# Treasury Derivatives

Treasury Borrowing Advisory Committee

November 4th, 2026

*Please comment on the growth in the use of Treasury derivatives, in particular swaps and futures.*
*How has use of these derivatives evolved?*
*Who are the primary users and what factors have driven their usage?*
*How do these derivatives affect demand for cash Treasury securities?*
*What effects do these derivatives have on Treasury repo markets?*
*Does the use of derivatives by investors reduce the size of the Treasury repo market?*
*Should Treasury consider any policy initiatives to increase demand for cash Treasury securities relative to Treasury derivatives?*

# Executive summary

Since the 2022 rise in yields, asset managers have built synthetic Treasury exposure through futures, and LDI investors (pension funds and insurers) have used rate swaps for duration, while heavy government and credit issuance have weighed on cash Treasuries.

**The reasons for expressing duration through derivatives are many:**

- Futures bring simplicity in execution (no repo infrastructure or counterparty lines). They are a versatile and liquid duration management tool (weekly volume is 1.5-2x the open interest and comparable to cash Treasury volume), anonymous (all-to-all central limit order books) and low maintenance (one roll a quarter) for deploying U.S. duration. Their usage leaves cash available for higher-yielding assets and avoids higher fund expense ratios (repo interest is booked as an expense).
- Swaps have been standardized in execution and clearing since the 2013/2014 clearing/SEF mandates but remain customizable (matched to liability cashflows, low initial margin, can extend beyond 30y), carry no roll, can be collateralized with securities, and hedge liabilities that are themselves discounted on swap curves.
- Historically, dealers would intermediate these positions directly. However, leverage ratio rules and balance-sheet constraints have led to reduced participation from that cohort and that gap has been filled by hedge funds.

Derivatives do not remove the underlying demand for Treasuries, they change who ends up holding them. They also broaden market access and add intermediation capacity.

Use of derivatives increases the size of repo market. Also, the availability of repo affects the pricing of derivatives which in turn influences the size of the derivatives market. The cash demand derivatives generate through leveraged, repo-funded positions is pro-cyclical and weakens when funding or margin tightens.

Policies that curb derivatives risk disrupting today's market structure. Treasury could consider policy initiatives that make cash Treasuries easier to hold and finance relative to derivatives: easing regulation that restricts balance sheet usage, making repo financing easier to access, improving the availability of term repo financing, opening repo market making to new entrants.

Together, these initiatives could help build a more diversified and robust base of cash Treasury holders and keep Treasury demand steady.

# Usage of U.S. rates derivatives and evolution over time

**1980s-2007: *Pre-Great Financial Crisis, dealer-centric and over-the-counter (OTC for short) markets***

- Swaps were a dealer product sold to banks (Asset and Liability Management or ALM for short) and corporates (fixed to floating). End users mostly received fixed while dealers paid fixed, hedged in cash Treasuries on repo and warehoused the residual. This flow, combined with LIBOR credit risk, kept swap spreads positive.
- Inter-dealer trades peaked at 66% of OTC IRD (Interest Rate Derivatives) turnover in 2001 (Bank for International Settlements or BIS for short)[2].
- Hedge funds were present at the long end as spread convergence traders (see Long-Term Capital Management and swap spreads in 1998).

**2008-2015: *Post-Great Financial Crisis, displacement of inter-dealer markets by buy-side participants***

- Inter-dealer trade share dropped to 44% in 2010 and 35% in 2013 (BIS)[2].
- Issuer swap demand faded with lower rates and pension funds and insurers (LDI for short) became the structural receivers of fixed. The 30y swap spread turned negative in 2008.
- Clearing/SEF mandates in 2013-14 standardized swap markets.
- GSE (Government-Sponsored Enterprises) swap usage shrank after conservatorship, removing a major structural payer of fixed (synthetic fixed-rate funding and convexity hedging of retained Mortgage-Backed Security - or MBS for short - portfolios).

**2015-2020: *Regulations, balance sheet constraints and dealer wind-down of warehousing***

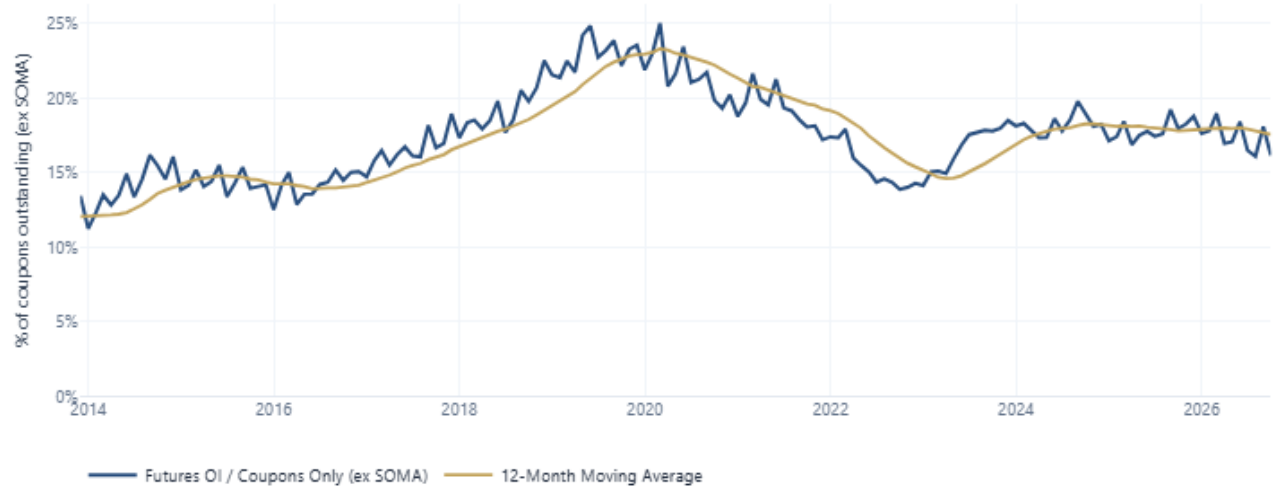
- Negative swap spreads and leverage ratio regulation pushed warehousing from dealers to hedge funds. The basis trade picked up before seeing a large unwind in March 2020 (Covid).

