Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

September 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 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 (September)	100%	0%	0%	0%	0%	0%	0%
Two Meetings Ahead (October)	100%	0%	0%	0%	0%	0%	0%
Three Meetings Ahead (December)	100%	0%	0%	0%	0%	0%	0%

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

A few dealers expected that the forecasts in the summary of economic conditions could be upgraded in some fashion, with a couple of dealers indicating that it could note improvement in the labor market. In contrast, a few dealers expected that the summary would be downgraded, and some dealers expected it would be little changed.

Most dealers expected some sort of easing to be announced in the September FOMC statement. Most dealers expected that the forward guidance on the path of the federal funds rate would be extended into 2015. Several dealers specified that the guidance to be extended to "mid-2015" and a couple of dealers expected that the forward guidance could be extended past mid-2015.

Some dealers noted that the announcement of an asset purchase program was possible, with a few dealers noting the possibility of open-ended purchases.

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

Most dealers expected a downward revision to at least one aspect of the advance materials of the September SEP. Several dealers expected the 2012 GDP forecast to be revised downward. Some dealers expected the same for 2013, though a couple of dealers noted that uncertainty over U.S. fiscal policy would delay significant downward revisions to 2013 GDP forecasts for now. Some dealers expected that unemployment forecasts would be revised higher, and some dealers expected the timing of policy rate firming to be pushed further into the future. A few dealers expected that near-term headline inflation forecasts would be revised higher, with a couple citing the drought as the driver of the revisions.

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

c) Please explain how your expectations for the economy or Federal Reserve policy have changed following the Jackson Hole Economic Policy Symposium, if at all.

Many dealers noted that Chairman Bernanke's comments at the Jackson Hole Economic Policy Symposium supported or reinforced their expectations for the economy or for monetary policy. Some dealers noted that while the remarks indicated that additional accommodation is likely in the near-term, the timing remains somewhat uncertain. A few dealers noted that the Chairman's remarks indicated that the FOMC is likely to announce additional accommodation at the September FOMC meeting.

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

	H2 2012	**H1 2013**	**H2 2013**	**H1 2014**	**H2 2014**	**H1 2015**	**H2 2015**	**H1 2016**	**H2 2016**	**≥ H1 2017**
Average	0%	1%	4%	9%	16%	21%	24%	12%	6%	6%

	Most likely quarter and year of first target rate increase:
25th Pctl	*Q2 2015*
Median	Q3 2015
75th Pctl	*Q3 2015*

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:

	H2 2012	**H1 2013**	**H2 2013**	**H1 2014**	**H2 2014**	**H1 2015**	**H2 2015**	**H1 2016**	**H2 2016**	**H1 2017**	**Longer Run**
25th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.50%*	*1.00%*	*1.50%*	*2.00%*	*3.75%*
Median	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	1.00%	1.75%	2.00%	3.00%	4.00%
75th Pctl	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0-.25%*	*0.75%*	*1.25%*	*2.00%*	*2.75%*	*3.50%*	*4.00%*

5. Of the possible outcomes below, please indicate the percent chance you attach to the federal funds target rate or range 1 year from now and at the end of 2014:

	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%**
September 2013 Average:	94%	5%	1%	0%	0%	0%	0%
Year-end 2014 Average:	63%	18%	11%	5%	2%	1%	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 7/23/12? 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	0
3	8
4	11
5 - Very Effective	2

Some dealers held an overall positive view of FOMC communication since the last meeting. In particular, a few dealers felt the Chairman's remarks at the Jackson Hole Economic Policy Symposium were clear and consistent with other forms of communication during the intermeeting period. A few dealers noted that the minutes of the August FOMC meeting were clear or informative.

A few dealers indicated that recent communication has raised expectations for some form of additional easing at the September FOMC meeting.

Some dealers felt that the various views expressed by Committee members have resulted in some ambiguity or confusion regarding potential policy actions. A few dealers said that the communication regarding what appropriate policy should be has not been clear.

