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FX Market Needs Global Code of Conduct: Ethical Banker

The financial market's need for clearly defined global principles that govern behaviour and ethics has never been more pronounced and the ACI Model Code could act as the bedrock for a formally adopted global standard, says Marshall Bailey.

The last 18 months has seen foreign exchange markets come under unprecedented public and regulatory scrutiny, with six banks collectively fined billions of dollars by regulators over some traders' misconduct around FX benchmark fixes. With a renewed focus on the self-regulating nature of the FX markets, there has never been a greater need for a set of clearly defined principles and guidelines that govern the behaviour and ethics of market professionals to be adopted universally.

ACI's Model Code, first presented in this form by ACI's Committee for Professionalism in 2000 and updated regularly since, defines the principles and ethics that professionals should adhere to in order to uphold market standards globally. It also makes a clear statement about the responsibilities of management and supervisors to ensure that codes of conduct are observed. The Model Code is backed by a number of central banks and FX committees.

"By implementing these standards, financial markets demonstrate their work to regain public trust in its institutions," says Marshall Bailey, President of ACI – the Financial Markets Association. "More progressive banks and clients have already decided to return to the ACI Model Code, and are showing leadership. We provide a moral compass and a global standard to which all professionals can adhere, regardless of institution, market segment or region."

Bailey, who was inaugurated as ACI's first full-time President in March this year, adds, "We have made a huge amount of progress and the entire set of global councillors is behind the strategy and the vision that I laid out at the ACI World Congress in Berlin.

"It is a vision of self-certification for the industry that revolves around ACI's ability to deliver best practice specifically in ethical conduct, and the way in which people participating in the wholesale financial markets need to behave. Training must be provided, and tests to certify understanding must be available. The more we look at the way in which global regulators have taken a view on the problems in the market, the more convinced we are that this vision is the right one.

"With sufficient backing and global enforcement, the ACI Model Code can act as the logical bedrock for a formally adopted global standard, governing behaviour and ethics across financial markets," he continues. "The use of a single, globally recognised, industry-wide, unbiased code, that addresses the specific issues of the foreign exchange market will provide a tremendous amount of value."

Bailey's comments come after misconduct at some of the world's biggest FX banks was laid bare. Regulators in the UK, the US and Switzerland imposed $4.3 billion in fines on six banks for failure to control business practices in their G10 spot trading operations. It remains unclear if other banks will be named in future announcements from these and other global regulatory bodies.

At the heart of the matter is the behaviour and ethical conduct of individual participants, who disclosed to each other confidential customer order information and trading positions, often ahead of the 4pm London Benchmark Fix, and altered their positions accordingly to benefit the interests of their collective group.

"The improper behaviour that has come to light has no place in financial markets and it is crucial that lessons are learnt from these events to ensure it does not reoccur," says Bailey. "Harmonising rules, guidelines and conduct expected of market participants is imperative if we are to stamp out unethical behaviour. It must also apply across borders, as regional regulation or codes will only result in arbitrage opportunities and create additional uncertainty."

ACI takes the view that the actions of a relatively small, unrepresentative minority should not be seen to reflect the broader health of the FX industry, which plays a vital role in the flow of global commerce. Nor should they trigger wider structural reforms.

"When considering the wider allegations of improper behaviour relating to benchmarks, it highlights the need to shift the emphasis away from prescribed regulation – which is certainly part of the answer but not a panacea – to governing

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human behaviour," Bailey says. "Market participants need to be uniformly educated about what is and isn't acceptable, and be aware that they, as individuals, are responsible for their actions."

ACI responded to the recent consultative document from the Financial Stability Board and will be responding similarly to the UK Treasury's Fair and Effective Markets Review (FEMR) consultation document, aimed at determining what needs to be done to reinforce confidence in the fairness and effectiveness of the fixed income, currency and commodities (FICC) markets.

The review is chaired by the Bank of England, the FCA and HM Treasury. BoE's Minouche Shafik has warned that confidence and trust in FICC markets has been severely damaged as a result of a series of "unacceptable abuses, such as the manipulation of benchmarks".

"Fixing these markets is essential to restore trust – among participants, and among the public. That requires market practitioners to recognise current market shortcomings and engage with each other and the official sector to enact lasting change to create real markets that are fair, effective, and trusted by all," she said.

ACI will be responding, as it did with the FSB, to the FEMR document. "We will also be encouraging our members to respond, both as individuals and through their employers to this," Bailey says. "The output that they will receive from ACI will be global. The fact that we can feed into this in such a constructive fashion is one of the strengths that ACI can bring to the industry."

A Year of Achievement

In discussing the strengths and achievements of ACI this year, Bailey points to the unification of the association's Council around the strategy of self-certification for the industry, as well as its expansion into new countries such as the USA, Ukraine, Zimbabwe, Ghana and Uganda.

ACI America, ACI's association for the North American region, opened for official membership registration in October, launching against a backdrop of rapid regulatory change. Its Executive Committee will represent market professionals spanning FX, interest rates, precious metals, commodities and derivatives and will focus on market practices, education, and technology that other regional bodies under the ACI umbrella have long supported.

In addition to actively promoting the ACI Model Code it will provide pertinent information, insight and guidance on a range of issues and challenges that impact professionals working across the North American financial markets.

"The USA is a hugely important financial market. New York is the second largest foreign exchange centre in the world and while a lot of the banks in New York that participate in foreign exchange are European banks, the large American banks who have been members in London, as well as individuals, can now join from New York. It's a big plus for us," says Bailey.

"We also acknowledge the establishment of the Foreign Exchange Professionals Association (FXPA) and we're happy to work with them. The FXPA is setting itself up in Washington DC to lobby specifically around foreign exchange regulation in the US and we welcome that. We, however, are more focused on best practice and conduct so ACI USA and the FXPA will be working closely together to ensure that the industry is well represented."

