Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

June 2014

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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] Brief summaries of the comments received in free response form are also provided.

Responses were received from 22 primary dealers. Except where noted, all 22 dealers responded to each question. In some cases, dealers may not have provided forecasts extending to the same time horizon as requested in the survey. In these instances, the number of respondents who answered all parts of the question is indicated.

Monetary Policy Expectations

1. a) Provide below your expectations for changes, if any, to the language referencing each of the following topics in the June FOMC statement. Limit your responses to changes you consider most likely.

Current economic conditions and the economic outlook:

Many dealers expected the June FOMC statement to acknowledge a modest improvement in economic activity, mainly driven by improvements in the labor market and business investment data. Several dealers expected the statement to note downside risks caused by weakness in the housing sector.

Communication on the overall size, pace, and composition of asset purchases, and factors influencing them:

All of the dealers expected the statement to announce a reduction in the pace of asset purchases by $10 billion.

Communication on the expected path of policy rates and forward guidance on the target federal funds rate:

Most dealers noted their expectation for no change in the forward guidance on the target federal funds rate.

Other: *(5 responses)*

Dealers did not provide substantial commentary in this section.

b) What are your expectations for the release of FOMC participants' economic projections in the advance materials of the Summary of Economic Projections (SEP)?

Most dealers expected FOMC participants to lower their projections for 2014 real GDP growth, mainly due to the weaker-than-expected growth in Q1. Many dealers expected a decline in the Q4 2014 unemployment rate projections due to recent labor data releases. Some dealers also expected a slight increase in inflation projections.

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

c) **What are your expectations for the release of FOMC participants' year-end target federal funds rate projections in the advance materials of the Summary of Economic Projections (SEP)?**

Some dealers expressed the view that no changes would be made to FOMC participants' target federal funds rate projections. Several dealers expected central measures of the year-end projections could decline, while several others anticipated that they could be modestly higher relative to March. Several dealers expected a decline in projections for the longer run federal funds rate, citing the view that potential GDP growth had declined. Several dealers noted that the addition of new FOMC participants at the June meeting added some uncertainty around their expectations for movement in the target rate projections.

d) **What are your expectations for the Chair's post-FOMC press conference?**

Many dealers expected Chair Yellen to discuss details of the FOMC's policy normalization strategy. Several dealers expected the Chair to focus on continued weakness in the labor market and emphasize the appropriateness of the current accommodative policy stance.

e) **Taken together, how do you expect the June FOMC events to influence market perceptions of the stance of monetary policy, if at all? (1 = less accommodative, 3 = neutral, 5 = more accommodative)**

Perceived Stance of Monetary Policy	
25th Pctl	2
Median	3
75th Pctl	3

Please explain:

Some dealers expressed an expectation for the June FOMC statement to be perceived as less accommodative by the market, while several dealers expected no change in market perceptions.

2. **What announced purchase pace, effective following the upcoming FOMC meeting, do you believe would result in roughly no change in the price of the 10-year Treasury note, assuming no other policy action?**

Monthly Pace Resulting in No Change in 10-year Treasury Yield	Treasuries	Agency MBS
25th Pctl	20	15
Median	20	15
75th Pctl	20	15

3. a) **Of the possible outcomes below, provide the percent chance you attach to the timing of the first target federal funds rate increase. Also, provide your estimate for the most likely quarter and year of the first target rate increase.**

	2014 H1	2014 H2	2015 H1	2015 H2	2016 H1	2016 H2	2017 H1	2017 H2	≥2018 H1
Average	0%	4%	28%	34%	21%	8%	3%	2%	2%

	Most Likely Quarter and Year of First Target Rate Increase
25th Pctl	Q2 2015
Median	Q3 2015
75th Pctl	Q4 2015

b) Provide your estimate of the most likely outcome (i.e., the mode) for the target federal funds rate or range at the end of each period below. In addition, provide your estimate of the longer run target federal funds rate and your expectation for the average federal funds rate over the next 10 years.

	2014 H1	2014 H2	2015 H1	2015 H2	2016 H1	2016 H2	2017 H1	2017 H2	2018 H1	Longer Run	10-yr Average FF Rate
25th Pctl	0-.25%	0-.25%	0-.25%	0.50%	1.06%	2.00%	2.56%	3.06%	3.31%	3.50%	2.62%
Median	0-.25%	0-.25%	0-.25%	0.63%	1.25%	2.13%	3.00%	3.50%	3.50%	3.50%	2.76%
75th Pctl	0-.25%	0-.25%	0.25%	1.00%	1.75%	2.44%	3.25%	3.88%	4.00%	4.00%	3.10%

If you changed your expectations for questions 3a) and/or 3b) since the last time the questions were asked, explain the factors that motivated you to make the change(s):

(18 responses)

Several dealers noted that they made no material changes relative to the last survey.