7. FOMC communications have 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 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
Raise interest on excess reserves	*25th Pctl*	*0%*	*0%*	*10%*
	Median	0%	1%	15%
	75th Pctl	*0%*	*5%*	*25%*
Drain reserves through temporary tools	*25th Pctl*	*0%*	*3%*	*15%*
	Median	0%	5%	20%
	75th Pctl	*0%*	*5%*	*50%*
Halt reinvestments	*25th Pctl*	*0%*	*5%*	*20%*
	Median	0%	5%	25%
	75th Pctl	*0%*	*10%*	*50%*
Reduce size of SOMA portfolio through selling securities	*25th Pctl*	*0%*	*0%*	*0%*
	Median	0%	0%	5%
	75th Pctl	*0%*	*1%*	*10%*
Reduce duration of portfolio*	*25th Pctl*	*0%*	*0%*	*0%*
	Median	0%	0%	3%
	75th Pctl	*0%*	*1%*	*10%*
Change the forward guidance in the FOMC statement on the path of the federal funds rate	*25th Pctl*	*0%*	*0%*	*20%*
	Median	0%	5%	30%
	75th Pctl	*0%*	*10%*	*50%*
Provide additional guidance on the likely path for the size and composition of the balance sheet	*25th Pctl*	*0%*	*0%*	*20%*
	Median	0%	5%	30%
	75th Pctl	*0%*	*15%*	*55%*

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

(17 primary dealer comments)

Dealers generally regarded the likelihood of any type of policy tightening within two years as unlikely, and some dealers noted that outright sales of assets from the SOMA portfolio would likely not occur for some time after tightening begins. Regarding the sequence of tools the FOMC may employ to tighten policy, some dealers noted that changing the forward guidance, halting reinvestment of maturing securities, and the draining of some quantity of excess reserves would likely precede the first increase to the federal funds target rate. A couple of dealers noted that the FOMC would probably raise the rate of interest paid on excess reserves (IOER) after these steps.

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*	*5%*	*10%*	*15%*
	Median	15%	25%	25%
	75th Pctl	*20%*	*30%*	*35%*
Expand SOMA portfolio through securities purchases	*25th Pctl*	*40%*	*60%*	*65%*
	Median	55%	70%	75%
	75th Pctl	*60%*	*80%*	*85%*
Increase duration of portfolio*	*25th Pctl*	*0%*	*5%*	*5%*
	Median	5%	5%	10%
	75th Pctl	*10%*	*20%*	*25%*
Change the forward guidance in the FOMC statement on the path of the federal funds rate	*25th Pctl*	*70%*	*75%*	*75%*
	Median	75%	85%	90%
	75th Pctl	*85%*	*95%*	*95%*
Provide additional guidance on the likely path for the size and composition of the balance sheet	*25th Pctl*	*13%*	*30%*	*35%*
	Median	25%	45%	50%
	75th Pctl	*50%*	*70%*	*75%*
Introduce new tools to promote more accommodative financial conditions	*25th Pctl*	*5%*	*25%*	*30%*
	Median	*10%*	30%	35%
	75th Pctl	*25%*	*45%*	*50%*

*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.

(20 primary dealer comments)

Many dealers expected some form of easing to be announced at the September FOMC meeting. Several dealers expected the forward guidance on the path of the federal funds rate to be extended, while some dealers expected asset purchases to be announced and a couple of dealers noted that open-ended purchases were possible. A couple of dealers felt that the outcome of the September FOMC meeting would be heavily dependent on the employment situation report for August. A few dealers did not expect any asset purchases to be announced at the September FOMC meeting.

Separately, several dealers expected that the FOMC would pursue some easing measures at the September meeting, followed by further easing in the near future and as soon as the December meeting. A few of these dealers specified that the FOMC would extend the forward rate guidance at the September meeting and announce additional asset purchases at the December meeting.

A few dealers viewed a cut to IOER in upcoming meeting as possible, though a couple of them noted that the benefits would be minimal.

Please describe what new tools might be introduced:

(19 primary dealer comments)

Some dealers noted the FOMC could undertake some form of targeted lending to small businesses and households. Some dealers noted a directed lending program might be similar to the funding-for-lending program announced by the Bank of England. A couple of dealers also pointed out legal or practical complications to pursuing lending programs that have been discussed in public so far. A few dealers suggested the FOMC could announce some sort of target for inflation and the unemployment rate.

c) Because respondents could see some of the choices from part b as overlapping, the answers to that part do not necessarily reveal the combined probability of various choices. Please indicate the probability that the FOMC will add any type of policy accommodation, including any of the actions listed in part b above. Please indicate the probability that any of these tools will be used at the next FOMC meeting and within the next 1 and 2 years.

		Probability at next FOMC meeting	Probability within 1 year	Probability within 2 years
	25th Pctl	*70%*	*80%*	*90%*
Add any type of policy accommodation	Median	80%	90%	90%
	75th Pctl	*90%*	*95%*	*95%*

(18 primary dealer comments)

Some dealers felt that the probability of any form of easing had increased since the time of the prior survey, and a few of these dealers noted that recent FOMC communication had contributed to this view. Several dealers noted that, if the FOMC were to pursue additional easing, such an announcement would at least include an extension of the forward guidance. A couple of dealers noted specifically that the FOMC would add further accommodation unless employment data clearly improved.

