

LIBOR Transition & CLOs

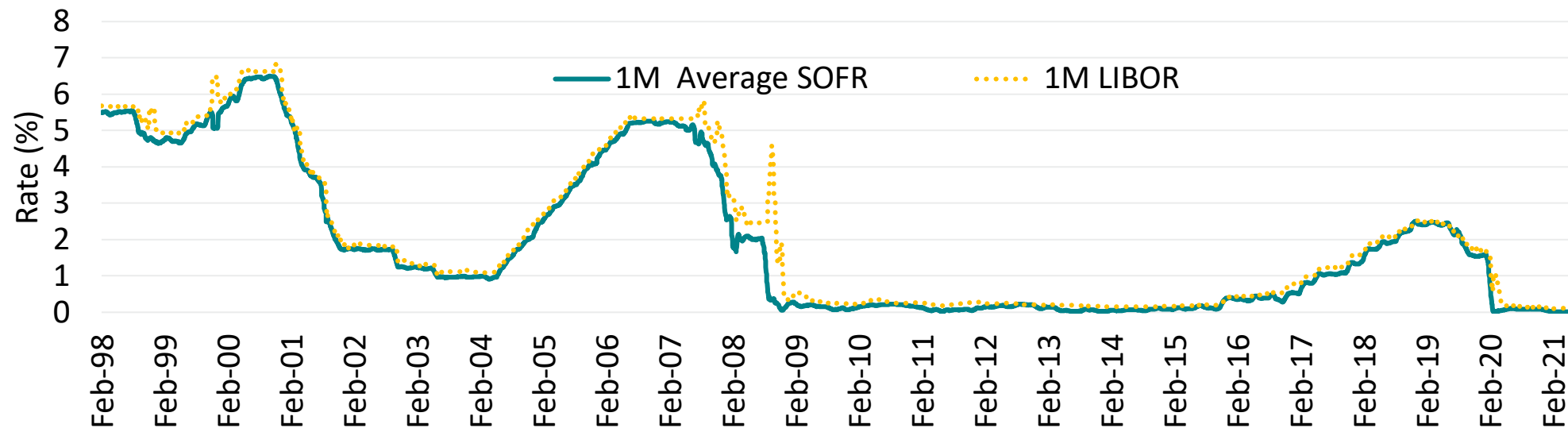
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Things to Know

- Economics: How SOFR behaves; why the CSA; relevance of the floor
- Where we go from here: All SOFR, (nearly) all the time; Getting your ducks in a row; Remediation looms

Economics: LIBOR & SOFR Generally Trend Together, May Separate in Market Disruptions

SOFR & LIBOR Trend Together; Both Affected by Fed Interest Rate Policy;
May Separate in Market Disruptions

