Question & Answer Report: Professional Repo Market & Collateral Management Workshop 2022

Day 1 - Monday, 31 October 2022

CET
10:15 The repo instrument: legal, economic and operational character
Richard Comotto, ICMA

11:30 Types of repo
Richard Comotto, ICMA

12:30 GC v specials; repo v securities lending, repo v derivatives
Richard Comotto, ICMA

13:15 Legal: what's so important about documentation
Richard Comotto, ICMA

Q: What is A/360 in the repo rate field?
A: The repo rate is quoted per annum. For the transaction period of one-week, you need to scale that rate down to one week, so multiply by 7/360, which is the actual number of days over the assumed number of days in the year, which is 360 for euro money markets.

Q: How do counterparties agree on the clean price on more illiquid (wider bid/ask spread) securities?
A: With difficulty. It is a more intuitive judgement and more reliant on comparisons with liquid benchmarks (ie government bonds) against which a premium can be applied to compensate for risk.

Q: What would be the definition of the term "clean price"?
A: The price of an interest-paying fixed-income security as a percentage of the nominal value excluding accrued interest.

Q: Is the trade date always same as settlement date and which date is relevant to calculate the interest?
A: No. Settlement is often one, two or more days after the trade date. The trade date is when the contract is agreed. The settlement date is when payments and deliveries are supposed to happen. Interest starts on the settlement date.

Q: Is there a limit to the reuse of the security and who is the legal owner in case of dispute?
A: Only practical limits (ie how long it takes to deal). The legal owner is the ultimate buyer as everyone else has bought and sold the collateral.

Q: What is the core difference between a Pledge and Collateral?!
A: Collateral is what you pledge.

Q: What will happen when a UK and US counterparty trade a repo? What language/ Legal agreements would be used?
A: The Americans still speak something like English, so the language is English. The typical agreement for cross-border trades is the GMRA.

Q: Is it safe to say, both terms mean the same. It only differs by the party who sees it. from my POV it's pledge, From CCP/Lender it's Collateral
A: No. A pledge is an action to create rights in property. Collateral is the property.

Q: The recharacterization risk of repo is not existent/low in Europe, correct?
A: Very low but not non-existent (people can do dangerous things in their trades).

Q: Is that Chinese 'repo' with account blocks then equivalent to an old-style held in custody repo where you have to transfer securities to an account where its then held?
A: The collateral is blocked but it is different in intent to HIC repo, where the intention was nevertheless to pass legal title. In fact, the failure to also pass legal title would have meant that, in many jurisdictions, it would have been judged to have been an attempt at a pledge.

Q: Is coupon payment considered a corporate event?
A: It shouldn't be, because it's not an additional benefit.

Q: What could happen/what are the options available on the table, if the lender wishes to forego, but the buyer would like to opt for a rights?!
A: You might undermine the legal character of the sale. Dangerous.

Q: For reporting to the trade repository under SFTR. does the seller report corporate action or buyer or both?
A: You do not report corporate events except to the extent that they change the value or nature of the collateral, in which case, there is a COLU report.

Q: So, for slide 30, even if the buyer is the owner under the GMRA until they sell them back to the seller, it remains the seller who decides how to deal with the corporate action all along?
A: Good question. The seller is only making a decision about what it gets back. It is not making a decision about the collateral sold to the buyer. Legally, these are two different properties, which is why the collateral is called the "purchases securities" and the collateral returned is called the "equivalent securities".

Q: What is the difference between the proceeds of redemption (covered by the definition of Equivalent Securities) and a payment or repayment of principal in respect of the securities (defined as Distribution in the GMRA)?
A: Under the GMRA 2000, the redemption proceeds would be Equivalent Securities. Under the GMRA 2011, there is some ambiguity in the drafting. The intention was to allow redemption proceeds to be treated as income to be repaid immediately as a manufactured payment where the collateral was in a basket in a long-term trade.

Q: Is it up to the buyer to reimburse the seller if they have received a coupon payment? Or does the seller have to claim from the buyer?
A: In a repurchase transaction, the buyer is obliged to make the payment.

Q: In the section when you mention the risk of collateral remains with seller: Can we not argue that also buyer bears a risk in the sense that if the buyback price (which is agreed in advance), is lower than market price at the time of repurchase, that the buyer could have also made a better sell by selling the collateralized securities to other buyers? for example in the event that the spread between purchase price and repurchase price is smaller than the price increase of that security in the market, the buyer would have been better off with just buying the security itself in the market and reselling it with the new market price, instead of buying it as a collateral/repo with a pre-defined price. So in this case can we not say that buyer also bears a risk?
A: That would be another trade so not relevant to the repo. And the buyer is just going into the deal to invest cash, not to invest in the security.

