

# The June 2022 Senior Credit Officer Opinion Survey on Dealer Financing Terms

## Summary

The June 2022 Senior Credit Officer Opinion Survey on Dealer Financing Terms (SCOOS) 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 dealers' assessments of changes in liquidity conditions in the U.S. Treasury and agency residential mortgage-backed security (RMBS) markets since the beginning of January 2022. 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 May 10, 2022, and May 23, 2022. The core questions asked about changes between mid-February 2022 and mid-May 2022.<sup>1</sup>

## Core Questions

(Questions 1–79)<sup>2</sup>

**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:

- On net, one-fifth of dealers reported that price terms on securities financing transactions and OTC derivatives offered to hedge funds tightened somewhat, while small net fractions of respondents pointed to somewhat tighter terms offered to nonfinancial corporations, trading real estate investment trusts, and separately managed accounts (see the exhibit “Management of Concentrated Credit Exposures and Indicators of Supply of Credit”).
- For hedge funds and nonfinancial corporations, small net fractions of dealers reported that nonprice terms on securities financing transactions and OTC derivatives, such as haircuts, maximum maturity, or covenants, tightened somewhat since the previous survey.
- A small fraction of respondents indicated that resources and attention devoted to managing concentrated credit exposure to central counterparties increased somewhat. However, most respondents indicated that changes in central counterparty practices have

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<sup>1</sup> 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”).

<sup>2</sup> Question 80, not discussed here, was optional and allowed respondents to provide additional comments.

not affected, or have minimally affected, the credit terms they offer to clients on bilateral transactions that are not cleared.

- Approximately one-fifth of dealers, on net, reported that the volume of mark and collateral disputes increased for separately managed accounts, while small net fractions of respondents noted an increase for most other counterparty types. In addition, a small net fraction of dealers reported an increase in the duration and persistence of mark and collateral disputes for dealers and hedge funds.

With respect to clients' **use of financial leverage**, respondents indicated the following:

- Approximately one-fourth of dealers indicated a decrease in the use of leverage by hedge funds, while all respondents noted that the use of leverage by other client types was basically unchanged (see the exhibit "Use of Financial Leverage").

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

- Initial margin requirements were largely unchanged for most types of OTC derivatives, although with respect to interest rate derivatives, one-fifth of dealers reported that initial margin requirements increased somewhat for both average and most-favored clients.
- Approximately one-fourth of dealers, on net, reported an increase in the volume of mark and collateral disputes over the past three months for commodity derivatives, while one-fifth of respondents reported an increase for foreign exchange derivatives and credit derivatives referencing corporates. Meanwhile, the duration and persistence of mark and collateral disputes remained largely unchanged for all types of contracts.

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

- For high-grade corporate bonds, small net fractions of dealers reported tightening of funding terms with respect to the maximum amount of funding, haircuts, and collateral spreads for average clients, and tightening of terms with respect to collateral spreads for most-favored clients. For high-yield corporate bonds, over one-fifth of respondents, on net, indicated tightening of funding terms with respect to collateral spreads for average and most-favored clients, and a small net fraction of dealers reported tighter terms with respect to haircuts for average clients. For all other asset classes, terms under which various types of securities are funded remained largely unchanged.
- On net, one-fourth of dealers reported decreased demand for funding equities. Demand for funding of other asset classes was largely unchanged (see the exhibit "Measures of Demand for Funding and Market Functioning").

- Small net fractions of dealers indicated that liquidity and market functioning for high-grade corporate bond, agency RMBS, and commercial mortgage-backed securities markets deteriorated over the past three months.
- The volume and duration of mark and collateral disputes remained largely unchanged across collateral types. A small net fraction of dealers reported that the volume of mark and collateral disputes related to lending against equities increased somewhat over the past three months.

### **Special Questions on Liquidity Conditions in the U.S. Treasury and Agency Residential Mortgage-Backed Securities Markets**

(Questions 81–91)

In the special questions, dealers were asked about their assessment of changes in liquidity conditions in the U.S. Treasury and agency RMBS markets since the beginning of January 2022. In these questions, market liquidity referred to the ease of buying and selling desired quantities of an asset without significant costs or delays.

