBOR discontinuation, was identified as one of the RFR Working Group's top-level priorities for 2020. The results of this survey confirm the necessity of the Chancellor of the Exchequer's announcement on 23 June that the government intends to bring forward legislation that could help deal with the problem of 'tough legacy' contracts that cannot transition away from LIBOR (as identified in the RFR Working Group's Tough Legacy report published in May). Through this, the provisions of existing benchmark regulations will be amended to grant the FCA powers to require a change of methodology to a critical benchmark if it is deemed no longer representative, offering a possible solution for legacy contracts that cannot be amended. This will go in parallel with a prohibition to use the benchmark in new contracts.

Chart 11. Taking into account the findings of the Tough Legacy Task Force paper, do you have any outstanding legacy exposure to LIBOR which you expect may end up being tough legacy

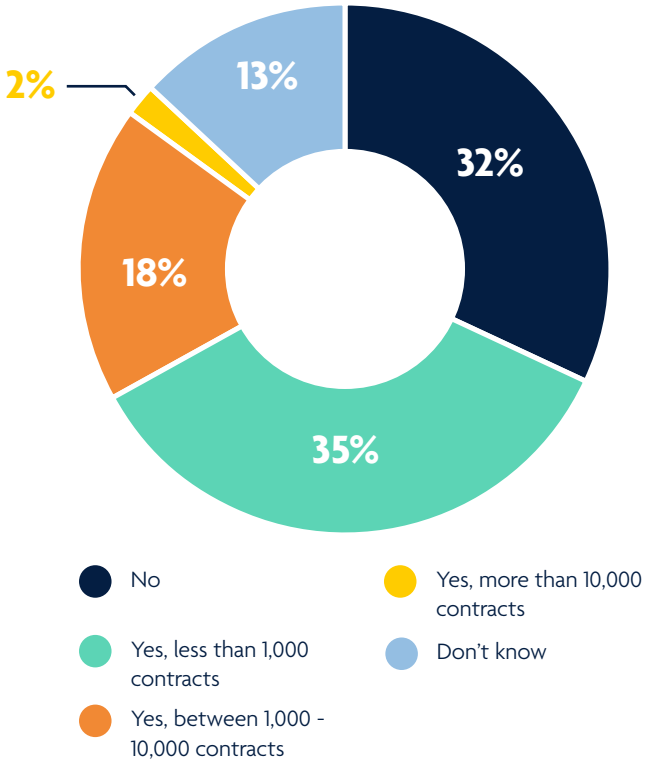
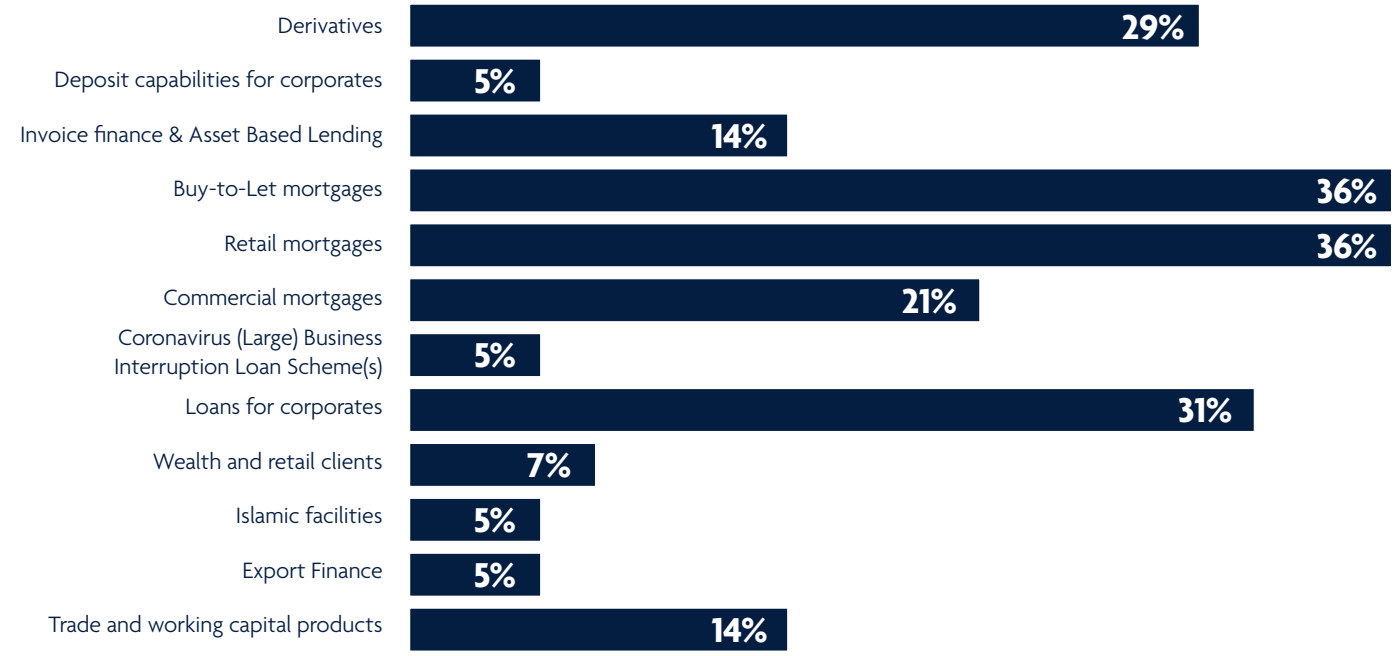


Chart 12. Chart showing which product categories respondents expect to find tough legacy contracts in their LIBOR exposure



This survey was opened and circulated prior to the announcement which addresses many respondents concerns and requests for transparency into how the RFR Working Group's recommendation of a legislative solution was to be taken forward.

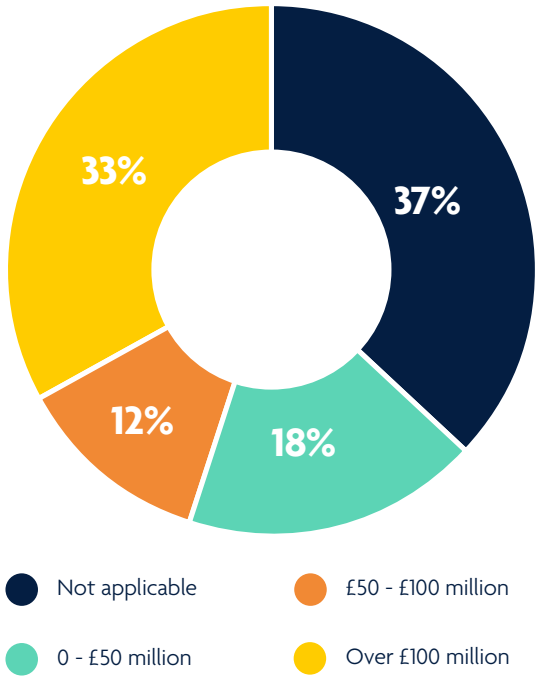
However, market participants should continue to focus on active transition, as this is the only way for parties to have certainty over the timing and substance of transition, with the legislative solution only replied upon where there is genuinely no other possible alternative.

Fallbacks and tough legacy contracts

20 per cent of respondents have more than 1000 contracts which they expect to end up being tough legacy. The value of these contracts has been estimated to be over £100 million for a third of respondents.

36 per cent of respondents with tough legacy exposure flagged this may be in their mortgage portfolios. Corporate loans also make a part of their tough legacy interim assessment for 31 per cent of respondents.

Chart 13. Chart showing respondents' estimations of the outstanding value of their LIBOR-linked contracts which could be identified as tough legacy.

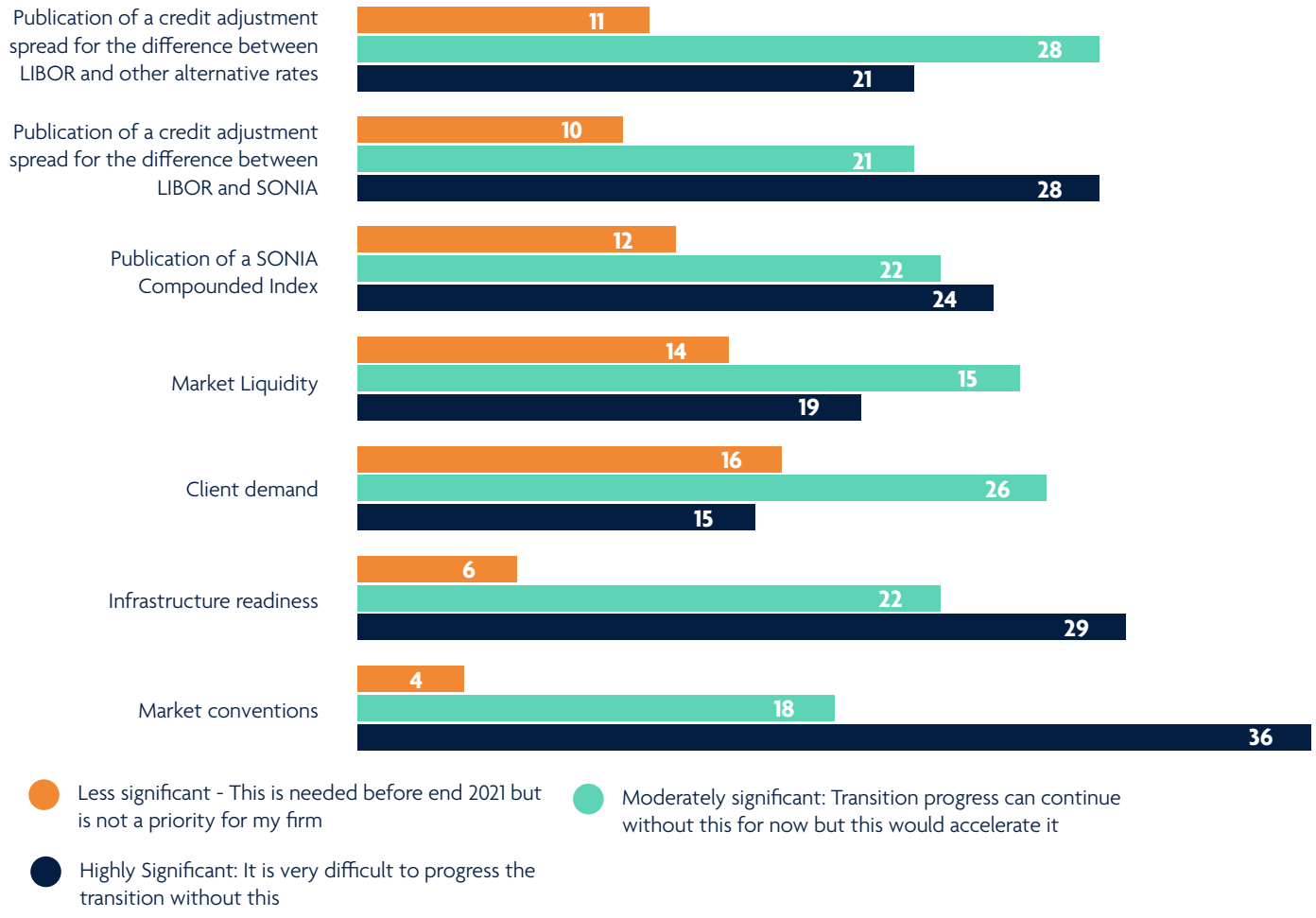


E. Dependencies to accelerate the transition

Many respondents flagged they would rely on tactical solutions this year to offer alternative rates and are waiting for progress on market conventions. As publicly stated, the RFR Working Group supports the use of SONIA compounded in arrears as the primary rate to facilitate the transition. In practice however, there are different conventions to support these calculations. Market conventions can involve referencing SONIA compounded in arrears over an interest period, with a margin added, and a "lag" (also known as a "lookback"), in respect of each interest period. Another involves using a five-day observation period "shift" approach. This is similar to the "lag" approach, but the compounding formula in the "shift" approach weights the SONIA rate to account for calendar days when the SONIA rate is not published according to the observation period, whereas the "lag" approach weights the SONIA rate according to the interest period. To date, there has been no consensus on an approach to favour. The RFR Working Group's Loan Enabler Task Force (LETF) is currently considering the implications of each approach and plans to publish considerations to the wider market as soon as possible.

Many market participants typically rely on internal or external systems to automate the calculation of interest. In the absence of a consensus of market conventions, the development of the required updates to these systems has been slowed. Our survey shows that many respondents have relied on 'tactical' solutions to date to offer new products based on alternative rates. This may involve for example the manual calculation of interests on spreadsheets. While this has allowed for testing of new products, the distribution of new products at scale could not be performed using these solutions. This is why over half of our respondents highlighted the need for consensus on market conventions as a highly significant dependency.

Chart 14. Assess how significantly the following outstanding product development enablers impact your transition plans.



F. Conclusion

While all within the industry will already be aware of the criticality of the coming months for ensuring the industry and its customers are ready for a world without LIBOR beyond the end of 2021, we hope these results demonstrate the steps being taken to translate that into action.

This survey is intended as a snapshot of UK Finance members' views on their readiness and intentions as at June 2020. We intend to run the survey again in Q4 2020, which we expect will demonstrate the scale and pace of transition actions taken which, moving into 2021, will include the significant exercise of transitioning legacy contracts on an active basis where this is possible.

3) PART 2 – BREAKDOWN OF PRODUCT BY PRODUCT SURVEY RESULTS

- Trade and working capital products
- Export finance
- Islamic finance
- Wealth and retail clients
- Loans for small corporates
- Loans for medium and large corporates
- Coronavirus (Large) Business Interruption Loan Scheme(s)
- Commercial Mortgages
- Retail Mortgages
- Buy-to-let mortgages
- Invoice finance and asset-based lending
- Deposit capabilities for corporates

G. Trade and Working capital products

It was noticeable that market participants expected the timeline for transitioning these products would extend into 2021, with the development of a term rate being seen as a more important dependency than almost any other cash product. However, it is also worth noting that many of these products are short term in nature or if rolling may include an annual renewal providing for the opportunity to transition to new rates in advance of end-2021.

