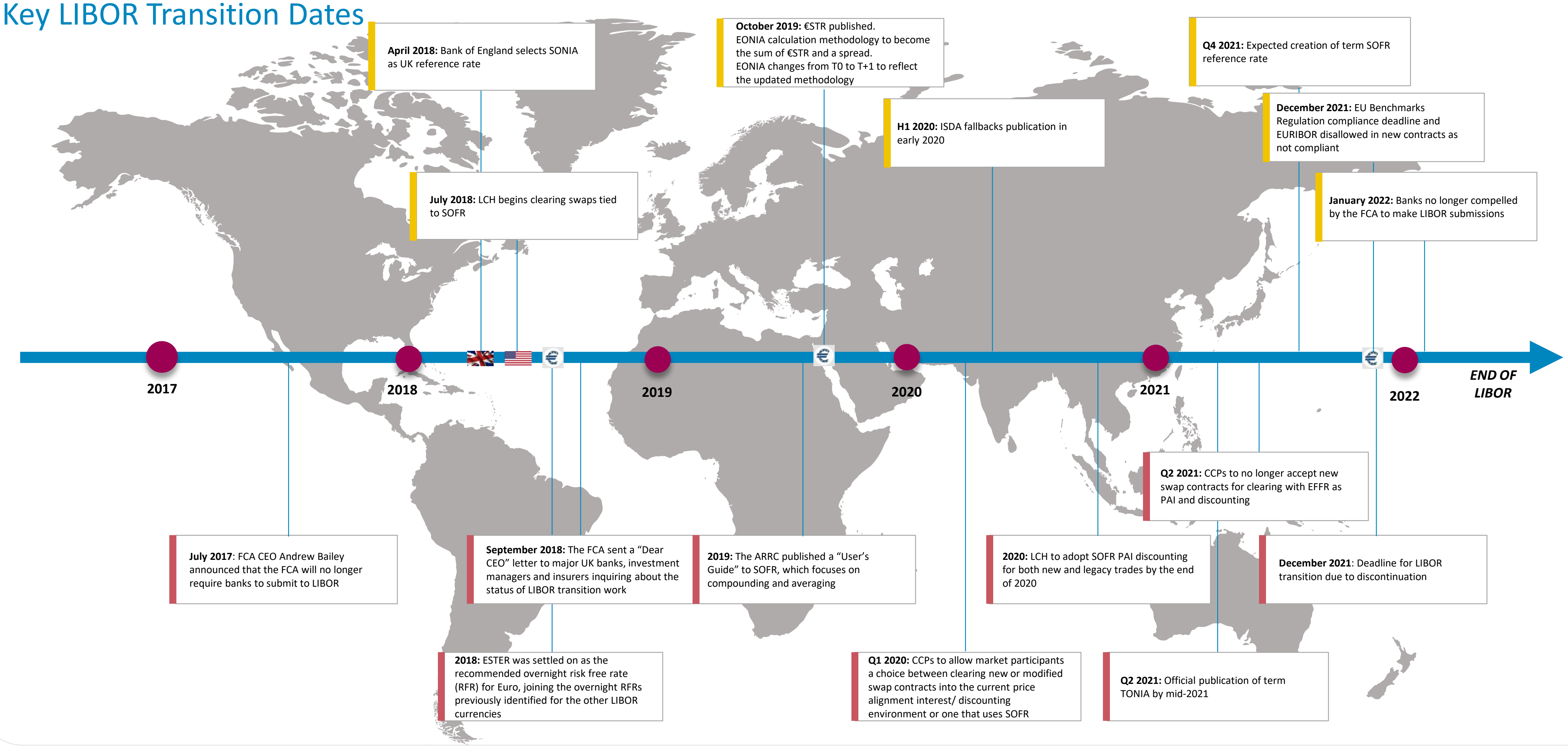
IBOR Transition roundtable for asset & investment managers

Impacts, risks and opportunities

Discussion topics

- Responding to market changes and deadlines
- Operational readiness and execution priorities for 2020
- Client communications and outreach

Key LIBOR Transition Dates



Your notes

Types	Impacts	Risks
Investments	• Likely to hold a large number of LIBOR based products in the portfolio • LIBOR derivatives used for hedging, FRNs, securitisations or loans • Managers still dependent on LIBOR based products as liquidity is not sufficient in RFRs • Fallback language is mostly inadequate for permanent IBOR discontinuation and may turn floating rate into fixed rate	• Change in economics and value transfer between counterparties during transition • Potential conduct risk in selling to customers who do not understand new RFRs • Counterparties may pursue litigation • Cash securities present a challenge as amendment requires concent from noteholders
Performance Tracking	• Managers typically use IBORs to track performance targets for some funds or mandates • Used primarily across Alternative funds, Money Market funds and Allocation funds • Benchmarks for funds might indirectly reference IBOR indices • Many fixed income funds reference (L)IBOR rates against which not only performance but also management fees are measured • Changes to the discounting curve or the reference rate within can change the NPV of FRN or derivatives	• New benchmark communication must avoid perception of artificially infated performance • Clients may reduce AUM if there is a perceived decrease in performance • Conduct risk in transitioning in a way that is perceived as creating a benefit for the Firm • Fund benchmark calculation methodology using ARRs (and spread) not yet defined • Changes in benchmark can affect the fee incomes • Risks of winner and losers value transfer due to NPV change when ISDA fallback is triggered
Operational Changes	• IBORs are an input across a variety of internal calculations, systems, FO models, spreadsheets • Finance change to accommodate differences in accrual calculations and hedge accounting • Risk calculation changes and measurement of historical stresses and correlations • Contracts with 3rd party providers may reference LIBOR (e.g. for late payment interest)	• Model accuracy decreases due to a lack of historical data • Systems are not updated in time to support RFRs or backward compounding of overnight RFR instead of using LIBOR terms tructure • Economic risk from poor handling of their client portfolios, operational, conduct and legal risk with clients and counterparties