**2020-2026: *Asset managers and leveraged funds/dealers mirrored positioning***

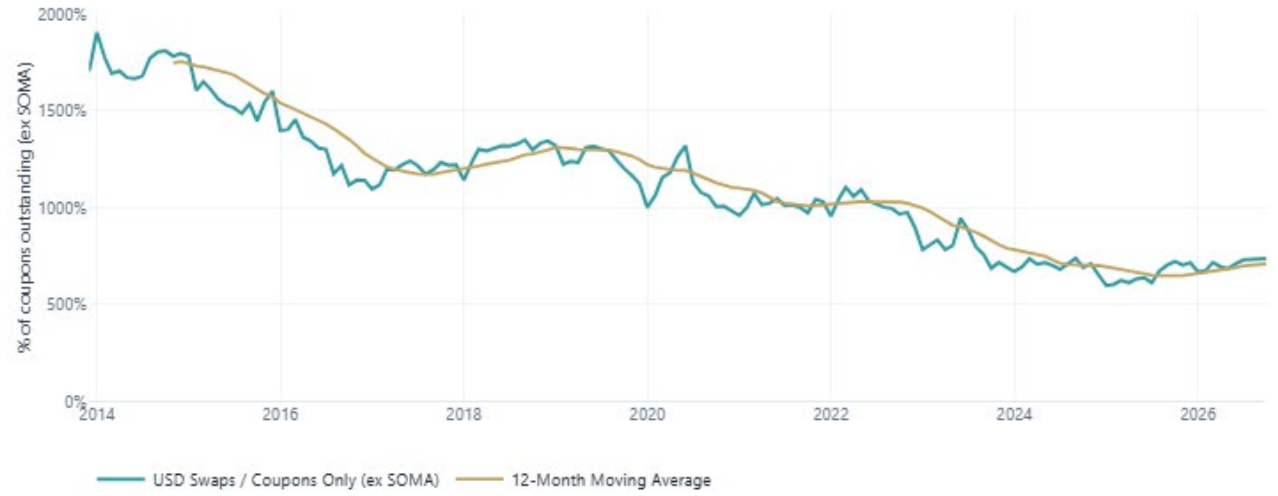
- Asset managers' futures long have roughly quadrupled since the end of 2021 and the leveraged funds (and dealer) community has seen a close to identical increase in their shorts (according to the Commodity Futures Trading Commission Traders in Financial Futures data - or CFTC TFF for short).

# Growth and evolution of U.S. rates derivatives usage (futures and swaps)

**Treasury futures OI % of coupons outstanding (ex SOMA)**




**USD swaps OI % of coupons outstanding (ex SOMA)**




* Sources: CFTC Weekly Swaps Report; US Treasury MSPD; NY Fed SOMA.

The open interest in Treasury futures has increased in line with the stock of U.S. public debt/marketable (share hovering between 12% and 25%, peaking right before the deleveraging of March 2020).

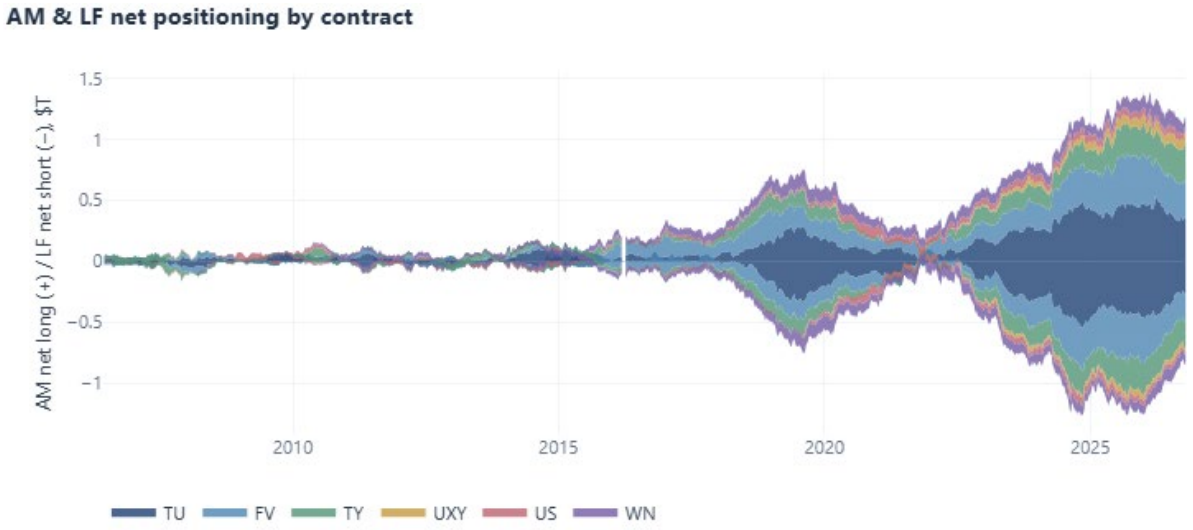
It has recently stabilized at around 18% of the stock of coupons.

Swaps open interest used to be much larger than the stock of debt and that ratio has compressed from ~18x coupons ex System Open Market Account (or SOMA for short) in 2014 to ~7x (CFTC Weekly Swaps Report).

Gross USD swap notional has ranged between $85tn and $135tn for about a decade (compression, then the SOFR conversion kept notional down) while coupons ex SOMA grew 2.5x, so the falling ratio reflects notional efficiency and fiscal expansion and QT rather than a retreat from swaps.

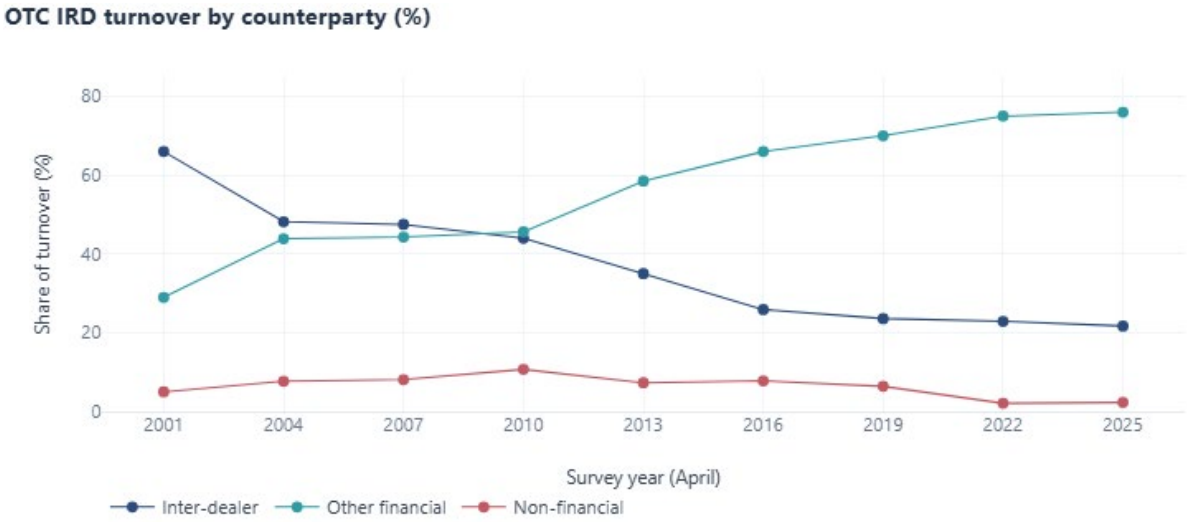
In terms of volumes, cash Treasury and futures volumes on a 13-week moving-average basis are similar at above $4tn a week. Swap volumes have run higher, at $6-7tn a week on the same basis, with the latest week above $8tn (see figure on slide 17).

