# INTEREST RATE BENCHMARK SURVEY REPORT

November 2019

Australian Securitisation Forum

# Executive Summary

The Australian Securitisation Forum (ASF) conducted this survey to gather feedback from participants in the Australian securitisation industry on the current and future use of interest rate benchmarks.

Global markets are changing and, with the likely cessation of LIBOR by late 2021, beginning to adopt new benchmarks to replace LIBOR. Australian securitisations are not isolated from the global market developments and the ASF has conducted this survey to gauge interest and opinions from a wide range of market participants.

Respondents were generally supportive of the use of 1-month BBSW as the preferred benchmark in AUD securitisations for the next twelve months. However, they were less sure of the longer-term (greater than twelve months) utility of 1-month BBSW.

Despite the lower support for 1-month BBSW in the longer-term, there was no distinct preference for an alternative benchmark. Several respondents were clear that the Australian market should adopt global practices where possible.

There was resounding support for the ASF providing guidance for standardised fallback and risk disclosure language. Many participants saw this as providing clarity on these important components of new issues as well as potentially saving costs for issuers and investors.

The survey respondents were very clear that the ASF should promote further discussion over 2020 on the key themes identified in the table that follows.

| Major themes | Commentary |
|---|---|
| Continued use of 1-month BBSW is largely supported in the short-term | • Well supported for the next 12 months (82% of responded 'mostly' or 'completely' suitable)<br>• Clear support dropped to 39% greater than 12 months |
| In the medium-term, there was no clearly preferred alternative to 1-month BBSW | • Three alternatives ( 3-month BBSW, AONIA and Term AONIA) all received support<br>• Respondents commented the ASF should continue to promote ongoing discussion as markets evolve here and offshore |
| ASF should consider providing guidance for the Australian securitisation market in fallback and risk disclosure language | • Both well supported by respondents<br>• Benchmark fallback language describing how alternatives would be implemented by issuers should be considered<br>• Risk disclosure language describing the risks of benchmark discontinuation or change to be included in new issues should also be considered |
| The AUD securitisation industry should aim for consistency with current and emerging global standards | • The choice of interest rate benchmark should be as consistent with evolving global practice as possible<br>• The language and application of fallbacks should be consistent with global standards as much as possible |
| Operational considerations are important in making any changes to the use of benchmarks and/or fallbacks for benchmarks | • Moving to another benchmark could be costly and very difficult for some market participants, especially smaller issuers and investors<br>• IT systems could be problematic to adapt to certain benchmarks<br>• Accounting, valuation and disclosure systems and processes are also important to consider |
| Levels of understanding of alternative benchmarks varies considerably across firms and within firms | • Many responses demonstrated a lack of understanding of the potential benchmarks and/or the implications of changing<br>• The ASF could consider working with the broader industry to improve understanding of alternatives to BBSW, and fallbacks and risk issues |
| The needs and requirements of all participants should be considered | • Smaller firms may have the same issues as larger firms but may not have the resources to change systems and processes quickly<br>• Offshore investors requirements are important when considering changes to benchmarks and/or fallbacks |
| Any proposed changes to the Australian securitisation market will require the support of many participants to be effective | • Investors and issuers will have to work towards consensus on any changes<br>• Other participants (e.g. warehouse suppliers, legal firms, custodians) will also need to be involved |

# Table of contents

# 1. The role of the Australian Securitisation Forum in interest rate benchmark reforms

Since 1989, the ASF has performed a pivotal role in promoting and representing the industry to government, regulators, the public, investors and others who have an interest or potential interest both in Australia and overseas, regarding the benefits of securitisation in Australia and aspects of the securitisation industry.

It is the peak industry body representing participants in the securitisation market, which includes issuers of securitisation paper - major banks, smaller Authorised Deposit-Taking Institutions and specialised non-banks - plus fixed income investors and service providers to the sector.

This survey was conducted in October 2019 to gather specific feedback from the ASF members and the wider participants in the Australian securitisation market concerning potential interest rate benchmark reforms both locally and globally.

## The Survey

*The global transition of floating rate benchmarks used in the debt capital and derivatives markets is a fundamental and important step in the evolution of the operations of financial markets. The Australian securitisation market is cognisant of the implications of global developments on the operation of the domestic mortgage and asset-backed markets.*

*Australia does not face the immediate time pressures other markets face with the phase out of IBOR reference rates for floating rate debt and derivative exposures. The ASX, as administrator of BBSW, has taken steps to improve the robustness and longevity of BBSW as the domestic floating rate benchmark rate.*

*The ASF has undertaken this consultation and asked PwC to produce a report based on industry views on the appropriateness of the continued use of 1-month BBSW for AUD securitisations and possible alternative risk-free rates that may better suit the global environment in the future. In addition, the ASF seeks to assist the industry adopt more comprehensive and consistent fallback language and risk disclosure in Information Memorandums.*

*We are very pleased with the large and representative number of responses we have received to this consultation and believe the report provides an important basis upon which industry discussion and planning for the evolution of the Australian securitisation market can be conducted.*

***Chris Dalton,***
*Chief Executive of the Australian Securitisation Forum*

# 2. Recent developments in interest rate benchmarks

The ASF questionnaire, released in September 2019, was accompanied by an explanatory paper that provided background information on interest rate benchmark changes. This paper is included in the Appendix to this report.

Since the launch of the questionnaire, there have been some developments in the global and Australian markets. As markets to replace LIBOR continue to develop this will very likely have an impact on the AUD securitisation markets.

The Sydney ISDA conference in October 2019 looked at the impending changes to IBOR benchmarks. Christopher Kent (Assistant Governor of RBA) highlighted the need to address benchmark changes with particular reference to LIBOR. The discontinuation of BBSW was also discussed by panel members focusing on the need for there to be robust fallback arrangements.

The UK markets continue to make progress with the replacement of LIBOR with SONIA. Several legacy debt issues have been successfully switched to SONIA in October (Lloyds and Nationwide). However, this only represents a small proportion of the outstanding debt.

The US markets are still developing SOFR. On 17 September 2019, SOFR had a significant spike (from 2.2% to 5.25%) due to liquidity issues on the day. This has attracted much debate and continues to be a concern for participants. The ARRC (Alternative Reference Rates Committee) in the US is focused on developing SOFR and its use as a replacement for LIBOR.

ISDA published the results of the pre-cessation triggers for fallbacks on 21 October 2019. This consultation assessed whether market participants favoured using a regulatory (or other) announcement that a benchmark should cease to be 'representative' to trigger fallbacks. The consultation had no clear results so discussion will continue on this point.

ISDA launched a consultation on 18 September 2019 to gather market views on the final parameters for the spread calculation that could be used for fallbacks. The spread is described as the difference between the compounded Risk Free Rate and LIBOR for that period. Results are expected in early December and will be included in the changes to the ISDA 2006 Definitions.

The Term Risk Free Rates (RFRs) have also seen some advances over September and October. Benchmark working groups in the UK, EUR and Japan have all shown their intention to support development of Term RFRs. The UK and EUR groups have published the proposals received from potential administrators while Japan has commenced a 'Request for Proposal' process.

The US and Australia are also making progress in the development of Term RFRs.
The global markets continue to move forward with LIBOR replacement. The domestic AUD market continues to monitor the global developments.

# 3. Scope and approach to the survey

The ASF conducted this survey in October 2019 to achieve two principal objectives:

- To further raise awareness amongst industry participants of developments in global and Australian interest rate benchmark reform the impacts on 1-month BBSW which is widely used as an interest rate benchmark in Australian securitisation transactions; and
- To solicit input into how the ASF should support the industry in addressing the changing environment globally for the use of benchmarks.

Participants in or connected with the Australian securitisation industry in Australia and offshore were invited to provide their views on the industry's future use of interest rate benchmarks by completing an online questionnaire.

The questionnaire had a number of opportunities for comment by respondents. In many cases, the comments received were valuable in explaining the results of the survey. In addition, fourteen interviews were held with a sample of respondents to gain further insight into the responses and the comments they provided in the questionnaire.

Participants were asked to consider both the short-term and long-term requirements of the Australian securitisation industry. Specifically, they were asked to consider some of the alternatives to the status quo, which could take time and/or effort to implement but might offer a better long-term outcome for the industry, particularly given the developments that are underway globally. Key areas covered by the survey were:

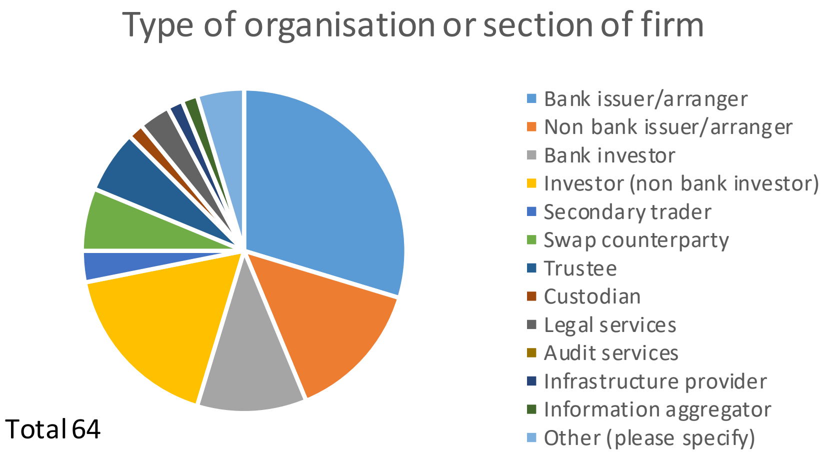
- The appropriateness of the current use of 1-month BBSW in AUD securitisations over the short-term (12 months) and longer-term (greater than 12 months);
- The use of alternative interest rate benchmarks;
- The use of more standardised fallback language in documentation; and
- The use of more standardised risk disclosure language.

The results of the questionnaire and interviews have been consolidated and are presented in this report. Any comments or quotes referred to in this report, whether made in written or verbal form, have been anonymised and/or presented in a consolidated form.

