

## CME Conversion Plan for Eris LIBOR Products

As the industry advances risk-free rate (RFR) indexed swaps, CME Group continues our collaborative approach to identify, understand, and create innovative solutions for hurdles faced by market participants.

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### Background:

IBOR Fallbacks have been widely implemented across the industry:

- ICE LIBOR Phase-out: Further to the UK FCA announcement on March 5, 2021, issued in coordination with ICE Benchmark Administration Limited (“IBA”), the authorized administrator of ICE LIBOR, all remaining USD LIBOR tenors (e.g., overnight, one-month, three-month, six-month and twelve-month) will either cease to be provided by IBA or will no longer be representative of the underlying market immediately after publication on June 30, 2023
- ISDA Fallbacks: ISDA confirmed that the FCA announcement constitutes an “Index Cessation Event” for the purposes of ISDA’s IBOR Fallback Supplement and Protocol. As a result, on July 3, 2023, affected USD OTC IRS will fall back to the relevant credit and spread adjusted fallback SOFR rate, the relevant ISDA “Index Cessation Effective Date” (ICED)
- CME Plan: CME incorporated ISDA IBOR fallbacks in January 2021 and the ISDA 2021 Definitions in October 2021. However, based on market feedback, in December 2021, ahead of the discontinuation / non-representativeness of the GBP, JPY, and CHF LIBOR rates, CME successfully converted these non-USD LIBOR cleared swap exposures into standard CME cleared Risk-Free Rate swaps, with a cash adjustment to compensate for changes in valuation. CME intends to use a similar approach for USD LIBOR products:
  - [Cleared USD LIBOR swaps](#)
  - [Eurodollar futures and options](#)

### Complications associated with ISDA Fallbacks for Eris LIBOR contracts

Analogous to the cleared swap market, participants have identified certain challenges associated with implementing ISDA Fallbacks for Eris LIBOR contracts, including:

- **Operational** – After the USD ICE LIBOR Index Cessation Effective Date, while the IBOR-referencing Eris contracts will “fall back” to SOFR, these resulting legacy contracts will not be fungible with Eris SOFR contracts. As a result, participants wishing to unwind these “fallback legacy” contracts will need to execute and book additional Eris LIBOR contracts.
- **Risk management** – Uncertainty will remain regarding what the liquidity profile for Eris LIBOR contracts will look like in the years post the Index Cessation Effective Date

### Conversion as a solution:

To help address these challenges, market participants have requested CME to convert existing Eris LIBOR positions to Eris SOFR contracts just prior to the USD ICE LIBOR Index Cessation Effective Date.

CME Group recognizes the challenges and has consulted with market participants to consider the merits of a mandatory conversion. Before addressing operational mechanics, we wish to emphasize that:

- The goal is to execute a solution that is aligned with other cleared and listed USD ICE LIBOR products in terms of approach.
- The core principle of any conversion solution will be to minimize disruptions, including any impacts to valuation, duration, or discounting risk.

Following the publication of a conversion proposal and an extended period for comment, we believe the market is supportive of converting Eris LIBOR positions to Eris SOFR contracts utilizing the following guidelines:

**Methodology and Timing:**

- On Friday, June 23, 2023, CME will conduct the final mark-to-market for Eris LIBOR contracts in accordance with the ISDA IBOR Fallbacks Pricing Methodology, using the Eris SOFR settlement curve.
- On Sunday, June 25, 2023, CME will close out existing Eris LIBOR positions and replace the risk by substituting positions of equal size in Eris SOFR contracts containing the same effective date and underlying tenor. Please note, this substitution will use the settlement prices from Friday, June 23, 2023.
- For most contracts, the fixed rate of the resulting Eris SOFR contract will be 25 bps below the corresponding Eris LIBOR contract, which difference is approximately aligned with the ISDA fallback spread of 26.161 bps for 3M USD ICE LIBOR and will minimize any changes to duration, discounting risk and the effective coupon carry between the new fixed rate of the resulting Eris SOFR futures contract and the floating SOFR rate. In the few cases where contracts have a coupon difference other than the 25 bps, the proposed adjustment methodology would incorporate the additional coupon difference when determining the value of the new Eris SOFR position.
- On a go-forward basis following the conversion for Eris position holders, CME will utilize the B & C values (historical fixed, floating and PAI cash flows, respectively) corresponding to the Eris SOFR contracts for the calculation of daily and final settlement prices.

**Example:**

The below example is an illustration to show how mandatory conversion will work for Eris LIBOR futures contracts on the conversion date:

Date	Position   Contract   Coupon	Settlement
Thursday, June 22, 2023	<p style="text-align: center;"><u>Original Position</u></p> <p style="text-align: center;"><b>+100   LIYU19   3%</b></p>	<ul style="list-style-type: none"> <li>• LiborSwapNPV is marked-to-market using the Eris LIBOR settlement curve</li> <li>• Settlement Price = 100 + LiborSwapNPV + B<sub>L</sub> - C<sub>L</sub></li> </ul>
Friday, June 23, 2023	<p style="text-align: center;"><u>Original Position</u></p> <p style="text-align: center;"><b>+100   LIYU19   3%</b></p>	<ul style="list-style-type: none"> <li>• LiborSwapNPV is based on the Eris SOFR settlement curve and will incorporate the ISDA IBOR Fallback spread</li> <li>• Settlement Price = 100 + LiborSwapNPV + B<sub>L</sub> - C<sub>L</sub></li> </ul>
Sunday, June 25, 2023	<p style="text-align: center;"><u>Original Position</u></p> <p style="text-align: center;"><b>+100   LIYU19   3%</b></p> <p style="text-align: center;"><u>Offset Position</u></p> <p style="text-align: center;"><b>-100   LIYU19   3%</b></p> <p style="text-align: center;"><u>Onset Position</u></p> <p style="text-align: center;"><b>+100   YIYU19   2.75%</b></p>	<ul style="list-style-type: none"> <li>• The Offset and Onset positions are priced using the prior day's settlements, resulting in no variation margin when compared to Friday</li> </ul>
Monday, June 26, 2023	<p style="text-align: center;"><u>Post-Conversion Position</u></p> <p style="text-align: center;"><b>+100   YIYU19   2.75%</b></p>	<ul style="list-style-type: none"> <li>• SOFRSwapNPV is marked-to-market using the Eris SOFR settlement curve</li> <li>• Settlement Price = 100 + SOFRSwapNPV + B<sub>S</sub> - C<sub>S</sub></li> </ul>

### **CME Group Next Steps and Timing Goals**

The contents of this document are for informational purposes only and provide an overview of CME's approach to the USD LIBOR transition for Eris LIBOR contracts. The plan is subject to change at any time without prior notice. Any implementation of the points discussed is subject to regulatory review and to any necessary internal and external approvals. Please contact your CME Group sales representative, or email [InterestRate@cmegroup.com](mailto:InterestRate@cmegroup.com) if you would like to raise any questions, provide feedback, and/or discuss the Eris LIBOR conversion in further detail.