Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

March 2013

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

Most dealers expected no major changes to be made to the FOMC statement. Several dealers did expect to see language reflecting an improvement in economic growth relative to the January statement, with some specifically expecting mention of improved labor market conditions. Some dealers also expected downside risks to growth from sequestration to be cited. Several dealers noted the statement could provide some additional information or guidance on the asset purchase program.

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

Some dealers expected no material changes to the SEP, while some expected a small downward revision to GDP due to fiscal drag from the sequestration taking effect. Several dealers expected small downward revisions to the unemployment rate in response to recent positive labor market data.

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

	H1 2013	H2 2013	H1 2014	H2 2014	H1 2015	H2 2015	H1 2016	H2 2016	H1 2017	≥ H2 2017
Average	0%	1%	5%	10%	23%	27%	18%	8%	4%	4%

	Most likely quarter and year of first target rate increase:
25th Pctl	Q2 2015
Median	Q3 2015
75th Pctl	Q4 2015

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 half-year period and over the longer run.

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

	H1 2013	H2 2013	H1 2014	H2 2014	H1 2015	H2 2015	H1 2016	H2 2016	H1 2017	H2 2017	Longer Run
25th Pctl	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0.50%	0.75%	1.50%	2.00%	2.50%	3.75%
Median	0-.25%	0-.25%	0-.25%	0-.25%	0-.25%	0.50%	1.00%	1.75%	2.50%	3.00%	4.00%
75th Pctl	0-.25%	0-.25%	0-.25%	0-.25%	0.25%	1.00%	2.00%	2.50%	3.00%	4.00%	4.00%

4. Of the possible outcomes below, please indicate the percent chance you attach to the 10-year Treasury yield falling in each of the following ranges at the end of 2013, 2014, and 2015.

		<1.00%	1.00 - 1.50%	1.51 - 2.00%	2.01 - 2.50%	2.51 - 3.00%	3.01 - 3.50%	>3.50%
Year-end 2013 :	Average	2%	10%	26%	37%	20%	5%	1%
Year-end 2014 :	Average	1%	4%	14%	22%	29%	22%	8%
Year-end 2015 :	Average	1%	3%	9%	15%	21%	30%	20%

5. In the January FOMC statement, the Committee announced it will continue purchasing additional agency mortgage-backed securities at a pace of $40 billion per month and longer-term Treasury securities at a pace of $45 billion per month, and also stated that it would take appropriate account of the likely efficacy and costs of such purchases in determining the size, pace, and composition of its asset purchases.

a) Please provide your expectation for the 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
March 19-20:	25th Pctl	45	40
	Median	45	40
	75th Pctl	45	40
April/May 30-1:	25th Pctl	45	40
	Median	45	40
	75th Pctl	45	40
June 18-19:	25th Pctl	45	40
	Median	45	40
	75th Pctl	45	40
December 17-18:	25th Pctl	25	20
	Median	35	35
	75th Pctl	45	40
1 Year ahead (March, 2014):	25th Pctl	0	0
	Median	20	0
	75th Pctl	25	25

b) Please indicate the quarter and year during which you expect flow-based purchases in Treasury and agency MBS securities to be completed.

	Most likely quarter and year of program end:
25th Pctl	Q4 2013
Median	Q1 2014
75th Pctl	Q2 2014

6. a) How would you rate market functioning in longer-term Treasury and agency MBS securities markets today relative to the worst and best conditions you have seen since the beginning of 2009? (1 = worst conditions since 2009, 5 = best conditions since 2009)

Relative Conditions Since 2009
Number of Respondents:

	1 - worst conditions	2	3	4	5 - best conditions
Treasury Market:	0	2	4	12	3
Agency MBS Market:	0	2	7	11	1

b) How has market functioning in longer-term Treasury and agency MBS securities markets changed since September 2012? (1 = significantly worse, 3 = same, 5 = significantly better)

Change in Market Functioning Since 2012
Number of Respondents:

	1 - Significantly Worse	2	3 - Same	4	5 - Significantly Better
Treasury Market:	1	1	16	3	0
Agency MBS Market:	1	8	12	0	0

Please explain, with reference to the impact of Federal Reserve asset purchases on market functioning, if applicable.