# 4. Summary of questionnaire respondents

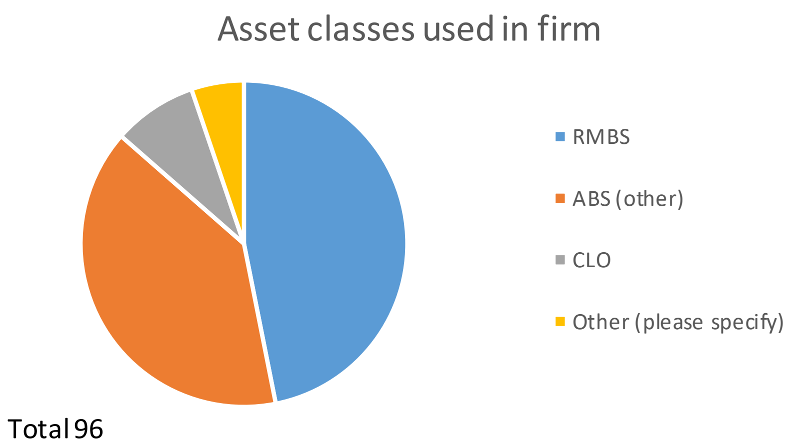
The questionnaire was completed by 51 persons representing 49 separate firms.
Two firms completed the survey twice with different business divisions of those firms preferring to have separate submissions based on the potential for different responses to questions.

**Chart 4.1 : Types of respondent - Respondents identified with 64 types of activity, with a number of firms selecting two or more activities within the same firm.**



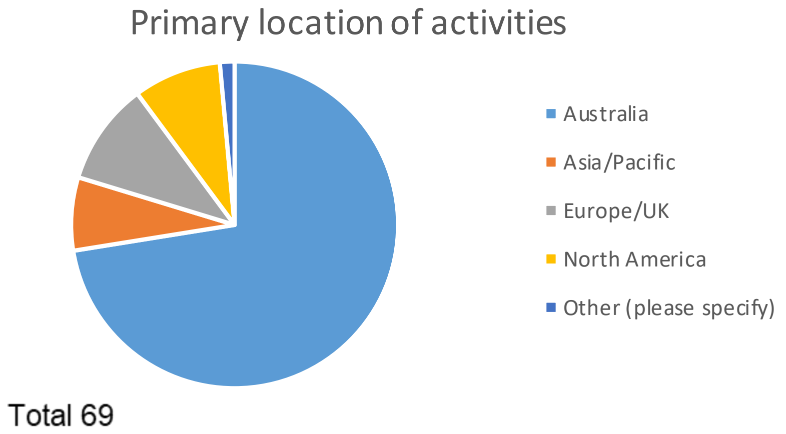

Issuers (bank and non-bank) submitted the most responses (44%) with investors second (28%). Each of the categories of organisations identified by the ASF (in the above chart) had at least one response.

**Chart 4.2 : Asset classes - Asset classes covered by the respondent firms. Most firms responded that they are involved with more than one asset class.**




The RMBS (47%) and ABS (40%) asset classes were the most represented across the respondents. The 'other' classes of assets included by respondents were small ticket CMBS, covered bonds, syndicated loans and private debt.

**Chart 4.3 : Primary location of the respondents – Some firms chose more than one location.**




Respondents were mainly located in Australia (72%) with other regions in the 6 – 10% range each.

# 5. Summary of preferences

Respondents were asked to rank their preferences across four options for an interest rate benchmark for AUD securitisations:

- 1-month BBSW;
- 3-month BBSW;
- Backward-looking AONIA; and
- Other.

**Chart 5.1 : Preferences for each option. Each bar in the chart is broken into the number of responses for 1 – 4 with 1 being the most preferred.**

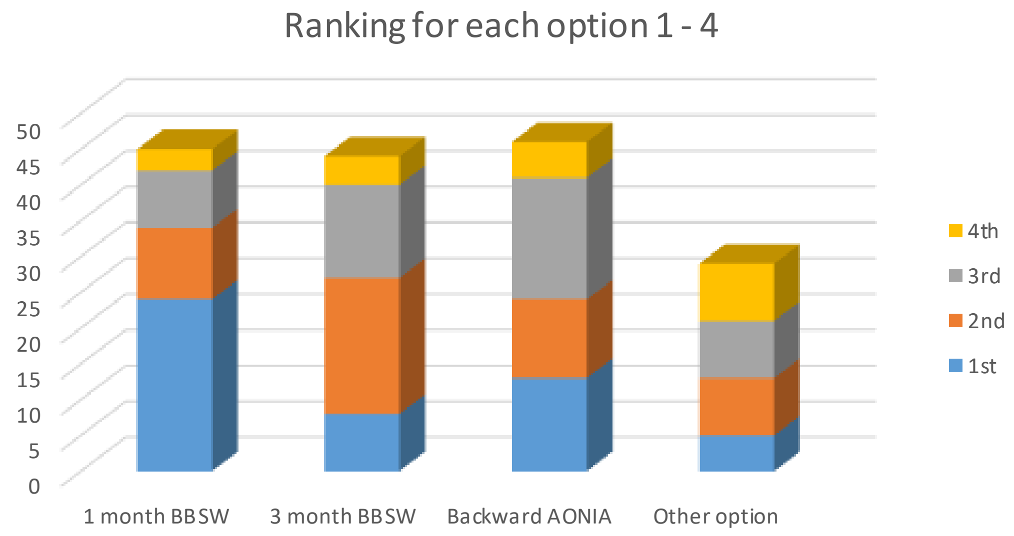



**Table 5.1 : Percentage per rank per option**

| Option | 1st preference | 2nd preference | 3rd preference | 4th preference |
|---|---|---|---|---|
| 1-month BBSW | 48% | 20% | 16% | 6% |
| 3-month BBSW | 16% | 38% | 26% | 8% |
| Backward AONIA | 26% | 22% | 34% | 10% |
| Other option | 10% | 16% | 16% | 16% |

Respondents have shown:

- 1-month BBSW as the highest first preference (48%);
- Backward looking AONIA (26%) as the second highest first preference;
- 3-month BBSW (38%) as the highest second preference; and
- Forward-looking Term AONIA was the dominant 'Other option'.

## Survey comments

There was strong support for a 1-month period benchmark as being best suited to securitisations due to the receivable's monthly collections. This is reflected in the relative popularity of 1-month BBSW and backward-looking AONIA because they can be relied on to match the monthly payments of securitised assets.

The positive reaction of rating agency to issuers matching receivables (assets) with income distributions (liabilities) was also mentioned in several interviews, further supporting the 1-month payment schedule.

The survey asked respondents to comment on what may encourage them to use an alternative to 1-month BBSW as an interest rate benchmark for AUD securitisations. Responses included:

- The adoption of a new benchmark by both issuers and investors;
- The role of the ASF in promoting a discussion between issuers and investors on alternatives;
- The role of government and semi-government issuers and investors in creating liquidity in alternatives;
- Changes to the preferences of global market participants based on LIBOR cessation (i.e. the need for AUD to remain competitive); and
- The development of market-accepted alternative.

Several interviewed firms were clear that remaining similar to or following larger, global securitisation markets would maintain the interest of the global investors in AUD securitisations. Any divergence from global standards could deter current investors and discourage new investors.

A further breakdown of the data showed some differences in the responses from bank/non-bank issuers and investors (representing the largest component of respondents). The following tables show the percentages of the ranking (1 - 4) for the alternative benchmarks given by each major type of respondent.

**Table 5.2 : Ranking of 1-month BBSW by category of respondent**

| Preference Rank | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| 1 | 53% | 44% | 14% | 55% |
| 2 | 21% | 22% | 43% | 9% |
| 3 | 11% | 11% | 29% | 18% |
| 4 | 5% | 0% | 0% | 9% |

Three of the four respondent types had a clear preference for 1-month BBSW with the exception being the bank investors who preferred to rank 1-month BBSW second or third. Comments from respondents largely echoed the clear preference for the standing 1-month BBSW benchmark, which is currently in wide use and accepted by issuers and investors. For example, respondents made the following comments:

> *'Prefer to stay with 1-month BBSW until a broad consensus is reached on one-step change to market.'*

*'Current regulatory uncertainty is a concern; however this benchmark is the status quo, liked by investors, and will not require significant system changes solely for the securitisation market.'*

Equally, some respondents acknowledged the longer-term concerns around maintaining the 1-month BBSW despite the challenges associated with shifting to an alternative benchmark.

**Table 5.3 : Ranking of 3-month BBSW by category of respondent**

| Preference Rank | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| 1 | 5% | 33% | 29% | 18% |
| 2 | 47% | 11% | 14% | 36% |
| 3 | 26% | 22% | 29% | 18% |
| 4 | 11% | 11% | 29% | 9% |

Non-bank issuers and bank investors showed interest in 3-month BBSW. Comments included that the relative robustness of 3-month BBSW (compared with 1-month BBSW) would be a possible better match with the funding arrangements for the bank investors.

Several respondents commented that the 3-month payment schedule would be difficult to manage by creating a mismatch between receivables and distributions that would need to be managed. For example, respondents made the following comments:

*'Negative carry in collections account will be punitive to non-Major Bank issuers, including xxx (our firm) and increase risk of ADIs becoming net payers under basis swap (capital deduction).'*

*'Some investors prefer 1-month payments for cashflow management and hedging and aligned to monthly payments on mortgages.'*

*'…reasonably deep and liquid alternative market, reflects an appropriate floating credit spread, some issues with alignment between repayments of the underlying assets and amortisation of the notes, may lead to higher transaction costs due to spread differential between 1month and 3month tenors.'*

*'At least has term structure.'*

Respondents generally saw challenges in using a 3-month period benchmark but still preferred the benefit of a term structure compared with backward-looking AONIA.

**Table 5.4 : Ranking of backward-looking, compounded AONIA by category of respondent**

| Preference Rank | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| 1 | 32% | 11% | 43% | 0% |
| 2 | 16% | 33% | 14% | 9% |
| 3 | 42% | 22% | 29% | 18% |
| 4 | 5% | 11% | 14% | 9% |

Respondents were varied in their support for a backward-looking compounded benchmark like AONIA. Banks (issuers and investors) ranked AONIA comparable to 1-month BBSW citing the benefit of good alignment with developing global practices in UK and USA and the performance of RMBS receivables.

