

Minutes of the Canadian Foreign Exchange Committee Meeting

17 June 2024

12:00 – 14:00

State Street

Present

In-person: Stephane Lavoie, Bank of Canada (Co-chair)
Dagmara Fijalkowski, RBC Global Asset Management (Co-chair)
Stephen Best, Refinitiv
Lorne Gavsie, CI Global Asset Management
Greg Debiene, TD Securities
Gaétan Reid, State Street Global Markets
Miro Vucetic, Citibank
Jean-Philippe Blais, BMO Capital Markets
Matthew Gierke, CME Group
Jian Cao, RBC Capital Markets
Sean Macdonald, Canada Pension Plan Investment Board
Harri Vikstedt, Bank of Canada
Zahir Antia, Bank of Canada (Secretary)

Virtual: Tobias Jungmann, Bank of America
Manuel Mondedeu, CIBC World Markets
Ivan Pelipenko, Ontario Teachers' Pension Plan

External speakers:

Lee Ferridge, State Street

The meeting was conducted in-person with a video-conference option.

1 Adoption of Agenda

The Chair welcomed members and thanked State Street for hosting the meeting. The Committee adopted the agenda as written.

2 Economic outlook

Mr. Lee Ferridge, Head of Multi-Asset Strategy at State Street Global Markets, presented his outlook on the global economy and markets. He noted that since the failure of Silicone Valley Bank in 2023, financial markets have consistently been pricing in rate cuts by the Federal Reserve within the following twelve months. However, at the same time, growth projections in the US have been revised higher. He challenged the widely held view that inflation will fall towards the Federal Reserve's target, and the central bank would lower interest rates this year. He cited three main factors why he believes inflation will remain elevated. First, he expects high wage growth will

continue to put upward pressure on services inflation. This is due to a structural shortage of labour supply driven by demographics. Second, shelter inflation is expected to remain elevated reflecting insufficient housing supply. Third, by some measures, financial conditions are looser than when the Federal reserves started raising rates, and household real net worth has increased by over 30% since the start of the pandemic, which will support demand. He further argued that monetary and fiscal policy remain accommodative despite the current level of the policy rate. While real interest rates have risen, they do not appear to be very restrictive from a longer-run perspective. Even though the Federal Reserve has been reducing the size of its balance sheet, it remains large by historical standards, and continues to be an additional source of monetary accommodation. In addition, fiscal policy is very stimulative as the US government continues to run large fiscal deficits and he noted the risk that this could continue following the outcome of the upcoming US Presidential election.

He expects many other major economies, including Canada, to underperform the US economy as tighter monetary policy is having the desired impact to slow economic growth. However, in his view, the path of US monetary policy rates priced in is not consistent with the economic divergence. He therefore expects the US dollar to remain strong as markets start to price in more a rate divergence between the Federal Reserve and other central banks. He expects the Canadian dollar to weaken modestly against the US dollar but remain resilient against other major currencies as markets already price in more rate cuts in Canada than in Europe and the UK.

Members discussed CAD market functioning. It was noted that volatility in the CAD is extremely low. Moves in the currency have been very muted even on days when macro-economic data has surprised markets. Liquidity has been good with bid-offer spreads tighter than pre-pandemic levels. FX swap funding conditions have also been benign.

3 Preview of the July GFXC meeting

Members discussed issues related to the three-year review of the FX Global Code that will be presented at the July GFXC meeting. A member from the FX Settlement Risk working group provided an overview of some of the changes to the Code with respect to settlement risk that are being considered and the proposed inclusion of a new principle. He noted that the working group's main objectives are to include a "risk waterfall" concept, promote consistent use of agreed settlement methods, and strengthen language around the use of multiple settlement instructions.

Another member provided a summary of the main areas of focus for the FX Data working group. The working group has established two workstreams. The first workstream is focused on increasing transparency on FX data/transactions under delegated execution. The second workstream is exploring ways to increase transparency on the use of data generated by clients on electronic trading venues.

A member of the Motivation for Adherence working group gave an update on the key initiatives to promote adoption of the Code. Finally, members discussed the possibility of inserting links to the existing GFXC guidance paper on pre-hedging to Principle 11.

4 Growth of CME FX futures volumes

Matthew Gierke, the representative from CME presented on the growth in volumes of FX futures. He noted that FX Futures volumes have grown at an annual rate of 8% over the past three years, even as FX volatility has declined to levels last seen in 2021. Average daily volumes of FX futures are over \$80 billion this year. The number of participants having at least 400 open contracts in major FX currency pairs and at least 100 open contracts in Emerging Market pairs reached a record high in April 2024. The growth has been driven by increased adoption of FX futures by asset managers. However, he emphasised that cash primary venues remain an integral part of the FX market and support liquidity during periods of market volatility. He highlighted the growth in volumes on FX link, a central limit order book on CME Globex for trading spreads between OTC FX Spot and CME FX futures. Finally, he noted that CME will be launching a new product known as FX Spot+, which will provide participants the ability to implicitly access FX Futures liquidity in spot terms within a firm, anonymous and all-to-all central limit order book.

5 Member's feedback on T+1 settlement

Members discussed the transition to T+1 settlement for securities which took place on May 27, 2024. Members agreed that the transition went smoothly with no significant issues. One member indicated that some clients using its electronic platform have requested that the rollover time be moved from 5pm ET to 6pm ET to allow more time to enter FX trades to facilitate T+1 settlement.

6 Other business

The next meeting will be held on September 24th.