# Asset managers' longs vs leveraged funds' shorts breakdown by contract




* Source: CFTC TFF data, market-value notional.

# Composition of global OTC IRD daily turnover by counterparty type[2,3]




* Source: BIS Triennial Central Bank Survey (2001–2025).

# USD swaps open interest and counterparty composition

As mentioned in slide 4, two episodes reduced outstanding notional in swaps without impacting activity:

- Compression took the open interest down 37% in 2014-16 as the leverage ratio and G-SIB (Global Systemically Important Bank) surcharge (both keyed to gross notional) made redundant line items a capital cost.
- The SOFR transition then replaced LIBOR fixed-float swaps with SOFR OIS, now ~$100tn outstanding.

Since 2025 notional has grown again, with OIS up $27tn, putting the total back around its 2014 level.

The non-dealer share of outstanding USD interest rate swap counterparty sides has roughly doubled, from about 15% in 2014 to about 31% in 2026 (CFTC Weekly Swaps Report participant tables). The remaining two-thirds are swap-dealer sides, which include inter-dealer trades and dealers' own hedges. The CFTC reporting-method changes in 2019 and 2022 each reset the level lower (indicated on the chart), so the trend within each regime is the more useful signal to interpret this data.

**USD swaps notional outstanding**




* Source: CFTC Weekly Swaps Report. SOFR swaps are classified under OIS; USD LIBOR swaps were classified under Fixed-Float.

**Non-dealer share of IRS notional**




* Source: CFTC Weekly Swaps Report.

# Positions by user cohort today

| Cohort | Instruments used | Usage | Why? (see slide 8-13 for details) | Position today | Scale anchor |
|---|---|---|---|---|---|
| **Asset Managers (Mutual Funds, ETFs, SMAs)** | Long TSY & SOFR futures, some cleared swaps | Duration overlay to track benchmark, liquidity, synthetic TSY exposure | Futures give duration without a repo desk and without rolling overnight financing. The financing cost sits in the futures price and does not appear as an expense-ratio line. Futures gains are taxed 60/40 under Section 1256. The 40 Act caps fund borrowing at one-third of assets, while SEC Rule 18f-4 lets futures run under a VaR limit | Structural net long of $1.14tn, mirrored by a $1.15tn net short at leveraged funds and dealers | Net long $1.14tn (CFTC TFF, Oct 2026). Mutual funds hold $455bn of long TSY futures ($314bn net) and futures are 43% of their TSY exposure (Fed, N-PORT data, Q4 2023)[5] |
| **Leveraged Funds(RV, Multi-manager, macro, CTAs)** | Short TSY futures and pay-fixed SOFR swaps vs cash TSY, SOFR futures | Cash/futures basis, swap spreads, asset swaps, curve RV, policy views | Positions are the other side of asset-manager futures longs and of receive-fixed demand from insurers and pensions. Leverage comes from futures margin, cleared swaps and FICC sponsored repo. The Fed traces the basis trade largely to Cayman-domiciled funds[8], outside the tax frictions that apply to US investors | Net short $0.83tn in TSY futures against cash TSY financed in repo | Fed estimates from Form PF[6], Sept 2025: $2.4tn long and $1.6tn short gross exposure, about $2.15tn of it in cash TSY (estimate), repo cash borrowing $3.1tn. Basis trade $832bn (Fed). Swap-spread trade $305bn (Fed) to $631bn (BIS upper bound, Q2 2025)[7] |
| **Dealers/banks** | Futures, swaps, swaptions, market-making books, futures hedging of inventory | Market making, client flow recycling, ALM, inventory hedging | The leverage ratio, G-SIB surcharge and NSFR charge capital and stable funding against cash TSY inventory and matched-book repo. Cleared derivatives and FICC-netted sponsored repo use far less balance sheet | As of Apr 2025, Inter-dealer trades are 21% of IRD turnover, down from 66% in 2001[2]. Dealer net short in TSY futures is $0.32tn | $205.9tn of interest rate derivatives at insured US banks, 68.5% of all derivatives, with four banks holding 80.2% (OCC, Q2 2026)[9]. Inter-dealer share 21% of global IRD turnover (BIS, Apr 2025)[3] and 31% of US-booked turnover (NY Fed, 2025)[4]. 36 FICC sponsoring members intermediate $1.7-2tn a day of sponsored repo (DTCC, 2025)[10] |
| **Pensions/insurers (LDI)** | Long dated receiver swaps, swaptions, ultra bond futures, STRIPS | Liability hedging while assets stay in credit. 95% of insurers' derivatives are designated as hedges | Liabilities are valued on swap or credit curves rather than Treasuries, and run beyond the 25-30 year maturity of the longest futures. Bilateral swaps can be collateralized with securities, futures require daily cash margin. Swaps qualify for hedge accounting against the liability. For pension trusts, repo borrowing creates taxable UBTI, derivatives do not | Direction is not reported in US filings. Where it is measured, it is receive-fixed: UK LDI funds £167bn net (BoE, Sept 2022)[15], over 70% of Dutch pension funds (DNB, 2024)[16] | Insurers' derivatives notional $3.0tn at YE2021, 98% life companies, 51% swaps, 95% hedging. Interest rate swaps $1.12tn, 73% of swap notional (NAIC)[11]. Life sector $3.1tn at YE2023 (S&P GMI)[13]. No US aggregate exists for pension funds' derivatives |
| **Mortgage investors/servicers/GSEs/FHLBs** | Swaps, swaptions, 10y/ultra 10y futures, caps | Fixed-to-floating conversion of debt and advances (FHLBanks), convexity and MSR hedging | Fixed-rate debt and advances swapped to floating qualify for fair-value hedge accounting. Negative convexity is hedged with options (swaptions, caps) rather than linear instruments. | GSE books grew sharply in 2025: Fannie Mae's risk-management derivatives up 43%, Freddie Mac's swaps up 46% (2025 10-Ks)[17] | Fannie Mae and Freddie Mac: $1.27tn of interest rate risk-management derivatives at YE2025, up 22% in a year, of which $1.0tn swaps (2025 Forms 10-K)[17]. FHLBanks: $1.17tn of interest rate swaps at YE2025 (FHLBanks Office of Finance, Combined Financial Report Q1 2026)[18]. Housing-GSE complex ≈ $2.45tn (sum of the above) |
| **Corporate/SSA issuers** | Receive-fixed swaps (fixed issuance to floating), pay-fixed swaps and rate locks (floating to fixed, pre-issuance) | Funding cost management | Hedge accounting under ASC 815 is simplest with a swap matched to the debt's terms, which can use the shortcut method; futures are eligible but need ongoing effectiveness testing, quarterly re-designation on roll and hedge-ratio rebalancing, so issuers use them mainly for short pre-issuance hedges. | Small and stable share of turnover, 2.1% in 2022 and 2.3% in 2025. Growing as a duration-supply source through S.I.-related issuance | Non-financial customers are 2.3% of global OTC IRD turnover (BIS, Apr 2025)[3] and 0.4% of US-booked turnover (NY Fed, 2025)[4]. AI-related hedging: about $50bn of 10y-equivalent pay-fixed in Q4 2025 (Dallas Fed, Feb 2026)[19] |
| **Foreign official/SWFs/Retail** | Futures (reserve/duration management) | Marginal | Reserve mandates require cash holdings, retail reaches futures only through funds | Marginal | Not identifiable in swap data. In TSY futures, the CFTC "other reportables" net position is about 1% of TY open interest (Oct 2026) |

