Schroders

London Interbank Offered Rate Transition

Impact and Changes to Schroder funds

This notification is to inform you of changes that are expected to arise due to the planned discontinuation of Interbank Offered Rates (IBORs), including the London Interbank Offered Rate (LIBOR) at the end of December 2021 and the consequent changes to certain Schroder funds.

As part of an industry driven reform to strengthen the resilience of global financial markets, some interest rate benchmarks (including London Interbank Offered Rate – (LIBOR) and other Interbank Offered Rates (IBORs)) are being discontinued by the end of December 2021.

A significant decline in interbank lending and some high-profile instances of LIBOR manipulation resulted in the recommendation in 2014 by the Financial Stability Board to transition away from LIBOR and other IBORs to new alternative rates.

In response to this and subsequent announcements from the UK Financial Conduct Authority and other regulators globally, we will be replacing the benchmark for funds that currently use LIBOR with an alternative benchmark. The new benchmarks will be set out in the fund(s) prospectus, the Key Investor Information Document (KIID) and the factsheet. The change is not expected to materially alter the way that a fund is managed or result in any additional charges to the fund. The funds' allowable investments and the risk profile will also be unchanged to any material extent.

The timing of this transition for each individual fund will differ. Shareholders in funds will be notified in advance of any benchmark changes and from when these will take effect. We will select the benchmark which we believe is the most suitable alternative for any given fund.

UK domiciled funds

If you have any questions about the proposal for any fund that you are invested in, please contact your financial adviser. If you do not have a financial adviser you can find one in your area by visiting www.unbiased.co.uk or call a member of our Investor Services Team on 0800 718 777. Please be aware that Schroder Investment Management Limited does not offer investment advice.

Luxembourg domiciled funds

If you have any questions about the proposal for any fund that you are invested in, please contact your local Schroders office, your usual professional adviser, or Schroder Investment Management (Europe) S.A. on (+352) 341 342 202 or on email at europeclientservices@schroders.com Please be aware that Schroder Investment Management (Europe) S.A. does not offer investment advice.

Further information

Our FAQs provide further information on this change.

What is a benchmark? A benchmark is a standard against which the performance of a financial asset or a fund can be measured. Benchmarks are used in our funds for a range of purposes including as a standard against which to compare the return or "performance" of the fund, as a target for the fund's performance and for defining what types and amounts of financial assets the fund may invest in. In some instances, they are also used to calculate performance fees that are paid to Schroders or a third party manager if the fund's performance rises above a set threshold.

What is an interest rate? An interest rate is the amount a lender charges a borrower for a loan. Interest rate benchmarks are a form of benchmark that a lender may use as an element of the interest rate it charges a borrower for a loan. The lender may add a percentage to an interest rate benchmark to arrive at the amount of interest it charges the borrower. The London Interbank Offered Rate (LIBOR) is the most widely used interest rate benchmark in the world.

Schroders uses interest rate benchmarks as the benchmarks for a number of our funds.

Frequently Asked Questions (FAQ)

LIBOR – An overview

The London Interbank Offered Rate (LIBOR) was officially adopted in 1986, with roots dating back to the 60s. Underpinning some $300 trillion (Refinitiv, October 2019) of financial instruments, it is one of the most widely quoted reference rates in the world. It is expected that LIBOR and other Interbank Offered Rates (IBORs) will cease to exist after the end of 2021.

1. What is LIBOR?

LIBOR is based on submissions by a panel of global banks. Each bank is asked every day to provide the rate at which they could secure short term lending from another major bank and those submissions are used to calculate LIBOR in accordance with an agreed methodology.

LIBOR is used as a reference rate in a wide range of financial contracts, including derivatives, bonds and loans. It is set for seven maturities, ranging from overnight to 12 months, and five different currencies for each maturity. LIBOR rates exist for the US dollar, sterling, euro, yen and Swiss franc.

Where there are insufficient actual transactions or transaction-related data on which to base their LIBOR submissions, the panel banks must use their "expert judgement" within certain agreed parameters to provide their submissions.

2. Why is LIBOR being replaced?

A significant decline in interbank lending and some high-profile instances of LIBOR manipulation resulted in the publication of the Financial Stability Board's (FSB) recommendation in 2014 to develop alternative so-called "risk-free" rates (RFRs) for use instead of LIBOR and other IBORs. In July 2017, the former Chief Executive of the Financial Conduct Authority (FCA) Andrew Bailey, said in a speech that "...the underlying market that LIBOR seeks to measure...is no longer sufficiently active."

