GLOBAL FOREIGN EXCHANGE DIVISION

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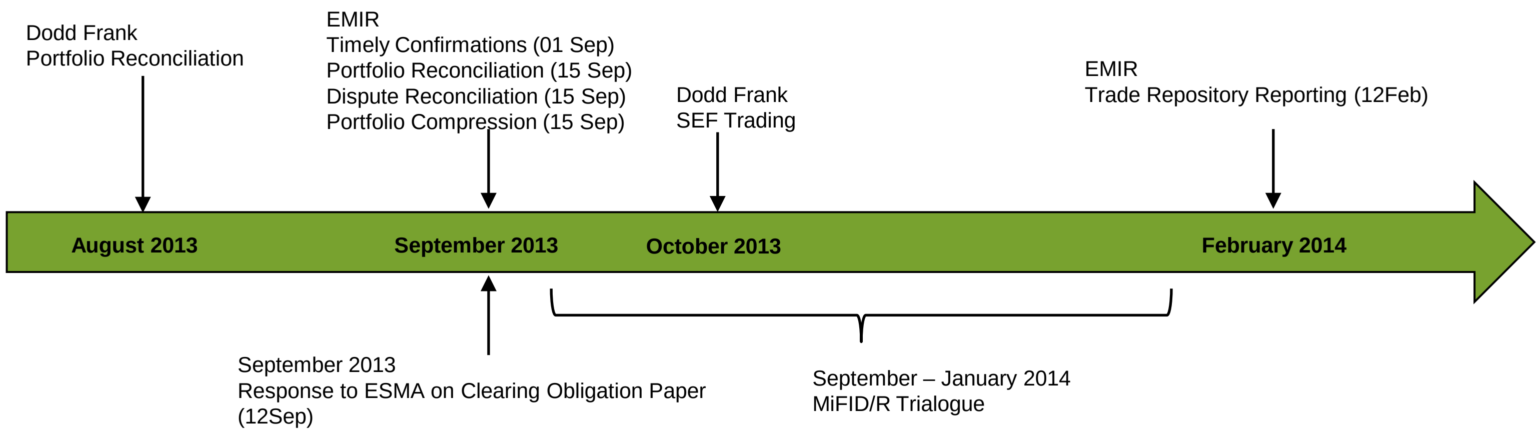
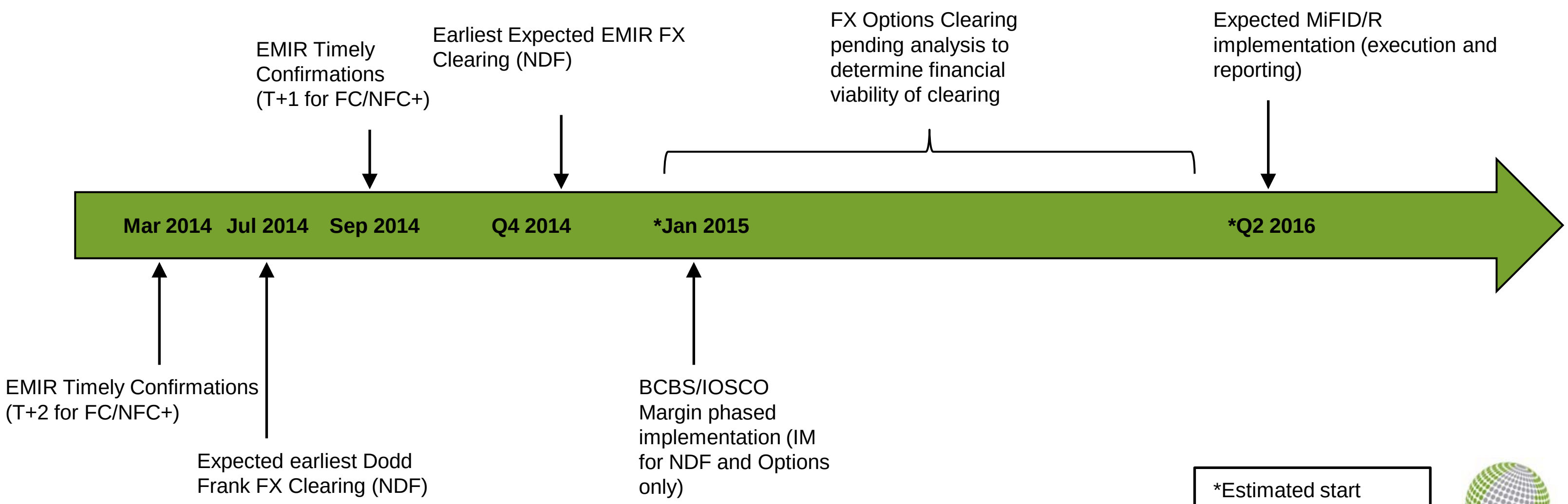
Global FX Division - Background