Other achievements of the association include a much a stronger media presence and recognition by the market of the good works that the ACI membership does.

"There has never been a time when the association has been so central to so many important things," says Bailey. "Every regulator I have met with agrees and understands the proposition of individual accountability and training, and ACI and is acting upon the need to embed this."

ACI America Launches in New York

ACI – The Financial Markets Association has launched ACI America, its new association for the North American region.

ACI America was officially launched on September 30, with an inaugural opening ceremony at Tribeca Rooftop in New York. More than 300 market participants attended the event, where Carl Weinberg, Chief Economist and Managing Director of High Frequency Economics, offered his views on market structure, regulation and FX valuation. Vincent Sangiovanni, President of ACI America, and Marshall Bailey, President of ACI International, also gave speeches at the event, introducing the new association to the gathered audience and explaining why this is a crucial time for ACI to become active in North America.

"We had a great event, a lot of people turned out for it because they wanted to hear what the new ACI America is all about," says Michael Guarino, managing director of ACI America. "We just felt that it was time for a degree of community to come back into the business and people are eager to talk about the FX market and exchange information."

According to Guarino, the record fines levied against banks for their behaviour in the FX markets emphasises the need for an ACI chapter in North America.

"I've been in the industry a long time and I've been very disappointed in the last year or two about all the things that are going on. There are a few bad apples out there, it's understandable and that's always going to be the case, but the degree to which it was embedded into the market place was surprising. These FX traders had lost sight of what was important and where their priorities and principles should reside," he says.

ACI America will focus on market practices, education, and technology that other regional bodies under the ACI umbrella have long supported.

It will actively promote the ACI Model Code and provide information, insight and guidance on a range of issues and challenges that impact professionals working across the North American financial markets.

"Our Model Code, education programmes and international community of over 13,000 members in 65 different countries are what places ACI - Financial Markets Association in a class of its own. There is no other organisation that was built by professional traders, for professional traders, with a strong global representation anywhere in the world," says Sangiovanni.

"Our main focus is going to be on the Model Code and our educational programmes. One of the ways we will be promoting this is through organising events for our members and other market participants," he adds.

Eddie Tan, the Chairman of ACI International, says that the US financial markets have always played a critical role in the global construct of the financial services industry.

"We are very excited to have ACI America as part of our global family. The new membership will be rewarded with a regional Executive Committee that is fully engaged to provide all the global benefits that ACI can deliver," he comments.

ACI World Congress

MILAN, 03-07.02.2015

Milan Programme Unveiled

Assiom Forex has released the draft programme for the upcoming 54th ACI World Congress in Milan, as well as details of how to register for ACI's premier global function.

The programme provides ample opportunity for networking as well as the chance to interact with a wide range of expert speakers during the business sessions. The event takes place from Thursday February 5 until Saturday February 7 at Europe's largest convention centre, MiCo (Milano Congressi). ACI board meetings will take place in Milan between February 3 and February 5.

The business programme will kick off with remarks from Assiom Forex (ASFX) President Giuseppe Attanà, Carlo Cottarelli, Executive Director of the IMF and Mario Nava, Director General, Internal Markets and Services, Director of the Financial Institution Directorate at the European Commission.

From there the workshop sessions will commence, starting with what is very likely to be a lively discussion, entitled "Currency War, No More!" Stephane Malrait, Chair of ACI's FX Committee will moderate the discussion involving David Lee, Member of the ASFX Committee and Gregorio De Felice, Head of Research and Chief Economist at Intesa Sanpaolo.

This will lead immediately into Workshop Two, "Liquidity Management and ALM Focus 2015", which will look at the funding challenges banks will face in an uncertain interest rate environment. Ilan Jaffè, Co-Chair ALM ASFX Committee, will moderate the session which features Ignazio Angeloni, Director General for Financial Stability, BCE; and Pierfrancesco Zeppieri, Head of Treasury Department, Deutsche Bank Italy.

The afternoon session in Milan opens with two workshops, the first looking at "EM vs DM: A New World Equilibrium". The panel will study China's leadership in helping to reinvigorate global economic growth. Claudia Segre, General Secretary of ASFX will moderate the session, featuring speakers Richard Miratsky, Head of the Corporates Analytical Team at Dagong Europe; Olgay Buyukkayali, Head of EM Research at Nomura International; and Piotr Chwiejczak, CEEMEA Strategist at BNP Paribas.

ACI World Congresses have always been a source of information, networking and education for our members, as well as market authorities and government institutions

Concurrently in a second stream, delegates will be able to partake in a regulatory update in Workshop Four. The session, moderated by ICAP's Director of European Affairs and former ACI President, Godfried De Vidts, will feature Piergiorgio Valente, Chairman, Fiscal Committee of Confederation Fiscale Europeenne, and Marco Castagna Member of the ASFX Money Market Committee. The session will look at the global structure of regulation under new directives such as EMIR, Dodd-Frank, and MiFID2.

The first day's business sessions come to a close with a panel discussion "Fixed Income vs Equity: Scenarios and Impacts on Portfolio Allocations 2015-16". Gabriele Sacerdote, Co-Chair Capital Market ASFX Committee, will moderate a session that will include Don Amstad, Director of Business Development Asia, Aberdeen Asset Management Asia.

After Friday night's networking event, delegates will be eager to hear Saturday's Keynote Speaker, Ignazio Visco, Governor of the Bank of Italy. ASFX is also in the throes of planning other panel sessions for Day Two, as speakers are confirmed they will be released via the Congress website, www.acimilan2015.it.

