The March 2022 Senior Credit Officer Opinion Survey on Dealer Financing Terms

Summary

The March 2022 Senior Credit Officer Opinion Survey on Dealer Financing Terms collected qualitative information on changes in credit terms and conditions in securities financing and over-the-counter (OTC) derivatives markets. In addition to the core questions, the survey included a set of special questions about the potential effects of hypothetical future changes in the interest rate environment on the price and nonprice terms of financing offered by dealers and on the demand for funding from different types of clients. The special questions also asked about how different classes of clients are positioned for such changes. The 23 institutions participating in the survey account for almost all dealer financing of dollar-denominated securities to non-dealers and are the most active intermediaries in OTC derivatives markets. The survey was conducted between February 8, 2022, and February 22, 2022. The core questions asked about changes between December 2021 and February 2022.[1]

Core Questions
(Questions 1–79)[2]

With regard to the credit terms applicable to, and mark and collateral disputes with, different counterparty types across the entire range of securities financing and OTC derivatives transactions, responses to the core questions revealed the following:

- Price and nonprice terms on securities financing transactions and OTC derivatives were generally unchanged across all classes of counterparties (see the exhibit "Management of Concentrated Credit Exposures and Indicators of Supply of Credit").

- A small fraction of respondents indicated that resources and attention devoted to managing concentrated credit exposure to central counterparties and other financial utilities increased somewhat. More than one-half of dealers indicated that changes in central counterparty practices have affected, at least to a minimal extent, the credit terms they offer to clients on bilateral transactions that are not cleared.

- Approximately one-fourth of dealers, on net, reported that the volume of mark and collateral disputes increased over the past three months for hedge funds; about one-fifth reported an increase for dealers, mutual funds, exchange-traded funds, pension plans and endowments, and insurance companies; and a small fraction reported an increase for

[1] For questions that ask about credit terms, net percentages equal the percentage of institutions that reported tightening terms ("tightened considerably" or "tightened somewhat") minus the percentage of institutions that reported easing terms ("eased considerably" or "eased somewhat"). For questions that ask about demand, net fractions equal the percentage of institutions that reported increased demand ("increased considerably" or "increased somewhat") minus the percentage of institutions that reported decreased demand ("decreased considerably" or "decreased somewhat").
[2] Question 80, not discussed here, was optional and allowed respondents to provide additional comments.

nonfinancial corporations. On net, dealers reported little change in the duration and persistence of mark and collateral disputes with all client types.

With respect to clients' **use of financial leverage**, dealers indicated little change, on net, over the past three months for all types of counterparties (see the exhibit "Use of Financial Leverage").

With regard to **OTC derivatives markets**, responses to the core questions revealed the following:

- Nonprice terms in master agreements for OTC derivatives remained largely unchanged.

- Approximately one-fourth of dealers reported an increase, on net, in the volume of mark and collateral disputes over the past three months for foreign exchange and equity derivatives, and a small fraction of respondents reported an increase, on net, for credit referencing corporates, credit referencing securitized products, and interest rate derivatives. The duration and persistence of mark and collateral disputes remained unchanged on net.

With respect to **securities financing transactions**, respondents indicated the following:

- For most asset classes, terms under which various types of securities are funded remained largely unchanged. About one-fifth of respondents, on net, indicated easing of collateral spreads for commercial mortgage-backed securities (CMBS) for both average and most-favored clients. For high-yield corporate bonds, a small fraction of respondents, on net, indicated tightening of collateral spreads for both average and most-favored clients.

- On net, about one-fifth of dealers reported increased demand to fund CMBS, and a similar net fraction reported increased demand for term funding of CMBS. On net, the demand for funding of other asset classes was largely unchanged (see the exhibit "Measures of Demand for Funding and Market Functioning").

- On net, liquidity and market functioning for all asset classes remained unchanged.

- The volume and duration of mark and collateral disputes remained unchanged, on net, across all collateral types.

Special Questions on the Effects of Hypothetical Changes in the Interest Rate Environment (Questions 81–87)

U.S. Treasury yields varied significantly over the past year, and interest rate volatility rose in the last quarter of 2021. The special questions asked about the potential effects of hypothetical future changes in the interest rate environment on the price and nonprice terms of financing offered by dealers and on the demand for funding from different types of clients. The questions also asked about how different classes of clients are positioned for such changes. Two hypothetical scenarios of the Treasury yield curve changes were considered.

