UOB 3-Month Compounded SORA Mortgage package

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SORA (Singapore Overnight Rate Average) has been selected as the new interest rate benchmark in Singapore.

Benchmark sustainability

There is a need to strengthen the benchmarks by anchoring them to actual transactions. SORA is based on actual transactions, unlike SIBOR which is constructed based on polling by major Banks in Singapore.

Fairness & transparency

SORA is anchored on actual transactions and is being administered by MAS.

Certainty & Stability

SORA has been selected as the new interest rate benchmark in Singapore. To avoid inconvenience and to some extent, uncertainty over how the transition of SOR and eventually SIBOR will pan out, a SORA pegged mortgage loan is encouraged if preference is for a loan rate pegged to a transparent market benchmark reference rate. A Compounded SORA commercial mortgage loan will result in a more stable interest rate due to reduced anomalies.

Comparison of financial benchmarks

Desired qualities	Financial benchmarks		
	SORA	SIBOR	Bank's Board Rate
Sustainability	✓ SORA is anchored on actual market transactions.	SIBOR is constructed based on polling by major Banks in Singapore.	Bank's board rate is a bank managed rate and not pegged to market.
Fairness & transparency	✓ SORA is anchored on actual transactions. ✓ SORA is administered by MAS.	SIBOR is constructed based on polling by major Banks in Singapore.	Bank's board rate is internally administered by the bank and takes into consideration its internal funding costs. Such rate may not move in tandem with market.
Certainty & Stability	✓ SORA has been selected as the new interest rate benchmark in Singapore. ✓ A Compounded SORA commercial mortgage loan will result in a more stable interest rate due to reduced anomalies.	With the gradual phasing out of SIBOR, there may be inconvenience and uncertainty when transition of SIBOR takes effect. SIBOR pegged loans are exposed to 'pin risk' and dependent on market conditions on a single day. E.g. if interest rate were to spike higher on 4 Jan 2021 (loan disbursement date), compared to the rest of the month, interest payment for the applicable period would be higher due to that single day's reading.	Bank's board rate is a bank managed rate and not pegged to market.

> **"SORA was selected as the new interest rate benchmark as it was found to be the "most robust and suitable alternative", underpinned by a deep and liquid overnight funding market."**

Source: https://www.straitstimes.com/business/banking/mas-to-ensure-singapore-banks-smooth-transition-to-sora-by-end-2021

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Commercial Mortgage package

how SORA

How does a 3-Month Compounded SORA work?

The Singapore Overnight Rate Average (SORA) is the volume-weighted average rate of borrowing transactions in the unsecured overnight interbank SGD cash market in Singapore between 8:00am and 6:15pm.

The 3-Month Compounded SORA is published by MAS at 9:00 am on all business days in Singapore.

The 3-Month Compounded SORA is computed by compounding the published SORA rate (in advance) over the historical 3-month period.

Compounded SORA-in-advance*, like SIBOR, will enable users to know their payment and interest amounts ahead of time.

SCAN ME

The rates can be downloaded from the MAS website at: https://eservices.mas.gov.sg/Statistics/dir/DomesticInterestRates.aspx
(Published by MAS since 5 August 2020)

Illustration of 3-Month Compounded SORA

The 3-Month Compounded SORA is updated every 3 months.

- **Customer accepts letter of offer** — 5 Jan 2021
- **Loan disburses** — 4 Mar 2021
  - D% 3-Month Compounded SORA for 1st 3 months
- **1st rate change notice** — 4 Jun 2021
  - E% 3-Month Compounded SORA for next 3 months

D% and E% are 3-Month Compounded* SORA published by MAS on 4 Mar 2021 and 4 Jun 2021 respectively.

3-Month Compounded SORA vs 3-Month SIBOR

SORA does not have a term and credit risk premium.
This economic difference results in SORA being typically lower than SIBOR.

Term premium:

Compounded SORA **SIBOR**

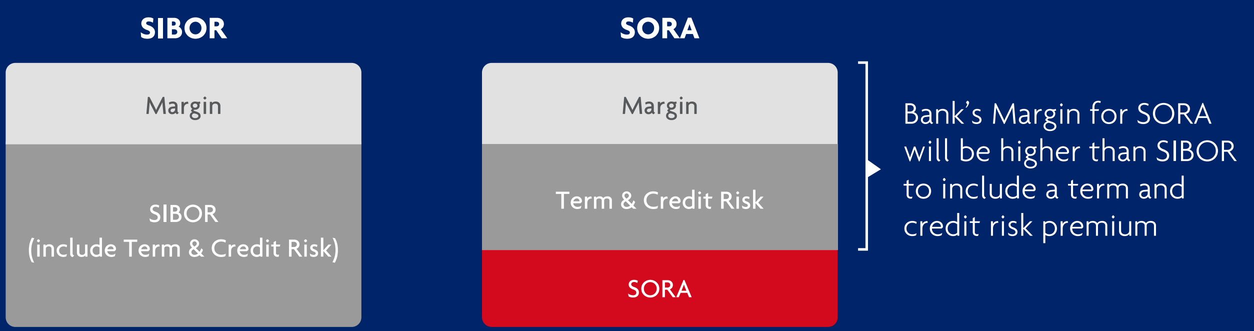
Compounded SORA is backward looking – computed from an average of daily realised SORA values over an interest period, and determined at the end of the interest period. In contrast, SIBOR, is forward looking, and will reflect market expectations of the interest rate over a future period.

Credit risk premium:

Compounded SORA **SIBOR**

SIBOR has a Credit risk premium priced in and SORA does not.

To illustrate the above, refer to illustration below:



Date	SORA (Published date, p.a.)	3M Compounded SORA (Published date, p.a.)	3M SIBOR (p.a.)	3M Compounded SORA vs. 3M SIBOR (p.a.)
30 Oct 20, Fri	0.1247%	0.1101%	0.4054%	-0.3043%
30 Nov 20, Mon	0.1870%	0.1171%	0.4054%	-0.2883%
10 Dec 20, Wed	0.0808%	0.1195%	0.4054%	-0.2859%

Explanation notes:

- For a SORA/SIBOR pegged loan, the total nett rate comprises of the benchmark rate (SIBOR/SORA) + Bank's Margin.
- For SORA, the Margin will be higher than a SIBOR pegged loan, to take into account a term and credit risk premium.
- This is because
  1) SIBOR already carries a credit risk premium and SORA does not;
  2) SIBOR is a forward looking rate while SORA is backward looking. The term premium is to compensate for the uncertainty over how rates may move in the future period.

*Further reading material on use of SORA in financial contracts:
Association of Banks Singapore, SIBOR REFORM AND THE FUTURE LANDSCAPE FOR SGD INTEREST RATE BENCHMARKS, 29 July 2020
https://abs.org.sg/docs/library/sibor-reform-and-the-future-landscape-for-sgd-interest-rate-benchmarks.pdf

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United Overseas Bank Limited Co. Reg. No. 193500026Z

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