Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

March 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 (March)	98%	2%	0%	0%	0%	0%	0%
Two Meetings Ahead (April)	98%	2%	0%	0%	0%	0%	0%
Three Meetings Ahead (June)	96%	3%	1%	0%	0%	0%	0%

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

Most dealers expected the March 2011 FOMC statement to include an upgrade to the Committee's assessment of economic conditions; some within this group expected the statement to acknowledge an improvement in the labor market in particular. Several dealers referenced inflation and/or commodities prices in their comments. While some referred to rising prices as a source of downside risk to growth, there were a few who viewed this as a positive development, lowering the risk of deflation. Many dealers expected the policy language in the statement to remain unchanged. Only a couple of dealers expected no changes to any part of the statement.

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

	Q1 2011	Q2 2011	Q3 2011	Q4 2011	Q1 2012	Q2 2012	Q3 2012	Q4 2012	≥ Q1 2013
Average	0%	1%	3%	13%	16%	18%	18%	16%	16%

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

	Most likely quarter and year of first target rate increase:
25th Pctl	*Q1 2012*
Median	Q3 2012
75th Pctl	*Q3 2012*

3. 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:

	Q1 2011	Q2 2011	Q3 2011	Q4 2011	Q1 2012	Q2 2012	Q3 2012	Q4 2012
25th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.41%*	*0.50%*
Median	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0.19%	0.63%	0.88%
75th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*0.75%*	*1.25%*	*1.56%*

4. 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	57%	21%	16%	4%	1%	0%	0%

5. If you have changed your federal funds forecasts from the prior survey, what were the main drivers of that change? Please note in particular how these changes relate to your economic forecasts, FOMC communications, or other factors.

(17 primary dealer comments)

Many dealers had not changed their federal funds forecasts since the time of last policy survey. However, a few indicated that their probability distributions had shifted; specifically, this group of dealers attached a higher probability to an initial rate hike occurring earlier. Only a couple of dealers had made official changes to their federal funds forecasts; these dealers moved up their expected dates of initial policy tightening by two quarters, citing the improved employment situation as a factor behind their updated expectations.

6. How would you grade the Federal Reserve System's communication with the markets and with the public since the last policy survey on 1/18/11? Please provide a rating between 1 and 5, with 1 indicating ineffectiveness and 5 indicating effectiveness.

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

(19 primary dealer comments)

Several dealers characterized the Federal Reserve System's communication with the markets and public as clear or consistent at the time of the March 2011 survey. A few dealers commented that the Fed's communication had improved since the time of the prior survey. A few dealers described policymakers' assessments of incoming data as clear or consistent. Some dealers mentioned the disparity of views voiced by various FOMC participants as a source of confusion on policy. Some dealers cited a lack of clarity regarding the communication of balance sheet policy.

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.

(20 complete primary dealer responses)

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

Several dealers expected the asset purchase program to be completed by the second quarter of 2011, as initially announced by the FOMC in November 2010. Only a few dealers expected a later finish date sometime in the third quarter. Several dealers mentioned the idea of tapering purchases in their comments. Some viewed tapering as possible, but unlikely; a few dealers thought it was somewhat likely. Tapering was considered unlikely for a variety of reasons: a few dealers mentioned a lack of signal from Fed communication and a few noted an improvement in incoming data.

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?

		2011	2012	2013	2014	2015
	25th Pctl	*2475*	*2178*	*1650*	*1200*	*1050*
Estimated amount of domestic securities	*Median*	2636	2250	1785	1475	1300
	75th Pctl	*2650*	*2425*	*2175*	*1875*	*1550*

In describing their expectations for the amount of domestic securities held outright in the SOMA portfolio over the next five years, most dealers noted their expectations for an eventual tightening of policy over this time horizon. In particular, most dealers noted that the SOMA portfolio was likely to shrink in size over the next five years, though there were mixed views about how this would be accomplished. Many dealers mentioned halting reinvestments as a likely option, while several specifically mentioned asset sales. Some dealers commented that they expected reinvestments to be halted in advance of asset sales. A few dealers expressed the view that a contraction in the size of the portfolio was not necessary for policy to be tightened. A couple indicated that they expected short-term interest rate increases to occur in advance of any reductions in the size of the portfolio.

9. The size of the SOMA portfolio can be influenced by several factors, including asset purchases, changes to the reinvestment strategy, and asset sales. Please indicate the likelihood of these outcomes over the next two and five years. Specifically, please indicate the percent chance you assign to: 1) the Federal Reserve expanding its securities portfolio through additional purchases in the given asset class, 2) the Federal Reserve halting the reinvestment of principal payments from its holdings of the given asset class, and 3) the Federal Reserve conducting sales of the given asset class. For each, please indicate the cumulative probabilities over horizons of within two years and within five years.