If you changed your expectations for the longer run federal funds rate over the past year, explain the factors that motivated you to make the change(s):

(14 responses)

Some dealers noted their expectation for a lower longer run federal funds rate as being driven by their perception of lower potential GDP growth. Several dealers noted that they made no changes to their estimates.

4. Of the possible outcomes below, provide the percent chance you attach to the 10-year Treasury yield falling in each of the following ranges at the end of 2014 and 2015.

Year End 2014

	≤2.00%	2.01 - 2.50%	2.51 - 3.00%	3.01 - 3.50%	3.51 - 4.00%	4.01 - 4.50%	> 4.50%
Average	4%	16%	33%	32%	11%	4%	2%

Year End 2015

	≤2.50%	2.51 - 3.00%	3.01 - 3.50%	3.51 - 4.00%	4.01 - 4.50%	4.51 - 5.00%	> 5.00%
Average	7%	14%	27%	29%	14%	8%	2%

If you changed your expectations for question 4 since the last time the question was asked on March 10, explain the factors that motivated you to make the change(s).

(19 responses)

Several dealers noted reach-for-yield behavior as contributing to a lowering of their expectations for Treasury yields, while several others noted the current low level of yields as leading them to revise down their expectations for year-end levels. Additionally, several dealers noted a lower perceived federal funds rate over the medium- to longer-term, as well as lower longer run GDP growth, as contributing to lower yield forecasts.

5. a) Provide the percent chance you attach to the unemployment rate falling within the following ranges at the time of the first increase in the target federal funds rate.

	< 5.5%	5.5 - 5.9%	6.0 - 6.5%	> 6.5%
Average	23%	49%	25%	3%

b) Provide the percent chance you attach to inflation between 1 and 2 years ahead falling within the following ranges at the time of the first increase in the target federal funds rate.

	< 1.25%	1.25 - 1.74%	1.75 - 2.24%	2.25 - 2.74%	≥ 2.75%
Average	3%	16%	49%	26%	6%

c) Provide your estimate for the most likely value of the following indicators at the time of the first increase in the target federal funds rate. When specifying values below, where appropriate, provide your estimate consistent with the last published value prior to the announcement of liftoff. For reference, the level of total U.S. employees on nonfarm payrolls for April, seasonally adjusted, was 138.3 million. For your calculations, please take into account the May data to be released on June 6.

(20 complete responses)

	Unemployment Rate	Labor Force Participation Rate	Total NFP*	12-Month Change in Average Hourly Earnings	Headline 12-Month PCE Inflation	Inflation Between 1 and 2 Years Ahead
25th Pctl	5.6%	62.8%	141.0	2.5%	1.7%	1.9%
Median	5.8%	63.0%	141.3	2.6%	1.9%	2.1%
75th Pctl	5.9%	63.1%	142.0	3.0%	2.0%	2.3%

**In millions*

d) **The minutes of the April FOMC meeting stated that Federal Reserve staff presented several approaches to raising and controlling the level of short term interest rates against the backdrop of a large balance sheet. The minutes also stated that, "the approaches differed in terms of the combination of policy tools that might be used to accomplish those objectives."**

Provide your forecast for the most likely levels of the following indicators immediately following liftoff in the target federal funds rate. If you do not believe a particular tool will be used in the context of monetary policy normalization, please enter "N/A". If you expect a target range, please enter the range. If you expect the Term Deposit Facility and Term Treasury RRP Rates will be used in normalization, please specify the term that you believe will be most heavily used and provide the expected rate for that term.

(16 complete responses)*

Administered Rates and Policy Tools

	Target Federal Funds Rate	Rate of Interest on Excess Reserves	O/N RRP Rate	Term Deposit Facility Rate	Term Deposit Facility Term (Days)	Term Treasury RRP Rate	Term Treasury RRP Term (Days)
25th Pctl	0.25%	0.25%	0.20%	0.30%	7	0.29%	7
Median	0.38%	0.50%	0.28%	0.45%	7	0.39%	7
75th Pctl	0.50%	0.50%	0.45%	0.60%	29	0.45%	12

Market Rates

	Federal Funds Effective Rate	Overnight Treasury GCF Repo Rate	4-Week T-Bill Rate	3-Month LIBOR Rate
25th Pctl	0.25%	0.25%	0.16%	0.38%
Median	0.38%	0.40%	0.35%	0.58%
75th Pctl	0.51%	0.46%	0.40%	0.70%

Federal Reserve Balance Sheet

	Expected Usage of O/N RRP ($ billions)	Expected Usage of Term RRPs and TDF ($ billions)
25th Pctl	300	175
Median	400	200
75th Pctl	800	500

**For dealers that submitted ranges, midpoints of the ranges are used. Complete responses only include responses that were specific numbers or ranges.*

Please further detail your expectations for the Committee's approach to monetary policy normalization and the combination of policy tools that might be used to accomplish those objectives.