However, comments did highlight the relative difficulty of using a compounded rate that is only known at the end of the relevant period in current systems and processes. IT systems were seen as challenging to amend (especially for non-banks), as were also the accrual and valuation processes. In several interviews, concerns were voiced about daily posting of unit prices for funds investing in AUD securitisations and that this could present challenges given that the next coupon is not known until the end of the current period.

Comments were generally supportive of AONIA as an option but did highlight the operational challenges with it, for example:

> *'Compounded AONIA is deemed a significant approved benchmark by ASIC and is based on liquid interbank market. AONIA is also aligned to offshore reference rate developments such as SONIA.'*
>
> *'Materially challenging to implement.'*
>
> *'The unavailability of this rate at the start of an interest period could present serious administrative difficulties in transactions where transaction participants currently forecast payments based on known interest accruals.'*
>
> *'…problems with investor acceptance.'*

In summary, respondents did see the value of backward-looking AONIA as a robust alternative to 1-month BBSW but were generally concerned about operational challenges for investors and issuers.

**Table 5.5 : Ranking of 'Other' by category of respondent**

| Preference Rank | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| 1 | 11% | 11% | 14% | 18% |
| 2 | 16% | 22% | 29% | 9% |
| 3 | 5% | 0% | 0% | 18% |
| 4 | 11% | 11% | 0% | 27% |

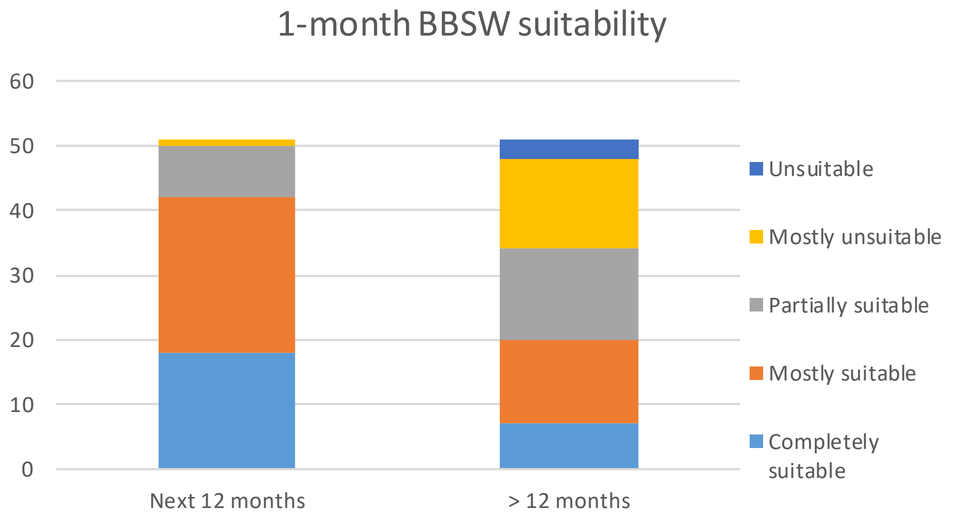
A number of respondents supported the forward-looking Term AONIA as an acceptable alternative. One respondent suggested a secured overnight rate (like SOFR in USA) while another mentioned the AOFM T-note index as a potential alternative. Individual comments included:

> *'Forward looking term AONIA as opposed to backward looking provides greater certainty of cashflows for investors and would require less work on building out system infrastructure.'*
>
> *'Term AONIA' (mentioned 10 times)'*
>
> *'AOFM T-note index provided issuance volumes are large enough and maintained. Also a forward looking OIS (OTC or listed future) product that provides a term structure.'*

# 6. Ongoing suitability of 1-month BBSW

Respondents were asked about the ongoing suitability of 1-month BBSW over different timeframes.

**Chart 6.1 : Respondent views on the suitability of 1-month BBSW over different timeframes**




They generally agreed that 1-month BBSW is mostly suitable (47%) or completely suitable (35%) for the next 12 months. However, for longer than 12 months the percentages shift towards mostly suitable (27%), partially suitable (25%) and mostly unsuitable (25%) with completely suitable (14%) showing a significant fall. This shift in the perceived suitability of 1-month BBSW over the course of next year is very clear from the chart above.

## Survey comments

The questions in this section of the questionnaire attracted significant comment from respondents, which can be summarised as:

- 1-month BBSW is accepted now with systems and processes well established to manage cashflows based on this benchmark;
- 1-month BBSW is perceived as acceptably robust for the next 12 months, but there are concerns about the longer-term viability of 1-month BBSW due to falling volumes of issued NCDs for trading leading to fewer trades to set this tenor of BBSW;
- Longer-term trends in global markets are towards cash-based benchmarks which could (and likely will) draw investors away from BBSW;
- These trends away from 1-month BBSW will likely become more pronounced in 12 months; and
- The ASF and regulatory bodies could play an important role in promoting a discussion on what the next steps could be to establish an alternative to 1- month BBSW that the market could adopt.

Responses were generally supportive of (the use of) 1-month BBSW for the next 12 months but also pointed out the need to change with global trends and the falling number of trades used to set 1-month BBSW. Almost all respondents provided an individual comment to these questions, for example:

> *'While we see no issues with the continuing use of 1-month BBSW, the RBA has called out that users of it as a benchmark should prepare to move toward an alternative benchmark, therefore we cannot ignore this issue. Further, we are seeing globally that nominated alternatives to current benchmarks are generally risk free rates.'*

> *'If 1m BBSW trade volumes continue to decline then it will not be a sufficiently liquid base rate instrument to serve as a benchmark rate. The overnight cash rate or AONIA would be more suitable.'*

> *'The speed of adoption of overnight rate based indices has been rapid in jurisdictions where encouraged, especially as the market sees the emergence of the 30 day look back/5 day calculation as a standard. The fear was being "stranded" in a non-standard index calculation format. This has given way to a fear of being stranded in an obsolete index beyond the mandatory submission date.'*

> *'Given the complexity involved, it is unrealistic to adopt an alternative measure within a 12 month timeframe. The adoption any change needs to be in line with global changes. However, in the medium to longer term, the lack of liquidity of the 1-month BBSW makes it unsuitable as a securitisation floating rate benchmark.'*

> *'We expect liquidity in the one month to worsen and liquidity in risk free benchmarks to increase as they are more widely adopted worldwide.'*

> *'It is currently market standard, so it is difficult to see it deviate much from market in the short term.'*

> *'I think it will take some time to move away from 1 month BBSW but with my limited knowledge/understanding it appears inevitable.'*

While there is support for 1-month BBSW in the short term, many responses highlighted the global transition to Risk Free Rates (including the potential impact on BBSW) and concerns about the robustness of 1-month BBSW over the next one or two years.

**Table 6.1 : Views on the suitability of use of 1-month BBSW by category of respondent within the next 12 months**

| Response | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| Unsuitable | 0% | 0% | 0% | 0% |
| Mostly unsuitable | 0% | 0% | 0% | 0% |
| Partially suitable | 16% | 0% | 14% | 18% |
| Mostly suitable | 42% | 78% | 57% | 36% |
| Completely suitable | 42% | 22% | 29% | 45% |

**Table 6.2 : Views on the suitability of use of 1-month BBSW by category of respondent beyond the next 12 months**

| Response | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| Unsuitable | 5% | 0% | 0% | 9% |
| Mostly unsuitable | 32% | 11% | 43% | 27% |
| Partially suitable | 26% | 33% | 43% | 27% |
| Mostly suitable | 21% | 33% | 14% | 27% |
| Completely suitable | 16% | 22% | 0% | 9% |

The shift in the level of suitability is evident in all four types of respondent. Over the next 12 months, no respondent from these types saw 1-month BBSW as either 'Unsuitable' or "Mostly Unsuitable'. However, beyond 12 months, all types had shifted significantly towards 'Partially suitable', 'Mostly Unsuitable' and 'Unsuitable'.

Comments were very widespread and showed variation within the types above. For example, the Bank issuer/arranger sector commented:

> *'Despite the lower volume of transactions, we believe that the 1m BBSW is still priced based on observable trades.'*
>
> *'1-month BBSW not completely suitable due to fragility re underlying transactions but serves purpose as widely accepted benchmark for now. Regulators seem to be motivated to move market off 1-month BBSW without stating it explicitly causing some uncertainty for some market participants whilst not firm enough to overcome inertia from others. Market can only move off 1-month BBSW when an alternative rate becomes widely used and with regulatory endorsement'*

There was a similar diversity of opinion within other categories of respondent.

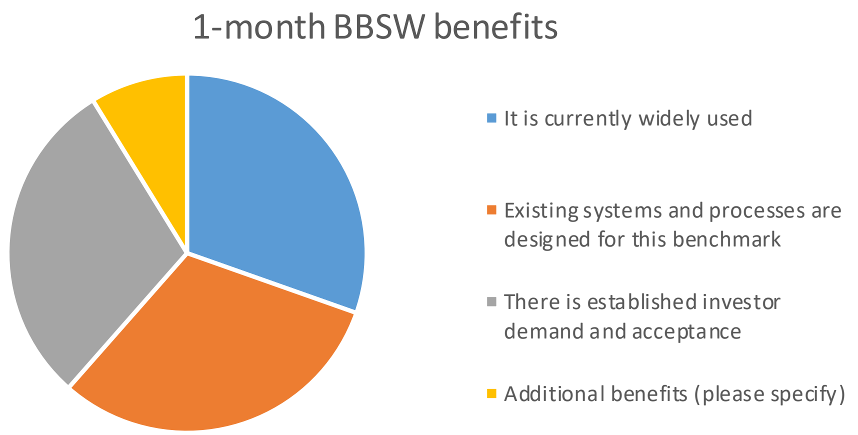
# 7. Summary of benefits and challenges associated with current benchmark alternatives

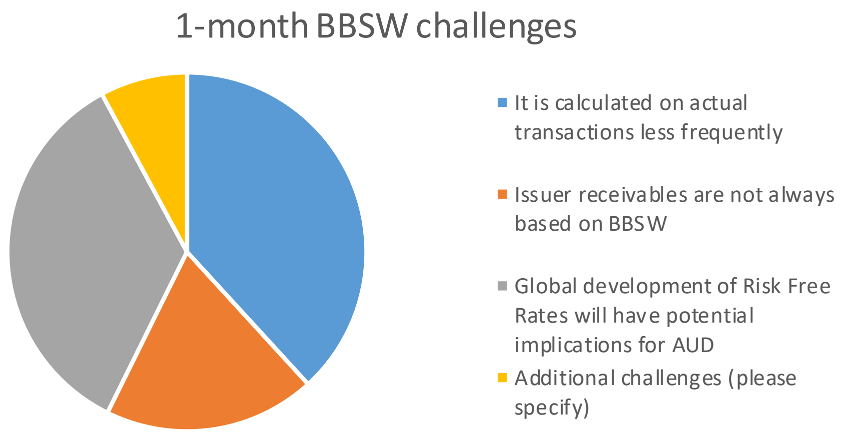
This section looks at the relative benefits and challenges of using either the 1-month BBSW, 3-month BBSW or backward-looking compounded AONIA as the interest rate benchmark.

