# JIBAR Transition

- Monocle Research Team

As the global financial services industry finally weans itself off the London Interbank Offered Rate (LIBOR), South Africa's financial industry is set to embark on its own reform. The country will transition from the Johannesburg Interbank Average Rate (JIBAR) to its own risk-free reference rate – the **South African Overnight Index Average** (ZARONIA).

For South African financial institutions, the last few years of LIBOR transition will no doubt have been an insightful undertaking, with operational and financial impacts across investment banking, global markets and treasury. JIBAR transition will follow a similar path, however, banks will need to account for tens of thousands of JIBAR deals, rather than a few hundred LIBOR-linked deals – **an increase in volume that comes with its own complexities.**

**The SARB found JIBAR to exhibit similar weaknesses to those found in the design of other international IBORs, such as vulnerability to manipulation. As such, ZARONIA – a near risk-free rate of commercial banks' cost of overnight borrowing – was chosen as the replacement RFR.**

## JIBAR's Next Three Years

Monocle's IBOR (Interbank Lending Rate) Transition insights paper, highlighted three main impact areas – *systems and processes, exposure analysis and new contracts* – for banks to prepare for the LIBOR transition in 2021 and beyond. Due to the similarities between the LIBOR and JIBAR transition, the operational changes that were made for new international risk-free rates (RFR) will cater to many of the ZARONIA requirements. However, with the increase in volume, the entrenchment of JIBAR across the South African financial system and the SARB's push to have the transition completed within three years, **Monocle has highlighted several key challenges banks should consider before their transition ramps up.**

*Draft JIBAR Transition Timelines*

**2023**

Q3
- ZARONIA to be added to ISDA interest rate definitions.
- Common conventions for cash markets to be published for consultation.
- Common conventions for OIS derivatives to be settled.

Q4
- ZARONIA expected to be endorsed.
- ZARONIA observation period ends and becomes available for use.
- Build-up in derivative market liquidity to begin.

**2024**

Q1
- Official cessation date to be announced.
- Cessation plan to be communicated to banks.

Q4
- **"ZARONIA first" begins for derivatives.**
- ISDA fallback protocol to be completed

**2025**

Q2/3
- **"No new JIBAR" to be enforced.**
- ZARONIA term rates to be endorsed and published.
- **"ZARONIA first" begins for cash products.**

**2026**

TBD
- **JIBAR cessation to be enforced.**

# Key Challenges

## Project Management

For JIBAR-linked loans and derivatives that are not set to mature before the JIBAR cessation date (2026), banks' legal teams will need to ensure that related contracts are amended to include the appropriate fallback language (contractual terms relating to the replacement rate that would apply if the relevant benchmark became unavailable) and renegotiate terms, including credit spread adjustments.

This is an **intensive administrative initiative** and could overwhelm a program if not managed consistently throughout the transition timelines. This was the case for American financial institutions where around $700 billion worth of US junk loans had not been delinked from USD-LIBOR just 30 days before its ultimate cessation (30 June 2023). As a result, these contracts were at risk of falling back on more costly base rates if not transitioned to SOFR (the benchmark RFR elected for dollar-denominated derivatives and loans) in time.

Strong program management that can consider and manage the distinct operational, financial, risk and legal tasks will be essential. However, program management will need to drive a collaborative approach that ensures functions and business units across the bank remain informed and aligned on emerging risks and complexities.

**With over R30 trillion worth of loans and securities that reset against three-month JIBAR, financial institutions must consider how their volume of contracts will impact their transition.**

**Critical tasks to be consider by program management include:**

- System and process updates to cater for ZARONIA.
- Existing JIBAR-linked contracts to be amended with fallback clauses and renegotiated for voluntary transition.
- Downstream risk, finance, tax, operational and reporting changes to accommodate ZARONIA.
- Effective communication (both internally and externally) of transition impacts and changes.
- Comprehensive change management across investment banking, markets, treasury and operational teams to fully understand and adapt to new ZARONIA processes.

See the IBOR (Interbank Lending Rate) Transition insights paper for further detail on these items.

