Basel Committee on Banking Supervision
BANK FOR INTERNATIONAL SETTLEMENTS

Committee on Payments and Market Infrastructures
BANK FOR INTERNATIONAL SETTLEMENTS

To: Supervisors, banks and other participants in the FX market

18 December 2020

Supervisory Guidance on managing FX settlement risk and the Global FX Code

Dear Sir/Madam

The Basel Committee on Banking Supervision (BCBS) and the Committee on Payments and Market Infrastructures (CPMI) encourage bank supervisors and banks and other participants in the FX market to follow the expectations set out in the 2013 BCBS *Supervisory Guidance on managing FX settlement risk*[1] (BCBS guidance) and the *Global FX Code* (Principles 35 and 50).[2] Bank supervisors should incorporate the BCBS guidance into their supervisory framework and, as part of their ongoing supervisory activities, assess whether banks that are engaged materially in FX trading are meeting that guidance. In cases where supervisors determine that a bank's management of FX settlement related risks is not adequate they should take appropriate action to correct the situation.

Settling FX trades can lead to significant principal risk when one counterparty to a trade sends a currency payment to the other before receiving the currency it is buying. Principal risk and other associated risks are often underestimated because the length of time between trade execution and final settlement is not fully taken into account.

The 2019 BIS Triennial FX survey (Triennial)[3] shows that FX settlement risk remains significant. Global FX trading activity was USD 6.6 trillion per day in April 2019, leading to gross payment obligations worth USD 18.7 trillion. Related analysis suggests that the proportion of trades with payment-versus-payment (PvP) protection has fallen in recent years.[4]

The BCBS guidance recommends eliminating principal risk by using PvP settlement where practicable. For FX transactions that do not settle via PvP, the guidance recommends that supervisors encourage banks to minimise the size and duration of their principal risk and to conduct timely reconciliation of payments received. To fully address FX settlement-related risks, banks' incentives, business practices and infrastructures must be properly aligned.

1 Available at www.bis.org/publ/bcbs241.htm.

2 Available at www.globalfxc.org/fx_global_code.htm.

3 Available at www.bis.org/statistics/rpfx19.htm?m=6%7C381%7C677.

4 See M Bech and H Holden, "FX settlement risk remains significant", *BIS Quarterly Review*, December 2019; available at www.bis.org/publ/qtrpdf/r_qt1912x.htm.

Expanding the availability of PvP settlement to a wider range of transactions and actors reduces FX settlement risk. This will support global financial stability, and can also help to lower costs for cross-border payments that involve exchanging two or more currencies. Increased adoption of PvP settlement is an important element in improving existing payment infrastructures and arrangements for cross-border payments.[5]

In response to the Triennial results, the BCBS and the CPMI have agreed an action plan. The plan involves concerted supervisory action, supplemented with education and improved data and analysis. The BCBS and the CPMI welcome the Global FX Committee's plans to strengthen the guidance on FX settlement risk in its Global FX Code.[6] The BCBS and the CPMI are also supportive of plans to collect data to monitor FX settlement risk on a regular basis.

The BCBS and the CPMI will continue to engage with a range of relevant public and private sector stakeholders and to support and monitor industry-wide actions and progress.

Yours faithfully

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Chair of the Basel Committee
on Banking Supervision

Jon Cunliffe
Chair of the Committee
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5 CPMI, *Enhancing cross-border payments: building blocks of a global roadmap*, Stage 2 report to the G20, 13 July 2020; available at www.bis.org/cpmi/publ/d193.htm.

6 G Debelle (Chair of the GFXC), "The global foreign exchange committee and the FX global code", speech at the FX Week Australia Webinar, 22 October 2020; available at www.bis.org/review/r201022c.htm.