The Voice of the Global FX Industry

- Formed in June 2010.
- Recognition that there was no coordinated trade body representing the FX industry on a global basis.
- The GFXD now has 23 members, representing the largest global FX dealers and accounting for over 90% of dealer market share (Euromoney survey).
- The Division is global, and represents the FX interests of the three Global Financial Markets Association (GFMA) bodies
  - AFME – Association for Financial Markets In Europe
  - SIFMA – Securities Industry and Financial Markets Association
  - ASIFMA – Asia Securities Industry and Financial Markets Association
- Led out of London by MD with staff in London, NY, HK.
- Desire to represent a truly Global Association representing the industry in multiple locations.
  - Frequent interaction with dealers outside the GFXD membership
  - Industry outreach to end users – corporates and real money as well as other investors
  - Outreach sessions with infrastructure providers, exchanges, CCP, technology providers
- 4 key Global groups: Board; Steering Committee; Operations Committee; Market Architecture Group.

Regulatory Timeline (US and Europe)





*Estimated start dates

EMIR Reporting

Recap

- Trade Reporting in Europe will go-live on February 12, 2014. Most GFXD members are using DTCC as their European trade repository.

Challenges

- Outreach suggests segments of the market are not prepared; either unaware or not technologically ready e.g. Corporates, Investment Mgrs.
- Regulators understand the challenges faced by the market and are largely sympathetic; expectation that they will not enforce immediately.
- The structure of the specific European trade identifier (UTI) has not been finalised by ESMA.
  - The UTI is a key piece of data that needs to be reported; challenges if ESMA revise the format – industry building to ISDA UTI whitepaper
  - ESMA have however confirmed that the US trade identifier can be used for European Reporting should participants have that; good for swap dealers
  - Communication of trade identifier significant hurdle for FX market – a bilateral exercise
- ESMA yet to provide clarity on at least 10 other required data fields – may result in mismatches as field population is open to interpretation.
  - GFXD partnering with ISDA to consult with ESMA for direction
  - GFXD are talking to Corporate and Investment Manager Trade associations to help provide clarity on progress and reporting expectations

Considerations

- Ensure that your firm is testing and ready to report. Client outreach important.
- Be prepared for mismatches.

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EMIR Clearing

Recap

- GFXD goal is to ensure that FX Swaps and FX Forwards are not included within the EMIR clearing mandate. Alignment with US regulation is key for global market. Any clearing for physically settling products, such as FX Options, will be dependant on the markets solving for the settlement challenges posed via our recent OTC FX options clearing project.

Progress Update/Next steps

- ESMA Clearing Discussion paper in September 2013 – GFXD submitted a response.
- GFXD has reminded the key regulators and central banks in Europe, as well as ESMA, that we believe clearing for FX Forwards and FX Swaps is not appropriate in Europe and international alignment is key.
  - Regulators understood the operational challenges regarding clearing physically delivered FX products
- ESMA have yet to provide any further comments on the responses they received. Further official opportunities to re-iterate or position via additional ESMA comment periods expected Q1-2 2014.
- Expected go-live for FX NDF clearing in Europe in Q4 2014 at earliest.
- GFXD to understand efforts by CCP/CLS to resolve the settlement challenges identified in our OTC FX options clearing project (noting pressure of BCBS/IOSCO IM regime for un-cleared derivatives in 2015).

