Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

August 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 (August)	100%	0%	0%	0%	0%	0%	0%
Two Meetings Ahead (September)	99%	0%	0%	0%	0%	0%	0%
Three Meetings Ahead (November)	99%	1%	0%	0%	0%	0%	0%

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

Many dealers expected that the August statement would contain a downgrade to the characterization of economic conditions, and a few expected the statement to contain reference to the benchmark revisions to GDP and its impact on the outlook for economic growth. A couple of dealers expected that the statement would reference the moderation in headline inflation. The announcement of additional policy action to lengthen the duration of the SOMA portfolio was expected by a couple of dealers, as was some indication of the Committee's willingness to ease policy. Some dealers did not expect any substantial changes to the statement.

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

	Q3 2011	**Q4 2011**	**Q1 2012**	**Q2 2012**	**Q3 2012**	**Q4 2012**	**Q1 2013**	**Q2 2013**	**≥ Q3 2013**
Average	0%	2%	5%	12%	14%	18%	18%	13%	18%

	Most likely quarter and year of first target rate increase:
25th Pctl	*Q3 2012*
Median	Q4 2012
75th Pctl	*Q1 2013*

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

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:**

(17 complete primary dealer responses)

	Q3 2011	**Q4 2011**	**Q1 2012**	**Q2 2012**	**Q3 2012**	**Q4 2012**	**Q1 2013**	**Q2 2013**
25th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*0.75%*
Median	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0.50%	0.50%	1.00%
75th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*1.00%*	*1.25%*	*1.75%*

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	66%	20%	11%	3%	1%	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 6/13/11? Please provide a rating between 1 and 5, with 1 indicating ineffectiveness and 5 indicating effectiveness.**

	Number of Respondents
1 - Very Ineffective	0
2	2
3	1
4	12
5 - Very Effective	4

(18 primary dealer comments)

Some dealers viewed Federal Reserve communications on the whole as portraying a consistent message and several others viewed the Chairman's public appearances over the intermeeting period in a positive light. A few others viewed the two days of Chairman Bernanke's monetary policy testimony as inconsistent, sending conflicting signals as to the prospects for further easing. A few dealers also viewed the diversity of comments issued by various Federal Reserve officials in their public remarks as confusing. A couple of dealers noted that they would like additional clarity on thresholds for further easing, and a couple of others stated that there was ongoing uncertainty as to the goals and success of the current LSAP program. Finally, a couple of dealers welcomed the adoption of the FOMC's new communications guidelines.

7. What are your expectations for the amount of domestic securities held outright in the SOMA portfolio and for the expected level of excess reserves at year-end for each of the next five years? For your reference, the current level of U.S. Treasuries in SOMA is $1,634 billion, the current level of agency debt and MBS is $1,018 billion and the current level of reserves is $1,625 billion according to the latest H.4.1 release.

(17 complete primary dealer responses)

		2011	**2012**	**2013**	**2014**	**2015**
				($ Billions)		
	25th Pctl	*1666*	*1558*	*1352*	*1200*	*1003*
Estimated amount of Treasuries	Median	1700	1680	1504	1315	1218
	75th Pctl	*1750*	*1878*	*1715*	*1495*	*1373*
	25th Pctl	*904*	*696*	*485*	*250*	*83*
Estimated amount of agency debt and MBS	Median	943	750	527	292	100
	75th Pctl	*964*	*799*	*620*	*420*	*220*
	25th Pctl	*2643*	*2303*	*1854*	*1458*	*1226*
Estimated amount of domestic assets in SOMA	Median	2650	2440	2032	1650	1400
	75th Pctl	*2650*	*2593*	*2264*	*1836*	*1535*
	25th Pctl	*1563*	*1063*	*572*	*300*	*25*
Estimated level of reserves	Median	1625	1357	890	380	150
	75th Pctl	*1651*	*1520*	*1070*	*700*	*400*

(18 primary dealer comments)

Some dealers viewed a halting of reinvestments as the first step in the exit sequence, while a few dealers expecting Agency debt redemptions to occur prior to Treasury redemptions. Some dealers noted that asset sales would start sometime after the halting of reinvestments, while some others expected the portfolio to remain constant for some amount of time before shrinking. A few dealers noted that the exit sequence they envisioned would reflect the guidance issued in the June FOMC meeting minutes. A couple of dealers expected that draining of excess reserves would occur following the halting of reinvestments, while a couple of others noted that they expected the Supplementary Financing Program to return.

8. 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 within the next 1 and 2 years. Please comment.

		Probability within 1 year	Probability within 2 years
Raise interest on excess reserves	*25th Pctl*	*10%*	*66%*
	Median	25%	75%
	75th Pctl	*50%*	*88%*
Drain reserves through temporary tools	*25th Pctl*	*18%*	*70%*
	Median	37%	75%
	75th Pctl	*50%*	*93%*
Halt reinvestments	*25th Pctl*	*29%*	*75%*
	Median	50%	80%
	75th Pctl	*60%*	*93%*
Reduce size of SOMA portfolio through selling securities	*25th Pctl*	*5%*	*25%*
	Median	5%	50%
	75th Pctl	*17%*	*60%*
Reduce duration of portfolio*	*25th Pctl*	*5%*	*8%*
	Median	10%	25%
	75th Pctl	*10%*	*30%*
Change guidance on the period over which the target rate will remain in effect	*25th Pctl*	*18%*	*70%*
	Median	37%	80%
	75th Pctl	*63%*	*95%*

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

(13 primary dealer comments)

A couple of dealers noted that they had pushed back their estimates of the timing of eventual tightening over the intermeeting period. A few other dealers expected the sequence of tightening to reflect the guidance announced in previous FOMC communications. A few dealers also commented in detail on the specifics of their expectations for the exit sequence.

