TMPG Meeting Minutes

June 16, 2020

TMPG attendees

Alberto Antonini (Tudor)	Ari Kavour (Wells Fargo)	Jerry Pucci (BlackRock)
Alex Blanchard (Goldman Sachs)	Chris Leonard (Barclays)	Rasmus Rueffer (ECB)
David Finkelstein (Annaly)	Edward McLaren (Bank of America)	Marc Seidner (PIMCO)
Doug Friedman (Tradeweb)	Andrea Pfenning (BNY Mellon)	Ryan Sheftel (GTS)
Rob Huntington (Credit Suisse)	Thomas Pluta (JP Morgan)	Gemma Wright-Casparius (Vanguard)

New York Fed attendees

Frank Keane	Rania Perry	Janine Tramontana
Lorie Logan	Matthew Raskin	Kyle Watson
Matt Milroy	Brett Rose	Nate Wuerffel

U.S. Department of Treasury attendees

Fred Pietrangeli	Nicholas Steele	Brian Smith

- Due to the coronavirus pandemic, the TMPG meeting was held via videoconference.

- The meeting commenced with the Chair welcoming Doug Friedman from Tradeweb and Alex Blanchard from Goldman Sachs as new members of the group. The chair then noted that it remained appropriate to keep the repo clearing and settlement working group on pause given the heightened focus on market functioning more broadly. A New York Fed representative then informed members that the search for a vice chair for the group remained ongoing.

- The TMPG meeting then transitioned to a discussion of recent market developments, followed by a discussion of the outlook for the second half of 2020 in TMPG covered markets. This discussion began with an overview of the New York Fed's announcement of plans to increase the System Open Market Account (SOMA) holdings of Treasury securities, agency mortgage-backed securities (MBS), and agency commercial mortgage-backed securities (CMBS) at least at the current pace to sustain the smooth functioning of markets for these securities.[1]
    - TMPG members agreed that market functioning had largely normalized from March/April and noted that the improvement in functioning has continued to be

[1] Federal Reserve Bank of New York, Statement Regarding Treasury Securities, Agency Mortgage-Backed Securities, and Agency Commercial Mortgage-Backed Securities Operations, June 10, 2020.

supported by Fed intervention. Looking ahead, members suggested that a watch point for the second half of the year would be how the Fed's actions continue to evolve with the goal of sustaining market functioning along with potential policy options over the medium to long term.[2] An overarching theme of discussion among members was the potential future impact of Treasury issuance on market functioning and Treasury yields. Members noted that Treasury issuance was expected to outpace Fed purchases in the second half of the year, and the ability for banks and broker dealers to serve as intermediaries would be in focus as issuance increases.

  - Members continued the market discussion by turning to mortgage markets. Members noted that potential negative impacts of increased forbearance requests on Agency MBS performance were now expected to be less than initially projected, and did not view forbearance as a likely source of future MBS market disruptions. Members also noted that the primary/secondary spread remained at historically wide levels, but expected the spread to begin gradually narrowing in the second half of 2020.
  - Concluding with funding markets, members described conditions as having largely returned to pre-COVID levels, with the Fed's announced changes to its repurchase agreement operations to more a of a backstop posture deemed to be appropriate and cited as a chance for typical private sector avenues of intermediation to return. However, members also cited a number of considerations surrounding money market functioning in the long term, as members remain concerned about regulatory and capital factors that might impede intermediation if one-way flows returned to short-term funding markets.

- Next, members discussed TMPG fails charge recommendations with respect to agency commercial mortgage-backed securities (CMBS). A member of the New York Fed informed members of reports that market participants may not be uniformly applying the fails charge best practice recommendation for agency CMBS, which is addressed in the TMPG Fails FAQs. Members also queried the uniformity of application of the fails charge recommendation on Treasury securities transactions settling outside the U.S. Members agreed to a survey of member firms on both fails-related topics in the intermeeting period, with anonymized results to be shared with the Group by the TMPG secretariat.

- Members then briefly discussed a recent working paper on Treasury market structure, authored by Darrell Duffie of Stanford University. The working paper cited earlier work by the TMPG in its white paper on clearing and settlement practices in the Treasury market. The Duffie paper

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[2] One TMPG member presented their outlook for the year, located here on the TMPG website.

hypothesizes that a broad official mandate for central clearing in the cash Treasury market would improve market structure and resiliency. Given the proximity with previous TMPG work, it was suggested that the TMPG may choose to invite the author to a future meeting and continue the discussion on central clearing at that time.

