



**From LIBOR's Legacy to
Risk-Free Rates**

An Analysis of Global Interest Rate Benchmarks

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Benchmark Interest Rates & Post-LIBOR Transition



- Rates have shifted post-LIBOR: Global transition from LIBOR to Risk-Free Rates (RFRs) completed in major markets
- Transition gaining momentum: SOFR dominates USD markets, SONIA leads GBP, ESTR for EUR
- Regional significance: Different rates serve different markets - MCLR/RLLR in India, TONAR in Japan
- Impact on pricing/hedging: Fundamental changes in credit valuation, discounting methodologies, and risk management

Market Impact Snapshot: The transition from LIBOR to RFRs represents one of the most significant changes in financial markets since the 2008 crisis. This shift affects over \$400 trillion in financial contracts globally and requires fundamental changes in pricing, valuation, and risk management practices.





Popular Interest rates

Rate	Region/Currency	Main Uses	Popularity
LIBOR	Global (USD, GBP, etc.)	Legacy loans, derivatives	Phased out
SOFR	USA (USD)	Loans, bonds, derivatives	New USD standard
SONIA	UK (GBP)	Loans, swaps, bonds	Main GBP benchmark
MCLR	India (INR)	Bank loans	Key for Indian lending
RLLR	India (INR)	Retail loans	Increasingly popular
€STR	Eurozone (EUR)	Derivatives, fallback	Replacing EONIA
TONAR	Japan (JPY)	Swaps, derivatives	Main JPY risk-free rate
EURIBOR	Eurozone (EUR)	Loans, mortgages, swaps	Still widely used



LIBOR – The Legacy Benchmark

London Interbank Offered Rate (LIBOR)

- Definition & Region: Global benchmark representing the rate at which major banks lend to each other
- Publisher: ICE Benchmark Administration (IBA) - formerly British Bankers' Association
- Methodology: Unsecured, forward-looking, based on panel bank submissions
- Tenor Availability: Overnight, 1 week, 1, 2, 3, 6, 12 months
- Currencies: USD, GBP, EUR, JPY, CHF

Historical Significance

LIBOR was once called "the world's most important number" - underpinning over **\$400 trillion** in financial contracts including loans, mortgages, derivatives, and bonds.

Transition Status

LIBOR publication ceased for most currencies on December 31, 2021. USD LIBOR continued until June 30, 2023, with synthetic rates available for tough legacy contracts.



SOFR – The USD Risk-Free Rate

Secured Overnight Financing Rate (SOFR)

- Definition & Region: USD risk-free rate based on overnight Treasury repo transactions
- Publisher: Federal Reserve Bank of New York
- Methodology: Secured, backward-looking, transaction-based
- Tenor Availability: Overnight (primary), with 30, 90, 180-day term rates
- Underlying Market: ~**\$1.7 trillion daily Treasury repo** transactions

Key Advantages

- Based on actual transactions, not estimates
- Secured by US Treasury collateral (virtually risk-free)
- Robust underlying market with high liquidity
- Transparent methodology and governance

Market Adoption

SOFR derivatives trading has grown exponentially, with daily volumes exceeding **\$200 billion** in interest rate swaps by 2024.



SONIA & ESTR – European RFRs

Sterling Overnight Index Average (SONIA)

- Sterling Overnight Index Average (SONIA)
- Region: United Kingdom (GBP)
- Publisher: Bank of England
- Methodology: Unsecured, backward-looking, based on overnight deposits

SONIA existed before the 2008 crisis but was revived and enhanced as LIBOR replacement achieved a 22.9% revenue increase over the past fiscal year, exceeding projections.

Euro Short-Term Rate (ESTR)

- Region: Eurozone (EUR)
- Publisher: European Central Bank (ECB)
- Methodology: Unsecured, backward-looking, based on overnight lending
- Market Basis: Wholesale euro unsecured overnight borrowing

Regional Adoption Patterns

SONIA: Strong adoption in GBP swaps, bonds, and syndicated loans

ESTR: Gradual adoption alongside EURIBOR in European markets

Both rates show lower volatility compared to their respective LIBOR equivalents



Asian Markets benchmark

Tokyo Overnight Average Rate (TONAR)

- Region: Japan (JPY)
- Publisher: Bank of Japan
- Methodology: Unsecured, backward-looking, call market based
- Characteristics: Low volatility, reflects BoJ's ultra-accommodative policy

Indian Benchmark Transition: MCLR to RLLR

MCLR (Marginal Cost of Funds-based Lending Rate):

- Internal benchmark based on bank's cost of funds
- Less transparent, slower transmission of policy rates

RLLR (Repo Linked Lending Rate):

- External benchmark linked to RBI's repo rate
- More transparent, faster policy transmission
- ~70% of new retail loans now use RLLR-linked pricing



Euro Interbank Offered Rate (EURIBOR)

- Definition: Rate at which eurozone banks lend to each other
- Publisher: European Money Markets Institute (EMMI)
- Methodology: Unsecured, forward-looking, hybrid (transaction + expert judgment)
- Tenor Availability: 1 week, 1, 3, 6, 12 months
- Status: Reformed and strengthened, remains active

Why EURIBOR Survived

- Successful reform program addressing regulatory concerns
- Hybrid methodology combining transactions and expert judgment
- Strong governance and oversight framework
- Deep integration in European financial markets
- Coexistence strategy with ESTR rather than full replacement

EURIBOR continues to play a significant role in European derivatives markets, particularly for term rates. It coexists with ESTR, with ESTR serving as the risk-free rate for discounting and EURIBOR maintaining its role in forward-looking products.



Historical Trends Analysis (2023–2025)

Key Rate Movements - Last 2 Years

Major Trends and Inflection Points:

1. **LIBOR Cessation (June 2023):** Final USD LIBOR settings published, marking end of an era
2. **SOFR/SONIA Rate Hikes:** Both rates climbed significantly with Federal Reserve and Bank of England tightening cycles, reaching multi-year highs
3. **TONAR Stability:** Remained near zero, reflecting Bank of Japan's ultra-accommodative monetary policy stance
4. **MCLR vs RLLR Divergence:** Indian rates showed clear divergence as RLLR responded faster to RBI policy changes
5. **EURIBOR Tightening:** Rose alongside ECB policy normalization, reflecting eurozone banking sector conditions



Conclusion

1. Resilience in Uncertainty: Despite elevated rates and policy divergence, global markets have demonstrated remarkable resilience, adapting to a “higher for longer” environment without widespread instability.
2. Transparency & Trust: The shift from legacy benchmarks like LIBOR to transparent, transaction-based rates (SOFR, SONIA, €STR, TONAR) has strengthened market credibility and reduced systemic risk.
3. Divergence Brings New Challenges: As central banks chart different paths, localized risks and capital flow volatility have increased, making active risk management and regional understanding more important than ever.
4. Credit Risk Evolution: With risk-free rates lacking embedded credit risk premiums, lenders must adapt their pricing strategies, and borrowers must be prepared for more dynamic interest costs.
5. Looking Ahead: The global financial system is better equipped for future shocks, but vigilance is essential. Monitoring basis risk, policy shifts, and market liquidity will remain crucial for financial stability.