

foreign exchange committee



Minutes of the Foreign Exchange Committee Meeting

Meeting: November 17, 2021

Host: Video Conference Meeting

FXC Attendees

Anthony Bisegna (State Street)
Yudhveer Chaudhry (Blackrock)
Natalia Chefer (DE Shaw)
Chris Chattaway (Goldman Sachs)
Jose Luis Daza (QFR Capital)
Maria Douvas (Morgan Stanley)
Anna Faustini (Societe Generale)
Hari Hariharan (NWI Management)

Robert Kim (JPMorgan Chase)
Ben Klixbull (XTX Markets)
Jeffrey Knapp (Coca-Cola)
Marisa Kurk (Northern Trust)
Russell Lascala (Deutsche Bank)
Dan Lennon (CLS)
Neill Penney (Refinitiv)

Jessica Sohl (HC Tech) - Vice Chair
Jodi Schenck (Citibank)
Chris Taendler (Barclays)
Bob Tull (Fifth Third)
Sean Tully (CME Group)
Chris Vogel (TD Securities) - Chair
Adam Vos (BNY Mellon)

Federal Reserve Bank of New York (FRBNY)

Anna Nordstrom
Michelle Ezer
Alex Cohen
Jim Bergin
Patricia Zobel
Thomas Noone

John Clark
Martin Prusinowski
Andrew Coflan
Geza Sardi
William Burchell
Ian Armstrong

Federal Reserve Board of Governors

Alain Chaboud

U.S. Dept. of Treasury

Susie Han

Other Attendees:

Neha Narula (MIT)

The Chair opened the meeting by noting the departure of Anthony Bisegna (State Street), Hari Hariharan (NWI Management), and Andy Maack (Vanguard) from the FXC. The Chair thanked them for their significant contributions and many years of service to the FXC. The Chair then introduced MIT's Neha Narula, who led the digital currency discussion.

1. Topical Discussion: Digital Currency

Presentation: "Stablecoins & Central Bank Digital Currency"

MIT's Neha Narula joined the meeting to give a presentation on stablecoins. The presentation began with an overview of MIT's Digital Currency Initiative, which focuses on independent technology research and development of decentralized networks and centralized digital currencies. The presentation noted some key operational and technology risks involving stablecoins, including potential issues with underlying blockchains, risks to the minting and redemption processes, and disagreements between blockchains and stablecoin providers. The presentation concluded with an update on the Central Bank Digital Currency (CBDC) research collaboration between the Federal Reserve Bank of Boston and MIT (i.e., "Project Hamilton").

FXC Discussion Summary

Challenges with the current U.S. payments infrastructure were then discussed, including high fees on retail transactions, many households without access to bank accounts, inefficient dispersal of stimulus payments, and concerns regarding limited growth in private payment options in the U.S. Development of stablecoins and CBDCs was highlighted as an opportunity for a ground-up redesign of the payments infrastructure to address these issues. Proposals for innovating payments and retail CBDCs were also discussed. In addition, members addressed China's "digital yuan" CBDC pilot program, the potential impact of CBDCs on the international role of the dollar, and the prospect for stablecoins to encourage innovation within the traditional banking system and to enable more U.S. dollar access globally. The discussion concluded with remarks on the evolving regulatory landscape within the digital currency space and the impact of Environmental, Social and Governance standards on digital currency adoption going forward.

The Vice Chair concluded the discussion by thanking Neha for her presentation. She then led a brief discussion on digital currency topics that the FXC could pursue in 2022. Topics proposed included decentralized exchanges, the future of FX settlement, and the potential impact of stablecoins and CBDCs on payment infrastructure.

2. Markets Discussion

The meeting then transitioned to a discussion on market developments since the September FXC meeting. The views of committee members on recent higher-than-expected inflation readings, their impacts on global yield curves, and the implications for U.S. and global monetary policy, were the primary focus of the markets discussion.

Inflation and Policy Outlook

- Committee members discussed both the current state of and the outlook for inflation. Some commented that debate over the "transitory" nature of inflation has become less relevant given that global inflationary pressures have been stronger and more persistent than previously expected. Members noted a growing market attention on *how* rather than *if* central banks will respond.

- Members shared varied views on the debate over so called “stagflation” risks that had emerged in market discourse over the recent weeks. Some noted that the risk of a stagflation scenario had increased given growing signs that the inflationary cycle would be more persistent and pronounced than previously expected. Others suggested that the risk was overstated given the view that growth would continue to remain elevated globally, albeit at a potentially slower pace than previously forecast.
- The meeting also included a discussion on employment dynamics in the U.S., including the possibility that structural changes in the labor market over the past year may have elevated the Non-Accelerating Inflation Rate of Unemployment above pre-COVID estimates. As such, some members suggested they were assessing current labor market trends within this context.

FX Movements and Liquidity Conditions

- Members noted that recent moves in currencies and FX volatility had been relatively contained compared to rates markets, but some anticipated that FX may begin responding to the current macro environment more visibly in 2022.
- The discussion then moved to an assessment of current liquidity conditions in FX. Members broadly characterized current FX market conditions as highly liquid, and in most cases, even more liquid than pre-pandemic. Some observations included:
 - Top of book bid-ask spreads in G-10 currencies are narrower on average compared to pre-COVID levels. In G-3 currencies, spreads are roughly 20 percent tighter than levels seen in 2019 on average.
 - Measures of market depth and density in G10 pairs are reportedly at or near all-time highs, as the low volatility environment and subsequent entrance of a greater number of high-frequency traders has encouraged greater participation in FX order books.
 - Broad measures of EM liquidity have also largely returned to pre-COVID levels or better. Currencies including CNH, KRW, HKD, ZAR, MXN and RUB were reported to have tighter bid-ask spreads when compared to 2019 levels.
 - Some EM currencies, such as TRY, continue to stand out as clear outliers with regards to liquidity, given idiosyncratic economic and financial risks.
 - Volume declines in the primary market venues remain notable, as these venues tend to host more activity in more volatile environments. Relatedly, internalization rates among major FX dealers reportedly reached all-time highs for many currency pairs.

3. Return to Work

The meeting concluded with a discussion on return to the office and how organizations are managing external meetings and conferences given the ongoing COVID-19 pandemic. Most members from banks reported full in-office operations, as well as a gradual resumption of business travel and in-person meetings for vaccinated employees. Progress on rolling out vaccines was cited as a determining factor in how quickly organizations were able to return to a more pre-pandemic work posture. Members representing non-bank institutions generally reported a less urgent return to the office posture. The discussion concluded with some remarks on the possibility of an in-person FXC meeting in the first half of 2022, should public health conditions allow it.

The next FXC meeting is scheduled for February 9, 2022.