Claire Paisley
Partner,
Financial Services

Bruce Laing
Partner,
Financial Services

Lucine Tatulian
Partner,
Financial Services

IBOR Transition roundtable for asset & investment managers

Impacts, risks and opportunities

Discussion topics

- Responding to market changes and deadlines
- Operational readiness and execution priorities for 2020
- Client communications and outreach

Are you ready to transition? Early-mover advantages

First movers are beginning to treat LIBOR's end as an event with strategic implications—and as an opportunity to improve operations and relations with clients, shareholders, and employees. They're using scenario planning to prepare for a variety of potential outcomes. They're also starting to make changes that will be needed regardless of the contours of post-LIBOR finance.

H1 2019

- **Determine the exposure** to IBORs by currency, product, client and legal entity
- **Complete an impact assessment** to understand the changes needed to models, processes, systems, controls, data, etc.
- **Start transition** in products for which there is sufficient liquidity for ARRs in the market
- **Create awareness** about the IBOR transition within the organisation

H2 2019

- Gather information on the **documents that reference LIBOR** and expire post 2021
- **Start implementation efforts** for the models, process, controls, technology & data changes needed
- **Plan for client outreach** to communicate the reasons for change and their effects
- **Continue transition** in products that are supported by market liquidity
- Include revised **fallback language** in new documents

2020

- **Continue to make implement changes** to models, processes, systems, controls, data, etc.
- **Engage with clients** to raise awareness of LIBOR transition and the possible impact on their portfolio
- Analyse **new benchmarks** required
- **Start to repaper** to switch to ARRs and include revised fallback language where required
- **Progress exposure transition** in products that are supported by market liquidity

2021

- **Finish operational changes** needed to models, processes, systems, controls, data, etc.
- **Regular communication** with clients to keep them aware of market changes
- **Complete repapering** efforts
- Finish moving **all remaining exposures to new rates**

Investment Managers should have completed the above planning items in 2019 *Today* *Transition execution priorities should be underway*

Investment Managers use LIBOR in 3 main ways and these will need to be managed carefully through transition:

- **LIBOR based products** in their portfolios (LIBOR-based derivatives used for hedging as well as LIBOR-based floating rate Notes, securitisations, or private debt)
- LIBOR as a **benchmark or performance target for funds** or mandates, particularly in alternatives, asset allocation/absolute return funds, and fixed income funds
- LIBOR as an **input into various calculations, systems and models** for operations and administration

Investment Managers, therefore, face a number of transition risks including; economic risk, operational risk, conduct and legal risk with clients and counterparties.

Immediate Transition Actions

Valuation and Risk

- Recalibration of internal valuation models, forecasting or scenario for replacement RFRs
- Vendor valuation changes
- Impact on margin calculations
- Adjusted valuation and risk models and policies
- Contract analysis/remediation and term renegotiations
- LIBOR dependencies for benchmark performance/fee generation

Communications

- Regulatory inquiries and disclosures
- Investor communication strategies
- Industry working group and consultations
- Fund documentation e.g. prospectus, KIIDs etc.
- Financing and vendor relationships
- Direct origination programs
- Client updates using blogs, FAQs etc.
- Notice requirements and executive management and board reporting

Operations

- Adequacy of fallback language
- Interest rate calculations changes
- Arrangements with third party providers (admin, tech, brokers, custodians)
- Policies, processes, model, risk, accounting, tax, legal and systems changes
- Coordination of multiple funds across jurisdictions
- Trade order management, collateral management and reconciliation systems
- Updates to information systems and security master data
- Contracts amendments and term changes

Investment Strategy

- Rethink pricing/fee structure
- New markets/products arising from use of new RFRs
- Evolving investment strategy
- Borrower communications and negotiations
- Change in volumes
- Change in liquidity in the RFRs' derivatives market
- Investor Master Agreements
- Portfolio company management

Your notes

Specific Challenges for Asset & Wealth Managers

- A variety of **asset classes in different geographies** through various strategies
- **Third party dependency** such as custodians, administrators, brokers, pricing vendors, co-investors, sub-advisors
- **Large and complex investor base** including institutional and retail clients, both direct and via intermediaries
- **Relatively opaque data sources** across front-to-back operations compared to banks who have undergone SMR and BCBS239