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

		Probability within 1 year	Probability within 2 years
Lower interest on excess reserves	*25th Pctl*	*5%*	*8%*
	Median	10%	10%
	75th Pctl	*28%*	*33%*
Expand SOMA portfolio through security purchases	*25th Pctl*	*15%*	*19%*
	Median	20%	25%
	75th Pctl	*25%*	*30%*
Increase duration of portfolio*	*25th Pctl*	*5%*	*8%*
	Median	20%	25%
	75th Pctl	*30%*	*45%*
Change the forward guidance on the path of the federal funds rate	*25th Pctl*	*10%*	*14%*
	Median	20%	25%
	75th Pctl	*40%*	*43%*
Provide guidance on the period over which the SOMA portfolio will remain at the current level	*25th Pctl*	*15%*	*17%*
	Median	20%	25%
	75th Pctl	*40%*	*40%*

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

(15 primary dealer comments)

A couple of dealers commented that the probabilities they assigned to additional easing had increased over the intermeeting period. A couple of dealers regarded the bar for further easing as high, while a couple of others commented that an additional round of asset purchases would be too risky considering current levels of inflation. A couple of dealers commented that more than one easing measure may need to be taken at the same time.

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

(13 complete primary dealer responses)

		Q2 2011	Q3 2011	Q4 2011	Q1 2012	Q4/Q4 2011	Q4/Q4 2012	Q4/Q4 2013
	25th Pctl	*1.30%*	*2.50%*	*2.60%*	*2.15%*	*1.65%*	*2.70%*	*2.70%*
GDP	Median	1.30%	2.50%	3.00%	2.50%	1.80%	2.90%	3.00%
	75th Pctl	*1.30%*	*3.05%*	*3.33%*	*2.95%*	*2.00%*	*3.05%*	*3.10%*
	25th Pctl	*1.20%*	*1.45%*	*1.60%*	*1.55%*	*1.60%*	*1.45%*	*1.60%*
Core PCE	Median	1.30%	1.50%	1.70%	1.80%	1.70%	1.80%	1.80%
	75th Pctl	*1.30%*	*1.60%*	*1.90%*	*1.95%*	*1.90%*	*1.95%*	*2.00%*
	25th Pctl	*2.50%*	*2.60%*	*2.55%*	*2.00%*	*2.55%*	*1.60%*	*1.70%*
Headline PCE	Median	2.50%	2.70%	2.70%	2.10%	2.70%	1.90%	2.00%
	75th Pctl	*2.50%*	*2.85%*	*2.90%*	*2.30%*	*2.90%*	*2.30%*	*2.30%*
	25th Pctl					*8.80%*	*8.20%*	*7.40%*
Unemployment Rate*	Median					8.90%	8.30%	7.70%
	75th Pctl					*9.00%*	*8.50%*	*8.00%*

*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.

2011 Forecasts

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	10	9	0
Core PCE	0	14	4
Headline PCE	2	13	3
Unemployment Rate	1	7	11

2012 Forecasts

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	13	5	1
Core PCE	4	8	6
Headline PCE	0	14	4
Unemployment Rate	1	6	12

2013 Forecasts

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	6	7	0
Core PCE	1	11	1
Headline PCE	2	9	2
Unemployment Rate	0	8	5

(15 primary dealer comments)

Many dealers discussed risks to the economic outlook. Some dealers noted downside risk from fiscal policy decisions, while a couple dealers specifically cited the failure to extend the payroll tax cut and expiration of stimulus measures as upcoming risks. A few dealers noted that recent benchmark revisions to GDP, which showed a deeper downturn and a weaker recovery, suggested greater downside risk to their growth forecasts. A few dealers mentioned that softer incoming data reinforced this view.

c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 6/13/11?

	Number of Dealers:		
	Less Uncertain	**Equally Uncertain**	**More Uncertain**
GDP Uncertainty	1	6	12
Core PCE Uncertainty	5	11	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 Q3 2012?

	Probability
25th Pctl	*4%*
Median	5%
75th Pctl	*8%*

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	5%	11%	23%	30%	21%	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		NBER Recession in 6 Months
25th Pctl	*5%*	*25th Pctl*	*15%*
Median	10%	Median	20%
75th Pctl	*15%*	*75th Pctl*	*25%*

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

Several dealers mentioned that they had lowered or were in the process of lowering their GDP growth forecasts. A few dealers noted that their forecast changes were consistent with the recent benchmark revisions to GDP. A few dealers also commented that their revised outlook had impacted their expectations for the timing of the first increase in the target federal funds rate. A couple of dealers noted making upward revisions to their inflation forecasts in response to higher-than-expected realized inflation.