"We want to give special thanks to the Major Sponsor of the event, Deutsche Bank, that from the beginning shared with us the important commitment for the success of our event," says Giuseppe Attanà, President of ASFX. "Since the very beginning, ACI World Congresses have always been a source of information, networking and education for our members on one hand, and for market authorities and government institutions on the other; as well as being an intensive economic and technical interaction phase covering all segments into international markets.

"For this reason, we are opening with the speech of IMF Executive Director, Mr. Andrea Montanino. The impact of post financial crisis effects have gradually increased uncertainty and volatility both nationally and globally," he adds. "As a result of this, and of the fact that it causes market turbulence, the debate on main market issues becomes even more crucial."

In inviting ACI members to the 54th World Congress, Attanà is keen to stress the level of support from the authorities, noting, "We are honoured to host the first address of the year of our Central Bank Governor, Mr. Ignazio Visco, to the financial community."

FSB Publishes FX Benchmark Reform Paper

The FX Benchmark Group, established by the Financial Stability Board, has published its recommendations over the reform of FX benchmarks. The report, which was commissioned as part of the industry's efforts to recover from the damage inflicted by the allegations surrounding the WM/Reuters 4pm London Fix, was published after a consultation period with the industry.

ACI – The Financial Markets Association participated fully in the consultation process, submitting a detailed response to the call for comment.

ACI was also quick to express its support for the recommendations when they were published, statingthey were a "positive step for the industry" that will provide greater clarity for markets, investors and global policymakers.

ACI's President, Marshall Bailey, says: "The importance and value of these recommendations cannot be understated and is a positive step towards improving the reputation of the FX industry and creating a fairer and more efficient market."

He stresses the need for global coordination in reforming the market to ensure that regulatory and ethical arbitrage doesn't occur. "A code of conduct that applies across all regions should also be introduced if they are to have a real and lasting impact," he adds.

ACI says it agrees with the recommendation of widening the fixing window to five minutes, which it proposed in its response to the consultative paper. "Lengthening the timeframe in which to fix the benchmark rate would limit opportunities for manipulation and make it far less likely that large volumes of business would create distortions in market price," says Bailey.

The report marks the end of the process, which was overseen by Guy Debelle, Assistant Governor, Financial Markets, Reserve Bank of Australia, and Paul Fisher, Executive Director, Markets, at the Bank of England.

The FSB's recommendations for market reform focus on five areas: the calculation methodology of the WM/Reuters 4pm London benchmark rates; recommendations from an International Organisation of Securities Commissions (Iosco) review of the WM fixes; the publication of reference rates by central banks; market infrastructure in relation to the execution of Fix trades; and the behaviour of market participants around the time of the major FX benchmarks (primarily the 4pm Fix).

The FSB's main recommendation is to widen the fixing window beyond the current 60 seconds. The report notes that market feedback suggests widening the calculation window to five minutes for the major currencies, but the FSB recommends that, "WM should determine the appropriate width in consultation with market participants". For less liquid currencies, the board proposes that the window should be wider than for the major currencies.

The FSB also advises that WM should incorporate price feeds and transactions data from "a broader range of sources" to increase its coverage of the FX market during the fixing window.

It supports the development of industry-led initiatives to create independent netting and execution facilities for transacting Fix orders, such as a central utility.

In addition, the report encourages banks to tighten up their internal guidelines and procedures for collecting and executing fixing orders, highlighting the importance of implementing codes of conduct that explicitly detail what level of information sharing between market-makers is or is not allowed.

Importantly, it recommends that fixing transactions should be priced in a manner that is "transparent and is consistent with the risk borne in accepting such transactions", but doesn't designate whether that should be done through a bid-offer spread or a fee structure.

Lastly, it recommends that asset managers, including those passively tracking an index, should conduct "appropriate due diligence" around their FX execution and be able to demonstrate that to their own clients if requested.

ACI Responds

In its submission to the call for comment, ACI welcomed the elevated importance that the Consultative Document placed on the behaviour of market participants. The FSB Consultative Document reflects the need for individual behaviour to be held to the highest standards of ethical conduct, and mentions the ACI Model Code.

ACI stated its belief that the Model Code should be adopted formally by the industry on both the "buy-side" and the "sell-side" and applied across the globe.

As is stated by the FSB Consultative Document, for codes of conduct to be effective they must be adhered to. "The use of a single, globally recognised, industry-wide, unbiased code, that addresses the specific issues of the foreign exchange market will provide a tremendous amount of value to this problem," ACI commented, adding that disseminating the information and training staff on the uses of the sections of the Model Code is a minimum requirement for market participants.

"ACI strongly endorses the application of the Model Code to the benchmarking issues addressed in the FSB Consultative Document," it continued. "ACI also reminds the reader that the Model Code makes a clear statement about the responsibilities of management and supervisors to ensure that codes of conduct are adhered to. Single-platform (company) and national/regional codes may sit alongside a global code, but there should be few (if any) differences in the application of these codes on market practice.

"Any differences increase the risk of ethical arbitrage amongst market participants, and give rise to the issues about which the Consultative Document was written," it added.

In response to specific requests for comment, ACI supported the widening of the window to five minutes and saw no need to change the time of the Fix from 4pm London. It also backed the call for an industry-based solution to netting requirements rather than the establishment of a utility.

On the subject of banks charging asset managers a fee or a fixed spread for executing Fix business, ACI observed, "It is perfectly possible for an agency/fee model based offering to co-exist with a principal-based model, but [ACI is] concerned that clear delineation exists between the two. A risk-based, principal model still provides value for a majority of clients. ACI believes that the "buy-side" should continue to have choice, and will adopt whichever model is required to allow both types to be deployed."

