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2019 Described as 'Mission Critical' for SOFR Transition.

WASHINGTON — The transition of financial markets to the Secured Overnight Financing Rate known as SOFR continues to make progress but needs to accelerate in the coming year ahead of a planned phase out of the the existing benchmark, members of the Financial Stability Board said Wednesday.

The municipal bond market, meanwhile, has been slow to issue SOFR-based floating rate notes despite the success of two issuances by New York's Metropolitan Transportation Authority in the fourth quarter of 2018.

The problem, according to some market participants, is that buy-side demand for SOFR-based debt has been slow to emerge as the industry moves toward a 2022 deadline for the phase out of the London Interbank Offered Rate, commonly referred to as Libor.

Randal Quarles, chairman of the Financial Stability Board and vice chairman of supervision for the Federal Reserve Board, described SOFR as "robust transaction-based rates."

"This is an important effort across the globe, but nowhere is it of more importance than in the jurisdictions relying on Libor," Quarles said.

Quarles pointed out that "much of the global financial system had come to rely on Libor" at the time of the financial crisis.

"And yet Libor was a very poorly structured rate," he said. "Contributing banks were asked to submit quotes without any requirement of evidence of transactions or other facts to back them up, which made them susceptible to manipulation."

Tom Wipf, vice chairman of institutional securities for Morgan Stanley (MS), described 2019 as "a mission critical year for this work."

Patrick McCoy, director of finance for the MTA and past president of the Government Finance Officers Association, said at Wednesday's meeting his agency was "very pleased" with its SOFR-based floating rate notes.

The MTA, McCoy told the panel, has a diverse portfolio of about $40 billion in bonds outstanding that include variable rate debt.

"Variable rate debt continues to be a lowcost method of financing as compared to issuing fixed-rate bonds," McCoy told the group.

McCoy said GFOA has published best practices recommendations for its members that are considering using SOFR.

Privately placed debt at banks by smaller issuers is often based on Libor, so GFOA wants smaller issuers to have the information they need to make the transition, McCoy said.

McCoy declined in an interview after the meeting to speculate on why other muni debt issuers haven't yet embraced SOFR and of reports of soft interest on the buy side.

"I can only speak for our experience with our issue and we had strong investor interest from a wide swathe of institutional investors who typically buy and hold FRN type obligations," he said.

The MTA issued the FRNs on behalf of the Triborough Bridge and Tunnel Authority with the first round of TBTA debt for one-year SOFR FRN and a day later for a term of two years.

"The one year was much more desired by the investor community than the two year, and I think that really spoke to the newness of the tax -exempt SOFR-based FRN," McCoy said.

Floating rate debt is only a small fraction of the municipal bond market.

The Securities Industry and Financial Markets Association listed $76.9 billion of publicly issued municipal bonds from 872 issuances that used floating rate debt as of Dec. 18, 2018. That's only 2% of the $3.8 trillion municipal bond market and includes debt that uses the SIFMA index but doesn't include swaps.

Libor-based municipal debt was an even smaller amount at $47.6 billion or about 1.3% of the overall muni market.

In the bigger picture, the Federal Reserve estimated last year there were roughly $200 trillion of financial securities referencing U.S. dollar Libor.

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