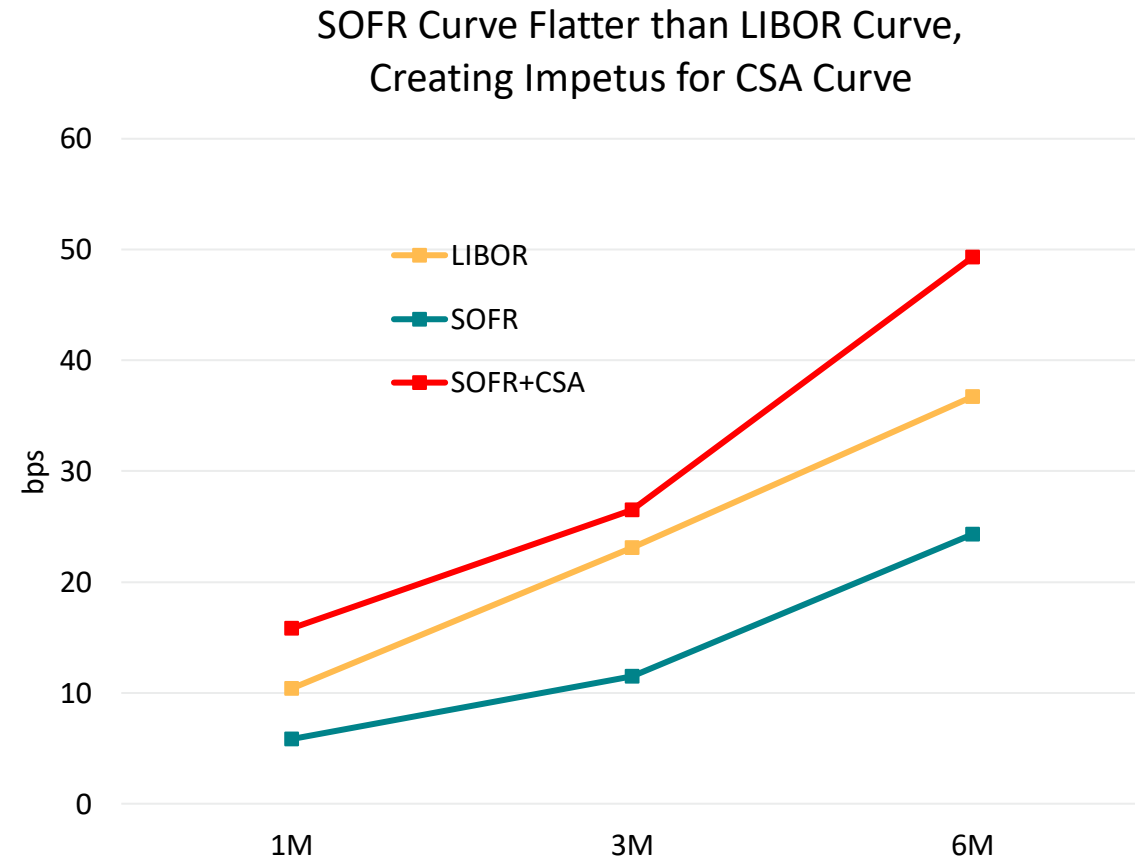


- LIBOR and SOFR both respond to interest rate policy
- Between 1998 and 2021, the difference between LIBOR & SOFR was between 5 and 30 bps 70% of the time
- However, the difference is not constant and LIBOR can widen materially in periods of market disruption (like 2008 or March 2020)

Source: LSTA, Wells Fargo, Bloomberg, FRBNY

Economics: Why the SOFR CSA Curve? Other Approaches?

- The SOFR curve is lower and flatter (green curve)
- The LIBOR curve is higher and steeper (e.g., 3M LIBOR tends to be higher than 1M LIBOR (yellow curve))
- To maintain a higher “reference rate” for longer interest rate contracts, many SOFR loans include a “Credit Spread Adjustment (CSA)” Curve of 10 bps for 1M/15 bps for 3M/25 bps for 6M (red curve)
- Some transactions have a flat CSA for all tenors
- Other transactions might pull the CSA into a wider margin itself
- Still others might use an “Adjusted SOFR”, which would be SOFR+a fixed spread adjustment
- There are strengths and weaknesses of each approach
- Review your documents to know what you have!

