Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

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

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

Several dealers suggested the FOMC would acknowledge some improvement in U.S. economic data since the release of the November statement, with some expecting an upgrade in the Committee's assessment of labor market conditions. While most dealers did not expect any policy changes at the December meeting, some suggested the FOMC could change its communication strategy, and a few saw a change in the guidance on the future path of the federal funds rate as likely. Several dealers suggested that changes in FOMC communication could come at a later meeting, with a few mentioning January as a possibility. Additionally, a couple dealers expected that a request for a cut to the discount rate could be initiated by a Reserve Bank and approved by the Board.

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

	Q4 2011	**Q1 2012**	**Q2 2012**	**Q3 2012**	**Q4 2012**	**Q1 2013**	**Q2 2013**	**Q3 2013**	**Q4 2013**	**Q1 2014**	**≥ Q2 2014**
Average	0%	0%	0%	1%	2%	3%	7%	14%	12%	15%	45%

	Most likely quarter and year of first target rate increase:
25th Pctl	*Q4 2013*
Median	Q2 2014
75th Pctl	*Q3 2014*

[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:

	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-.25%*	*0.50%*	*0.75%*

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	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 10/24/2011? Please provide a rating between 1 and 5, with 1 indicating ineffectiveness and 5 indicating effectiveness. Please explain.

	Number of Respondents
1 - Very Ineffective	0
2	2
3	10
4	8
5 - Very Effective	1

Many dealers viewed FOMC communication over the intermeeting period as clear and effective. However, several others were more critical, with some indicating that their grade was reflective of disparate messages coming from Federal Reserve officials' public communications. Additionally, some respondents mentioned confusion around the discussion of potential changes to the Fed's communication policy. A few dealers highlighted Chairman Bernanke's press conferences as helpful.

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%*	*10%*
	Median	0%	1%	10%
	75th Pctl	*0%*	*4%*	*35%*
Drain reserves through temporary tools	*25th Pctl*	*0%*	*0%*	*11%*
	Median	0%	5%	25%
	75th Pctl	*0%*	*10%*	*50%*
Halt reinvestments	*25th Pctl*	*0%*	*1%*	*10%*
	Median	0%	8%	30%
	75th Pctl	*0%*	*15%*	*75%*
Reduce size of SOMA portfolio through selling securities	*25th Pctl*	*0%*	*0%*	*2%*
	Median	0%	0%	5%
	75th Pctl	*0%*	*4%*	*20%*
Reduce duration of portfolio	*25th Pctl*	*0%*	*0%*	*3%*
	Median	0%	0%	5%
	75th Pctl	*0%*	*5%*	*20%*
Change guidance on the period over which the target rate will remain in effect	*25th Pctl*	*0%*	*1%*	*15%*
	Median	0%	10%	30%
	75th Pctl	*0%*	*20%*	*50%*

(19 primary dealer comments)

Several dealers highlighted their expectations that there would be no policy tightening within the next two years. Some explained that their relatively higher probabilities over the 2-year horizon for halting reinvestments, changing guidance on the target rate, and draining reserves reflected the likelihood that such steps will precede any rate increase, even if such a move is not expected to occur within 2 years. A few dealers noted that the anticipated timing of any securities sales remains far off.

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%*	*10%*
	Median	2%	10%	10%
	75th Pctl	*5%*	*20%*	*20%*
Expand SOMA portfolio through security purchases	*25th Pctl*	*0%*	*40%*	*45%*
	Median	5%	60%	60%
	75th Pctl	*5%*	*65%*	*70%*
Increase duration of portfolio	*25th Pctl*	*0%*	*5%*	*10%*
	Median	0%	10%	10%
	75th Pctl	*1%*	*20%*	*26%*
Change the forward guidance on the path of the federal funds rate	*25th Pctl*	*10%*	*65%*	*75%*
	Median	20%	80%	85%
	75th Pctl	*40%*	*90%*	*90%*
Provide guidance on the period over which the SOMA portfolio will remain at the current level	*25th Pctl*	*5%*	*35%*	*40%*
	Median	15%	40%	50%
	75th Pctl	*25%*	*50%*	*60%*

(20 primary dealer comments)

Many respondents commented on the possible form that a change in forward guidance on the path of the federal funds rate might take. The following options were mentioned: including federal funds target rate forecasts in the FOMC's Summary of Economic Projections, conditioning the federal funds target rate on economic thresholds, and extending the mid-2013 language into the future. Regarding potential SOMA expansion and duration increases, several dealers stated expectations that these operations would likely be carried out using agency MBS. In accordance with the similarity in probabilities at the one year to two year horizons, some specifically mentioned that if further easing were to occur, it would occur within one year.

8. The November FOMC minutes stated that meeting participants discussed potential approaches for enhancing the clarity of their public communications. Please indicate the probability you attach to each of the below changes in public communications occurring within the next 1 year. Additionally, if the Committee were to make the below change, please describe what changes would be made. Please explain.