The **upward parallel yield curve shift scenario** assumed an upward parallel shift in the Treasury yield curve over the first half of 2022 with 2-year and 10-year Treasury yields increasing 50 basis points from the levels observed at the end of January 2022 by July 2022. With respect to this scenario, dealers reported the following:

- Approximately one-fifth of respondents, on net, indicated that both price and nonprice terms offered to clients would tighten somewhat under the scenario.[3]

- A net fraction of about one-fourth of respondents indicated that insurance companies as well as pension plans and endowments were more typically net long with respect to this scenario than net short.[4] For other client types, the fraction of respondents reporting that more clients were net long than net short was similar to the fraction reporting the opposite.

- Nearly one-half of dealers, on net, expected somewhat increased demand for funding from global macro hedge funds under this scenario. Approximately two-fifths of respondents, on net, expected somewhat increased demand for funding from insurance companies and fixed income arbitrage hedge funds, and one-fourth expected somewhat increased demand for funding from trading real estate investment trusts and nonfinancial corporations.

The **yield curve flattening scenario** assumed a flattening of the Treasury yield curve over the first half of 2022 with 10-year Treasury securities remaining comparable with those observed at the end of January 2022, and with yields on 2-year Treasury securities increasing 50 basis points from the levels observed at the end of January 2022 by July 2022. With respect to this scenario, dealers reported the following:

- Approximately one-fifth of respondents, on net, indicated that both price and nonprice terms offered to clients would tighten somewhat under the scenario.

- Approximately one-fourth of respondents, on net, reported that nonfinancial corporations were more typically net long with respect to this scenario than net short. For other client types, the fraction of respondents reporting that more clients were net long than net short was similar to the fraction reporting the opposite.

- A small net fraction of dealers expected somewhat decreased demand for funding from fixed income arbitrage hedge funds under the scenario. On net, dealers expected basically unchanged demand for funding from other types of clients.

This document was prepared by Pawel Szerszen, Division of Research and Statistics, Board of Governors of the Federal Reserve System. Assistance in developing and administering the

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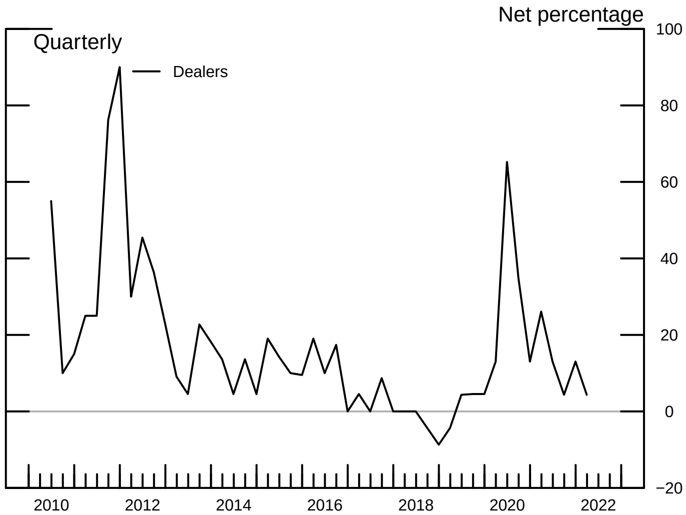
[3] In the survey, tightening and easing of price terms were defined as widening and tightening of spreads offered for clients above a dealer's cost of funding, respectively.

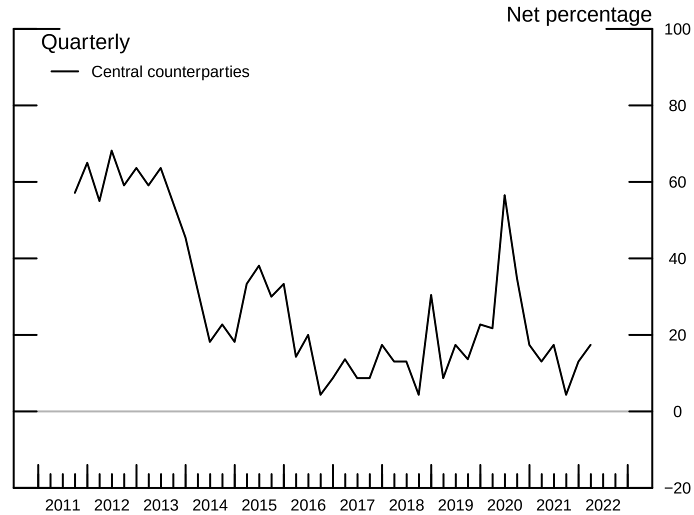
[4] In the survey special questions, "net long" was defined to mean that the clients' positions would be expected to increase in value, on net, under the given scenario, and "net short" was defined to mean that the clients' positions would be expected to decrease in value on net.

survey was provided by staff members in the Capital Markets Function, the Statistics Function, and the Markets Group at the Federal Reserve Bank of New York.