With respect to **liquidity conditions in the market for on- and off-the-run U.S. Treasury securities**, dealers reported the following:

- All dealers indicated that liquidity in the market for **on-the-run U.S. Treasury securities** has deteriorated since last January, with over one-third of respondents reporting a substantial deterioration in liquidity conditions.
- In the on-the-run market, dealers most frequently cited a decrease in the depth of the limit order book as the main indicator used in making their assessment. Price impact was most often cited by dealers as the next most important indicator, followed by bid-ask spreads.
- Over four-fifths of respondents pointed to increased interest rate volatility as a very important reason for the deterioration of liquidity conditions. In addition, more than one-half of dealers cited more unbalanced client order flows, diminished availability of dealer balance sheets, reduced willingness of dealers to take risk in U.S. Treasury markets, reduced willingness of PTFs to provide liquidity, and elevated Treasury issuance net of System Open Market Account (SOMA) purchases as somewhat important reasons supporting their liquidity assessments.
- With respect to the market for **off-the-run U.S. Treasury securities**, over three-fourths of dealers indicated that liquidity conditions have deteriorated since January 2022. Approximately one-half of these respondents indicated that liquidity conditions deteriorated substantially over the period.
- In the off-the-run market, dealers indicated that price impact was the most important indicator used in making their assessment of a deterioration in liquidity conditions, closely followed by bid-ask spreads.

- Roughly four-fifths of dealers noting a deterioration in off-the-run U.S. Treasury liquidity cited increased interest rate volatility as a very important reason leading to the deterioration, while approximately one-half of respondents also pointed to more unbalanced client order flows as a very important contributing factor. In addition, between roughly one-third and two-fifths of dealers cited diminished availability of dealer balance sheets and reduced willingness of dealers to take risk in U.S. Treasury markets as important reasons supporting their liquidity assessments.
- Dealers were also asked about the main risks to Treasury market liquidity over the remainder of 2022. Elevated interest rate volatility and the Federal Reserve's balance sheet reductions were most often cited as the main risks ahead, followed by reduced willingness of dealers to intermediate the U.S. Treasury markets.

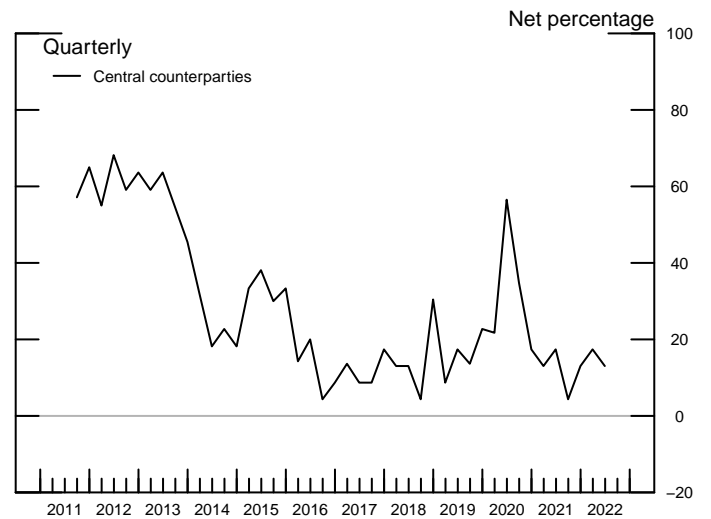
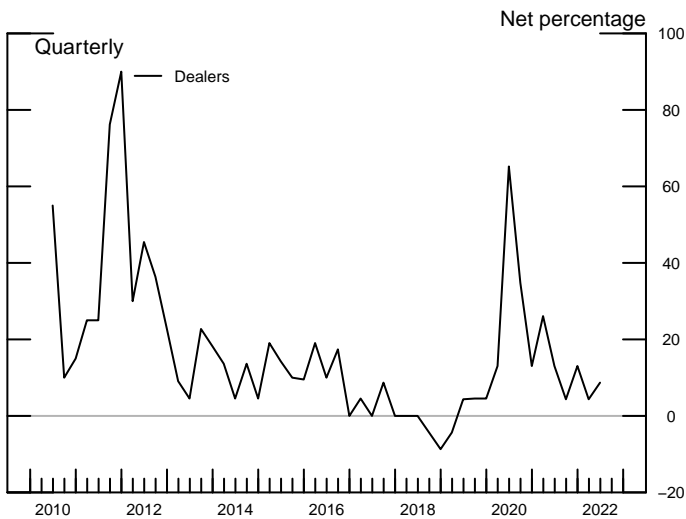
With respect to **liquidity conditions in agency RMBS markets**, dealers reported the following:

- Approximately three-fifths of dealers reported a deterioration in liquidity in the to-be-announced (TBA) market for agency RMBS since last January, while the remaining fraction of respondents indicated that liquidity in this market remained basically unchanged.
- In the TBA agency RMBS market, roughly one-half of dealers noting a deterioration of liquidity conditions reported that price impact was the most important indicator used in making their assessment, while bid-ask spreads was cited as the next most important indicator.
- Nearly all respondents noting a deterioration in liquidity conditions cited increased interest rate volatility as a very important reason leading to the deterioration, while roughly two-fifths of those reporting a deterioration also pointed to more unbalanced client order flows as a very important reason. Respondents also cited reduced willingness of dealers to take risk in RMBS markets, elevated RMBS issuance net of SOMA purchases, and diminished availability of dealer balance sheets as somewhat important contributing factors.
- Similar to Treasury markets, elevated interest rate volatility was most often cited as the main risk to agency RMBS market liquidity over the remainder of 2022. The Federal Reserve's balance sheet reductions and deterioration in financing conditions were cited as the next most important risks.

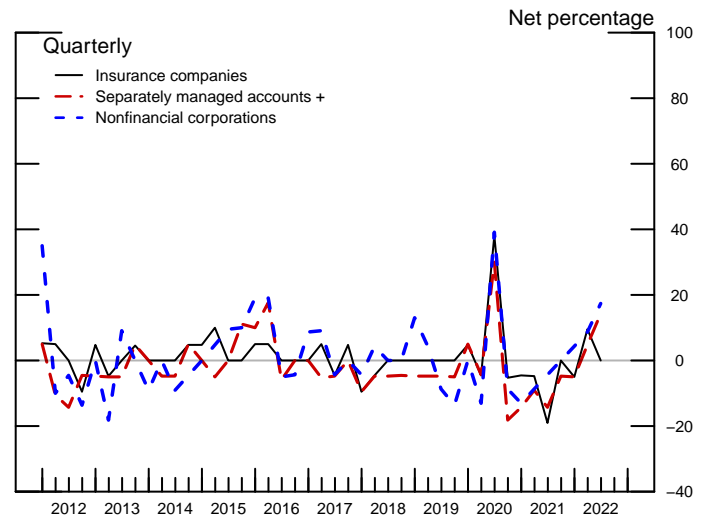
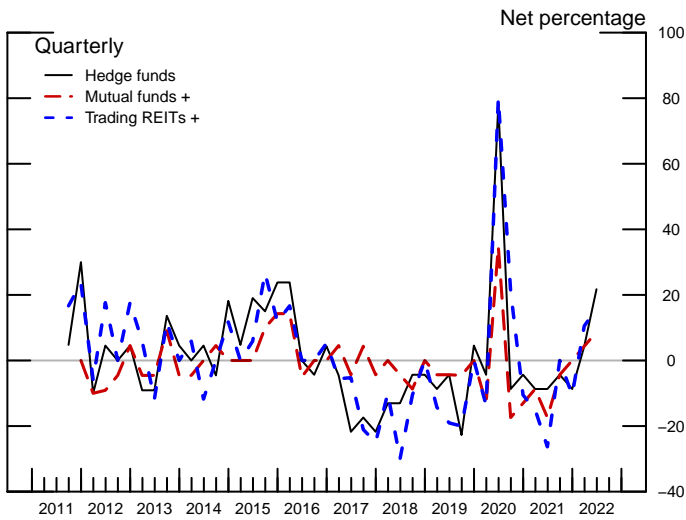
*This document was prepared by Ayelén Banegas, Division of Monetary Affairs, Board of Governors of the Federal Reserve System. Assistance in developing and administering the survey was provided by staff members in the Capital Markets Function, the Statistics Function, and the Markets Group at the Federal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

