Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

April 2012

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 federal funds target range or target rate following each of the next three 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)	99%	1%	0%	0%	0%	0%	0%
Three Meetings Ahead (July)	99%	1%	0%	0%	0%	0%	0%

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

Many dealers expected either no changes or very limited changes to the monetary policy section of the April FOMC statement. A few dealers expected the statement to provide more clarity on current policy measures, possibly including whether the maturity extension program (MEP) will conclude as currently scheduled.

Many expected minor changes to the economic conditions section of the statement. Several dealers expected a softer characterization of the recent improvement in economic conditions than was included in the March statement. Within this group, changes discussed included an acknowledgement of modest slowing in the pace of labor market improvement, and some renewed tensions in global financial markets. A few dealers expected an update to the statement's description of recent energy price trends.

b) Do you expect any revisions to FOMC participants' forecasts provided in the advanced materials of the Summary of Economic Projections (SEP) and, if so, what changes?

Many dealers anticipated slightly lower unemployment rate projections and slightly higher GDP growth rate projections in the near term. Some dealers noted expectations for upward revisions to headline PCE inflation projections as well. A few dealers expected 2012 projections of core PCE inflation to be revised higher. Some dealers noted the possibility that a few FOMC participants might bring forward their projections for the timing of the first increase in the federal funds target rate.

c) What additional information do you expect Chairman Bernanke to provide in his post-FOMC meeting press conference on April 25th?

While a few dealers noted no specific expectations for the Chairman's post-meeting press conference, many dealers anticipated a discussion of whether additional accommodative policy action is possible. A few of these dealers expected a discussion of what would justify further accommodation. A couple of dealers expected a discussion of what actions, from the perspective of the FOMC, would constitute a change in policy stance or even exit from

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

accommodation. Some dealers expected a discussion about the MEP. Finally, a couple of dealers expected the discussion to address labor market topics similar to those covered in recent speeches, including how recent declines in the unemployment rate are being interpreted by FOMC participants.

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

	H1 2012	H2 2012	H1 2013	H2 2013	H1 2014	H2 2014	H1 2015	H2 2015	H1 2016	≥ H2 2016
Average	0%	1%	5%	12%	19%	26%	14%	9%	8%	6%

	Most likely quarter and year of first target rate increase:
25th Pctl	*Q2 2014*
Median	Q3 2014
75th Pctl	*Q4 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 half-year period:

(20 complete primary dealer responses)

	H1 2012	H2 2012	H1 2013	H2 2013	H1 2014	H2 2014	H1 2015	H2 2015	H1 2016	H2 2016
25th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*0.94%*	*1.44%*	*2.00%*	*2.50%*
Median	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0.75%	1.25%	1.63%	2.25%	2.88%
75th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*1.00%*	*1.81%*	*2.50%*	*2.63%*	*3.63%*

5. Of the possible outcomes below, please indicate the percent chance you attach to the fed funds target rate or range one year from now and at the end of 2014:

Average:	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%
April 2013:	92%	6%	2%	0%	0%	0%	0%
Year-end 2014:	32%	27%	17%	12%	5%	4%	2%

6. How would you grade the Federal Reserve System's communication with the markets and with the public since the last policy survey on 3/5/12? Please provide a rating between 1 and 5, with 1 indicating ineffectiveness and 5 indicating effectiveness.

	Number of Respondents
1 - Very Ineffective	1
2	0
3	9
4	11
5 - Very Effective	0

Several dealers characterized recent speeches by the Chairman and other FOMC members as informative. Some dealers specifically mentioned Vice Chair Yellen's April 11 speech as improving their understanding of current policy. Conversely, some dealers noted that the wide array of public remarks made by Federal Reserve officials over the intermeeting period contributed to a general lack of clarity. Regarding specifically the thresholds for additional easing measures, a couple of dealers cited a lack of clarity while another couple noted the opposite. Finally, a few dealers noted specifically that the forward policy rate guidance in the FOMC statement remains difficult to reconcile with the interest rate forecasts of the SEP.