# Primary users of Treasury futures

Consistent with a previous TBAC charge (TBAC Charge, Q1 2024[1]), the CFTC data show that since 2015 (with a near-full unwind between 2020 and late 2021 after rates bottomed), asset managers have built a large net long position in Treasury futures of ~$1.15tn notional (peaking at ~$1.4tn in February 2026).

In lockstep, leveraged funds, followed by dealers more recently (coinciding with de-regulation developments such as the SLR (Supplementary Leverage Ratio) relaxation in 2020-21 and eSLR reform of 2026), have taken a mirrored position in short futures. Other cohorts have maintained negligible positions throughout the period.

Since the end of 2022, hedge-fund repo borrowing is up $1.9tn (Form PF)[6], leveraged funds' net short Treasury futures $0.7tn (CFTC) and MMF (Money Market Funds) lending through FICC sponsored repo $1.0tn (OFR). These three series moving together since 2018 are evidence of the basis trade financing chain.

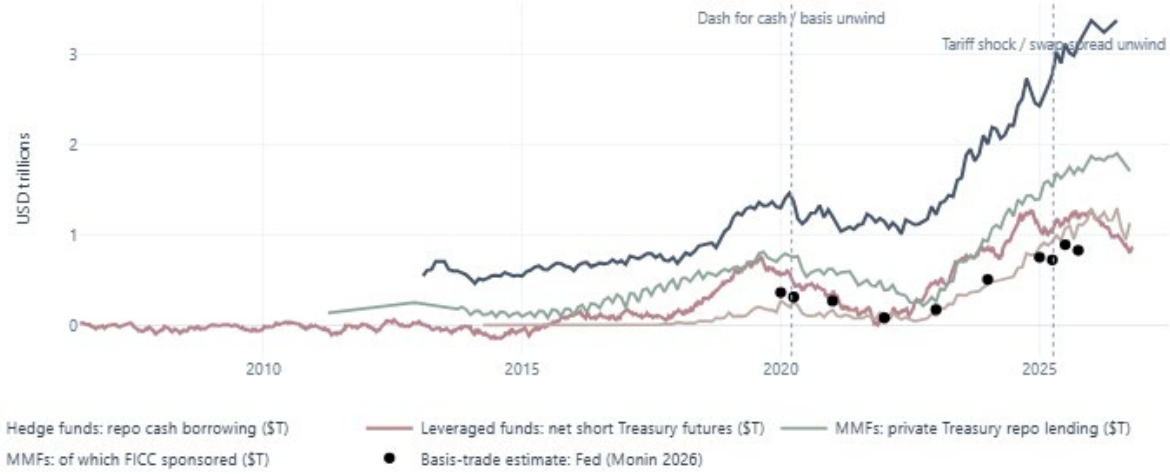
The size of the basis trade is estimated at $0.8-1.2tn depending on the methodology used (see slide 15)[6,22].

**Treasury futures net positioning by cohort**




* Source: CFTC TFF data, market-value notional.

**Basis-trade triangulation**




* Sources: Fed, Monin 2026 (Figures 1 & 3, SEC Form PF) and OFR; CFTC TFF data, market-value notional; OFR Money Market Fund Monitor.

# Primary users of interest rate swaps

## Insurers (U.S. life companies)

- The latest published aggregates (National Association of Insurance Commissioners or NAIC for YE2021[11], S&P Global Market Intelligence for YE2023[13]) put U.S. insurers' derivatives at about $3tn of notional, half of it swaps across all asset classes. 95% of the total is designated as hedging and 98% is held by life companies. The latest NAIC industry report covers YE2021.
- Interest rate swaps have been the largest swap type in every NAIC report we reviewed since 2010: $911bn at YE2017[12] (80% of swap notional) and $1.12tn at YE2021 (73%)[11], with life companies alone at $1.16tn by Q4 2022 (Risk.net, Q4 2022)[14]. On the data released, the book roughly tripled from 2010 to 2018 and has grown more slowly since, to $1.1-1.2tn.
- The swaps lengthen asset duration against annuity and other long-dated liabilities while the assets stay in credit. NAIC's published aggregates do not give direction, but the liability structure makes insurers receivers of fixed, and the one filings-based aggregation that reports it (Risk.net, Q4 2022) finds just over half the book received-fixed.
- Futures are marginal (5.8% of notional, NAIC YE2021).

## Pension funds/LDI

- U.S. corporate defined benefit (DB) plans discount liabilities on AA corporate yields (ASC 715), so their LDI is largely physical long credit and STRIPS, with swaps and futures in completion overlays. There is no U.S. aggregate of their derivatives. Public plans discount at expected return (GASB 67/68) and hedge little.
- Where we can observe direction, it is one-way: UK LDI and pension funds held £167bn net receive-fixed interest rate swaps and £57bn inflation swaps in September 2022[15]. More than 70% of Dutch pension funds hedge liabilities as net fixed receivers in long-dated swaps[16], because the FTK (Dutch regulatory financial assessment framework) values liabilities off the swap curve. De Nederlandsche Bank (DNB) and market participants expect the Dutch pension reform (2026-28) to reduce that long-end receive demand.

**SOFR swap spreads (synthetic before July 2018)**




* Source: J.P. Morgan DataQuery. Pre-2018-07-01 synthetic SOFR spreads follow J.P. Morgan (2022) methodology.