In the same speech, Andrew Bailey also said, "In our view, it is not only potentially unsustainable, but also undesirable, for market participants to rely indefinitely on reference rates that do not have active underlying markets to support them". He went on to say that the FCA would not compel banks to make LIBOR submissions after the end of 2021 which was widely understood as a sign that LIBOR would cease to exist post-2021.

The FCA further confirmed that LIBOR would be discontinued at the end of December 2021 by publishing statements in September 2018 and February 2020 asking for firms' plans for the transition away from LIBOR and setting out the FCA expectations for the end of LIBOR.

On 25 March 2020, despite the impact of the coronavirus on financial markets the FCA stated that the central assumption that firms cannot rely on LIBOR being published after the end of 2021 has not changed and should remain the target date for all firms to meet.

3. What is LIBOR being replaced with?

Following the FSB's recommendation in 2014, industry working groups were established to develop the new RFRs (also known as "alternative reference rates") that are expected to replace LIBOR and other IBORs. LIBOR has a clear cessation date, whereas in some markets an IBOR will continue to exist beyond 2021.

The new RFRs selected for the five major currencies of LIBOR are as follows:

LIBOR currency	New risk-free rate
Sterling LIBOR	Reformed SONIA (Sterling overnight index average)
US dollar LIBOR	SOFR (Secured overnight financing rate)
Yen LIBOR	TONAR (Tokyo overnight average rate)
Swiss franc LIBOR	SARON (Swiss average overnight rate)
Euro LIBOR	€STR (Euro short term rate)

4. What is Schroders' plan for the transition away from LIBOR?

Schroders has a robust plan for the effective management of the impact on our funds' investments as a result of the transition away from LIBOR and has established a dedicated team responsible for this task.

- **Impact assessment**

  Schroders has completed an assessment to determine the impacts of the transition away from LIBOR, and certain other key IBOR, to RFR for our funds and our business. As part of this impact assessment we have analysed the work required to transition investments, change legal documents and update operational and technology systems.

- **Our funds' LIBOR exposures**

  During the course of 2020 and into 2021 we aim to incrementally reduce our exposures to LIBOR for the investments we make on behalf of our funds. In addition to those funds that have a benchmark that references LIBOR many of our funds have made investments in financial assets that reference LIBOR. Depending on the type of financial asset there are different ways in which the fund may transition away from such financial assets over the next 18 months before LIBOR ceases to be published. Some financial assets will already contemplate LIBOR ceasing to exist and their terms will automatically change to an alternative rate. Other financial assets will need to be amended and our funds will be engaging with the relevant parties to try to agree a suitable amendment where possible. Other options are for the funds are to sell existing LIBOR-referencing assets and purchase other financial assets that already use an alternative rate. It is possible that some financial assets will not be easily amended or sold due to their terms or the lack of a buyer. We are discussing in industry working groups and with regulators the issue of those assets that are difficult to amend or sell.

- **Shaping the future use of RFR, post LIBOR**

  We believe that it is essential for the industry to move together as a whole to define a consistent approach and that remaining in step with the broader industry will ultimately be in the interests of investors in our funds. Schroders is participating in industry working groups (e.g. the Bank of England's Working Group on Sterling Risk-Free Reference Rates) and following developments in the transition away from LIBOR, with the aim of adopting, in due course, measures aimed at managing transition risks that are consistent with industry best practice.

5. What progress has been made globally for LIBOR transition?

The new RFRs have been selected for the five major currencies of LIBOR. In addition to this interest rate benchmark transition is making good progress globally.

- **Asia**

  Across Asia, a multi-rate approach has largely been adopted for the transition away from LIBOR, which sees existing rates being used alongside replacement rates.

- **Hong Kong**

  In Hong Kong, it is expected that an enhanced Hong Kong Interbank Offered Rate (HIBOR) will continue to exist alongside adjusted Hong Kong Overnight Index Average (HONIA) as the likely fall back rate.

- **Indonesia**

  In Indonesia, the existing Jakarta Interbank Offered Rate (JIBOR) is being supplemented with IndONIA, which is replacing the overnight JIBOR as an overnight interest rate benchmark. JIBOR has also been enhanced with contributor banks having to quote rates by underpinning it to the greatest extent possible with transaction data in order to better reflect market rates.

- **Singapore**

  In Singapore, the existing Singapore Interbank Offered Rate (SIBOR) which is referenced in cash products will continue to exist, although enhanced methodology for its calculation is expected to be implemented following recent transitional testing. The Singapore Overnight Rate Average (SORA) or an adjusted form of the Singapore Dollar Swap Offer Rate (SOR) is expected to be the fall back rate for SOR.