MiFID/R Developments

Recap

The 2 key strands to MiFID/R are:

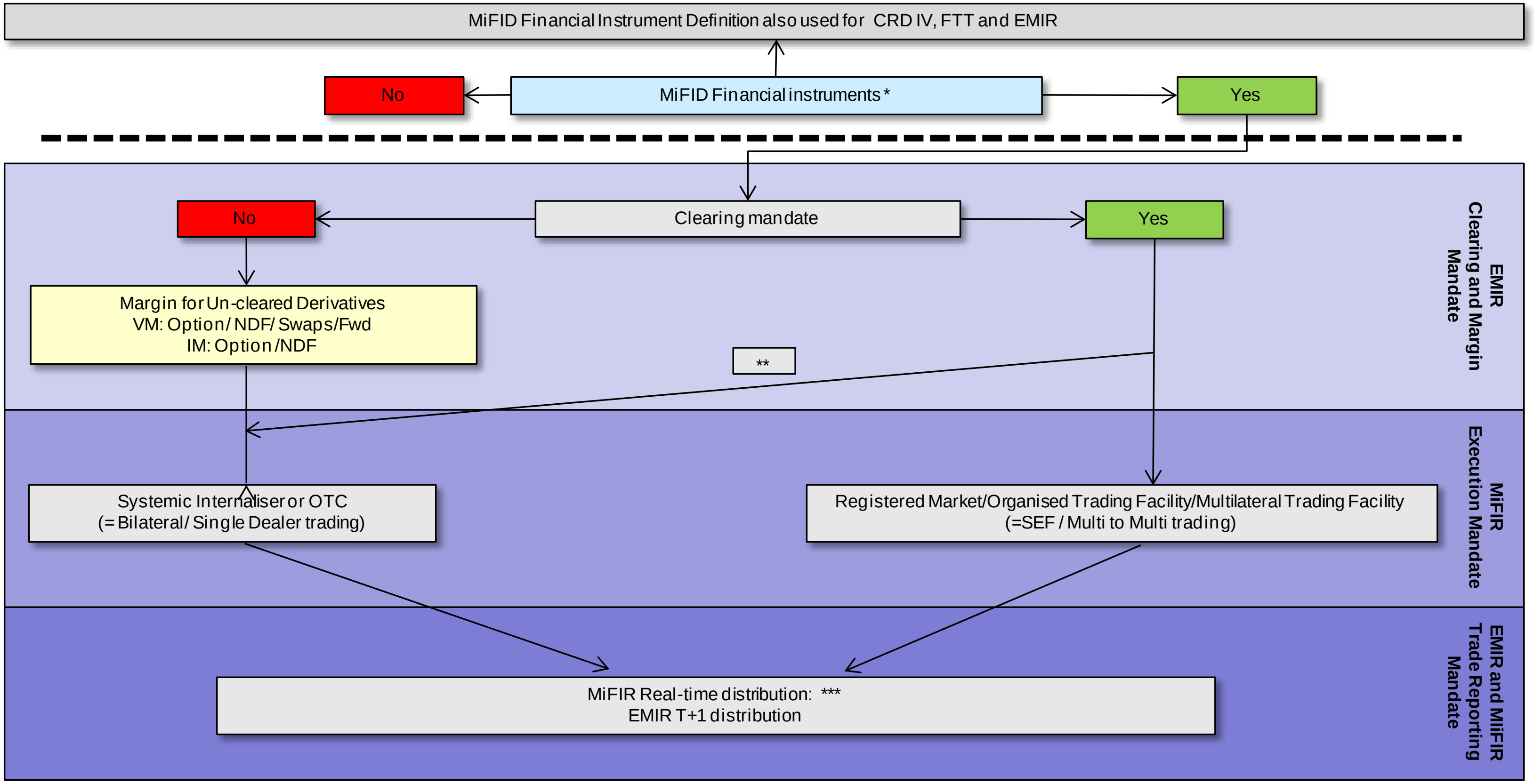
1. **Definition of Financial Instruments.**
   - Analysis completed on the jurisdictional interpretation of FX under the definition of MiFID Financial Instruments.
     - Important as this defines what products are included in EMIR, CRD IV, FTT
     - Differences exist in Europe - UK FCA generally excludes all FX products < 7 days duration with additional commercial purposes test. Other jurisdictions broadly include transactions > T + 2; Italy potentially also has commercial test.
     - GFXD also advocating for carve out of securities related FX transactions across Europe. GFXD partnering with EFAMA on this effort as they believe this is important. Would mirror US and Canada positions.

