Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

November 2011

Responses to the Primary Dealer Policy Expectations Survey
Distributed: 10/20/2011 – Received by: 10/24/2011

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 (November)	99%	1%	0%	0%	0%	0%	0%
Two Meetings Ahead (December)	99%	1%	0%	0%	0%	0%	0%
Three Meetings Ahead (January)	99%	1%	0%	0%	0%	0%	0%

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

Several dealers expected no substantial changes in the FOMC statement, but did look for an upgrade to the Committee's assessment of current economic conditions to reflect stronger recent economic data. However, some of these dealers expected the statement to maintain that risks to growth outlook remain on the downside. A few dealers commented on potential changes to the forward guidance in the statement, but there was no consensus on what this change would be. Some dealers expected no changes to the FOMC statement at all.

b) What additional information do you expect Chairman Bernanke to provide in his post-FOMC meeting press conference on November 2nd?

Many dealers expected Chairman Bernanke to discuss options to improve the FOMC's communication strategy, possibly through future policy rate guidance and/or a clarification of long-term goals. Some dealers expected the Chairman to discuss conditions for possible further easing steps, including additional asset purchases. A few dealers expected the Chairman to elaborate on the rationale for and the objectives of the Maturity Extension Program (MEP). A few dealers noted the possibility of a discussion of measures aimed at improving the housing market and/or the market for mortgage finance. Finally, a couple of dealers expected the Chairman to discuss changes to the rate of interest on excess reserves (IOER) as a possible easing tool.

[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:**[2]

	Q4 2011	Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014	≥ Q2 2014
Average	0.10%	0.20%	0.50%	1.20%	1.85%	3.45%	8.50%	14.40%	12.65%	15.85%	41.30%

	Most likely quarter and year of first target rate increase:
25th Pctl	*Q3 2013*
Median	Q1 2014
75th Pctl	*Q2 2014*

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:**

(19 primary dealer complete responses)

	Q4 2011	Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014
25th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*
Median	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%
75th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*0.75%*	*0.88%*

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	95%	3%	1%	0%	0%	0%	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 9/12/11? Please provide a rating between 1 and 5, with 1 indicating ineffectiveness and 5 indicating effectiveness.**

[2] This table has been revised since its original release.

	Number of Respondents
1 - Very Ineffective	0
2	2
3	7
4	11
5 - Very Effective	0

(19 primary dealer comments)

Some dealers viewed the Fed communication during the intermeeting period as clear and effective. However, several dealers noted that the diverging views expressed by FOMC participants through their different public appearances created some confusion. Some dealers commented that they had expected broader communication about the rationale for and the objectives of the Maturity Extension Program (MEP).

7. Recent FOMC communication has discussed several different ways monetary policy could be altered to provide either less or more accommodation.

a) For each listed policy tool, please indicate the probability the tool will be used to signal future policy tightening or to tighten policy at the next FOMC meeting and within the next 1 and 2 years. Please comment.

		Probability at next FOMC meeting	Probability within 1 year	Probability within 2 years
	25th Pctl	*0%*	*0%*	*5%*
Raise interest on excess reserves	Median	0%	1%	20%
	75th Pctl	*0%*	*5%*	*40%*
	25th Pctl	*0%*	*0%*	*11%*
Drain reserves through temporary tools	Median	0%	5%	23%
	75th Pctl	*0%*	*11%*	*56%*
	25th Pctl	*0%*	*0%*	*14%*
Halt reinvestments	Median	0%	7%	38%
	75th Pctl	*0%*	*21%*	*71%*
	25th Pctl	*0%*	*0%*	*2%*
Reduce size of SOMA portfolio through selling securities	Median	0%	1%	5%
	75th Pctl	*0%*	*3%*	*21%*
	25th Pctl	*0%*	*0%*	*5%*
Reduce duration of portfolio*	Median	0%	1%	8%
	75th Pctl	*0%*	*5%*	*31%*
	25th Pctl	*0%*	*1%*	*19%*
Change guidance on the period over which the target rate will remain in effect	Median	0%	10%	40%
	75th Pctl	*0%*	*19%*	*64%*

*i.e. a deliberate action to decrease the duration of the SOMA portfolio, independent of other policy changes

(16 primary dealer comments)

Several dealers commented that they did not expect any tightening over the next two years. Some dealers, however, commented on the sequence and tools with which they expect the FOMC to tighten policy, with a few of them viewing a change to the forward rate guidance as the first action to be taken to signal future policy tightening or to tighten policy.

b) For each listed policy tool, please indicate the probability the tool will be used to signal future policy easing or to ease policy at the next FOMC meeting and within the next 1 and 2 years. Please explain.