# Management of Concentrated Credit Exposures and Indicators of Supply of Credit

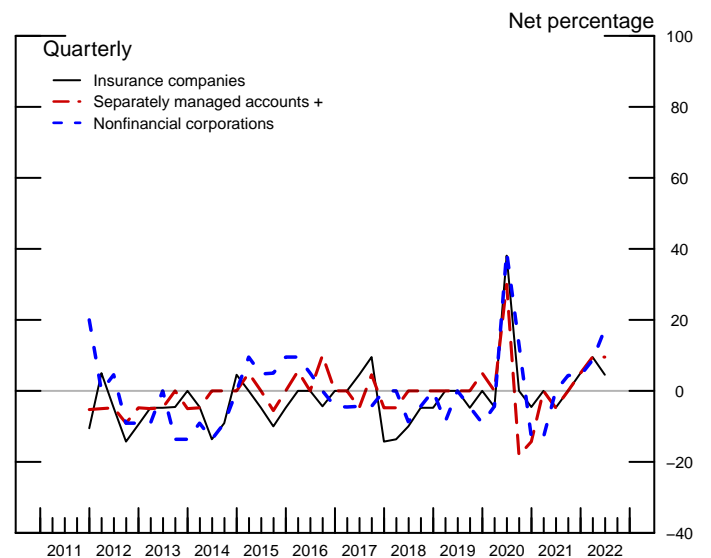
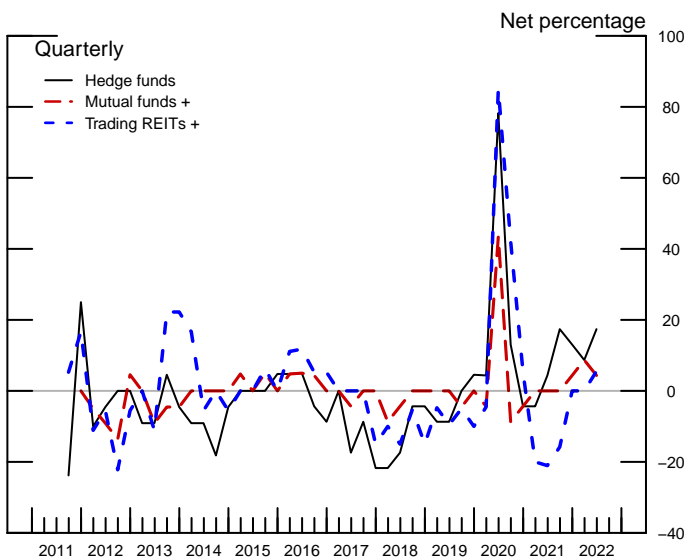
Respondents increasing resources and attention to management of concentrated exposures to the following:



Respondents tightening price terms to the following:



Respondents tightening nonprice terms to the following:



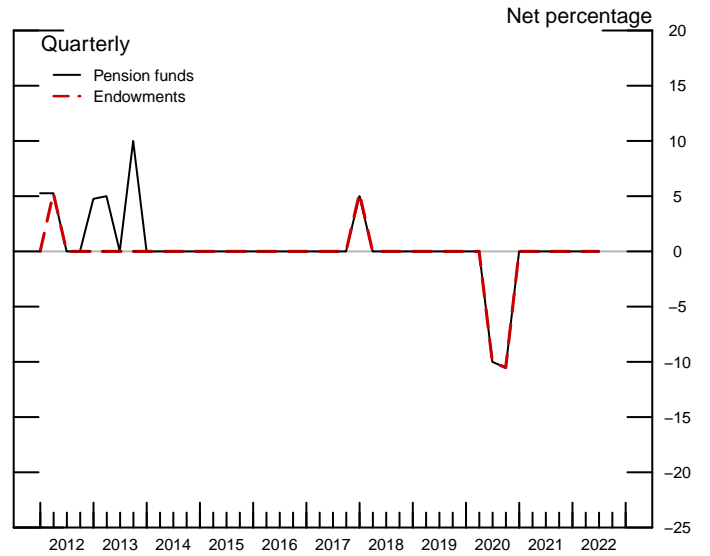
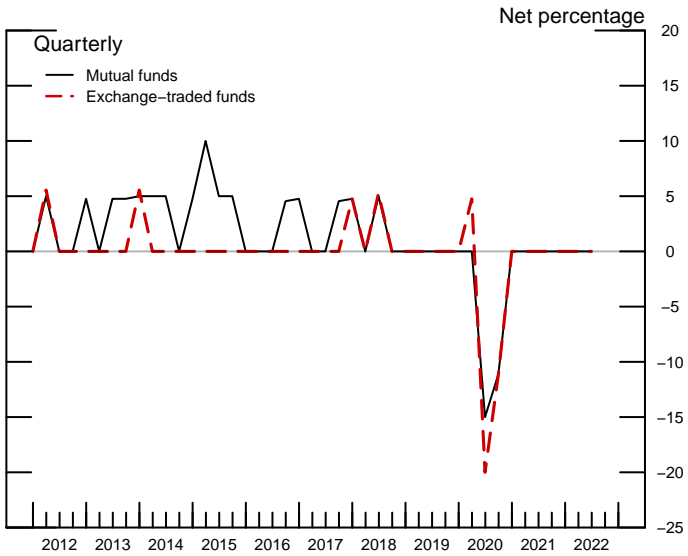
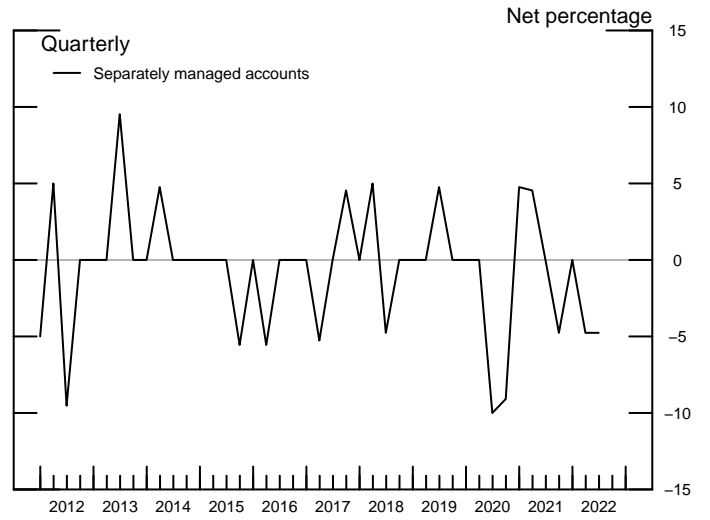
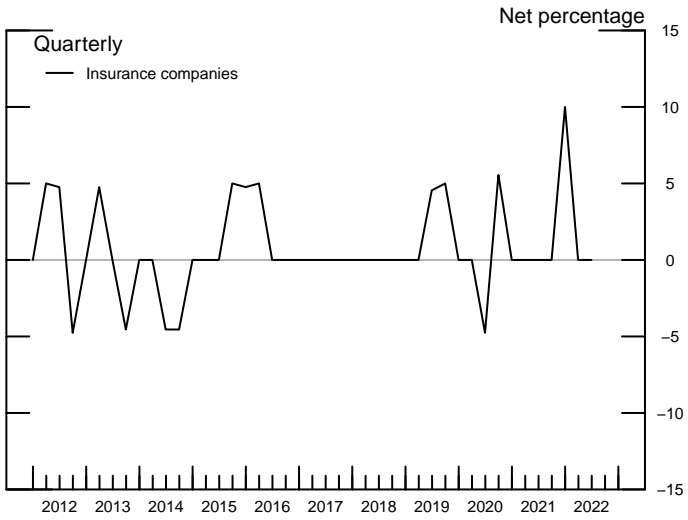
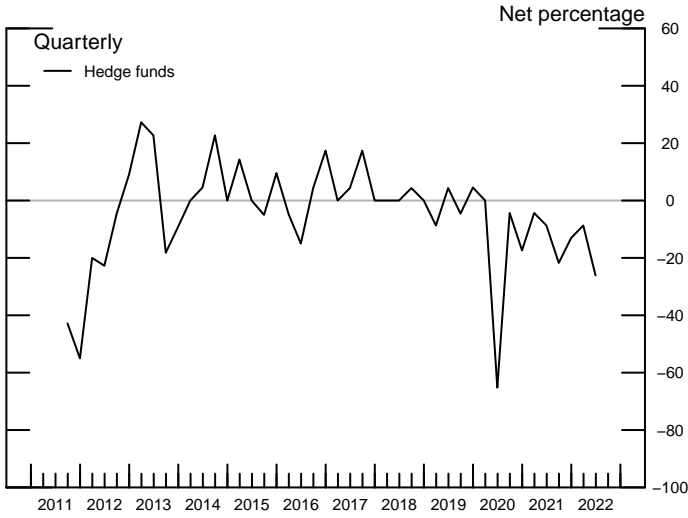
Note: REIT is real estate investment trust.