This was not necessarily surprising given that the Use Cases paper[10] noted the RFR Working Group view that "Trade and working capital products such as supply chain finance and receivable facilities require a term rate or equivalent to calculate forward discounted cash flows to price the value of assets into the future ... The product requires a rate that is transparent and observable to all parties. Clients typically do not have access to live market curves, which may be available in a dealing room".

Larger lenders tended to be closest to the findings of the Use Cases report, with some large banks making clear Term SONIA Rate use was intended for only a limited part of the product suite that required a discounting rate. Several respondents referenced that it was likely across these products that new development would span all three options in Chart 18, depending on the product.

A smaller number of firms cited the role of their own bank reference rate in these products.

As across the survey a number of firms, particularly large international banks, emphasised the need for customer choice to drive adoption away from LIBOR.

Chart 15. When do you plan to start development of non-LIBOR alternatives?

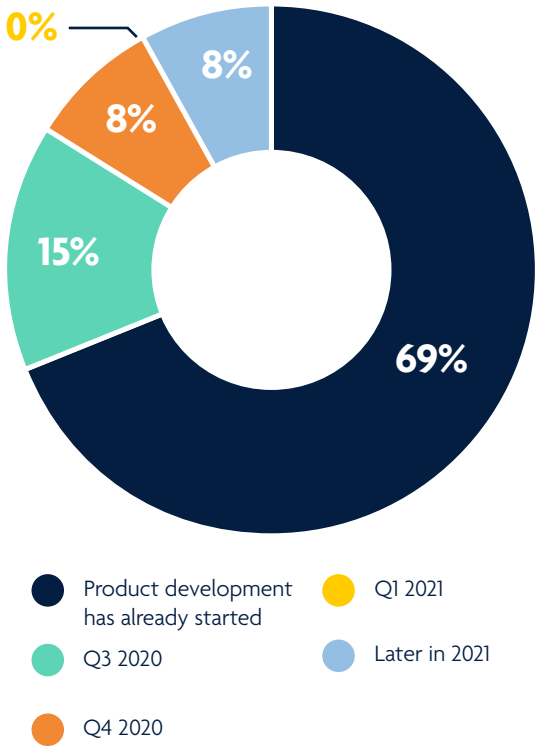
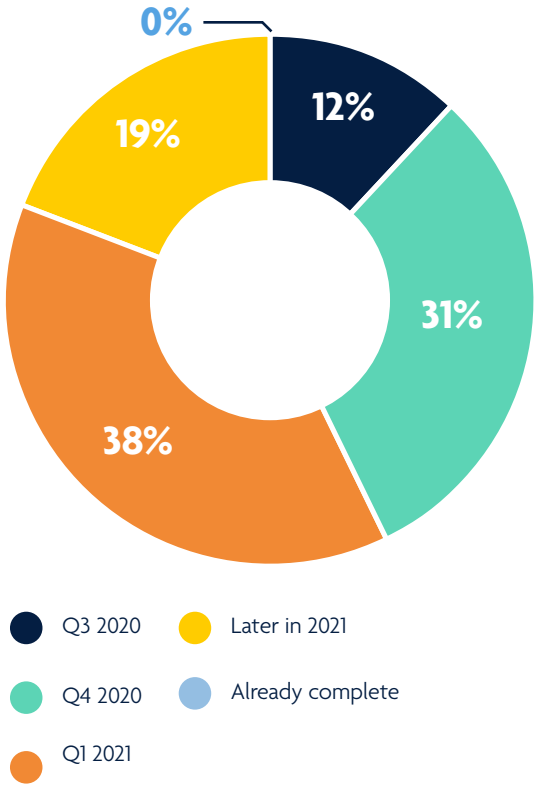


Chart 16. When do you expect development of non-LIBOR alternatives to be largely complete?



10. https://www.bankofengland.co.uk/-/media/boe/files/markets/benchmarks/rfr/use-cases-of-benchmark-rates-compounded-in-arrears-term-rate-and-further-alternatives.pdf

Chart 18. Intended rate selection

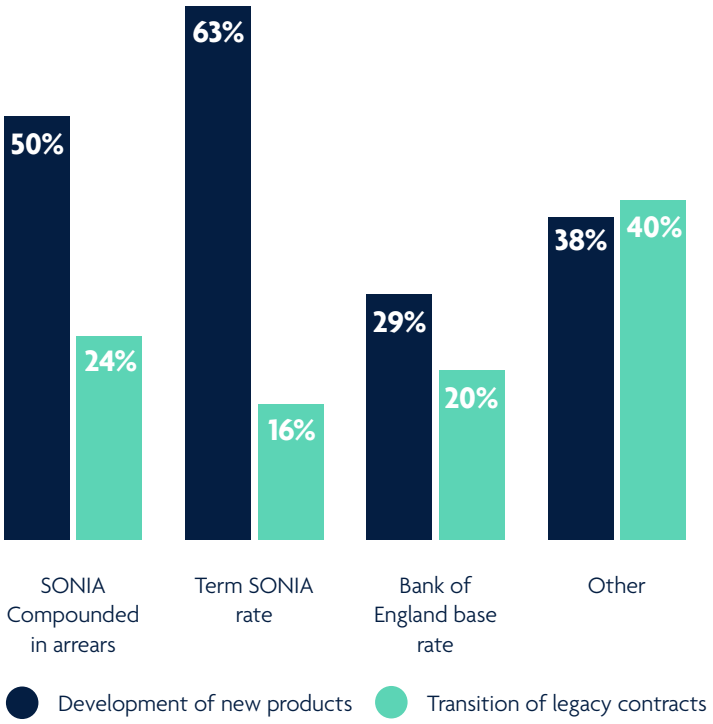
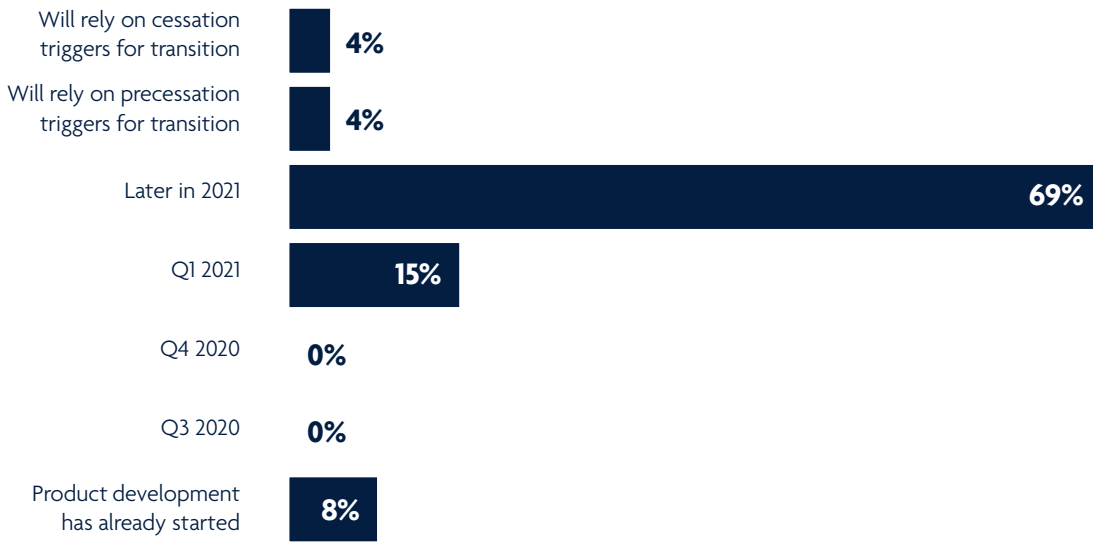


Chart 17. Expected timeline for transitioning legacy contracts to an alternative rate:



H. Export finance

Only around a fifth of respondents reported export finance being part of their LIBOR transition plans. Responses were similar in nature to trade and working capital with some evidence this would transition as one of the later products as planned. Legacy contracts will be transitioned to alternative rates later than Q1 2021 for 86 per cent of respondents to this question.

The intended use of SONIA compounded in arrears, Term SONIA Rate and BoE Base Rate was evenly spread between participants.

Outside of the survey a number were keen to ensure that conversations with UK Export Finance, which provides a variety of guarantees products in the export finance market, were linked into and were clear on the implications of LIBOR transition for those facilities.

Chart 19. When do you plan to start development of non-LIBOR alternatives?

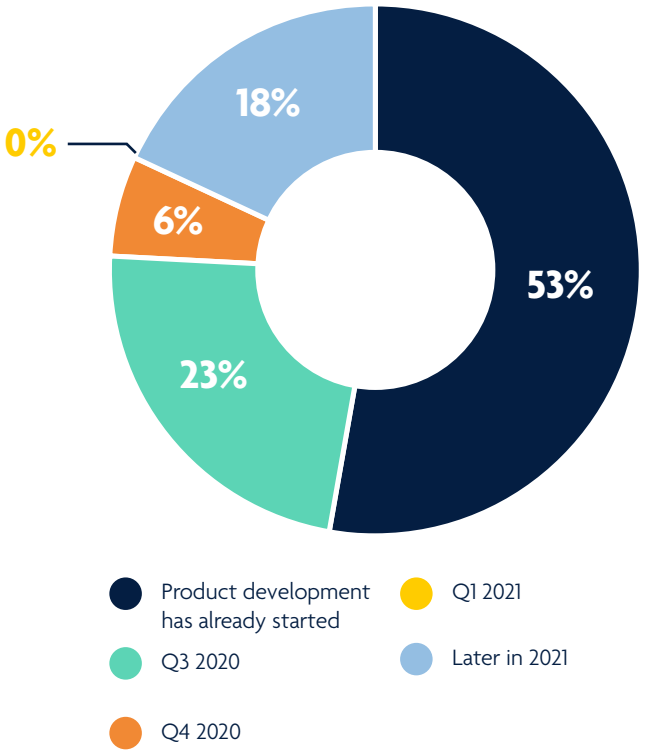


Chart 20. When do you expect development of non-LIBOR alternatives to be largely complete?

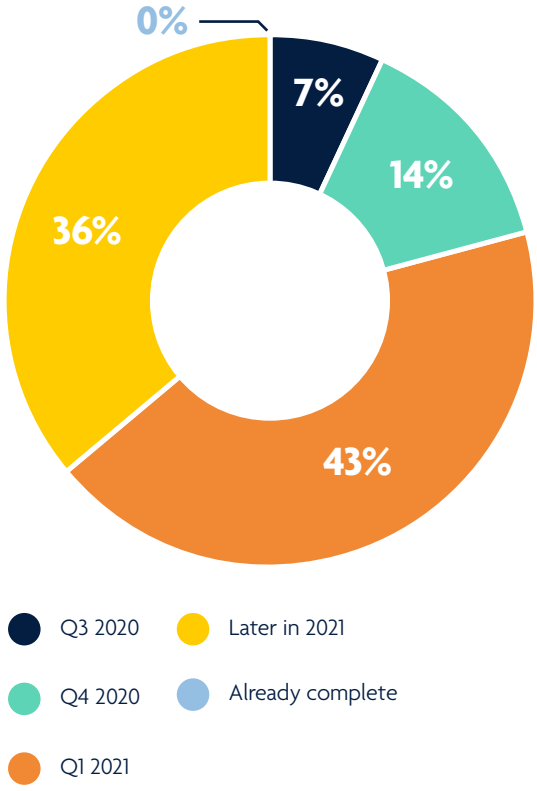


Chart 22. Intended rate selection

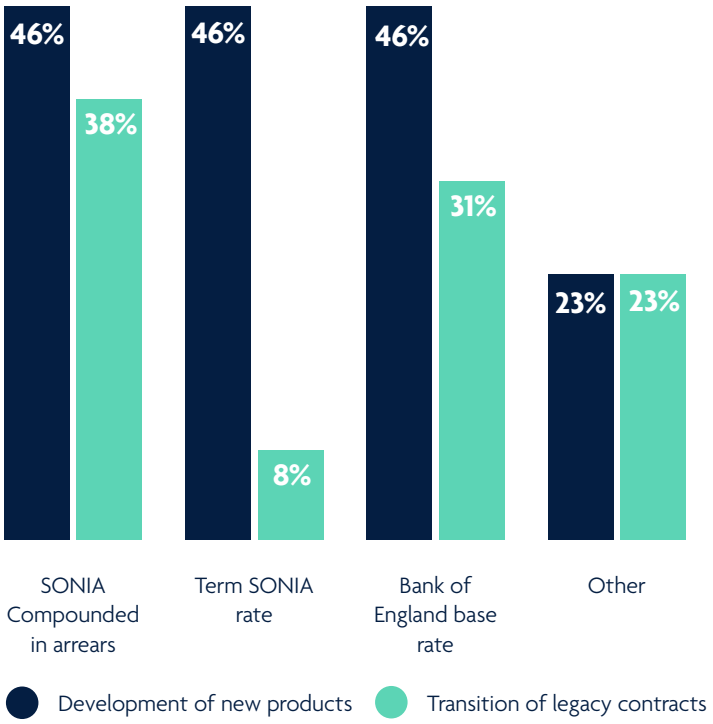
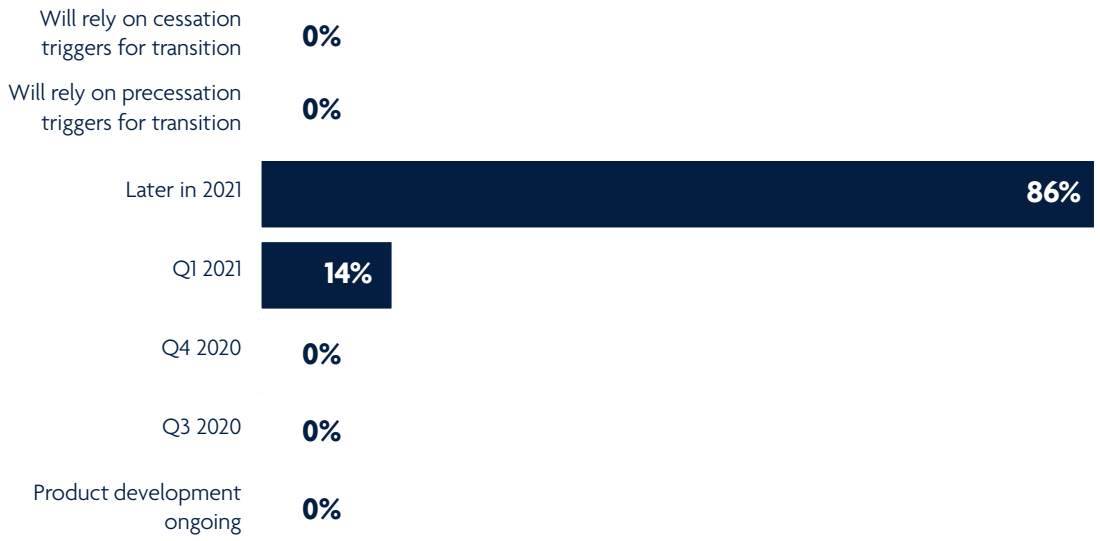


Chart 21. Expected timeline for transitioning legacy contracts to an alternative rate:



I. Islamic Finance

Islamic finance is a relatively niche product area. Only a small number of firms referenced this as part of their transition. However, the importance of this product for certain lenders and communities was acknowledged in the Use Cases paper[11] from the RFR Working Group which noted that it was unlikely to be compatible with SONIA compounded in arrears as "Islamic facilities can pay variable rates of return, so long as the variable element is pre-determined". One firm however did note the potential use of SONIA compounded in arrears.

