



HONG KONG MONETARY AUTHORITY
香港金融管理局

Our Ref.: B1/15C

23 April 2020

The Chief Executive
All Authorized Institutions

Dear Sir / Madam,

Reform of interest rate benchmarks

I am writing to share with you the results of an earlier Survey on Reform of Interest Rate Benchmarks (the survey) conducted by the Hong Kong Monetary Authority (HKMA) and update you on the latest developments relating to the reform.

Survey results

The HKMA launched the survey in November 2019 to monitor the banking sector's progress in preparing for the transition to alternative reference rates (ARRs). The survey results indicate that there were HK\$4.5 trillion of assets and HK\$1.6 trillion of liabilities in the Hong Kong banking system referencing the London Interbank Offered Rate (LIBOR) at the end of September 2019, representing about 30% and 11% respectively of the banking system's total assets and total liabilities denominated in foreign currencies. Additionally, there were derivatives contracts involving an aggregate amount of HK\$35 trillion in notional value referencing LIBOR. Around one-third of these LIBOR-linked assets and liabilities, and almost half of these derivatives contracts would mature after end-2021 and did not have adequate fall-back provisions.

Regarding authorized institutions' (AIs) preparation for transition to ARR, many AIs had established a committee or appointed a senior executive to oversee the preparatory work, and were in the process of developing a firm-wide transition plan. Major challenges cited by AIs in preparing for the transition included: (i) the lack of standard and consistent fall-back languages for adoption by the industry; (ii) insufficient liquidity for products referencing ARR; and (iii) the lack of well-established term structures for ARR. These challenges are not unique to the Hong Kong market and, as explained below, are being addressed by authorities and leading organisations overseeing the transition. More details of the survey results can be found in **Annex 1**.

Updates on international and local developments

The HKMA has been monitoring developments relating to the benchmark reform closely. The UK Financial Conduct Authority issued a statement in March pointing out that the central assumption that firms cannot rely on LIBOR being published after

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the end of 2021 has not changed, notwithstanding the Covid-19 outbreak. Some of the organisations leading the transition to ARR, including the Working Group on Sterling Risk-Free Reference Rates in the UK and the Alternative Reference Rates Committee in the US, have published their work plans and expected milestones for 2020 to facilitate market participants' preparation. In parallel, these organisations as well as other industry bodies such as the International Swaps and Derivatives Association (ISDA) have kept on developing fall-back provisions for different types of products and market conventions in using ARRs (e.g. term structure). New issuance and trading volume of products referencing ARRs have continued to increase, thanks to the initiatives undertaken by authorities and industry organisations to promote the use of ARRs in financial contracts.

In Hong Kong, the Working Group on Alternative Reference Rates formed under the Treasury Markets Association (TMA) has been following up on issues that need to be addressed locally (e.g. taxation). The TMA has developed a dedicated web page containing a collection of useful information about the benchmark reform, aiming to help local market participants prepare for the transition (https://www.tma.org.hk/en_market_LIBOR.aspx). More details on latest developments relating to the benchmark reform can be found in **Annex 2**.

AIs should continue to closely monitor international and local developments relating to the benchmark reform, leveraging the resources available on the TMA's web page and other sources. They should take these developments into account in updating their own transition plans. Specifically, AIs should prepare to confirm their adherence to the ISDA Protocol that incorporates fall-back provisions for LIBOR once it is published.

The HKMA will continue to use the survey to monitor the banking sector's preparation for the transition. Should you have any questions about this letter, please contact Mr Gordon Wong on 2878-1272 or Mr Anthony Choy on 2878-1547.

Yours faithfully,

Raymond Chan
Executive Director (Banking Supervision)

Encl.