

08/05/2020

Dear Customer,

We are reaching out to you to inform you that certain interest rate benchmarks, such as the Euro Interbank Offered Rate (EURIBOR) and the London Interbank Offered Rate (LIBOR), among others, are being reformed.

What are Interest Rate Benchmarks?

Interest Rate Benchmarks are indices, also known as base rates or reference rates, used worldwide, among others, to determine the amount of interest payable on a wide range of financial contracts, such as personal loans, mortgages, bank overdrafts and other more complex financial instruments, such as derivatives and bonds.

Interest rate benchmarks are calculated by an independent body, most often to reflect the cost of borrowing funds in different markets.

Why was reform required?

After the financial crisis, global regulators became increasingly concerned about the reliability and integrity of benchmarks. This concern has resulted in recommendations made by the Financial Stability Board (FSB) towards the global financial industry to reform the major interest rate benchmarks and/or develop new alternative benchmarks.

The European Commission has therefore introduced the Benchmarks Regulation (BMR), which sets out a common framework for benchmarks aiming to provide high-level protection to consumers and investors within the EU. More specifically, it sets out certain criteria and conditions for benchmark rates to improve governance and ensure that such benchmarks are reliable and robust. BMR applies to Cyprus as an EU member state, and the supervisory authority responsible for its implementation is the Cyprus Securities and Exchange Commission (CySEC).

How is the Bank preparing for the transition and what should clients be doing?

The Bank is reaching out to its clients since the above changes affect some of its products and services linked to the specific benchmarks.

We have been preparing for these changes for quite some time, in order to ensure that the changes are transposed to our products and services in the most effective and efficient manner possible. The Bank has been participating in industry working groups and continues to closely monitor developments in this area.

Additional information on the Euribor and Libor indicators can be found in the attached text.

The Bank will reach out to you in due course, if needed.

Sincerely,

Bank of Cyprus Public Company Ltd

EURIBOR

EURIBOR is an unsecured market interest rate, administered and published daily by the European Money Markets Institute (EMMI), for transactions in Euro.

In order to comply with the BMR, EMMI, as administrator of the EURIBOR benchmark, proceeded with its reform by reformulating the EURIBOR definition and by changing the methodology used to provide the index. This was achieved by moving from a quote-based methodology to a hybrid methodology based on actual transactions to the extent possible, and on expert judgement, where actual transactions are not available.

To change the methodology, beginning in the second quarter of 2019, EMMI performed the so-called 'phase-in' approach, in order to minimise operational and technological risks for Panel Banks (i.e. banks contributing to the calculation of EURIBOR), EURIBOR users, and the benchmark itself. On 28 November, 2019, EMMI formally confirmed the successful completion of the phase-in of all EURIBOR Panel Banks to the new hybrid methodology. EURIBOR is currently BMR-compliant.

As per EMMI, EURIBOR represents the rate at which wholesale funds in Euro can be obtained by credit institutions in the European Union and European Free Trade Association (EFTA) countries in the unsecured money market.

Further details on the calculation methodology for EURIBOR, including the factors contributing to a change in the EURIBOR rate, can be found in the Blueprint for the Hybrid Methodology for the Determination of EURIBOR¹ and the Benchmark Determination Methodology for EURIBOR².

EMMI is of the opinion that the EURIBOR reform does not change the economic variable that the index seeks to measure, which has always been the banks' costs of borrowing in unsecured money markets.

LIBOR

LIBOR is published daily by the ICE Benchmark Administration (IBA) and reflects the lending cost for banks in the unsecured money market for various currencies, such as the British pound, the US dollar, the Swiss franc and the Japanese yen.

Regarding LIBOR's reform, in April 2019 IBA confirmed that, after a gradual transition designed to minimise operational and technological risk, all LIBOR Panel Banks (i.e. banks contributing to the calculation of LIBOR) successfully completed the transition to the so-called 'Waterfall Methodology'.

Based on the new methodology, LIBOR represents a wholesale funding rate anchored in LIBOR panel banks' unsecured wholesale transactions to the greatest extent possible, with a waterfall to enable a rate to be published in all market circumstances (in case actual transactions are not available, expert judgment is used).

¹ https://www.emmi-benchmarks.eu/assets/files/D0034A-2019%20Euribor%20Hybrid%20Methodology_2019_02_12.pdf

² <https://www.emmi-benchmarks.eu/assets/files/D0016A-2019%20Benchmark%20Determination%20Methodology%20for%20EURIBOR.pdf>

Notwithstanding this transition, IBA announced that there is no guarantee that LIBOR will continue to be published after year-end 2021, and thus industry working groups are working to identify alternative rates to transition to.

Further details on the calculation methodology for LIBOR, including the factors contributing to a change in the LIBOR rate, can be found on IBA's website (ICE LIBOR Evolution)³.

Read more:

Please refer to the links below for further information.

European Commission – Benchmark regulation

<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016R1011&from=FR>

ECB: What are benchmark rates, why are they important and why are they being reformed?

https://www.ecb.europa.eu/explainers/tell-me-more/html/benchmark_rates_qa.en.html

Please note that the above is a non-exhaustive update on what is currently the position in relation to these two indices.

³ <https://www.theice.com/iba/libor>