7. a) Recent FOMC communication has discussed several different ways monetary policy could be altered to provide either less or more accommodation. 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
Raise interest on excess reserves	*25th Pctl*	*0%*	*0%*	*15%*
	Median	0%	2%	20%
	75th Pctl	*0%*	*10%*	*35%*
Drain reserves through temporary tools	*25th Pctl*	*0%*	*5%*	*18%*
	Median	0%	5%	25%
	75th Pctl	*0%*	*22%*	*55%*
Halt reinvestments	*25th Pctl*	*0%*	*5%*	*20%*
	Median	0%	10%	30%
	75th Pctl	*0%*	*20%*	*60%*
Reduce size of SOMA portfolio through selling securities	*25th Pctl*	*0%*	*0%*	*2%*
	Median	0%	0%	5%
	75th Pctl	*0%*	*5%*	*15%*
Reduce duration of portfolio*	*25th Pctl*	*0%*	*0%*	*2%*
	Median	0%	0%	5%
	75th Pctl	*0%*	*5%*	*10%*
Change the forward guidance in the FOMC statement on the path of the federal funds rate	*25th Pctl*	*0%*	*7%*	*28%*
	Median	0%	15%	40%
	75th Pctl	*0%*	*25%*	*79%*
Provide additional guidance on the likely path for the size and composition of the balance sheet	*25th Pctl*	*0%*	*7%*	*25%*
	Median	0%	15%	35%
	75th Pctl	*0%*	*35%*	*80%*

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

(20 primary dealer comments)

Several dealers described what they viewed as the likely sequence of measures the FOMC would employ to tighten monetary policy. Of the dealers that discussed a tightening sequence, some saw a change to the forward guidance on interest rates as the first step, while a few thought that a halt to SOMA portfolio reinvestments would be the first step.

Regarding the timing of tightening, a few dealers noted that some initial steps towards tightening could take place in the 2-year horizon. Additionally, a few dealers noted that the first sales of assets from the SOMA portfolio are likely a considerable distance off into the future. Finally, a couple of dealers noted that their view on tightening did not change since the March FOMC meeting.

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
Lower interest on excess reserves	*25th Pctl*	*0%*	*5%*	*5%*
	Median	0%	5%	10%
	75th Pctl	*1%*	*10%*	*15%*
Expand SOMA portfolio through securities purchases	*25th Pctl*	*0%*	*20%*	*33%*
	Median	1%	45%	45%
	75th Pctl	*5%*	*60%*	*70%*
Increase duration of portfolio*	*25th Pctl*	*0%*	*10%*	*15%*
	Median	0%	20%	25%
	75th Pctl	*5%*	*33%*	*45%*
Change the forward guidance in the FOMC statement on the path of the federal funds rate	*25th Pctl*	*0%*	*15%*	*20%*
	Median	1%	30%	35%
	75th Pctl	*5%*	*50%*	*50%*
Provide additional guidance on the likely path for the size and composition of the balance sheet	*25th Pctl*	*1%*	*20%*	*30%*
	Median	5%	35%	40%
	75th Pctl	*10%*	*60%*	*65%*

*i.e. a deliberate action to increase the duration of the SOMA portfolio beyond the currently announced maturity extension program, independent of other policy changes.

Several dealers noted that additional easing remained possible, and a few expected such measures to be announced as early as June 2012. A few dealers noted that the overall likelihood of additional easing had declined since the last survey, and a couple noted that the next policy action would most likely be tightening.

Several dealers viewed some form of asset purchases (either sterilized or unsterilized) as the most likely policy option the FOMC would take were it to ease further. A few dealers noted the possibility for a future asset purchase program to be composed in whole or in part of agency MBS securities. A couple of dealers mentioned an extension of the current MEP as another possible easing option.