Where firms had selected 'other' when considering their intended rate selection it was because they were currently undecided.

One firm noted that this product was, for various reasons, likely to be within their stock of tough legacy contracts.

Chart 23. When do you plan to start development of non-LIBOR alternatives?

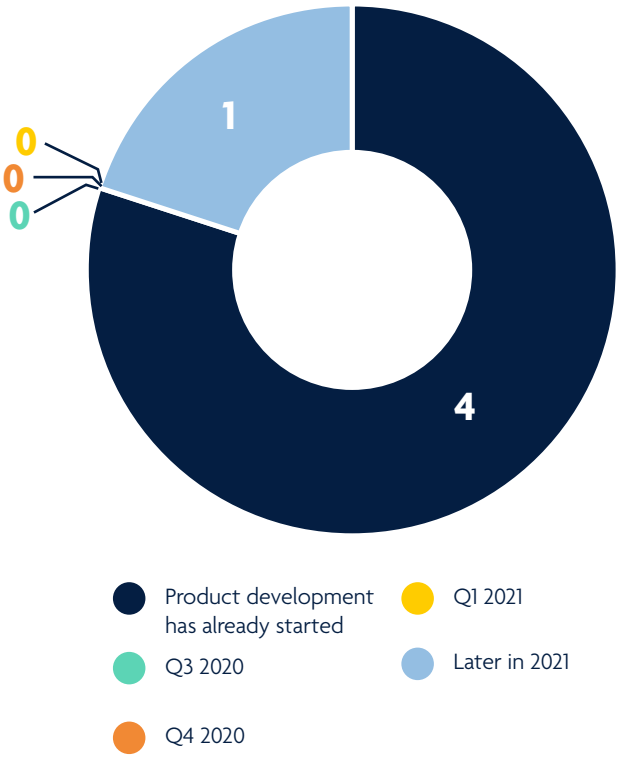
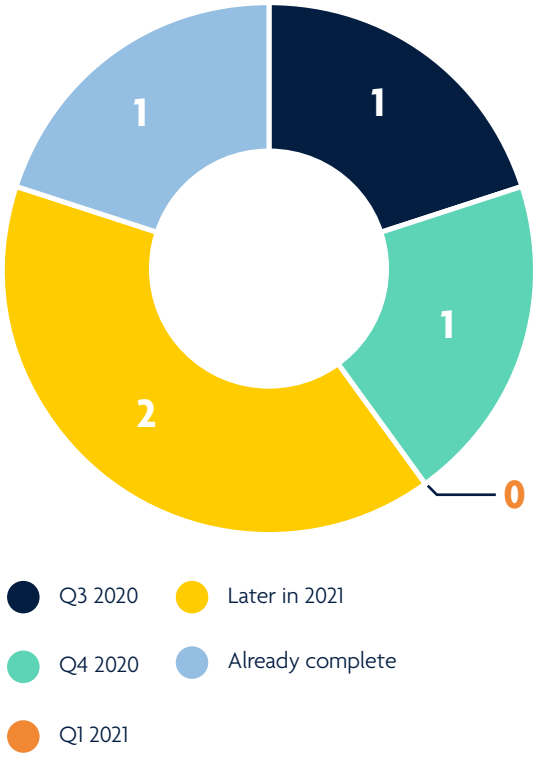


Chart 24. When do you expect development of non-LIBOR alternatives to be largely complete?



11. https://www.bankofengland.co.uk/-/media/boe/files/markets/benchmarks/rfr/use-cases-of-benchmark-rates-compounded-in-arrears-term-rate-and-further-alternatives.pdf

Chart 26. Intended rate selection

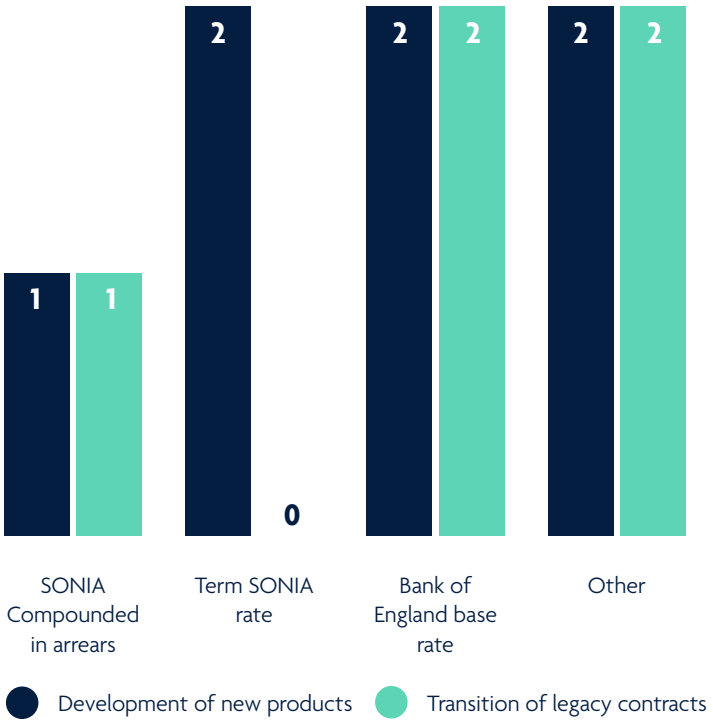
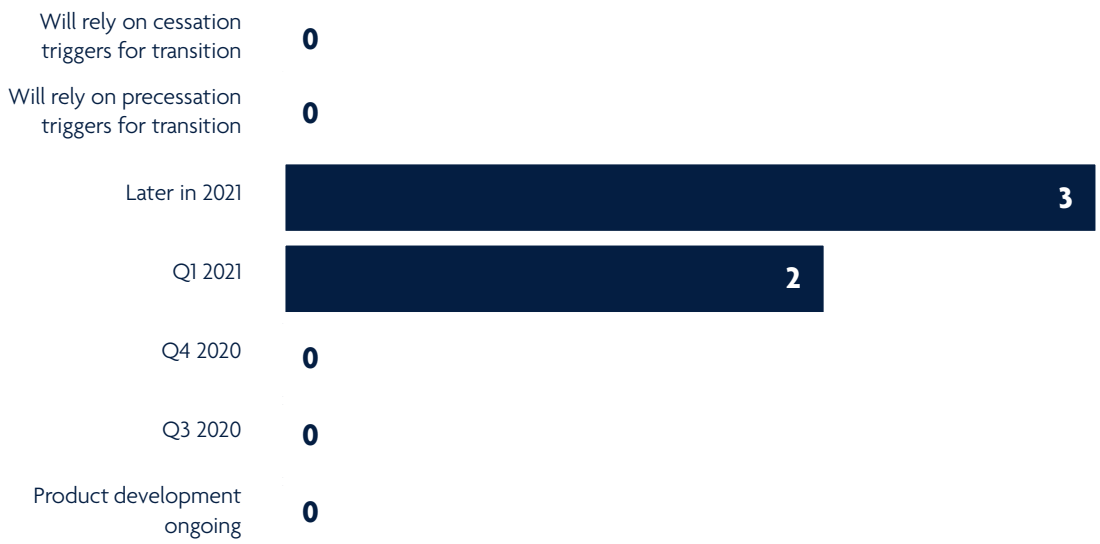


Chart 25. Expected timeline for transitioning legacy contracts to an alternative rate:



J. Wealth and retail clients

A number of firms noted that rate selection may depend on the client, with smaller clients being offered perceived simpler rates such as BoE Base rate, with larger clients being offered SONIA compounded in arrears.

One firm noted that lack of current Term SONIA Rate optionality meant that while they would prefer to have the option going forward between this and BoE Base Rate, BoE Base Rate had become the default available today. Others talked about the role of SONIA term rate for 'selective use' where appropriate which again demonstrated good awareness of the Use Cases paper and the RFR Working Group's view that SONIA compounded in arrears is likely to be the default option where possible.

There was no consistent expected timeline across the market for the development of non-LIBOR alternative products to be largely complete, possibly reflecting the diversity of lender segments in responding on this product which was broad.

Chart 27. When do you plan to start development of non-LIBOR alternatives?

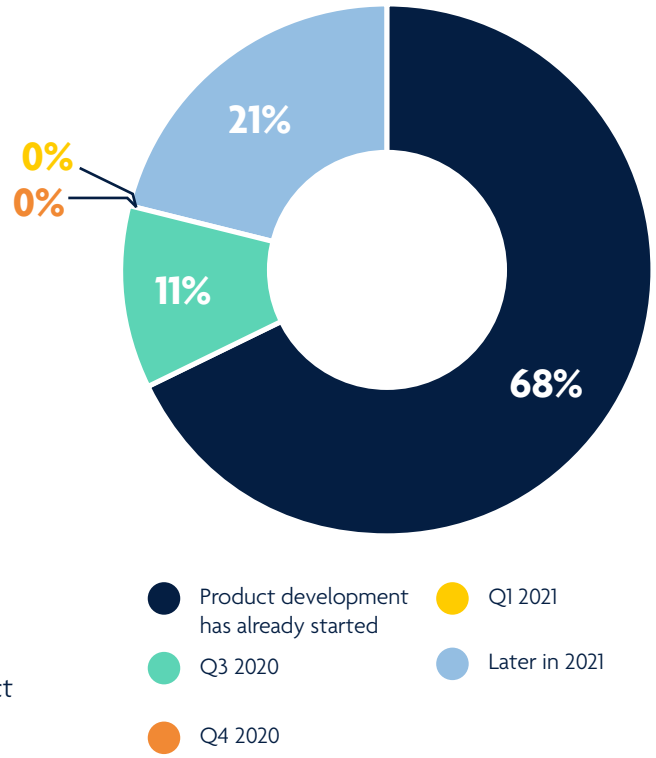


Chart 28. When do you expect development of non-LIBOR alternatives to be largely complete?

