

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
DIVISION OF MONETARY AFFAIRS
FOMC SECRETARIAT

Date: October 21, 2011
To: Governors and Reserve Bank Presidents
From: Deborah J. Danker
Subject: Request for November SEP and Trial-Run Projections

Overview

As part of the upcoming policy cycle, FOMC meeting participants are requested to submit both their regular quarterly economic projections and their responses to new trial-run questions. I would like to draw your attention to several points about this round of projections:

- As usual at this point in the year, we are requesting an additional year of projections (through 2014).
- Trial-run projections of the target federal funds rate are being collected.¹
- Charts of the responses about risks and uncertainties (information which has been collected all along) will be published for the first time in the upcoming Summary of Economic Projections.²
- Attachment 2 includes a clarification regarding the treatment of answers to the question about the length of the convergence process.

Each of these points is elaborated later on in this document. Attached to this cover note is a timeline of the projections process (Attachment 1), a description of the regular projection information we are requesting (Attachment 2), an updated version

¹ The trial run was introduced in the memo, "Collecting Information on FOMC Participants' Policy Projections," sent to the FOMC on October 5, 2011.

² These new charts were discussed in the memo, "Update on Potential SEP Enhancements," sent to the FOMC on September 13, 2011.

of the usual table providing background information on forecast uncertainty (Attachment 3), and further information on the trial run (Attachment 4).

The trial run collects participants' projections for the average level of the target federal funds rate in the fourth quarter of each calendar year and over the longer run—the same reporting convention as for the unemployment rate. For those participants who expect policy firming to commence only after 2014, the trial run also requests their assessments of the most likely year of initial policy firming and their projections for real GDP growth, PCE inflation, and core PCE inflation in that year and for the average unemployment rate and the average target federal funds rate in the fourth quarter of that year. All participants are asked to describe the key factors informing their judgments regarding the appropriate path of policy. Trial-run information will be submitted separately from the regular projections; please use the SDS "Create Comment" feature to submit trial-run responses.

Logistics

In light of the tight timing associated with the Chairman's press conference, the deadlines for submission and revision of projections will again be extremely important. We will continue to use the logistical arrangements utilized for the April and June rounds. Your initial projections are due by **5:00 pm Eastern Time on Friday, October 28** (a link to the electronic collection system will be sent to users early next week). We will be following up with each of your offices to verify contact information in case there is a need to discuss or correct the projections over the weekend of October 29-30.

As in the last two rounds, any revisions to your projections will need to be received on a stepped-up schedule, and you will no longer have until the day after the meeting to revise your forecasts. Please provide us with any projection revisions as soon as you have them, but in any case by **9:00 pm on Tuesday, November 1**. If necessary, a revision could be submitted up until the end of the coffee break on the second day of the meeting—or, if it turns out that there is no coffee break, until

shortly after the meeting has ended. At that point, however, projections will be finalized and no further revisions will be possible.

For the convenience of Bank Presidents and Bank staff, connections to the System IT network will be available in the Special Library on November 2, so that any last-minute revisions could be submitted with the standard Lotus Notes application (please be sure to bring your laptop if you intend to use these connections). Alternatively, we will have paper copies of individual projections available, and participants could write in revisions, if necessary

Attachment 1

November Projections Timeline

October 21 (Friday)	Request for participants' regular and trial-run projections
October 24 (Monday)	Templates for regular and trial-run projections made available via Lotus Notes links
October 28 (Friday)	Initial regular and trial-run projections due by 5:00 pm ET
October 31 (Monday)	Initial summary projections package distributed to FOMC participants
November 1 (Tuesday)	First day of FOMC meeting. Briefings on participants' regular projections and trial-run projections. Deadline for projection revisions.
November 2 (Wed.)	Second day of FOMC meeting. <u>Absolute</u> deadline for projection revisions. Summary information on the regular projections will be released at the Chairman's press conference.
November 3 (Thurs.)	Final summary projections package distributed to FOMC participants
November 10 (Thurs.)	First draft of the minutes and Summary of Economic Projections (SEP) distributed to participants
November 15 (Tuesday)	Second draft of the minutes and SEP distributed to participants
November 17 (Thurs.)	Final version of the minutes and SEP distributed for notation vote
November 21 (Monday)	Voting on minutes and SEP closes at noon ET
November 22 (Tuesday)	Minutes and SEP published at 2:00 pm ET

Attachment 2

Scope of the Regular November Projections

Variables and Periods:

2011-2014: Please provide your projections of the most likely outcomes for the percent change in **real GDP** (Q4/Q4), the percent change in the chain-weighted price index for **PCE** and for **core PCE** (Q4/Q4), and the level of the **unemployment rate** (Q4 average) for 2011, 2012, 2013, and 2014. Please also provide your current estimates for the annualized percent change in real GDP, the total PCE price index, and the core PCE price index in the first half of 2011³, i.e. $Q2^{2011}/Q4^{2010}$. Please express all of these projections to the nearest tenth of a percentage point (for example, 2.5 percent).

Longer Run: Please provide your best assessment of the rate to which the variables below would converge over the longer run (say, five to six years from now) in the absence of shocks and assuming appropriate monetary policy. **If you anticipate that the convergence process will take shorter or longer than about five or six years, please indicate your best estimate of the duration of the convergence process.** (If you do not submit any comments regarding the convergence process, it will be assumed that you anticipate the convergence processes for all three of the variables will take about five or six years.) Please provide your estimates as single numbers (that is, not as ranges), rounded to tenths of a percentage point. You may also include in your submission any explanatory comments that you think would be helpful.

