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HIGHLIGHTS

BASED ON DATA RELEASED AT 9:00 A.M. EST, MARCH 20, 2013

FED POLICY DRIVES EQUITIES: CFS MONEY SUPPLY STATISTICS

DATA FOR FEBRUARY 2013

Today, CFS monetary and financial data should help the Federal Reserve and market participants assess relative benefits and costs from the present monetary policy mix.

Economy Poised to Benefit

The broadest measure of money (CFS Divisia M4 or DM4) gained 5.3% in February 2013 on a year-over-year basis relative to a modest 2.7% in the preceding year ending in February 2012. The recent expansion in DM4 is critical for economic growth, as it measures financial activity in the private sector and is a strong indicator of nominal monthly GDP. For instance, DM4 accounts for a stunning 84% of monetary services created by the private sector. In contrast, the high powered money controlled by the Federal Reserve (or monetary base) represents a scant 16% of the total expenditure on the components of DM4.

So, DM4 matters for the economy. It is no wonder that the economy grew by only 1.8% and 2.2% in 2011 and 2012. DM4 expanded by a tepid 1.3% and 3.2% in 2011 and 2012 (see Figure 1).

Figure 1. DM4 Gains are Needed to Push GDP Growth Higher, year-over-year

	<u>GDP Growth</u>	<u>CFS DM4</u>	<u>Monetary Base</u>
2011	1.8%	1.3%	25.4%
2012	2.2%	3.2%	5.7%
2013 (*)	2.5 - 3%	5.7%	4.8%

(*) Average in January and February for DM4 and monetary base. Expected GDP growth if present expansion persists.

Source: Bureau of Economic Analysis, Bloomberg LP and Center for Financial Stability.

Recent gains in DM4 – averaging 5.7% in January and February – are consistent with economic growth of 2.5% to 3%.

Reliance of the Stock Market on QE

The policy of purchasing Treasury and mortgage securities by the Federal Reserve or quantitative easing (QE) accentuates swings in equity markets.^{1 2} For example, the Standard and Poors' 500 equity index gained 22% and 32% on an annualized basis, respectively during QE1 and QE2. The gains required a respective 32% and 40% annualized expansion in the monetary base. Not surprisingly, when the

¹ "QE3 and Markets: CFS Money Supply Statistics" – Center for Financial Stability, December 19, 2012.

² Goodman, Lawrence, "Bernanke Still Pouring Shots Of QE To Markets Already Drunk On Liquidity" – *Forbes*, January 30, 2013.

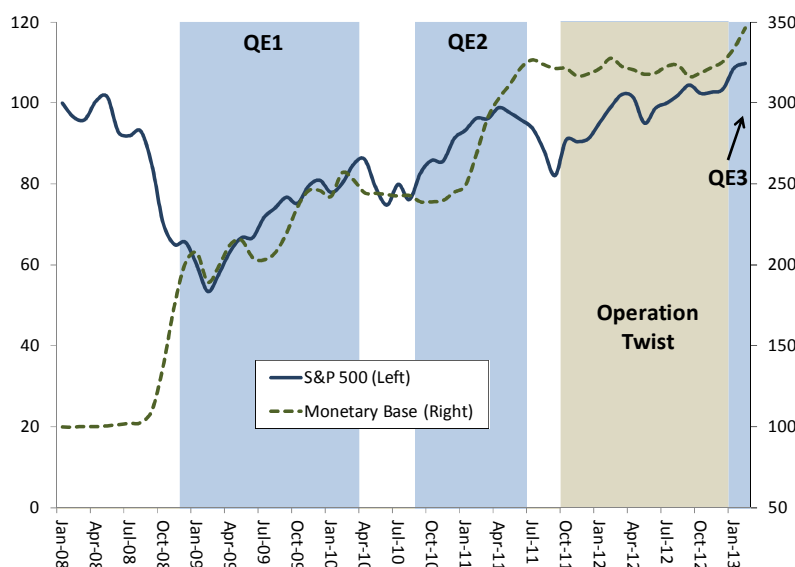


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extraordinary monetary policy operations ceased and the monetary base slid by 9% and 1%, stocks plunged an annualized 23% and 46%.

Figure 2. Dependence of Stocks on Absence or Presence of QE (Jan 2008 = 100)



Source: Federal Reserve, Bloomberg LP and Center for Financial Stability.

Equity markets are off to a strong start in 2013 with an annualized gain in the S&P of 44% and a 45% push higher in the monetary base on an annualized basis.

Figure 3. Major CFS Monetary Aggregates and Reserve Balances, % year-over-year

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Sep-12</u>	<u>Oct-12</u>	<u>Nov-12</u>	<u>Dec-12</u>	<u>Jan-13</u>	<u>Feb-13</u>
CFS DM4	7.3%	8.4%	-4.9%	-0.7%	0.9%	4.2%	4.4%	5.1%	6.8%	6.1%	5.3%
CFS DM4-	7.3%	2.6%	-5.0%	-0.6%	2.7%	3.6%	3.9%	4.5%	6.7%	6.2%	5.0%
CFS DM3	8.1%	3.0%	-2.3%	0.1%	3.6%	4.2%	4.5%	4.8%	6.7%	5.9%	4.8%
Reserves	0.0%	1802%	38.8%	-5.4%	48.2%	-7.7%	-6.9%	-2.8%	-1.8%	1.0%	4.4%

Source: Center for Financial Stability and Federal Reserve Board (total reserves of depository institutions).

About CFS Money Supply

CFS Divisia monetary measures were developed under the direction of Professor William A. Barnett - one of the world's leading experts on monetary and financial aggregation theory. CFS money supply data are essential, especially since the Federal Reserve ceased production of M3 in 2006. Similarly, Divisia measures are superior, as they accurately weight various classifications of money from cash to leverage in the shadow banking system.

For more information about CFS Divisia please contact:

William A. Barnett (Methodology)
Lawrence Goodman (Policy and Market Application)

(212) 626-2660 / wbarnett@the-cfs.org

(212) 626-2660 / lgoodman@the-cfs.org

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