Q: In the GMRA documentation, the terminology of 'collateral' is not used, the documentation only talkes about 'margin' (cash margin or securities margin). When ICMA refers to 'collateral' on their website and Q&A's, does it refer to Purchased Securities (and Margin)? This is something that is very confusing when people refer to collateral in the repo industry while in fact the documentation does not use this terminology and only talks about purchased securities and margin. Should we consider the purchased securities as 'collateral'?
A: GMRA does not use the term "collateral" because it is a term that is strictly-speaking associated with security interests such as pledges, so it would be unwise to use it in a repo agreement. However, the market uses the term. Collateral means Purchased Securities and margin.

Q: In certain market, it is a common practice to pay manufactured coupon before buyer actually receives the coupon from the issuer. How can the buyer argue to get back the already paid manufactured payments from the seller if the issuer defaults? on which GMRA clause can the buyer get it back?
A: I'd be interest to know which market. Why pay before an obligation becomes due. If you've been unwise enough to make a premature payment, you will have created a debt which will have to go into the close-out netting.

Q: Is the buyer obliged to make the payment of the coupon to the seller, while buyer has not received such coupon since it has sold the collateral during the term of the repo transaction?
A: The GMRA says the buyer must pay only what it would have received had it still been holding the security during the repo. So, the answer is yes. Remember the seller is still taking the risk on the collateral, even though the buyer has sold it.

Q: Please can you explain the accounting treatment increasing the sellers balance sheet but buyers remains same?
A: The seller keeps the collateral on its balance sheet (because it has the risk on the collateral due to its repurchase commitment) and receives cash, so increasing the balance sheet. The buyer gives away ownership of cash, which creates a receivable, so the size of the balance sheet remains unchanged.

Q: In the US its same day settlement for Repo. Is it the same for Cash (as in Bonds, not O/N repo)
A: I think it is for UST but, for others, the US market is just starting to talk about moving to T+2

Q; For buy/sell-backs, how do you agree on a reinvestment rate for the coupon payments? is there a benchmark?
A: In euros, it is convention to use ESTR. In sterling, it's SONIA. Where such OIs are not available or are not liquid, it can be a problem and parties might agree to use a different bond.

Q: For evergreens, is there a setup akin to SL to clear accrued interest at month end?
A: If you expressly agree to that.

Q: Does ICMA have any template/guidance on the details of the confirmation of Evergreens?
A: There is some information in an annex of the Guide to Best Practice that is relevant but no express confirmation template.

Q: For evergreen repos, you explained that the buyer or the seller has the right to exercise the option to terminate. Is it legally speaking or should we understand that there is an optional model involved in the pricing of these repos?
A: In theory but not sure how formal the pricing is.

Q: Is the difference between evergreen repo (extended rep date) and dynamic evergreen repo that in the first one the purchase date is fixed?
A: That's true in both.

Q: For extendable repos, what are usually the inputs on the market when initiating a new transaction? X-Y-Z?
A: The prime inputs are the dates needed to avoid an LCR exposure. The value of the extendible will relate to the LCR cost avoided.

Q: What is OIS+ in this slide?
A: Overnight Index Swap rate plus a spread in basis points. OIS would be a SOFR, SONIA, ESTR, etc curve.

Q: Could you argue with the TRS there is actually risk and return for the provider of the TRS: if the fee outweighs the increase of the collateral value or its negative, red gets everything
A: That would be bad pricing or bad luck.

Q: Do you think there's slippage risk with TRS at all? eg selling back collateral at diff price to close out price of TRS? or do you think is closing at say trade web close mitigates that completely?
A: There would be slippage.

Q: Are there really many market participant that trust words over legally enforceable contracts?
A: Finance is often about trust.

Q: Is this balance sheet gain still relevant? I've noticed some counterparties don't want to sell and repurchase the collateral as it causes diff balance sheet implications, think it may get recategorized as repo - not 100% though
A: Just covered that but there are netting advantages if you do the two legs with different parties.

Q: in a synth repo there is a derecognition of the assets for the seller? in other words in which BS is the asset?
A: IFRS treats a synthetic like a real repo, so no. But you break up the synthetic if you do the two legs with different counterparties and that would also derecognition.

Q: Can we say that a Repo is then economically a derivative, in a different form???
A: Absolutely no way! A derivative only pays P&L. Repo is a full-on gross instrument. And even if we use the word ""derivative"" loosely, there are legal differences with SL.

Q: Was that a plan with the counterparty to deliberately over change on margin?
A: You mean MF Global? No.

Q: What are the main regulations governing the repos in EU?
A: CCR for capital, LCR, NSFR and Leverage Ratio, Large Exposures, etc. SFTR and Short Selling Reg.