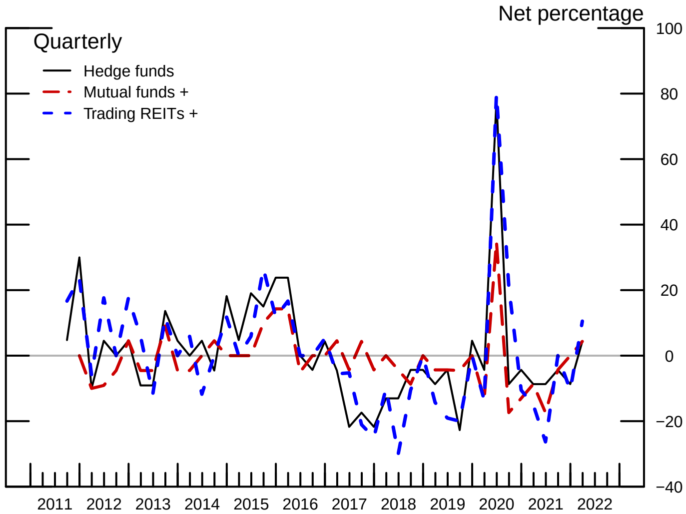
Management of Concentrated Credit Exposures and Indicators of Supply of Credit

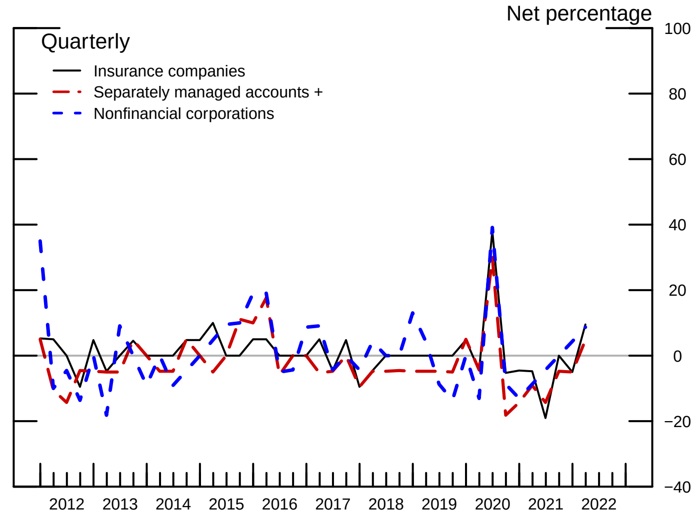
Respondents increasing resources and attention to management of concentrated exposures to the following:



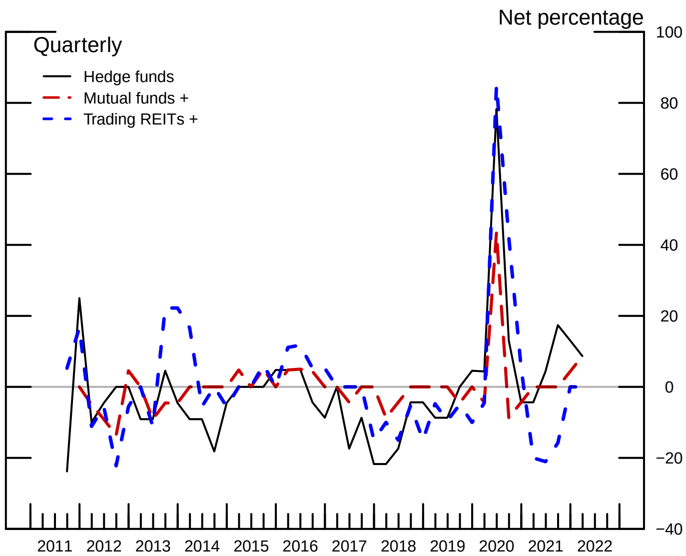


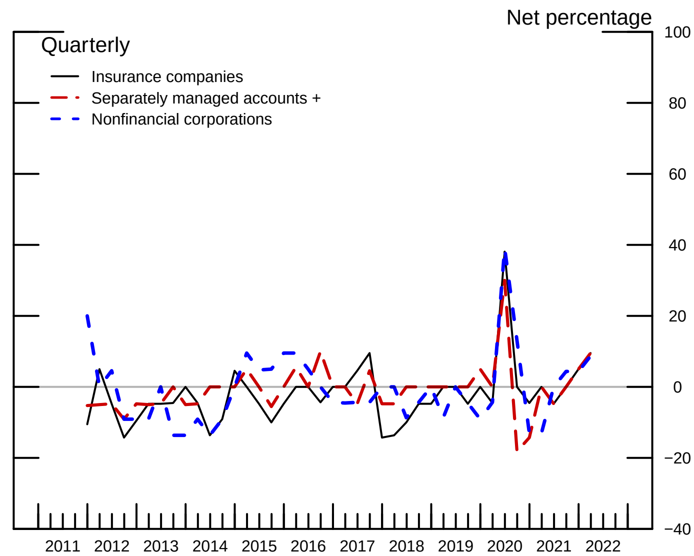
Respondents tightening price terms to the following:





Respondents tightening nonprice terms to the following:

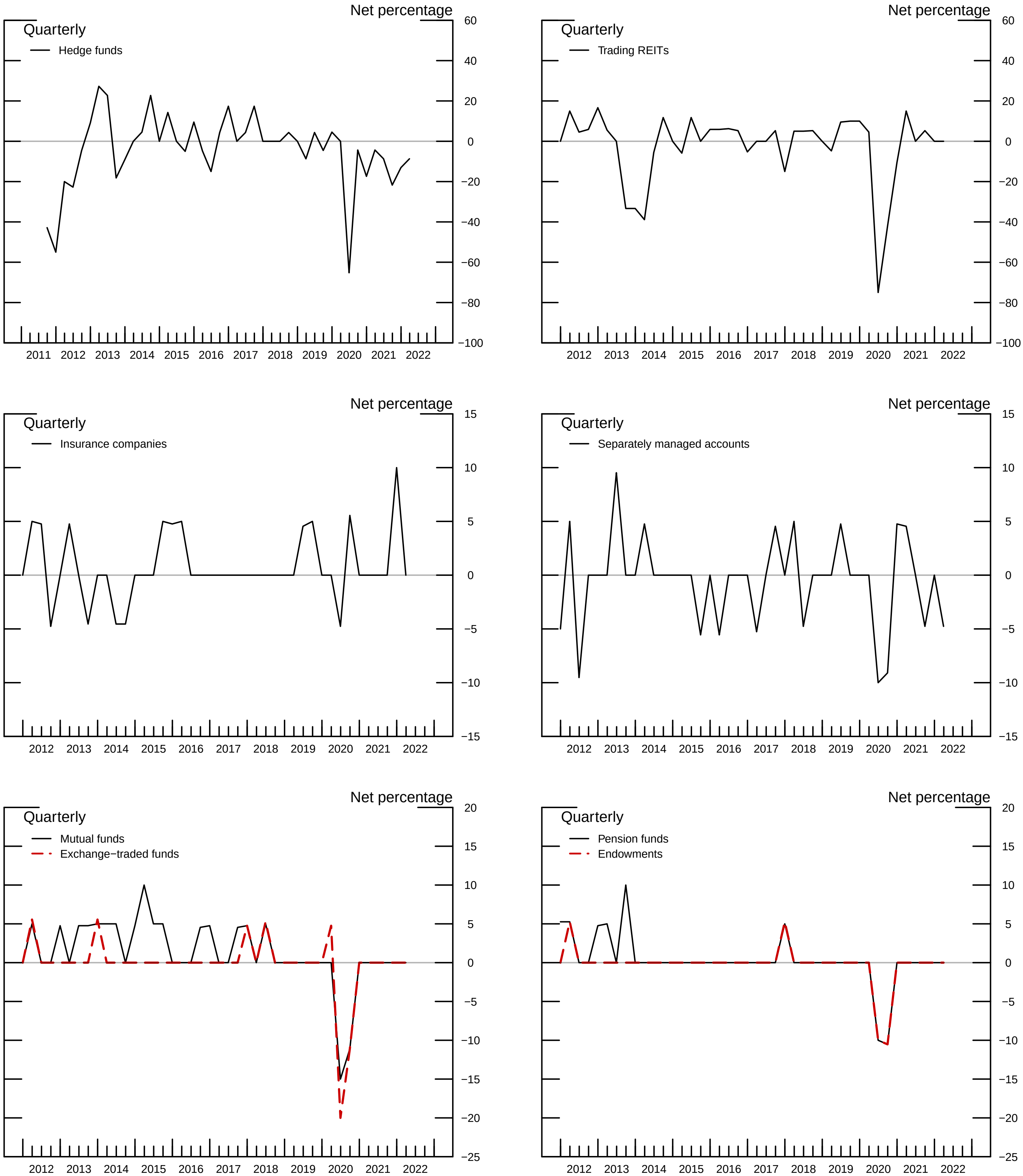




Note: REIT is real estate investment trust.
+ The question was added to the survey in September 2011.
Source: Federal Reserve Board, Senior Credit Officer Opinion Survey on Dealer Financing Terms.

Use of Financial Leverage

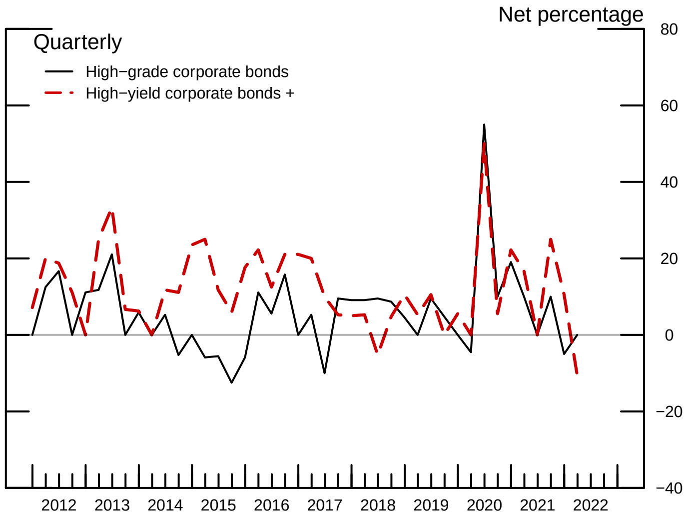
Respondents reporting increased use of leverage by the following:

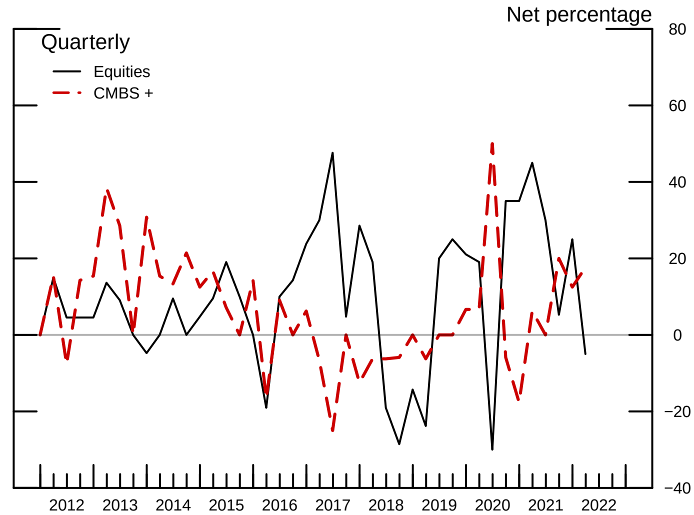


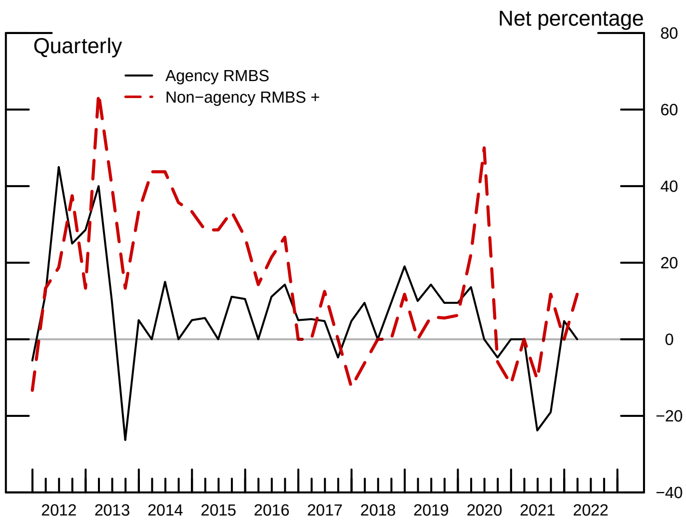
Note: REIT is real estate investment trust.
Source: Federal Reserve Board, Senior Credit Officer Opinion Survey on Dealer Financing Terms.

