

The March 2021 Senior Credit Officer Opinion Survey on Dealer Financing Terms

Summary

The March 2021 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 between December 2020 and February 2021. In addition to the core questions, the survey included a set of special questions about the transition away from LIBOR (London interbank offered rate) for U.S. dollar-denominated OTC derivatives. 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, 2021, and February 22, 2021. The core questions asked about changes between December 2020 and February 2021.¹

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:

- Small net fractions of dealers reported an easing in price terms on securities financing transactions and OTC derivatives across all counterparty types (see the exhibit “Management of Concentrated Credit Exposures and Indicators of Supply of Credit”). Nonprice terms generally remained unchanged, although one-fifth reported an easing of nonprice terms for trading real estate investment trusts (REITs). Improvement in general market liquidity and functioning and more-aggressive competition from other institutions were the most cited reasons for this easing of nonprice terms. Nearly one-half of respondents indicated an increase in trading REITs’ efforts to negotiate more-favorable price and nonprice terms.
- Approximately one-fourth of respondents noted an increase in resources and attention devoted to managing concentrated credit exposure to dealers over the past three months. A smaller net fraction indicated such for central counterparties and other financial utilities.
- Small net fractions of dealers indicated a decrease in dispute volume, dispute duration, or both across all classes of counterparties.

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.

With respect to clients' **use of financial leverage**, on net, dealers indicated little change over the past three months for most types of counterparties, although a small net fraction of dealers indicated an increase in trading REITs' use of leverage (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. A small fraction of dealers reported that initial margin requirements on OTC derivatives referencing equities and interest rates increased for both average and most-favored clients.
- A small fraction of dealers reported a decrease in the posting of nonstandard collateral permitted under relevant arrangements.
- The volume and duration of mark and collateral disputes remained largely unchanged over the past three months, although one-fifth responded that the duration of mark and collateral disputes has decreased for OTC commodity derivatives.

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

- Nearly one-half of dealers reported increased demand to fund equities, and a smaller net fraction reported such for high-yield corporate bonds (see the exhibit "Measures of Demand for Funding and Market Functioning"). Demand for funding remained largely unchanged across all other asset classes.
- Dealers reported easing of funding terms for various types of securities, especially non-agency residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), and consumer asset-backed securities (ABS). Specifically, net fractions of three-fifths, one-half, and four-fifths of dealers reported easing of haircuts and collateral spreads for non-agency RMBS, CMBS, and consumer ABS, respectively. One-fourth, one-third, and one-fifth of respondents, on net, reported an easing of haircuts in high-grade corporate bonds, high-yield corporate bonds, and agency RMBS, respectively. Dealers reported that funding terms for equities remained unchanged.
- Approximately one-third of respondents, on net, indicated an improvement in liquidity and market functioning for the non-agency RMBS and consumer ABS markets.³ Smaller net fractions of respondents indicated improvements for other markets.

³ Note that survey respondents were instructed to report changes in liquidity and functioning in the market for the underlying collateral to be funded through repurchase agreements and similar secured financing transactions, not changes in the funding markets themselves. This question was not asked with respect to equity markets in the core questions.

Special Questions on London Interbank Offered Rate Transition for Over-the-Counter Derivatives

(Questions 81–87)

In the special questions, dealers were asked about the LIBOR transition for U.S. dollar-denominated OTC derivatives such as interest rate swaps and forward rate agreements that reference USD LIBOR.⁴ Dealers were asked how the notional value of LIBOR-based OTC derivatives contracts changed since the beginning of 2020. Dealers were also asked about the adoption by counterparty type of the International Swaps and Derivatives Association (ISDA) fallback protocol, which provides a mechanism for parties to amend their existing derivative transactions to account for a permanent discontinuation of LIBOR.⁵

With respect to the change in the notional value of LIBOR-based OTC derivative contracts since the beginning of 2020, dealers reported the following:

- One-half of dealers reported a decrease in the notional value for mutual funds, exchange-traded funds (ETFs), pension plans, and endowments. A majority of those that indicated a decrease reported a decrease of 0 to 25 percent.
- One-fourth of dealers, on net, indicated a decrease for dealers and insurance companies.
- Respondents, on net, reported no change for all other counterparty types included in the survey.