		Probability at next FOMC meeting	Probability within 1 year	Probability within 2 years
	25th Pctl	*0%*	*10%*	*10%*
Lower interest on excess reserves	Median	5%	15%	20%
	75th Pctl	*11%*	*25%*	*26%*
	25th Pctl	*4%*	*34%*	*38%*
Expand SOMA portfolio through security purchases	Median	5%	50%	50%
	75th Pctl	*15%*	*55%*	*60%*
	25th Pctl	*0%*	*4%*	*4%*
Increase duration of portfolio*	Median	0%	10%	13%
	75th Pctl	*1%*	*28%*	*36%*
	25th Pctl	*5%*	*38%*	*48%*
Change the forward guidance on the path of the federal funds rate	Median	18%	50%	58%
	75th Pctl	*31%*	*71%*	*78%*
	25th Pctl	*2%*	*29%*	*30%*
Provide guidance on the period over which the SOMA portfolio will remain at the current level	Median	13%	40%	42%
	75th Pctl	*25%*	*53%*	*63%*

*i.e. a deliberate action to decrease the duration of the SOMA portfolio, independent of other policy changes

(16 primary dealer comments)

Some dealers viewed changes to the forward rate guidance as a likely tool employed to ease policy. Some dealers also commented on the possibility of additional asset purchases over the next two years, with a few specifically expecting purchases to be concentrated in agency MBS securities. Another couple of dealers expected the FOMC to provide forward guidance on the path of the SOMA portfolio.

8. What are your expectations for the amount of domestic securities held outright in the SOMA portfolio and for the expected level of reserves at year-end for each of the next five years?

		2011	2012	2013 ($ Billions)	2014	2015
	25th Pctl	*1669*	*1669*	*1664*	*1400*	*1195*
Estimated amount of Treasuries	Median	1669	1670	1670	1599	1300
	75th Pctl	*1670*	*1848*	*1948*	*1747*	*1719*
	25th Pctl	*979*	*979*	*900*	*700*	*400*
Estimated amount of agency debt and MBS	Median	979	980	979	800	650
	75th Pctl	*980*	*1192*	*1314*	*1285*	*1043*
	25th Pctl	*2648*	*2648*	*2540*	*2138*	*1615*
Estimated amount of domestic assets in SOMA	Median	2648	2649	2648	2415	1954
	75th Pctl	*2649*	*3063*	*3232*	*3032*	*2777*
	25th Pctl	*1633*	*1569*	*1313*	*888*	*500*
Estimated level of reserves	Median	1633	1629	1568	1100	650
	75th Pctl	*1635*	*1825*	*1950*	*1707*	*1404*

(17 primary dealer comments)

In describing their expectations for the path of the SOMA portfolio and the expected level of reserves, several dealers commented on their expectations for the sequence with which they envision an eventual tightening of policy. However, some dealers expressed expectations for additional asset purchases, with few of these dealers anticipating that these purchases would include both U.S. Treasuries and agency MBS securities.

9. a) Provide your firm's estimate of the most likely outcome (i.e. the mode) for output, inflation and unemployment.

