Minutes

Global Foreign Exchange Committee Meeting
22 June 2020

Location: Videoconference

Chair: Guy Debelle (Reserve Bank of Australia)

Vice-Chairs: Akira Hoshino (Citi) and Neill Penney (Refinitiv)

Attendees: AUSTRALIA – Australian Foreign Exchange Committee
Public Representative: Christopher Kent (Reserve Bank of Australia)
Private Representative: Stuart Simmons (QIC)
Other Attendees: Matthew Boge and Jason Griffin (Reserve Bank of Australia)

CANADA –Canadian Foreign Exchange Committee
Public Representative: Grahame Johnson (Bank of Canada)
Private Representative: Dagmara Fijalkowski (RBC Global Asset Management)
Other Attendees: Zahir Antia and Harri Vikstedt (Bank of Canada)

CHINA – Foreign Exchange Committee
Public Representatives: Sun Guofeng (People's Bank of China) and Sun Jie (China Foreign Exchange Trade System)
Private Representative: Sun Yu (Bank of China)
Other Attendees: Qiao Linzhi (State Administration of Foreign Exchange), Sun Wei (China Citic Bank), Hu Ying and Sun Jia (China Foreign Exchange Trade System)

EURO AREA –Foreign Exchange Contact Group
Public Representative: Torsti Silvonen (European Central Bank)
Private Representative: Ankur Pruthi (Norges Bank Investment Management)
Other Attendees: Roswitha Hutter (European Central Bank)

GEORGIA – Financial Markets Treasuries Association
Public Representative: Archil Mestvirishvili and Giorgi Laliashvili (National Bank of Georgia)
Private Representative: Lasha Jugeli (GFMTA)

HONG KONG – Treasury Markets Association
Public Representative: Kim-Hung Li (Hong Kong Monetary Authority)
Private Representative: Chordio Chan (Bank of China)

INDIA – Foreign Exchange Committee
Public Representative: Radha Shyam Ratho (Reserve Bank of India)
Private Representative: Ashwani Sindhwani (FX Dealers' Association of India) and H K Jena (State Bank of India)

<u>JAPAN – Tokyo Foreign Exchange Market Committee</u>
Public Representative: Shuntaro Hara (Bank of Japan)
Private Representative: Naoto Nakamura (MUFG Bank)
Other Attendees: Akira Hasabe (Bank of Japan)

<u>MEXICO – Mexican Foreign Exchange Committee</u>
Public Representative: Gerardo Garcia (Banco de Mexico)
Private Representative: Javier Alvarado (MONEX Brokerage House)
Other Attendees: Mayte Rico (Banco de Mexico)

<u>RUSSIA – Moscow Foreign Exchange Joint Standing Committee</u>
Private Representative: Sergey Romanchuk (Metallinvest Bank)

<u>SINGAPORE –Singapore Foreign Exchange Market Committee</u>
Public Representative: Jaqueline Loh (Monetary Authority of Singapore)
Private Representative: Lam Kun Kin (OCBC Bank)
Other Attendees: Cindy Mok (Monetary Authority of Singapore)

<u>SOUTH AFRICA – South African Foreign Exchange Committee</u>
Public Representative: Zafar Parker (South African Reserve Bank)
Private Representative: Richard De Roos (Standard Bank of South Africa)

<u>SOUTH KOREA – Seoul Foreign Exchange Committee</u>
Public Representative: Daeseok Kim (Bank of Korea)
Private Representative: Kyungho Kim (Woori Bank)

<u>SWEDEN - Scandinavian Foreign Exchange Committee</u>
Public Representative: Anders Gange (Sveriges Riksbank)
Private Representative: Svante Hedin (SEB)

<u>SWITZERLAND – Swiss Foreign Exchange Committee</u>
Public Representative: Marcel Zimmermann (Swiss National Bank)
Private Representative: Ernst Lienhard (Swiss Re)
Other Attendees: Barbara Döbeli (Swiss National Bank)

<u>UK – London Foreign Exchange Joint Standing Committee</u>
Public Representatives: Andrew Hauser (Bank of England)
Private Representative: Russell Lascala (Deutsche Bank)
Other Attendees: Grigoria Christodoulou, Rohan Churm, David Edmunds and Frederick Ladbury (Bank of England)

<u>US – New York Foreign Exchange Committee</u>
Public Representative: Anna Nordstrom (Federal Reserve Bank of New York)
Private Representative: Christopher Vogel (TD Securities)
Other Attendees: Alex Cohen, Michelle Ezer, Sanja Peros, Dan Reichgott and Shawei Wang (Federal Reserve Bank of New York)

<u>Guests</u>
Session 4: Jenny Hancock, Tara Rice and Takeshi Shirakami (Bank for International Settlements); Alan Marquard (CLS); Laurence Sweet (Federal Reserve Bank of New York).

