# Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

April 2011

# Responses to the Primary Dealer Policy Expectations Survey
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*For most questions, median responses across dealers, along with the 25th and 75th percentiles, are reported. For questions that ask respondents to give a probability distribution, the average response across dealers for each potential outcome is reported.[1] For multiple choice questions, the number of responses for each option is reported. Brief summaries of the comments received in free response form have also been provided.*

*Except where noted, all primary dealers responded to each question. In some cases, dealers may not have forecasts extending to the same time horizon as requested in the survey. In these instances, the number of respondents who fully answered all parts of the question is provided.*

### *Monetary Policy Expectations*

**1. Of the possible outcomes below, please indicate the percent chance you attach to the indicated policy target range or target rate following each of the next 3 FOMC meetings:**

| | Policy Target Range or Rate | | | | | | |
|---|---|---|---|---|---|---|---|
| | **0 - .25%** | **0.25%** | **0.50%** | **0.75%** | **1.00%** | **1.25%** | **>1.25%** |
| Average: | | | | | | | |
| One Meeting Ahead (April) | 99% | 1% | 0% | 0% | 0% | 0% | 0% |
| Two Meetings Ahead (June) | 98% | 1% | 1% | 0% | 0% | 0% | 0% |
| Three Meetings Ahead (August) | 96% | 2% | 2% | 0% | 0% | 0% | 0% |

**2. a) Do you expect any changes in the FOMC statement and, if so, what changes?**

*Several dealers commented that they expected the FOMC statement to confirm that the Committee intends to complete its current asset purchase program as planned. Some dealers noted expectations for the 'extended period' language to be unchanged. A couple of dealers expected the statement to address the eventual exit sequence from current levels of monetary accommodation.*

*Some contacts expected the Committee to acknowledge the deterioration in economic data for Q1, with a couple expecting some change to the 'firmer footing' language. Some others, however, expected that there would be no meaningful change to the economic assessment. Some dealers expected the statement to acknowledge upside risk to inflation.*

**b) What additional information do you expect Chairman Bernanke to provide in his post-FOMC meeting press conference on April 27th?**

*Some dealers expected the Chairman to comment on the Committee's view on the economic outlook and the economic projections provided by FOMC participants. Some also expected the Chairman to specifically address the issue of higher inflation. Conversely, some dealers were not expecting any material new information to come out of the press conference.*

*Expectations regarding policy-related topics were varied. The expectation that the Chairman would acknowledge that the current LSAP program would be completed as expected and that the Committee would hold the size of the balance sheet constant following the end of the program were each cited by a few dealers. A couple of dealers expected the Chairman to comment on the success and effectiveness of the LSAP program. A few other dealers expected some discussion of the eventual exit sequence.*

[1] Answers may not sum to 100 due to rounding.

3. **Of the possible outcomes below, please indicate the percent chance you attach to the timing of the first federal funds target rate increase.**

| | **Q2 2011** | **Q3 2011** | **Q4 2011** | **Q1 2012** | **Q2 2012** | **Q3 2012** | **Q4 2012** | **Q1 2013** | **≥ Q2 2013** |
|---|---|---|---|---|---|---|---|---|---|
| Average | 1% | 3% | 12% | 20% | 19% | 17% | 13% | 8% | 7% |

| | **Most likely quarter and year of first target rate increase:** |
|---|---|
| *25th Pctl* | *Q1 2012* |
| Median | Q2 2012 |
| *75th Pctl* | *Q4 2012* |

4. **Provide your firm's estimate of the most likely outcome (i.e. the mode) for the federal funds target rate or range at the end of each quarter:**

| | **Q2 2011** | **Q3 2011** | **Q4 2011** | **Q1 2012** | **Q2 2012** | **Q3 2012** | **Q4 2012** | **Q1 2013** |
|---|---|---|---|---|---|---|---|---|
| *25th Pctl* | *0-.25%* | *0-.25%* | *0-.25%* | *0-.25%* | *0-.25%* | *0.50%* | *0.75%* | *0.94%* |
| Median | 0-.25% | 0-.25% | 0-.25% | 0-.25% | 0.19% | 0.63% | 1.13% | 1.50% |
| *75th Pctl* | *0-.25%* | *0-.25%* | *0-.25%* | *0.50%* | *0.75%* | *1.25%* | *1.56%* | *2.06%* |