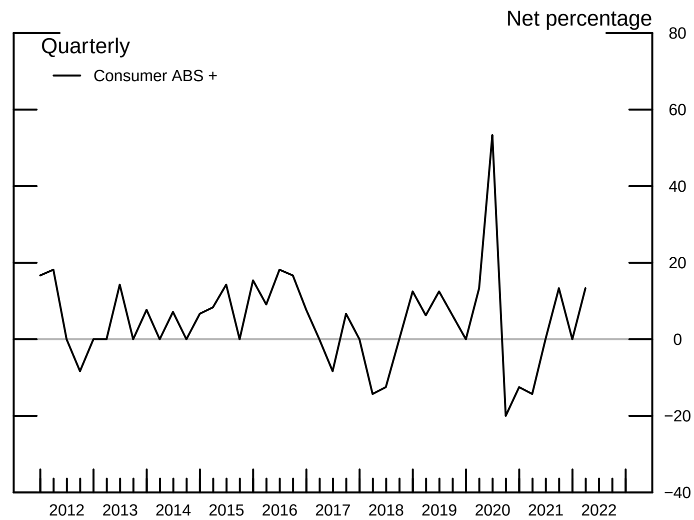
Measures of Demand for Funding and Market Functioning

Respondents reporting increased demand for funding of the following:

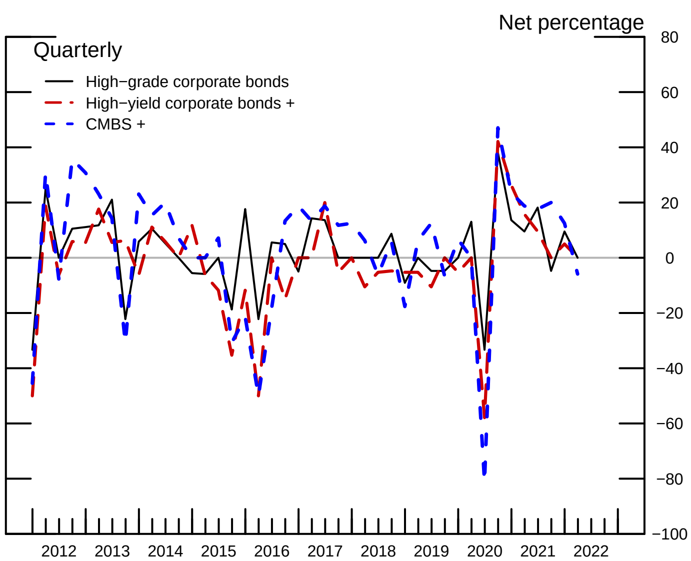


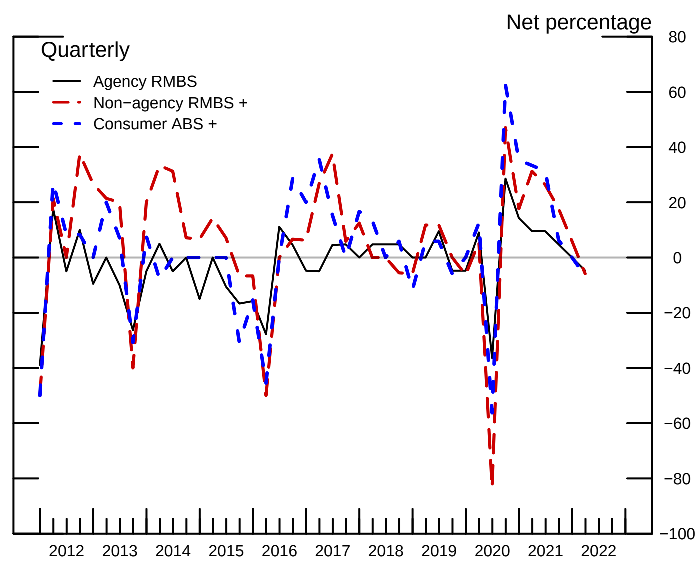






Respondents reporting an improvement in liquidity and functioning in the underlying markets for the following:





Note: CMBS is commercial mortgage−backed securities, RMBS is residential mortgage−backed securities, and ABS is asset−backed securities.
+ The question was added to the survey in September 2011.
Source: Federal Reserve Board, Senior Credit Officer Opinion Survey on Dealer Financing Terms.