Responses to Survey of Primary Dealers

Markets Group, Federal Reserve Bank of New York

June 2016

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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] Brief summaries of the comments received in free response form are also provided.

Responses were received from 23 primary dealers. ***Except where noted, all 23 dealers responded to each question.*** *In some cases, dealers may not have provided forecasts extending to the same time horizon as requested in the survey. In these instances, the number of respondents who answered all parts of the question is indicated.*

Monetary Policy Expectations

1. a) Provide below your expectations for changes, if any, to the language referencing each of the following topics in the June FOMC statement.

Current economic conditions:

Many dealers expected the Committee to upgrade its current growth assessment in the June FOMC statement, with several pointing to upward revisions to estimates of U.S. economic growth in the second quarter. Most dealers also suggested that the Committee would downgrade its assessment of labor market conditions or note that employment growth had slowed. Some dealers also expected that the Committee would acknowledge a pickup in household spending in the June FOMC statement.

Economic outlook:
(22 responses)

Some dealers specifically noted expectations for few significant changes to the Committee's communication on the economic outlook in the June FOMC statement, while several dealers noted that they expected the Committee to acknowledge the recent weakening in labor market data.

Communication on the expected path of policy rates and forward guidance on the target federal funds rate:
(22 responses)

Many dealers specifically noted expectations for no significant change in the Committee's communication on the expected path of policy rates and forward guidance on the target federal funds rate in the June FOMC statement.

Communication on the Committee's policy of reinvesting principal payments on Treasury and agency securities:
(22 responses)

All dealers that submitted responses to this question expected no change in the Committee's communication on its policy of reinvesting principal payments on Treasury and agency securities.

Other:
(8 responses)

Dealers did not provide substantial commentary in this section.

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

b) What are your expectations for the medians of FOMC participants' economic projections in the Summary of Economic Projections (SEP)?

Some dealers anticipated that FOMC participants' economic projections for 2016 would be adjusted in response to recent data releases, with some dealers noting their expectation that the median of participants' forecasts for 2016 GDP growth would likely decrease, and some also suggesting that the medians of their forecasts for 2016 headline and/or core PCE inflation may increase slightly. Several dealers also noted the potential for downward revisions to participants' forecasts for the unemployment rate, while several dealers reported that they expected few significant changes to the medians of FOMC participants' economic projections in the SEP.

c) What are your expectations for the medians of FOMC participants' target federal funds rate projections in the Summary of Economic Projections (SEP)?
(22 responses)

	Federal Funds Rate			
	Year-End 2016	Year-End 2017	Year-End 2018	Longer Run
25th Pctl	0.88%	1.63%	2.75%	3.25%
Median	0.88%	1.88%	2.88%	3.25%
75th Pctl	0.88%	1.88%	2.90%	3.25%

Please explain any assumptions underlying your expectations.
(22 responses)

In explaining their responses, several dealers indicated that they expected the median of FOMC participants' projections for the target federal funds rate at year-end 2016 to be revised downward. In addition, some dealers noted their expectation that the medians of FOMC participants' rate projections would reflect a more gradual expected pace of policy normalization, with several dealers citing perceived downside risks to the outlook from recent global economic and financial market developments and several others noting the impact of an expected lower real neutral federal funds rate. Several dealers also reported that they expected few significant changes to the medians of participants' target federal funds rate projections.

d) What are your expectations for the Chair's post-FOMC conference?

Several dealers expected that the Chair would express confidence in the economic outlook while some expected her to acknowledge the recent weaker-than-expected labor market data. Additionally, several dealers expected that the Chair would continue to emphasize data dependency and to signal a gradual pace of further increases in the target range. In addition, several dealers reported that they expected the Chair to discuss the possibility of the next rate hike taking place either at the July meeting or in the coming months. Lastly, some respondents expected that the Chair would adopt a tone consistent with her speech on June 6.

2. a) Provide your estimate of the most likely outcome (i.e., the mode) for the target federal funds rate or range, as applicable, immediately following the FOMC meetings and at the end of each quarter or half-year period below. For the time periods at which you expect a target range, please indicate the midpoint of that range in providing your response.