5. **Of the possible outcomes below, please indicate the percent chance you attach to the federal funds target rate or range 12 months from now:**

| | **0.00 - 0.25%** | **0.26 - 0.50%** | **0.51 - 1.00%** | **1.01 - 1.50%** | **1.51 - 2.00%** | **2.01 - 2.50%** | **≥2.51%** |
|---|---|---|---|---|---|---|---|
| Average | 51% | 22% | 17% | 7% | 2% | 1% | 0% |

6. **How would you grade the Federal Reserve System's communication with the markets and with the public since the last policy survey on 3/7/11? Please provide a rating between 1 and 5, with 1 indicating ineffectiveness and 5 indicating effectiveness.**

| | **Number of Respondents** |
|---|---|
| 1 - Very Ineffective | 0 |
| 2 | 6 |
| 3 | 13 |
| 4 | 1 |
| 5 - Very Effective | 0 |

***(19 primary dealer comments)***

*Most dealers mentioned that the wide variety of views expressed by Federal Reserve officials in their public commentary created an inconsistent message over the intermeeting period, while a few noted that the Chairman's press conferences could serve to alleviate this confusion. A few dealers noted a lack of clarity regarding balance sheet policy since the last policy survey.*

**7. In the November 2010 FOMC statement, the Committee announced the following: "The Committee intends to purchase a further $600 billion of longer-term Treasury securities by the end of the second quarter of 2011, a pace of about $75 billion per month. The Committee will regularly review the pace of its securities purchases and the overall size of the asset-purchase program in light of incoming information and will adjust the program as needed to best foster maximum employment and price stability." What is your current expectation for the total cumulative size of the asset purchase program, and when do you expect the program to be completed? In your estimate of total cumulative size, please include securities already purchased under this program since November 3, but exclude purchases associated with agency and agency MBS reinvestment.**

| | Cumulative Size of Program (Billions) | Total Length of Program (months) |
|---|---|---|
| *25th Pctl* | *600* | *6.7* |
| Median | 600 | 6.7 |
| *75th Pctl* | *600* | *6.7* |

***(17 primary dealer comments)***

*Many dealers expected the Federal Reserve to complete its large scale asset purchase (LSAP) program as initially outlined in the November FOMC statement; this was the majority view expressed by dealers who provided written comments. Several of these dealers mentioned that Federal Reserve communication had led them to adopt this view, with a few dealers citing the March FOMC meeting minutes in particular. Some dealers noted that a tapering of the program was unlikely. A few mentioned that additional asset purchases were also unlikely.*

**8. What is your expectation for the amount of domestic securities held outright in the SOMA portfolio at year-end for each of the next five years? For your reference, the current level of domestic assets in SOMA is $2,428 billion, according to the latest H.4.1 release.**

***(19 complete primary dealer responses)***

**Estimated amount of domestic securities**
*($ Billions)*

| | 2011 | 2012 | 2013 | 2014 | 2015 |
|---|---|---|---|---|---|
| *25th Pctl* | *2567* | *2123* | *1655* | *1225* | *1100* |
| Median | 2600 | 2257 | 1950 | 1600 | 1325 |
| *75th Pctl* | *2637* | *2381* | *2112* | *1850* | *1525* |

***(19 primary dealer comments)***

*Comments suggest dealers had varied expectations for the size and composition of the SOMA portfolio over the next five years. Some dealers, in giving their view of the potential exit sequence, expected that asset sales would only follow portfolio redemptions. A couple of dealers noted that their portfolio estimates were based on an assumption of no outright asset sales.*

**9. a) In question 3, you stated that you expect that the first increase in the fed funds target rate is most likely to occur in ____. What is your expectation for the level of reserves held with Federal Reserve Banks at the time of the first target rate increase? For your reference, the most recent H.4.1 lists reserve balances at $1,503 billion.**

| | Level of reserves at time of first target rate increase *($ Billions)* |
|---|---|
| *25th Pctl* | *956* |
| Median | 1,275 |
| *75th Pctl* | *1,419* |