### 1-month BBSW

The charts below summarise the benefits and challenges highlighted by respondents when considering the status quo option of continuing to use 1-month BBSW:

**Chart 7.1 : Benefits and challenges of continuing to use 1-month BBSW**




Additional benefits included alignment with the periodicity of underlying cashflows, current investor preferences and the rate set at the start of the period to give certainty about returns. Additional challenges highlighted the regulatory concerns about the robustness of 1-month BBSW and the basis swap issues where receivables are often based on cash while the issuance is linked to BBSW leading to the potential for unusual payment outcomes.

## Survey comments

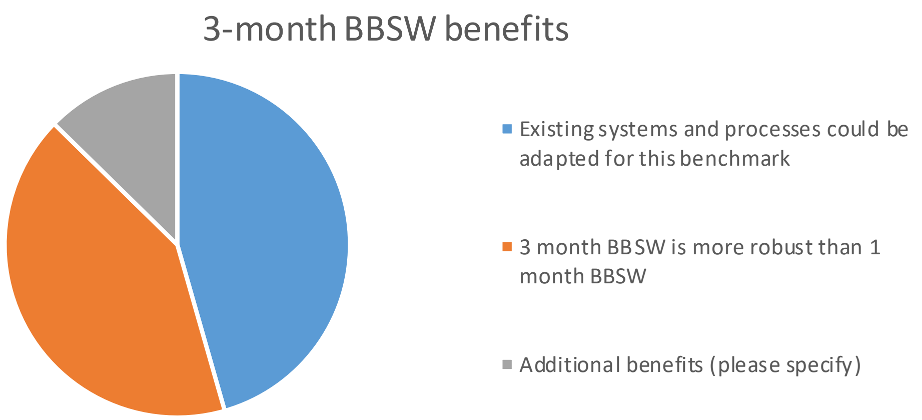
Comments in this section were quite varied and included:

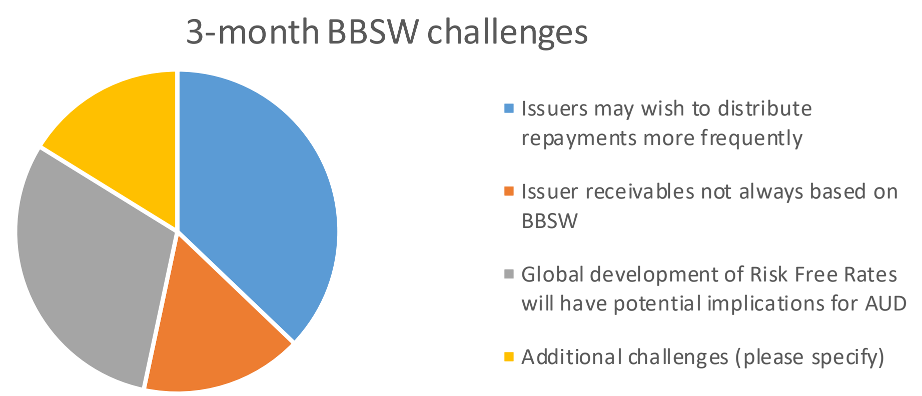
- 1-month BBSW is based on observable transactions and has good oversight which was countered by several observations that less than 50% of days 1-month BBSW sets from trades;
- A diversity in comments on the benchmark for RMBS receivables (cash or BBSW). Some argued for a cash securitisation benchmark (to align with RMBS) while others were in favour of 1-month BBSW (to similarly align with RMBS cashflows);
- The basis risk between cash-based receivables and 1-month BBSW can create problems for issuers especially from a ratings perspective; and
- The issues raised by regulators about the ongoing use of 1-month BBSW may create a challenge for the longer-term use of this benchmark.

## 3-month BBSW

The charts below summarise the benefits and challenges highlighted by respondents when considering 3-month BBSW as an alternative benchmark:

**Chart 7.2 : Benefits and challenges of using 3-month BBSW**



Additional benefits included alignment with the internal benchmarks often used by issuers (i.e. 3-month BBSW) and the relative ease of incorporating into current systems. Additional challenges focused on the mismatch between the receivable periodicity (monthly) and the 3 months for issuance creating additional basis risk. Finally, there was also some concern that 3-month BBSW, while more robust than 1-month BBSW, was still potentially problematic in the long term.

### Survey comments

Comments in this section included:

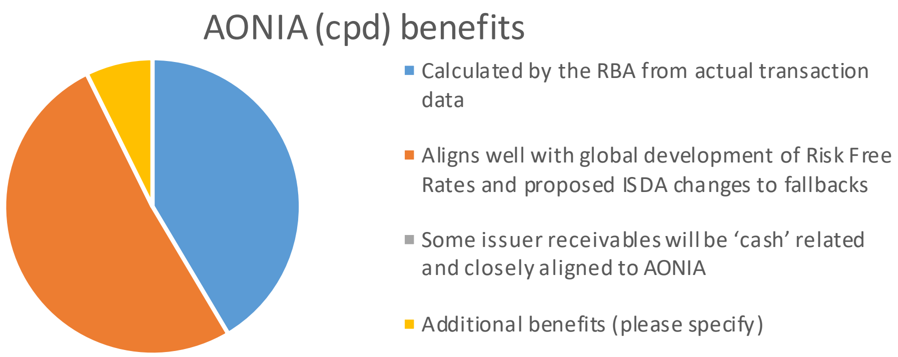
- Costs to update systems and processes to accept the longer periodicity could be a challenge;
- Moving away from the preferred 1-month periodicity could create challenges for issuers in cash management and rating agency reviews; and
- Challenges in moving investors to a different benchmark.

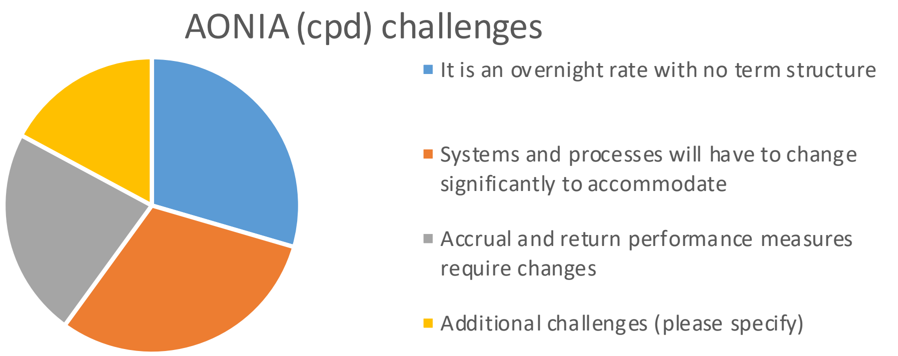
Several banks also commented that 3-month BBSW was a common internal funding benchmark and aligning securitisations to 3-month BBSW could be a benefit by reducing basis risk.

### AONIA – Compounded daily in arrears (cpd)

The charts below summarise the benefits and challenges highlighted by respondents when considering AONIA on a daily compounded in arrears basis as an alternative benchmark:

**Chart 7.3 : Benefits and challenges of using AONIA (cpd)**



Additional benefits included alignment with the periodicity of receivable (i.e. 1 month) and global developments in risk free rates in other currencies like GBP and USD. Additional challenges focused on the expected difficulties of incorporating compounded AONIA calculation changes into current systems, the backward-looking feature (where the cashflows are not known until the end of the period) and changing performance and return parameters for funds.

### Survey comments

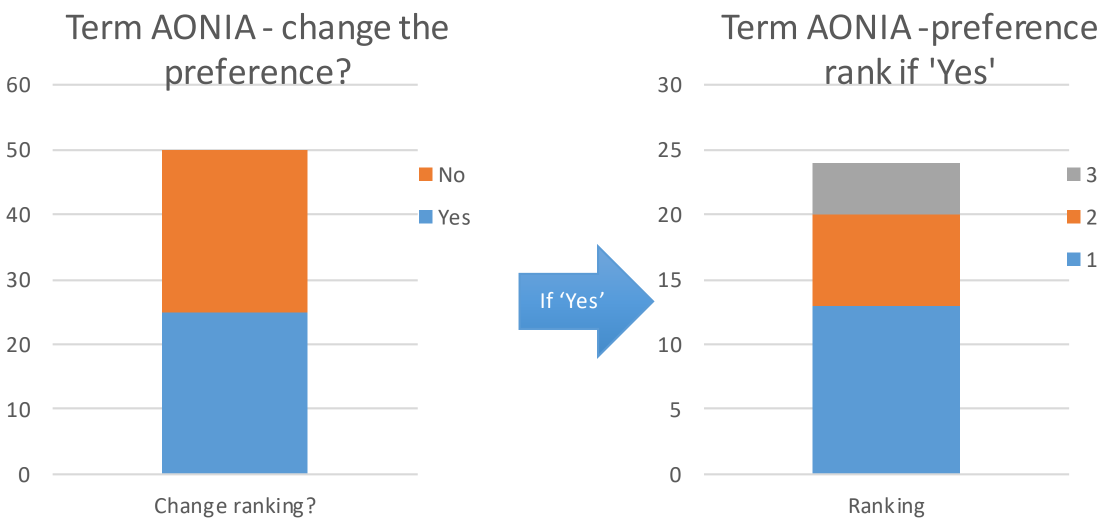
Comments in this section demonstrated that respondents were quite varied in their level of understanding of AONIA. Comments included:

- Systems and processes (especially for smaller firms) would be challenging to adapt to a backward-looking benchmark;
- Many global markets are adopting cash-based benchmarks which would support the use of AONIA in the future as long as AONIA is similar to the global benchmarks;
- The calculation of unit prices between coupons may be challenging if the next coupon is not known for AONIA;
- Some responses were supportive of the lower volatility of AONIA (compared with BBSW) while others saw this as a challenge;
- The lack of a credit component to AONIA represents a shift of performance returns which would need to be manages with trustees; and
- Interviewees commented several times that changing the fundamental benchmark from BBSW to cash could take time to explain to trustees as well as adjust performance targets.