	Target Rate / Midpoint of Target Range					
	Jun. 14-15 2016	Jul. 26-27 2016	Sep. 20-21 2016	Nov. 1-2 2016	Dec. 13-14 2016	Jan. 31 - Feb. 1 2017
25th Pctl	0.38%	0.38%	0.63%	0.63%	0.63%	0.63%
Median	0.38%	0.38%	0.63%	0.63%	0.63%	0.63%
75th Pctl	0.38%	0.63%	0.63%	0.63%	0.88%	0.88%
# of Responses	23	23	23	23	23	23

	2017 Q1	2017 Q2	2017 Q3	2017 Q4	2018 H1	2018 H2	2019 H1
25th Pctl	0.88%	0.88%	1.13%	1.13%	1.63%	1.63%	1.88%
Median	0.88%	1.13%	1.38%	1.63%	2.00%	2.13%	2.31%
75th Pctl	1.13%	1.38%	1.63%	1.88%	2.13%	2.50%	2.75%
# of Responses	23	23	23	23	21	21	20

b) In addition, provide your estimate of the longer-run target federal funds rate and your expectation for the average federal funds rate over the next 10 years.
(22 responses)

	Longer Run	10-yr Average FF Rate
25th Pctl	2.75%	2.20%
Median	3.13%	2.48%
75th Pctl	3.25%	2.75%

c) The following questions relate to your expectations for the Committee's next policy action in 2016 and some associated conditional outcomes for the year-end 2016 target federal funds rate or range. Only fill out the conditional probability distributions in parts (ii), (iii), and (iv) if you assign a non-zero probability to the conditioning event occurring.

i) Please indicate the percent chance that you attach to the following possible outcomes for the Committee's next policy action in 2016.
(22 responses)

	Next Change is Increase in Target Rate or Range	Next Change is Decrease in Target Rate or Range	No Change in Target Rate or Range in 2016
Average	65%	6%	29%

ii) Conditional on the Committee's next policy action in 2016 being an increase in the target federal funds rate or range, please indicate the percent chance that you attach to the following possible outcomes for the timing of such a change. Only fill out this conditional probability distribution if you assigned a non-zero probability to the next change in the target rate or range being an increase.
(22 responses)

	Increase Occurs at June FOMC Meeting	Increase Occurs at July FOMC Meeting	Increase Occurs at September FOMC Meeting or Later
Average	6%	34%	61%

iii) **Conditional on the Committee's next policy action in 2016 being a <u>decrease</u> in the target federal funds rate or range, please indicate the percent chance that you attach to the following possible outcomes for the timing of such a change. <u>Only fill out this conditional probability distribution if you assigned a non-zero probability to the next change in the target rate or range being a decrease</u>.**
(22 responses)

	Decrease Occurs at June FOMC meeting	Decrease Occurs at July FOMC Meeting	Decrease Occurs at September FOMC Meeting or Later
Average	1%	7%	92%

iv) **Of the possible outcomes below, please indicate the percent chance that you attach to the target federal funds rate or range falling in each of the following ranges <u>at the end of 2016</u>, conditional on the following possible scenarios for the direction and timing of the Committee's next policy action in 2016. <u>Only fill out the conditional probability distributions for which you assigned a non-zero probability to the conditioning event occurring</u>. If you expect a target range, please use the midpoint of that range in providing your response.**
(22 responses)

Next change is increase, occurs at Jul. meeting or earlier

	<0.00%	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	0%	2%	7%	76%	13%	1%	0%	0%

Next change is increase, occurs at Sep. meeting or later

	<0.00%	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	0%	2%	8%	84%	6%	0%	0%	0%

Next change is decrease

	<0.00%	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	9%	86%	5%	0%	0%	0%	0%	0%

d) i) **Of the possible outcomes below, please indicate the percent chance that you attach to the target federal funds rate or range falling in each of the following ranges <u>at the end of 2017 and 2018, conditional on not moving to the zero lower bound (ZLB) at any point during 2016-2018</u>. If you expect a target range, please use the midpoint of that range in providing your response.**
(22 responses)

Year-end 2017

	≤1.00%	1.01-1.50%	1.51-2.00%	2.01-2.50%	2.51-3.00%	3.01-3.50%	≥3.51%
Average	15%	36%	33%	12%	3%	1%	0%

Year-end 2018

	≤1.00%	1.01-1.50%	1.51-2.00%	2.01-2.50%	2.51-3.00%	3.01-3.50%	≥3.51%
Average	12%	17%	27%	20%	14%	7%	3%

ii) Please indicate the percent chance that you attach to moving to the ZLB at some point in 2016-2018.