**b) Please indicate whether the measures listed below will most likely be used for the first time before, concurrent with, or after the first increase in the fed funds target rate, if at all (excluding any operational readiness exercises). Secondly, if you select "before" or "after," please indicate the number of FOMC meetings relative to the first increase in the fed funds target rate you expect each measure to be first utilized.**

| | | Number of meetings before (-) or after(+) first target rate increase |
|---|---|---|
| Increase IOER* | *25th Pctl* | *0* |
| | Median | 0 |
| | *75th Pctl* | *0* |
| Change in "Extended Period" Language in FOMC Statement | *25th Pctl* | *-4* |
| | Median | -3 |
| | *75th Pctl* | *-2* |
| Reverse Repurchases Operations | *25th Pctl* | *-3* |
| | Median | -1 |
| | *75th Pctl* | *-1* |
| Term Deposits | *25th Pctl* | *-3* |
| | Median | -1 |
| | *75th Pctl* | *-1* |
| Halting Treasury Reinvestment | *25th Pctl* | *-4* |
| | Median | -2 |
| | *75th Pctl* | *2* |
| Halting Agency Debt Reinvestment | *25th Pctl* | *-5* |
| | Median | -3 |
| | *75th Pctl* | *-3* |
| Halting Agency MBS Reinvestment | *25th Pctl* | *-5* |
| | Median | -3 |
| | *75th Pctl* | *-3* |
| Treasury Sales | *25th Pctl* | *2* |
| | Median | 4 |
| | *75th Pctl* | *6* |
| Agency Debt Sales | *25th Pctl* | *3* |
| | Median | 4 |
| | *75th Pctl* | *6* |
| Agency MBS Sales | *25th Pctl* | *3* |
| | Median | 4 |
| | *75th Pctl* | *6* |

** IOER refers to the rate paid on excess reserves.*

***(19 primary dealer comments)***

*Several dealers thought that the first increase in the federal funds target rate would follow temporary draining of some kind, with some specifying expectations for a halting of reinvestments and temporary draining operations. Some dealers also expected that asset sales would follow the first increase in the federal funds rate. A few dealers expected to see a halt to reinvestments as the first action, and a couple saw draining using temporary tools as the second action. Some dealers also noted that a change to the forward guidance would precede the first increase in the federal funds rate, with a couple expecting that this action would occur after the halting of reinvestments. A few dealers thought the federal funds target rate and IOER would be increased simultaneously. Some dealers highlighted uncertainty around the exit sequence.*

**c) How do you expect the forward policy guidance (i.e. "exceptionally low levels for the federal funds rate for an extended period" language) could evolve in future FOMC statements?**

*Many dealers thought that the “extended period” part of the phrase could be altered, with a few suggesting that it could be replaced with the phrase “some time”. A few dealers thought the “extended period” part of the language would be altered first, with the “exceptionally low” part of the phrase altered later. A couple of dealers thought that the guidance could be completely reworked. Some dealers expected the Committee to maintain the “extended period” language for the time being. A couple believed that the phrase could be dropped in September 2011, while November and December were cited each by a couple of dealers. A couple of dealers expected that the Committee might drop or alter the forward guidance 2 to 3 meetings before the first rate hike.*

**10. What is the maximum dollar amount of reserves that could be drained over a six week period using temporary open market operations without creating market dislocations? Please answer by filling out the following table indicating the amount using only reverse repos, using only term deposits, and using reverse repos and term deposits. Please assume market conditions similar to current market conditions.**

**Maximum Dollar Amount of Reserves Drained**

*($ Billions)*

| | Reverse Repos Only | Term Deposits Only | Reverse Repos & Term Deposits Combined |
|---|---|---|---|
| *25th Pctl* | *150* | *100* | *300* |
| Median | 225 | 225 | 500 |
| *75th Pctl* | *425* | *425* | *681* |