+ 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:

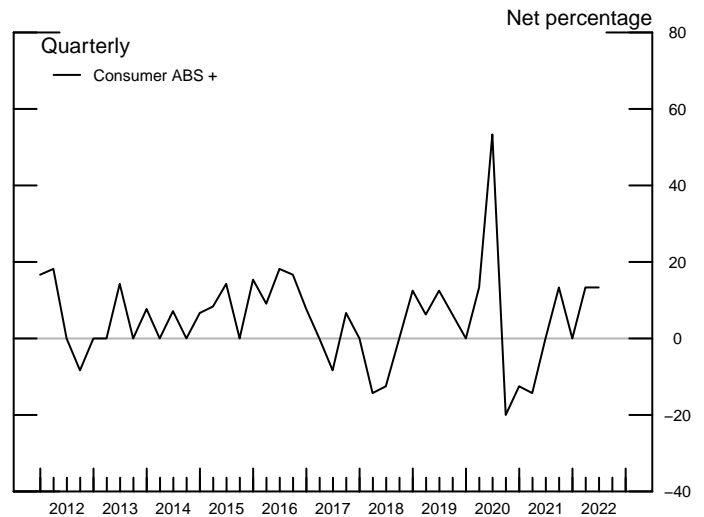
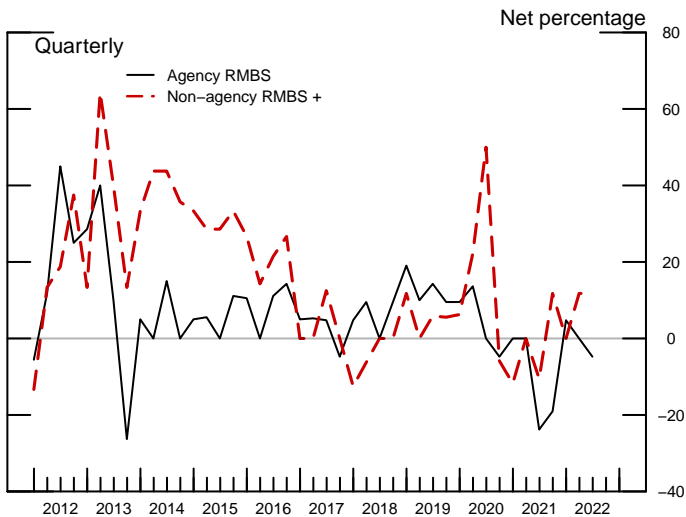
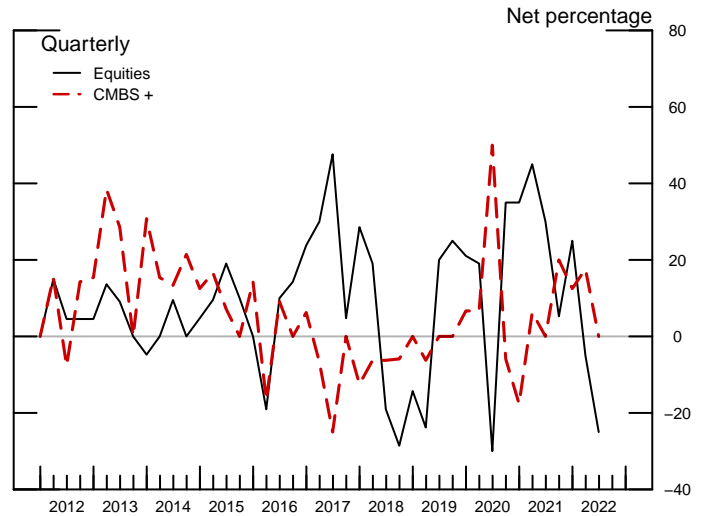
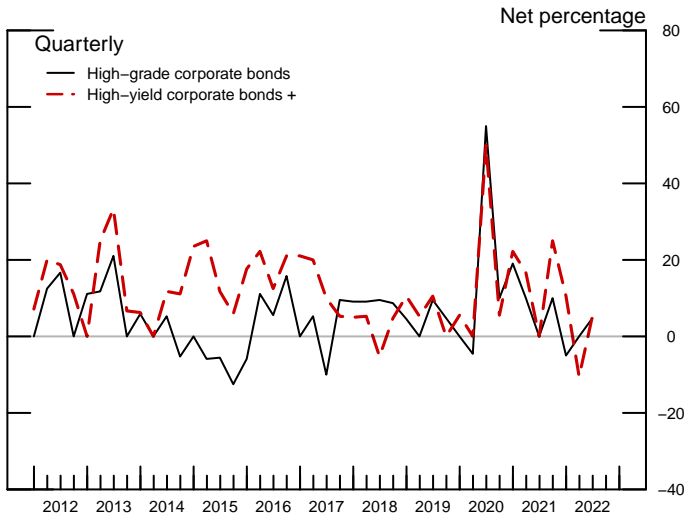