ACIFXC Responds to ESMA Consultation on NDF Clearing

ACI – The Financial Markets Association was part of a major feedback programme to a consultation launched by the European Securities and Markets Authority (ESMA) on the framework necessary for NDF clearing.

In its feedback on behalf of ACI, the association's Foreign Exchange Committee says it "strongly supports" the global initiatives to fulfil the reform programme objectives regarding improved global financial stability and financial markets transparency, which were declared at the 2009 G20 Pittsburgh Summit.

A key component of this reform programme was the proposed obligation to centrally clear standardised OTC derivatives via central counterparties (CCPs), which had been recognised and authorised under the requirements of the European Market Infrastructure Regulation (EMIR).

ACIFXC says it recognises and concurs regarding the benefits that centralised clearing can bring to the OTC derivatives markets in such areas as operational efficiencies and counterparty credit risk reduction.

Whilst noting the variety of uses end users have for the foreign exchange market, the association also warns about the potential for new risks. "ACI's Foreign Exchange Committee recognises the potential impacts and burdens (legal, technical, operational, etc.) of compliance with the on-going regulatory and legislative reform on FX market participants," it states. "Therefore, we would advocate prudence and consideration in that standards introduced to fulfil the implementation of regulatory reform should not cause the emergence of new systemic risks or impact market liquidity."

The association's feedback further notes, citing Bank of International Settlements' data, that FX NDFs represent 2.4% of the average daily turnover of the global OTC FX market, with approximately $2.8 trillion in notional outstanding and approximately $90 billion in market value.

"While concurring that NDFs are treated and defined globally as OTC derivative products and agreeing that mandatory FX NDF clearing would transfer a certain amount of bilateral exposure, which exists between market participants to CCPs, ACI would propose that since the NDF market is substantially smaller than either the OTC IRS or CDS market, the amount of risk in the NDF market is significantly less than for IRS and CDS," ACIFXC states. "Additionally, as reported in the Bank of England FXJSC paper on the Foreign Exchange Market (September 2009), the FX market continued to function throughout the 2008 crisis and operationally the FX market coped well despite occasions of extremely high global volatility and transaction volumes.

"Therefore, we find no evidence that the FX NDF market was a contributory factor to the systemic instability of the 2008 financial markets crisis, the catalyst for the G20 reform programme," it continues.

"Nevertheless, as voluntary NDF clearing is still in its "infancy" (2012) in comparison to IRS (1999) and CDS (2009) and in the likely event of a mandatory clearing obligation for FX NDFs, ACI would advocate an extended, phased approach to the introduction of any FX NDF CCP services to ensure a mature, rigorously tested, robust and stable clearing environment to aid risk mitigation rather than increase systemic risk.

"The Consultation does not address the concern that should a CCP decide to withdraw a clearing service from specific contracts post authorisation and where no other CCP is authorised to offer clearing of those contracts, this would effectively amount to a "trading ban"

Points of Concern

As part of its extensive feedback, ACIFXC also highlighted some specific concerns regarding the proposed framework for mandatory NDF clearing.

ACI notes that the NDF market, as stated in the ESMA Consultation document, has traditionally developed because of some legal or regulatory constraints preventing the offshore settlement of transactions in certain currencies. Additionally, geo-political uncertainty may also facilitate FX NDF contract growth, despite the existence of a convertible currency for a particular country.

As noted in the Consultation document; "the level of standardisation of NDFs has increased as a result of industry initiatives led by associations such as the Emerging Markets Trade Association (EMTA) and the International Swaps and Derivatives Association (ISDA)".

ACI says this has been achieved by the development, acceptance and utilisation of standard market contracts and templates, which contain terms, conditions and provisions to facilitate a robust risk trade lifecycle from execution through to settlement even in the event of a potential market disruption. "Therefore, this standardisation is directly attributable to market-driven and industry-led best practices, which have been identified as supporting appropriately established risk mitigation standards," it asserts.

ACI says it believes that the EMTA template should be adopted without modification by transacting parties, including CCPs, for any FX NDF contract, which is subject to mandatory clearing. In the event that an EMTA template is modified, the standardisation developed by the industry for a given currency pair would be compromised and may result in new risks for market participants.

Additionally, Article 5(4) of EMIR, which proposes the overarching aim of reducing systemic risk, whereby the draft RTS for the part referred to in Article 5(2)(a) of EMIR (i.e. the specification of the class of OTC derivatives that should be subject to the clearing obligation) states that the degree of standardisation of the contractual terms and operational processes of the relevant class of OTC derivatives should be considered:

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ACIFXC. Continued from p.6

"Any modification of the EMTA template would undermine this and the G20 commitment to clearing and trading mandates, which relies on standardisation in contract," ACIFXC says.

Further, ACI notes the current ESMA preferred proposal for counterparty categorisation is a cumulative approach (Option 2) whereby a Category One clearing member for one asset class would also treated as Category One counterparty for another asset class, regardless of whether they are clearing members for this second asset class.

Whilst ACI recognises ESMA's objective for the inclusion of the most sophisticated and experienced counterparties within Category One, its stresses that it regards this as a cause for concern for the following reasons:

- Counterparties would need to organise additional clearing capabilities or join a new CCP as a clearing member
- NDF clearing is less developed than IRS (110 Clearing Members (CMs) over five CCPs) or CDS. There is currently only one authorised CCP clearing NDFs (20 CMs and only two offering client clearing currently)
- The timeframe for admission to the CCP/mandatory clearing is very short (six months after the date of force of the Regulation) and does not take into consideration any potential for legal, technical or any other admission criteria challenges on either the side of the counterparty/CCP or scalability on the part of the CCP.

In conclusion to this point, ACI says that these technological and operational challenges would need to be addressed and overcome before mandating central clearing for FXNDFs begins.

