US Treasury ‘proposed determination’ to exempt FX from central clearing under Dodd-Frank is the right one, says Global FX Division

The US Treasury ‘proposed determination’ to exempt foreign exchange forwards and swaps transactions from forced clearing under the Dodd-Frank Act is a major step in ensuring the continued availability of cost-effective hedging for corporates and investors and the on-going functioning of a well performing market, according to the Global FX Division¹.

Requiring FX transactions to be made through a central clearing house would have serious negative consequences for corporate and asset manager end-users, which use foreign exchange as a key element of their risk management programmes. It could also introduce new risks into a stable market that performed well during the crisis.

The US Treasury has undertaken a diligent and comprehensive consultation process, during which the Global FX Division has focused on outlining the case for exempting FX from mandatory clearing.

AFME/Oliver Wyman research conducted in October 2010 shows that the key risk in foreign exchange is settlement risk, comprising 94% of the estimated maximum loss exposure in a trade for FX instruments with a maturity of six months and 89% for instruments with a maturity of two years.

Settlement risk is already managed effectively through the existing CLS settlement system, which is backed by 22 central banks and overseen by the Federal Bank of New York.

James Kemp, Managing Director of the Global FX Division, comments:

“We very much welcome the US Treasury ‘proposed determination’, as moving FX swaps and forwards to centralised clearing will not only create additional costs for business users, but could also increase systemic risk.

“We believe that this should remain the final outcome and sincerely hope that the European regulators and decision makers acknowledge the US Treasury's key points and, for the same reasons, follow suit in outlining the arguments for exempting FX from mandatory clearing and ensuring that the global FX market is not fragmented into two different regimes.”
Tim Ryan, president and CEO of SIFMA (US partner of the Global FX Division), comments:

“It's important for business to be able to access an efficient and liquid market for FX swaps and forwards to better manage their foreign exchange needs. Today's 'proposed determination' goes far in ensuring these markets will remain vital tools for business.”

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Contact

AFME
James White +44 (0)20 7743 9367

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1. The Global Foreign Exchange (FX) Division was formed in co-operation with the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and the Asia Securities Industry and Financial Markets Association (ASIFMA). Its members comprise 22 global FX market participants, collectively representing more than 85% of the FX market.

2. AFME (Association for Financial Markets in Europe) promotes fair, orderly, and efficient European wholesale capital markets and provides leadership in advancing the interests of all market participants. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association through the GFMA (Global Financial Markets Association). For more information please visit the AFME website, www.afme.eu