The following two questions ask about the changes to the economic outlook that would be expected to lead to either a change in the forward guidance in the FOMC statement or to additional balance sheet policy action. We measure these changes in terms of the shift in the midpoint of the central tendency projections for 2014 from the SEP. In the January SEP, the midpoints of the central tendency projection ranges for 2014 PCE inflation and Q4 2014 average unemployment were 1.8% and 7.15%, respectively.

8. **The March FOMC Minutes stated "the Committee's forward guidance is conditional on economic developments, and members concurred that the date given in the statement would be subject to revision in response to significant changes in the economic outlook."**

a) Holding the 2014 inflation projection listed above constant, in your view how much would the Q4 2014 unemployment projection listed above have to change for the Committee to shorten the forward guidance's timeframe? Similarly, how much would the Q4 2014 unemployment projection have to change for the Committee to lengthen the forward guidance's timeframe? Assume that this unemployment projection would appear in the SEP before the end of 2012. Please ensure that your signs are correct.

Change to Q4 2014 Average Unemployment Rate Central Tendency Projection

Shorten Guidance				Lengthen Guidance		
75th Pctl	Median	*25th Pctl*	Midpoint from SEP	*25th Pctl*	Median	*75th Pctl*
-0.65%	-0.50%	*-0.40%*	7.15%	*+0.30%*	+0.50%	*+0.55%*

b) Holding the Q4 2014 average unemployment rate projection listed above constant, in your view how much would the 2014 inflation projection listed above have to change for the Committee to shorten the forward guidance's timeframe? Similarly, how much would the 2014 inflation projection have to change for the Committee to lengthen the forward guidance's timeframe? Assume that this inflation projection would appear in the SEP before the end of 2012. Please ensure that your signs are correct.

Change to 2014 PCE Inflation Central Tendency Projection

Lengthen Guidance				Shorten Guidance		
75th Pctl	Median	*25th Pctl*	Midpoint from SEP	*25th Pctl*	Median	*75th Pctl*
-0.50%	-0.40%	*-0.30%*	1.80%	*+0.40%*	+0.50%	*+0.75%*

(20 primary dealer comments)

Some dealers commented that thresholds for shortening the forward guidance are higher than for lengthening the forward guidance. Some further indicated that, for a variety of reasons, the FOMC may be more sensitive to a higher unemployment rate outlook relative to a higher inflation rate outlook.

9. In the January post-meeting press conference, Chairman Bernanke stated that expanding the Federal Reserve's balance sheet would be considered if progress toward full employment was "inadequate" or if inflation remained "exceptionally low."

a) Holding the 2014 inflation projection listed above constant, in your view how much would the Q4 2014 unemployment projection listed above have to change to prompt additional accommodative balance sheet policy action before the end of 2012? Assume that this unemployment projection would appear in the SEP before the end of 2012. Please ensure that your signs are correct.

	Change to Q4 2014 Average Unemployment Rate Central Tendency Projection
25th Pctl	*+0.25%*
Median	+0.35%
75th Pctl	*+0.60%*

b) Holding the Q4 2014 average unemployment rate projection listed above constant, in your view how much would the 2014 inflation projection listed above have to change to prompt additional accommodative balance sheet policy action before the end of 2012? Assume that this inflation projection would appear in the SEP before the end of 2012. Please ensure that your signs are correct.

	Change to 2014 PCE Inflation Central Tendency Projection
25th Pctl	*-0.25%*
Median	-0.30%
75th Pctl	*-0.50%*

(20 primary dealer comments)

Several dealers noted that factors other than changes in inflation and/or unemployment rate projections might influence FOMC easing decisions. For instance, some dealers suggested that a tightening in global financial conditions or deterioration in the global economic outlook might prompt additional easing.

A few dealers indicated that a significant risk of deflation would likely prompt additional balance sheet easing. A few dealers noted that policy decisions would more likely be driven by near-term forecasts rather than medium-term forecasts. Some dealers discussed the relative merits of changing the forward rate guidance vs. expanding the Federal Reserve’s balance sheet.