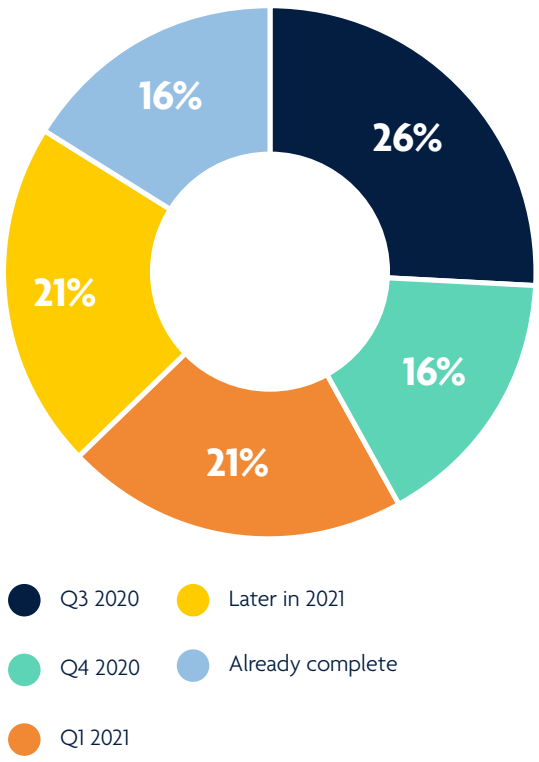


Chart 30. Intended rate selection

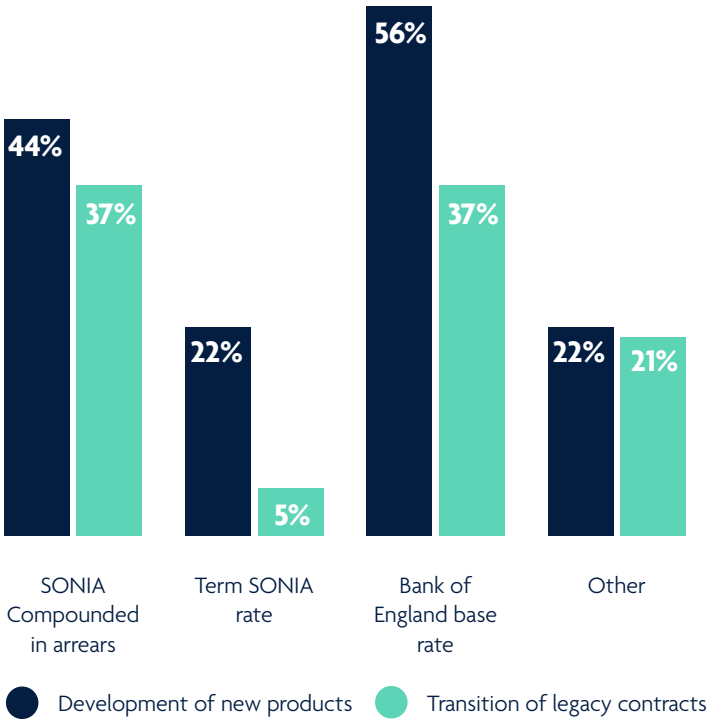
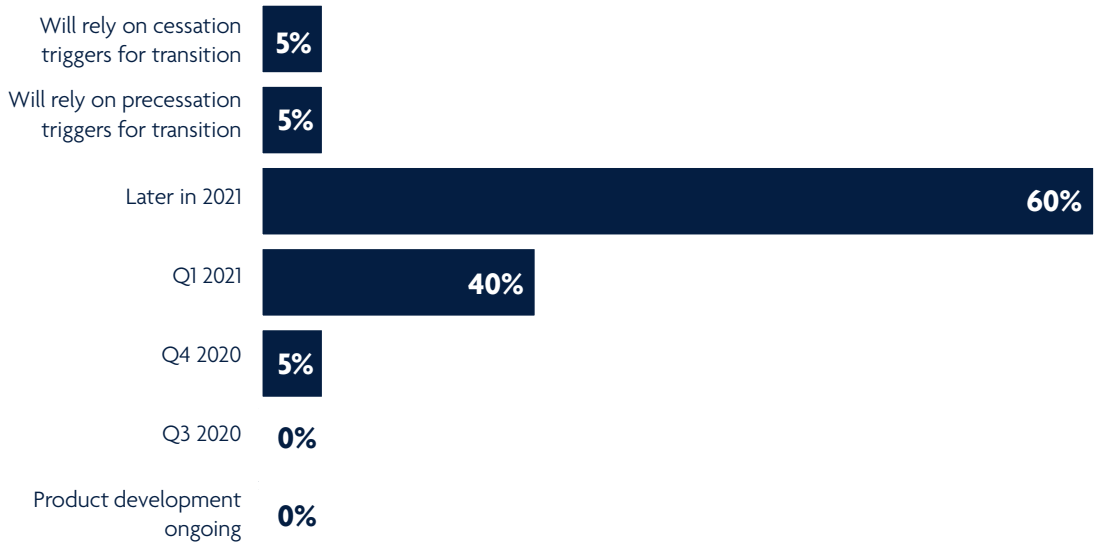


Chart 29. Expected timeline for transitioning legacy contracts to an alternative rate:



K. Loans for small corporates

This segment is a critical priority in the broader LIBOR transition and it was therefore reassuring that evidence of product development underway was high for this category. 97 per cent expect to have begun alternative rate product development before end 2020, with 87 per cent of respondents having already done so. 43 per cent expected their development of non-LIBOR alternatives to be largely complete when they reach the end of Q3 2020.

Where firms were still yet to make decisions and progress this, established market conventions were cited most commonly, perhaps unsurprisingly, and therefore the expected output from the RFR Working Group on this is likely to allow for significant increases in the pace of transition in this segment. Others cited, particularly where referencing the potential role of a Term SONIA Rate, own bank base rate and BoE Base Rate.

Ensuring good customer outcomes at the smaller end of the business lending spectrum was clearly on the minds of most, with the role of the Lending Standards Board for instance cited and the importance of guidance and supporting working papers from the UK authorities and the RFR Working Group. This segment of the borrowing community was also felt to need the clearest outreach and education approach.

We expect the remainder of the year to be a critical one for the transitioning of this cohort of customers in new lending and familiarising with new rates and the progress would be significant in line with RFR Working Group's view.

Chart 31. When do you plan to start development of non-LIBOR alternatives?

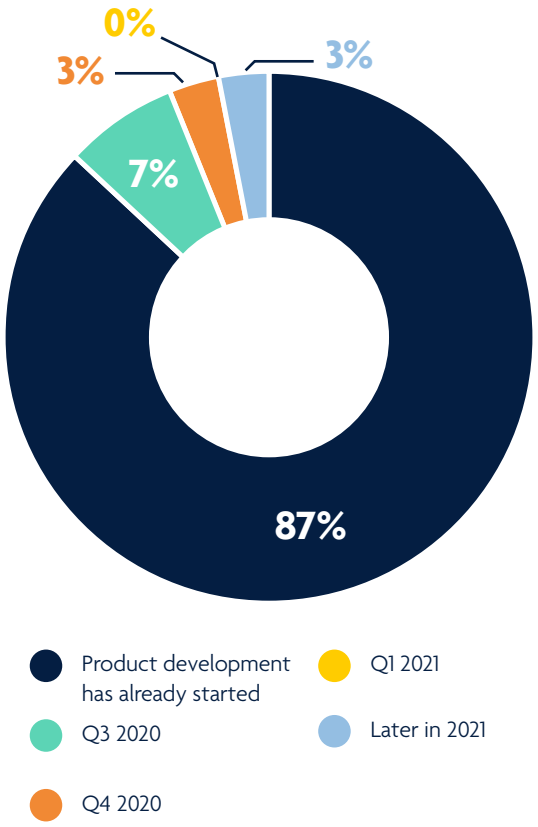


Chart 32. When do you expect development of non-LIBOR alternatives to be largely complete?

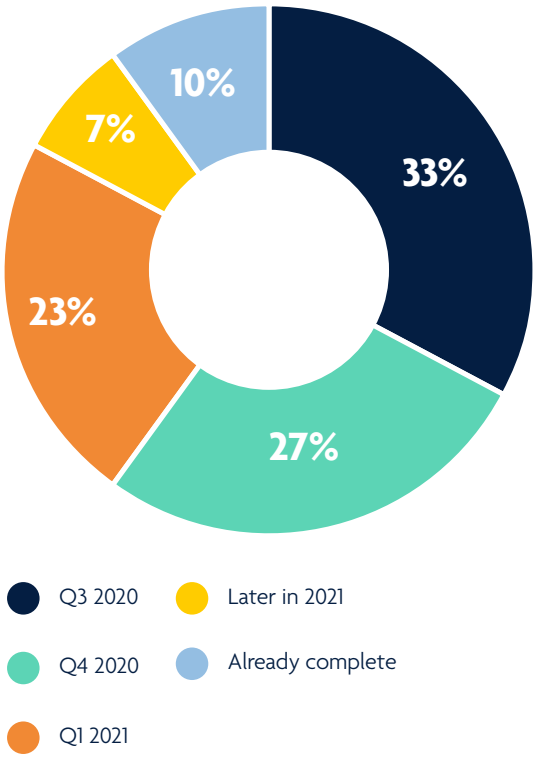


Chart 34. Intended rate selection

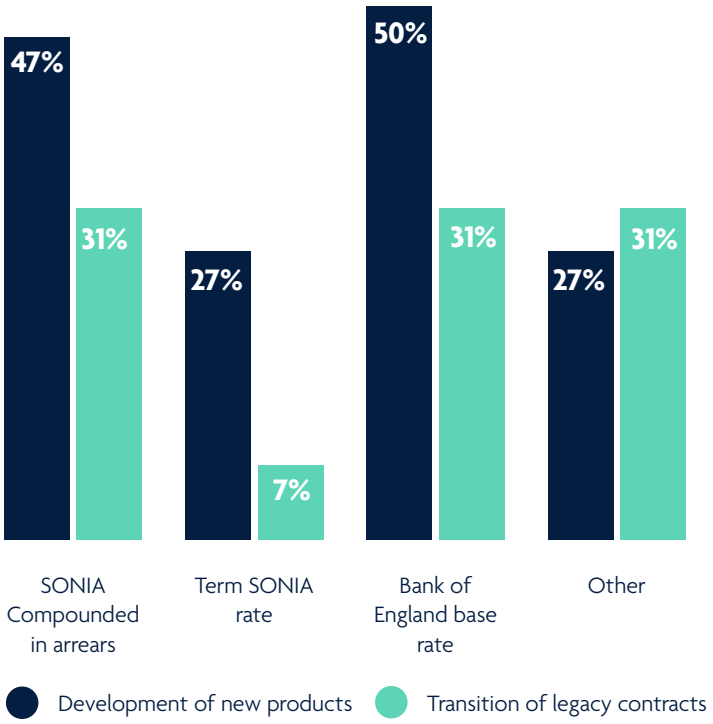
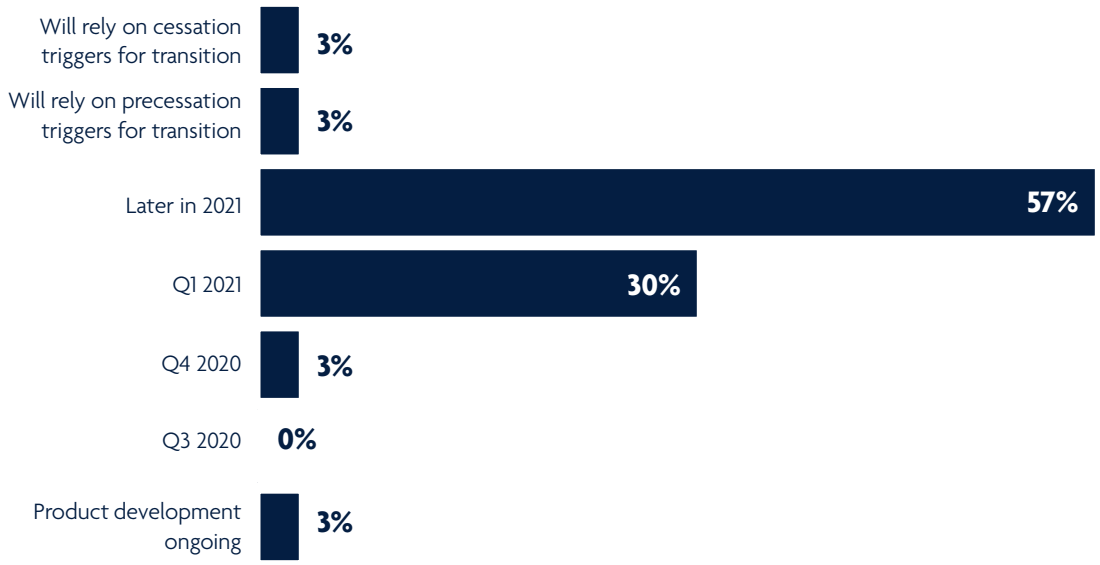


Chart 33. Expected timeline for transitioning legacy contracts to an alternative rate:



L. Loans for medium and large corporates

The survey revealed a good deal of recognition of the RFR Working Group's view that SONIA compounded in arrears is the clear preference for replacement to sterling LIBOR for larger businesses. SONIA compounded in arrears was referenced by 81 per cent of respondents for the development of new products. A small proportion (26 per cent) referenced Term SONIA Rate and BoE Base Rate as well – though comments noted that rate selection may depend on the value of the loan. This is in line with the work of the use case taskforce which noted that 'mid corp' was a possible use case which may not be well suited for SONIA compounded in arrears in the same way larger corporates would be.

Overwhelmingly lenders noted the dependency on guidance on loan conventions in the sterling market which as of June 2020 was anticipated shortly from the RFR Working Group.

The timeline for development of new products is expected to be largely similar to that of loans for small corporates, with 97 per cent of respondents expecting to have begun product development by end 2020, and 81 per cent having already started.

Few firms expect to need to rely on cessation or pre-cessation triggers for the transition of legacy contracts, but the bulk of this migration will happen after Q1 2021.

Chart 36. When do you expect development of non-LIBOR alternatives to be largely complete?

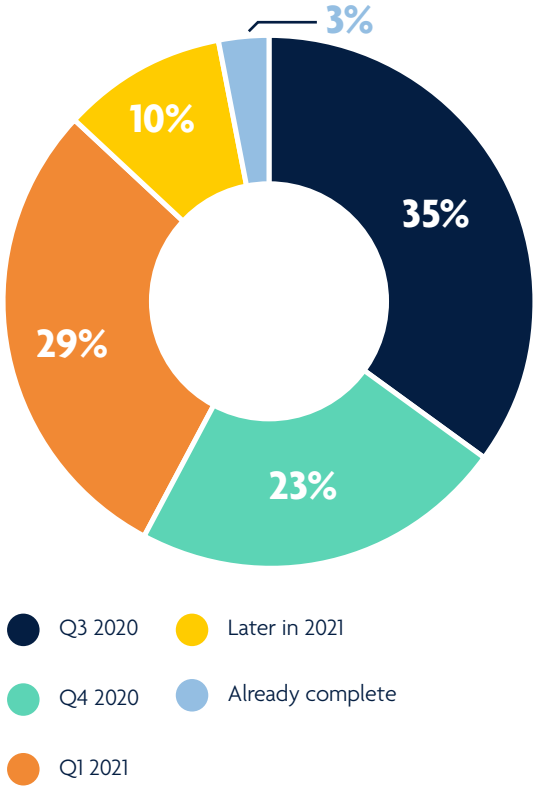


Chart 35. When do you plan to start development of non-LIBOR alternatives?