(17 primary dealer responses)

Many dealers noted that Treasury markets were generally functioning smoothly, with several stating that Treasury market functioning was relatively little changed since September of 2012. Some dealers noted that Federal Reserve asset purchases were not impairing market functioning in the Treasury market, while several specifically stated that the presence of the Federal Reserve had improved market functioning in the Treasury market since 2009.

In their written comments, dealers' views on agency MBS markets were more mixed. Several dealers noted that market functioning in the agency MBS market was not significantly changed since September 2012, while several others cited poorer liquidity or lighter flows in certain segments of the market since that time. Some dealers viewed the Federal Reserve's presence in the market as not negatively affecting liquidity, while several thought it did.

7. a) Please provide your expectation for the change in the amount of domestic securities held in the SOMA portfolio during each of the periods below. In the case of purchases, please include settled and unsettled amounts.[2]

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[2] Respondents provided their expected change in the SOMA portfolio of Treasuries and agency debt and MBS at each time horizon. The above 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 above data represent the changes in these portfolios at each time horizon.

		2013 Q3	2013 Q4	2014 H1	2014 H2	2015 H1	2015 H2	2016 H1	2016 H2	2017 H1
						$Billions				
Change in the estimated amount of Treasuries:	25th Pctl portfolio	135	90	45	0	0	0	-100	-100	-100
	Median portfolio	135	135	60	0	0	0	-60	-60	-85
	75th Pctl portfolio	135	135	170	10	0	0	-80	-40	-50
Change in the estimated amount of agency debt and MBS:	25th Pctl portfolio	120	85	35	0	-70	-150	-160	-160	-179
	Median portfolio	120	120	0	0	0	-71	-117	-187	-182
	75th Pctl portfolio	120	120	150	0	0	-90	-30	-60	-110

Please explain any assumptions underlying changes in the pace and/or composition of asset purchases.

Most dealers provided their views on when they expected a change in the monthly pace of securities purchases or when they expected the program to come to an end. Many expected asset purchases to continue into the first half of 2014, while several dealers saw purchases extending into the second half of 2014. There were also several dealers who expected the purchases to end in the second half of 2013. Most dealers expected a reduction in the monthly pace of asset purchases to commence at some point, with several dealers noting that they expect the monthly pace of asset purchases to be lowered more than once before the program is halted. Several dealers cited labor market improvement as an important factor in bringing about expected future reductions in the pace of purchases.

Please explain any assumptions underlying any declines in SOMA portfolio levels.

Some dealers predicted that the SOMA portfolio would begin to decline in 2015, while several mentioned 2016. Some dealers assumed that future declines in the SOMA portfolio would be due to halting reinvestments only, while some dealers assumed halting reinvestments combined with sales. Several dealers expected such declines in the SOMA portfolio to occur at a fixed time before or after the first interest rate increase. Several dealers mentioned their views were based on the June 2011 exit principles while several others mentioned the FOMC will likely review its exit strategy, citing recent communication from Federal Reserve officials.

b) Please describe your expectations for the pace and extent of sales of securities held in the SOMA portfolio, if any, during the exit from accommodative monetary policy.

Some dealers expected sales of agency MBS securities to be a part of the exit strategy from accommodative policy. Some others thought that sales are unlikely or do not expect them to occur, with several mentioning that sufficient tightening could be brought about through other tools, including raising the interest rate paid on excess reserves (IOER) as well as temporary reserve draining. Several dealers referred to the timeframe over which they expect balance sheet normalization to occur, while several also noted their view that the FOMC's exit principles could be revised in the near future.

8. Of the possible outcomes below, please indicate the percent chance you attach to the SOMA portfolio level falling in each of the following ranges at year-end 2013 and year-end 2014. For your reference, the current level of the SOMA portfolio including inflation accretion and settled and unsettled agency MBS according to the January 10 H.4.1 is $2817 billion.