8. Please provide your most likely expectation (i.e., the mode) for the amount of domestic securities held outright in the SOMA portfolio and for the expected level of reserves at year-end for each of the next five years. Please explain.

(20 complete primary dealer responses)

		2012	2013	2014	2015	2016
				$Billions		
	25th Pctl	1640	1663	1663	1660	1495
	Median	1663	1899	1850	1795	1650
Estimated amount of Treasuries	*75th Pctl*	1744	1960	1989	1953	1778
	25th Pctl	931	1081	1044	888	700
Estimated amount of agency debt and MBS	*Median*	1000	1200	1181	1058	878
	75th Pctl	1044	1250	1335	1275	1087
	25th Pctl	2600	2902	2809	2662	2196
Estimated amount of domestic assets in SOMA	*Median*	2724	3070	3000	2835	2461
	75th Pctl	2795	3170	3170	3103	2795
	25th Pctl	1529	1759	1642	1238	741
	Median	1605	1936	1841	1581	1066
Estimated level of reserves	*75th Pctl*	1715	2020	1944	1829	1419

Many dealers expected that the SOMA portfolio would expand to some extent over the coming years. Several dealers noted expectations for SOMA-expanding securities purchases to extend through 2013, and several noted expectations that such purchases would include both U.S. Treasury securities and agency MBS. A couple of dealers expected purchases to only include agency MBS. Some dealers expected that such purchases could be open-ended, and a few dealers expected that such asset purchases would be dependent on economic data.

Regarding expectations for policy tightening, some dealers noted a halting of reinvestments and outright sales of securities from the SOMA portfolio beginning in 2015 or later. A few noted that large-scale reserve-draining operations would begin at some point in 2015. A couple of dealers noted that some form of tightening will commence in 2014.

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.

(12 complete primary dealer responses)

		Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q4/Q4 2012*	Q4/Q4 2013*	Q4/Q4 2014*	Q4/Q4 2015*	Long Run
GDP	*25th Pctl*	*1.50%*	*1.40%*	*1.00%*	*2.00%*	*1.60%*	*1.90%*	*2.35%*	*2.50%*	*2.25%*
	Median	1.80%	1.80%	1.50%	2.10%	1.80%	2.20%	2.55%	2.75%	2.38%
	75th Pctl	*2.00%*	*2.00%*	*2.10%*	*2.30%*	*1.90%*	*2.30%*	*2.88%*	*3.20%*	*2.50%*
Core PCE	*25th Pctl*	*1.70%*	*1.70%*	*1.60%*	*1.60%*	*1.70%*	*1.70%*	*1.80%*	*1.78%*	
	Median	1.70%	1.80%	1.70%	1.80%	1.80%	1.80%	1.90%	1.90%	
	75th Pctl	*1.80%*	*2.00%*	*1.90%*	*1.90%*	*2.00%*	*2.00%*	*2.00%*	*2.00%*	
Headline PCE	*25th Pctl*	*1.50%*	*1.60%*	*1.50%*	*1.60%*	*1.60%*	*1.50%*	*1.68%*	*1.90%*	*2.00%*
	Median	1.60%	1.80%	1.60%	1.80%	1.80%	1.90%	2.00%	2.00%	2.00%
	75th Pctl	*1.60%*	*2.00%*	*1.80%*	*2.10%*	*2.00%*	*2.10%*	*2.10%*	*2.20%*	*2.20%*
Unemployment Rate	*25th Pctl*					*8.10%*	*7.80%*	*7.33%*	*6.90%*	*5.80%*
	Median					8.20%	7.90%	7.60%	7.00%	6.00%
	75th Pctl					*8.20%*	*8.10%*	*7.60%*	*7.10%*	*6.50%*

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

(12 complete primary dealer responses)

2012 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	8	13	0
Core PCE	6	13	2
Headline PCE	3	13	5
Unemployment Rate	10	10	1

2013 Forecasts
Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	15	6	0
Core PCE	5	15	1
Headline PCE	4	11	6
Unemployment Rate	11	9	1

2014 Forecasts

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	5	9	0
Core PCE	2	8	3
Headline PCE	1	9	4
Unemployment Rate	7	7	0

2015 Forecasts

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP	3	9	1
Core PCE	1	8	3
Headline PCE	1	9	3
Unemployment Rate	5	7	1

(20 primary dealer comments)

Most dealers noted the U.S. fiscal cliff as an important downside risk to their GDP forecast, and a few dealers noted that uncertainty over fiscal policy is already having an impact on the economy. A few dealers also cited potential fiscal policy developments as putting upward pressure on their unemployment rate forecasts.