# 8. Potential future benchmark alternatives - Term AONIA

The survey also introduced the option of using Term AONIA. This option, while still in development, addresses a number of challenges with using a backward-looking, compounded AONIA. Respondents were split 50:50 on whether they would use a Term AONIA if it were available. Further exploration of this issue in interviews did confirm that there was some confusion over the question and that the responses may have reflected this confusion.

**Chart 8.1 : Would respondents change their alternative benchmark preferences if a Term AONIA were available**




For those who did indicate that they would change the ranking if a Term AONIA were available in the near future, 54% indicated that they would have placed Term AONIA as their first choice of benchmark.

**Table 8.1 : Yes/No split**

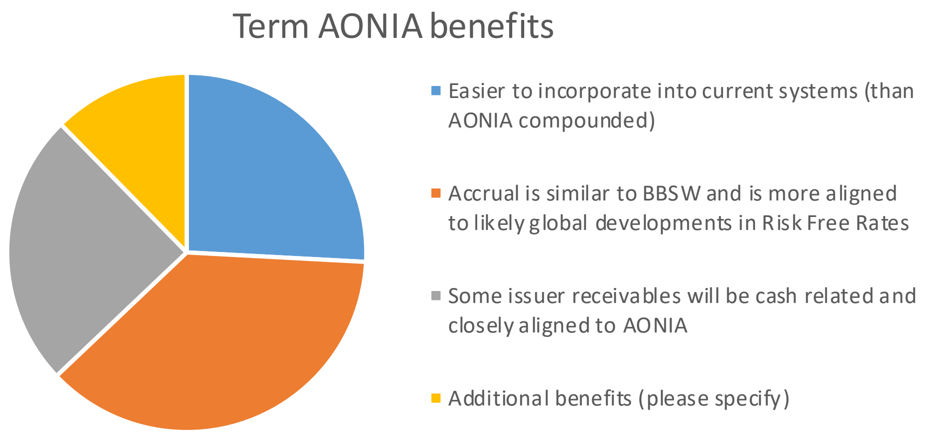
| Response | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| Yes | 47% | 33% | 43% | 60% |
| No | 53% | 67% | 57% | 40% |

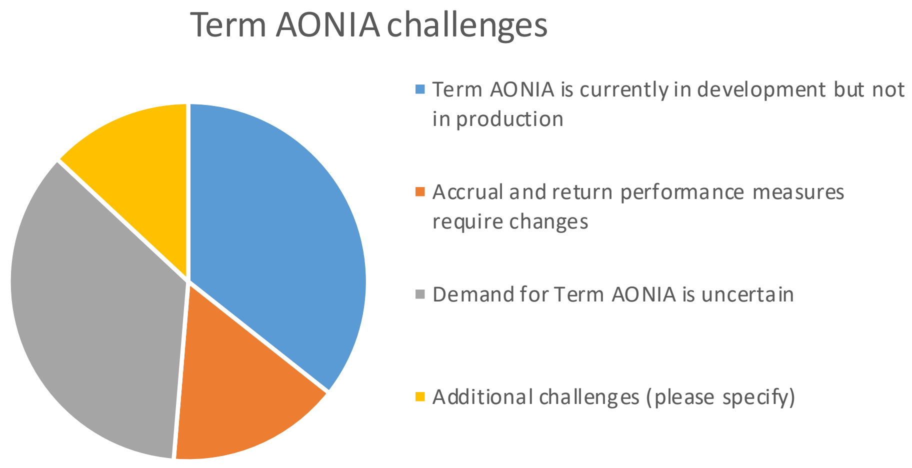
**Table 8.2 : Ranking of Term AONIA as an alternative benchmark if it were available for those respondents who indicated its availability would change their original preferences**

| Rank | Bank issuer/arranger | Non-bank issuer/arranger | Bank investor | Investor (non-bank investor) |
|---|---|---|---|---|
| 1 | 44% | 67% | 67% | 33% |
| 2 | 22% | 33% | 33% | 50% |
| 3 | 33% | 0% | 0% | 17% |

The four types of participant were generally aligned in their approach to Term AONIA. The Yes/No split was around 50:50 across all four while the ranking (if they answered 'Yes') generally had term AONIA ranked 1 or 2.

**Chart 8.2 : Term AONIA benefits and challenges**




The additional benefits cited were:

- Alignment with the periodicity of receivable (i.e. 1-month);
- Global developments in risk free rates in other currencies like GBP and USD; and
- The forward-looking nature of Term AONIA and particularly the relative ease of incorporating into current processes compared with 3-month BBSW or backward-looking, compounded AONIA.

Additional challenges focused on those to establish a new benchmark with investors and trustees. This may take some time to fully develop.

**Survey comments**

Comments in this section, like those for backward-looking AONIA, demonstrated variability in understanding. Since term AONIA is still in development, the question was presented as 'assuming Term AONIA is available'.

Some respondents, when interviewed, did provide a different view based on further information and consideration of the question. The comments presented here reflect the interviews where appropriate as well as those in the survey. They included:

- Many responses found a Term AONIA that is set at the start of the period (like a BBSW rate) would be an easier transition compared with backward-looking AONIA;
- Systems and processes could be easier to adapt to Term AONIA compared with AONIA;
- Several responses suggested a 'credit' adjustment could be attractive to replicate the BBSW;
- Regulatory support (via licensing) which is essential for the uptake of a benchmark may be difficult to achieve for Term AONIA;
- Term AONIA is still in development and the respondents need to see the actual benchmark before committing; and
- Investors and issuers will need information and education before moving to Term AONIA.

Comments on the benefits of a Term AONIA included:

> *'Will allow market participants to know the coupon they can expect from the beginning of the accrual period.'*
>
> *'In line with likely path for global benchmarks for cash products.'*
>
> *'Is unit pricing friendly for a portfolio and regulatory friendly for fair value pricing.'*

Comments on the challenges included:

> *'Investor education and confidence will be required.'*
>
> *'Term AONIA only useful if term RFR are developed, and widely adopted, in offshore securitisation markets.'*
>
> *'Generally, development of risk-free benchmarks globally is uncertain as is regulatory acceptance of these as a suitable replacement for securitised products.'*

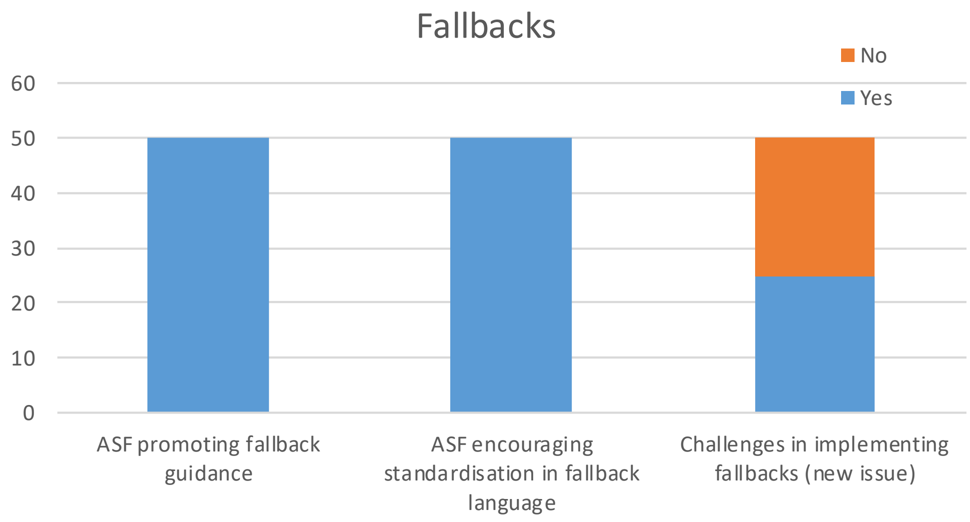
Overall, respondents were generally supportive of the Term AONIA but had reservations about the development and the regulatory approval for its use. This is summed up in the following comment:

> *'Term AONIA would seem to be the better calculation but we have not investigated or formed an opinion on this.'*

# 9. Fallbacks

The survey also asked a number of questions about the development of fallback language. The questions focused on the role of the ASF and whether a high degree of consistency would assist the AUD securitisation industry to adopt more robust fallback arrangements.

**Chart 9.1 : Number of respondents answering "Yes / No" questions in respect of the ASF providing further guidance on fallback language and whether there were challenges to implementing these**




Respondents all agreed that there is a role for the ASF to promote standardisation and provide guidance for fallback language in AUD securitisations. Further comments emphasised the need to keep the fallback language aligned with global practice as far as possible.

