Discussion of “Securities Financing . . . “
Breach and King

Gary Gorton

Yale and NBER

New Evidence on Securities Financing

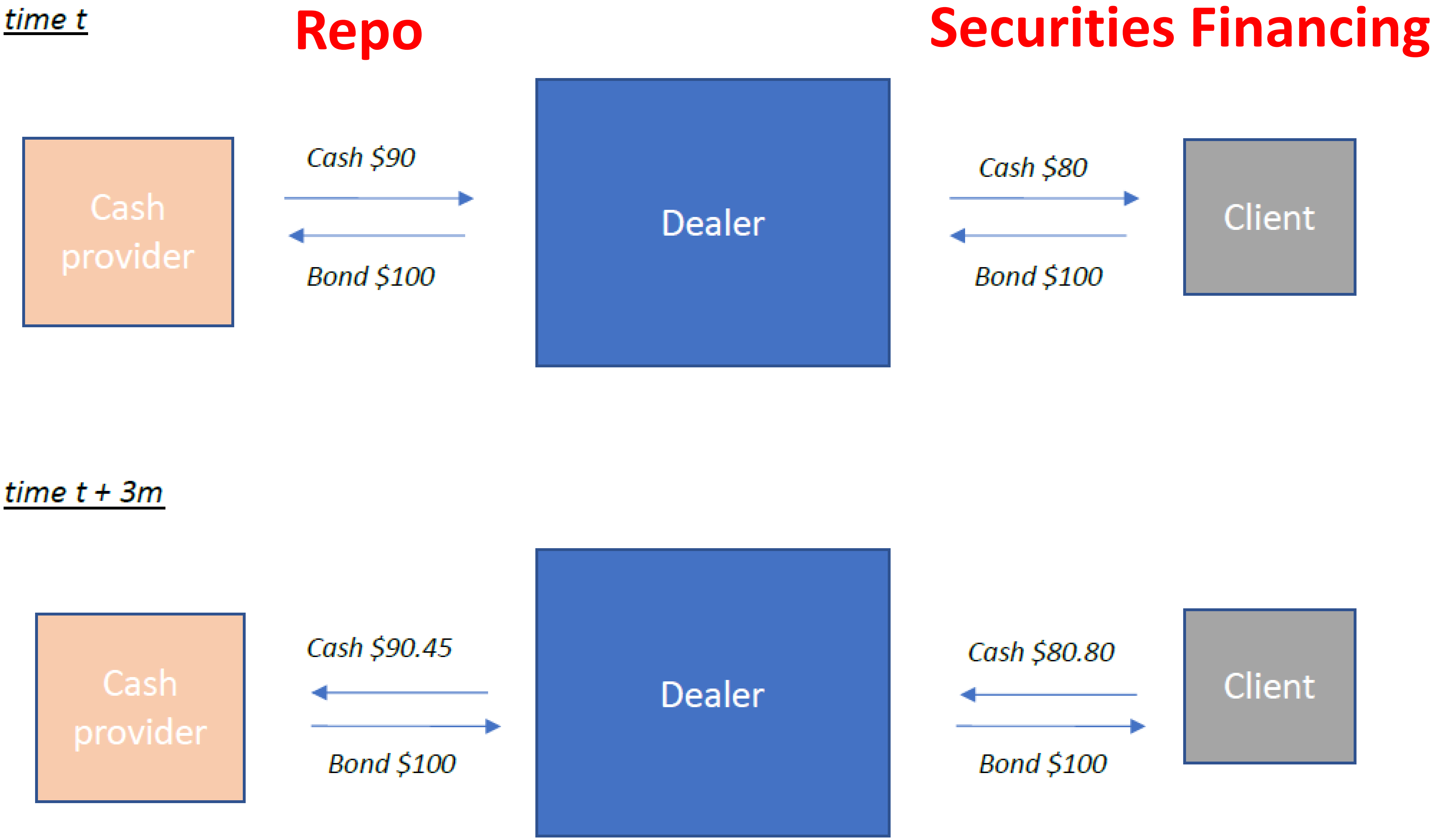
- More evidence/data on opaque markets is welcome.
- First authors to use this survey data.

Data

- Analogous to Senior Loan Officer Opinion Survey—substitute dealer bank for commercial bank.
- Survey BDs about "lending to clients collateralized by securities".
- Quarterly data over 2010Q2-2017Q4.
- Seven asset classes: agency MBS, HY bonds, IG bonds, equities, ABS CMBS, RMBS.
- Ask about spread, haircut, maximum maturity, maximum amount.
- Average borrower and most-favored borrower.
- No info about identities of DBs.

What moves lending terms? Some Candidates

- Returns and realized vol
- Issuance
- Trading volume
- Financing volume
- Fails to deliver
- Amihud liquidity
- Tri-party data


time t
Repo
Securities Financing
Cash provider
Cash $90
Bond $100
Dealer
Cash $80
Bond $100
Client
time t + 3m
Cash provider
Cash $90.45
Bond $100
Dealer
Cash $80.80
Bond $100
Client

Not About Repo

- Repo is how BDs finance themselves. Pick up the liquidity premium by producing private money.