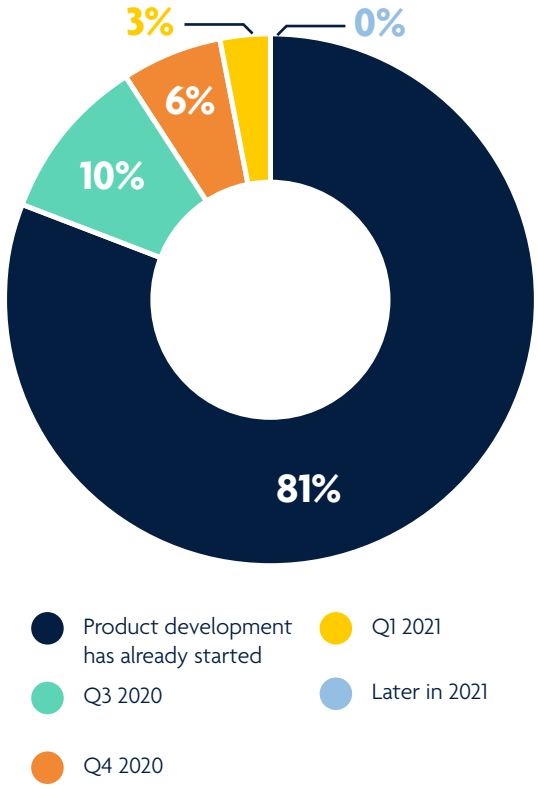


Chart 38. Intended rate selection

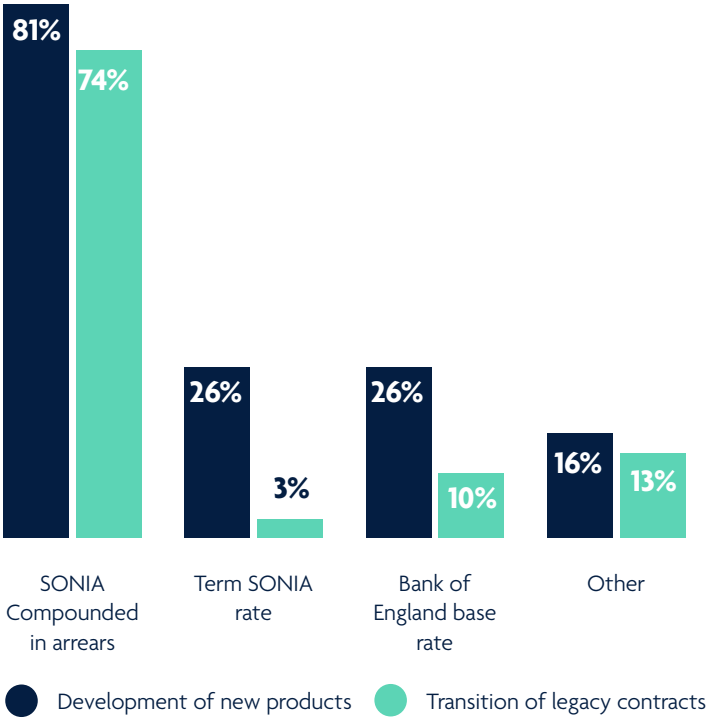
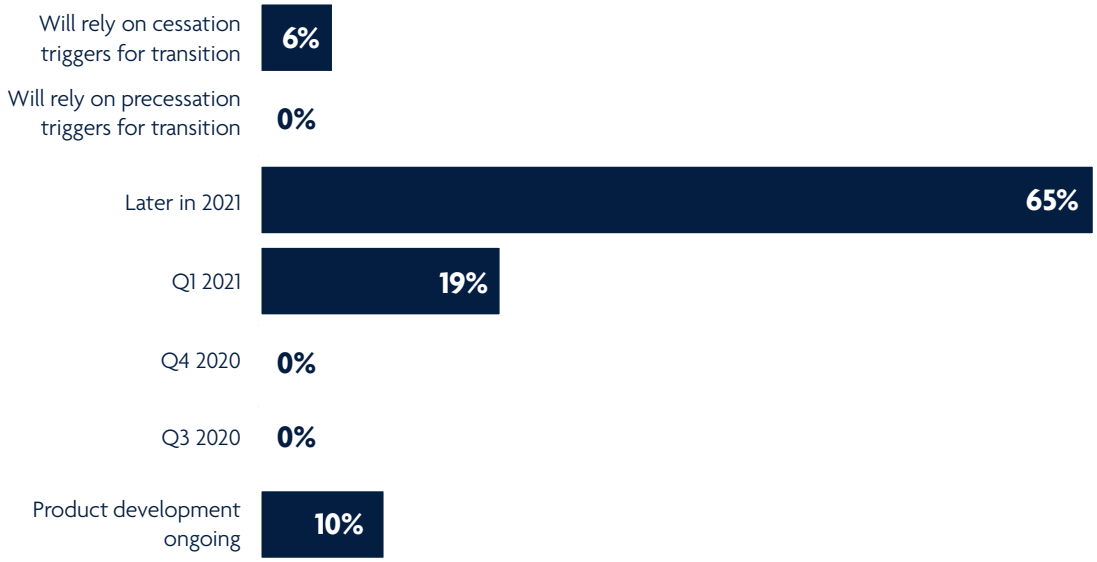


Chart 37. Expected timeline for transitioning legacy contracts to an alternative rate:



M. Coronavirus (Large) Business Interruption Loan Scheme(s)

Since the start of the Covid-19 crisis, the banking and finance industry has provided an unparalleled package of support to businesses of all sizes impacted by the pandemic. These include commercial lending, capital repayment holidays, extended overdrafts, asset finance and invoice finance and asset-based lending. One of the most important areas of support has been through the various government lending schemes, which include the Bounce Bank Loans Scheme (BBLS), the Coronavirus Business Interruption Loan Scheme (CBILS), the Coronavirus Larger Business Interruption Loan Scheme (CLIBILS) and the Covid Corporate Financing Facility (CCFF).

As of 2 August 2020, the banking and finance industry has provided approximately £50.7 billion to nearly 1.2 million businesses through Covid-19 business finance schemes.[12] The government-backed BBLS has helped over 1.1 million businesses to access £34.3 billion worth of loans to help small and micro businesses absorb the Covid-19 financial shock. For the country's small and medium sized businesses, the industry has provided £13.08 billion worth of facilities through the CBIL scheme to 58,595 companies. CBILS supports a range of types of finance facility, including term loans, revolving credit (overdrafts), invoice finance and asset finance. The CLBILS introduced in April to help larger UK enterprises has provided £3.27 billion in loans.

There were some knock-on implications of this for LIBOR transition. While the overwhelming majority of the value of lending was provided through the Bounce Bank Loans Scheme which has a fixed interest rate set by government, in order to enable rapid deployment of the government lending schemes to meet the cashflow needs of businesses, some banks and lenders provided this referencing LIBOR, which it was noted at the time may lead to increases in LIBOR exposures. Around 17% of firms surveyed have LIBOR exposures linked under the government-backed lending schemes with a total of at least £1 billion referencing LIBOR.

Chart 39. When do you plan to start development of non-LIBOR alternatives?

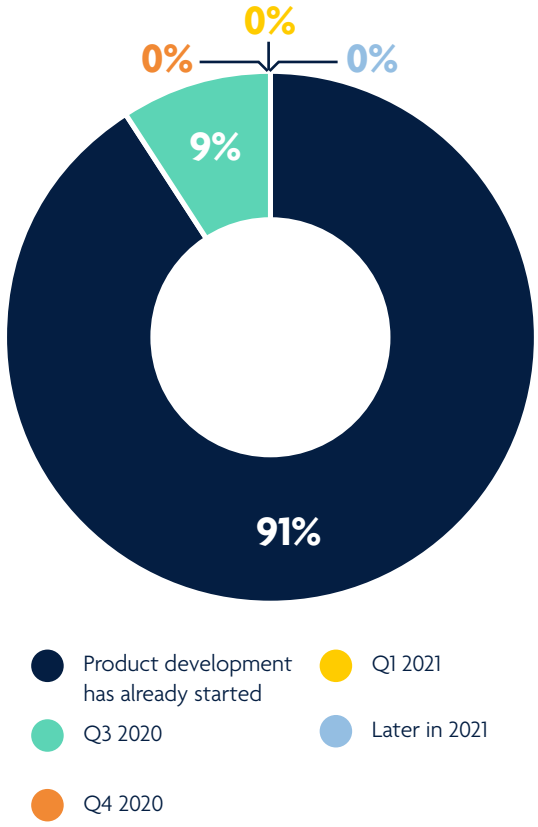
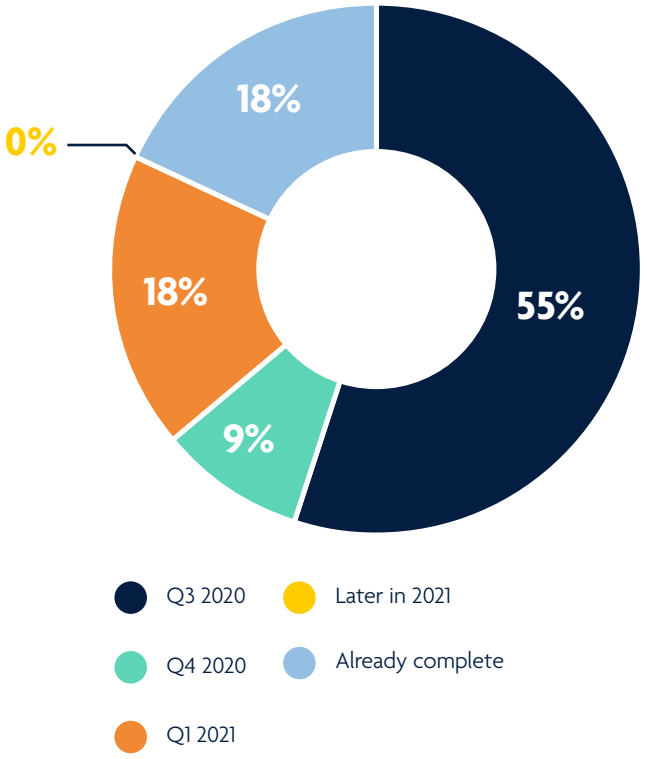
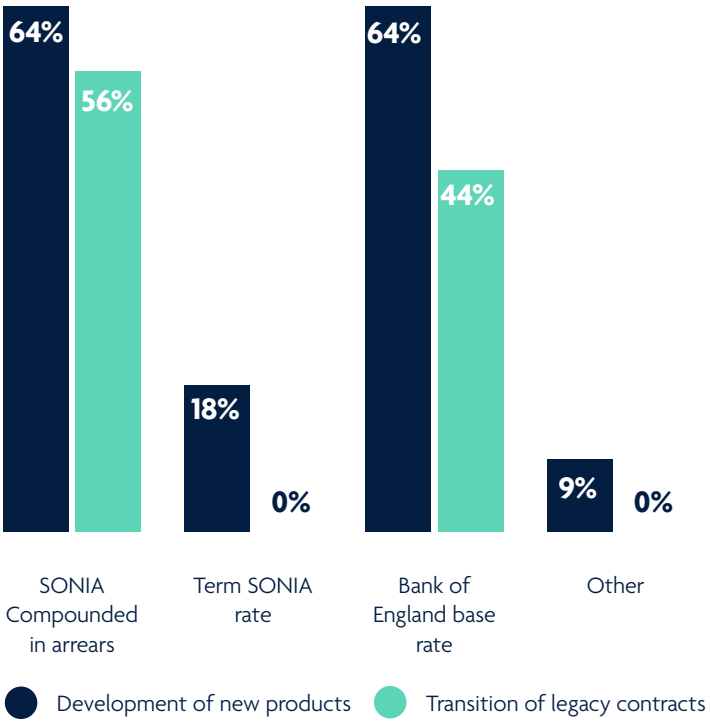


Chart 40. When do you expect development of non-LIBOR alternatives to be largely complete?



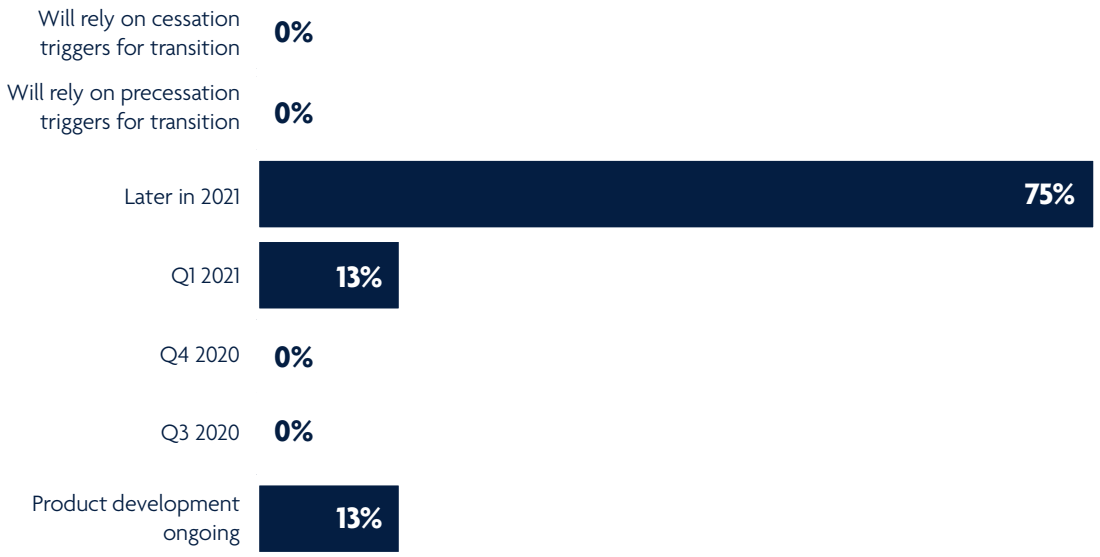
12. https://www.gov.uk/government/collections/hm-treasury-coronavirus-covid-19-business-loan-scheme-statistics

Chart 42. Intended rate selection



However, there is good evidence that firms have clear transition plans in place to ensure that the support provided under these schemes will be compatible with achieving the RFR Working Group's roadmap. One firm noted that their new CLBILS lending was already being offered on a SONIA compounded in arrears basis, while others noted that this was a very small part of their book relatively and would transition in line with other corporate lending. Firms noted recognition of the RFR Working Group's view that mandatory transition language would be included as standard after Q3 2020. This question blended both CBILs and CLBILS and it is likely that those cited on BoE Base Rate correlate with the smaller facilities provided under CBILS, with SONIA compounded in arrears at the higher end and into CLBILS.

Chart 41. Expected timeline for transitioning legacy contracts to an alternative rate:



N. Commercial Mortgages

The mortgage market, including commercial mortgages, is well advanced, particularly for new lending. An extremely low number of firms are not expecting product development to have begun by the end of 2020.

