

## Purpose:

The purpose of this document is to provide Abu Dhabi Islamic Bank PJSC ("ADIB")'s customers and counterparties with an overview of the discontinuation of the London Interbank Offered Rate (LIBOR). This document is provided for general guidance purposes only and should not be construed as any recommendation, nor any legal nor regulatory advice, on the part of ADIB. We recommend that you should, together with your own independent, professional advisors, conduct your own assessment on the potential impact of benchmark rate reform, including LIBOR discontinuation, on your business. Using these new alternative benchmarks will have no impact on the Shari'a compliant nature of ADIB products and it will not convert any of them to be based on borrowing or lending basis.

## Background of LIBOR Transition

### What is LIBOR?

The London Interbank Offered Rate (LIBOR) is a measure of the average rate at which banks are willing to borrow wholesale unsecured funds<sup>1</sup>. For more than 40 years, LIBOR has been extensively used as a reference rate in a range of Islamic financial products and instruments with a Shari'a compliant structure of floating rates such as Commodity Murabaha, Ijarah, Wakala. LIBOR is often used as benchmark rate to determine profit payments for these products.

Immediately prior to December 2021<sup>3</sup>, LIBOR was calculated for five currencies (USD, GBP, EUR, CHF and JPY) and for seven tenors in respect of each currency (Overnight/Spot Next, One Week, One Month, Two Months, Three Months, Six Months and 12 Months), resulting in the publication of 35 individual rates each applicable London business day<sup>2</sup>.

### What is LIBOR transition?

Since the global financial crisis in 09-2008, activity in the markets that LIBOR measures has reduced. The low volume of underlying transactions means that LIBOR is no longer sustainable<sup>1</sup>. In 2017, the UK Financial Conduct Authority (FCA) announced that it would no longer be necessary to compel (quotation) banks to submit LIBOR quotes<sup>3</sup>. The LIBOR panel banks agreed to continue submitting to LIBOR until end2021- (later extended to end-June 2023 for US dollar LIBOR only), to enable time for the market to move away from LIBOR<sup>4</sup>. The series of announcements by other regulators have followed supporting further the process of transitioning IBOR.

In March 2021, the FCA and ICE Benchmark Administration (the administrator of LIBOR) announced that sterling, euro, Swiss franc and Japanese yen LIBOR panels, as well as panels for -1week and -2month US dollar LIBOR, will cease at end2021-, with the remaining US dollar LIBOR panels ceasing at end-June 2023<sup>4</sup>. The regulatory timelines, transition milestones and cessation / non-representativeness dates are outlined further in this document.

ADIB is currently not aware of any forthcoming changes to the Emirates Interbank Offered Rate administered by the Central Bank of the United Arab Emirates, which is also an IBOR and more commonly referred to as "EBOR" or "EIBOR". The Central Bank of the United Arab Emirates may in the future mandate reforms to this benchmark rate, and advance notice of the timing or nature of such changes may not be available to market participants

## Alternatives to LIBOR

### What are the alternatives to LIBOR?

The two major financial regulators, Financial Conduct Authority (FCA) and Federal Reserve Bank of New York (Fed), have set up specific working groups, 'The Alternative Reference Rates Committee' (ARRC) and 'Working Group on Sterling Risk-Free Reference Rates' (UK RFR WG) with the objective of developing the alternative benchmarks to LIBOR and providing the transition directions to the market. Similarly, other regulators have also established working groups with the same mandate.

Select examples of benchmarks which are either being replaced or benchmarks where changes either have or will be made to their methodology (notably the way in which they are determined) are set out in the table below.

The table is not exhaustive and there may be other benchmarks which are either discontinued or where changes have or will be made to their methodology.

Currency	Existing IBOR	Alternative Reference Rate	Transaction Type
USD	USD LIBOR	SOFR (Secured Overnight Financing Rate)	Secured
GBP	GBP LIBOR	SONIA (Sterling Overnight Index Average)	Unsecured
EUR	EURIBOR/EONIA	€STR (Euro Short-Term Rate)	Unsecured
JPY	JPY LIBOR	TONAR (Tokyo Overnight Average Rate)	Unsecured
CHF	CHF LIBOR	SARON (Swiss Average Rate Overnight)	Secured

## What are the differences between LIBOR and ARR's?

ARRs are structurally and economically different to LIBORs. LIBOR implicitly consists of three components: credit risk-free component; Liquidity and tenor adjustment; and Credit risk (related to AA rated client). The quotations are based on actual transactions as well as on the subjective / discretionary element arising from the quotation bank's market expectation. ARR's, on the other hand, are near (credit) risk-free rates (RFRs) and are backward looking overnight rates based on actual transactions, unlike LIBORs.

