FX Global Code of Conduct Launch

Panel debate presented by the GFMA Global FX Division

Global Financial Markets Association
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Introduction

To mark the launch of the FX Global Code of Conduct on 25 May 2017, the GFMA's Global FX Division, in conjunction with the Investment Association, the ACI and a number of other trade bodies, hosted an evening panel session in London with some of the leading figures behind the development of the Code.

The Global Financial Markets Association (GFMA) represents the common interests of the world's leading financial and capital market participants, and speaks for the industry on the most important global market issues.

The complete FX Global Code of Conduct is a set of global principles of good practice in the foreign exchange market. It was developed to provide a common set of guidelines to promote the integrity and effective functioning of the wholesale foreign exchange market. It is intended to promote a robust, fair, liquid, open, and appropriately transparent market in which a diverse set of market participants, supported by resilient infrastructure, are able to confidently and effectively transact at competitive prices that reflect available market information and in a manner that conforms to acceptable standards of behaviour.

The GFMA's Global FX Division is fully supportive of this initiative. Given that foreign exchange underpins international trade and investing, a single, global code provides a common reference point to encourage good practice and re-build public confidence in the FX market.

The GFMA is pleased to provide the following summary of the May 25 panel discussion.

Further information, together with video highlights from the event, is available on:
gfma.org/initiatives/Foreign-Exchange-(FX)/Foreign-Exchange-(FX)/

Moderator:

James Kemp
Managing Director
Global FX Division of GFMA

Panellists:

Guy Debelle
Deputy Governor
Reserve Bank of Australia

Simon Potter
Head of Markets
New York Federal Reserve Bank

Chris Salmon
Executive Director, Markets
Bank of England

Adrian Boehler
Global Co-Head of FXLM
and Commodity Derivatives
BNP Paribas

James Kemp (JK): Can you give us a recap of the global code story so far?

Guy Debelle (GD): The foreign exchange industry has faced a deficit of trust over the last few years. As a result, the central bank community was commissioned by the BIS Governors to develop the Global Code of Conduct. The production of the Code was a public-private exercise where the central banks worked with the private sector and the market participants group, chaired by David Puth, Chief Executive Officer at CLS.

The FX Global Code is firstly a *single* code, replacing existing codes which have been released across the various markets and it is also a *global* code that involves all the top 16 FX trading centres in the world.

Alongside the Code, we have also published our blueprint for adherence, and launched the Global Foreign Exchange Committee (GFXC), a newly constituted body. Chris Salmon, Executive Director for Markets at the Bank of England, is the Chair of the new Committee, with David Puth acting as Vice Chair. A key objective of the group will be to ensure that the Code remains up-to-date.

JK: The first phase of the Code covered issues such as ethics, information sharing, execution, confirmations and settlement. What have been the focus areas of Phase 2?

Simon Potter (SP): The second phase of the Code has covered four areas: execution, governance, risk and compliance. We wanted to make sure that the new Code is dynamic and places emphasis on some of the issues that are top of mind to many in the FX industry, such as electronic trading and last look.

Additionally, we wanted to include examples in the Code. Examples are hard to get exactly right so we formed a working group to ensure that they would speak not just to traders but to everyone in the industry. We want people to think through those examples to help them further understand the underlying principles behind the Code. This is not a checklist - it is for you to think how to support an FX market that is robust, liquid, fair and open to all participants.

Adrian Boehler (AB): That's the beauty of having the Code written by market practitioners for market practitioners – it's real, it's written in language we can all easily understand and the examples take it a step further, to really bring the principles and the practices to life so we see what that looks like in our daily jobs, wherever we sit in the industry. Some of the examples are written with specific roles in mind, but they should be interpreted as applying to all market participants and not just a particular role or client segment.

JK: Let's address perhaps the most controversial issue – Principle 17 on last look. Can you take us through why last look was such a challenge, and how you reached the text as it stands?

SP: What the industry is essentially trying to do is work together to give guidance and apply best practices. We want this to be in areas that are relevant right now, including last look. Last look is an extensively debated issue and a lot of time was spent writing this principle - it is one of the longest principles in the execution section.