Another specific area of concern raised in the feedback is the "bottom-up" approach triggered by the authorisation of one CCP, LCH to clear OTC FX NDFs.

"Historically, FX NDFs have tended to exhibit limited liquidity as the currency pairs often involve emerging market currencies, while longer tenors are even more illiquid," ACIFXC states in its feedback. "The Consultation does not address the concern that should a CCP decide to withdraw a clearing service from specific contracts post authorisation and where no other CCP is authorised to offer clearing of those contracts, this would effectively amount to a "trading ban". Nevertheless, this would not remove the regulatory clearing mandate. Article 5(6) of EMIR does not cover the potential for a CCP withdrawal of service, rather it only addresses the removal of the clearing obligation in the event that no CCPs are authorised or recognised to clear a particular class of contracts," it adds, arguing that in order to preclude such an event, ACI would advocate that this concern should be addressed by ESMA in order to provide legal certainty to market participants in advance of any introduction of mandatory clearing for FX NDFs.

ACI also says it believes that because, as noted in the feedback, NDFs have tended to exhibit limited liquidity as the currency pairs often involve emerging market currencies, longer tenors are even more illiquid. "Analysis of the BIS Data, as contained within the Consultation Document, confirmed that for all currencies, deliverable or otherwise, the turnover was concentrated for contracts with a maturity below one year," the association states. "The average turnover across currencies of FX forward contracts with a maturity above one year was 4.7%.

"Additionally, the Consultation documentation referenced analysis of DTCC data (NDF only). This dataset revealed that liquidity was concentrated on the shortest maturities. For all currencies except CNY, 90% of the contracts in the sample had a maturity below three months, 98% of the contracts in the sample had a maturity below six months. The share of contracts with a maturity above one year was around 1%, again with the exception of CNY where it reached 2.8%.

"The ESMA proposal to introduce a maximum clearing tenor of two years for the 11 NDF currency pairs to preclude attempts by market participants to circumvent mandatory clearing requirements is, in the opinion of ACI, unwarranted," it continues. "Firstly, as evidenced, the majority of transactions are in shorter tenors as dictated by either commercial requirements and/or lack of liquidity in longer tenors. Secondly, the tenor proposal does not differentiate or take into consideration the diverse liquidity/transactional size of the various 11 currency pairs. Thirdly, given the truncated liquidity in the FX NDF market, in the event of a CCP member (with portfolio exposures beyond one year) default, the CCP would be unable to manage the default process due to lack of liquidity.

"The ESMA proposal to introduce a maximum clearing tenor of two years for the 11 NDF currency pairs to preclude attempts by market participants to circumvent mandatory clearing requirements is, in the opinion of ACI, unwarranted."

Stephane Malrait

The association also points out in its response that the Lehman Brothers default in 2008 was probably greatly ameliorated by the maturity of the IRS clearing offering from LCH SwapClear and the existing liquidity in IRS markets.

"Finally," it continues. "With the phased introduction (2015) of mandatory risk mitigation measures (margin requirements) for non-centrally cleared OTC derivatives, the cost of bi-lateral execution of FX NDFs will, of necessity, make the prospect of NDF clearing more attractive for market participants."

With this in mind, ACI says it encourages the adoption of a shorter currency pair tenor, for example one year, for any mandatory clearing of NDFs.

In the feedback document, ACI also states its belief that considering the legal, operational and systemic challenges that any mandatory NDF directive would involve, ESMA should consider a longer term phased approach to the introduction of mandatory clearing, which should be staggered according to the categorisation of the counterparty. This should be agreed in consultation with market participants and trade organisations and should be harmonised to coordinate and align with the timing of clearing requirements, mandatory trading requirements of other regulators and jurisdictions to avoid the creation of unnecessary market risks.

ACI Clarifies Position on FX Market Structure

ACI has been moved to ensure a correction was made to a recently published in the *Financial Times* entitled "Forex Body Suggests Shift to Exchanges."

This article, and the headline in particular, is a materially inaccurate representation of the ACI's position, and we have complained formally to the newspaper on the grounds of inaccurate reporting. To better reflect the comments made in interview, the *FT* has changed the title of their story, which is now entitled “How to reform foreign exchange trading”

To be clear: ACI – The Financial Markets Association’s policy is that FX and fixed income markets trade effectively at the moment as they are, and serve the industry well.

With the exception of unacceptable recent conduct of a few, these markets continue to serve clients and the economy. By using a combination of OTC, bi-lateral and multi-lateral electronic portals, and exchange trading, end-users in the industry have a number of choices to suit their particular needs.

These choices will undoubtedly be expanded in the coming years as markets continue to evolve. When and if clients see the benefits of a new system or venue, they may migrate in that direction. This has been our history. Exchanges are one of the choices currently available, and used successfully by some. They are by no means the only venue, and much of the market continues to respond to client FX needs through over the counter, including automated trading services.

All markets evolve, and having this combination of choice available remains the best route.

By no means should ACI President Marshall Bailey’s answer to the *FT*’s question on future feasibility of exchange-traded FX be interpreted as an endorsement of mandated change, nor should ACI be understood to be advocating a certain type of trading venue.

As always, we at the ACI – The Financial Markets Association continue to focus on ethical conduct. As we have for decades, we advocate the education of the buy-side and sell-side, as well as the regulators, on industry best practice FX and fixed income markets. Our solution to conduct issues is for the globally accepted, well regarded and widely adopted ACI Model Code be further integrated by market participants, and serve to provide a conduct benchmark against which behaviour can be monitored.