# Primary users of interest rate swaps (continued)

## Negative swap spreads and hedge fund positioning

- A cleared swap costs a bank very little in leverage ratio terms while a repo-financed Treasury position costs capital. Swap rates are therefore pushed below Treasury yields, most of all at the long end, where receiving demand is deepest and duration supply heaviest. The 30y spread has averaged -73bp this year and touched -97bp on 8 April 2025, the widest since SOFR spreads began trading in 2018. At the front end, where futures carry little delivery optionality, the same balance-sheet cost shows up in the futures basis: the 2y swap spread and TU futures richness have moved together since 2018 (see chart at top right)
- Hedge funds take the other side (long cash Treasuries on repo, pay fixed). The Fed's Form PF decomposition (Monin, 2026)[6] puts the swap-spread trade at $305bn in September 2025 (see chart at bottom right), which is about ten times its end-2022 size. The BIS's upper-bound method gives $631bn at Q2 2025 and when applied to the Fed's September 2025 aggregates it gives about $750bn (our calculation).
- Like the basis trade, it is a levered short on the dealer balance-sheet constraint, which is why it loses and de-levers when that constraint binds (March 2020 and April 2025, when the BIS measure contracted 11% between March and June 2025).




* Source: J.P. Morgan DataQuery. Futures richness is the 21-day moving average over non-roll trading days (days to first delivery ≥ 15), connected across contract rolls.




* Source: Fed, Monin 2026 (Figure 5, SEC Form PF).

# Supporting evidence of swap use by insurers and pension funds/LDI

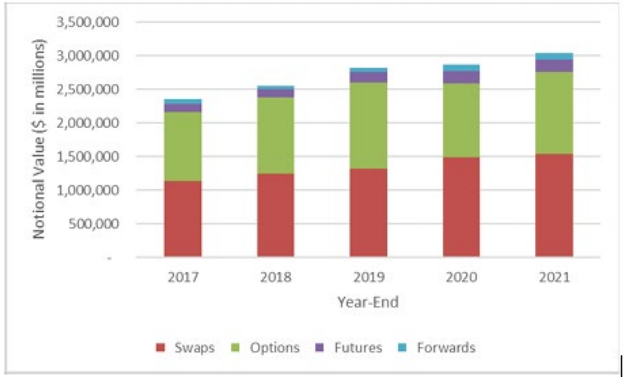
**Supporting charts for the statements made on slide 9. Note that the direction of the swap positions is not published for U.S. insurers (NAIC aggregates) while it is for UK and Dutch pension funds.**

NAIC Schedule DB aggregates (YE2017 to YE2021[11]) show that the insurance derivatives book grew from $2.4tn to $3.0tn, with swaps the largest type over the entire period. Table 2 below gives the YE2021 breakdown by type and filer: options 40.1%, futures 5.8%, forwards 3.5% and life companies 98.3% of the total.

Table 2: Total U.S. Insurance Industry Derivatives Exposure by Derivatives Type, Year-End 2021 (Notional $ in millions)

| Statement Type | Swaps | Options | Futures | Forwards | Total | % of Total |
|---|---|---|---|---|---|---|
| Life | 1,523,760 | 1,195,280 | 174,291 | 101,181 | 2,994,512 | 98.3% |
| P/C | 17,482 | 25,039 | 3,169 | 5,262 | 50,952 | 1.7% |
| Health | 209 | - | 281 | 79 | 569 | 0.0% |
| **Total** | **1,541,451** | **1,220,319** | **177,742** | **106,521** | **3,046,033** | **100%** |
| % of Total | 50.6% | 40.1% | 5.8% | 3.5% | 100% | |

Chart 1: U.S. Insurance Industry Derivatives Exposure, 2017–2021 (Notional $ in millions)




**Bottom left**: Gilt repo is the larger leverage channel for UK LDI and pension funds (September 2022[15]). The interest rate swaps are net received-fixed (negative bars in the authors' convention) and inflation swaps net paid.



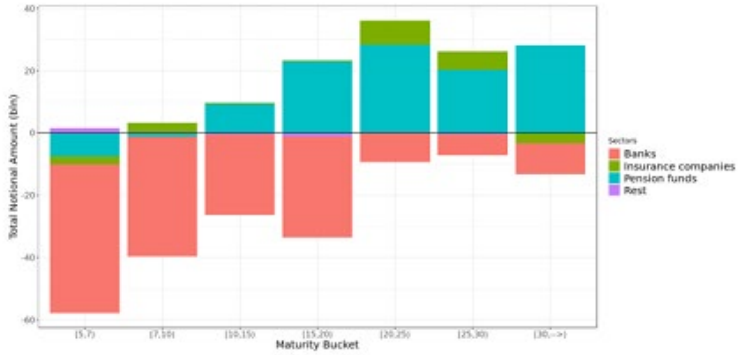

**Chart 1: Net notional of outstanding swap positions (by contract maturity) and net repo borrowing (by collateral maturity) as of 22 September 2022** [(a)]

Sources: SMMD and EMIR TR data, and Bank calculations.

**Bottom center and right**: the share of Dutch pension funds[16] using swaps rose from about 75% in 2012 to over 90% by 2022, and their net Euribor swap positions are concentrated as receivers in the 15-year-plus buckets, opposite to banks at the short end.




(a) Swap usage by Dutch pension funds




(b) Net notional Euribor interest rate swaps Dutch counterparties

Source: DNB Working Paper 801[16]

# Why do users gravitate towards derivatives?

## Operational hurdles: asset managers, corporates, pensions

- Levering Treasuries in cash form requires financing them in repo, which means having a functional repo desk, counterparty lines and documentation, collateral management and settlement infrastructure.
- That set-up cost is borne regardless of position size. Derivatives deliver the equivalent exposure without these hurdles.
- Futures are the lightest route: one exchange-traded contract per curve point, central clearing, anonymity, no documentation beyond a futures commission merchant (FCM for short). Asset managers and anyone without a financing desk start here.
- Similarly, swaps are standardized from a product standpoint yet customizable in their details and can match liabilities precisely.
- While not as demanding as setting up repo trading infrastructure, the set-up required to trade swaps is heavier, involving an ISDA (International Swaps and Derivatives Association) agreement, clearing-broker relationships, swap trading platforms and collateral operations. Pensions, insurers, GSEs and corporates accept that cost because only a swap can be matched to a liability or a bond issue, which a future cannot.

## Funding certainty: asset managers, pensions, insurers

- Repo-financed Treasuries must be rolled continuously (mostly overnight to one week), exposing the holder to rate and availability risk at every roll date.
- Derivatives embed the availability of term financing (but not its rate): a future locks it to the delivery date at the implied repo rate (three months, rolled quarterly) while a swap funds at SOFR for the life of the trade with no roll required, but at whatever rate SOFR prints. Bilateral swaps can be collateralized with securities rather than daily cash.
- Someone still has to carry the cash bond and roll the repo. That is the role hedge funds and dealers play through the basis and swap-spread trades: they have the infrastructure and provide the term financing the end users have outsourced.