Last look is primarily a risk control mechanism, so clients need to understand how a particular provider is using it as such. This is an area where incentives can be a problem, for example where there is an option that is being offered to the person providing that service to accept or reject an order that has not been priced correctly. That can lead to problems and we are very careful to articulate in the latter part of that principle what those problems can be. For example, it is completely inappropriate to use last look to gather information with no intention to trade. If, when utilising last look, there is a belief that you can more efficiently execute an order by doing some related in the last look window, it must get past two tests: what is it that you need to do, given how recent that price is, and if you do not execute, how can you get the client in a good position? It's very hard to pass those tests and that made us think that trading in the last look window is probably not going to benefit the client.

JK: We know that Principle 17 is being consulted on – when are we likely to see the output from that?

Chris Salmon (CS): There was debate on the issue around trading in the last look window about whether or not 'likely' is the correct language for Principle 17. This was one area where the newly-formed Global Foreign Exchange Committee could play a role, by initiating a more public consultation to try and get further information from the widest range of market participants about that particular aspect of last look.

We have launched a consultation today specifically on trading in the last look window. We want people to send in their reactions and their feedback, anticipating any input to be made public. The consultation runs to 21 September 2017. The Global Foreign Exchange Committee will then come together during the fourth quarter of this year, look at that feedback systematically, and reach conclusions.

GD: To that point, any of the Code's principles may need to evolve in the future as the market changes. Last look happens to be the one that is being debated and in a state of flux at the moment. However, in 12 months' time there might be another aspect which will be worthy of going through the same sort of process.

JK: It all sounds as though there have been some really challenging topics - on some of which views greatly differ across the industry. What has your experience been of bringing market participants together though the Market Practitioners Group (MPG) to get consensus?

AB: Personally, I've been very impressed throughout the process by the degree of engagement from market participants. The discussions have always been constructive and respectful and opinions have been listened to. The construct of the MPG is also very important. It is not just the sell-side representation on the MPG, there is a healthy cross section of all segments.

Moreover, the FXWG and the MPG received over 10,000 comments over the two drafting phases and I can attest to the fact that the MPG went through every single one of those comments line by line. The industry has been given an opportunity to voice its opinion and it has.

When it comes to forming consensus, particularly on some of the hottest topics, there has been a huge amount of debate, particularly on Principle 17, and the MPG thought it was appropriate to settle on less granularity and prescriptiveness than perhaps individual participants might have wanted, for the greater good of the Code. What that does not prevent is individual market participants requesting or seeking a greater degree of implementation or interpretation of a particular principle or practice in their bilateral discussions with their counterparties and, if nothing else, the Code definitely gives a comprehensive framework for having those discussions.

JK: The code has a very clear focus on increasing transparency and disclosure and we've seen a number of disclosure statements in the last two years. How would you like to see those disclosure statements now reflect the Global Code?

GD: Those statements should be consistent with the Code. To be able to say that you're committed to the Code and adhering to the Code, the communication you should be having with any of your counterparties should be completely consistent. And the easy way to be consistent is to use the same language.

SP: When you receive a disclosure statement as a client, you should be reading through it and feel comfortable that you understand it and reading through the Global Code alongside it will be helpful. One of the things we want people to do is ask questions so they understand exactly what services are being provided. The responsibility of the buy-side to do so is reasonably critical. The buy-side have to be very active participants in improving the FX market: if they are just accepting the services and not asking questions, that will not help us achieve the goals of the Code.

JK: In addition to the topics we've just discussed, Phase 2 has involved a dedicated workstream on adherence. Can you take us through the 'Statement of Commitment', and why you opted for that approach?

CS: The goal was to develop a Code of Conduct which improves integrity in the market. For that to happen, it has to be adopted by a wide range of market participants across a broad range of jurisdictions, whilst recognising this is not regulation, it is a voluntary code. The blueprint published today sets out the four tenets that underpin steps towards widespread adherence.

The first is the most obvious one - the Code itself needs to provide clear, relevant guidance which reflects good practice in the FX market and the exercise we have been through over the past two years, which is unprecedented in its depth and ambition to achieve that, leaves us in a situation where the Code published today meets our standard.

The second makes it is the responsibility of market participants to take that Code and to embed it into their systems and processes, so that they are following the guidelines. As an Annex to the Code, we have developed a short Statement of Commitment which firms can use to demonstrate to their clients that they have taken those steps and are acting in a way that is consistent with the Code. What we hope is that, through time, firms across the market will choose to make those statements and will expect their counterparties to do the same. If we can move to a world where there is an expectation that firms are following the Code and demonstrating it, that will create confidence in the market that there is widespread adoption.

The third is that the central banks themselves will take leadership in trying to facilitate that process.