The full interview with comments in context interview is available here: http://podcast.ft.com/p/2399

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Letters

Email: letters.editor@ft.com or
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Forex market serves clients and needs no structural change

Sir, I write with reference to a recent FT podcast (“How to reform foreign exchange trading”, November 17) in which I was interviewed on the topic of the future of foreign exchange trading. The related write-up of my comments in the FT was misleading (“Forex chief concedes scandals likely to force shift to exchange-based trading”, November 18). The ACI, the trade body that I head, does not consider it “desirable” that forex trading moves to public exchanges or is in need of structural change. All markets evolve, and having the current combination of choice available remains the best route. The ACI categorically does not advocate mandating FX trading on to an exchange or any individual trading venue or model.

Despite the widely reported and unacceptable recent conduct of some foreign exchange traders, the FX market remains well structured and serves clients and the global economy well. One of our main goals is the education of the buyside and sellside, as well as the regulators, on industry best practice in FX and fixed income markets. We believe strongly that the solution to conduct issues is the global adoption of a practical ethical code to be further integrated by market participants to provide a conduct benchmark against which behaviour can be monitored.

The organisation I am proud to lead represents 13,000 members across the global financial services industry with a focus on professional and ethical standards and conduct. Currently the market is made up of a combination of over-the-counter, bilateral and multilateral electronic portals, and exchange trading provides counterparties with a number of choices to suit their particular needs for investment, speculation, risk management and hedging. These choices will undoubtedly be expanded in the coming years as markets continue to evolve. When and if clients see the benefits of a new system or venue, they may migrate in that direction. Exchanges are one of the choices currently available and used successfully by some. They are by no means the only venue and much of the market continues to respond to client FX needs through OTC trading, including automated services.

Marshall Bailey
President, ACI Financial Markets Association International, Paris, France

UK Launches Market Review

The Fair and Effective Markets Review (FEMR) established in June by UK Chancellor George Osborne and Mark Carney, Governor of the Bank of England, has launched a consultation aimed at determining what needs to be done to reinforce confidence in the fairness and effectiveness of the fixed income, currency and commodities (FICC) markets.

It follows the end of a separate consultation period on 23 October, which proposed extending the existing criminal offence of making false or misleading statements in relation to London Interbank Offered Rate (Libor) to cover other key financial benchmarks, including the WM/Reuters Fix.

The joint review is chaired by the BoE's Deputy Governor for Markets and Banking, Nemat Minouche Shafik, with Financial Conduct Authority (FCA) CEO Martin Wheatley and Director General, Financial Services, HM Treasury, Charles Roxburgh acting as co-chairs.

In a bid to have a lasting impact, the review now intends to focus its final recommendations on what it determines to be a “core range of high priority actions” and identify potential structural and conduct solutions.

Shafik warns that confidence and trust in the FICC markets has been severely damaged as a result of a series of “unacceptable abuses, such as the manipulation of benchmarks”.

“Fixing these markets is essential to restore trust – among participants, and among the public,” she adds. “That requires market practitioners to recognise current market shortcomings and engage with each other and the official sector to enact lasting change to create real markets that are fair, effective, and trusted by all."

Much of the remainder of FEMR looks at how to deal with a market that is essentially wholesale and global in nature, and therefore does not fall under regional regulations, industry observers believe.

Responses to the review's list of are sought consultation questions by Friday 30 January 2015.

Osborne adds that the integrity of the City matters to the economy of Britain and he is determined to deal with abuses, "tackle the unacceptable behaviour of the few" and ensure that markets are fair for the many who depend on them.

"I want to make sure it is done in a way that preserves the UK's position as the global financial centre for many of these markets, with all the jobs and investment that brings," he says. "The consultation that FEMR has launched today is comprehensive, balanced and rigorous, and asks all the right questions. I look forward to the review's final recommendations in June next year."

FEMR adds that is conscious of the global scope of the FICC markets and that they are "shaped by forces far wider than those in the UK alone".

"Much has been done to tackle the underlying causes of past misconduct, but the perception remains that too often private interests are placed ahead of fair competitive markets," says Wheatley. "Rebuilding trust in these markets will take time and requires firms and the authorities to take action, both at the UK level and internationally. Given the essential role of these markets, it is vital that we get this right."

In each case, the review says it will need to evaluate the extent to which change is either for the industry (which has the capacity to act globally) to implement, or for the UK authorities or for wider discussion with the international authorities.

It plans to make its final recommendations in June 2015.

FSB Proposes Central Repository

The Financial Stability Board has put forward proposals to build a single centralised repository to bring together data on trades for over-the-counter derivatives worth a notional $710 trillion.

Its recommendation for a mechanism to produce and share aggregated data is seen by many as an important step in helping regulators to obtain a global view of the OTC derivatives market and activity.

To date, a total of 25 trade repositories in 11 jurisdictions are either operational or have announced that they will be. G20 leaders agreed in 2009 that all OTC derivatives contracts should be reported to trade repositories, as part of their commitments to reform OTC derivatives markets in order to improve transparency, mitigate systemic risk and protect against market abuse.

However, enacting this reform has been complicated by issues over privacy laws and a lack of data standardisation, as well as the proliferation of trade repositories.

"TR data are fragmented across many locations, stored in a variety of formats and subject to many different rules for authorities' access," the FSB says.

Its feasibility study of the various options for a mechanism to aggregate data follows a consultative version of the report published on 4 February 2014. The public feedback received was taken into account in its latest report, which compares three basic options for aggregating OTC derivatives trade repository data.

Option 1 is a physically centralised model; Option 2 is a logically centralised model; and Option 3 is the collection and aggregation by authorities of raw data from trade repositories.

The report finds that Options 1 and 2 are highly preferable to Option 3. While Option 3 is the only one of these choices that is currently available for use, it has practical limitations that allow it to meet only part of authorities' data needs, beyond protecting against market abuse, the FSB says.