	Probability of Moving to ZLB at Some Point in 2016-2018
25th Pctl	10%
Median	25%
75th Pctl	30%

If you placed a non-zero probability on moving to the ZLB at some point in 2016-2018 above, please indicate your estimate for the most likely <u>timing</u> of such an event.
(22 responses)

	Timing of Moving to ZLB at Some Point in 2016-2018
25th Pctl	H1 2017
Median	H2 2017
75th Pctl	H1 2018 / H2 2018

iii) Of the possible outcomes below, please indicate the percent chance that you attach to the target federal funds rate or range falling in each of the following ranges <u>at the end of 2017 and 2018</u>, <u>conditional on moving to the ZLB at some point in 2016-2018</u>. <u>Only fill out these conditional probability distributions if you assigned a non-zero probability to moving to the ZLB at some point in 2016-2018</u>. If you expect a target range, please use the midpoint of that range in providing your response.
(22 responses)

Year-end 2017

	<0.00%	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	8%	44%	14%	13%	9%	9%	3%	1%

Year-end 2018

	<0.00%	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	11%	54%	18%	9%	5%	2%	1%	1%

iv) What is your estimate of the target federal funds rate or range at the effective lower bound?
(22 responses)

	Level of Target Fed Funds Rate or Range at ELB
25th Pctl	-0.38%
Median	-0.06%
75th Pctl	0.13%

For parts a-d, please explain the factors behind any change to your expectations, where applicable, since the last policy survey.

(16 responses)

Several dealers indicated that they revised their responses to reflect a more gradual expected path of increases in the target range, which they noted was driven by weaker-than-expected recent labor market data, communication from some Committee participants, and increased uncertainty over the economic outlook.

3. **Of the possible outcomes below, please indicate the percent chance that you attach to the 10-year Treasury yield falling in each of the following ranges at the end of 2016 and 2017.**
(22 responses)

Year-end 2016

	≤1.50%	1.51-2.00%	2.01-2.50%	2.51-3.00%	3.01-3.50%	3.51-4.00%	≥4.01%
Average	14%	41%	31%	10%	3%	1%	0%

Year-end 2017

	≤1.50%	1.51-2.00%	2.01-2.50%	2.51-3.00%	3.01-3.50%	3.51-4.00%	≥4.01%
Average	10%	23%	29%	22%	11%	3%	2%

4. **In a question in the March policy survey, respondents on average rated “changes in oil and commodity prices” as one of the most important factors in explaining changes in some components of the 5-year/5-year forward breakeven rate since mid-2014. Since the April FOMC meeting, prices on oil futures have increased while measures of the 5-year/5-year forward breakeven rate have declined. Please discuss your view on whether the relationship between oil prices and the forward breakeven rate has changed recently. If so, please discuss why.**
(22 responses)

Several dealers indicated that there had been no material change in the relationship between oil prices and the forward breakeven rate, while several other dealers indicated that the relationship between oil prices and forward breakeven rates appeared less strong than it had been previously. In addition, several dealers indicated that they did not view oil prices as being structurally related to forward breakeven rates.

In explaining the recent changes in the forward breakeven rates, several dealers attributed the movements to U.S. policy expectations and/or movements in the U.S. dollar, changes in the levels of inflation risk premia, and structural changes in the economy and/or expected rates of global growth. In addition, several dealers indicated that oil prices have been driven recently by idiosyncratic or supply-side factors.

5. **What are your expectations for the ON RRP facility over the next year?**

Several dealers suggested that aggregate ON RRP demand will remain near recent ranges. Some dealers also expected increased aggregate ON RRP demand given an expected increase in demand for short-term, high-quality assets stemming from money fund reform implementation in the second half of 2016. Additionally, some dealers expected that the Committee will reduce the aggregate ON RRP cap from its current level in the future, likely sometime following money fund reform implementation in the second half of 2016.

6. **In its most recent FOMC statement, the Committee indicated that it anticipates continuing reinvestments “until normalization of the level of the federal funds rate is well under way.”**

a) **Provide your estimate for the most likely timing (in months forward) of a change to the Committee's policy on reinvesting payments of principal on Treasuries and/or agency debt and MBS. If you do not** expect the FOMC to change its policy on reinvestments for either or both asset classes during the process of policy normalization, please enter "N/A."

	Months Forward	
	Treasuries*	Agency Debt and MBS
25th Pctl	13	13
Median	18	18
75th Pctl	21	21

*Four dealers expect no end to reinvestments of Treasury securities and three dealers expect no end to reinvestments of agency debt and MBS.

b) What is your estimate for the most likely level of the target federal funds rate or range if and when the Committee first changes its reinvestment policy?
(22 responses)

	Level of Target Fed Funds Rate/Range
25th Pctl	1.13%
Median	1.25%
75th Pctl	1.63%

c) In its Policy Normalization Principles and Plans, the Committee indicated that it "expects to cease or commence phasing out reinvestments" after liftoff. Of the possible outcomes below, please indicate the percent chance that you attach to the Committee during the process of policy normalization ceasing its reinvestments all at once, phasing out its reinvestments over time, or not changing its reinvestments.