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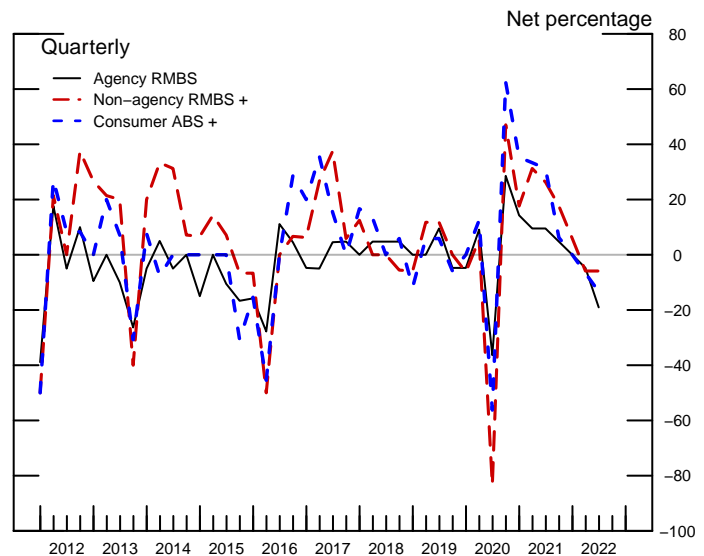
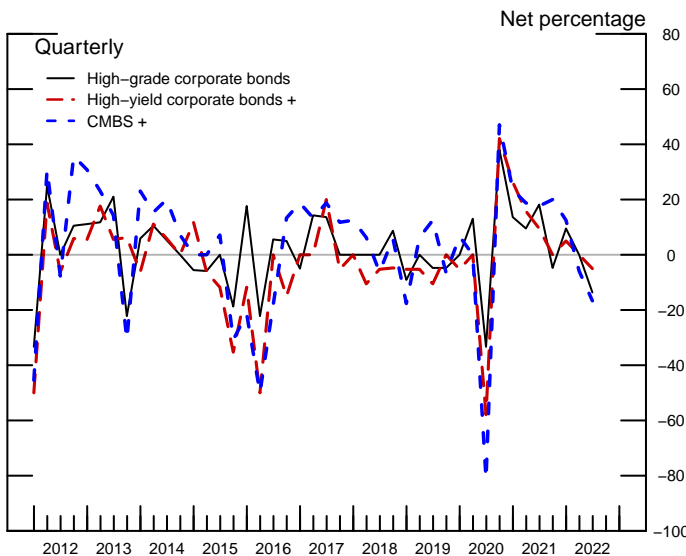
Source: Federal Reserve Board, Senior Credit Officer Opinion Survey on Dealer Financing Terms.

# 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.