The physical model would typically involve a central database or hub where all the data are collected from TRs, stored and subsequently aggregated within the central database for onward provision to authorities as needed.

The logical model would involve a physically decentralised data collection and storage system. Logical centralisation could take a number of forms but the key feature would be a type of logical indexing mechanism that enables the use of technology to aggregate data from local TR databases rather than the use of a physically central facility. In this option the underlying transaction data would remain in local TR databases and be aggregated with the help of the central index.

One variant of logical centralisation is a model where data is collected and stored locally but, instead of authorities using the logical indexing mechanism themselves to obtain the data from local databases, a designated agent would maintain the central index and the platform for responding to requests from authorities.

In either case, the report recommends a number of key steps that should be undertaken as part of the preparatory work before any formal project is launched to implement a global aggregation mechanism.

It notes that, amongst these steps, it is critical for any aggregation option that the work on standardisation and harmonisation of important data elements be completed, including the global introduction of a legal entity identifier (LEI), and the creation of a unique transaction identifier (UTI) and unique product identifier (UPI).

The report also indicates, in broad terms, the types of legal and regulatory changes that would be needed to allow a central mechanism to access the necessary data from TRs and to aggregate the data for authorities.

Acting on its recommendations, the FSB has asked the Committee on Payments and Market Infrastructures (CPMI), which falls under the Bank for International Settlements (BIS), and the International Organisation of Securities Commissions (Iosco) to develop global guidance on the harmonisation of data elements that are reported to trade repositories.

It will also work with CPMI and Iosco to provide official sector impetus and coordination for the further development and implementation of uniform global UTIs and UPIs.

In September, Australia and Singapore became the first countries to allow their regulators mutual access to trading data stored in electronic warehouses in each country.

FX Turnover Steady

Average daily global FX turnover in key financial centres has seen modest growth or little change in April 2014 compared to October 2013, according to recently released central bank semi-annual surveys.

Daily FX turnover rose slightly in the UK, Canada and Singapore, and was little changed in the US and Australia. Japan saw volume fall, mainly as a result of the Bank of Japan's quantitative easing programme that has kept interest rates at zero and volatility low.

Across the six centres, activity increased by 2.6% to $4.1 trillion per day from $3.99 trillion last October.

However, five out of the six centres report a fall in volume compared with the same period last year. Many attribute the boost in activity seen last April to a spike in yen trading.

In the most recent survey, the UK, which remains the largest centre for FX trading, reports a daily FX turnover of $2.4 trillion in April, which is a 7% increase on October volumes, but still 6% lower than a year previously.

According to the Bank of England's Joint Standing Committee (JSC), turnover in all instruments, including spot transactions, outright forwards, non-deliverable forwards (NDFs), FX swaps and FX options, rose from six months earlier.

FX spot turnover rose 3% to $795 billion per day, but was down 21% year-on-year; outright forwards rose 10% to $179 billion; and FX swap turnover continued to rise, up 8% to a new survey high of $1.2 trillion per day.

EUR/USD remains the most traded currency pair in the UK, making up 28.4% of the total and amounting to $681 billion, a drop of 0.6% from October 2013.

In the US, average daily volume was $811 billion in April 2014. This is 0.6% lower than the average daily volume reported in October 2013 and almost 20% lower than a year earlier, according to the New York Fed's Foreign Exchange Committee (NYFXC).

Unlike the small increase in UK spot turnover, the average US daily spot volume dropped 9% since the last survey in October 2013, to $352 billion, with a year-on-year drop of 32.2%.

This decrease appears to have been widely anticipated throughout the US foreign exchange industry.

According to the NYFXC, the decline in volume since the last survey was driven by reporting dealers and other dealers, while turnover across other financial customers and non-financial customers increased.

The data also showed that this decline in spot volume was partially offset by growth in forwards and OTC options, which increased 14% and 24%, respectively.

Swap volume remained stable with a decrease of less than 1%, totalling $237 billion.

In Tokyo, the FX turnover in April 2014 decreased by almost 3%, constituting $363 billion per day, compared to the previous survey. Japan also suffered a fall in spot transactions, experiencing a drop of 12.8% to $109 billion over the past six months.

On the other hand, forwards increased by 27% to $39 billion. Japan's daily FX volume in April increased 4.3% from a year ago, mainly due to a change in the Tokyo Foreign Exchange Committee's (TFXC) methodology.

Singapore saw almost a 3% rise in April compared to October 2013, with average daily turnover of $291 billion. OTC FX derivatives experienced the largest increase, up 29% to $79 billion.

Total average daily turnover in all OTC FX instruments in the Australian market was $167.8 billion in April 2014. This was little changed from October 2013 (-0.5%), but a decline of 8% over the year.

Average daily turnover in OTC options and cross-currency interest rate swaps (currency swaps) in the Australian market was $6.4 billion in April 2014. This was an increase of 54% from October 2013, but a decline of 10% over the year.

In Canada, the monthly turnover of spot, outright forwards and FX swaps in April totalled more than $1.2 trillion.

Average daily turnover rose by 11.3% to $58.2 billion, up from $52.3 billion in October 2013. However, this is still a 5.2% decrease from the $61 billion recorded in April 2013.

On an average daily basis, survey results showed that derivatives turnover decreased by 17.5% to $3.3 billion in April 2014 compared to $4 billion in October last year.

Currency swaps and options declined by 20% and 15%, respectively, over the same period, totalling $1 billion and $2.3 billion on an average daily basis.

Electronic Trading Levels Wane

A well-worn mantra of the electronic era in foreign exchange markets has been that when things get busy, people pick still up the phone. Alongside that mantra was the assumption that quieter markets led more people to squeeze every efficiency dollar out of their business by using e-trading.