## Survey comments

Comments in this section were generally very similar and supportive of the ASF developing and promoting standardisation of fallback language that may be used in AUD securitisations. They included:

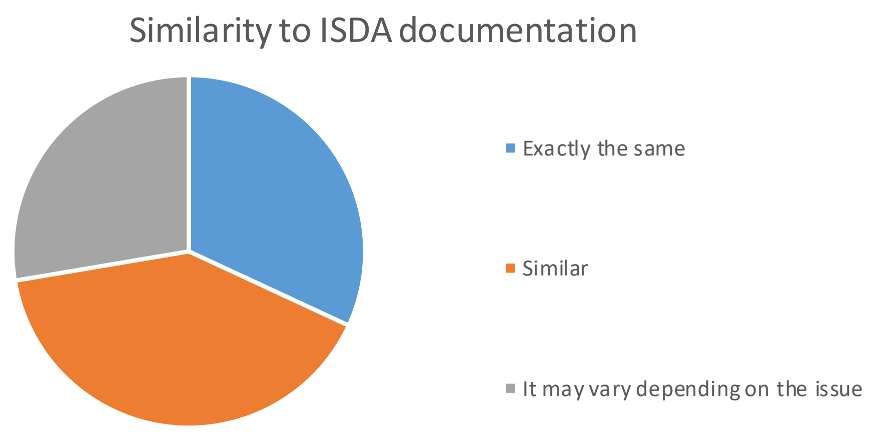
- Guidance in fallback language that could be used in AUD securitisations could encourage consistency across issues and lower legal costs for issuers and investors;
- Many mentioned the ISDA work on fallbacks (see below in 9.2) and encouraged a close alignment with the ISDA documentation;
- Some comments noted that debt fallback language and securitisation fallback language should stay aligned and may differ slightly to ISDA;
- The general view that consistency with global standards is strongly preferred;
- Adopting new fallback language could lead to 'orphan' issues that could be difficult to amend to newer language leading to liquidity concerns; and

- New fallback language implies that systems and processes must support any proposed fallback, and this could take time to implement.

Respondents supported the need for standardization of documentation while preferring fallback language to be guidance (rather than mandated) and be flexible enough to accommodate a range of outcomes. In addition to reiterating comments that standardization would should aide in maintaining global consistency as well as enhancing investor acceptance, some of the individual comments were:

> *'The market would benefit from ASF leading the development of fallback language best practices and following up with detailed implementation blueprints.'*
>
> *'There needs to be an emphasis on international harmonisation with any standardisation in documentation of fallback language.'*
>
> *'We would not support fallback language which did not permit the flexibility to respond to unexpected changes or developments. We suggest this be drafted as guidelines rather than a market standard.'*
>
> *'It would be critical to have significant investor participation in any such initiative. A standard is only useful if it has broad acceptance.'*
>
> *'Standardisation in documentation would be a positive for Australian RMBS transactions but the ability of different issuers and law firms deviating away from the industry endorsed language is still a possibility. Who determines what's a minor variation vs major deviation? To the extent that variations will exist, we would be interested to see repo eligibility requirements & hope that the RBA will not apply a restrictive application of these definitions.'*

**Chart 9.2 : Extent of similarity to ISDA documentation fallback language desired by respondents**




The survey responses showed that most respondents supported a close link to ISDA fallback documentation while acknowledging that there will have to be some differences to accommodate specific requirements.

Comments reflected this need for flexibility while generally supporting a high degree of consistency.

Also, comments reflected a need for greater understanding and education of the fallback language and how this can be included in AUD securitisations.

For example, supporting alignment with ISDA language:

> *'If securitisation bond fallback language does not follow swap fallback language then a mismatch will exist which will create market, operational and legal risk.'*

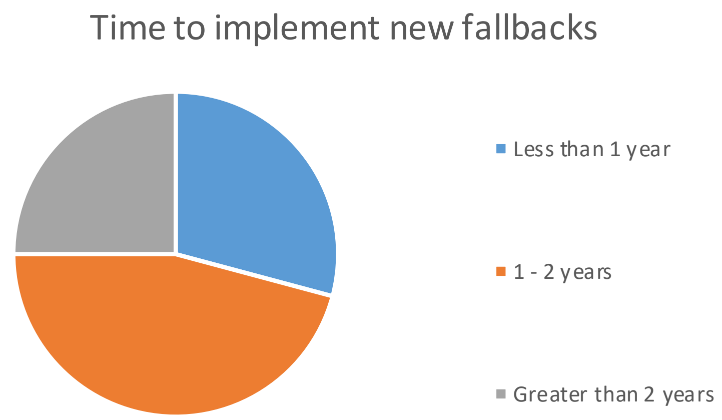
While another example allowed for some differences:

> *'It is important that the approach taken by the securitisation industry is compatible with the direction taken by ISDA.'*

Finally, one respondent suggested it was dependent on the situation:

> *'…in Securitisation warehouses, not all Warehouse Financiers are members of all of those organisations or have access to all the market data to which the Banks have access. So, the fallbacks in Australian securitisation transactions need to have the flexibility to cover smaller Warehouse Financiers who do not have access to all the same data that Banks acting as Calculation Agents in ISDA documents have. So, in this case, the simple approach (exactly match ISDA) is not going to be the right approach for all Australian Securitisation transactions.'*

**Chart 9.3 : Respondents views on the time required to implement new fallback language**

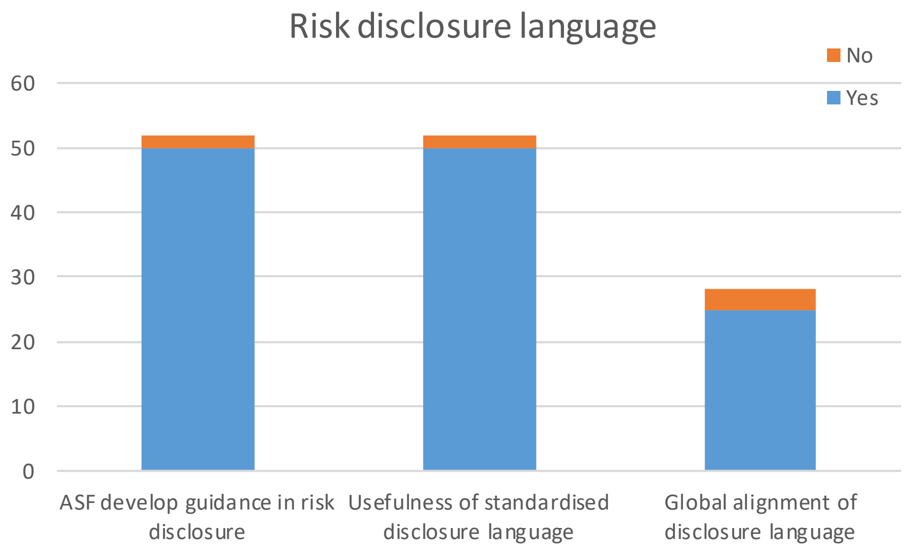



Respondents were generally of the opinion that it will take greater than 1 year to implement new fallbacks for new issues. Additionally, respondents showed a clear preference for fallback language to be exactly the same or similar to the ISDA documentation once it is finalised.

# 10. Risk disclosures

The survey questionnaire also looked at the role of the ASF and the benefits of standardised risk disclosure language in relation to benchmark changes and/or cessation.

**Chart 10.1 : Respondents views on the time required to implement new fallback language Number of respondents answering "Yes / No" questions in respect of the ASF providing further guidance on risk disclosures and the desired extent of global alignment**




Respondents were almost universally in favour of the ASF developing guidance for standardised language in risk disclosure related to the use of benchmarks in AUD securitisations. Additionally, many firms supported a close alignment to global practice in risk disclosure language.

### Survey comments

The comments received in this section were also generally supportive of the ASF developing and promoting standardisation of risk disclosure language that may be used in AUD securitisations. They included:

- Risk disclosure for benchmarks was considered important and there should be a level of consistency across issues conforming to global standards;
- Costs could be reduced if issuers adopted a more standardised approach to benchmark risk disclosure; and
- Some responses supported a role for the ASF in leading discussion and assisting with the development of benchmark risk disclosure language.

Respondents provided a number of comments on risk disclosure language. These included:

> *'Securitisation market would benefit from having standardised benchmark risk disclosure language.'*

*'Broadly speaking, the risk disclosure as presented by the ASF seems adequate however we note once again that different issuers and law firms may add to or subtract from the currently drafted contents. Any such variations should not result in a restrictive / punitive application by the RBA for repo eligibility assessments.'*

*'[The] ASF should publish a Best Practice Guideline.'*

*'It makes sense. Saves cost in individual transactions to agree this up front as an industry.'*

*'Again as a smaller issuer, I believe having standardised language would only help us.'*

*'It would reduce potential friction and help investors more quickly identify if there are structural nuances that require a non-standard disclosure.'*

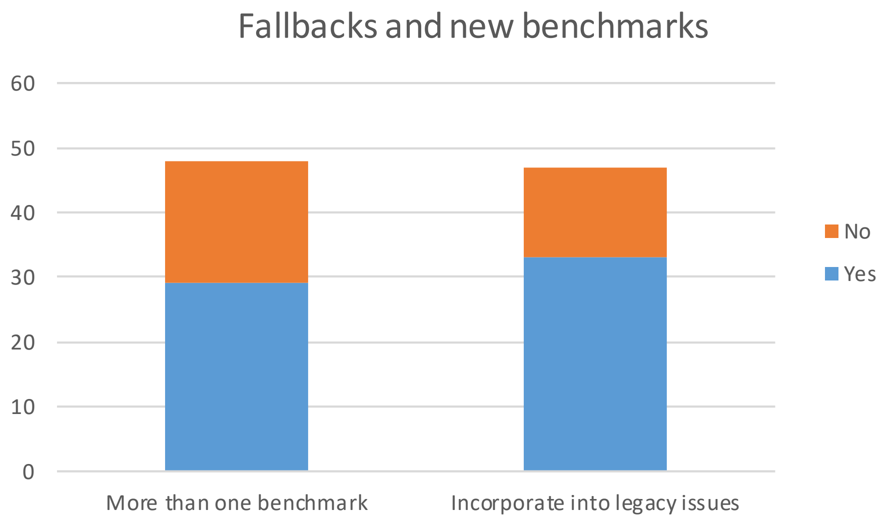
*'The Australian securitization [industry] should [not] depart too far from what [is] considered standard global practice. This would make it easier to attract offshore investors.'*

In summary, the comments again followed a theme of global consistency, cost savings for smaller issuers with a preference for guidelines.

# 11. Market practice and legacy products

The survey questioned whether the AUD securitisation market could support more than one benchmark and whether any firms would consider incorporating any changes to benchmarks and/or fallback language in legacy products.

**Chart 11.1 : Number of responses to questions in respect of whether the market can support more than one benchmark and whether changes to fallback language could be incorporated into legacy issues**




Respondents were generally split in their views over using more than one benchmark with a slight preference for only one.

### Survey comments

Comments reflected this uncertainty. In most cases responses accepted that more than one benchmark may be required but were wary of fragmentation of the market and the impacts on liquidity that it may cause.