(13 primary dealer complete responses)

		Q3 2011	Q4 2011	Q1 2012	Q2 2012	Q4/Q4 2011	Q4/Q4 2012	Q4/Q4 2013
	25th Pctl	*2.48%*	*1.60%*	*1.25%*	*1.78%*	*1.40%*	*1.85%*	*2.00%*
GDP	Median	2.70%	2.00%	1.75%	2.20%	1.60%	2.15%	2.40%
	75th Pctl	*2.83%*	*2.35%*	*2.13%*	*2.43%*	*1.70%*	*2.43%*	*2.80%*
	25th Pctl	*1.60%*	*1.78%*	*1.75%*	*1.58%*	*1.78%*	*1.38%*	*1.50%*
Core PCE	Median	1.70%	1.90%	1.90%	1.70%	1.90%	1.60%	1.70%
	75th Pctl	*1.70%*	*2.00%*	*2.03%*	*1.90%*	*2.00%*	*1.80%*	*2.00%*
	25th Pctl	*2.88%*	*2.50%*	*1.98%*	*1.40%*	*2.50%*	*1.45%*	*1.70%*
Headline PCE	Median	2.90%	2.70%	2.05%	1.70%	2.70%	1.90%	2.00%
	75th Pctl	*2.90%*	*2.83%*	*2.30%*	*2.10%*	*2.83%*	*2.30%*	*2.10%*
	25th Pctl					*9.08%*	*8.70%*	*8.00%*
Unemployment Rate*	Median					9.10%	8.80%	8.20%
	75th Pctl					*9.20%*	*9.20%*	*8.80%*

*Average level over Q4 in the case of the unemployment rate.

b) 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.

(13 primary dealer complete responses)

2011 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	0	16	4
Core PCE	1	15	4
Headline PCE	3	14	3
Unemployment Rate	2	16	2

2012 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	6	13	1
Core PCE	2	13	5
Headline PCE	3	13	4
Unemployment Rate	1	12	7

2013 Forecasts

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	5	6	2
Core PCE	3	8	2
Headline PCE	2	10	1
Unemployment Rate	2	7	4

(15 primary dealer comments)

Many dealers cited the ongoing European sovereign debt and banking crisis and the uncertainty over U.S. fiscal policy as key risks to their economic forecasts. A few other dealers commented that the risks to their forecasts were balanced or slightly reduced, with a couple citing positive developments in Europe as a factor.

c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 9/12/11?

Number of Dealers:

	Less Uncertain	Equally Uncertain	More Uncertain
GDP Uncertainty	5	11	4
Core PCE Uncertainty	4	13	3

10. What percent chance do you attach to the 4-quarter change in the core PCE deflator falling below zero by the end of Q4 2012?

	Probability
25th Pctl	*5%*
Median	5%
75th Pctl	*10%*

11. 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%	10%	22%	32%	22%	10%

	Point Estimate
25th Pctl	*2.00%*
Median	2.30%
75th Pctl	*2.50%*

12. 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	*5%*
Median	10%
75th Pctl	*20%*

	NBER Recession in 6 Months
25th Pctl	*25%*
Median	30%
75th Pctl	*31%*

13. Please quantify the net impact that the maturity extension program and the change in reinvestment policy announced in the September FOMC statement has had on the following yields. In your responses, the impact should be in basis points and should be estimated as the difference between the current level of yields (which includes any maturity extension and reinvestment program effects) and what the level of yields would be today if the maturity extension program and the change to the reinvestment policy had not been enacted (and was not expected to be enacted in the near term), but the financial and economic environment was otherwise identical.

(18 primary dealer complete responses)

	2-Year Treasury Yield	10-Year Treasury Yield	30-Year Treasury Yield	Current Coupon MBS Yield
		(Basis Points)		
25th Pctl	*5*	*-15*	*-26*	*-24*
Median	7	-10	-20	-15
75th Pctl	*9*	*-10*	*-15*	*-10*

(14 primary dealer comments)

Several dealers believed that the maturity extension program and the change in reinvestment policy contributed to lower long-term Treasury yields. Some dealers commented on the impact of these measures on mortgage rates. A couple of dealers considered that the actions, combined with the FOMC not lowering the rate of interest on excess reserves (IOER), also raised short-term Treasury yields. A few dealers noted the challenges of estimating the impact of the program on yields.

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

(19 primary dealer comments)

Many dealers commented that they had upgraded their forecasts of GDP growth in the second half of 2011, particularly forecasts for Q3. A few dealers mentioned that near-term recession risks had receded to some degree. However, several dealers continued to emphasize downside risks to the growth outlook. A few dealers characterized their macroeconomic assessment as largely unchanged.