With respect to the adoption of the ISDA fallback protocol, dealers reported the following:

- Respondents indicated that nonfinancial corporations and hedge funds account for the largest amount (in notional value) of outstanding LIBOR-based OTC derivatives contracts that have not yet adopted the ISDA fallback protocol. Of the respondent firms that have nonnegligible amounts of LIBOR-based OTC derivatives contracts that have not yet adopted the protocol, almost all cited nonfinancial corporations as one of the top three counterparty types with such contracts, and about two-thirds indicated such for hedge fund clients. Smaller fractions of dealers reported such for insurance companies and mutual funds, ETFs, pension plans, and endowments.
- Desire to negotiate bespoke terms, counterparties' desire to see final all-in ISDA fallback rates, and lack of operational readiness on the counterparties' end were cited as the primary reasons for the ISDA fallback protocol not having yet been adopted.

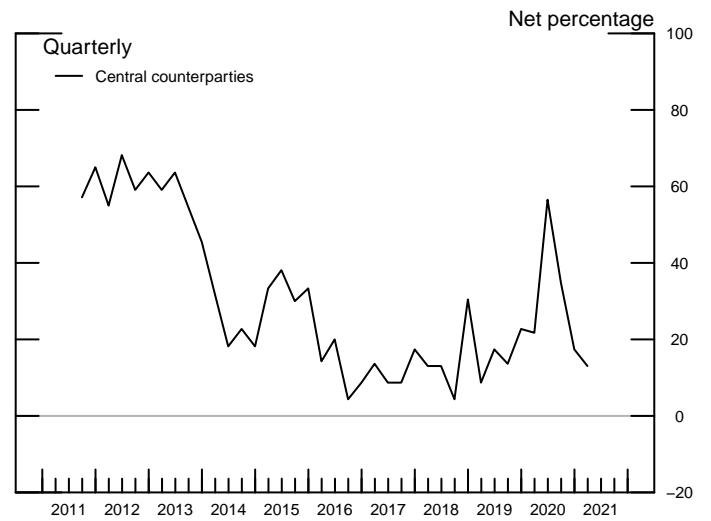
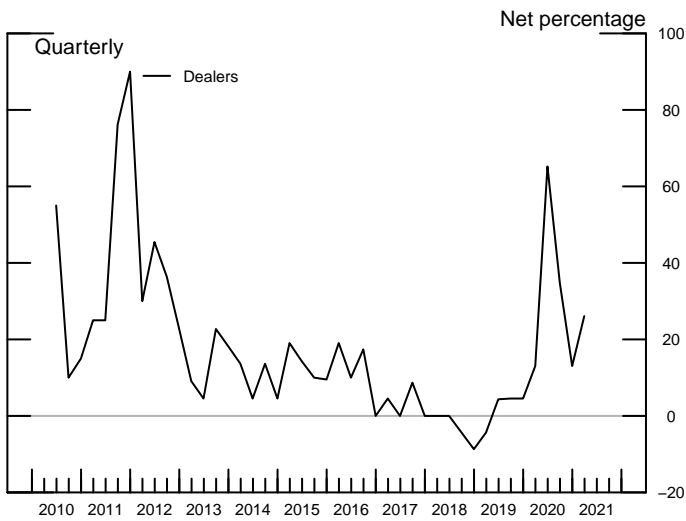
This document was prepared by Yesol Huh, Division of Research and Statistics, Board of Governors of the Federal Reserve System. Assistance in developing and administering the survey was provided by staff members in the Capital Markets Function, the Statistics Function, and the Markets Group at the Federal Reserve Bank of New York.

⁴ Dealers were asked to exclude derivatives that reference multiple currencies, such as cross-currency swaps.