(21 responses)

Several dealers expressed the expectation that a mix of tools would be used in the policy normalization process. Specifically, several dealers put particular emphasis on the use of the O/N RRP rate and the IOER rate. Several dealers did not expect TDF and term RRP operations to be significant components of the exit strategy. Additionally, several dealers noted that the federal funds rate may be deemphasized in importance as a policy rate due to the diminished size of the federal funds market relative to the pre-crisis period.

6. a) **Since December 31, 2013, the 5-year nominal Treasury yield 5 years forward has declined by nearly 90 basis points. Please rate the importance of the factors below in explaining these moves. (5 = very important, 1 = not important)**

Factors Explaining Decline in the 5y/5y Forward (Number of Respondents)

	Downgrade to Longer Term U.S. Economic Growth Outlook	Downgrade to Longer Term U.S. Inflation Outlook	Decline in Expected Level of Long-Run Real Federal Funds Rate	Reduced Uncertainty Around U.S. Economic and/or Policy Outlook	Change in Economic and/or Policy Outlook in Other Advanced Foreign Economies	U.S. Dollar Reserve Accumulation	Market-Related Factors (e.g., Portfolio Reallocation, positioning, safe haven flows)	Other
1 - Not Important	4	7	0	8	0	2	1	2
2	5	7	4	4	5	11	3	0
3	5	2	5	8	6	6	6	1
4	4	4	6	2	4	3	6	1
5 - Very Important	4	2	7	0	7	0	6	0

If "Other", please explain:

(2 responses)

Dealers did not provide substantial commentary in this section.

b) **Since September of 2013, implied volatility has declined across equity, foreign exchange, and long term interest rate markets, achieving or approaching historically low levels. Please rate the importance of the factors below in explaining these moves. (5 = very important, 1 = not important)**

Factors Explaining Decline in Implied Volatility (Number of Respondents)

	Reduced Uncertainty Around Global Economic Outlook	Reduced Uncertainty Around Global Central Bank Reaction Functions	Low Levels of Realized Volatility	Investor Reach-For-Yield Behavior	Other
1 - Not Important	3	2	1	0	1
2	6	3	1	2	0
3	10	7	5	4	0
4	3	8	5	7	2
5 - Very Important	0	2	10	9	2

If "Other", please explain:

(5 responses)

Dealers did not provide substantial commentary in this section.

7. a) **Provide your estimate for the most likely monthly pace of purchases that will be in effect after each of the below FOMC meetings.**

Monthly Pace of Longer-Term Security Purchases ($ billions)

			Treasuries	Agency MBS
2014	June 17-18:	25th Pctl	20	15
		Median	20	15
		75th Pctl	20	15
	July 29-30:	25th Pctl	15	10
		Median	15	10
		75th Pctl	15	10
	September 16-17:	25th Pctl	10	5
		Median	10	5
		75th Pctl	10	5
	October 28-29:	25th Pctl	0	0
		Median	0	0
		75th Pctl	0	0
	December 16-17:	25th Pctl	0	0
		Median	0	0
		75th Pctl	0	0
2015	January 27-28:	25th Pctl	0	0
		Median	0	0
		75th Pctl	0	0
	March 2015:	25th Pctl	0	0
		Median	0	0
		75th Pctl	0	0
	April 2015:	25th Pctl	0	0
		Median	0	0
		75th Pctl	0	0
	June 2015:	25th Pctl	0	0
		Median	0	0
		75th Pctl	0	0

Please explain any changes to your expectations for the increments of pace reduction and/or any changes in the expected composition of Treasury and agency MBS purchases since the last survey on April 22:

(13 responses)

Some dealers noted that they did not change their forecasts for the expected path of asset purchases.

b) **Provide the percent chance you attach to a reduction in asset purchase pace being announced at the June FOMC meeting.**

	Percent Chance of Reduction
25th Pctl	99%
Median	99%
75th Pctl	100%

c) **Provide your expectation for the most likely change in the amount of domestic securities held in the SOMA portfolio during each of the periods below. In the case of purchases, include settled and unsettled amounts.**[2]

(21 complete responses)

		2014 H2	2015 H1	2015 H2	2016 H1	2016 H2	2017 CY*
		($ billions)					
Change in the estimated amount of Treasuries:	25th Pctl portfolio	60	0	0	-140	-73	-197
	Median portfolio	60	0	0	-60	-107	-187
	75th Pctl portfolio	60	0	0	0	-96	-109
Change in the estimated amount of agency debt and MBS:	25th Pctl portfolio	40	0	-46	-102	-82	-130
	Median portfolio	40	0	0	-70	-70	-150
	75th Pctl portfolio	40	0	0	-40	-50	-139