Alongside those beliefs, surveys are released almost monthly highlighting how e-ratios in FX markets continue to climb as more customers and participants generally adopt the e-channel.

It makes for strange reading then, to see in the latest data from the UK's FX Joint Standing Committee's semi-annual FX survey that e-ratios in spot FX are at their lowest since the survey began recording execution data in April 2008 – and in all probability the lowest it has ever been.

It could be that there are some serious adjustments to be made to what is preliminary data, for this has happened before. In April 2012, the JSC's initial data indicated a spot e-ratio of just 49%, however six months the final data meant the final e-ratio was in fact 10% higher at 59%. That said, sources in the FX industry suggest that e-ratios have been drifting lower in recent months, begging the question; why?

The issue does appear to be related to the UK only, for in the US, the New York FX Committee's data has a spot e-ratio just above 62% – broadly in line with the last two years' numbers. Likewise, in Japan, where the e-channel took off much later than in the other two centres, the overall e-ratio drifted slightly lower that the previous two marks, but remains comfortably above the long term average.

In the JSC survey, however, things are very different. April 2014 reported an e-ratio on spot FX of 55.7%, down from 58.4% in October 2013 and 62% in April 2013. With the aforementioned April 2012 data, the last two surveys make up the only three JSC reports to record a spot e-ratio below 60%.

It has to be noted that if one listens to

anecdotal evidence, even 60% seems a low e-ratio for the spot markets. Most, if not all, of the top 10 FX banks suggest their spot e-ratios remain above 70-75%, with several claiming it to be approaching 90%. This infers that problems remain with where some respondents to the JSC survey are allocating trading volume.
There would appear to be evidence to support that assumption in the JSC data, although it is by no means concrete. Over the past two years, during which time aggregation has accelerated as the mechanism of choice among liquidity consumers, the market share of electronic broking systems in the JSC report has fallen sharply, initially from above 40%, to just above 30%, to 22.2% in the latest survey following a 24.8% share in the October 2013 data.
At the same time, multi-dealer platforms have seen their share of spot business rise from around 12-13% to 21.4% in the latest survey, following a 19.5% share in October 2013. Part of this rise will undoubtedly be due to trades received through an aggregator, however industry experts believe that not all aggregator-derived trades are being captured.
Single dealer platforms have maintained a 12-14% share of spot turnover pretty much since the survey first started recording execution data.
Another factor in the low e-ratio for the UK could be the change in the currencies being traded.
In April 2014, just 44.9% of spot FX business reported by the JSC was in EUR/USD, USD/JPY and EUR/JPY, the G3 as they are known. In previous years, the share of activity held by the G3 has consistently been above the 50% mark, a mark it first dropped below in the previous survey, hitting 46%.

ACI EDUCATION UPDATE

ACI – The Financial Markets Association has a considerable reputation as a provider of examinations and certification on specific aspects of the wholesale financial markets.

This year ACI has made progress on the expansion of the platform to include a modular style of training and examination that leads to the ACI Diploma.
Furthermore, ACI's Model Code is a popular component of what we offer to members. As such, an exam is being prepared and will be made available to our membership for a sense of surety that they have read, understood and pledge to adhere to the principles contained in the Model Code. It can be taken by individuals for their personal benefit, but is also available to financial institutions as part of their suite of education.
For many institutions, having the chance to offer continuous learning to staff is desirable, and in some cases mandatory. ACI is continuing to support the industry's continued drive to establish the highest possible standards and level of understanding by providing modern, Internet accessible support for both ethical conduct training and professional development.

New Diploma Structure

At the recent ACI Council Meeting in New York, the new ACI examination framework was unveiled to update national associations on the implementation, which commenced October 2014.
Under the new ACI Diploma structure, the FX and Fixed Income and Money Market units (One and Two) are mandatory for candidates, who must then select one additional unit from the prospectus. These units are, Asset Liability Risk; Advanced Derivatives; Compliance; Islamic B; and Operations.
Before taking the ACI Diploma, candidates must have passed the ACI Dealing Certificate, the ACI Operations Certificate, or have 10 years' market experience.
For the latter two channels, candidates must pass the ACI Model Code Certificate.

NEWS FROM THE ASSOCIATIONS

ACI Lebanon Celebrates Golden Jubilee

ACI Lebanon celebrated 50 years of existence at the start of September, when 430 guests, members of the local banks, financial institutions, and brokerage firms and from BDL Management, gathered at the Four Seasons Hotel in Beirut to attend the celebration program hosted by the association under the patronage of Central Bank Governor, His Excellency Riad Salamé.
The event, widely covered by the local media, treated guests to a 90 minute conference session, during which prominent international and local economists, H.E. Demianos Kattar, Kelvin Tay from UBS and Apostolos Bantis from Commerzbank shared insights on issues surrounding the prospects of the local and international economy in addition to their expectations on the price trends in different asset classes.
Following the conference, attendees got the opportunity to visit sponsors' booths while networking at the welcome reception before heading to the dinner hall.
Guests then watched a short film recounting ACI Lebanon's history, its accomplishments and achievements during the past 50 years and then listened to eloquent speeches given by Salamé, as well as Naji Echo and Marshall Bailey, the respective Presidents of ACI Lebanon and ACI International.
During their speeches, Governor Salamé highlighted the stable economic and monetary situation in Lebanon while Echo and Bailey stressed the achievements of ACI Lebanon, namely among others, being the largest chapter in the Arab world with its number of members reaching 385 in addition to attracting many traders to its training courses.
Then, guests relished the tasty dinner while Jubilee trophies were being bestowed on the BDL governor as well as founders and former presidents of the association.