1. Change in real GDP (percent, annual rate)
2. Civilian unemployment rate (percent)
3. Total PCE inflation rate (percent, annual rate)

³ If your H1 assumptions do not differ from the official published numbers, you can simply enter those numbers: GDP: 0.8 percent, PCE Inflation: 3.6 percent, Core PCE Inflation: 1.9 percent.

Judgments about Uncertainty and Risks:

Please also indicate whether you judge that the uncertainty attached to your projections for each variable is higher/lower/broadly similar to levels of uncertainty over the past 20 years, and also whether the risks around your projections for each variable are weighted to the upside/downside/broadly balanced. As with your modal projections, these judgments concerning the uncertainty and risks attached to your projections should be based on the assumption that the System pursues an appropriate monetary policy. We have provided an updated table summarizing a range of alternative measures of past forecast uncertainty as background for your judgments. **Please note that we expect to publish histograms of the uncertainty and risks responses for the first time in the November SEP** (in the past, this information has been described only in text).

Underlying Assumptions: As before, no common assumptions are proposed for fiscal policy and other exogenous factors, such as energy prices. However, if your assumptions for these types of variables differ materially from those in the Tealbook forecast, it would be helpful if this was noted in your narrative. With respect to monetary policy, projections should be based on the assumption that the System pursues what, in your judgment, would be an appropriate monetary policy, i.e., a policy that is most likely to achieve paths for economic activity and inflation that best satisfy your interpretation of the dual economic objectives. To aid the interpretation of your projections, it would be appreciated if you would indicate whether your monetary policy path deviates materially from the path assumed by the staff in the Tealbook and, if so, in what way. These deviations can be described qualitatively or, if you prefer, quantitatively.

Narrative: The value of the projections process would be increased greatly if you could supply a narrative of the key considerations shaping your outlook. Some

possible headings to help structure your narrative are suggested below (and are included in the online template for submitting projections).

- Please describe the key factors shaping your central economic outlook and the uncertainty and risks around that outlook.
- Please describe any important differences between your current economic forecast and the Tealbook.
- Please describe the key factors causing your forecasts to change since the projections submitted for the **June** FOMC meeting.

Attachment 3

Table 1: Historical Projection Errors
Root Mean Squared Errors of Fall Projections for 1991 to 2010¹

<i>Source</i>	Real GDP ² (percent change, Q4 to Q4)				Unemployment Rate (Q4 average)				Consumer prices ³ (percent change, Q4 to Q4)			
	2011	2012	2013	2014	2011	2012	2013	2014	2011	2012	2013	2014
Monetary Policy Report ⁴	0.47	1.29	—	—	0.17	0.92	—	—	—	—	—	—
Federal Reserve staff	0.65	1.43	1.61	—	0.20	0.96	1.57	—	0.33	0.97	1.07	—
Congressional Budget Office Administration	0.58	1.40	1.93 ⁵	1.85 ⁵	0.09 ⁶	0.67 ⁶	1.34 ⁶	1.74 ⁶	0.58	0.89	1.01 ⁵	1.04 ⁵
Blue Chip	0.68	1.49	1.69	1.66	0.25	1.03	1.67	1.90	0.38	0.85	0.93	0.90
Survey of Professional Forecasters	0.66	1.39	—	—	0.17	0.88	—	—	0.49	0.90	—	—
Average	0.65	1.37	—	—	0.13	0.86	—	—	0.49	0.88	—	—
	0.62	1.39	1.74	1.76	0.18	0.89	1.52	1.82	0.45	0.90	1.00	0.97

1. For methodological details and discussion see “Gauging the Uncertainty of the Economic Outlook from Historical Forecasting Errors” by David Reifschneider and Peter Tulip (Finance and Economics Discussion Series 2007-60). The table above is updated to include forecasts and outcomes for 2007 through 2010 (data which became available subsequent to the FEDS paper) and minor methodological changes.
2. Real GNP before 1992.
3. Based on the total consumer price index. Evidence based on Federal Reserve staff projections suggests that, on average, forecast errors for CPI inflation are slightly larger than those for PCE inflation.
4. Monetary Policy Report projections equal the mid-points of the published central tendency ranges. Results for inflation are not reported because the forecast price measure has changed over time.
5. Percent change, calendar year over calendar year.
6. Annual average. CBO results are included in unemployment rate averages for 2012, 2013 and 2014 but not 2011.

Attachment 4

Information about the Trial Run

Scope of Trial-Run Projections:

1. Please provide your projections for the average level of the target federal funds rate in the fourth quarter of 2011, 2012, 2013, and 2014, and over the longer run. As with the regular projections, these trial-run projections should reflect your assessment of appropriate monetary policy, and the longer-run projection refers to the federal funds rate to which the economy will converge over time in the absence of further shocks.
2. If you anticipate that, under appropriate monetary policy, the target federal funds rate will not be raised until after 2014, please indicate the year in which the first increase in the target federal funds rate is likely to occur. In addition, please indicate your projections for the rates of real GDP growth, PCE inflation, and core PCE inflation in that year and your projections for the unemployment rate and the target federal funds rate in the fourth quarter of that year.
3. Please describe the key factors informing your judgments regarding the appropriate path of monetary policy.

Logistics:

We will make available through SDS a downloadable template for your trial-run responses. Please submit the completed template through the SDS “Create Comment” feature by **5:00 pm Eastern Time on Friday, October 28**. (For record-keeping purposes, we ask that you **not** send in your projections via email.)