Transition of legacy contracts is likely to occur later in 2021 with some (although a definite minority) expecting they will have to rely on cessation or pre-cessation triggers which has been identified as less desirable than active transition.

Within this product, it was largely BoE Base Rate or internal rates to be used, but a few are waiting to see if Term SONIA Rate would be appropriate before transitioning.

The RFR Working Group's report on tough legacy issues and subsequent announcement from HMT on legislation are likely to be particularly important for this cohort based on responses.

Chart 43. When do you plan to start development of non-LIBOR alternatives?

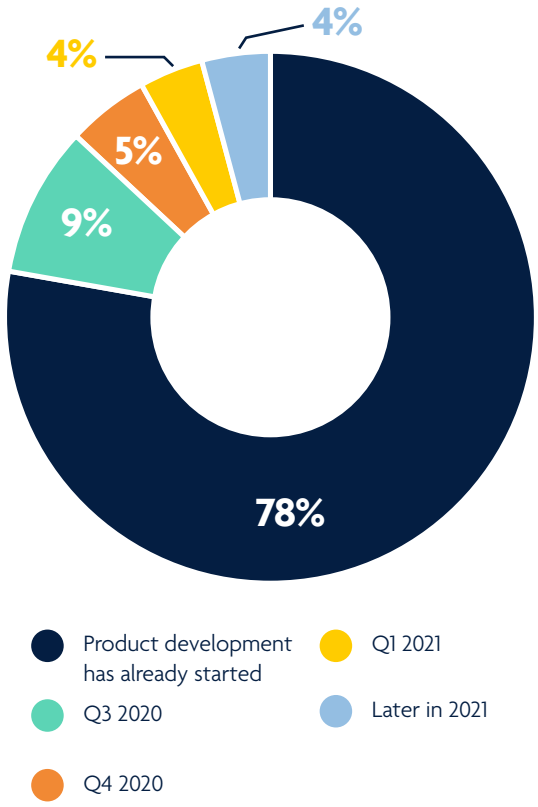


Chart 44. When do you expect development of non-LIBOR alternatives to be largely complete?

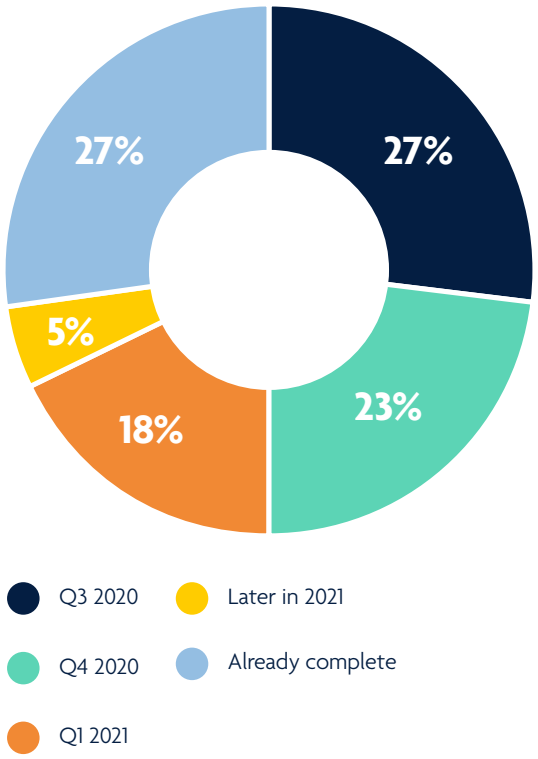


Chart 46. Intended rate selection

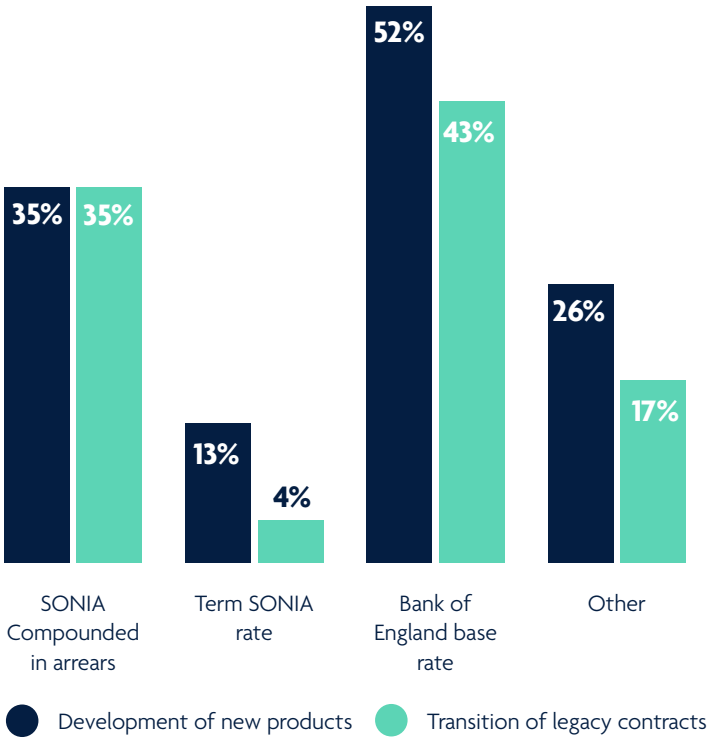
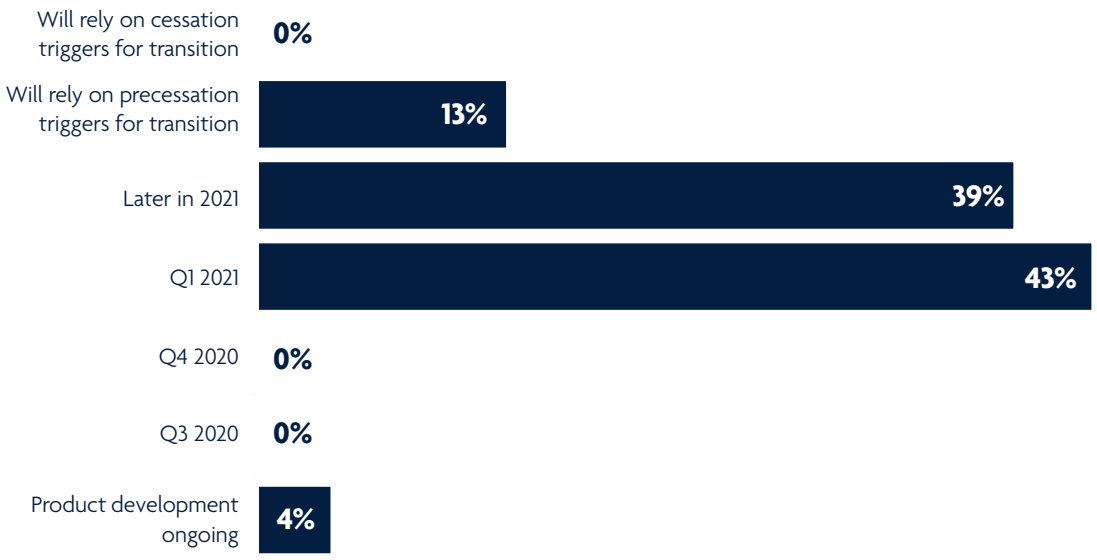


Chart 45. Expected timeline for transitioning legacy contracts to an alternative rate:



O. Retail Mortgages

Just under half the firms recorded retail mortgage products within their LIBOR transition plans. Reflecting the diversity of the UK Finance mortgage membership, of those with mortgage exposures, the scale of these was one of the widest ranging. While for around 40 per cent of firms affected this exposure was over £500 million, for around 25 per cent it was less than £10 million.

In alignment with the rest of the mortgage market, the development of alternative rate retail products has seen good progress, with only four per cent of firms not expecting to start their product development until 2021 and 91 per cent expected to have completed their product development of alternative rate products by the Q1 2021 milestone for the cessation of all LIBOR linked lending. BoE Base Rate is currently viewed as the preferred rate for both the development on new products and the transition of legacy contracts, although internal rates were also seen as a favourable option. It was noted that firms considered it difficult to assess whether a Term SONIA Rate would be a suitable alternative at this stage given the delay in its development.

Only 18 per cent of firms expect to begin their transition of legacy LIBOR contracts ahead of 2021, with 68 per cent not expecting to start until beyond Q1 next year. A key issue for the transition of legacy products was identified for those firms whose own back books cannot be amended until LIBOR cessation or who administer closed mortgage books for third parties which predate considerations of LIBOR cessation and therefore do not include any fall back provisions. To date LIBOR exposure in these particular books have largely only reduced as mortgages were redeemed. Subsequently, with this having impacted lenders' ability to reduce their LIBOR exposure it has meant the recent announcement from HM Treasury on legislation has been a very welcome development for this cohort.

Chart 47. When do you plan to start development of non-LIBOR alternatives?

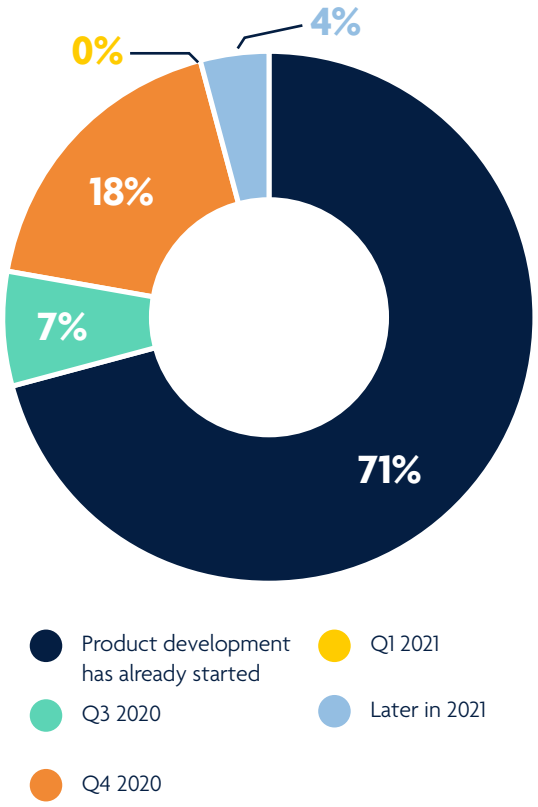


Chart 48. When do you expect development of non-LIBOR alternatives to be largely complete?

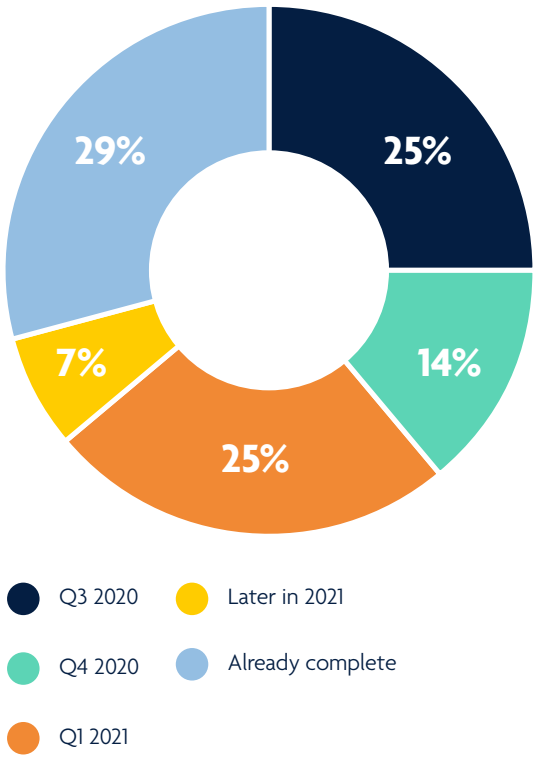
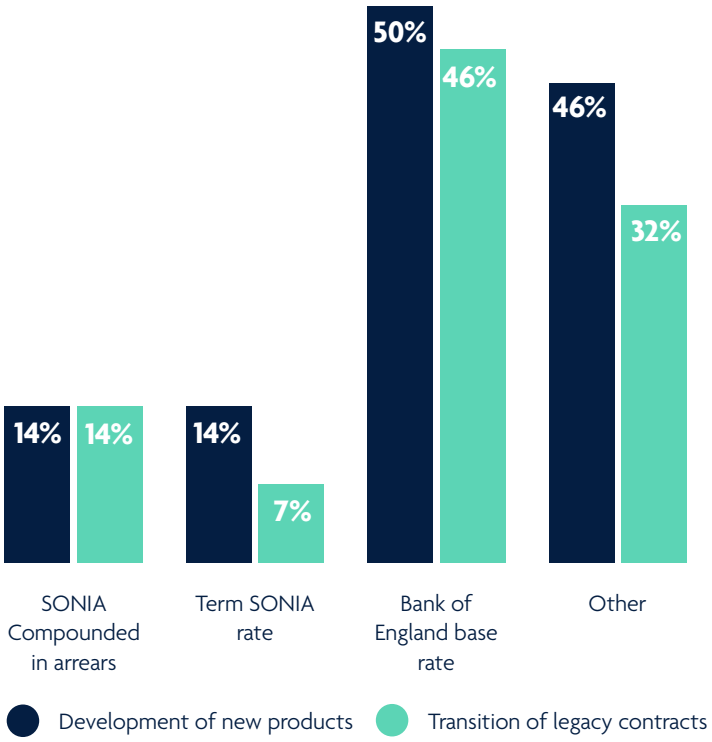
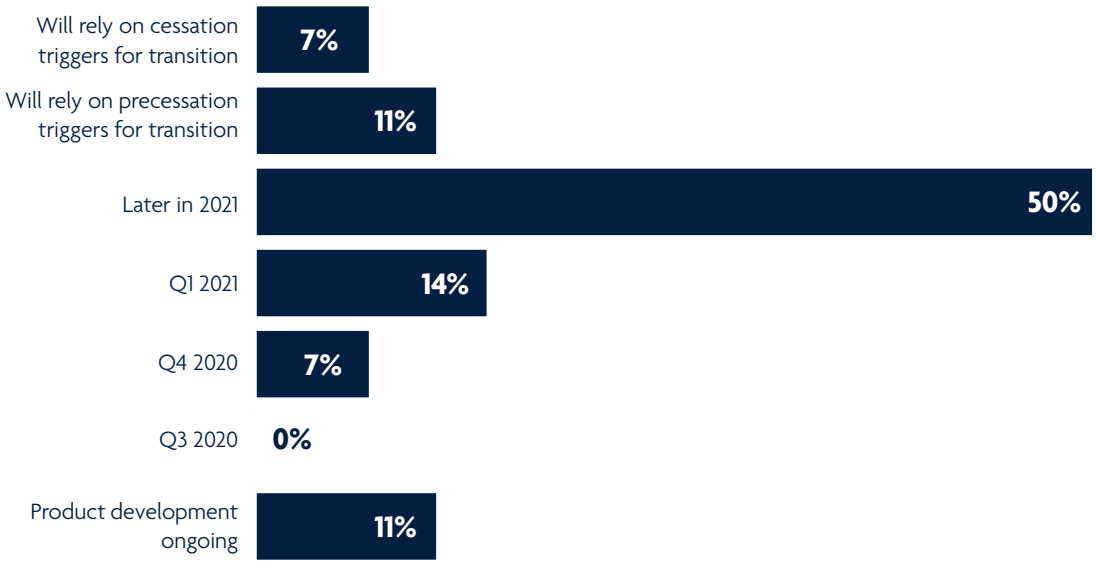


Chart 50. Intended rate selection



However, as a regulated, retail product, it was noted that minimising conduct risk where customers with legacy LIBOR contracts are able to be migrated to an alternative reference rate was still a key concern for some mortgage providers. When considering additional initiatives that could be taken to facilitate engagement with clients, a mortgage provider highlighted greater guidance on fair credit adjustment rates for alternatives beyond SONIA compounded in arrears would help ensure a smoother transition for both lender and customer.