2. **Market Framework, trading and transparency obligations.**
   - The GFXD key focus areas – Trading Obligation; Pre-Trade Transparency; Market Structure - are all moving in the right direction.
     - Political trialogues completed 14 January, final text expected by April
     - We believe text now included for a carve-out from the trading obligation for large-in-scale (block) transactions
     - Level 2 details and rule writing will now follow – estimated implementation 2016

GFXD Additional Work

- GFXD has offered to help ESMA with its analysis and definition of liquidity.
  - Liquidity is used in the definition of what products will be required to clear and where they are required to be traded.
    - Initial effort is supported by Bloomberg who will be providing data
    - ISDA are also looking at a similar exercise for Rates/Credit. GFXD is in communication with ISDA to prevent duplication

Europe : MiFID/R and EMIR – The FX Jigsaw



* MiFID interpretation of Financial instruments will be open to country by country interpretation, expected to include for FX some /all of Options, NDF, Swaps, Fwds
** For instance if a trade is Large in Scale it may be traded off venue, but still subject to the rules of a venue
*** Expected difference to Dodd-Frank where Swaps/Fwds are not publically reported real-time

Global Summary – Clearing, Execution and Reporting

AsiaPac – > 7 example regulators

Reporting

- Japan April 2013 (NDF, Options)
- Australia Oct 2013 or Oct'14 (Fwd/Swap/NDF/Options)
- HK Dec 2013 (NDF)
- SING Oct 2014 (Fwd/Swap/NDF/Options)
- China ongoing
- S Korea ongoing
- India ongoing

Clearing / Margin

- Japan March 2014
- Australia 2014
- HK Mid 2014 NDF
- SING Mid 2014 NDF
- China ongoing
- S Korea mid 2015 NDF
- India Q4 2014 INR Fwd/Swaps

Execution

- Working with regulators on the reciprocal impact in these AsiaPac hubs

Europe – ESMA

Reporting

- Feb 12th 2014
- Dual sided reporting

Clearing

- July 2014 clearing obligations start*
- Q4 2014 NDF*

Execution

- Mifid Trialogue completed for L1
- L2 go-live 2014/2016*

North America – CFTC and CSA

Reporting

- US Feb 28th 2013 FX
- Canada July 2nd 2014

Clearing

- US Q2 2014 NDF*
- US 2015 Options*
- US Margin 2015
- Canada model rules consultation underway

Execution

- US Permitted Transactions Oct 2013
- NDFs Q2/3 2014
- Options 2015/16

*estimate

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Proposed EU FTT and FX

Position of FX in the Proposed European FTT and status:

- The current products included by the proposed tax are taken from the definition of Financial Instruments in MiFID. The Proposed tax rates are: 0.01% (Corp/Dealers) and 0.02% (Fund Managers).
- The Commission's view is that the inclusion of FX spot in such a tax would be incompatible with The Treaty of the Functioning of European Union; essentially restricting the free movement of capital. GFXD believe this is also the case for other FX instruments
- In the EU Council, technical discussions on the Commission's proposal have resumed: next EU11 meeting 15-16 January , Council working group on 29 January. France and Germany meeting on 19 February to agree a common position with France being supportive of a narrower scope FTT – this date critical.