# Why do users gravitate towards derivatives? (continued)

## Classification bias: asset managers, insurers, GSEs, corporates

- Fund accounting treats repo interest as an explicit expense: it raises the reported expense ratio and reduces net investment income available for distribution, both of which matter to the end investor and therefore the managers.
- The identical financing cost inside a future or swap is netted within the instrument's price and never appears as a fund expense. Economically equivalent leverage is therefore presented asymmetrically, biasing fund managers toward derivatives.
- Section 18 of the 1940 Act caps fund borrowing, including repo, at one-third of assets, while under SEC Rule 18f-4 (2020) derivatives are governed by a VaR limit that permits far more exposure.
- Hedge accounting pulls the liability hedgers towards swaps: a swap whose terms match the debt or liability qualifies cleanly under ASC 815 (FASB), IFRS 9 (IASB) or SSAP 86 (NAIC), whereas a futures hedge must be re-designated at every roll and tested for effectiveness each period.

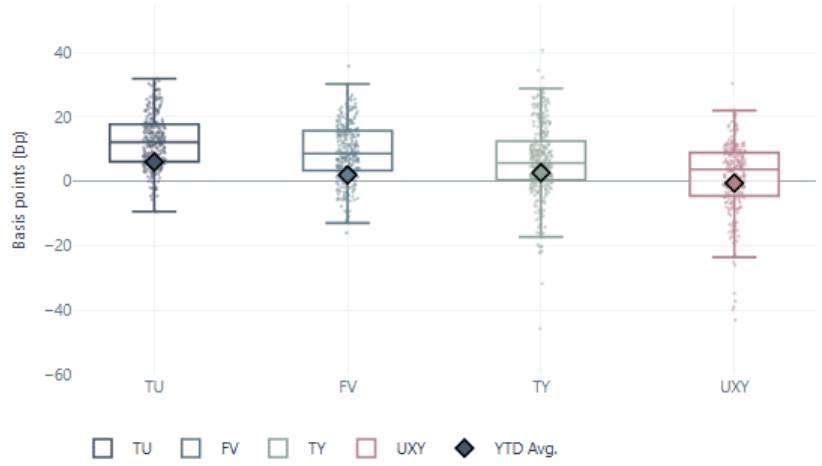
## Tax implications: tax-exempt investors, taxable individuals

- For tax-exempt investors such as pensions, endowments and foundations, financing cash Treasuries with repo makes the bonds' income partly taxable as unrelated business taxable income (UBTI) and requires a Form 990-T filing. Treasury futures and swaps give the same leveraged duration without borrowing, so their gains generally stay tax-exempt. This pushes these investors toward futures rather than owning cash Treasuries on repo, unless they invest through a corporate blocker such as a mutual fund or offshore feeder fund.
- For taxable U.S. investors, futures gains are 60/40 long- and short-term capital gains under U.S. Internal Revenue Code Section 1256 while repo interest is an ordinary deduction limited by Section 163(d) (the same leverage is cheaper after tax in futures).

# Futures basis

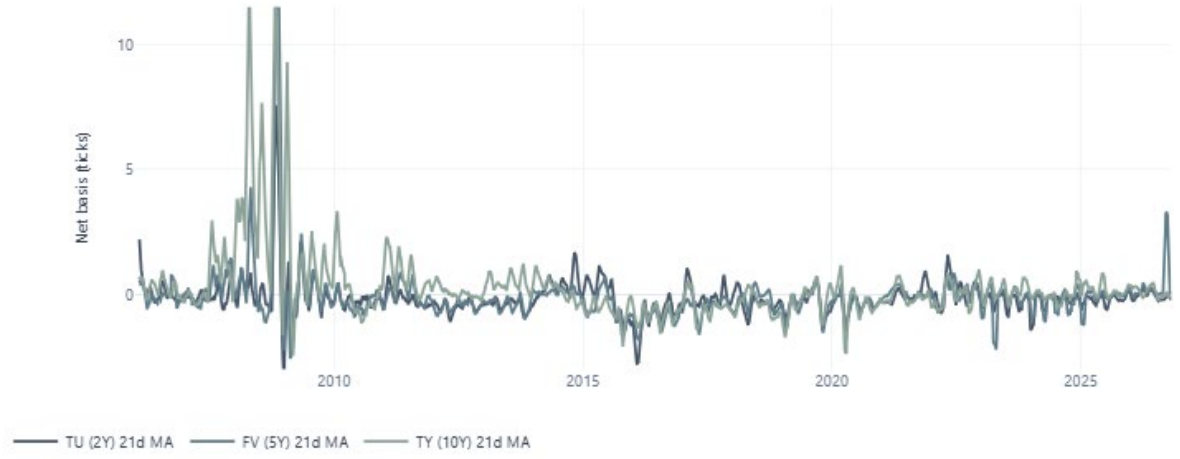
- Futures have traded fair to slightly rich to the replicating cash-plus-repo position for most of the post-2008 period[21]. Over the last two years, the implied repo on TU, FV, TY and UXY ran roughly 0-15bp above matched SOFR OIS, highest in TU and FV (Morgan Stanley, Sept. 2026)[22].
- Net basis equals gross basis less carry to the assumed delivery date, where carry reflects coupon and accrued interest income less the cost of funding the cheapest-to-deliver (CTD) issue in the term repo market.
- Term repo generally trades at a 5-15bp premium (higher in rate) to SOFR OIS to the same date. In addition, CTDs trade special occasionally, which benefits basis-trade holders by lowering funding costs.
- As a result, futures that screen fair to term repo carry a positive margin when financing is rolled overnight.
- Hedge-fund basis positions are financed through a mix of overnight cleared repo and term uncleared repo. The positive carry pick-up applies to the overnight-financed portion, in exchange for daily roll risk.
- Per OFR Brief 26-01[20], about one-third of the $2.4tn hedge fund repo book (~$800bn as of Q3 2024) is cleared through FICC sponsored repo, which is mostly overnight. The rest is largely uncleared bilateral repo, which runs at longer tenors.
- Recent spikes in US and WN net basis reflect embedded optionality and reveal less about implied funding conditions.

**Implied repo rate less equivalent SOFR rate: YTD vs last 2 years (bp)**



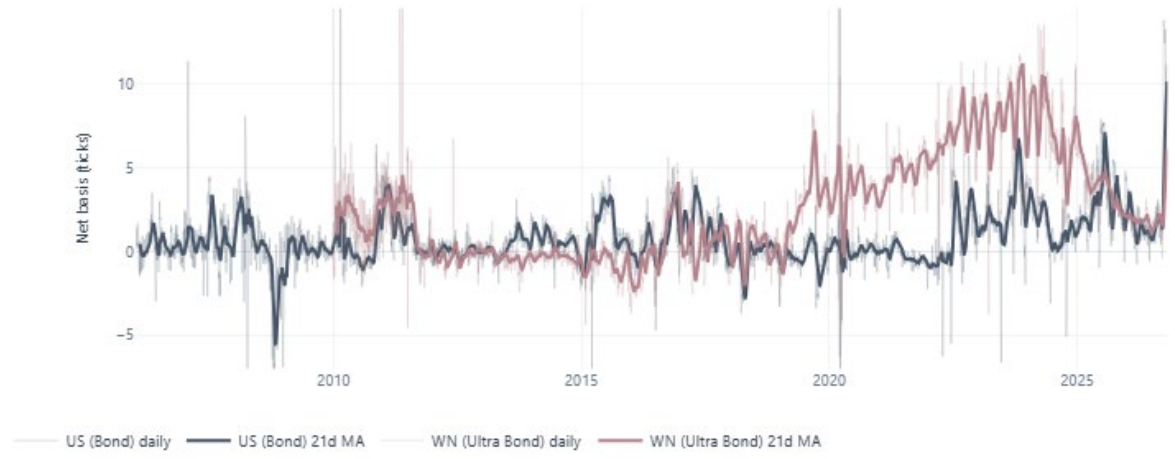

* Sources: Morgan Stanley, Sep 2026 (Exhibit 5); J.P. Morgan DataQuery.

