BANK OF CANADA
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Staff analytical paper / Document analytique du personnel—2026-39

Last updated: September 14, 2026

Uncovering the use of haircuts in the Canadian repo market

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DOI: https://doi.org/10.34989/sap-2026-39 | ISSN 3110-9195

Acknowledgements

We thank Natasha Khan, Philippe Muller and Maks Padalko for valuable comments. We are also grateful to Alasdair Graham, Adnann Syed and André Zanga who co-chair the Collateral Infrastructure and Market Practices Advisory Group’s Pricing and Haircuts Workstream for sharing their insights.

Abstract

We document haircut practices in the Canadian dealer-to-client repo market using transaction level data. We find that haircuts are rarely used across repos for different collateral, maturities and most counterparty types. Notable exceptions include wealth managers and some foreign official institutions, which use haircuts more often, likely due to their specific regulations or requirements. We also find no evidence that haircut use increased materially during periods of market stress, including March 2020.

Topics: Financial institutions and intermediation; Financial stability; Financial system regulation and policies; Market structure

JEL Codes: G0, G01, G18, G2, G23, G28

Introduction

Repurchase agreement (repo) markets play a central role in the Canadian financial system by supporting the financing and intermediation of Government of Canada (GoC) and other fixed-income securities. In recent years, policymakers globally have devoted increased attention to the resilience of repo markets, particularly given the growing role of leveraged non-bank financial institutions (NBFIs) and the potential for deleveraging episodes to put pressures on liquidity in core fixed-income markets.

One policy tool that has attracted attention in discussions about repo market resilience is repo haircuts. A repo haircut is the percentage by which the market value of securities posted as collateral in a repo is greater than the amount of cash borrowed.[1] As a result, haircuts can provide overcollateralization to the cash lender, mitigating the their risk of potential losses in the event of a counterparty default, if the value of the collateral declines (International Capital Markets Association, 2025).[2] Proponents of greater use of repo haircuts argue that, by mitigating cash lenders' exposure to counterparty credit and market risks before periods of market stress, haircuts can make them less likely to tighten lending terms or withdraw funding when stress occurs, thereby contributing to more stable repo funding conditions (Financial Stability Board, 2026; Bank of England, 2025).

Past work on repo haircuts in Canada found that their use was limited. This work was based on surveys and market intelligence (Investment Industry Association of Canada, 2023). In this note, we build on this work by documenting repo haircut practices between dealers and their clients in Canada using transaction-level repo data from Market Trade Reporting System over the period from 2020 to 2025.[3]

Our analysis confirms the main finding of earlier work: repo haircuts are rarely used in Canadian repo markets.[4] We find that the vast majority of repo transactions are conducted without a haircut, regardless of collateral type or maturity. This pattern is broadly consistent across market participants, although wealth managers and some foreign official institutions use haircuts more frequently, potentially reflecting regulatory requirements or internal risk management practices. We also find no evidence of broad-based increases in haircuts during periods of market stress, including at the onset of the COVID-19 crisis. Together, our results suggest that counterparty credit quality or market risks do not appear to be a primary driver of haircut use in the Canadian repo market.

[1] Though the underlying securities in a repo transaction are sold and then repurchased at maturity of the repo, for simplicity, we refer to these securities as 'collateral'.

[2] While the discussion around haircut practices mostly focuses on positive haircuts, in practice, negative haircuts can also exist. In such cases, the market value of collateral is less than the amount of cash received by the security provider, which could occur due to high demand of a specific security, possibly for covering a short position. See The international dimension of repo: five new facts (ECB, 2025) for details on sources of negative haircuts in repos.

[3] Our data from the Market Trade Reporting System contains repo transactions by Canadian Government Securities Distributors. Notably, the data does not include repo transactions conducted by the Bank of Canada or the Government of Canada.

[4] When describing our analysis, unless specified, we use the term 'repo' to describe both repo and reverse repo transactions.

