Minutes of the Canadian Foreign Exchange Committee

11:00 – 13:00
15 February 2022
Video conference call

Present:
Stephen Best, Refinitiv (substitute)
Christine Bourgeois, Caisse de dépôt et placement du Québec
Dagmara Fijalkowski, RBC Global Asset Management
Lorne Gavsie, CI Global Asset Management
Tom Gillie, RBC Capital Markets
William Kellett, Scotiabank
Sharon Kim, TD Securities
Russell Lascala, Deutsche Bank
Martin Legault, National Bank Financial
Jim McCrindle, Bank of America
Manuel Mondedeu, CIBC World Markets
Charles Perreault, Department of Finance, Canada
Gaétan Reid, State Street Global Markets
Elizabeth Steele, HSBC Bank Canada
Miro Vucetic, Citibank
Simon Watkins, BMO Capital Markets

Grahame Johnson, Bank of Canada (Chair)
Zahir Antia, Bank of Canada (Secretary)
Harri Vikstedt, Bank of Canada
Thomas Thorn, Bank of Canada
Sean Durr, Bank of Canada

External speakers:
Elsa Lignos, RBC Capital Markets

The meeting was conducted as a video conference call.

1 Adoption of Agenda

The Committee adopted the agenda as written. The Chair welcomed Elizabeth Steele from the HSBC Bank Canada as the new CFEC member.

2 FX market outlook

Ms. Elsa Lignos, Global Head of FX Strategy at RBC Capital Markets, presented the firm's outlook for currency markets. She noted that since the end of 2021, interest rate differentials have become a key driver of moves in exchange rates. She highlighted that the sensitivity of the US dollar trade weighted index (DXY) to 2-year nominal interest rates has risen to near historically high levels. Going forward, she expects this trend to continue as the divergence of interest rates between different countries is expected to increase. In her view, there is scope for some modest appreciation of the US dollar as markets price in higher yields in the US.

Ms. Lignos indicated that recent moves in the CAD have been driven mainly by narrowing interest rate differentials with the US and a deterioration in the broader risk sentiment – proxied by the fall in equity markets. Oil prices have had only a small positive impact on the CAD. Members discussed the decline in the sensitivity of the CAD to changes in oil prices. Ms. Lignos suggested that recent rise in oil prices has been driven by supply constraints rather than increased demand, which benefits the CAD less. Some members opined that higher crude oil prices do not necessarily lead to increased investment as the energy sector's share of total business investment in Canada has declined over the years. The growing importance of ESG could further dampen the impact of higher oil prices on business investment, and therefor the CAD.

Finally, members discussed the potential impact of central banks reducing the size of their balance sheets (commonly known as quantitative tightening or QT) on exchange rates.

3 Update on buy-side outreach initiatives

A member from the Bank of Canada updated the Committee on the Bank's ongoing outreach efforts to raise awareness of the Code amongst buy-side firms. He welcomed the news that two large pension funds have recently signed the Statement of Commitment. He also informed members that the Bank of Canada participated in a panel discussion with other central banks to promote the benefits of the Code. The Bank of Canada will continue to engage bilaterally with large buy-side firms to encourage them to adopt the Code.

4 The future of CDOR

Mr. Harri Vikstedt Co-Chair of CARR provided a summary of the recent White Paper on the Future of CDOR. He noted that CDOR, originally developed in the 1980s as the basis for pricing Bankers' Acceptance (BA) related credit facilities, is currently the primary interest rate benchmark in Canada. It is referenced in more than $20 trillion of gross notional exposure across the Canadian wholesale financial system, including in derivatives, bonds, and loans. About 97% of this exposure relates to derivatives, while only about 1% relates to loans.

CDOR is based predominantly on expert judgement and is therefore not consistent with evolving global best-practices for global benchmarks. CARR determined that reforming or enhancing CDOR was not feasible as it would almost certainly result in a benchmark that was both legally and economically different from what CDOR is today.

As a result, in December 2021, CARR recommended that Refinitiv Benchmark Services (UK) Limited (RBSL), the administrator of CDOR, should cease the calculation and publication of CDOR after June 30, 2024. CARR proposed a two-staged approach to the transition from CDOR. The first stage would run until June 30, 2023, by when all new derivative contracts and securities are expected to have transitioned to using CORRA, with no new CDOR exposure after that date except with limited exceptions. The second and final stage would end on June 30, 2024 and would provide firms with additional time to transition their loan agreements and deal with potential issues related to the redocumentation of "legacy" securities.

He highlighted that RBSL recently published their consultation for the potential cessation of CDOR and encouraged members to provide any feedback to the consultation.

5 2022 BIS Triennial Survey

The Secretary provided an overview of the 2022 BIS Triennial Survey. This is the thirteenth survey conducted by the BIS and is comprised of two unique surveys. The first collects data on turnover in FX and OTC derivatives markets. The second survey collects data on the outstanding notional amounts and gross market values of foreign exchange, interest rate, equity, commodity, credit and other OTC derivatives contracts. He highlighted the key timelines and changes to the 2022 turnover survey from previous years.

6 GFXC workplan

The Chair informed members that the GFXC was looking for feedback on potential workplan topics from local FX committees. Members were asked to provide suggestions on other workplan topics to the Secretary, which will then be sent to the GFXC leadership for consideration.

7 Other business

One member provided an update on their firm's plan to join CLSNow.