		Additional Purchases		***Halting Reinvestment***		***Sales***	
		Probability within 2 years	***Probability within 5 years***	***Probability within 2 years***	***Probability within 5 years***	***Probability within 2 years***	***Probability within 5 years***
	25th Pctl	*N/A*	*N/A*	*29%*	*79%*	*15%*	*48%*
Treasuries	Median	N/A	N/A	73%	90%	23%	65%
	75th Pctl	*N/A*	*N/A*	*86%*	*99%*	*63%*	*86%*
	25th Pctl	*0%*	*0%*	*75%*	*90%*	*5%*	*16%*
Agencies	Median	4%	5%	85%	97%	18%	43%
	75th Pctl	*10%*	*15%*	*96%*	*100%*	*26%*	*65%*
	25th Pctl	*5%*	*5%*	*75%*	*90%*	*14%*	*34%*
MBS	Median	9%	10%	90%	99%	20%	50%
	75th Pctl	*21%*	*23%*	*96%*	*100%*	*45%*	*80%*

Several dealers viewed asset sales as a likely outcome within 5 years, but there were conflicting views regarding the expected composition of these sales. Several dealers noted that the FOMC would prefer to let assets run off rather than sell them. If the FOMC were to commit to further purchases, a couple of dealers viewed purchases of Treasuries as most likely; another couple of dealers commented that purchases would most likely consist of Agency debt and/or Agency MBS securities.

10. 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.

		Q1 2011	Q2 2011	Q3 2011	Q4 2011	Q4/Q4 2011	Q4/Q4 2012	Q4/Q4 2013
	25th Pctl	*3.18%*	*3.00%*	*3.18%*	*3.15%*	*3.38%*	*2.98%*	*3.30%*
GDP	Median	3.45%	3.55%	3.50%	3.50%	3.50%	3.30%	3.45%
	75th Pctl	*3.73%*	*4.00%*	*3.83%*	*4.00%*	*3.73%*	*3.63%*	*3.88%*
	25th Pctl	*0.80%*	*0.80%*	*0.90%*	*1.00%*	*1.00%*	*1.28%*	*1.63%*
Core PCE	Median	0.90%	0.95%	1.10%	1.25%	1.25%	1.55%	1.95%
	75th Pctl	*0.90%*	*1.03%*	*1.20%*	*1.40%*	*1.40%*	*2.03%*	*2.38%*
	25th Pctl					*8.50%*	*7.48%*	*6.60%*
Unemployment Rate*	Median					8.60%	7.85%	7.00%
	75th Pctl					*8.65%*	*8.20%*	*7.55%*

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

(10 complete primary dealer responses)

2011 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	4	13	3
Core PCE	0	12	8
Unemployment Rate	8	9	3

2012 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	3	13	4
Core PCE	0	11	9
Unemployment Rate	6	12	2

2013 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	2	7	1
Core PCE	0	4	6
Unemployment Rate	2	7	1

(15 primary dealer comments)

Several dealers commented on various sources of downside risk to GDP growth: several cited continued increases in commodities prices, a few mentioned the U.S. fiscal outlook, a couple referred to the European debt crisis, and a couple cited the U.S. housing market. Upside risks to growth were noted by only a few dealers. Some dealers commented on upside risks to their inflation forecasts; a few mentioned continued increases in commodities prices as posing upside risk in particular. A couple of dealers mentioned downside risks to unemployment.

c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 1/18/11?

	Number of Dealers:		
	Less Uncertain	**Equally Uncertain**	**More Uncertain**
GDP Uncertainty	2	10	8
Core PCE Uncertainty	3	7	10

11. 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	*5%*
Median	7%
75th Pctl	*11%*

12. 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	5%	12%	24%	32%	18%	9%

	Point Estimate
25th Pctl	*2.15%*
Median	2.30%
75th Pctl	*2.50%*

13. 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		NBER Recession in 6 Months
25th Pctl	*0%*	*25th Pctl*	*5%*
Median	1%	Median	10%
75th Pctl	*3%*	*75th Pctl*	*15%*

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

(14 primary dealer comments)

Some dealers commented on revisions they had made to their macroeconomic forecasts since the time of the last policy survey. While a few dealers reported downward revisions to GDP growth forecasts in one or more quarters, a couple within this group also raised projections for growth in later quarters. A couple of dealers lowered their unemployment rate forecasts since the last survey in response to incoming labor market data. Another couple mentioned that they took limited signal from the recent declines in the unemployment rate. A couple of dealers noted they made upward revisions to their inflation forecasts. A few dealers noted that their forecasts were not significantly changed from those made at the time of the last FOMC meeting.