**Calendar Year*

d) **Provide your estimate of the most likely quarter and year during which the FOMC will first cease reinvesting some or all payments of principal on Treasuries and/or agency debt and MBS. In addition, please provide your expectation for the timing, in months, relative to the first increase in the target rate. If you do not expect the FOMC to cease reinvestments for either or both asset classes during the process of policy normalization, please leave the fields blank. Please ensure your signs are correct.**

(21 complete responses)

Most Likely Quarter and Year of End to Reinvestments

	Treasuries*	Agency Debt and MBS
25th Pctl	Q2 2015**	Q2 2015
Median	Q1 2016	Q1 2016
75th Pctl	Q1 2016***	Q1 2016

**Two dealers expect no end to reinvestments of Treasury securities*
***Median falls between Q2 and Q3*
****Median falls between Q1 and Q2*

Number of Months Relative to Liftoff*

	Treasuries	Agency Debt and MBS
25th Pctl	-3	-3
Median	3	1
75th Pctl	7	6

**Negative values signify reinvestments ending prior to liftoff*

Please explain your assumptions for the timing, size, and pace of redemptions and sales of securities, if applicable. Please also explain the factors behind any change in your expectations since the last survey on April 22:

(20 responses)

Some dealers noted that they expected reinvestments to end following liftoff. Several of these dealers cited FRBNY President Dudley's recent speech on May 20th as causing them to push back their expected timing relative to the April survey. Additionally, several dealers expect reinvestments to end at the same time as liftoff. Some dealers expressed the view that there will be no outright sales of securities.

[2] Respondents provided their expected change in the SOMA portfolio of Treasuries and agency debt and MBS at each time horizon. The data is constructed by creating a portfolio level for each respondent at each time horizon based upon their responses. The 25th percentile, median, and 75th percentile portfolio level are then sampled at each time horizon. The data represent the changes in these portfolios at each time horizon.

8. **Of the possible outcomes below, indicate the percent chance you attach to the SOMA portfolio level falling in each of the following ranges at year-end 2014 and year-end 2015. For your reference, the level of the SOMA portfolio including inflation accretion and settled and unsettled agency MBS according to the January 2, 2014 H.4.1 was $3,814 billion.**

Year-end 2014

	<3500	**3500-3750**	**3750-4000**	**4000-4250**	**4250-4500**	**4500-4750**	**4750-5000**	**>5000**
Average	0%	0%	4%	32%	58%	5%	1%	1%

Year-end 2015

	<3500	**3500-3750**	**3750-4000**	**4000-4250**	**4250-4500**	**4500-4750**	**4750-5000**	**>5000**
Average	0%	2%	10%	40%	40%	5%	1%	1%

9. Provide your estimate of the most likely outcome for output, inflation, and unemployment.

(16 complete responses)

		Q4/Q4 2014	Q4/Q4 2015	Q4/Q4 2016	Longer Run
GDP:	25th Pctl	2.00%	2.70%	2.70%	2.11%
	Median	2.15%	3.00%	3.00%	2.25%
	75th Pctl	2.48%	3.10%	3.00%	2.48%
Core PCE:	25th Pctl	1.50%	1.70%	1.90%	
	Median	1.60%	1.85%	2.00%	
	75th Pctl	1.68%	1.98%	2.20%	
Headline PCE:	25th Pctl	1.60%	1.70%	1.98%	2.00%
	Median	1.70%	1.85%	2.10%	2.00%
	75th Pctl	1.88%	1.98%	2.20%	2.00%
Unemployment Rate*:	25th Pctl	6.00%	5.40%	5.30%	5.50%
	Median	6.10%	5.60%	5.50%	5.50%
	75th Pctl	6.10%	5.70%	5.70%	5.80%

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

If you have changed your expectations for longer run economic variables (e.g., GDP growth, inflation rate, unemployment rate) over the past year, explain the factors that motivated you to make the change(s).

(9 responses)

Several dealers noted a decline in their longer run GDP and unemployment rate forecasts over the past year, citing perceived changes in the outlook for labor force participation.

10. For the outcomes below, provide the percent chance you attach to the annual average CPI inflation rate from 2019 - 2024. Please also provide your point estimate for the most likely outcome.

	≤1.0%	1.01-1.5%	1.51-2.0%	2.01-2.5%	2.51-3.0%	≥3.01%
Average	3%	10%	24%	34%	19%	9%

	Most Likely Outcome
25th Pctl	2.16%
Median	2.28%
75th Pctl	2.38%

11. 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	1%
Median	5%
75th Pctl	5%

	NBER Recession in 6 Months
25th Pctl	5%
Median	10%
75th Pctl	14%