- E.g., BDs pay, say 3% overnight and provide collateral; BD gets the return on the collateral, say 6%.

- Not clear how much matched book there really is.

Result #1

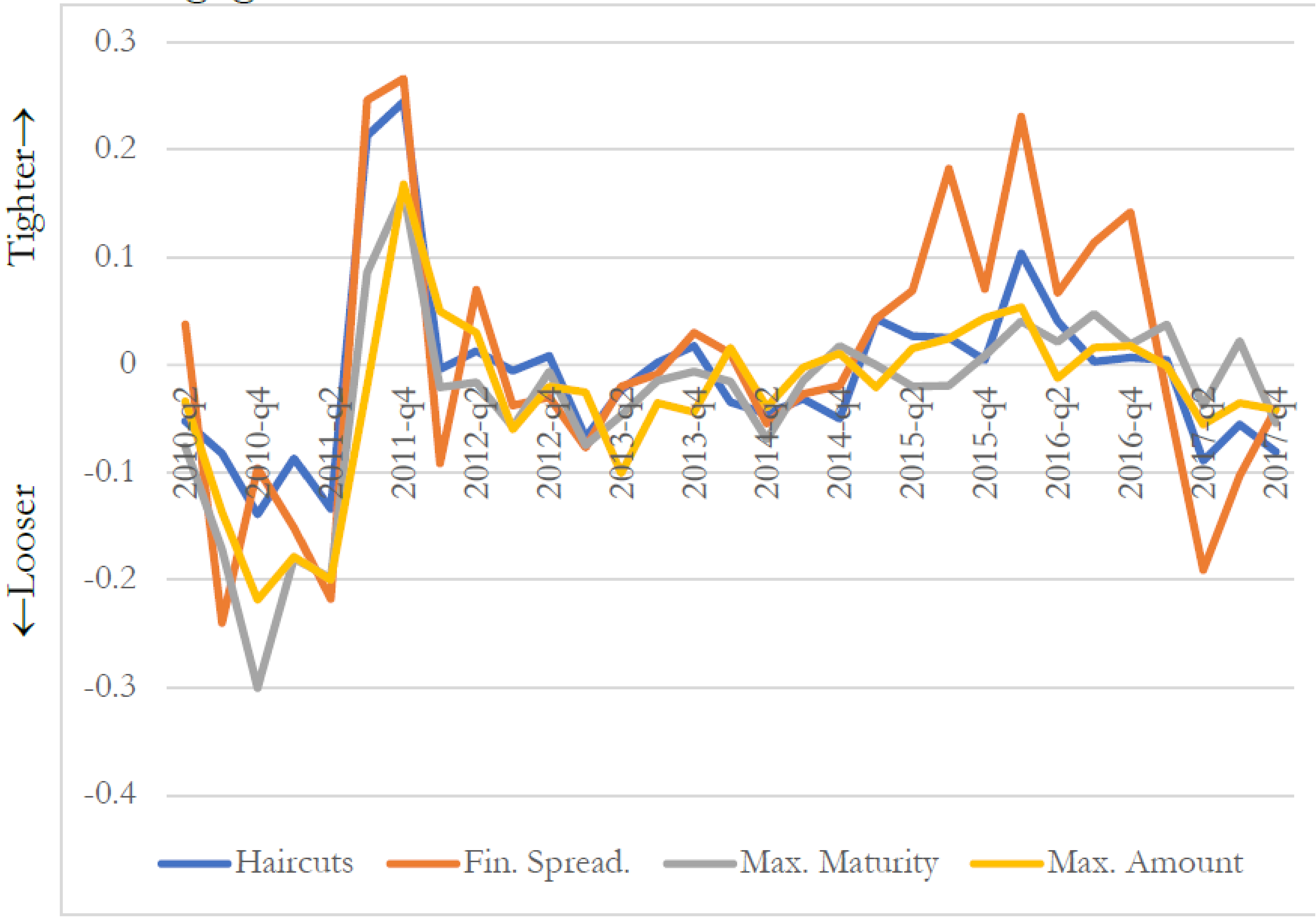
- “. . . Dealers do not change securities-financing terms very frequently.”

% dealers changing terms	Ave.	0.16	0.08	0.08	0.10
	MF	0.14	0.08	0.09	0.11

- Haircuts designed to fully secure the loan, so nothing changes if the loan is then “riskless” in “normal” times.

- When do the changes happen? When market conditions change.

A. Averaging across all asset classes



HEDGE FUNDS - AMERICAS JANUARY 11, 2012 / 11:45 AM / 7 YEARS AGO

The great hedge fund humbling of 2011

Svea Herbst, Katya Wachtel

8 MIN READ

2011: Disastrous Year For Mutual, Hedge Fund Managers

Result #2

- “When terms do change . . . they all tend to change together.”

- Change favorably or unfavorably? Mostly tighter over sample period.

Result #3

- “. . . The single factor that emerges as most important is the liquidity of the underlying markets.”