**Treasury futures CTD net basis · TU / FV / TY (21-day MA, ticks)**




* Source: J.P. Morgan DataQuery.

**Treasury futures CTD net basis · US / WN (daily & 21-day MA, ticks)**

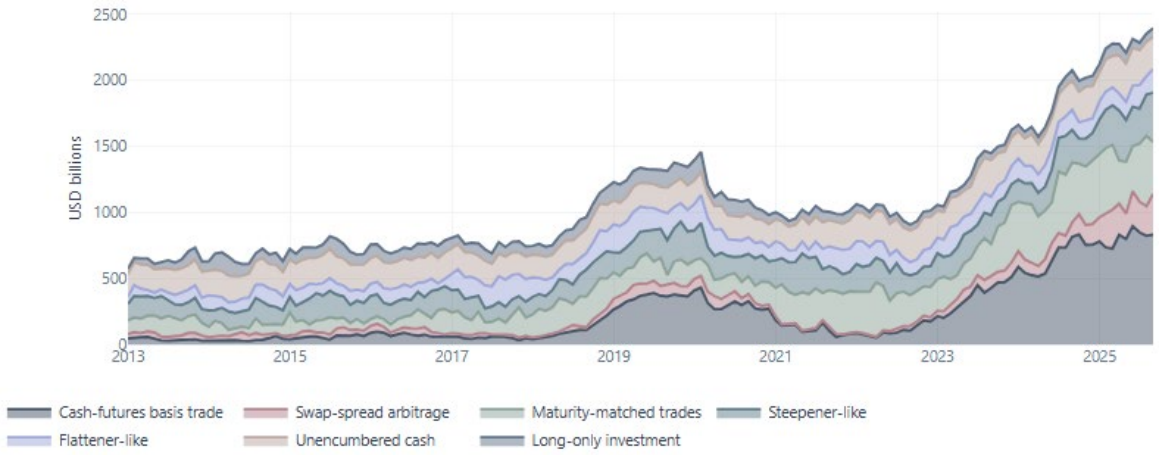



* Source: J.P. Morgan DataQuery.

# Sizing up the basis and swap-spread trades

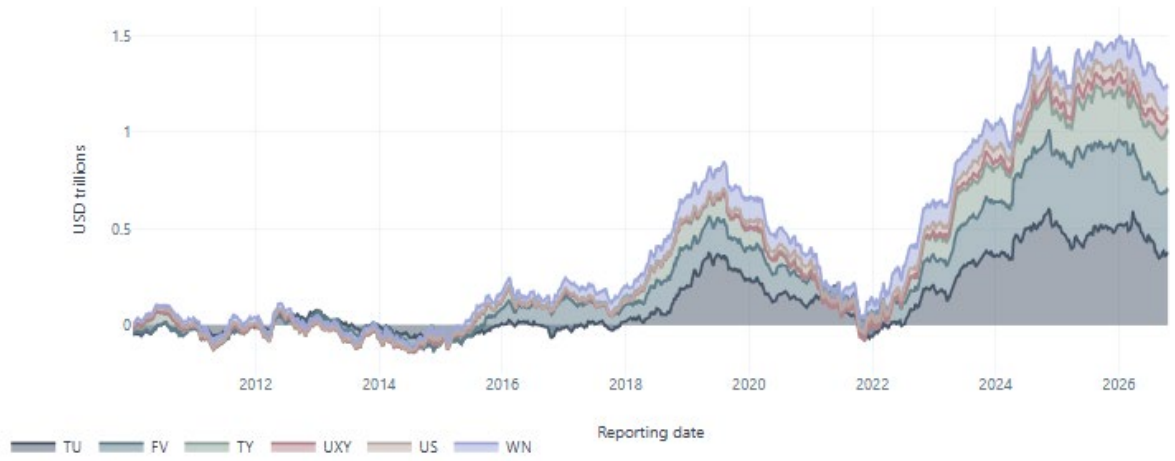
- Fed (Monin, 2026[6]) estimates the basis trade at about $830bn and swap-spread trade at about $305bn as of September 2025.
- Morgan Stanley[22] puts the basis trade at about $1.2tn as of late September 2026 (about $1.35tn in late May and a $1.5tn peak in January).
- The BIS upper-bound method puts the swap-spread trade at $631bn at Q2 2025 (Box B, BIS Quarterly Review, Dec 2025[7]).

**Hedge fund long Treasury decomposition**




* Source: Fed, Monin 2026 (Figure 3, SEC Form PF).

**Basis size by Treasury futures tenor ($T)**




* Source: Reproduced from CFTC TFF data and Bloomberg following Morgan Stanley's Jan 2026 methodology (Exhibit 5).

# End-user derivative exposure creates cash Treasury and repo demand through intermediaries

Derivatives broaden and deepen demand for cash treasuries –

- by expanding market access: lower operational barriers have doubled the number of reportable traders in TU/FV/TY since 2008 (CFTC, TFF)
- by providing capital efficient access to leverage.
- by adding hedging capacity that helps the market absorb and redistribute issuance.

Long derivative exposure increases repo demand through leveraged cash intermediation, which:

- creates pro-cyclical intermediation risk.
- concentrates cash demand among hedge funds and, increasingly, dealers, who offset about half of each week's change in their cash Treasury inventory with futures
- weakens when funding or margin tightens.
- can unwind precisely when the cash market needs buyers (March 2020).
- requires wider basis and swap spreads to compensate intermediaries for scarce balance sheet and repo capacity.