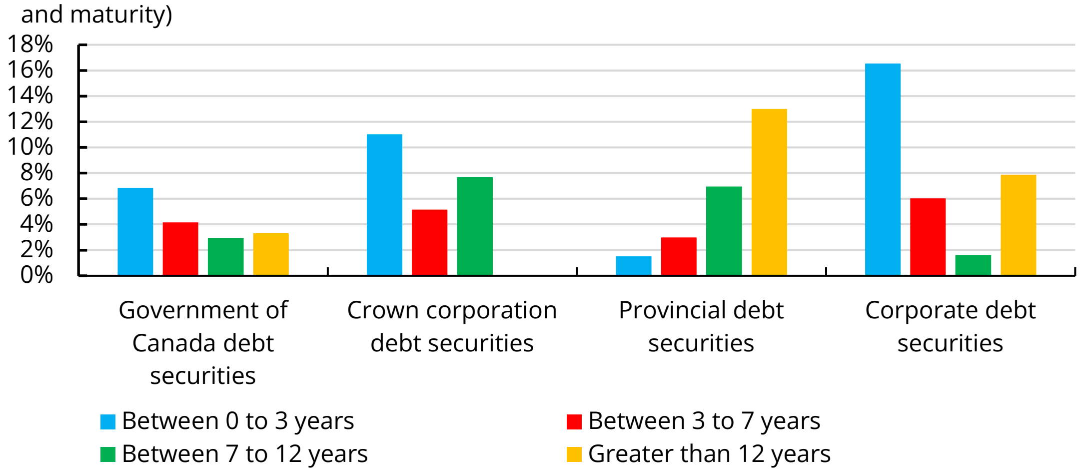
While the motivations for the limited use of haircuts are not directly observable in our data, market intelligence points to several potential explanations, including competitive pressures among dealers and the use of alternative risk management tools such as position limits and internal liquidity buffers. Overall, our findings complement previous work by providing a detailed view of haircut practices in Canadian repo markets. This transaction-level evidence may help inform initiatives such as those of the Collateral Infrastructure and Market Practices Advisory Group (CIMPA), which is considering best practices for the use of repo haircuts in Canada.[5]

Haircuts are rarely used in the Canadian repo market

Only a small share of Canadian repo transactions involve haircuts. Their use is particularly limited in repos backed by GoC securities, where only about five percent of transactions include any non-zero haircut (**Chart 1**). By comparison, haircuts are slightly more common in repos backed by other types of collateral segments, such as crown corporation debt, or longer-maturity provincial bonds or some maturity-segments of corporate bonds. These differences could reflect higher market risk relative to GoC securities or could reflect differences in the type of counterparty. For the remainder of the analysis, we focus on repos backed by GoC securities as collateral, as they account for the largest share of the Canadian repo market (Belkacem, Padalko and Walton, 2026).

Chart 1: Repos backed by Government of Canada securities have lowest incidence of haircuts

(Share of dealer-to-client repo volume with non-zero haircuts by collateral type and maturity)



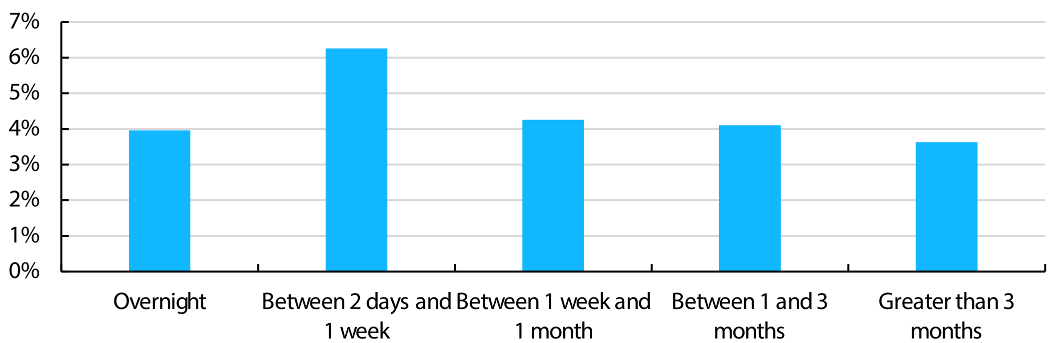
Note: Crown corporation debt securities include securities issued by the Canada Mortgage and Housing Corporation, public pension funds, and other crown corporations.

Sources: Market Trade Reporting System and Bank of Canada calculations
Last observation: December 31, 2025

[5] In Canada, the CIMPA valuations and haircuts sub-group is working on developing a principles-based guidance note on repo haircuts in consultation with broader industry participants. See CIMPA Minutes (April 16, 2026) for details.

When examining different repo maturities, we find that haircut usage in dealer-to-client repos remains limited and fairly stable across all maturity types (**Chart 2**). Discussions with market participants indicate several reasons for the limited use of haircuts. Some pointed to competitive pressures, noting that requiring haircuts could prompt clients to obtain repo financing elsewhere. Others highlighted the high credit quality and liquidity of GoC securities as reducing the need for haircuts. Dealers also noted that they manage counterparty risk using other tools, including strict counterparty limits and internal capital buffers. Similarly, asset managers reported maintaining their own liquidity buffers to absorb potential losses in the event of counterparty default.