Several dealers noted a further deterioration of European financial stresses or economic growth trajectory as another significant downside risk to their GDP forecasts, A few dealers noted further slowing of growth in emerging market nations. A couple of dealers noted impacts on household budgets from higher food prices that could potentially result from domestic droughts.

Regarding upside risks to GDP forecasts, a few dealers suggested that momentum in the housing market might continue, and that the uncertainty over fiscal policy could be resolved sooner than is currently expected.

On inflation, a few dealers cited higher food prices from the drought as an upside risk, and a couple of dealers pointed to possible upward pressure on energy prices stemming from geopolitical tensions.

c) Do you feel more, less or equally uncertain regarding your economic forecasts since the last survey on 7/23/12?

Number of Dealers:

	Less Uncertain	Equally Uncertain	More Uncertain
GDP Uncertainty	0	17	4
Core PCE Uncertainty	1	17	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 2013?

	Probability
25th Pctl	*4%*
Median	5%
75th Pctl	*10%*

11. 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%	9%	24%	33%	20%	9%

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

12. 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	*5%*
Median	5%
75th Pctl	*10%*

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

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

(18 primary dealer comments)

Some dealers indicated that they downgraded their macroeconomic assessment. Several dealers indicated no change or very slight changes to their assessment. A few dealers highlighted uncertainty related to U.S. fiscal policy.

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Updated as of September 11, 2012

Following the ECB meeting (September 6), the U.S. employment situation report (September 7), and the associated market reaction, primary dealers were asked to update their responses to parts of questions 7 and 8.

7) FOMC communications have discussed several different ways monetary policy could be altered to provide either less or more accommodation.

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.

		Probability at next FOMC meeting
Expand SOMA portfolio through securities purchases	*25th Pctl*	*55%*
	Median	65%
	75th Pctl	*75%*
Change the forward guidance in the FOMC statement on the path of the federal funds rate	*25th Pctl*	*75%*
	Median	80%
	75th Pctl	*90%*

c) Because respondents could see some of the choices from part b as overlapping, the answers to that part do not necessarily reveal the combined probability of various choices. Please indicate the probability that the FOMC will add any type of policy accommodation, including any of the actions listed in part b above. Please indicate the probability that any of these tools will be used at the next FOMC meeting.

		Probability at next FOMC meeting
Add any type of policy accommodation	*25th Pctl*	*75%*
	Median	90%
	75th Pctl	*95%*

8) Please provide your most likely expectation (i.e., the mode) for the amount of domestic securities held outright in the SOMA portfolio and for the expected level of reserves at year-end for each of the next five years. Please explain.[2]

		2012	2013
		$Billions	
	25th Pctl	1670	1860
	Median	1715	1940
Estimated amount of Treasuries	*75th Pctl*	1760	2000
	25th Pctl	994	1150
Estimated amount of agency debt and MBS	*Median*	1019	1225
	75th Pctl	1061	1335

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Updated as of September 19, 2012:
Following the September FOMC meeting (September 12-13), primary dealers were asked to update their responses to question number 8 – expectations for the path of the SOMA portfolio and reserves balances.

8) Please provide your most likely expectation (i.e., the mode) for the amount of domestic securities held outright in the SOMA portfolio and for the expected level of reserves at year-end for each of the next five years. Please explain.

(20 primary dealer responses)

		2012	2013	2014	2015	2016
				$Billions		
	25th Pctl	1639	1929	1900	1847	1641
	Median	1639	2048	2067	1997	1893
Estimated amount of Treasuries	*75th Pctl*	1650	2119	2205	2205	2129
	25th Pctl	1065	1391	1376	1161	817
Estimated amount of agency debt and MBS	*Median*	1074	1502	1502	1323	1123
	75th Pctl	1074	1550	1671	1583	1458
	25th Pctl	2705	3383	3283	3074	2478
Estimated amount of domestic assets in SOMA	*Median*	2713	3496	3496	3325	2996
	75th Pctl	2720	3611	3756	3696	3527
	25th Pctl	1639	2148	2106	1736	1047
	Median	1659	2399	2280	2033	1492
Estimated level of reserves	*75th Pctl*	1674	2529	2526	2322	2155

(17 primary dealer comments)

Many dealers expected Treasury and agency MBS purchases to continue after 2012. While several dealers expected that asset purchases would end during 2013, some dealers expected that purchases would extend into 2014. Some dealers noted that security purchases would taper off as the program progressed.

[2] This table has been revised since its original release.