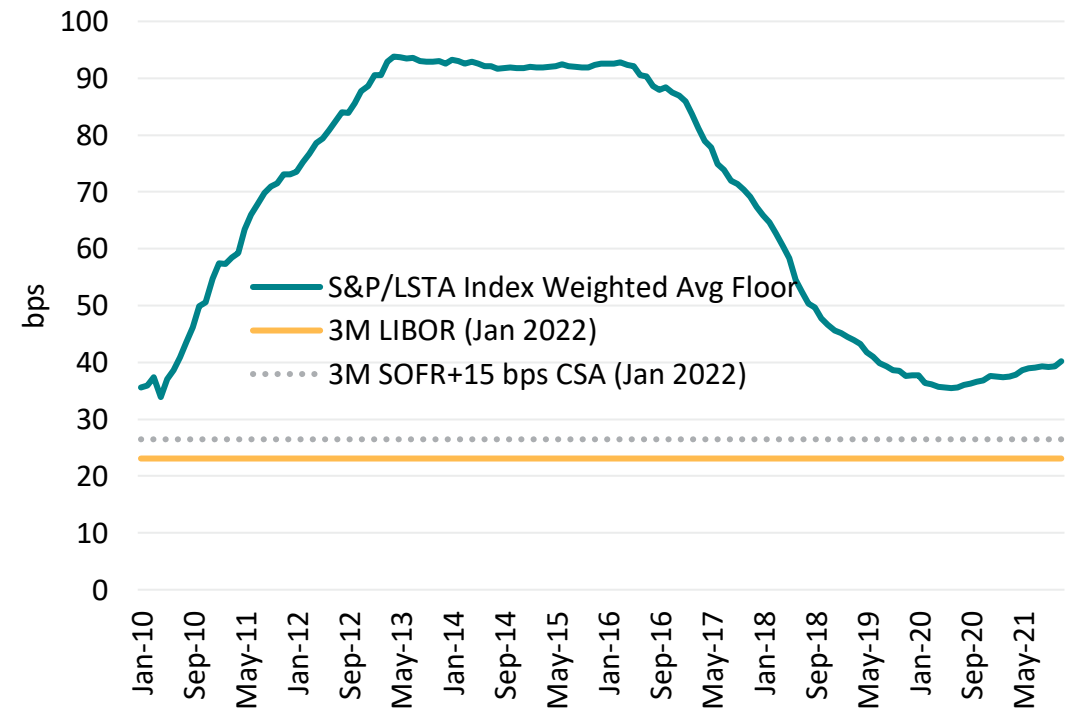


Source: LSTA, CME Group, WSJ

Economics: An Interest Rate Floor Can Address Economics, Ease Transition *if it is Still Applicable at Transition*

- There are questions about whether new SOFR loans or loans that flip from LIBOR to SOFR may pay less
- LIBOR floors can mitigate this risk if they are still applicable at transition
- Roughly half the loans in the S&P/LSTA Leveraged Loan Index (and nearly all new BSL institutional loans) have a LIBOR floor
- The average floor is 75 bps on Index loans and 60 bps on new issue loans; both currently are above either LIBOR or the typical SOFR+CSA
- An interest rate floor that reduces economic mismatches between LIBOR and SOFR, and also could ease transition frictions (***assuming your floor is high enough and also ports over to SOFR during transition...***)

Weighted Average Floor Level in S&P/LSTA Loan Index vs LIBOR, SOFR+CSA



Source: S&P/LSTA Index, LCD, CME Group, WSJ, LSTA Calculations

Now That We Survived 12.31.21...Where to Now?

- Why are there some LIBOR loans still?
 - Loans underwritten in 2021 and sold in 2022
 - Some private credit transactions may continue on LIBOR for a period of time
 - Incrementals/fungible add-ons that are contemplated under pre-existing contracts remain a gray area
- Are you ready for all new SOFR loans?
 - Do you have your CME Term SOFR License?
 - Are your systems able to handle CSAs, CSA Curves?
 - Look at the LSTA Term SOFR Concept Credit Agreement to understand SOFR loan doc structure - <https://www.lsta.org/content/term-sofr-concept-document/>
 - Look at LSTA LIBOR Transition Checklist to see forms that SOFR and CSAs can take - <https://www.lsta.org/news-resources/advisory-libor-transition-checklist/>
- Prepare for many loans falling back from LIBOR to SOFR well before June 2023
 - Do you have a remediation plan in place?
 - LSTA is working on a universal fallback amendment, which may streamline Early Opt In transitions
 - Be prepared to watch for – and quickly vote on! – 51% negative consent transition amendments