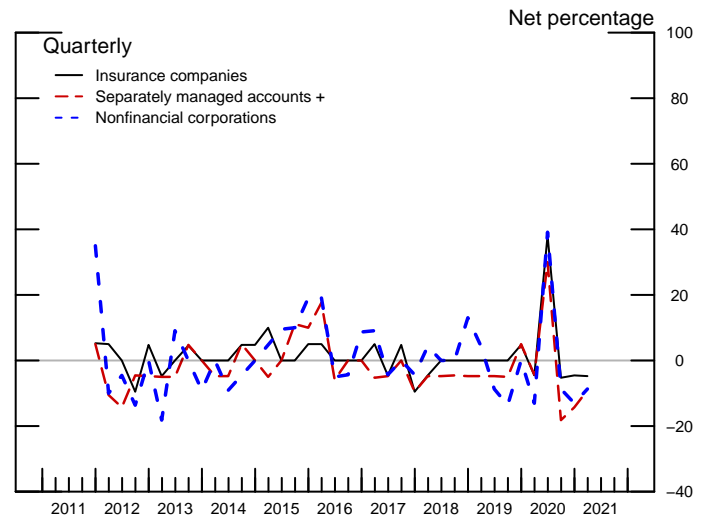
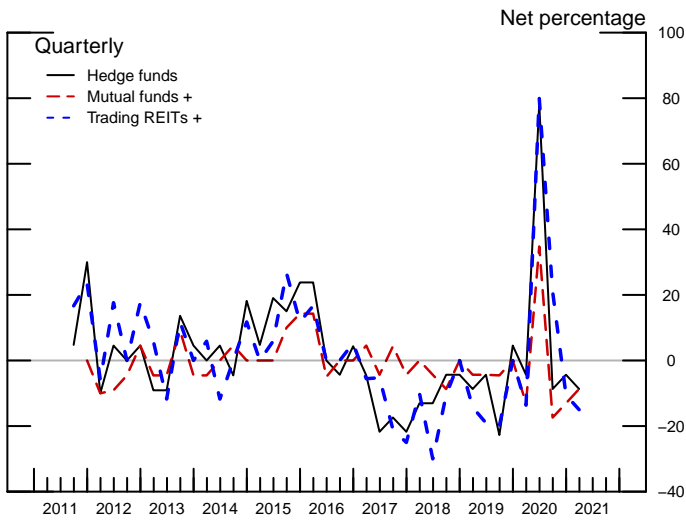
⁵ See International Swaps and Derivatives Association (2020), "ISDA Board Statement on the IBOR Fallbacks Supplement and Protocol," press release, October 9, <https://www.isda.org/2020/10/09/isda-board-statement-on-the-ibor-fallbacks-supplement-and-protocol>.

Management of Concentrated Credit Exposures and Indicators of Supply of Credit

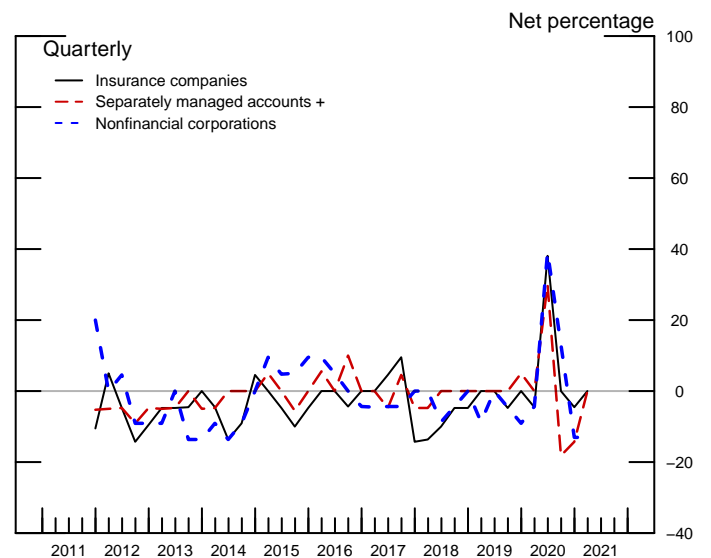
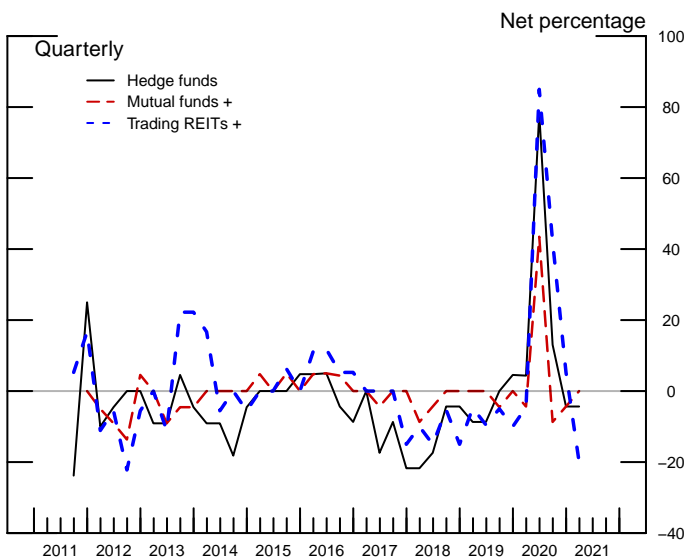
Respondents increasing resources and attention to management of concentrated exposures to the following:



Respondents tightening price terms to the following:



Respondents tightening nonprice terms to the following:



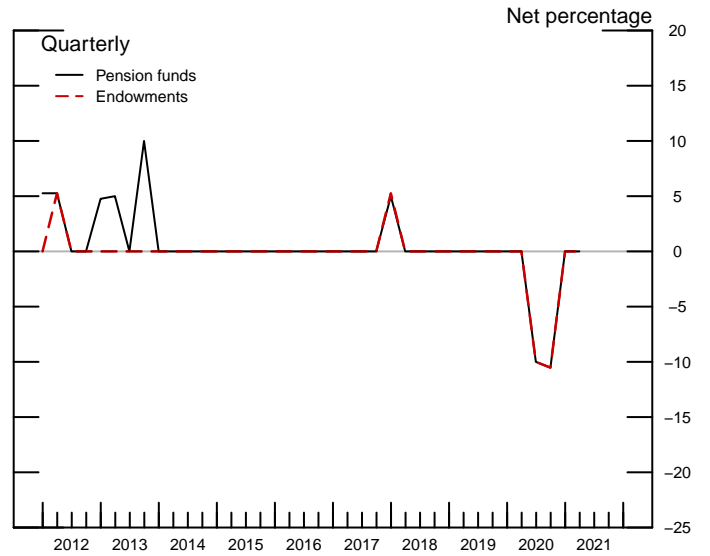
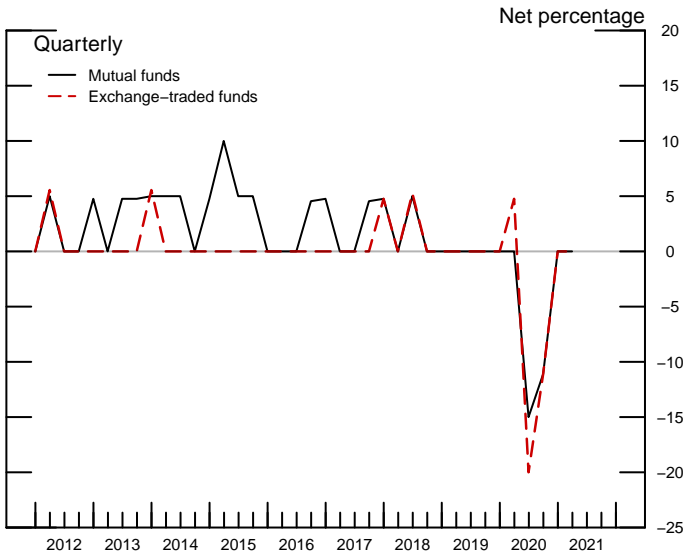