# Key Challenges

## Exposure Monitoring and Analysis

Currently, South African banks are required to report their JIBAR-linked exposures to the SARB on a quarterly basis – with the frequency to increase to a monthly submission as the transition deadlines approach. This reporting process will form the backbone of a firm's programme management for the transition as a consolidated and continuously updated view of a bank's exposure.

However, the need for **additional data points**, beyond those required by the SARB, will play a pivotal role in assisting legal teams in identifying legal contracts that need to be amended or renegotiated as JIBAR cessation approaches. This is particularly troublesome when it comes to legal enrichment data, such as the assigned legal advisor for each contract, that is traditionally stored solely in unstructured PDF legal agreements. For many banks, the sourcing and review of these legal agreements and the required data points remain part of a largely manual process.

**"In America, around $700 billion worth of US junk loans had not been delinked from LIBOR just 30 days before its complete cessation (30 June 2023) – leaving these contracts at risk of falling back on more costly base rates if not transitioned to SOFR in time."**

Strategically, JIBAR transition provides firms with the opportunity to begin standardising their legal agreements as they renegotiate certain deals for the transition. This paves the way for a **data digitisation process** for these legal contracts, whereby standardised data inputs to legal agreements can be automatically identified, captured via optical character recognition tools and loaded onto front-end loan and trade systems at a deal/trade level. Similar solutions can be implemented for ISDA contract support annexes agreements.

Not only does this eliminate the risk of fat-finger errors when transaction managers manually capture the contractual terms and conditions, but critically ensures that **JIBAR exposure reporting can be based off the primary and legally enforceable arrangements rather than system data.** The reliability of data is a critical issue for banks that are involved in complex investment bank deals that cannot be accurately booked on a front-end system to reference JIBAR (due to system or operational constraints). This can lead to certain JIBAR linked deals not being identified.

## System Performance

South African banks will need to complete a **system and process impact assessment** for JIBAR transition. Such an assessment will need to consider that updates for vendor systems or in-house development may have been completed over the last few years to cater for backwards looking reference rates through a compounded in arrears calculation as part of their LIBOR transition.

While impacts to systems and processes may be minimal, IT operation teams will now need to assess the implications that a compounded in arrears calculation will have on performance, considering the significantly larger scope of ZARONIA-linked contracts compared to SOFR and SONIA. For large corporate and investment banks in South Africa, their exposure consists of tens of thousands of derivative trades and thousands of loans linked to JIBAR – **a 10x increase in volume from their LIBOR exposures.**

# How Monocle Can Assist

Throughout several years of LIBOR transition, Monocle has been actively involved across the banking value chain to help prepare for and manage the operational changes at our various banking clients.

With extensive expertise across trade management, treasury, finance, front office risk and pricing, as well as system and data infrastructure, Monocle is expertly positioned to assist our clients as they prepare for the challenges associated with their JIBAR transitions. Our risk-free rate transition project experience includes:

- Operational system design and build to enable the sourcing of RFRs, as well as the calculation of interest for trading and loan platforms through Monocle-built interest models (SQL).
- Legal contract analysis focused on flagging fallback rate clauses.
- Development of a single view of contracts (or the larger but more intense project of single view of customer) to provide effective contract negotiations by identifying all relevant contracts ahead of time.
- Design and build of a legal agreement service to integrate trade and master service agreement data which enables netting and collateral calculations.
- Data analysis of all loans and derivative securities to facilitate exposure analysis reporting, transition progress reporting, as well as ad hoc regulatory reporting (IBOR and JIBAR transition reporting to the SARB).
- Advisory services around rate reset dates, interest methodologies, and other transitional process and data issues.
- Program management across LIBOR and JIBAR transitions in markets and investment banking business units.

# About Monocle

Monocle is a management consulting firm specialising in banking and insurance. Since 2002, we have assisted industry-leading banks and insurance companies around the world, including institutions in the United Kingdom, Europe, Scandinavia, Asia, South Africa and throughout sub-Saharan Africa.