- Finally, TMPG members discussed lessons learned from developments in the Treasury and Agency MBS market over the past year, continuing a discussion on this topic from the May TMPG meeting.[3] At a high level, members highlighted that no single driver was behind the periods of volatility and illiquidity over the past 12 months. But, in discussing some of the potential factors behind volatility, members continued to refine the broad categories of drivers related to both market structure and market practices. On market structure, several members discussed the role of electronic trading in the Treasury market. Specifically, it was noted that although electronic trading continued to be prevalent throughout recent bouts of market volatility, activity in rules-based electronic trading (e.g. algorithmic trading) appeared to have declined in March 2020. Similar to the last meeting, members agreed to continue discussing and refining their takeaways as the market continues to evolve.
- The next regularly scheduled TMPG meeting will take place on September 3, 2020, from 3:00-5:00 PM.

[3] Member discussion was oriented around the discussion questions and summary of the May TMPG discussion, included in this document's appendix.

Appendix: Market Structure and Recommended Best Practices Lessons Learned

At the May meeting, the TMPG discussed lessons learned from periods of elevated volatility dating to Q3 2019. The discussion summarized views expressed by members to date, and members continue to contemplate whether there is a need to refine the group's consensus on key lessons learned with respect to the TMPG covered markets. The views summarized below are part of an ongoing study by the TMPG.

1. **Market Structure (*the composition of participants, products, venues, infrastructure, rules and regulations in the secondary market for the TMPG covered markets*)**
    a. Discussion Questions:
        i. Have changes in market structure, or the composition of market participants, over the past decade impacted access to liquidity during periods of elevated volatility?
        ii. Could potential changes to market structure improve the durability of liquidity provision across the range of Treasury securities or Agency MBS during periods of elevated volatility?
        iii. Aside from ETFs, which were discussed at the May TMPG, are there other products that may have impacted liquidity in the TMPG covered markets during the most recent periods of elevated volatility?

    b. Member views expressed at the May TMPG:
        i. <u>Intermediation</u>: Members suggested that, since the financial crisis, SLR and other regulatory requirements have played a role in reducing the capacity of banks and broker dealers to intermediate. Members noted that less-well-capitalized firms have stepped in to fill some of these intermediation gaps that were previously filled by larger banks and broker dealers. Members speculated, however, that firms with lower amounts of capitalization may be less able to intermediate as effectively as a well-capitalized institution in instances where the expansion of balance sheet is required for intermediation.
        ii. <u>Electronification</u>: The prevalence of electronic trading in the Treasury market has increased over the past decade. However, members suggested that in times of great stress the ease of executing via electronic platforms can degrade, which may impede price discovery, reduce transparency and increase market fragmentation.
        iii. <u>Increased use of Exchange Traded Funds (ETFs)</u>: Members noted that they have learned more about the growth of ETFs – especially in the credit market. It was noted that the TMPG may choose to continue monitoring ETF developments, especially in TMPG covered markets.

2. **Market Practices (*the behavior or actions of market participants in the secondary market for TMPG covered markets*)**

a. Discussion Questions:
    i. Are there areas where practices by market participants, such as margining, may have contributed to liquidity or market functioning in the TMPG covered markets during recent periods of elevated volatility?
    ii. Have changes in the behavior of market participants due to work-from-home (WFH) arrangements impacted liquidity or market functioning in the TMPG covered markets during recent periods of elevated volatility?

b. Member views expressed at the May TMPG:
    i. Margining: Members agreed that margining forward exposures in Agency MBS transactions is important to maintain order and market functioning during a crisis. Members reaffirmed the usefulness of two-way margin collection for forward settling trades as a TMPG best practice.
    ii. Contingency: Members noted that widespread work-from-home arrangements were not foreseen by most contingency and resiliency planners. Members noted that although the transition to working from home was relatively smooth, this crisis is a reminder of the value of continuously re-examining contingency and resiliency plans and identifying any gaps. For example, it was noted that it may be prudent to assess the impact of regional power outages, or the security of tele-meeting platforms.
    iii. Incentives: Members observed that, for some time, markets have not been prepared for substantial one-way flows, such as those that occurred during the COVID-19 crisis. Moreover, it was noted that the flows that resulted in a significant widening of the cash futures basis in Q1 2020 further amplified volatility related to portfolio and liquidity adjustments amid the pandemic.