Item no. **Minute**

1. **Welcome and Competition Guidelines**

Guy Debelle (the Chair) welcomed the Global Foreign Exchange Committee (GFXC, or 'the Committee') members. Shawei Wang (Federal Reserve Bank of New York) gave an overview of the Competition/Antitrust Law Guidelines for Members of the Global Foreign Exchange Committee. The need for the Committee to take care to ensure that the GFXC did not facilitate or act as a focal point of any anti-competitive behaviour was noted.

2. **Market Conditions**

GFXC co-Vice Chair Akira Hoshino (Citi) provided the Committee with an overview of market developments throughout the first half of 2020. In highlighting the initial phase of the market reaction to the outbreak of Covid-19, parallels with earlier market crises (such as the 2008 global financial crisis) were noted. The peak in volatility during March saw functioning impaired in even the most liquid of markets. Measures of market liquidity (such as bid-offer spreads, depth of book) worsened significantly, most notably in emerging markets, and for all FX asset classes, but particularly in FX swaps. There were also significant rapid or 'flash' adjustments in the values of different currencies. Tightness in funding markets was evident in the cost of borrowing US dollars via foreign exchange swaps. Members were also presented with analysis which suggested that as volatility increased during March, dealers' rates of internalisation declined.

Significant price movements across financial markets globally led to large asset and hedge rebalancing trades during March. However, it was noted that interbank volumes over the March quarter-end were not as large as anticipated, suggesting that some market participants had brought forward their hedging flows to reduce concentration around end-of-month benchmark fixings.

Gerardo Garcia (Bank of Mexico) provided members with an assessment of conditions in emerging markets. The sharp depreciation of emerging market currencies was noted as capital outflows accelerated over February and March, possibly exacerbated in some countries by the decline in oil prices. The outperformance of 'safe haven' currencies when compared to the sharp underperformance of higher yielding currencies pointed to an unwinding in large 'carry trade' positions. The broad usage of derivatives in recent intervention operations by central banks was highlighted.

Sun Guofeng (PBC) noted that Chinese markets had experienced some fluctuations due to the turbulence in global markets but RMB exchange rate had exhibited greater resilience than observed in many other currencies. China's cross-border capital flows were also less affected by the pandemic than observed elsewhere.

In general, the broad array of policy responses from central banks – including the expansion of US dollar swap lines by the Federal Reserve – was thought to have improved market conditions. The speed with which market functioning recovered was acknowledged, particularly as compared to the experience of 2008. Nevertheless, conditions were yet to fully normalise, with measures of spot market liquidity (such as depth of market and top of book bid-offer spreads) generally worse than pre-March levels.

Some members noted there was an increased prevalence in the use of execution algorithms during the Covid-19 period although others felt there was inconclusive evidence of a clear directional trend. As liquidity deteriorated, some market participants favoured the algorithms' ability to continuously execute transactions, rather than paying wider bid-offer spreads in a risk transfer transaction. Additionally, with many working from home throughout this period, the inbuilt controls and strong audit trails provided by execution algorithms were thought to offer a further advantage.

The GFXC also discussed recent trading conditions around FX benchmark fixings. Following the GFXC Statement on 26 March, the quarter-end benchmark fixings proceeded smoothly, although heightened volatility was observed at April month-end. Members reiterated the importance of benchmark users assessing regularly whether executing at the time of a particular fix suited their requirements. The methodology for the WM/Reuters 4pm fix was discussed. The GFXC Chair had discussed some of these issues with the administrator, Refinitiv Benchmark Services Limited (RBSL). GFXC members agreed that more public engagement from RBSL about their considerations for the benchmark's methodology would be beneficial. It was noted that the cost charged to clients for executing orders at the fix had been declining, in part reflecting the increased use of algorithms to manage these orders. But there would be a limit as to how far the cost could decline, given that charges set by market participants for handling fixing orders should be transparent and consistent with the risk borne in accepting these transactions (as per Principle 10 of the Code).

3. Operational Resilience

Following the outbreak of Covid-19, a significant proportion of FX market participants had to adapt their working arrangements away from offices and dealing rooms to a home working environment. The unprecedented scale of this change, with some of the largest FX market participants noting that 90% of their staff were working from home, posed a number of operational challenges. Overall, members agreed that the transition had been surprisingly smooth, with limited impact on market participants' ability to execute, risk manage and settle transactions in the FX market.

GFXC members felt that the FX Global Code had made a positive contribution to the operational resilience of the FX market by advocating the adoption of robust operational and risk management practices by market participants. The Code's emphasis on improving transparency and disclosures also allowed market participants to gain a better understanding of the rapidly changing market conditions and how they may be affected by them.