We design and execute bespoke change projects from start to finish, bridging the divide between business stakeholders' needs and the complex systems, processes and data that sit under the hood. We offer several unique capabilities to our clients, which have been forged over time through the combination of a highly specialised skill set and extensive experience working with the systems, processes and people that are at the heart of the financial services industry.

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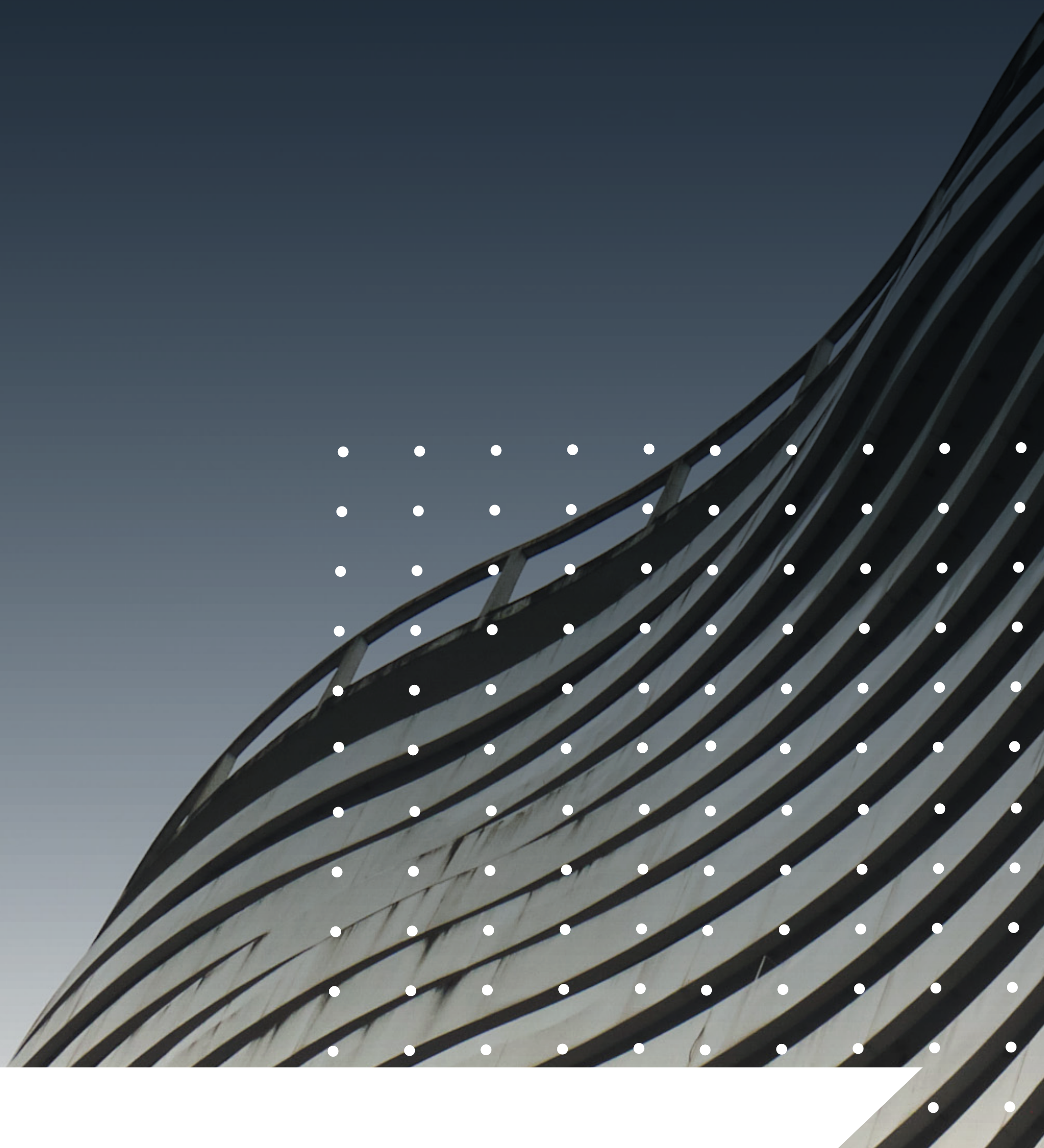

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