Overview:
The $2.3 trillion daily turnover in the repurchase, or repo, market is a vital, but not always well understood, part of the U.S. financial system. The repo market represents a liquid, efficient, tested and safe way for firms to participate in a short-term financing arrangement, providing funding for their day-to-day business. Repurchase agreements, or repos, are a sale of financial assets combined with a promise to repurchase those assets in the future (in many cases, the repurchase is agreed for the following business day). These arrangements have the economic characteristics of a secured loan – cash vs. collateral – and are used by short-term institutional cash investors as a secured money market instrument and by dealers as a way to finance long positions in securities.

While a broad array of assets may be financed in the repo market, the financial assets most commonly used include U.S. government and Federal agency securities, high quality mortgage-backed bonds and corporate bonds and money market instruments. Recent data for the tri-party repo (a form of repo that uses an agent to maintain cash and securities accounts for both parties) market, which represents a significant part of the entire U.S. repo market, indicates that U.S. government securities account for approximately 40.1 percent by dollar value of the most common collateral types, agency mortgage-backed securities and collateralized mortgage obligations account for 32.8 percent, and equities make up 10.4 percent. In addition, non-agency mortgage-backed and asset-backed securities account for roughly 6.3 percent, corporate bonds represent 4.9 percent, Federal agency and government sponsored enterprises securities (for example, Fannie Mae and Freddie Mac) account for approximately 3.6 percent, and other (which includes collateralized debt obligations, international securities, municipality debt, and whole loans) account for 2.1 percent.

Benefits for both individual market participants and the financial system:
A liquid and developed repo market allows market participants, most prominently the primary dealers1, to act as market makers in fixed income securities and thus contribute to the highly liquid secondary markets in these securities. In particular, the active repo market allows market makers to finance an inventory of securities and to source securities that are not in inventory in order to meet secondary market, or investor, demand. This ability to finance and source securities in an efficient way contributes to lowering interest rates paid by the issuers, most notably the U.S. Treasury. This, in turn, lowers the debt-service cost borne by taxpayers.

The repo market presents significant advantages to both cash providers (investors such as money market funds and insurance companies) and those who require financing (such as primary dealers and other market

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1 The current list of firms that are U.S. primary dealers is available on the Federal Reserve Bank of New York’s website at [http://www.newyorkfed.org/markets/pridealers_current.html](http://www.newyorkfed.org/markets/pridealers_current.html).
makers). Cash investors have flexibility as to term of investment (overnight to, in some cases, one year), are fully collateralized, usually with additional margin, by the financial assets subject to repurchase, and receive competitive money market rates of return. Repo allows these investors to manage excess cash balances safely and efficiently. Dealers, on the other hand, benefit from the significantly reduced funding costs that repo provides, the ability to finance long positions in financial assets, and the ability to borrow securities in order to cover short positions and satisfy client needs. Long-holders of securities can also gain incremental returns by engaging in repo transactions with cash investors for securities they own but have no immediate need to sell.

**Important sectors of the economy participate in the repo market:**

Significant participants in the repo market include the primary dealers, central banks, (including the U.S. Federal Reserve in connection with its implementation of monetary policy), banks, insurance companies, industrial companies, municipalities, mutual funds, pension funds and hedge funds. These entities all benefit from the operational efficiency, security, and low funding costs available in the repo market.

**Safety of the repo market:**

The repo market has been tested over the years and during the recent credit crisis, and performed reliably. Repos offer cash providers collateralization (with additional margin requirements in most cases) and that collateral is marked-to-market daily to ensure continuing protection. The operational efficiencies developed through tri-party repo and the largely-centralized settlement mechanism for repos further minimizes risks. In addition, recent reforms in the tri-party repo market have further enhanced the resiliency of this market. Market standard documentation, broadly accepted in the market, provides further certainty for market participants.

**STATISTICS**
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