Reviewing the experience of the past few months, the Committee agreed that the increased use of more flexible working arrangements could have a positive impact in the industry's ability to recruit and retain diverse employees in future. There was an acknowledgement that while existing employees were able to transfer their working practices and institutional culture to their home working environment, recruiting and training new staff remotely posed challenges for many. Although firms were actively planning how to transition their staff safely back into the office environment, it was clear that this was likely to be a protracted process. Safeguarding staff well-being and ensuring continued focus on strategic planning and medium-term change initiatives were therefore key.

The GFXC agreed to publish a short paper on the operational resilience of the FX market following the outbreak of Covid-19.

4. **FX Settlement Risk**

Guests from the Bank for International Settlements (BIS) and CLS briefed the Committee on recent trends in FX settlement. Takeshi Shirakami (BIS) drew on the results of the 2019 BIS Triennial Survey to highlight that FX settlement risk remains significant and that the share of FX transactions not being settled on a payment-versus-payment (PvP) basis may be increasing. There were two elements to this: a declining share of trades in CLS currencies being settled PvP, and also an increased share of turnover in non-CLS currencies. In terms of the former, Alan Marquard (CLS) discussed the potential role played by internalisation as well as trades contracted for same-day settlement and the need for more detailed data in order to properly understand what proportion of these trades could be settled PvP.[1] In terms of the latter, it was highlighted that the vast majority of these transactions are settled without PvP protection and that consideration should be given to the creation of a global solution to this risk. The mitigation of settlement risk in certain non-CLS currencies through local settlement facilities was also highlighted by members.

The GFXC will engage with its member FXCs to consider ways it could assist with gaining a better understanding of trends in settlement activity, perhaps by utilising the semi-annual turnover surveys, and with supporting the management and reduction of FX settlement risk, including reviewing the guidance in the Code. It also agreed to reiterate the importance of minimising settlement risk.

5. **GFXC Work Program**

At its December 2019 meeting, the GFXC agreed to launch five working groups focussing on the key priorities for the Committee's review of the Global Code: buy-side outreach; anonymous trading; disclosures; algorithmic trading and transaction cost analysis (TCA); execution principles. The groups were established in early 2020 and comprised both central bank and market participants. Their work was paused towards the end of March following the outbreak of Covid-19.

[1] CLS shared their publication "CLS Unsettling – The increase of FX without Settlement Risk Mitigation" as background material in advance of the videoconference.

The GFXC agreed to resume this work in the coming months with a view to completing the review of the Code in the first half of 2021. Working group leads provided a short summary of their earlier progress and expected next steps. In particular:

The *buy-side outreach* working group had been exploring ways to make the Global Code and Statement of Commitment even more accessible to buy-side firms. They had continued to make progress on the establishment of a buy-side liaison working group, assessing the feasibility of conducting an impact study to analyse the Code's impact on the FX market, reviewing effective means of engagement, and were soliciting further case studies on Code adoption from buy-side market participants. The *anonymous trading* working group has reconvened and is starting to build upon the work conducted prior to the hiatus. The group has identified specific sub-topics related to anonymous trading as the areas of focus for the review, and has now started to assess each topic in greater depth. The eventual aim of the review is to identify if any enhancements to the Code are warranted with respect to these topics, and if so, to propose specific recommendations. The *disclosures* working group had held discussions with some market participants on the processes they use to produce, use and disseminate disclosures. Building on these discussions, and previous GFXC work, the group had identified a set of key issues in the FX disclosures landscape including challenges around the accessibility and clarity of existing disclosures. The group had started to consider different ways to help facilitate more effective disclosures. Following an information gathering exercise among its members, the *algorithmic trading/TCA* working group agreed in early March to proceed with four workstreams (transaction cost analysis and data availability, control mechanisms and liability, conflicts of interest, disclosure and user education) before its work came to a halt. The *execution principles* working group had been focussing on three principles of the Code: Principle 8 on the capacities in which market participants act; Principle 11 on pre-hedging; and Principle 17 on the use of last look. In particular, following the feedback collected by the GFXC in 2019, the group were considering if there was a need for the GFXC to issue any further guidance or additional examples in these areas.

6. **Wrap up and Next steps**

The Chair summarised the points that had been agreed at the videoconference, noting that the Committee would publish a press statement the following day. The statement would provide a high level summary of the Committee's discussion on trading conditions and operational resilience in FX markets in the wake of the Covid-19 outbreak; touch on the performance of benchmark fixings during the March quarter-end and April month-end; update on the expected timetable for the Code review and provide an overview of the 2019 BIS triennial survey results on FX settlement risk. The next meeting of the GFXC would take place in September 2020 via videoconference.