10. a and b) Provide your firm's estimate of the most likely outcome (i.e. the mode) for output, inflation and unemployment. 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 complete primary dealer responses)

		Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q4/Q4 2012*	Q4/Q4 2013*	Q4/Q4 2014*
	25th Pctl	*2.10%*	*2.00%*	*2.10%*	*2.30%*	*2.20%*	*2.10%*	*2.75%*
GDP	Median	2.50%	2.20%	2.50%	2.50%	2.30%	2.50%	3.00%
	75th Pctl	*2.60%*	*2.40%*	*2.70%*	*2.80%*	*2.50%*	*2.70%*	*3.00%*
	25th Pctl	*1.90%*	*1.70%*	*1.60%*	*1.70%*	*1.70%*	*1.50%*	*1.80%*
Core PCE	Median	1.90%	1.80%	1.70%	1.80%	1.80%	1.70%	1.90%
	75th Pctl	*1.90%*	*1.90%*	*1.90%*	*1.90%*	*1.90%*	*2.00%*	*2.10%*
	25th Pctl	*2.30%*	*1.80%*	*1.80%*	*1.90%*	*1.90%*	*1.70%*	*2.00%*
Headline PCE	Median	2.30%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
	75th Pctl	*2.30%*	*2.10%*	*2.10%*	*2.20%*	*2.20%*	*2.00%*	*2.20%*
	25th Pctl					*7.90%*	*7.30%*	*6.50%*
Unemployment Rate	Median					8.00%	7.60%	7.00%
	75th Pctl					*8.20%*	*8.00%*	*7.60%*

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

2012 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	3	13	5
Core PCE	0	14	7
Headline PCE	0	11	10
Unemployment Rate	5	14	2

2013 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	6	12	3
Core PCE	1	14	6
Headline PCE	2	11	8
Unemployment Rate	6	11	4

2014 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	1	11	1
Core PCE	1	9	3
Headline PCE	2	8	3
Unemployment Rate	2	10	1

(17 primary dealer comments)

Many dealers noted potential downside risks to their GDP forecasts; the most frequently cited concerns included the risk of fiscal tightening in the U.S. and the sovereign and banking crisis in Europe. Some cited potentially higher energy prices as creating additional downside risks. A couple noted that a potential re-entry of workers into the labor force may push the unemployment rate higher.

Some dealers commented on upside risks to their GDP forecasts. A few viewed the U.S. fiscal outlook as a source of upside risk if the "fiscal cliff" in 2013 is reduced or eliminated. A couple noted the potential for a stronger-than-expected housing sector or labor market recovery as an additional source of upside risk to growth forecasts.

Finally, a couple of dealers noted that higher oil prices could lead to upside inflation risks.

c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 3/5/12?

Number of Dealers:

	Less Uncertain	Equally Uncertain	More Uncertain
GDP Uncertainty	3	16	2
Core PCE Uncertainty	1	17	3

11. What percent chance do you attach to the 4-quarter change in the core PCE deflator falling below zero by the end of Q2 2013?

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

12. For the outcomes below, please indicate the percent chance you attach to the annual average CPI inflation rate from 2017 - 2022. 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%	23%	32%	21%	10%

	Point Estimate
25th Pctl	*2.00%*
Median	2.25%
75th Pctl	*2.50%*

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

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

	NBER Recession in 6 Months
25th Pctl	*15%*
Median	15%
75th Pctl	*20%*

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

(17 primary dealer comments)

Most of the dealers who provided comments noted that they had not made any significant changes to their macroeconomic assessment. However, several dealers indicated that they had upgraded their Q1 2012 GDP growth estimates on account of incoming U.S. economic data. A couple of these dealers noted that they continue to assess the impact of unseasonably warm weather on the U.S. data.