***(19 primary dealer comments)***

*Some dealers noted that the ability of the TDF to drain reserves would depend on the structure of the program, including the rates and tenors offered. A few dealers thought that the TDF would have a larger capacity than RRPs in draining reserves, while a couple of dealers viewed that RRPs would have a larger capacity than the TDF. A few dealers noted that the inclusion of money funds as counterparties would allow RRPs to absorb more reserves than would have been the case otherwise. A couple of dealers each thought that the status of the Treasury’s Supplementary Financing Program (SFP) would also be a consideration, and that the market would need time for adjustment. A few dealers expected that draining operations could cause market dislocations or disruption. A couple noted that the amount of draining would be limited by the 6-week timeframe laid out in the question. Some dealers saw a high level of uncertainty around this question.*

**11. Currently, the level of excess reserves is $1.5 trillion, the IOER rate is 25 basis points, and the average federal funds effective rate during the current maintenance period is 9 basis points. For each level of reserves and IOER rate given in the table below, please enter your expectation for the level of the fed funds effective rate that would result. Please assume market conditions similar to current market conditions.**

| | | Effective Federal Funds Rate | | |
|---|---|---|---|---|
| | | IOER=0.25% | IOER=1.00% | IOER=2.00% |
| Reserves= $1,500 Billion | *25th Pctl* | *0.09%* | *0.75%* | *1.65%* |
| | Median | 0.09% | 0.83% | 1.75% |
| | *75th Pctl* | *0.09%* | *0.85%* | *1.85%* |
| Reserves= $1,000 Billion | *25th Pctl* | *0.15%* | *0.80%* | *1.74%* |
| | Median | 0.16% | 0.86% | 1.85% |
| | *75th Pctl* | *0.20%* | *0.92%* | *1.92%* |
| Reserves= $500 Billion | *25th Pctl* | *0.20%* | *0.90%* | *1.85%* |
| | Median | 0.23% | 0.95% | 1.94% |
| | *75th Pctl* | *0.25%* | *1.00%* | *2.00%* |
| Reserves= $0 - $25 Billion | *25th Pctl* | *0.25%* | *1.00%* | *2.00%* |
| | Median | 0.26% | 1.03% | 2.00% |
| | *75th Pctl* | *0.31%* | *1.14%* | *2.08%* |

***(18 primary dealer comments)***

*Some dealers cited that they perceive a high degree of uncertainty around this issue. A few dealers believed that the FDIC insurance fee change introduced more uncertainty into the relationship between the federal funds rate and IOER, while a couple of dealers cited the idiosyncratic nature of the federal funds market as creating uncertainty around how the federal funds rate will behave when IOER and/or the level of reserves are changed. A few dealers noted the fed funds rate is difficult to manage at higher levels of reserves, and a couple cited that that reserves would have to decline below a certain point before the federal funds effective would follow IOER closely . A few dealers also expected that the federal funds rate could exceed IOER if excess reserves were to fall below a certain point.*

## Economic Indicator Forecasts

**12. a and b) Provide your firm's estimate of the most likely outcome (i.e. the mode) for output and inflation. Are the risks to output, inflation and unemployment skewed to the downside, balanced or skewed to the upside relative to your forecast? Please comment on any risks you see to your forecast.**

***(10 complete primary dealer responses)***

| | | Q1 2011 | Q2 2011 | Q3 2011 | Q4 2011 | Q4/Q4 2011 | Q4/Q4 2012 | Q4/Q4 2013 |
|---|---|---|---|---|---|---|---|---|
| GDP | *25th Pctl* | *1.50%* | *2.88%* | *3.00%* | *3.00%* | *2.68%* | *3.00%* | *3.40%* |
| | Median | 1.80% | 3.30% | 3.35% | 3.40% | 3.00% | 3.30% | 3.50% |
| | *75th Pctl* | *2.00%* | *3.55%* | *3.85%* | *4.00%* | *3.23%* | *3.63%* | *3.50%* |
| Core PCE | *25th Pctl* | *0.80%* | *1.00%* | *1.10%* | *1.25%* | *1.25%* | *1.35%* | *1.63%* |
| | Median | 0.90% | 1.00% | 1.20% | 1.35% | 1.35% | 1.70% | 1.85% |
| | *75th Pctl* | *0.90%* | *1.10%* | *1.30%* | *1.53%* | *1.53%* | *2.03%* | *2.38%* |
| Unemployment Rate | *25th Pctl* | | | | | *8.30%* | *7.30%* | *6.68%* |
| | Median | | | | | 8.40% | 7.70% | 7.00% |
| | *75th Pctl* | | | | | *8.50%* | *8.00%* | *7.38%* |