Impact of the proposed FTT on FX Users:

- Using 2012 data for actual transactions executed in the FX market, across all end-user segments, the GFXD has performed an in depth analysis to size the impact of the proposed FTT. The results demonstrated an increase in end user transaction costs between 163% to 4722% (see next slide).
- The FX Market is primarily short-dated in nature with tight, transparent pricing and large notionals . Little material difference in a spot transaction of 2 days and a swap of 6 days for "movement of capital". Such tight spreads and large notionals cause a high impact on transaction costs in the FX market.
- These increased transaction costs are likely to discourage companies and investors to hedge their risks and increase funding costs. Such a change in behaviour will likely be associated with increased earnings volatility, increased business risks and costs. It will also reduce return for investors.
- Finally, we expect such a proposed FTT for FX to discourage activity in international commerce, or if users have to accommodate the tax, it has the potential to reduce the funds available to fund growth.

The GFXD shares the view that the Proposed FTT is detrimental to overall economic growth in Europe. This is well demonstrated by the impact on FX markets which supports our position that the proposed FTT should not apply to FX instruments -FX forwards, FX swaps, FX options and FX NDFs.

Impact of FTT on Client Transaction Costs and a Working Example

End User Type and Location	Dealer Location	2012 FX Products traded	Increase in Direct Transaction Cost from FTT
Corporate, in Tax Zone	Tax zone	FX Swaps	**738%**
Corporate Non Tax Zone	Tax Zone	FX Forwards, Swaps, Options	**326%**
Corporate Non Tax Zone	Tax Zone	FX Forwards, Swaps, Options	**216%**
Corporate, Tax Zone	Tax Zone	FX Swaps	**706%**
Fund manager, Tax Zone	Non Tax Zone	FX Swaps	**1489%**
Fund manager, Tax Zone	Non Tax Zone	FX Swaps	**163%**
Fund manager, Tax Zone	Non Tax Zone	FX Swaps and Options	**1027%**
Fund Manager, non Tax Zone	Tax Zone	FX Swaps, fwds, Options	**4722%**
Corporate, Tax Zone	Tax Zone	FX Swaps, fwds, Options	**484%**
Fund Manager, Tax Zone	Tax Zone	FX Swaps, fwds	**751%**
Corporate, Tax Zone	Tax Zone	FX Swaps	**768%**
Corporate Non Tax Zone	Tax Zone	FX Forwards, Swaps, Options	**191%**
Fund Manager, Tax Zone	Tax Zone	FX Swaps, fwds	**675%**
Corporate, Tax Zone	Tax Zone	FX Swaps, fwds	**241%**
Corporate, Tax Zone	Tax Zone	FX Swaps, fwds	**333%**

Worked example: Multinational Corporation in Tax Zone

A multi-national corporation has weekly cashflows of approximately $2,000,000,000 ($2bn) in multiple currencies, which it seeks to convert into a single currency for cash management purposes and then swap back again to meet outgoing requirements.

It uses short term FX swaps for this purpose, converting the various currency streams into dollars before swapping them back again. This gives rise to $4,000,000,000 ($4bn) in notional value of FX swaps on a weekly basis, which amounts to $200,000,000,000 ($200bn) on an annual basis (assume 50 weeks * $4bn). These short-dated swaps are competitively priced in the market (given that they can be seen as a short term collateralised loan of one currency for another and then reversal of that position) and the transaction costs (calculated through the bid-offer spread) for the annual amount to $2,500,000.

The FTT when applied to the notional values of the transactions for the year amount to $200,000,000,000 * 0.01% = $20,000,000. Given that the dealer will need to pass on these costs, for this straightforward and cost effective service, the corporate sees its transaction costs rise from $2.5m to $22.5m – an 800% increase.

The example above demonstrates how the FTT would impact a Multinational Corporation in the Tax Zone.

The table on the left illustrates the findings from the GFXD analysis of actual FX transactions executed in 2012.