Chart 49. Expected timeline for transitioning legacy contracts to an alternative rate:



P. Buy-to-let mortgages

Just over 40% of the respondents recorded buy-to-let mortgage products within their LIBOR transition plans. For the majority, these exposures were above £500 million. Total exposure estimated is at over £7.2 billion.

The vast majority of firms have already begun their development of alternative rate products, with only 15 per cent of respondents seeing this as something that will begin post-Q3 2020. A significant 41 per cent have already completed this product development, contributing towards the large majority (81 per cent) of firms expecting to have largely completed product development by end of 2020. When asked the expected interest rate that will be selected for this there is a clear preference for BoE Base Rate, though others were cited.

For transitioning legacy contracts, over 50 per cent of firms expect the transition of legacy products to take place after Q1 2020, with just over ten per cent relying on pre-cessation triggers. No firms currently are planning to rely on cessation triggers for this transition or indeed expect this will be necessary.

Some cited concerns on rate selection, based on the timing and lack of understanding on a Term SONIA Rate making it difficult to consider all options.

Chart 52. When do you expect development of non-LIBOR alternatives to be largely complete?

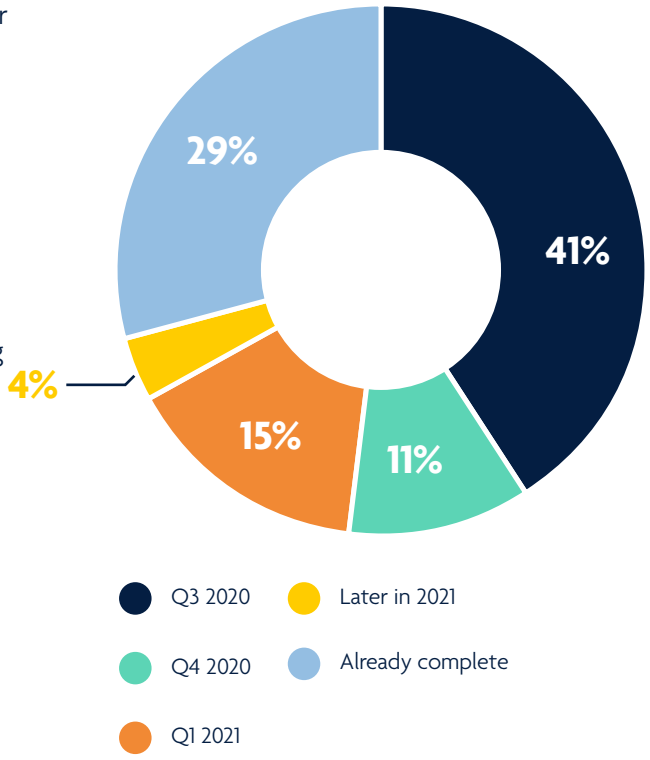


Chart 51. When do you plan to start development of non-LIBOR alternatives?

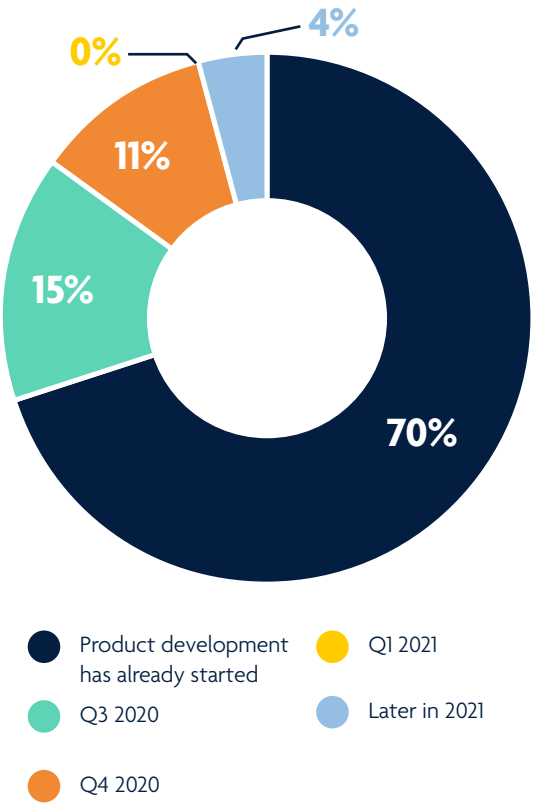


Chart 54. Intended rate selection

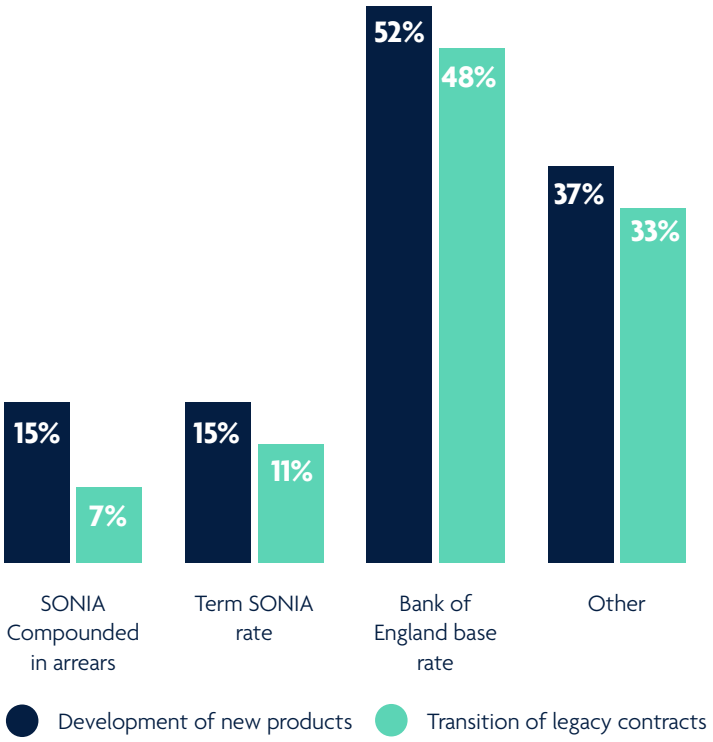
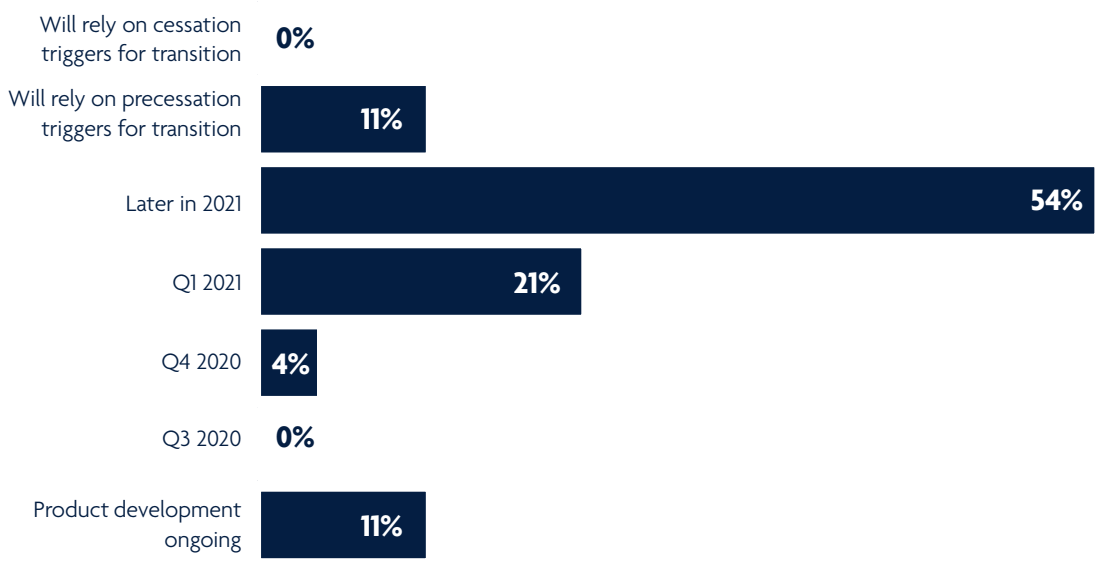


Chart 53. Expected timeline for transitioning legacy contracts to an alternative rate:



Q. Invoice finance and asset-based lending

Around a third of firms noted invoice finance and asset based lending featuring as part of their transition plans, with a high level of product development already underway. Within invoice finance and asset based lending, firms commented that often their books were short-term and therefore simply ceasing transacting in GBP LIBOR would remove the need to consider the transition of legacy stock. For others this was a very small part of their overall transition plan or they already largely referenced alternative rates such as BoE Base Rate.

Client appetite was noted as a key dependency in the transitioning of existing contracts alongside "the pace of negotiations and market developments". Term SONIA Rate is likely to play a role as the Use Cases paper from the RFR Working Group concluded. As with other trade and working capital products, firms referenced its likely use in a "small number of products requiring cash flow discounting upfront".

Chart 55. When do you plan to start development of non-LIBOR alternatives?

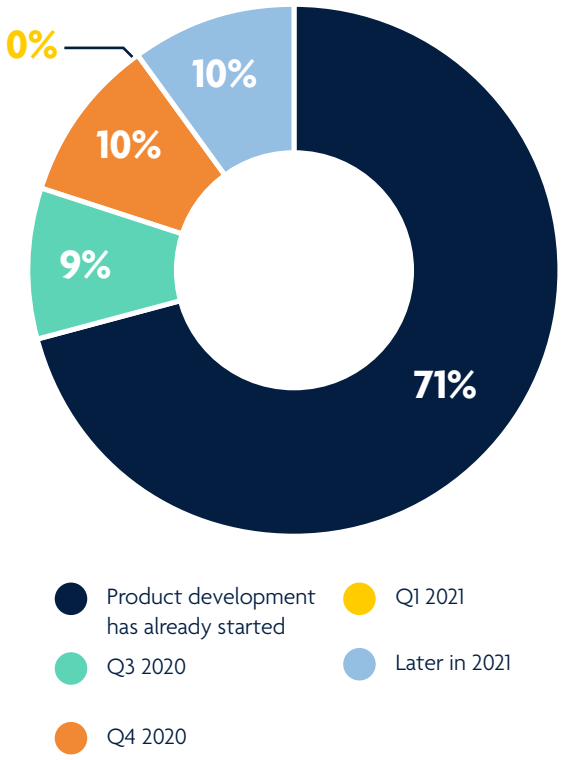


Chart 52. When do you expect development of non-LIBOR alternatives to be largely complete?

