BANK OF ENGLAND

Speech

Why the buy-side should buy into the FX Global Code

Remarks given by

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Introduction

Thank you very much for the invitation to speak with you today. Much of your agenda is rightly focused on the future: on how to exploit new technology; how to trade with new platforms and market participants; and how to meet ever more demanding customer needs. That relentless push to innovate is one of the great strengths of the global FX markets, and it is a privilege to be part of that conversation.

Against that backdrop, my own remarks – on getting the buy-side signed up to the FX Global Code – might seem a little backward looking. I hope to convince you otherwise. At a time when FX markets are evolving rapidly, there has never been a more important time for investors active in those markets – all of you – to be shaping, and adopting, the norms, conventions and standards embodied in the Code. You are a vital part of the market, and play a crucial role in maintaining market discipline. Leaving the maintenance of standards to others – to the sell-side, to public authorities and regulators, or (worst of all) to no-one, as happened a decade ago – cannot serve either your interests, or those of your investors.

In my remaining remarks, I want first to review the strong progress that has already been made on developing and embedding the Code, including in some buy-side firms. I will then turn to review four specific concerns sometimes heard from buy-side colleagues still unsure about signing up, and set out what I hope will be persuasive responses. Strengthening buy-side adoption is one of the Global FX Committee's top priorities for the coming year – and we have asked senior figures from both sides of the market to lead that work, working either as individual liaison representatives, or as members of a new buy-side outreach working group. I am pleased to see several of them here today – including David Clark, Robbie Boukhoufane and Richard Purssell – and I know they would be happy to answer any questions you may have, either now or later.

Take up of the Global Code: progress so far

Before turning to review progress, I must first confess more than a little self interest in this subject. In my current role, as Executive Director for Markets at the Bank of England, Chair of the London Foreign Exchange Joint Standing Committee, and a member of the Global FX Committee, I have a responsibility to foster strong, efficient and fair foreign exchange markets in sterling and other currency pairs. But I was also in at the birth of the Code itself, because in 2014-15 I led the team that produced the Fair and Effective Markets Review, which recommended amongst other things that the 'Global Preamble' produced by national FX committees in March 2015 should be expanded into a full-blown Global Code, sweeping away the various national texts that preceded it, and setting a new standard for trading practices and behaviours in a market that urgently needed reform.

Two years later, in May 2017, the Global Code was launched, setting out a common set of guidelines for good practice in the FX market. The Code contains 55 principles covering ethics, governance, execution and transparency, information sharing, risk management, confirmation and settlement; and it tackles aspects of current and future market development, including electronic trading, algorithmic trading and prime brokerage. The drafting process was a truly global effort, taking two years and involving central banks and market participants, including buy-side, sell-side and end-users, from 16 jurisdictions around the world. Many of you, or your institutions, played a vital role in that process.

Takeup of the Code, which is voluntary, has grown rapidly. The number of 'Statements of Commitment' (SoCs) – which record organisations' recognition of, and commitment to adopt, the Code – has risen sixfold, from 100 in April 2018 to 605 in November, as recorded on the GFXC's global index. That index, available on the GFXC website,[1] allows market participants to see who signed up, and when. It includes statements from banks, asset managers, corporate treasurers, infrastructures, non-bank liquidity providers – and 41 central banks, including the Bank of England, who have committed to following the principles in the Code in their official operations and investment activities, except where doing so would inhibit the discharge of their legal duties or policy functions.

Adoption of the Code is now widespread amongst banks and other sell-side firms. Table 1 shows that all of the largest 30 firms by asset size have signed up to the Code. Progress on the buy-side has been slower, though still quite encouraging: 11 of the largest 30 asset managers, accounting for over $17 trillion of assets under management, have so far committed to the Code (Table 2). That number will rise over time, as firms currently working towards adoption reach the end of their internal processes.

Nonetheless, it is clear that more remains to be done to secure the same degree of signup to the Code as there has been on the sell-side. What are the remaining obstacles, and how can we address them?

[1] https://www.globalfxc.org/global_index.htm

Table 1: Statements of Commitment to the FX Global Code by the 30 largest sell-side institutions

	Firm	Assets ($billions)	SoC on public register, or have otherwise informed the Bank of England
1	Industrial and Commercial Bank of China Limited	4,211	✓
2	China Construction Bank Corporation	3,632	✓
3	Agricultural Bank of China	3,439	✓
4	Bank of China	3,204	✓
5	MUFG Bank	2,774	✓
6	HSBC	2,652	✓
7	JP Morgan Chase	2,610	✓
8	BNP Paribas	2,354	✓
9	Bank of America NA	2,329	✓
10	Citigroup	1,922	✓
11	Wells Fargo	1,915	✓
12	Crédit Agricole	1,862	✓
13	Mizuho Bank	1,850	✓
14	Sumitomo Mitsui	1,848	✓
15	Deutsche Bank	1,817	✓
16	Santander S.A	1,769	✓
17	Barclays	1,533	✓
18	Societe Generale	1,531	✓
19	Bank of Communications	1,473	✓
20	Postal Savings Bank Of China	1,467	✓
21	Lloyds Bank	1,099	✓
22	RBC Capital Markets	1,040	✓
23	Royal Bank of Scotland	1,036	✓
24	TD Securities	1,028	✓
25	Industrial Bank	1,023	✓
26	ING Bank	1,016	✓
27	UniCredit	1,005	✓
28	China Merchants Bank	994	✓
29	Shanghai Pudong Development Bank	975	✓
30	Goldman Sachs	974	✓

