

# GoC Market Functioning Steering Group – Terms of Reference

## Background

The Financial Crisis was followed by a period of persistently low interest rates in many jurisdictions. Low interest rates provide diminished financial incentives to deliver fixed-income securities for timely settlement. In response, several jurisdictions, including the US, the EU and Japan, have adopted measures that incentivize the timely delivery of securities for settlement.

The Bank of Canada’s comprehensive post-crisis analysis suggests that Canadian financial markets can generally function at low rates, but that additional measures may be needed to support repo market functioning.<sup>1</sup> The Bank’s research further documents that a price cap exists in the market for borrowing Government of Canada (GoC) securities.<sup>2</sup> As in other jurisdictions, this price cap limits the financial incentives to deliver the securities for timely settlement, which could dampen the well-functioning of GoC markets. The cap also potentially disincentivizes market participants from supplying fixed-income securities through the securities lending market to support market functioning.

The Bank presented its work on the price cap in GoC markets at the April 2019 CFIF meeting.<sup>3</sup> CFIF supported considering the development of a framework for market well-functioning in a low-rate environment. CFIF subsequently sponsored an in-depth workshop to further discuss GoC market functioning with a broad set of participants. The workshop takeaways were discussed at the June CFIF meeting, and it was agreed that the Bank should conduct additional outreach to assemble a comprehensive picture of settlement frictions in GoC markets.<sup>4</sup> The findings were presented at the October CFIF meeting, where CFIF agreed that a Steering Group should be formed to take next steps.<sup>5</sup>

## Mandate of the GoC Market Functioning Steering Group (GMF)

The GMF’s mandate is twofold:

1. To study a framework for supporting **GoC market functioning in a low-rate environment** (Design Phase) and present design recommendations to CFIF; and
2. Pending endorsement and further direction from CFIF, take steps to implement the framework (Implementation Phase).

The framework’s design phase is expected to investigate: 1) potential mechanisms that provide financial incentives for the timely settlement of GoC trades (such as a fail fee) and that can be applied consistently across the full range of market participants; (2) criteria for implementing/activating the framework; and

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<sup>1</sup> See Witmer and Yang (2016), [Estimating Canada’s Effective Lower Bound](#).

<sup>2</sup> See Berger-Soucy, Fontaine and Walton (2019), [Price Caps in Canadian Bond Borrowing Markets](#).

<sup>3</sup> Available at: <https://www.bankofcanada.ca/wp-content/uploads/2019/04/09-Apr-19-CFIF-presentation.pdf>

<sup>4</sup> See workshop debrief at: <https://www.bankofcanada.ca/wp-content/uploads/2019/06/GoC-market-functioning-workshop-Debrief-June-4-2019.pdf>.

<sup>5</sup> See outreach findings at: <https://www.bankofcanada.ca/wp-content/uploads/2019/11/goc-market-functioning-framework-industry-october-16-2019.pdf>

(3) complementary policies or market practice changes that seek to improve market functioning and mitigate any potential unintended consequences.

## Organization

- The GMF will comprise senior members in the Canadian financial industry that have an excellent understanding of at least one of the following: (1) the functioning of GoC cash or securities financing markets; and (2) GoC settlement processes and infrastructure.
- The GMF will be co-chaired by a senior representative of the Bank of Canada and a CFIF member.
- In addition to the co-chairs, the GMF will comprise 9-11 members. Membership composition should broadly reflect the various stakeholders in the GoC market, include relevant industry associations (IIAC, CBIA and CASLA), and may incorporate a limited number of additional (non-voting) members, including from the official sector. Changes to the size or composition of the GMF will be at the discretion of the co-chairs.
- Members represent their firms and are expected to:
  - Dedicate the necessary time and resources to the work of the GMF;
  - Lead and/or participate in working groups formed to focus on specific issues;
  - Have sufficient authority to commit their firms' support and endorsement of the GMF's activities;
  - Communicate issues identified to their senior management;
  - Aim to achieve outcomes that improve the overall efficiency and well-functioning of the Canadian financial market;
  - Attend all regularly scheduled meetings in person or in special cases via video conference; and
  - Be aware of their obligations under the Competition Act and avoid the disclosure of any competitively sensitive information. Members should inform the co-chairs if they become aware of any Competition Act concerns that arise from the GMF's discussions.
- Decisions taken by the GMF should be made by consensus, but in the event of an inability to reach consensus, decisions will be made with a simple majority, where each GMF member will have one vote.
- The GMF may form ad-hoc working groups to focus on specific issues, such as the infrastructure and technical requirements for fail fee computation and payments, and legal implications. Working group composition can be broader or narrower than the GMF's individual members or member institutions and will take into account the relevant required expertise.
- Working groups will be co-chaired by at least one GMF member.
- Working groups will report their assessment and/or recommendation to the GMF on a regular basis for discussion and approval.
- The GMF will update CFIF on its progress on a regular basis. It will also seek feedback from a wide range of stakeholders to create the transparency necessary to achieve broad consensus around the GMF's proposals. Feedback channels could include targeted industry roundtables and the publication of consultation papers.
- The GMF and any working group will meet as required. Meetings will be held either at the Bank of Canada office in Toronto, or at a member institution.
- The Bank of Canada will provide the secretariat function to the GMF.
- Working groups' secretariat functions will be the responsibility of the respective working group chairs.