RP's, GC, FF

If I sell 1 MIL 10YR NOTE
I need to borrow the NOTE & give the note holder 1 million$. The lender of the note will earn the RP rate. The lender of the note can then lend the one MIL out @ GC, if there's a beneficial spread.

Say, 10YR Rate = 1.35
GC Rate = 3.00.

That benefits the owner of the note because he will make the difference between those rates

Another Example

I'm long 1 5yr note. Coupon = 2.50. I see that the 5YR is on special @ 1.35%. So, I lend the 5YR out and receive 1 million $'s @ a cost of 1.35%. I ~~E~~ then turn around & lend the $ out @ GC for 3%. ~~The~~ I earn the difference of the two rates 1.35 & 3.00%.

The risk is what I'm receiving in GC as Collateral.

GC & FF are 2 different markets.

Federal Funds are o/n borrowings & lendings by banks in the Federal Reserve System. ~~If I have extra $~~ [illegible]
The Funds are based on reserve requirements.
If I have more reserves than I need, then, I'll lend the excess out to another bank that ~~needs~~ needs the $ to meet reserves. →

The Interest rate on the loan is "The Federal ~~Fund~~ Funds Rate".
This lending & borrowing of Reserves is simply a redistribution of $ within the system.
Participants: Commercial Banks, S&Ls, GSEs, Securities firms etc...

Repo Buyer	Repo Seller
Receives security ⟷	Gives ~~$~~ Security
Gives $ ⟷	Receives $
~~Earns Interest rate on~~	

	Receives Security	Receives $
Buyer	~~Pay~~ Earns Coupon Interest Rate	Pays GC Interest rate OR SPECIAL RATE
Seller	Pays Coupon Interest	Earns GC or Special I.R.

	RePo	Reverse RePo
	Borrower	LENDER
	Seller	Buyer
	Receives $	Gives $
Near leg	Sells securities	Buys securities
Far leg	Buys "	Sells "

Basic motivation for transacting RPs is the borrowing & lending of cash.
Reverse Repo is from the buyers viewpoint. They are the same ~~as~~ a RP. They're simply being described from a different viewpoint

Buyer of RP = opportunity to invest cash for a customized period of time.
Inside a trading firm RPs are used to finance positions (long), obtain access to cheaper funding cost of other speculative instruments & cover short positions in securities.
If the fed does "matched sales" they're simply doing Reverse RPs.

<u>Fed Funds</u> are <u>un</u>collateralized lending rate between banks
<u>Repos</u> are collateralized, usually by U.S. Treasuries.
When the fed is dealing w/RPs the are usually always collateralized by UST.