The December 2016 Senior Credit Officer Opinion Survey on Dealer Financing Terms

The December 2016 Senior Credit Officer Opinion Survey on Dealer Financing Terms collected qualitative information on changes over the previous three months 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 use of central clearing services for OTC derivatives and the ease of porting client portfolios from another clearing agent. The 23 institutions participating in the survey account for almost all dealer financing of dollar-denominated securities to nondealers and are the most active intermediaries in OTC derivatives markets. The survey was conducted between November 15, 2016, and November 28, 2016. The core questions asked about changes between September 2016 and November 2016.[1]

Core Questions
(Questions 1–79)[2]

Survey respondents generally reported little change in conditions over the past three months in pricing and across markets and instruments covered in the core questions of the survey. The responses, however, offered a few insights regarding recent developments in dealer-intermediated markets:

- A small fraction of dealers indicated that the use of financial leverage by hedge funds has increased somewhat over the past three months. For all other classes of counterparties, use of financial leverage was little changed.
- One-fifth of respondents indicated that the duration and persistence of mark and collateral disputes with dealers and other intermediaries has increased in the past three months. Smaller fractions indicated such an increase with other classes of counterparties. One-fifth of dealers reported an increase in the duration and persistence of mark and collateral disputes on contracts related to interest rates and foreign exchange.
- With respect to securities financing transactions, one-fifth of dealers, on net, noted an increase in financing rates (collateral spreads over the relevant benchmark) over the past three months for average and preferred clients on high-grade and high-yield corporate bonds. Smaller fractions of respondents reported

[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.

an increase in financing rates for other collateral types. One-fifth of dealers indicated an increase in the maximum amount of funding provided for average clients on equities.

- More than one-fifth of respondents, on net, reported an increase in funding demand for high-yield corporate bonds and equities. One-fifth of dealers responded that liquidity and functioning in the underlying markets have improved for commercial mortgage-backed securities and consumer asset-backed securities.

Special Questions on Central Clearing
(Questions 81–86)

In the September 2015 survey, respondents were queried about the use of central counterparty clearing services for OTC derivatives denominated in U.S. dollars (USD). In the current survey, we revisited questions about the use of central counterparty clearing services for derivatives that are eligible for clearing but for which clearing is not mandated. We also asked additional questions related to risk management and the ease of porting portfolios for clearing of all USD-denominated OTC derivatives.

With respect to clients' use of central clearing services for derivatives that are eligible for clearing but for which clearing is not mandated, responses to the special questions revealed the following:

- Nearly two-thirds of respondents indicated that their clients' use of central clearing services for these derivatives has increased somewhat since September 2015. In contrast, in the September 2015 survey, a net fraction of only one-tenth of the respondents reported an increase since the beginning of 2014 in their clients' use of clearing services for OTC derivatives that are not subject to mandatory clearing but are eligible to clear.
- The most important reasons for the increase since September 2015 were counterparty risk mitigation associated with central clearing, expansion in the types of clearing-eligible products, and better prices for cleared transactions than for noncleared transactions.[3] Dealers may offer lower prices on cleared transactions because the lower capital requirements on such transactions make them more desirable.

With respect to dealers' management of counterparty credit exposures that arise from serving as clearing agents, respondents indicated the following:

- Nearly all respondents pointed to margin requirements as being the most important tool. Other important tools were netting with the same client,

[3] Respondents were asked to choose at most three reasons from the following: expansion in the types of clearing-eligible products, differential prices on cleared and noncleared transactions due to differences in capital requirements, anticipation of higher margin requirements for noncleared transactions, counterparty risk mitigation associated with central clearing, margin efficiency (for example, through netting benefits) or other cost savings for cleared transactions, and other.

monitoring concentrated exposures across clients, and avoiding or limiting activity with certain clients.[4]

With respect to the ease of porting portfolios from another clearing agent, responses revealed the following:

- Three-fifths of dealers responded that it would take between one week and one month to absorb the OTC derivatives portfolios of large clients that need to be ported from another clearing agent *when the client is not already one of theirs*. One-fourth indicated a porting time of more than one month, and a small fraction indicated a porting time of between two days and one week.
- Two-fifths of respondents indicated that it would take between two days and one week to absorb the OTC derivatives portfolios of large clients that need to be ported from another clearing agent *when the client is already one of theirs*. One-fourth and one-fifth of dealers responded two days or fewer and between one week and one month, respectively.

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 Statistics Function and the Markets Group at the Federal Reserve Bank of New York.

[4] Price adjustments and netting across clients were the other choices given in the survey. Very few respondents chose either of these options.