Appendix: Resources, ARRC Recommended Spread Adjustments for Fallbacks

LSTA Resources: LIBOR Call, Podcasts, Documents & News

The screenshot shows the LSTA website's 'Weekly LIBOR Q&A Call' page. The header includes the LSTA logo and navigation links: ABOUT, ADVOCACY & REGULATORY, DATA & ANALYSIS, LEGAL & DOCUMENTATION, OPERATIONS, and LSTA UNIVERSITY. The main heading is 'WEEKLY LIBOR Q&A CALL'. Below this, there is a brief introduction: 'The LSTA has initiated a weekly live LIBOR Q&A call on Monday afternoons at 3PM(ET). This call is intended to address LIBOR questions coming into the LSTA. There are two ways to ask questions: You can ask questions live on the call or You can email your question to LIBOR information and we will collect these questions and answer them on the call.' There are also sections for 'EVENT DETAILS' (Next Scheduled For Monday, February 22, 2021) and 'DOCUMENTS TO VIEW (18)'. A sidebar on the right contains 'WHAT'S TRENDING' (Request For Member Access, Past Event Slides/Replays, Fitch Ratings: Outlook 2021 Leveraged Finance, Sign Up For US Leveraged Finance CLO Weekly Newsletter from Fitch Ratings) and 'NEWS' (LSTA Publishes Updated Green Loan Principles and Guidance February 16, 2021).

The screenshot shows the LSTA website's 'LSTA Podcasts' page. The header is identical to the previous screenshot. The main heading is 'LSTA PODCASTS'. Below this, there is a grid of podcast thumbnails. Each thumbnail features the LSTA logo and a title: 'CREDIT SENSITIVE RATES - BLOOMBERG', 'CREDIT SENSITIVE RATES - ICE BENCHMARK ADMINISTRATION', 'CREDIT SENSITIVE RATES - AFX', and 'CREDIT SENSITIVE RATES - IHS MARKIT'. All podcasts are dated 'March 31, 2021'. There is also a search bar at the top left and navigation links at the top right.

The screenshot shows the LSTA website's 'Content Archive' search results for 'LIBOR'. The search bar shows 'LIBOR' and '13' results. The page is divided into 'REFINE RESULTS' and 'WHAT'S TRENDING' sections. The main content area is titled 'LOAN MARKET LEGAL & DOCUMENTATION' and includes a search results list with items like 'LIBOR FALLBACK LANGUAGE AMENDMENT FEES' and 'LIBOR REPLACEMENT PROVISIONS FOR AMENDMENT OF CLO INDENTURE'. A sidebar on the right contains 'WHAT'S TRENDING' and 'NEWS' sections, similar to the other screenshots.

The screenshot shows an email message from LSTA News. The subject is 'LSTA Week in Review: Ops Vision (& Passion); ESG's ERA; LIBOR's Deathline; Bankruptcy Buzzes'. The sender is 'LSTA News <lstanews@lsta.org>' and the recipient is 'Meredith Coffey'. The email content includes a 'PRINTABLE PDF VERSION AVAILABLE HERE' link and a 'Friday 2/12/2020' date. The email body text says 'Happy Friday!' and 'This Week in Review:' followed by a list of links to articles: 'Ellen Helfferan shares her Ops Vision & Passion', 'Tina Vinnago heralds ESG's Era... and the Toolkit to make it happen', 'Meredith Coffey details LIBOR's deathline', and 'Elbet Ganz reviews the new Buzz in Bankruptcy'. The email footer says 'We hope you enjoy the newsletter and the (long) weekend.'

Economics: ARRC Spread Adjustments on Legacy Loans vs Market CSAs on New Loans

- ARRC spread adjustments (11 bps for 1M, 26 bps for 3M) are specifically and explicitly for contracts that fallback from LIBOR to SOFR using hardwired fallback language.
- They were not intended to be used in new contracts.
- See [ARRC Spread Adjustment Public Consultation](#), which stated:
 - *It is important to emphasize that any ARRC-recommended spread adjustments are intended for use in LIBOR contracts that have incorporated the ARRC's recommended hardwired fallback language or for legacy LIBOR contracts in which parties are able to and choose to select an ARRC recommended spread-adjusted rate as a fallback. **The recommended spread adjustments would not and are not intended to apply to new contracts referencing SOFR.***
- The ARRC Fallback Spread Adjustment reflects the results of two public consultations, and was set as the 5-year historical median difference between LIBOR and SOFR on the date that the FCA announced LIBOR's cessation (March 5, 2021).
- The ARRC has said that ***it would not reconsider*** the spread adjustment as it went through a robust consultation process; an ex-post change would disrupt a long-anticipated approach.