The final tenet will be to make sure that the Code stays up-to-date as the market moves forward. The Statement of Commitment is very important as an element in the blueprint that we have for adoption. For firms, it is the part that they can contribute to, by thinking about their behaviours and whether they are working in a way that is consistent with the Code.

JK: Are there any plans for central banks or regulators to audit firms' compliance?

CS: That is not something that has been mandated. For some market segments, market players might want to seek a third-party perspective, i.e. for their own purposes or to be able to demonstrate to their counterparties. The GFXC will create a global index of registers where people can collect the statement of commitments that they have made, so that they are easily searchable and where people can see which firms have signed a statement of commitment relevant for the market segment that they are working in. In the next couple of months, the GFXC will publish the guidelines around this.

JK: What plans are firms themselves making?

AB: It is going to be down to every single market participant to interpret the Code in the context of their own business because it must be proportionate: how a large sell-side participant adheres versus how a less frequent or more casual user of the foreign exchange market adheres are going to be very different.

The adherence workstream within the MPG was acutely conscious of making sure that, on the one hand, we had a credible adherence framework and that, on the other hand, we captured the largest possible audience of market participants. It will be the responsibility of individual market participants to read the Code, see how the principles apply to their own business and choose the best way forward to adhere. For large sell-side market participants, the feedback suggests that one of the challenges is knowing which entity should sign. This is because large sell-side market participants or complex financial institutions have foreign exchange activity warehoused in different entities. Is it one statement of commitment or is it possibly a few to reflect the different activities under the umbrella of the group?

JK: How does the Global Code of Conduct fit with the Senior Managers' Regime? – what is the UK position?

CS: The Code is not regulation in the UK. The FCA has been consistent for over a year that it sees the Code providing relevant guidance about what good market practice is in the FX market. If you look at the Senior Managers' Regime, it talks about ensuring that firms follow generally accepted market standards. So the Code is an input that enables the FCA to consider how Senior Managers fulfil their responsibilities. One of our challenges has been to develop a single code that can work in many different jurisdictions, so we have been agnostic about how market supervisors in different jurisdictions will choose to take account of the Code in their region.

JK: Where are the 'teeth' outside of the UK?

SP: The Code is not regulation, it is a voluntary code. We use best practices often in the United States and they have been very successful. From a US perspective, the Code is a supplement to the regulatory and supervisory regime we have. The 'teeth', particularly in the treasury market, is reflected by the relationship the New York Fed has with its counterparties. The participating central banks have been clear that we will be committing and adhering to the Code, and that we expect our counterparties to do so. In addition, we expect all the members of our best practice groups to be adhering to the Code. We have found that to be a very effective supplement to regulation and supervision.

JK: How do we get the message out to the broader market?

SP: The membership of the GFXC is very diverse, and once you have a significant mass of people who are following the Code, the market itself will enforce some discipline. That's something that we will all expect to happen and we believe the Code is going to prove useful to people. It will establish some of the trust and integrity, not only amongst the public but the people in the wholesale market themselves. However, there is no way that this Code or any regulation will prevent a single person or a group of people from violating law or exploiting some loophole. What we want is for the industry, as a whole, to be more aware of when that might be happening in order to address it as soon as it occurs.

JK: Does the buy-side have a perception that much of the Code is focused on sell-side practices? How do they figure out which provisions are relevant to them, and which are not?

GD: We make it clear in the Code that proportionality matters. It depends on the nature of your engagement in the market as to how much of the Code is directly relevant to your own operations. The relevance to a corporate treasurer, for instance, is that the Code is a guide as to what they should be expecting when they are interfacing with the foreign exchange market and that's where the value is to some of those segments of the market.

AB: Awareness has increased. For example, we received 4,000 comments in Phase One and 6,000 in Phase Two. It can be argued that a part of that is because of the contentiousness of last look in Phase Two, however, we also had the topic of 'agency versus principal' in Phase One which was not a small discussion either. This demonstrates that awareness and a desire to participate in the discussion is clearly improving.

JK: What positive changes are you already seeing from the industry?

AB: There are many, but two changes that I would highlight. The first one is around information sharing. You will recall when the MPG got together for the first time in New York in January 2016 we were given the list of topics on which the FXWG wanted input. We felt that noticeable in its absence from that list was the subject of information sharing. At the time, the MPG acutely sensed the paralysis when it came to the dissemination of market colour, because of all the investigations. So in May 2016, alongside the delivery of Phase One, guidelines and principles around safe information sharing was released and that has already unlocked the paralysis. Information and market colour is flowing much more efficiently then it has done in the past and that is a major step in the right direction and key to efficient functioning of the market.