LIBOR	ARR
Forward Looking rate with the defined Term Structure (7 tenors)	Overnight only (at this stage), backward looking rates with limited forward term structure
Based on expectations/speculations; quotes submitted by panel banks	Based on actual transactions; calculated volume-weighted median
Includes a built-in Credit Risk and Liquidity Spread across the tenors	Nearly risk-free rates
Centrally calculated in the London Interbank Market	Each country has its own rate calculation mechanism
Responsive to risk free rate, liquidity and credit pricing (especially in the event of stress)	Only responsive to change in risk free rates

## When will LIBOR be discontinued?

On 5 March 2021, the FCA announced that the following LIBOR benchmark rates will either cease to be provided or will no longer be representative of the underlying market immediately after the following dates (Cessation Dates):

### 31 December 2021:

- With respect to Sterling, Euro, Swiss Franc and Japanese yen, all LIBOR benchmark rates for all tenors. Six sterling and yen LIBOR settings will continue for the duration of 2022 on a 'synthetic' basis; and
- With respect to United States dollars (USD), for one week (USD LIBOR 1week) and for two months (USD LIBOR 2month)

### 30 June 2023:

- In the case of USD, all LIBOR benchmark rates for the remaining tenors, although its use for new business will be restricted from end2021-, with limited exceptions<sup>2</sup>.

## What is the potential impact on LIBOR referencing financing arrangement between you and ADIB?

Financing Arrangement	Existing Contracts Financing Maturity and Action Required	
	Pre June 2023	Post June 2023
USD LIBOR referencing contracts	No action required	The Bank will approach you in the upcoming period to initiate the transition process and reach a mutual agreement
GBP LIBOR referencing contracts	GBP LIBOR referenced contracts are priced using Synthetic LIBOR from 1 Jan 2022. The Bank will approach you in the upcoming period to initiate the transition process and reach a mutual agreement	

**New Contracts:** The Bank is actively working towards ensuring readiness to start issuing new ARR products from 2022.

For your facilities that reference LIBORs, you should now consider the following impacts:

1. Understand the structural differences between RFRs and LIBORs
2. Amendments to the calculation of the relevant payments under the product
3. Fallback arrangements under the relevant agreement(s) becoming operative, which may change the rate used to calculate amounts that you pay or amounts that might be paid to you;
4. Consequential changes to other provisions, such as changes to margin and associated fees;
5. Practical implications, such as changes to your systems and accounting practices.
6. Mismatch between the reference rate(s) under the product and the reference rate(s) under any products linked to Shari'a compliant hedging arrangements.

This is not an exhaustive list and there are likely to be other factors for you to consider without reliance upon ADIB. We recommend that you keep up to date with the latest developments in relation to the changes and the potential alternative benchmark rates that may be relevant to you.

## What is a fallback language?

"Fallback language" refers to the contractual provisions that lay out the process through which a replacement rate can be identified if a benchmark (e.g., USD LIBOR) is not available. Fallback language comprises three key components: fallback trigger event, benchmark replacement, and benchmark replacement adjustment.

In December 2021, The International Islamic Financial Market (IIFM) and The International Swaps and Derivatives Association (ISDA) published IBOR fallback definitions booklet and Bilateral Amendment Agreement to support market participants in their transition of Islamic Hedging Transactions. In an event the benchmark rates such as LIBOR as ceased or otherwise become unavailable, then the calculation of amounts such as profit, rental,

fees, incentives and other provisions which reference the benchmark rate will be determined using fallback arrangements (if any) set out in the relevant agreement. Any changes made to ADIB's products, contracts or agreements to reflect the adoption and implementation of an alternative rate shall be made after appropriate review and approval by the Internal Shari'a Supervisory Committee of the Bank.

### What is a credit adjustment spread?

Given the structural and economic differences between LIBOR and ARR, some of the regulators and trade associations have introduced the Credit Adjustment Spread (CAS) to be added to ARR rates to eliminate or minimize and value transfer. On 5th March 2021, ISDA published -5year CAS spreads for each of the tenors of the five LIBOR currencies. Many regulators and associations such as FCA, ARRC and ISDA recommend and support the use of ISDA CAS spreads for the transition of legacy LIBOR contracts that mature after the respective cessation dates. By way of an example, the credit adjustment spread for USD LIBOR would be as follows:



### Next steps and further information

If you wish to discuss this further with us, please contact your ADIB Relationship Manager or you can also write to us on the email ID dedicated to handle IBOR transition requests. You can also visit our website for further updates.

For further information in relation to the transition away from LIBORs, including anticipated timeframes, please refer to the table below for details of the relevant LIBOR transition working group:

LIBOR	Relevant Transition Working Group	Website
Sterling LIBOR	Bank of England and FCA working group	<a href="http://www.bankofengland.co.uk">www.bankofengland.co.uk</a>
US Dollar LIBOR	Federal Reserve Alternative Reference Rates Committee	<a href="http://www.newyorkfed.org">www.newyorkfed.org</a>
EURIBOR and EONIA	European Central Bank working group	<a href="http://www.ecb.europa.eu">www.ecb.europa.eu</a>
JPY LIBOR and JPY TIBOR	Bank of Japan cross-industry committee on Japanese yen interest rate benchmarks	<a href="http://www.boj.or.jp">www.boj.or.jp</a>
CHF LIBOR	Swiss National Bank working group on Swiss franc reference rates	<a href="http://www.snb.ch">www.snb.ch</a>

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