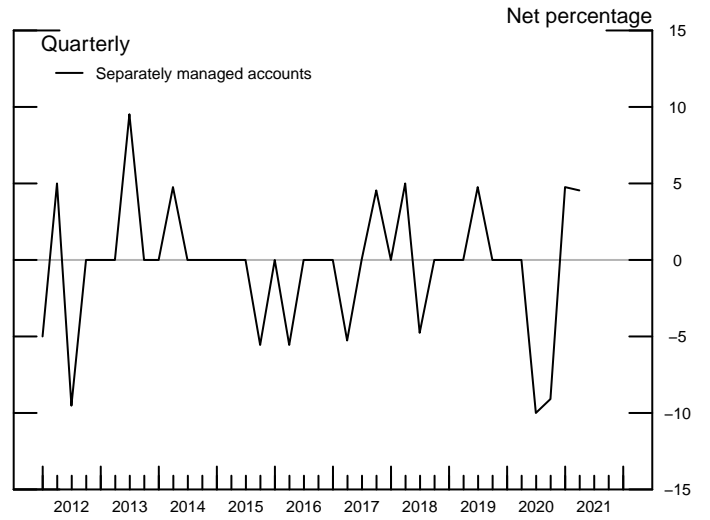
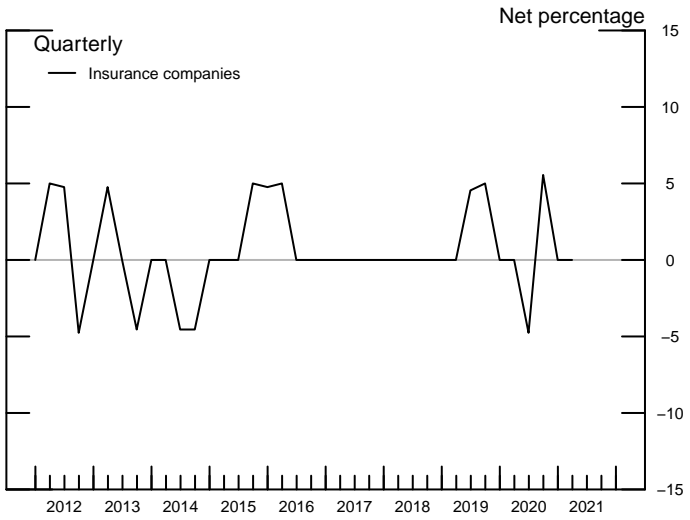
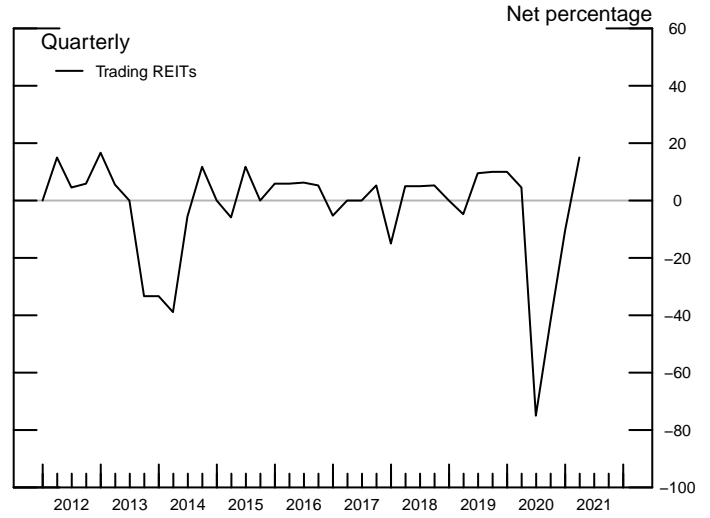
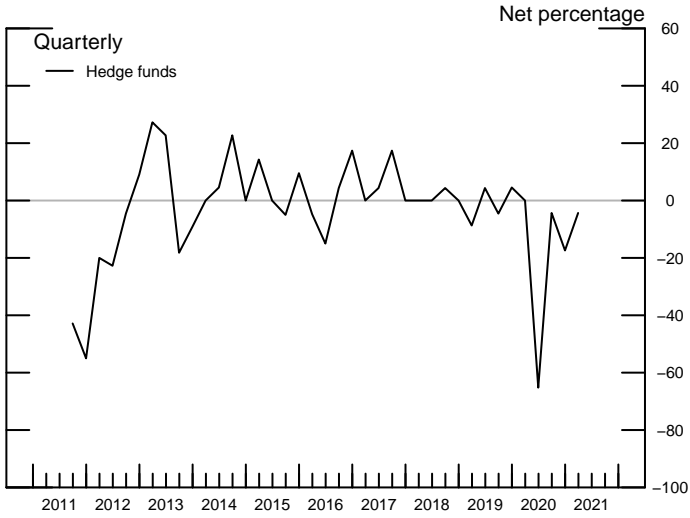
+ The question was added to the survey in September 2011.