Source: Firm asset rankings from ‘Forbes Global 2000’ list for 2018, https://www.forbes.com/global2000/list/. GFXC signup data from the GFXC global index of public registers, https://www.globalfxc.org/global_index.htm.

Table 2: Statements of Commitment to the FX Global Code by the 30 largest asset managers

	Firm	Assets Under Management ($billions)	SoC on public register, or have otherwise informed the Bank of England
1	Blackrock	6,060	✓
2	Vanguard Asset Management	4,663	
3	State Street Global Advisors	2,641	✓
4	Fidelity Investments	2,284	
5	BNY Mellon Investment Management	1,808	
6	Capital Group	1,715	
7	J.P. Morgan Asset Management	1,677	✓
8	PIMCO	1,667	
9	Amundi	1,626	
10	Prudential Financial	1,323	
11	Legal & General Investment Management	1,263	
12	Goldman Sachs Asset Management	1,224	✓
13	Wellington Management International	1,026	
14	Natixis Investment Managers	947	✓
15	T. Rowe Price	941	
16	Nuveen	923	
17	Nothern Trust Asset Management	913	✓
18	Invesco	890	
19	AXA Investment Managers	850	
20	DWS (Deutsche Asset Management)	800	✓
21	Affiliated Managers Group	794	
22	UBS Asset Management	756	✓
23	Insight Investment	751	✓
24	Sumitomo Mitsui Trust Bank	748	✓
25	Aberdeen Standard Investments	739	
26	Legg Mason	733	
27	Franklin Templeton Investments	716	
28	BNP Paribas Asset Management France	649	
29	Mitsubishi UFJ Trust and Banking	611	✓
30	Allianz Global Investors	568	

Source: Firm AUM rankings from IPE's 'Top 400 Asset Managers 2018', https://www.ipe.com/Uploads/k/x/x/Top-400-Ranking.pdf.
GFXC signup data from the GFXC global index of public registers, https://www.globalfxc.org/global_index.htm.

Why not sign up to the Global Code? Four explanations and responses

In this section, I want to respond to four stylised explanations sometimes heard from buy-side firms still uncertain about signing up to the Code.

Explanation (1): Lack of awareness – "What is the Global Code? I've never heard of it, and don't know what signing up involves."

Given the breadth of engagement during the drafting of the Code, and the raft of publicity since its launch, it is hard to believe that asset managers of the size listed in Table 2 are unaware of its existence. A wealth of materials on the Code is available on the GFXC[2] and national FX Committee[3] websites. The UK's Investment Association has produced a public summary of the Code[4] and a guide to signing up,[5] explaining the process of making a public commitment for buy-side firms. Similar material is available from the Association of Corporate Treasurers[6]. And a raft of conferences and training courses have covered the main themes of the Code. Nevertheless, the global buy-side is a diverse community, so a key priority for the GFXC outreach work is to consider what more can be done to 'push' targeted material to a wider range of firms, using the contacts of national FX committees and trade associations to help organise a dedicated event in the New Year.

Explanation (2): Lack of relevance – "I've read the Code but most of it seems to be for the sell-side: parts of it aren't relevant to my business, others are disproportionate. In areas of sell-side behaviour I do care about – like last look and disclosures – the original Code didn't go far enough"

It would be quite wrong to think that the Code is irrelevant to buy-side firms. The principles on Ethics, Governance, Information Sharing, and many parts of those on Risk Management and Compliance and Confirmation and Settlement apply directly. Examples of principles of particular relevance include:

- Principle 8 ('market participants should be clear about the capacities in which they act', including to their own clients);

- Principle 9 ('market participants should handle orders fairly and with transparency in line with the capabilities in which they act' – which assigns specific duties to clients, including being aware of

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2 https://www.globalfxc.org/

3 eg https://www.newyorkfed.org/fxc/index.html, https://www.bankofengland.co.uk/markets/london-foreign-exchange-joint-standing-committee or http://www.sfemc.org/

4 https://www.theinvestmentassociation.org/assets/files/press/2018/FX%20Global%20Code_summary.pdf

5 https://www.theinvestmentassociation.org/assets/files/consultations/2018/20181105-guidetosigninguptothefxgobalcode.pdf

6 https://www.treasurers.org/technical/codes

responsibilities they should expect of others, being aware of risks associated with the transactions they request and undertake, and regularly evaluating the execution they receive);

- Principle 12 ('market participants should not request transactions… with the intent of disrupting market functioning or hindering the price discovery process'); and

- Principle 31 ('market participants should have independent processes in place to mark-to-market trading positions to measure the size of their profit and loss and the market risk arising from trading positions')

Throughout the whole Code, however, there is no suggestion of a 'one size fits all' approach: for buy-side firms, as for all organisations covered by the Code, proportionality is a key principle. Part II of the Foreword explicitly recognises that 'the steps that different Market Participants take to align their activities with the principles of the Global Code will necessarily reflect the size and complexity of the Market Participant's FX Market activities, and the nature of the Market Participant's engagement in the FX Market.'