- Aside from the Amihud measure, not clear what “liquidity” is here.

- Changes in issuance?, TED spread?

Result #4

- “For all counterparties, ‘competition’ is the most frequently cited reason for changing terms.”
- “Apart from that, dealers generally cite ‘liquidity’ . . . “
- “Competition”---but BDs do not change the terms often, so who is the competition?

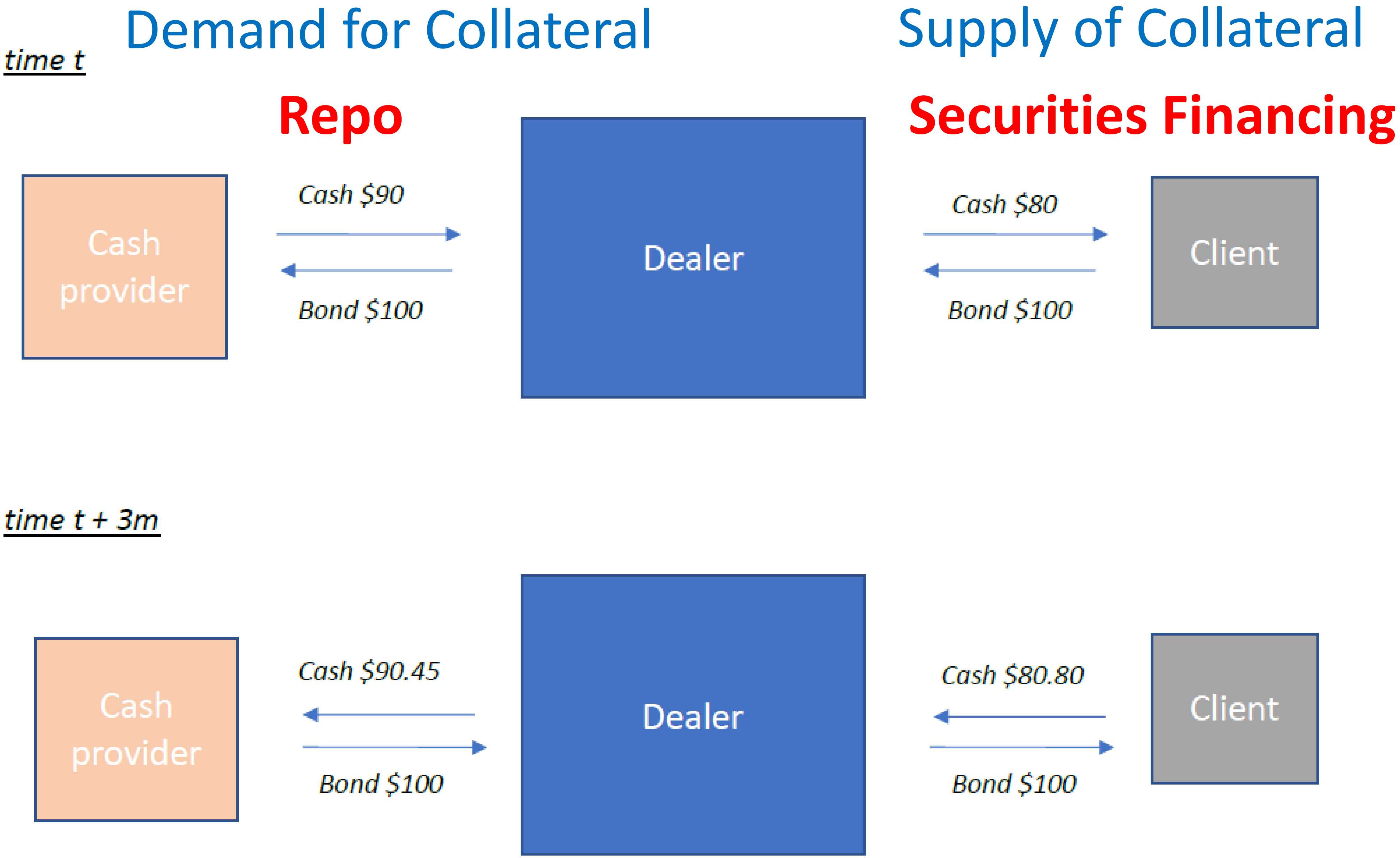
What’s going on?

- Who are the agents borrowing $$ and providing collateral? Hedge funds who want leverage.

- But BDs also need collateral. They source collateral from these agents.

The Collateral Market

- If the demand for repo goes up, more collateral must be sourced: terms change.
- Collateral more valuable when it is scarce, reflected in convenience yields.
- Convenience yields related to outstanding amounts.


Demand for Collateral
Supply of Collateral
time t
Repo
Securities Financing
Cash provider
Cash $90
Bond $100
Dealer
Cash $80
Bond $100
Client
time t + 3m
Cash provider
Cash $90.45
Bond $100
Dealer
Cash $80.80
Bond $100
Client

Conclusion

- Interesting paper. First look at secured financing.
- Terms move together; related to market conditions.