

FORUM

Triparty repos – secure investments with regulatory benefits

Triparty repos are a secure investment choice for treasurers and can be a door-opener to the wider world of securities financing. For example, the securities received through triparty repos can be re-used to meet margining requirements for derivative trades under the upcoming EMIR regulation. Otto Vaisanen, Clearstream's Head of Sales for Global Funding and Financing for Continental Europe, Africa and EMEA, tells us more.

Triparty repos are increasingly popular amongst corporate treasurers. We have not just been witnessing this trend amongst large corporates such as airlines and automotive companies, medium-sized enterprises have also begun to enter the repo world. This is hardly surprising, given that repos are a very secure investment product for treasurers who are looking to diversify their cash investments beyond term bank deposits and money market funds.

Let's quickly recap the basics of repos. The term 'repo' is short for repurchase agreement and under this agreement corporates receive collateral (defined securities) in return for cash for the duration of the trade with the financial counterparty.

At the end of the term, both the securities and the cash (plus a fee to the corporate – the 'repo rate') are returned. The tri-party element comes in when a collateral agent handles all the administration, segregation, margining and reporting in addition to ensuring that the deal is closed out. The tri-party service fees are only paid by the counterparty that borrows the cash.

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Triparty repo is low risk investment product with reduced counterparty risk. Monitoring and operations are handled by third party agents. In addition, triparty repos offer security and potentially better yields compared to normal cash deposits in the current negative interest environment. The fact that the cash traded in a repo is fully collateralised – daily mark-to-market adjustments maintain this throughout the term – provides welcome reassurance to treasurers. In the past, treasurers have sometimes been deterred from entering the repo market because of the lengthy GMRA negotiations with each counterparty. The Clearstream Repurchase Conditions (CRC) set out triparty provisions and collateral acceptability in one single document and give the signatories access

to all the counterparties within the CRC community. Generally speaking, the CRCs make it easy to get started in triparty repos and this is another reason why we are witnessing an increasing interest from medium-sized corporate treasuries.

Re-use of securities

Triparty repos are not only attractive for corporate treasuries as an investment tool; they can also re-use the securities they receive for other purposes, such as for meeting regulatory requirements.

The margining challenge

Corporates are increasingly affected by regulations adopted in the aftermath of the financial crisis, such as EMIR. EMIR will strengthen central clearing requirements for standardised derivative transactions and introduce additional margin requirements on uncleared derivatives to reduce systemic risk. The securities received from triparty repos could be used to meet these requirements.

However, it is not enough to dispose of securities for margining, the actual margining process under EMIR is very complex. Both financial and non-financial counterparties will be required to exchange two-way initial margin on a non-netted basis. The collateral needed for meeting the initial margin must be segregated at a non-affiliated, third-party custodian or triparty agent.

It is therefore advisable to outsource all derivatives margining to third-party providers as this not only increases efficiency but also gives corporate treasurers the reassurance that their operations are compliant with increasingly complex regulations. More specifically, corporate treasurers will face the following challenges:

- Matching instructions

Differing margin calculation methods can lead to disputes over the amount of initial margin required by each party. With a central service, both amounts are compared and the lower of the two values will automatically be transferred while the remaining amount needs to be resolved bilaterally between the counterparties. This is faster and more efficient than waiting for delivery until both sides have made their call.

- Selection of assets

Risk tolerance levels for specific issues or assets can be cumbersome to apply without automation. In our Global Liquidity Hub, customers can set concentration and risk limits for asset classes, resulting in bespoke asset allocation with the cheapest-to-deliver securities.

- Asset servicing

EMIR requires that the assets covering initial margin are held by an independent party and segregated from other assets in an escrow model. We do exactly this but also handles automatic substitution, corporate actions and reporting in real-time. In addition, assets are re-valued daily, and automatically topped up/returned as the market value changes.

In sum, corporates can turn to triparty providers for all their secured financing needs. In addition to a comprehensive triparty repo service, optimal collateral re-use is ensured to support corporate treasurers in complying with the upcoming EMIR regulation.

QUICK FACTS – REPOS

- 'Repo' is an abbreviation of 'repurchase agreement'. To the seller, the instrument is known as a repo, and to the buyer (the investor) it is known as a reverse repo.
- A repo (or reverse repo) is a secured form of money market instrument in which one counterparty sells securities or other assets to another with the agreement to sell them back on a pre-agreed date.
- A variety of assets are eligible for tri-party repo, including government bonds, corporate bonds, equities and funds.
- The interest rate (or repo) rate is calculated as the difference between the sale and repurchase date of the security.
- The use of 'haircuts' (margins) adds additional protection against changes in asset prices, usually assessed in percentage terms. For example, a haircut of 2% may be added to the market value of an asset, which can differ according to asset class.
- The maturity of a repo is variable, usually up to 90 days, but longer maturities are also widely supported.



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