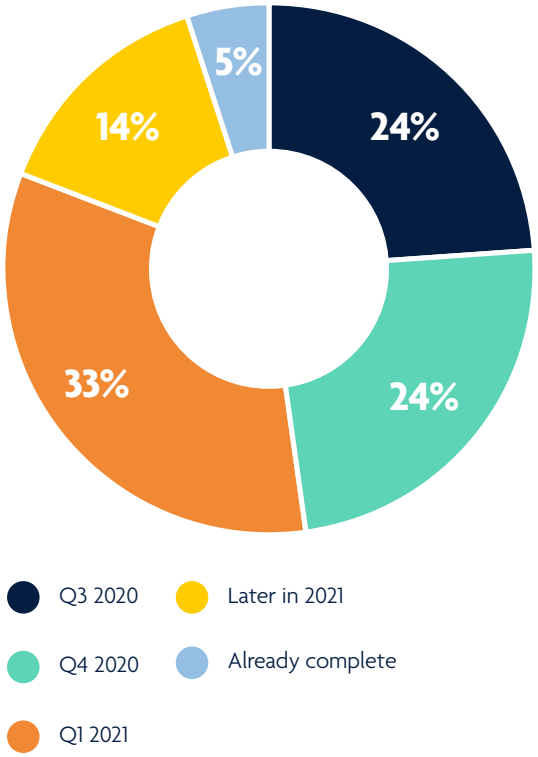


Chart 58. Intended rate selection

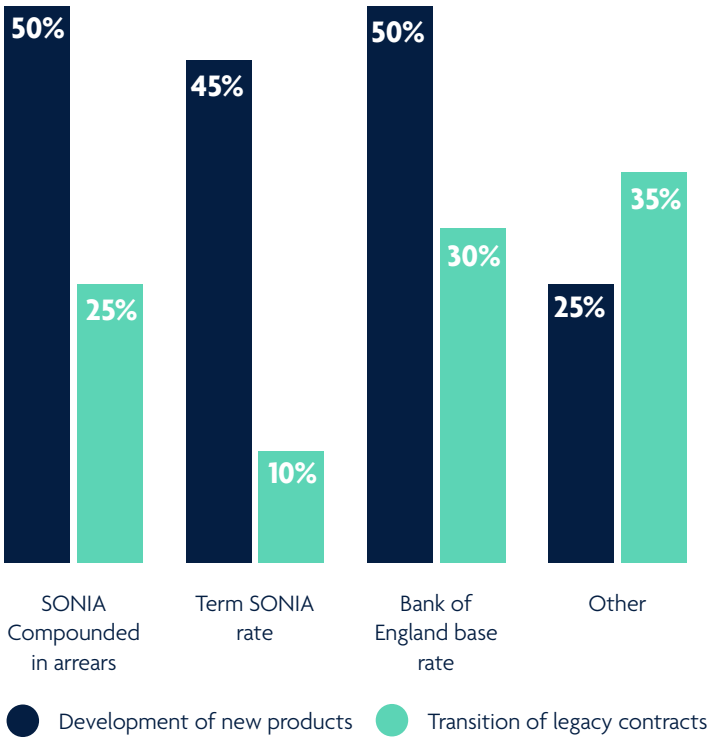
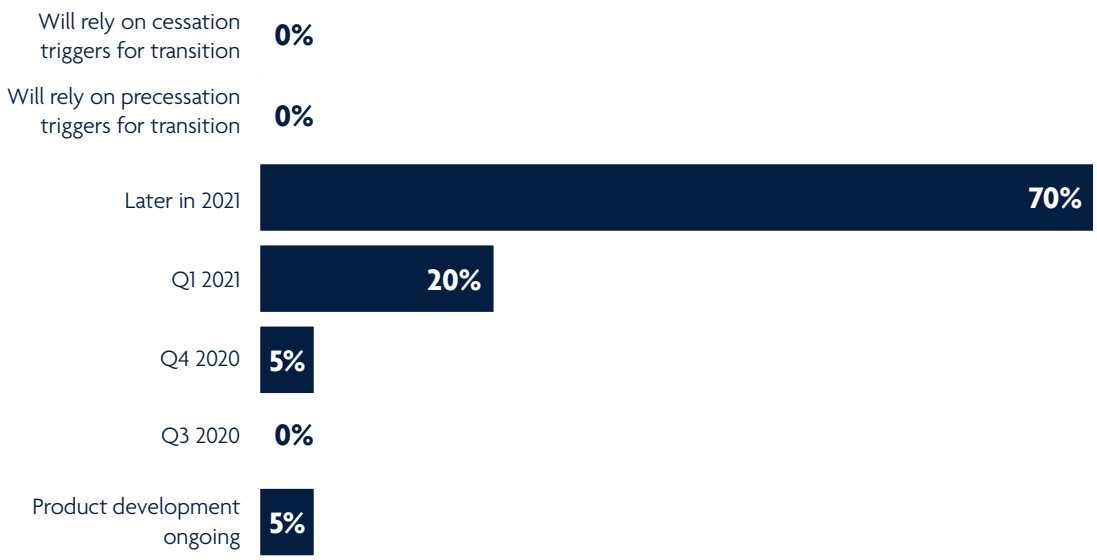


Chart 57. Expected timeline for transitioning legacy contracts to an alternative rate:



R. Deposit capabilities for corporates

Less than a third of firms noted this product featuring as part of their transition plans. SONIA compounded in arrears was the key rate being considered (59 per cent), suggesting that many of these deposit facilities were in place for larger corporates, but BoE Base Rate (27 per cent) will also play a role. There was a very high level of product development already underway.

Chart 59. When do you plan to start development of non-LIBOR alternatives?

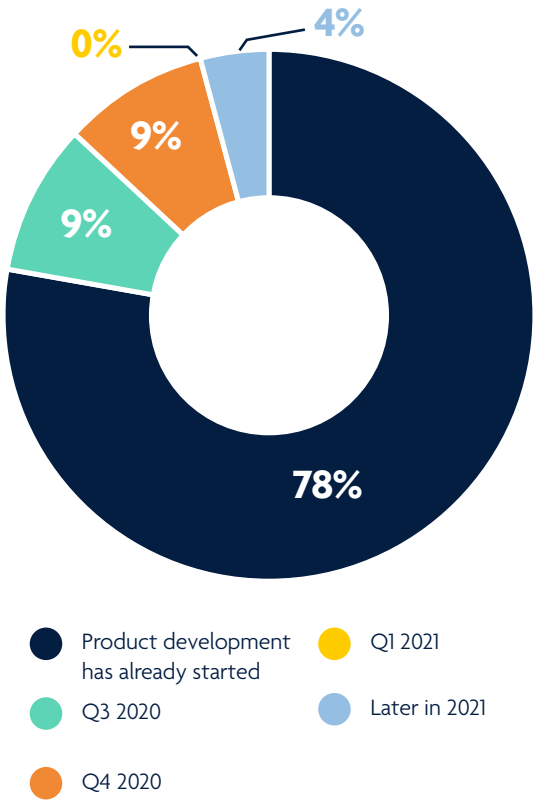


Chart 60. When do you expect development of non-LIBOR alternatives to be largely complete?

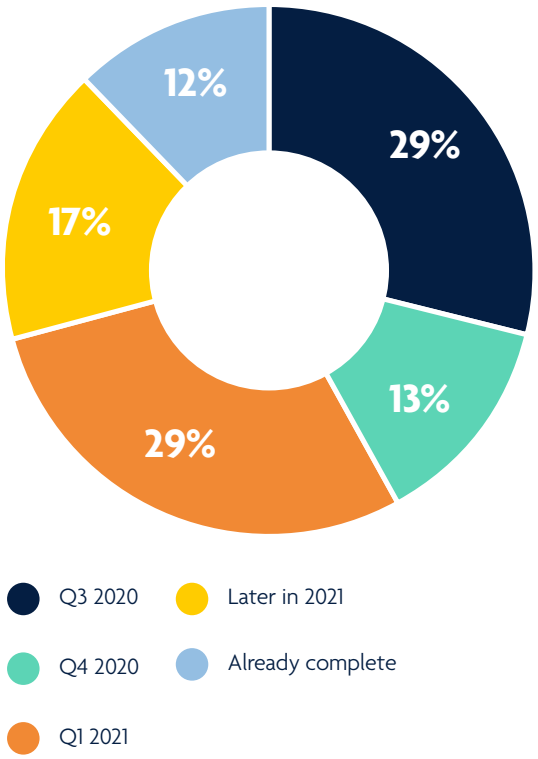


Chart 62. Intended rate selection

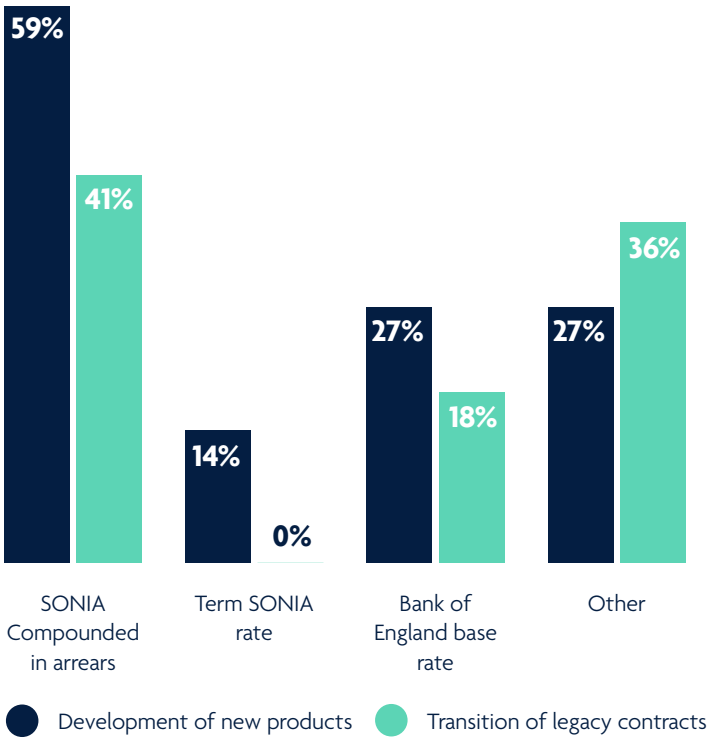
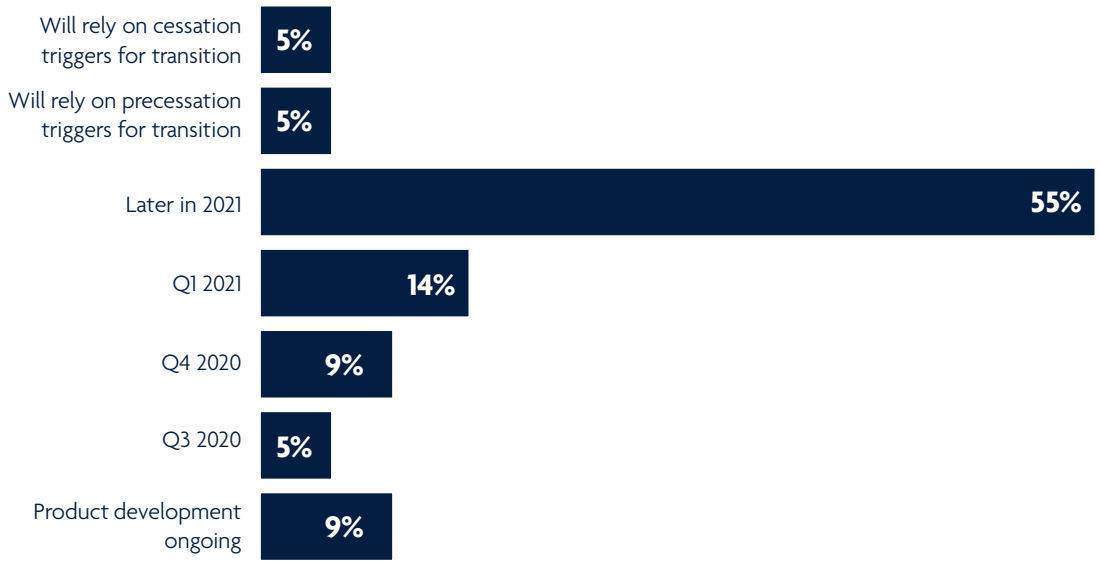


Chart 61. Expected timeline for transitioning legacy contracts to an alternative rate:



List of firms surveyed

AIB Group (UK) plc
Aldermore Group
Bank Leumi (UK) plc
Bank of China
Bank of Ireland (UK) plc
Bank of London and Middle East
Barclays Bank Plc
Belmont Green Finance Ltd.
Bibby Financial Services
C. Hoare & Co.
Capital Home Loans Limited
Citibank
Close Brothers
Coventry Building Society
Credit Suisse (UK) Ltd.
Cynergy Bank
Danske Bank
EFG Private Bank Ltd.
First Abu Dhabi Bank
Fleet Mortgages Ltd
Hampshire Trust Bank plc
Handelsbanken plc
HSBC Bank plc
Hodge Bank Ltd.
Investec Bank plc
JP Morgan Chase Bank, N.A.
Landbay Partners Ltd.
Leeds Building Society
Lloyds Banking Group
Metro Bank plc
Nationwide Building Society
NatWest Group
OakNorth Bank plc
OneSavings Bank Group
Paragon Banking Group
Paratus AMC Ltd.
Principality Building Society
Santander UK plc
Skipton Building Society
Sumitomo Mitsui Banking Corporation Europe Ltd.
Standard Chartered
TD Securities Ltd.
The Bank of New York Mellon
The Co-operative Bank plc
The Mortgage Lender Ltd.
The Norinchukin Bank
Topaz Finance (Computershare Loan Services)
UKAR Ltd.
Virgin Money UK plc
Wells Fargo
West Bromwich Building Society
Westpac Banking Corporation
And 12 other respondents

Table showing base number of respondents for each chart

Chart 1.	63
Chart 2.	58
Chart 3.	64
Chart 4.	64
Chart 5.	64
Chart 6.	50
Chart 7.	44
Chart 8.	55
Chart 9.	59
Chart 10.	62
Chart 11.	60
Chart 12.	42
Chart 13.	60
Chart 14.	See chart
Chart 15.	26
Chart 16.	26
Chart 17.	26
Chart 18. New products	24
Legacy contracts	25
Chart 19.	17
Chart 20.	14
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Chart 22. New products	13
Legacy contracts	13

Chart 23.	5
Chart 24.	5
Chart 25.	5
Chart 26. New products	5
Legacy contracts	5
Chart 27.	19
Chart 28.	19
Chart 29.	19
Chart 30. New products	18
Legacy contracts	19
Chart 31.	30
Chart 32.	30
Chart 33.	30
Chart 34. New products	30
Legacy contracts	29
Chart 35.	31
Chart 36.	31
Chart 37.	31
Chart 38. New products	31
Legacy contracts	31
Chart 39.	11
Chart 40.	11
Chart 41.	8
Chart 42. New products	11
Legacy contracts	9

Chart 43.	23
Chart 44.	22
Chart 45.	23
Chart 46. New products	23
Legacy contracts	23
Chart 47.	28
Chart 48.	28
Chart 49.	28
Chart 50. New products	28
Legacy contracts	28
Chart 51.	27
Chart 52.	27
Chart 53.	28
Chart 54. New products	27
Legacy contracts	27
Chart 55.	21
Chart 56.	21
Chart 57.	20
Chart 58. New products	20
Legacy contracts	20
Chart 59.	23
Chart 60.	24
Chart 61.	22
Chart 62. New products	22
Legacy contracts	22

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