Chart 2: Haircut use remains stable across repo maturities
(Share of dealer-to-client Government of Canada repo volume with non-zero haircuts by repo maturity)



Sources: Market Trade Reporting System and Bank of Canada calculations
Last observation: December 31, 2025

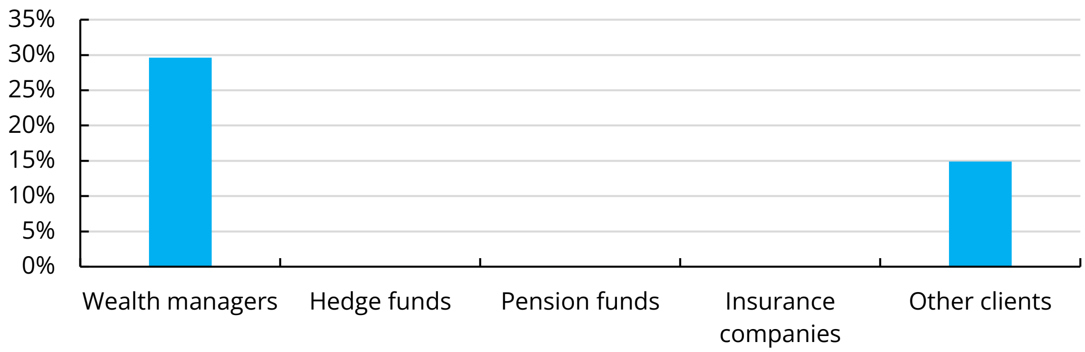
Wealth managers and some foreign official institutions use haircuts more often, likely reflecting specific institutional requirements

In this section, we examine whether haircut use differs across types of asset managers. Because policy discussions often focus on haircuts as a tool for mitigating risks associated with highly levered NBFIs, particularly hedge funds, one might expect greater use among these participants.

We find that the limited use of repo haircuts is broadly consistent across most market participants, including hedge funds. Hedge funds, pension funds and insurers conduct almost all their repo transactions without haircuts (**Chart 3**). Wealth managers and some other market participants are the main exceptions, with a higher share of transactions involving haircuts.

Chart 3: Apart from wealth managers and some other participants, limited haircut use is fairly broad-based

(Share of dealer-to-client repos with non-zero haircuts; Government of Canada collateral)



Note: "Other clients" mostly include foreign central banks and other foreign official institutions.

Source: Market Trade Reporting System and Bank of Canada calculations
Last observation: December 31, 2025

For wealth managers, this pattern likely reflects their specific regulatory requirements. Canadian investment regulations require mutual funds to receive at least a two percent haircut in their favour, when entering repo or reverse repo transactions.[6] Consistent with these requirements, we find that wealth managers typically receive excess collateral when they lend cash and receive excess cash when they borrow collateral through repos. We also find that when haircuts are applied on wealth managers' repos, the average absolute value of haircut is around two percent, which is consistent with their regulatory requirements. In discussions, some wealth managers also noted that they manage funds on behalf of clients with higher counterparty risk, which may result in larger haircuts imposed on these clients when they borrow cash using repos.

Among other market participants, the higher incidence of haircuts is driven primarily by foreign central banks and other foreign official institutions. These entities may have their own strict internal risk management requirements that require haircuts.[7] Apart from wealth managers and foreign official institutions, the broad-based limited use of haircuts across other asset manager types suggests that counterparty credit quality is not a primary driver of haircut use in the repo market.

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[6] Canadian investment fund regulations require that all repo and reverse repo transactions involving mutual funds to have at least a two percent haircut in favour of the mutual fund (overcollateralization when the fund lends cash; under-collateralization when the fund borrows cash). See National Instrument 81-102 for details.

[7] See Alridge, Sandhu and Tchamova (2024) for more details on foreign central banks and their investment goals.