The Code is also a living document, which allows it to be strengthened or clarified where necessary, including in areas of particular interest to the buy-side, such as last look and disclosures. In December 2017, Principle 17 of the Code was updated to make it clear that market participants should not undertake trading activity that utilises information from a client's trade request during the last look window. Though I know this remains a topic that can arouse real passions in a room full of asset managers, it does show the commitment of the Global FX Committee to ensure that the Code responds to buy-side concerns. And it's working: a recent report from Nex suggested that hold times and reject rates have fallen materially since the change.[7] Similarly, on sell-side disclosures regarding service levels and protections – another contentious and uneven area of the market in the past – the Global FX Committee is preparing to publish new guidance aimed at improving transparency.[8] I hope this will have a similarly positive effect on market norms, and the Global FX Committee will be critically monitoring its impact in due course.

Explanation (3): Uncertain business case – "The Code is a useful guide to market conventions, but that doesn't mean we need to sign up. The Code is really about the sell-side putting its house in order – the buy-side has nothing to apologise for. At best, the Code just reiterates what we already do; at worst, it's more regulation in disguise."

This is for me the most important observation to address, and vital for securing the buy-in of CEOs and Boards. In putting together that case, I think there are five points worth stressing:

[7] https://www.nex.com/insights/20180904-fx-code-changing-behaviour.
[8] https://www.globalfxc.org/press/p181129a.htm

- First, the Code provides a simple and powerful 'off the shelf' way to educate and promulgate globally-recognised best practice amongst your FX trading and operations staff internally, complementing other tools and regulations;

- Second, it sends a clear signal to your sell-side counterparties of the standards you expect them to uphold in their dealings with you, and your intention to hold them to account for those standards – strengthening market discipline and sending a clear collective message that the buy-side expects the highest standards of service for their customers;

- Third, in demonstrating a commitment to best practice both by your own traders and from those you trade with externally, it gives your firm a competitive advantage in the market for investors and other customers. That is all the more important as the boundaries between 'buy-side' and 'sell-side' activities become increasingly blurred.

- Fourth, from the end of 2019, when the Senior Managers Regime comes into force in the UK for FCA-regulated asset managers, behaving in accordance with a recognised market Code will help Senior Managers demonstrate they are observing 'proper standards of market conduct' – a key requirement of the regime[9]. That is a significant positive benefit to signing up to the Code – and to ensure firms are able to take full advantage of that, the Global Code has been submitted to the FCA for formal recognition; and

- Fifth, signing up to the Code gives buy-side firms a stronger voice in the ongoing development of the Code and the FX market as a whole: a vital part of ensuring the Code is fit for purpose, future-proofed, and reflective of the needs of the whole market.

Explanation (4): Concern about the cost of signing up and implementing the Code – "this is just one of many things we are being asked to comply with. We act for 1000s of different investors, with multiple expectations and mandates. Our regulatory team is overwhelmed."

We understand that buy-side firms face many competing challenges, and have taken steps to help with implementation. I have already mentioned the proportionality principle that lies at the heart of the Code, and the steps that the new GFXC buy-side groups will be taking to help improve understanding and promulgate best practice for implementation. In the UK, the Investment Association is also finalising with its members a guide intended to assist firms navigate their own assessment of the Code's requirements against existing requirements, for public release in early 2019. All of these should help firms looking for assistance in signing up.

[9] https://www.fca.org.uk/about/recognised-industry-codes

But it is worth remembering too the cost of not supporting the Code: the heightened risk of returning to the doubt, uncertainty and collapse in trust in the operation of the FX and other core wholesale markets that we saw a decade ago, and the more restrictive regulation that would inevitably follow. The Code offers the opportunity for the market collectively to recognise its responsibilities in a fair, balanced and cost effective way in the interests of the users of the capital markets: your customers.

Conclusions

If there was one lesson of the Financial Crisis ten years ago, it was the importance of the market taking collective responsibility for raising and maintaining standards in financial markets, of which foreign exchange forms a vital part. Buy-side firms, as huge and growing players in those markets, have a vital role to play in that. By signing up to the Global Code, you signal a commitment not just to uphold those standards yourselves, but also to hold others to them – and in so doing help ensure the markets remain deep, liquid, safe and fair to everyone. Over the coming year, the Global FX Committee and the broader international community will be working towards bringing the level of signup to the Code on the buy-side up towards that seen on the sell-side. Please join us in that campaign.