***(10 complete primary dealer responses)***

**2011 Forecasts**
**Number of Respondents Citing:**

| | Downside Risk | Balanced Risk | Upside Risk |
|---|---|---|---|
| GDP | 7 | 11 | 2 |
| Core PCE | 1 | 10 | 9 |
| Unemployment Rate | 6 | 11 | 3 |

**2012 Forecasts**
**Number of Respondents Citing:**

| | Downside Risk | Balanced Risk | Upside Risk |
|---|---|---|---|
| GDP | 4 | 13 | 3 |
| Core PCE | 0 | 13 | 7 |
| Unemployment Rate | 7 | 10 | 3 |

**2013 Forecasts**
**Number of Respondents Citing:**

| | Downside Risk | Balanced Risk | Upside Risk |
|---|---|---|---|
| GDP | 2 | 8 | 0 |
| Core PCE | 0 | 8 | 2 |
| Unemployment Rate | 2 | 6 | 2 |

***(16 primary dealer comments)***

*Several dealers discussed risks to forecasts as a result of higher oil and energy prices. The majority of these dealers focused on the downside risks to growth from recent energy price movements; only a few noted upside risk to inflation forecasts as a result of higher energy prices. Downside risks to growth from fiscal consolidation and disruptions to global supply chains caused by the earthquake in Japan were also each cited by a few dealers.*

**c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 3/7/11?**

**Number of Dealers:**

| | Less Uncertain | Equally Uncertain | More Uncertain |
|---|---|---|---|
| GDP Uncertainty | 2 | 8 | 10 |
| Core PCE Uncertainty | 4 | 10 | 6 |

**13. What percent chance do you attach to the 4-quarter change in the core PCE deflator falling below zero by the end of Q1 2012?**

| | Probability |
|---|---|
| *25th Pctl* | *3%* |
| Median | 5% |
| *75th Pctl* | *10%* |

**14. For the outcomes below, please indicate the percent chance you attach for the annual average CPI inflation rate from 2016 - 2021. Please also indicate your point estimate for the most likely outcome (i.e. the mode).**

| | ≤1.0% | 1.01-1.5% | 1.51-2.0% | 2.01-2.5% | 2.51-3.0% | ≥3.01% |
|---|---|---|---|---|---|---|
| Average | 4% | 11% | 22% | 30% | 22% | 10% |

| | Point Estimate |
|---|---|
| *25th Pctl* | *2.08%* |
| Median | 2.30% |
| *75th Pctl* | *2.50%* |

**15. a and b) What percent chance do you attach to the US economy currently being in a recession (NBER-defined)? What percent chance would you attach to the US economy being in a recession in 6 months (NBER-defined)?**

| | Currently in NBER Recession |
|---|---|
| *25th Pctl* | *0%* |
| Median | 2% |
| *75th Pctl* | *5%* |

| | NBER Recession in 6 Months |
|---|---|
| *25th Pctl* | *5%* |
| Median | 10% |
| *75th Pctl* | *15%* |

**16. Please comment on any changes to your macroeconomic assessments since the last FOMC meeting.**

*Several dealers commented that they had lowered their GDP forecasts over the intermeeting period. Some dealers noted the revision owed to weaker incoming economic data in the first quarter, but energy prices movements and severe weather were also each cited as factors by some dealers. A few and a couple of dealers, respectively, viewed the Japanese earthquake and the euro area sovereign debt and banking crisis as leading them to downgrade their economic outlook. A couple of dealers characterized the current economic situation as fragile. Separately, a few dealers mentioned that they had raised their inflation forecasts.*