	Year End 2013						
	<3000	**3000-3250**	**3250-3500**	**3500-3750**	**3750-4000**	**4000-4250**	**>4250**
Average	0%	3%	11%	33%	43%	9%	2%

	Year End 2014						
	<2500	**2500-3000**	**3000-3500**	**3500-4000**	**4000-4500**	**4500-5000**	**>5000**
Average	0%	2%	12%	45%	27%	12%	2%

9. **The January 2013 FOMC statement noted, "If the outlook for the labor market does not improve substantially, the Committee will continue its purchases of Treasury and agency mortgage-backed securities… until such improvement is achieved in a context of price stability. In determining the size, pace, and composition of its asset purchases, the Committee will… take appropriate account of the likely efficacy and costs."**

   The FOMC's December 2012 Summary of Economic Projections shows the expected central tendency for the unemployment rate at the end of 2013 falling between 7.4 and 7.7 percent. Please indicate the percent chance you attach to the dollar level of the SOMA portfolio falling within the following ranges at year-end 2014 for each of the following *hypothetical* scenarios. First, assume the unemployment rate declines to less than 7.4 percent by the end of 2013; second, assume it remains within the 7.4 to 7.7 percent range at the end of 2013; and third, assume it remains greater than 7.7 percent at the end of 2013. Please consider all possible conditions that may be associated with these scenarios in providing your responses.

		Year End 2014						
Unemployment rate at year-end 2013		**<2500**	**2500-3000**	**3000-3500**	**3500-4000**	**4000-4500**	**4500-5000**	**>5000**
Less than 7.4 percent	Average	1%	4%	21%	48%	18%	8%	1%
Between 7.4 and 7.7 percent	Average	0%	1%	10%	49%	27%	10%	4%
Greater than 7.7 percent	Average	0%	0%	4%	35%	35%	19%	6%

10. 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/Q4 2013	Q4/Q4 2014	Q4/Q4 2015	Long Run
	25th Pctl	1.80%	2.70%	3.00%	2.25%
GDP:	Median	2.10%	2.90%	3.00%	2.40%
	75th Pctl	2.50%	3.10%	3.00%	2.50%
	25th Pctl	1.50%	1.70%	1.90%	
Core PCE:	Median	1.60%	1.90%	2.00%	
	75th Pctl	1.80%	2.10%	2.03%	
	25th Pctl	1.50%	1.60%	1.98%	2.00%
Headline PCE:	Median	1.60%	2.00%	2.00%	2.00%
	75th Pctl	1.90%	2.10%	2.05%	2.20%
	25th Pctl	7.40%	6.70%	6.29%	5.80%
Unemployment Rate*:	Median	7.50%	6.90%	6.50%	6.00%
	75th Pctl	7.60%	7.00%	6.50%	6.25%

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

2013 Forecasts*

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP:	2	13	6
Core PCE:	4	17	0
Headline PCE:	2	18	1
Unemployment Rate:	1	12	8

2014 Forecasts*

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP:	4	16	1
Core PCE:	2	16	3
Headline PCE:	1	16	4
Unemployment Rate:	2	14	5

2015 Forecasts*

Number of Respondents Citing:

	Downside Risk	Balanced Risk	Upside Risk
GDP:	4	12	1
Core PCE:	0	12	4
Headline PCE:	1	11	4
Unemployment Rate:	3	13	0

**Upside risk is a risk towards higher GDP growth, a higher inflation rate, and a lower unemployment rate. Downside risk is a risk towards lower GDP growth, a lower inflation rate, and a higher unemployment rate.*

(18 primary dealer comments)

Most dealers saw fiscal tightening as the primary downside risk to their forecasts, with several others mentioning global growth concerns and Europe as additional risks. Some dealers noted housing as a source of upside risk to their forecasts, while several mentioned further strengthening in domestic demand as posing upside risk to their forecasts.

11. For the outcomes below, please indicate the percent chance you attach to the annual average CPI inflation rate from 2018 - 2023. 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	3%	9%	24%	34%	19%	10%

	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 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	3%
Median	5%
75th Pctl	10%

	NBER Recession in 6 Months
25th Pctl	15%
Median	20%
75th Pctl	25%

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

(19 primary dealer comments)

Some dealers had no material changes to their forecasts, while some dealers downgraded their forecasts based on the full implementation of sequester cuts and reduced expectations for growth relative to their previous forecasts. Several other dealers noted positive housing and economic data as leading to modest upgrades in their near term forecasts.