- **Australia**

  In Australia, a modified version of the existing IBOR, the AUD Bank Bill Swap Rate (BBSW), will continue to be used and co-exist alongside the Australian Interbank Overnight Cash Rate (AONIA) Australia's new RFR.

6. By what date will Schroders stop referencing LIBOR for new business?

The FCA confirmed on 25 March 2020 that the central assumption that firms cannot rely on LIBOR being published after the end of 2021 has not changed and should remain the target date for all firms to meet. Schroders is committed to meeting the target of the end of Q3 2020 to cease launching new products with benchmarks or performance fees linked to LIBOR. In addition, we are working towards the transition away from LIBOR-referencing investments for all our funds by the end of 2021 at the latest, in line with market developments, subject to viable alternative investments being available which reference RFRs.

7. Are there risks for investors resulting from the LIBOR transition?

There is arguably an inherent risk of market disruption in any significant regulatory transition exercise that impacts a significant number of market participants and instrument types.

However, market participants (including Schroders) are working to minimise the impact of LIBOR / IBOR transition, including impacts on investors in our funds, by adopting measures developed through market participant feedback on an industry-wide basis.

The conversion from a LIBOR-linked product to a RFR-linked product will most likely result in a payment being made from one party to the other to account for the change in the characteristics of the underlying reference rate. While the use of industry developed methodologies (such as those developed by ISDA for the derivatives markets) to calculate the alternative reference rate should help to minimise this value transfer it will not remove it entirely. This payment could be due to or required to be paid by, a fund's portfolio. These costs related to the transition will need to be considered as part of each fund's transition plan.

Glossary

Alternative Reference Rate Committee (ARRC) – a group of financial industry participants focused on the successful transition from United States Dollars (USD) London Interbank Offered Rate to an alternative rate.

Asset-Backed Securities – a financial asset that is supported by a pool of assets, e.g. credit card debt, loans.

Benchmark – a standard against which the performance of a financial asset or a fund can be measured. Benchmarks are used in our funds for a range of purposes including a standard against which to compare the return or "performance" of the fund, as a target for the fund's performance to try to beat and for defining what types and amounts of financial assets the fund will invest in. In some instances, they are also used to calculate performance fees, being fees that are paid to the investment manager of the fund if the fund's performance rises above a set threshold.

Bonds or Notes – a form of financial asset that represents a loan from a financial investor (the bondholder or noteholder) to a borrower called the "issuer" (usually corporates or governments).

Credit Risk – the risk that a borrower will become bankrupt or otherwise fail to repay a loan.

Derivatives – a financial asset with a value that is set by reference to other assets e.g. shares, bonds, interest rates.

Derivatives exchange – a form of organised market place for the trading of derivatives on certain prescribed terms.

Fall back – a contractual term of a financial asset that outlines the alternative rate to be used if London Interbank Offered Rate or Interbank Offered Rate is discontinued.

Financial Conduct Authority (FCA) – the conduct authority for financial services firms in the United Kingdom.

Financial Stability Board – an international body that works to promote international financial stability.

Floating Rate Notes (FRN) – a note (see above) with a variable rate of interest that resets at specified intervals.

Interbank Offered Rate (IBOR) - a rate at which major global banks expect they can borrow from other major global banks. This is often not based on actual loans between those banks but is created from estimates submitted by those banks.

Interest Rate – the amount a lender charges a borrower for a loan.

International Swaps and Derivatives Association (ISDA) – a trade association representing participants in the derivatives market.

Maturities - represents the number of days before a financial asset must be repaid.

Note – see bonds above.

Noteholder consent – a process whereby the issuer of a note has to obtain the consent of a certain percentage of the noteholders before the terms of that note can be amended.

Over-the-counter derivative – a derivative entered into bilaterally between two parties and not traded on a derivatives exchange.

Portfolio – a range of investments held by a person or company.

Reference Rate - an interest rate benchmark used to set other interest rates in financial assets. London Interbank Offered Rate and Interbank Offered Rates are examples of reference rates.

Risk Free Rate – a reference rate that does not include in its calculation the credit risk of the borrower.

Risk Free Rate Working Group (RFRWG) - the Bank of England and Financial Conduct Authority's group of financial services members focused on the transition away from London Interbank Offered Rate.

Swaps – a type of derivative between two parties to exchange the cash flows or liabilities of two financial assets for a defined period.

For further information about LIBOR Transition please contact libor.transition@schroders.com