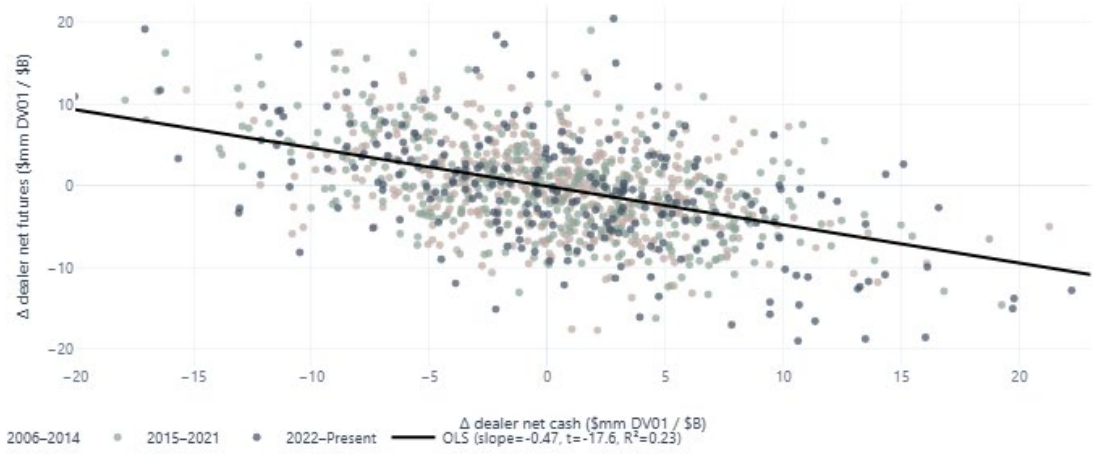
Derivatives increase market access and intermediation capacity, in the process reshape who holds treasuries. The associated cash Treasury demand becomes less reliable when leverage is scarce.

**Reportable traders per US Treasury futures contract (4-week MA)**




* Source: CFTC TFF data.

**Weekly change: dealer futures vs dealer cash Treasuries**




* Sources: NY Fed Primary Dealer Statistics (FR 2004); CFTC TFF data.

# Investors' derivative longs become hedge-fund and dealer cash Treasuries financed in repo

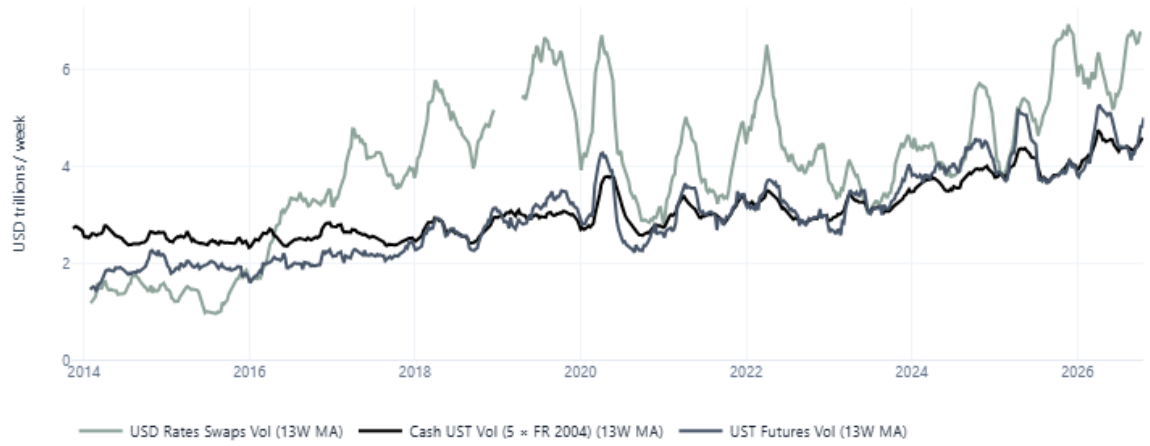
Indirectly through hedge funds and dealers, the usage of derivatives for leverage expands the demand for cash Treasuries as it gives access to Treasury exposure for investor cohorts that might otherwise be unable to participate directly (by lowering operational barriers and enabling efficient leverage).

An increase in long derivative positions by the structural participants therefore raises repo usage, since hedge funds intermediate by buying Treasuries on a levered basis. That intermediation rests mainly with hedge funds, with dealers stepping in more recently as balance-sheet constraints eased.

Importantly, a reduction in the structural longs (a return of rates towards zero, as in 2020-21, could be one trigger) could lead to an unwind of the basis and swap-spread trades and the paired long Treasury holdings of hedge funds and dealers.

Derivatives pricing is tied to repo availability: scarcer or costlier repo means hedge funds and dealers demand more to provide liquidity, widening the basis and swap spreads. Conversely, easier repo compresses them.

**Weekly trading flow ($T / week)**




* Sources: NY Fed Primary Dealer Statistics (FR 2004); CFTC Weekly Swaps Report; CME Group via Bloomberg.

**AM futures positioning vs rates (2010–present)**




* Sources: CFTC TFF data, market-value notional; US Treasury 5Y par yield; NY Fed EFFR.

# Policy initiatives: strengthen cash Treasuries through repo

Policies that curb derivatives risk disrupting today's market structure. A more durable approach is to make cash Treasury financing broader, cheaper and more reliable.

### Robust repo access reinforces what makes Treasuries unique: depth, liquidity, resilience and global benchmark status

- Broaden repo participation by incentivizing institutions to build repo infrastructure.
- Encourage new intermediaries that can aggregate and consolidate repo flows and offer repo services to end users that lack direct market access.
- Expand access to the Fed's Standing Overnight Repo Operations (SRP) beyond primary dealers and banks.
- Preserve seven-day put structures in sponsored repo to maintain MMF participation in term financing.
- Assess potential trade-offs between higher MMF liquidity buffers and term repo market depth.
- Develop deeper term liquidity in cleared repo.

### Reduce operational frictions associated with Treasury settlement

- Streamline Fedwire settlement, fails management and intraday liquidity processes to lower participant burden.
- Improve matching of receives and deliveries to reduce operational and funding costs.
- Automate pair-off and exception management to cut the manual resources required.

### Reduce balance-sheet constraints

- Exempt Treasuries from the supplementary leverage ratio and re-evaluate the Tier 1 leverage ratio.
- Recognize pre-positioned discount-window collateral in liquidity metrics, freeing capacity for Treasury holdings and intermediation.

### Reduce onboarding friction through greater standardization of repo and clearing documentation

- Consolidate the multiple legal agreements needed before market participation into a single, streamlined framework.
- Standardize terms on industry templates to limit bespoke negotiation.
- Shorten and standardize onboarding to encourage participation in cash Treasury and repo markets.

### Leveling the playing field between repo and derivatives

- Fund expenses: Exempt interest on Treasury-collateralized repo from the operating expense ratio, with a separate disclosure of financing costs, so that levered cash Treasury positions aren't penalized relative to futures.
- Tax exempt investors: Clarify or, if necessary, amend the tax rules so that short-term, cleared Treasury repo doesn't create taxable income for tax-exempt investors.
- Registered funds: Raise awareness of the Rule 18f-4 option to treat repo as a derivative, with risk limits and disclosure.

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