	Treasuries		
	No Change to Reinvestments	Reinvestments Ceased All at Once	Reinvestments Phased Out Over Time
Average	22%	15%	63%

	Agency Debt and MBS		
	No Change to Reinvestments	Reinvestments Ceased All at Once	Reinvestments Phased Out Over Time
Average	18%	15%	67%

d) i) <u>Conditional on not moving to the ZLB at any point in 2016-2018</u>, what is your mean expectation for the par value of the SOMA portfolio at the end of 2018? For reference, the current level of the SOMA portfolio, including inflation compensation and settled and unsettled agency MBS according to the May 25, 2016, H.4.1, was $4259 billion.*
(22 responses)

	SOMA Value at Year-end 2018 Conditional on <u>Not</u> Moving to ZLB ($ bn)
25th Pctl	3,603
Median	3,824
75th Pctl	4,000

ii) **<u>Conditional on moving to the ZLB at some point in 2016-2018</u>, what is your mean expectation for the par value of the SOMA portfolio at the end of 2018?**

	SOMA Value at Year-end 2018 Conditional on Moving to ZLB ($ bn)
25th Pctl	4,259
Median	4,550
75th Pctl	4,859

**This level references the most recent H.4.1 release at the time this survey was sent out to respondents.*

Please explain the factors behind any change to your expectations in parts a-d since the last policy survey.
(15 responses)

Several dealers specifically noted that they made few significant changes to their responses in parts a-d since the last policy survey. Several other dealers explained that they shifted out their expectation for the most likely timing of a change to the Committee's policy on reinvestments as a result of having revised later their expectations for the timing of additional rate hikes.

7. a) Provide your estimate of the most likely outcome for output, inflation, and unemployment.
(20 responses)

		Q4/Q4 2016	Q4/Q4 2017	Q4/Q4 2018	Longer Run
GDP:	25th Pctl	1.70%	1.90%	1.60%	1.75%
	Median	1.90%	2.20%	1.95%	1.95%
	75th Pctl	2.10%	2.40%	2.25%	2.20%
Core PCE Deflator:	25th Pctl	1.70%	1.80%	1.85%	
	Median	1.70%	1.90%	2.00%	
	75th Pctl	1.90%	2.10%	2.05%	
Headline PCE Deflator:	25th Pctl	1.50%	1.90%	1.95%	2.00%
	Median	1.70%	2.00%	2.00%	2.00%
	75th Pctl	1.80%	2.10%	2.20%	2.00%
Unemployment Rate*:	25th Pctl	4.60%	4.40%	4.50%	4.70%
	Median	4.70%	4.50%	4.70%	4.85%
	75th Pctl	4.80%	4.70%	4.80%	5.10%

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

8. a) For the outcomes below, provide the percent chance you attach to the annual average CPI inflation rate from June 1, 2016 - May 31, 2021. Please also provide your point estimate for the most likely outcome.
(22 responses)

	≤1.00%	1.01-1.50%	1.51-2.00%	2.01-2.50%	2.51-3.00%	≥3.01%
Average	3%	11%	33%	37%	12%	4%

Point estimate for most likely outcome:
(22 responses)

	Most Likely Outcome
25th Pctl	2.00%
Median	2.10%
75th Pctl	2.20%

b) For the outcomes below, provide the percent chance you attach to the annual average CPI inflation rate from June 1, 2021 - May 31, 2026. Please also provide your point estimate for the most likely outcome.
(22 responses)

	≤1.00%	1.01-1.50%	1.51-2.00%	2.01-2.50%	2.51-3.00%	≥3.01%
Average	3%	9%	29%	39%	15%	5%

Point estimate for most likely outcome:
(22 responses)

	Most Likely Outcome
25th Pctl	2.10%
Median	2.25%
75th Pctl	2.30%

9. a) What percent chance do you attach to the U.S. economy currently being in a recession*?
(22 responses)

b) What percent chance do you attach to the U.S. economy being in a recession* in 6 months?

c) What percent chance do you attach to the global economy being in a recession in 6 months?**
(22 responses)

	Currently in NBER Recession		NBER Recession in 6 Months		Global Recession in 6 Months
25th Pctl	5%	25th Pctl	15%	25th Pctl	15%
Median	6%	Median	15%	Median	21%
75th Pctl	15%	75th Pctl	20%	75th Pctl	30%

**NBER-defined recession*
***Previous IMF staff work has suggested that a "global recession" can be characterized as a period during which there is a decline in annual per-capita real global GDP, backed up by a decline or worsening in one or more of the following global macroeconomic indicators: industrial production, trade, capital flows, oil consumption and unemployment.*

Please explain the factors behind any change to your expectations in parts a-c since the last policy survey.
(17 responses)

Some dealers noted that their expected likelihood of a recession had increased given recent weak U.S. economic activity data, while several dealers indicated no change to their expectations since the last policy survey.