Secondly, disclosure statements are becoming much more common practice for market participants, to explain how they operate. Transparency is at the heart of the Code so that is a huge step in the right direction. The Code certainly gives market participants the framework for requesting, or, in some cases, challenging for, more transparency if they are not comfortable with what they observe from other market participants.

GD: One of the positive changes is ensuring a common understanding of what good practice is, which was not there before. People had their own views as to what good market practice was and often in some cases they were fairly aligned but in other cases not so much. One of the main benefits is setting out that collective judgement from a broad range of perspectives as to what constitutes good practice in the market and that allows those conversations to happen in a much more effective way than they would have in the past.

CS: One of the most common themes from one of our recent FX Committee meetings was that the process of developing the Global Code made all the regional Committees think about their composition and membership. The FX Committees themselves have been changed by the process of developing the Code and its recognition, as well as the thoughtful dialogue about what good practice means, which can help us come up with better guidance.

The FX Global Code of Conduct is accessible at: http://www.globalfxc.org/fx_global_code.htm

Note: This live discussion was edited for brevity and clarity.

About the speakers

James Kemp
Moderator

James Kemp is the Managing Director of the GFMA's Global FX Division, having established it in 2010. He also established AFME's Technology and Operations Division in 2016, and more recently took management responsibility for the Compliance, Tax and Accounting Committees which he has merged to form the new Policy Division. He is heavily involved with efforts to enhance industry conduct, having been involved in the Global FX Code work and as a Board member of the UK's FICC Market Standards Board. He sits on the Bank of England's FX Joint Standing Committee.

James has previously been a business strategy consultant at The LEK Partnership; working out of London and Chicago, as well as UK Head of Equities and Fixed Income Products at Reuters. He was the founder and managing director of the financial markets technology consultancy, Stentra, a market leader in FX e-trading, as well as commodities, fixed income and swaps.

Guy Debelle
Panellist

Guy Debelle is the Deputy Governor of the Reserve Bank of Australia, a position he has held since September 2016. He is Deputy Chair of the Reserve Bank Board and Chair of the Reserve Bank's Risk Management Committee. Dr Debelle is also Chair of the Australian Foreign Exchange Committee and Chair of the BIS Foreign Exchange Working Group developing the Global Code of Conduct for the Foreign Exchange Market.

Prior to his current role, Dr Debelle was the Assistant Governor (Financial Markets) at the Reserve Bank of Australia. Prior to that, Dr Debelle also worked at the International Monetary Fund, Bank for International Settlements, Australian Treasury and as a visiting professor in economics at the Massachusetts Institute of Technology (MIT).

Simon Potter
Panellist

Simon Potter is the Head of the Markets Group at the Federal Reserve Bank of New York. His main research area is applied time series analysis using Bayesian methods.

Simon has written extensively on nonlinear dynamics over the business cycles. Recent topics have included forecasting the probability of recession, large panel forecasting models modeling structural change and inflation expectations.

Chris Salmon
Panellist

Chris Salmon has been the Bank of England's Executive Director for Markets since June 2014. He is responsible for all Bank operations in financial markets; management of the Bank's balance sheet and the UK's official foreign exchange reserves on behalf of HMT; and delivering market intelligence for monetary and financial stability.

Chris has worked at the Bank for over twenty years, and recent previous positions include Executive Director, Banking & Chief Cashier (2011 – 2014) and Private Secretary to then Governor, Sir Mervyn King (2006-2009).

Adrian Boehler
Panellist

Adrian Boehler is the Global Co-Head of FXLM and Commodity Derivatives at BNP Paribas. Adrian is a member of both the European Central Bank's FX Contact Group and of the Bank of England's FX Joint Steering Committee. He is also a member of the Market Participants Group that has been working alongside a number of central banks globally on the FX Global Single Code of Conduct.

Prior to BNP Paribas, Adrian worked at HSBC Bank plc as Head of Foreign Exchange Sales, EMEA, and in that role was responsible for the distribution of FX to all client groups – Institutional, Corporate and MME/SME. He joined HSBC in June 2004 from Goldman Sachs where he had spent 10 years in Institutional FX Sales working in London and also Hong Kong during the Asian currency crisis in 1998.

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