



Transition from LIBOR

June, 2020

What is SOFR?

SOFR (Secured Overnight Financing Rate) is the average rate at which institutions can borrow US dollars overnight while posting US Treasury bonds as collateral.

- Similar to a mortgage rate, SOFR is a secured borrowing rate in the sense that collateral is provided in order to borrow cash. SOFR differs from US LIBOR in that the latter is a rate for unsecured borrowing (where no collateral is posted).
- SOFR is intended to replace the US dollar London Interbank Rate (US LIBOR) in future financial contracts.

How Is SOFR Calculated?

SOFR is calculated as a volume-weighted median of transaction level tri-party repo data, GCF Repo transaction data & data on bilateral Treasury repo transactions cleared through FICC's DVP service (from DTCC Solutions).

- SOFR is published each business day on the New York Fed's website.

- Secured overnight financing rate (SOFR) is a benchmark interest rate for dollar-denominated derivatives and loans
- SOFR is based on transactions in the Treasury repurchase market and is seen as preferable to LIBOR since it is based on data from observable transactions rather than on estimated borrowing rates.
- While SOFR is becoming the benchmark rate for dollar-denominated derivatives and loans, other countries have sought their own alternative rates, such as SONIA and EONIA.

SOFR vs LIBOR

SOFR	LIBOR
Risk free rate (no credit risk)	Bank lending rate (includes credit risk)
Overnight (backward looking)	Forward looking
Secured (collateralized)	Unsecured (uncollateralized)
Calculated & published daily by the NY Fed	Calculated & published daily by ICE Benchmark Administration
Transaction based	Based on LIBOR bank submissions & expert judgement
Based on ~\$1T transactions pd (repo markets)	Based on ~\$1B transactions pd (3-month LIBOR)
No term structure	Term structure

Currently in the News

"The US Federal Reserve has agreed **to ditch** the secured overnight financing rate, or SOFR, as the benchmark for its emergency loans in response to the Covid-19 pandemic, deciding to use US dollar LIBOR as the reference rate instead"

"The central bank had originally wanted to use its preferred replacement for Libor in its two Main Street Lending Programs for new loans and expanded loans when it released details on April 9. But pushback from the industry prompted a rethink at the Fed"

Timeline for Transition



What is AMERIBOR?

AMERIBOR (American Interbank Offered rate) is an index of overnight unsecured lending taking place across the Chicago Board Options Exchange platform AFX (American Financial Exchange)

- Overnight unsecured loans from "small and mid-sized banks, broker-dealers, insurance companies, private equity firms, hedge funds, FCMs, asset managers and finance companies."
- AMERIBOR is mainly concerned with the interbank market between smaller, regional US banks.

How Is AMERIBOR Calculated?

- AMERIBOR is calculated as the transaction volume weighted average interest rate of the daily transactions in the AMERIBOR overnight unsecured loan market on the AFX.
- It is an interest rate expressed on an Actual/360 Day Count and Following Business Day convention that is rounded to the fifth decimal place.
- Calculated after the close of trading on the AFX and is published nightly by CBOE under ticker symbol AMBOR.

Benefits : - SOFR vs AMERIBOR

SOFR

SOFR relies entirely on transaction data, whereas LIBOR is based partially on market-data expert judgment

SOFR is derived from transactions in a very large existing base of liquid markets

SOFR is the most robust rate available with underlying transactions of about \$1 trillion per day or more, much larger than the volumes associated with other potential Libor alternatives

AMERIBOR

SOFR is excellent for large banks that own government securities. But for regional, midsize, and community banks, their lack of familiarity with that market makes the transition to AMERIBOR easier.

Regional, midsize, and community banks borrow unsecured. This gives AMERIBOR an advantage, because it creates assets that are correlated to their own borrowing cost

AMERIBOR is highly correlated with the old LIBOR and the least volatile of interest rate benchmarks

SOFR Transition – What Banks need to address