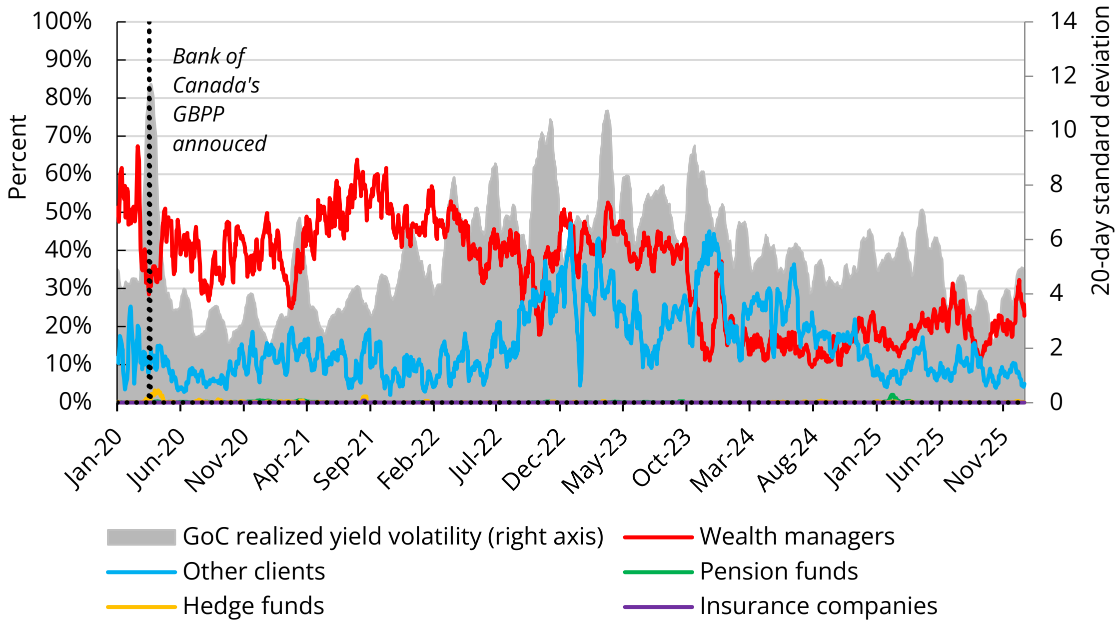
We do not find evidence that haircuts are procyclical in Canada

In some jurisdictions, repo haircuts have increased during periods of market stress, requiring borrowers to post additional collateral. This can force asset sales to meet collateral calls and amplify illiquidity in fixed-income markets. The 2022 UK liability-driven investment (LDI) episode is a prominent example. Rapid increases in UK gilt yields led to large collateral and margin calls on leveraged LDI fund positions, resulting in worsened liquidity conditions. Illiquidity was further amplified by sharp increases in haircuts on gilt repos to LDI funds, from their typical zero or near-zero levels (Bank of England, 2025). While increases in haircuts can reflect prudent risk management, it can amplify illiquidity if the increases are large and sudden during stress events. In this context, it has been argued that having some level of repo haircuts in normal times could reduce the need for dealers to increase haircuts during periods of market stress.

We do not find evidence of this type of procyclicality in Canada. Haircut use remained generally stable within groups of market participants during periods of elevated volatility in the GoC bond market (**Chart 4**). Most notably, during the highest period of market volatility in March 2020, there was no meaningful increase in haircut use across any counterparty type. Looking at other periods of elevated volatility, haircut use does increase for "Other clients" during parts of 2022 and 2023, the increase is modest and largely reflects greater repo market activity by foreign central banks and other foreign official institutions, rather than higher haircuts being imposed in a particular segment of the repo market.

Chart 4: Haircut use among market participants has not historically increased with market volatility

7-day moving averages
(Left scale: Share of each client type's Government of Canada repo volume with non-zero haircuts; Right scale: Realized volatility of Government of Canada bonds)



Note: The Bank of Canada announced the Government of Canada Bond Purchase Program (GBPP) on March 27, 2020, to address market strains caused by the COVID-19 pandemic.

Source: Market Trade Reporting System, Refinitiv Workspace and Bank of Canada calculations
Last observation: December 31, 2025

We also examine changes in the level of repo haircuts in response to market volatility using a regression framework that controls for a range of transaction characteristics, including counterparty and bond fixed effects. We do not find a significant positive relationship between changes in haircuts and market volatility. Overall, our analysis suggests that procyclical increases in repo haircuts have not been a prominent feature of the Canadian repo market in our sample, likely reflecting the competition among dealers and alternative approaches to risk management discussed earlier.

Conclusion

Our analysis shows that haircuts are rarely used in the Canadian repo market. This pattern is broadly consistent across repo maturities and market participants. Wealth managers and foreign central banks and other official institutions are notable exceptions, likely reflecting regulatory requirements and institution-specific risk-management practices. We do not find evidence that repo haircuts have been procyclical in Canada, as haircut use did not change during periods of market stress, including March 2020. Overall, our results suggest that counterparty credit and market risks do not seem to be the main drivers of haircuts in Canadian repo markets.

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