There was a clearer preference for a single benchmark for AUD securitisations expressed in the comments than in the Yes/No answers.

The preference for one benchmark was repeated in many interviews where interviewees generally preferred to concentrate liquidity in a single benchmark. However, there was also a concern that system and process changes (if there were a change in benchmark) could take some time to implement depending on the type of benchmark.

Most respondents provided a comment on this question. Examples of individual comments included:

> *'A single benchmark would be ideal, but multiple ones could coexist.'*

> *'Technically yes. But practically this would be difficult because as a credit product we/investors compare spreads. Different benchmarks would make that challenging or the least confusing.'*

> *'In theory [the] market could adapt to more than one benchmark but the market is relatively small, especially on an international scale, so preferably [the] market doesn't become bifurcated'*

When looking at legacy issues, respondents generally preferred to incorporate changes to benchmarks and/or fallback language in existing products while recognising the challenges of doing so. These included:

> *'…system changes, investor appetite, communication…'*

> *'Agreeing what they are!'*

> *'The issues can be summarised as follows: cost - system changes; documentation, reporting.'*

# 12. The top legal and operational issues associated with changing to new benchmarks

The questionnaire also asked for comments on the top two or three legal and operational challenges involved with moving to an alternative benchmark(s). This was an open question and there were a number of key themes:

- Establishing consensus on alternative benchmarks;
- System and process changes (cost and complexity);
- Dealing with legacy transactions;
- Including fallback language in new securitisations;
- Alignment of documentation (issue and derivative hedge);
- Consistency with global change; and
- Issuer and investor alignment for any changes.

Most respondents provided two or three challenges. The themes expressed above in earlier chapters of this report encompass the majority of the responses.

# Appendix - Overview of developments in benchmark reforms

## Global developments

### *Interest rate benchmarks reform*

Work has been underway to strengthen global interest rate benchmarks for some time. Concerns about benchmarks such as LIBOR have become clear since 2012 when market abuse cases in the US and UK highlighted the need to reform benchmarks in general. This has led to a response by global regulatory bodies to improve or replace certain benchmarks such as LIBOR.

In 2013, IOSCO (the International Organization of Securities Commissions) published a report titled 'Principles for Financial Benchmarks' which detailed the basic requirements of a benchmark for use in financial contracts. These principles have led to a review of the use and suitability of benchmarks globally, including in Australia. The BIS (Bank for International Settlements) published a report in 2014 following the IOSCO report titled 'Reforming Major Interest Rate Benchmarks' which focussed on improving the robustness of LIBOR, EURIBOR and TIBOR.

This publication also introduced the concept of a 'robust' benchmark. As far as possible, a 'robust' benchmark should be based on real transactions and have an effective fallback in the case of a temporary or permanent discontinuation of the benchmark.

### *The replacement of LIBOR*

Despite efforts to improve the robustness of LIBOR, the chair of the regulator of LIBOR (UK FCA - Financial Conduct Authority) indicated in a July 2017 speech that LIBOR would effectively cease by the end of 2021.

This has led to:

- National working groups in each of the five LIBOR currencies being formed to select alternative reference rates
- All market participants involved with products and contracts that reference LIBOR to firstly assess the alternatives to LIBOR and then execute plans for its replacement in their obligations before the end of 2021.

The nominated alternatives for LIBOR are generally Risk Free Rates (RFRs) based on unsecured cash or secured repo transactions. For example, in the US the nominated alternative to USD LIBOR is SOFR (Secured Overnight Financing Rate) which is calculated from repo transactions while in the UK the nominated RFR is SONIA (Sterling Overnight Index Average) which is calculated from unsecured cash transactions collected by the Bank of England.

Among the many implications from the cessation of LIBOR, the industry is working through two key differences between LIBOR and the RFRs:

- LIBOR contains a bank credit/liquidity component whereas the RFRs do not; and
- LIBOR is a forward-looking rate published over various tenors (overnight, 1 month, 3 month and 6 month) whereas the RFRs are overnight rates only.

Therefore, for an RFR to replace LIBOR in a transaction, adjustments are required for the credit spread (typically through a margin or spread adjustment) and the tenor (typically through daily compounding over the coupon period).

At this time, neither SOFR nor SONIA have developed a forward-looking term structure (i.e. a rate that is set at the start of the period for the term, say 1 month) that replicates forward looking nature of LIBOR. The UK Working Group on Sterling Risk Free Rates issued a request for proposal for approaches to defining a Term SONIA in May 2019 which attracted 3 responses. However, at this time forward looking term RFRs are still in development and market participants have been advised (by regulators) not to delay their preparations for LIBOR transition by waiting for the development of forward-looking term rates.

*Market responses to LIBOR cessation*

The discontinuation of LIBOR as an effective benchmark by the end of 2021 has been taken very seriously by global market participants. Regulators are strongly encouraging firms to reduce or eliminate their exposures to LIBOR and have targeted 2020 as a pivotal year for the changes.

Global market participants in all products that reference LIBOR (e.g. derivatives, loans, debt and investment returns) have already commenced the necessary activities required to prepare for LIBOR cessation. These include:

- Analysing current exposures post 2021:
- Reviewing and updating documentation for new transactions and contracts;
- Preparing to make changes to existing transactions where possible; and
- Contacting other market participants in preparation for making amendments to contracts and transactions.

Although participants are making progress, much work is still to be completed before 2021. Many firms are working towards a 2020 timetable and are devoting considerable resources to the relevant projects.

*The impact on fallbacks*

ISDA are consulting on the implications of using RFRs as fallbacks in derivative contract documentation. In the context of derivatives, these alternatives are being introduced as contractual fallbacks for LIBOR with the intention of making fallbacks more robust. This replaces the fallback language generally in use now which was designed to deal with the temporary unavailability of LIBOR rather than its permanent cessation.

It is expected that other markets, apart from derivatives, will adopt the same or similar fallback approaches to those proposed by ISDA. Many industry associations have indicated their support for the ISDA while acknowledging potential differences based on the products and/or jurisdiction.

*Derivatives reform*

It is estimated that over 80% of global LIBOR notional exposures are derivatives, and therefore ISDA (International Swaps and Derivatives Association) is playing a leading role in benchmark reform.

ISDA consulted on the GBP, AUD, CHF and JPY derivatives fallback provisions in late 2018. The changes to the 2006 Swap Definitions are likely to be finalised and implemented by late 2019. These include the use of compounded AONIA (AUD Overnight Index Average) plus a spread to be used as a fallback for BBSW. This replaces the current fallbacks with a more robust and prescriptive alternative.

More recently, ISDA released the results of its consultation for USD, CAD and HKD. It expects to add revised fallbacks to the 2006 Definitions as soon as practical for these currencies.

*Securitisation developments*

Notwithstanding the challenges in replacing LIBOR, markets have started to adapt to RFR, albeit at different speeds.

In the UK, the adoption of SONIA has been faster than other currencies, in part because SONIA has been used in Sterling markets for some time. SONIA linked floating rate note issuances, including securitisation, are happening and recent transactions have been almost exclusively based on SONIA. Australian issuers have issued a covered bond referencing SONIA (ANZ) and a floating rate note referencing SONIA (CBA).

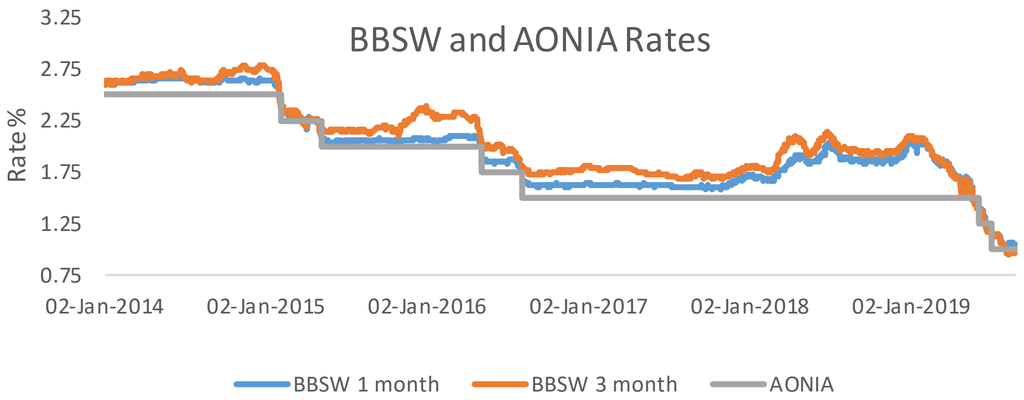
In the US, markets are still in the early stages of the adoption of SOFR. The USD national working group on benchmark reform, the Alternative Reference Rates Committee (ARRC), has finalised fallback consultations with the market for a number of cash products including securitisation. However, we are yet to see the use of SOFR in public securitisation issuance.

**Australian developments**

In Australia, legislation was introduced in 2018 for the use and administration of benchmarks and is supported by ASIC Rules. This important step brought Australia into line with global regulation and provides a very clear framework for the use of benchmarks.

ASIC have recognised two 'significant' interest rate benchmarks; BBSW and AONIA. The term 'significant' reflects ASIC's view that the given benchmark is an important component of the financial system and is covered under the licensing (or exemption) requirements. Currently, the ASX is the licensed administrator of BBSW while the RBA, as the publisher of AONIA, is exempt from holding a license.

**Chart 1: BBSW and AONIA rates over the past 5 years.**



AONIA follows the target cash rate very closely while BBSW is generally higher (in yield) than AONIA and is significantly more volatile. On some occasions, BBSW is lower than AONIA. This occurs prior to an expected change in the RBA target cash rate (lower) because BBSW is forward looking (and taking into account future, lower rates) while AONIA is daily (and would not change until the target rate changes).

In Australia, the RBA and ASIC have worked with the ASX and market participants to reform BBSW such that it is expected to remain a robust benchmark for the foreseeable future. However, they have highlighted that 1 month BBSW could be considered less robust than other tenors given a relative lack of underlying 1 month market transactions.

In August 2019, the Deputy Governor of the RBA, Guy Debelle, emphasised this issue again at the Risk Australia Conference. This speech strengthened two points: the use of the most appropriate benchmark and the need to ensure robust fallbacks are included in contracts.

