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FACILITATING CROSS-MARGINING: TREASURY MARKET TRADES AND INTEREST RATE FUTURES

Cross-margining of U.S. Treasury positions and interest rate futures can improve the efficiency and resilience of the U.S. Treasury market by tying margin requirements more closely to the risk of a given portfolio. However, only the largest and most sophisticated market participants have historically been able to cross-margin these positions. The principal reason for this limitation is that U.S. Treasury positions and interest rate futures are cleared at different central counterparties and subject to different regulatory regimes. Although these factors certainly present complications, the authors argue that there are well-established mechanisms that can allow customers to benefit from cross-margining without losing critical customer protections.

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I. INTRODUCTION

Market participants, regulators, and scholars have recently sought to identify mechanisms that will increase the liquidity, resilience, and stability of the U.S. Treasury market.[1] Although these authors have differed on a number of issues, one area of clear agreement is that cross-margining of U.S. Treasury positions and interest rate futures would increase liquidity, improve risk-management, and reduce the likelihood of market disruption in the U.S. Treasury market. For example, the Group of Thirty recently observed that "[w]ider use of cross-margining would reduce the risk that increases in initial margin requirements on the futures leg of cash-futures basis trades result in forced sales of Treasury securities, which may have contributed to selling pressures in the Treasury market in March 2020."[2]

[1] Group of Thirty Working Group on Treasury Market Liquidity, *U.S. Treasury Markets: Steps Toward Increased Resilience*, GROUP OF THIRTY (July 2021), https://group30.org/publications/detail/4950 [hereinafter *Steps Toward Increased Resilience*]; FIA Principal Traders Group, *Clearing a Path to a More Resilient Treasury Market*, FIA (July 2021), https://www.fia.org/sites/default/files/2021-07/FIA-PTG_Paper_Resilient%20Treasury%20Market_FINAL.pdf; The Depository Trust and Clearing Corporation, *Making the U.S. Treasury Market Safer for All Participants: How FICC's Open Access Model Promotes Central Clearing*, DTCC (Oct. 2021) https://www.dtcc.com/-/media/Files/Downloads/WhitePapers/Making-the-Treasury-Market-Safer-for-all-Participants.pdf;

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U.S. Department of the Treasury et al., *Recent Disruptions and Potential Reforms in the U.S. Treasury Market: A Staff Progress Report*, TREASURY.GOV (Nov. 8, 2021), https://home.treasury.gov/system/files/136/IAWG-Treasury-Report.pdf [hereinafter *Staff Report*].

[2] *Steps Toward Increased Resilience* at 14.

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