		Probability Within 1 Year
Provide more information on policy objectives (such as a longer-run inflation goal)	*25th Pctl*	*60%*
	Median	75%
	75th Pctl	*85%*
Provide information about participants' assessment of appropriate monetary policy in the Summary of Economic Projections	*25th Pctl*	*60%*
	Median	75%
	75th Pctl	*80%*

Many respondents expect that additional information on policy objectives will come in the form of an explicit inflation objective. Most of these dealers also commented that the inflation target would likely be accompanied by an explicit unemployment forecast or further guidance on the FOMC's goals for this aspect of the Federal Reserve's mandate. A couple of dealers commented that the central tendency forecasts already provide sufficient information on the FOMC's goals for inflation and unemployment.

With regards to the Summary of Economic Projections, many respondents cited the publishing of a federal funds rate forecast as one possible change. A few dealers also highlighted the possibility of including thresholds for inflation and unemployment at which a federal funds target change would take place.

Some respondents cited the potential risk of outlining explicit targets or expectations for inflation, unemployment or the federal funds rate. These respondents mainly focused on the constraints that explicit goals may put on policy makers.

Economic Indicator Forecasts

9. 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.

(19 complete primary dealer responses)

		Q4 2011	Q1 2012	Q2 2012	Q3 2012	Q4/Q4 2011*	Q4/Q4 2012*	Q4/Q4 2013*
	25th Pctl	*2.50%*	*1.30%*	*1.50%*	*1.70%*	*1.60%*	*1.60%*	*1.95%*
GDP	Median	2.80%	1.70%	2.00%	2.20%	1.60%	2.10%	2.50%
	75th Pctl	*3.00%*	*2.20%*	*2.20%*	*2.50%*	*1.70%*	*2.30%*	*2.73%*
	25th Pctl	*1.70%*	*1.70%*	*1.50%*	*1.40%*	*1.70%*	*1.43%*	*1.50%*
Core PCE	Median	1.80%	1.80%	1.70%	1.60%	1.80%	1.70%	1.70%
	75th Pctl	*1.80%*	*1.90%*	*1.80%*	*1.80%*	*1.80%*	*2.00%*	*1.93%*
	25th Pctl	*2.54%*	*1.80%*	*1.30%*	*1.20%*	*2.54%*	*1.20%*	*1.60%*
Headline PCE	Median	2.60%	2.10%	1.70%	1.60%	2.60%	1.70%	1.79%
	75th Pctl	*2.70%*	*2.30%*	*1.90%*	*2.10%*	*2.70%*	*2.40%*	*2.13%*
	25th Pctl					*8.8%*	*8.6%*	*8.0%*
Unemployment Rate*	Median					8.9%	8.7%	8.3%
	75th Pctl					*9.0%*	*8.9%*	*8.8%*

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

2011 Forecasts
Number of Respondents

	Downside Risk	Balanced Risk	Upside Risk
GDP	0	17	3
Core PCE	1	19	0
Headline PCE	2	18	0
Unemployment Rate	5	14	2

2012 Forecasts
Number of Respondents

	Downside Risk	Balanced Risk	Upside Risk
GDP	10	9	2
Core PCE	3	14	3
Headline PCE	3	11	6
Unemployment Rate	5	8	7

2013 Forecasts
Number of Respondents

	Downside Risk	Balanced Risk	Upside Risk
GDP	7	11	1
Core PCE	4	13	2
Headline PCE	4	13	2
Unemployment Rate	3	12	4

(20 primary dealer comments)

Most respondents cited the eurozone sovereign debt and banking situation as a major source of downside risk to their forecasts. Many also mentioned uncertainty concerning the U.S. fiscal situation. A couple of dealers cited fluctuations in the labor force participation rate as a source of uncertainty in their unemployment forecasts.

c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 10/24/11?

Number of Dealers

	Less Uncertain	Equally Uncertain	More Uncertain
GDP Uncertainty	2	11	8
Core PCE Uncertainty	2	19	0

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%	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)?

	Recession currently
25th Pctl	*5%*
Median	10%
75th Pctl	*10%*

	Recession in 6 months
25th Pctl	*20%*
Median	25%
75th Pctl	*30%*

13. We are interested in understanding the degree to which the European fiscal and banking situation has weighed on your U.S. GDP forecast. If a fully convincing resolution to the European situation was announced in a timely manner, what would be the change to your 2012 U.S. GDP forecast? Please ensure that your sign is correct. Please explain, including what would be the key elements of a fully convincing resolution.

(20 complete primary dealer responses)

	Effect of European Solution on 2012 GDP
25th Pctl	*0.25%*
Median	0.50%
75th Pctl	*0.75%*

Many respondents commented that stronger fiscal integration of member countries would be a necessary component of a resolution to the euro area crisis. Several dealers mentioned fiscal austerity measures as necessary, while a couple of dealers specifically mentioned the need for a eurobond as part of a fiscal framework. Several also mentioned that a legitimate enforcement method for any centralized fiscal policies would be necessary. Some also cited the need for the ECB to provide a stronger backstop to European sovereign debt, with some suggesting that the ECB would need to purchase securities as part of a quantitative easing program.

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

Many dealers noted upgrades to their 2011 growth forecasts, with some pointing to recent improving data releases as supporting these revisions. Several respondents, however, noted that changes to their outlook from the time of the November survey were fairly minimal. A few respondents highlighted headwinds to growth due to the European sovereign debt crisis, while a few others pointed to U.S. fiscal developments as affecting their forecasts.