> *"We have been encouraging users of Australian dollar benchmarks to be choosing the benchmark that is most appropriate for their circumstances. Sometimes it makes sense to use a credit-based benchmark, such as BBSW, particularly when banks are issuing funding instruments. However, it often makes more sense to use a risk-free benchmark, such as when governments raise funding. There has been progress on this in recent months, with the South Australian Government Financing Authority issuing the first FRN referencing the cash rate. Nevertheless, the lesson from LIBOR is that no benchmarks should be taken for granted. So while BBSW remains robust, it is prudent to have robust fallbacks in your contracts in case it were ever to cease. This is why we have been working with ISDA to strengthen the contractual fallbacks for BBSW too. Once ISDA has finalised the fallback provisions, we expect all users of BBSW to adopt them where possible. The RBA will be managing our own risks in this area by requiring new securities referencing BBSW to have robust fall-back provisions in order to be eligible in the RBA's market operations."*

*Challenges for 1 month BBSW*

Although most BBSW tenors have sufficient underlying qualifying transaction volumes to support their calculation using transactions, 1 month BBSW has some inherent structural issues. The changes in Prime Bank's issuance profile (based on regulatory liquidity requirements) has reduced the volume of 1 month securities available for trading. This will continue to impact 1 month BBSW for the foreseeable future.

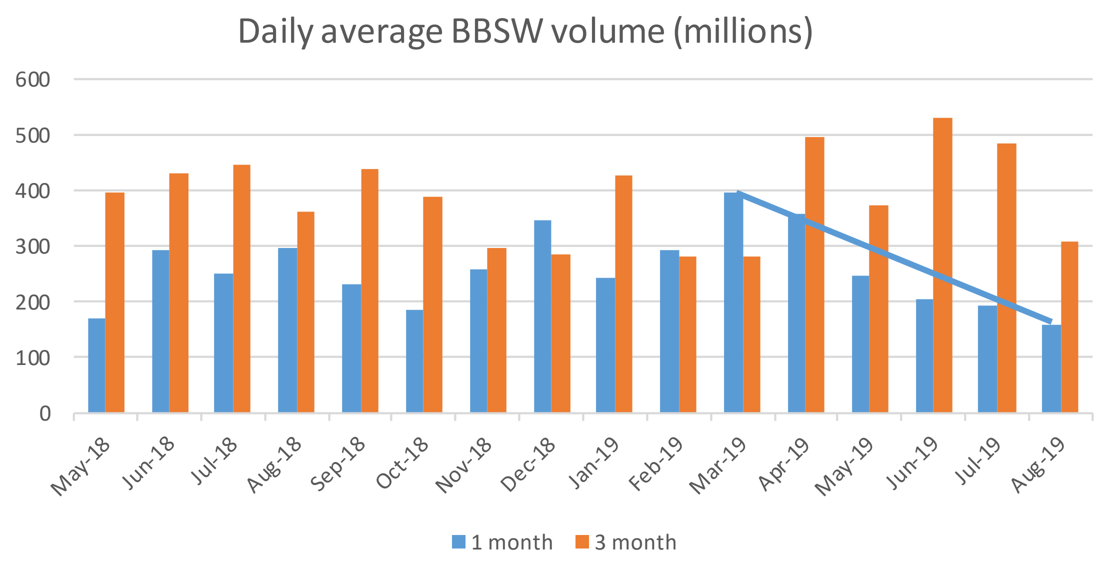
In March 2019, Assistant Governor of the RBA, Christopher Kent referred to BBSW in a speech to the KangaNews DCM Summit. He is quoted as follows:

> *"Users of BBSW should be aware that the market underpinning the 1-month tenor is not as liquid as for the 3-month and 6-month tenors. Given these issues, users of 1-month BBSW should be preparing to use alternative benchmarks. This is particularly relevant to the securitisation and derivatives markets, which frequently reference the 1-month rate."*

As shown in the chart below, in recent months, the 1 month average volumes have been falling and are now below the minimum volume ($200 million) on average to calculate 1 month BBSW from actual trades. When daily volumes are analysed, they show that the 1 month volumes only exceed the minimum trade volume threshold on 55% of days since May 2018. By comparison, the 3 month BBSW is above the 200 million for the monthly average and is above for 71% of days since May 2018.

The chart below shows the daily average turnover for 1 and 3 month BBSW since the 2018 reforms.

**Chart 2 : Average daily trading volumes to calculate BBSW**




Accordingly, because 1-month BBSW is regularly referenced in Australian securitisation markets, the RBA has encouraged market participants to consider:

- Whether BBSW is the most appropriate benchmark for their financial contracts, specifically the use of 1 month BBSW in securitisations; and
- Planning for an uncertain future by adopting more robust contractual fall backs where BBSW is referenced in financial contracts including securitisations.

## Determining a way forward

As a result of these global and local developments, the ASF is consulting with Australian securitisation market participants to assess the level of consensus around the need to change existing practices regarding the use of benchmarks (including fallback language) and which options would be the preferred basis of new ASF benchmark market practices for Australian securitisation products. Specifically, the ASF is seeking to address two fundamental issues:

- Whether, in light of global benchmark reforms, 1 month BBSW remains the most appropriate benchmark for asset-backed and mortgage-backed securities – both in the near term and over the long term; and
- How can the ASF support, and encourage, the adoption of more robust contractual fall backs, especially where BBSW is referenced in securitisation transactions.

Initiatives being considered by the ASF to support markets adapting to these reforms include:

- Developing ASF guidelines for market participants including a standard definition of BBSW, BBSW fallbacks and BBSW risk disclosures for offering documents;

- Raising awareness of the level of consensus around changing existing practices, preferred alternatives and transition challenges; and
- Advocacy with authorities for measures that would mitigate transition risks and challenges faced by the Australian securitisation industry.

Through this consultation, the ASF is seeking feedback on key specific questions regarding the use of benchmarks and fallbacks in the Australian securitisation market, namely:

- How the ASF can best support the development and encourage the adoption of more robust fallback language in securitisation;
- Whether BBSW, especially 1 month BBSW, is the most appropriate benchmark for use in the Australian securitisation market?
- If the Australian securitisation market considers changes to the underlying benchmark used in transactions, what are the options for alternate benchmarks and what are their risks and challenges?
- Is there a place for more than one benchmark (e.g. credit-based BBSW and risk-free AONIA) that can better reflect the issuer's underlying assets and investor demand?
- Whether the use of more robust, consistent interest rate benchmark fallback language that aligns with underlying receivable's fallbacks across all benchmarks is required;
- How better risk disclosure practices can be implemented; and
- How does the Australian market need to adapt to the global changes in international securitisation markets?

When responding to this survey, you may wish to consider the following risks, challenges and potential benefits:

- Ease of addressing operational impacts such as;
    a. IT systems;
    b. Accounting issues;
    c. Tax issues;
    d. Accrual processes;
    e. Trustee concerns with changes; and
    f. Impact on fallback waterfalls in the new issues.
- Benefits such as;
    a. More standardised market conventions (where appropriate);
    b. Connectivity to global changes;
    c. Fewer cost increases (for certain alternatives);
    d. Closer match of receivable cashflows to securitisation product; and
    e. Investor demand for particular returns based on alternative benchmarks.

The ASF also recognises that you may also have other considerations that are relevant to your firm: there will be opportunities to mention these throughout the questionnaire.

The following tables give descriptions of the potential benchmarks being considered in this questionnaire for use in the Australian securitisation industry. The tables are arranged in two categories: currently available benchmarks and a proposed, but not yet in existence, benchmark. These are listed in no particular order.

**Table 1 – Current potential interest rate benchmarks**

| Benchmark option | Description | Risks and Benefits for the Australian Securitisation Markets |
|---|---|---|
| 1 month BBSW | Continue with current 1 month BBSW benchmark | *Benefits*<br>• Currently widely used<br>• Systems and processes are designed for this benchmark<br>• Established investor demand and acceptance<br>*Challenges*<br>• Less based on transactions to calculate rate than previously<br>• Issuer receivables not always based on BBSW<br>• Global development of RFRs is replacing LIBOR with potential implications for AUD |
| 3 month BBSW (quarterly settlement) | Switch to quarterly settlements and use 3 month BBSW as the benchmark | *Benefits*<br>• Systems and processes could be adapted for this benchmark<br>• 3 month BBSW is more robust than 1 month BBSW<br>*Challenges*<br>• Issuers may wish to distribute repayments more frequently<br>• Issuer receivables not always based on BBSW<br>• Global development of RFRs is replacing LIBOR with potential implications for AUD |
| AONIA Backward-looking. (compounded daily, settled in arrears) | The AONIA cash rate is compounded for the period, say 1 month, and the final rate (simple interest rate equivalent) is known on the last day of that period. Settlements | *Benefits*<br>• Very robust benchmark calculated by RBA from transaction data<br>• Aligns well with proposed ISDA changes to fallbacks<br>• Some issuer receivables will be 'cash' related and closely aligned to AONIA |

| Benchmark option | Description | Risks and Benefits for the Australian Securitisation Markets |
|---|---|---|
| | are typically 2 days later. | • More aligned to likely global changes<br>*Challenges*<br>• Systems and processes will have to change significantly to accommodate<br>• Accrual and return performance measures require changes |

**Table 2 – Proposed, but not yet in existence, future interest rate benchmarks**

| | | |
|---|---|---|
| Term AONIA | The Term RFR for AUD is Term AONIA. While this rate is not available now, it under development. The rate is operationally similar to BBSW but is based on AONIA OIS trades. Term AONIA is set at the start of the period and settled at the end of the period as is the case for BBSW. | *Benefits*<br>• Easier to incorporate into current systems (than AONIA compounded)<br>• Accrual is similar to BBSW<br>• Some issuer receivables will be 'cash' related and closely aligned to AONIA<br>• More aligned to likely global changes<br>*Challenges*<br>• Term AONIA is currently in development but not in production<br>• Accrual and return performance measures require changes |

The proposed Term AONIA is being developed to address the need for a rate that is set at the start of a period and settles in arrears like BBSW. This term rate would be based on current derivative markets referencing AONIA and potentially cover tenors from 1 to 12 months.

WWW.SECURITISATION.COM.AU