Note: REIT is real estate investment trust.

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:

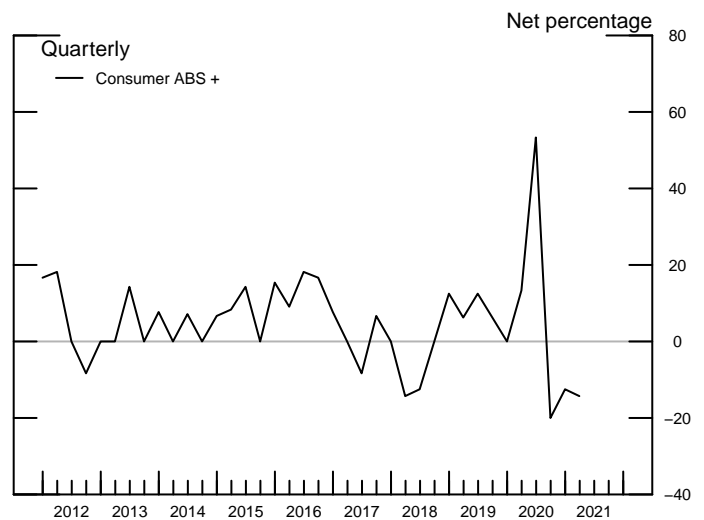
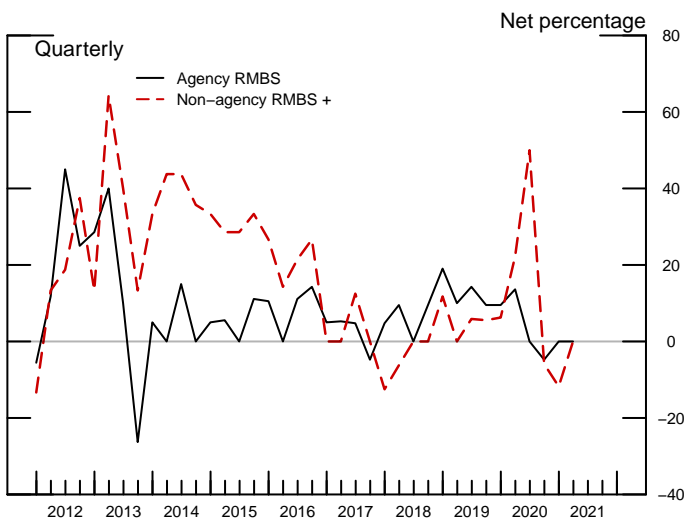
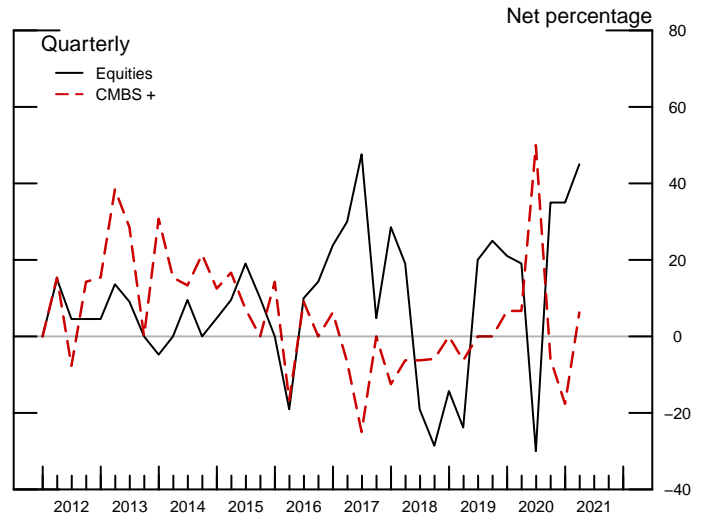
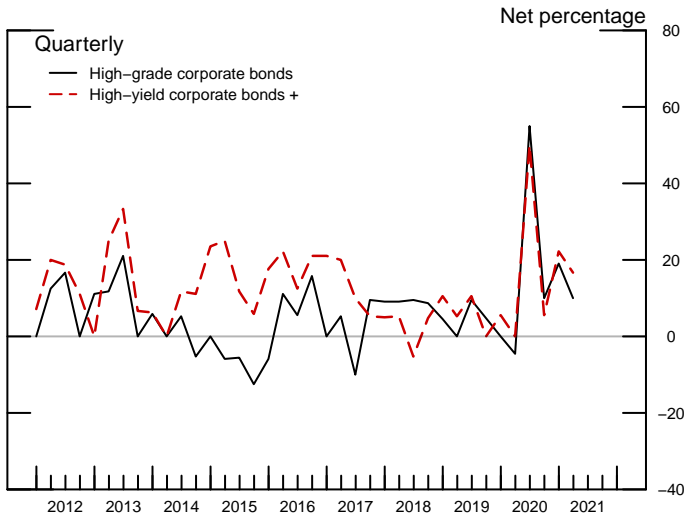


