



EUROPEAN CENTRAL BANK

EUROSYSTEM

Foreign Exchange Contact Group

Frankfurt am Main, Thursday, 6 September 2018, 13:00-17:00 CEST

SUMMARY OF THE DISCUSSION

1. The role of credit in the foreign exchange market – Trends and Solutions – Futurisation, Clearing, Credit Proxies

Carlo Kölzer and Jens Quiram (360T/Deutsche Börse Group) presented their views on the role of credit in the foreign exchange (FX) market. They argued that the credit component in FX transactions has gained in importance following a series of significant changes affecting the FX landscape. These changes have led to a lower number of market participants, an increase in credit costs, lower market liquidity conditions and a high concentration of credit risk, the latter especially seen in the FX prime brokerage space.

There have traditionally been two credit models for spot FX transactions, i) prime broking, and ii) bilateral credit facility. To address the effects leading to reduced credit capacity and enhance safety and efficiency, a multilateral clearing solution for FX spot, forward and swap transactions is being developed.

2. Technological developments – crypto assets

Stephane Malrait (ING Bank), Mark Bruce (Jump Trading) and Andrea Pinna (ECB) made a presentation on the technological developments in crypto asset markets. The Group discussed the emergence of certain crypto assets as well as underlying technological solutions. As an illustration of the industry effort in this domain, Global Digital Finance has recently conducted a consultation on a new global Code of Conduct for crypto assets with a supporting taxonomy.

Some members viewed crypto asset markets as dominated by the retail investor segment, which includes the millennial generation. The investor base composition may contribute to crypto assets' erratic price movements, but also offer profit opportunities which have begun to attract some speculative trading firms. Meanwhile, members discussed that banks have generally not ventured into crypto assets trading at this stage on concerns that there is still a lack of market standards and regulatory clarity around the definition and use of Crypto assets. Moreover, two other issues were mentioned, that crypto assets expose investors to the risk of hacking and that trading which require presence in multiple exchanges can be costly.

3. FX Outlook: Review of Foreign Exchange markets developments and outlook

Tobias Helmersson (ECB) presented the recent global FX market developments while Alan Stewart (Goldman Sachs International) focused on an analysis of FX developments in China. The US dollar had been strengthening against a basket of currencies since the end of April 2018 on the back of continued US-China trade tensions, strong US economic performance and continued normalisation of US monetary policy. Despite the Chinese renminbi's underperformance and volatility over the summer, capital flows were seen as more stable than in previous episodes as officials have implemented successive measures since 2015 and the market have become structurally more mature.

The Group discussed the latest episode of volatility in selected emerging market currencies, with the fallout expected to remain largely idiosyncratic and contained. Some members saw this development as distinct from the environment prevailing during the Global Financial Crisis in 2008 when increased volatility affected all markets and led to broad based risk off scenarios. Other members linked the recent appreciation of the Swiss franc against the euro to the ongoing fiscal policy discussions in Italy. Finally a few members reported that over the recent weeks the substantial short positioning in the British pound had recently been scaled down as a potential adverse outcome in the negotiations of the United Kingdom's withdrawal from the EU was seen as more fairly priced in.

4. FX Global Code and Global Foreign Exchange Committee

Roswitha Hutter (ECB) introduced the ongoing work of the Global FX Committee (GFXC). One year after the FX Global Code's (the Code) launch, the GFXC noted an overall positive market reception with well above 300 Statements of Commitment available in public. Still, the GFXC recognised that the adoption of the Code had been skewed to the sell-side institutions and set as a priority for the upcoming year broader awareness and adherence by buy-side market participants.

Overall members agreed that the Code is fostering further transparency in the FX market. In that respect, some members had seen indications of market participants being offered greater transparency, in turn improving counterparty relations as market participants adopted the principles of the FX Global Code. Members also discussed the role of trading venues in case of disputes between market players. Even if venues monitor activities on their platforms, due to their heterogeneity, it was felt that a single point of arbitration for the industry was both unlikely to emerge and possibly an inappropriate solution. Instead, encouraging transparency and disclosure, active dialogues between counterparties and robust internal compliance procedures are deemed to be more effective means to solve disputes and promote good market practice.