Note: REIT is real estate investment trust.

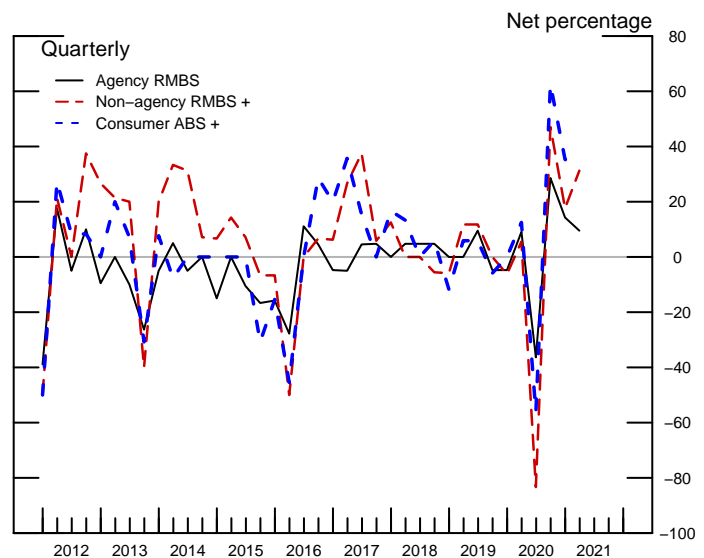
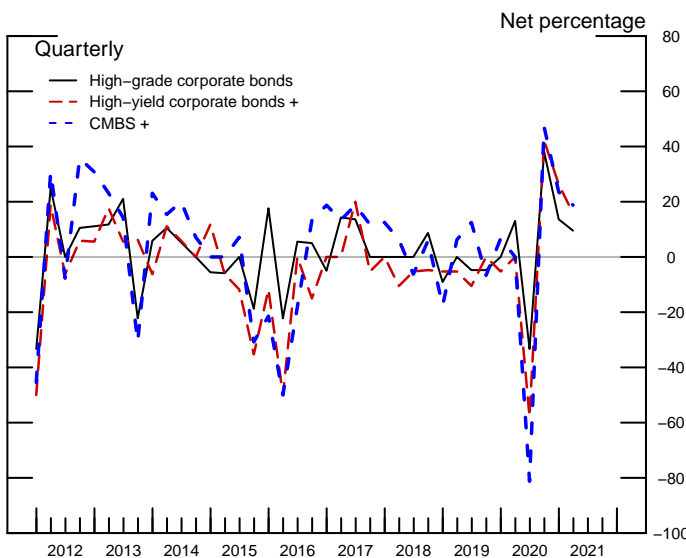
Source: Federal Reserve Board, Senior Credit Officer Opinion Survey on Dealer Financing Terms.

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:



+ The question was added to the survey in September 2011.

Note: CMBS is commercial mortgage-backed securities, RMBS is residential mortgage-backed securities, and ABS is asset-backed securities.

Source: Federal Reserve Board, Senior Credit Officer Opinion Survey on Dealer Financing Terms.