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HIGHLIGHTS

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CFS NEW MONEY SUPPLY DATA REVEAL POLICY UNCERTAINTY AND REGIME CHANGE

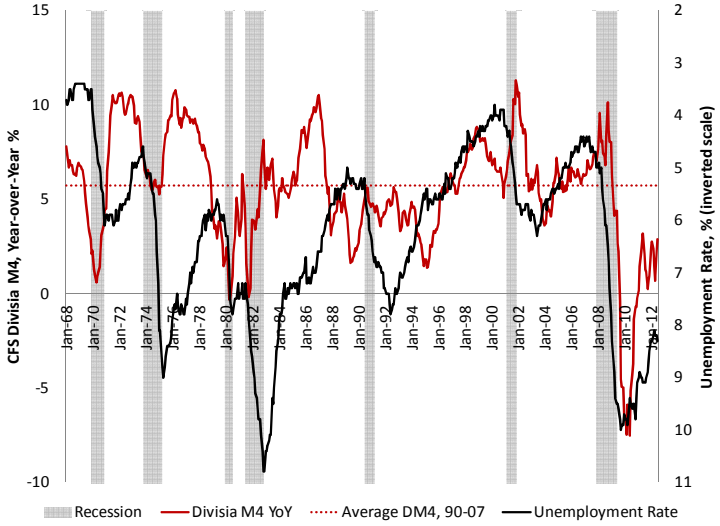
DATA FOR JULY 2012

Today, Center for Financial Stability (CFS) broad money supply data for July 2012 illustrate that the US economy is improving modestly. However, growth remains extremely weak. For instance, CFS Divisia M4 (DM4) for July advanced by 2.9% on a year-over-year (YoY) basis or well below the 6% to 6.5% typically associated with historical trend GDP growth of 3¼%.

CFS proprietary money supply data provide a crucial barometer to measure the traditional and shadow banking system in real time. Today's release illustrates how "policy uncertainty in the US and Europe is restraining activity in the financial system and economy more broadly," according to CFS President Lawrence Goodman.

A reduced stock of commercial paper and institutional money-market funds is contracting broad money (DM4) growth by 0.8% and 0.7%, respectively. In contrast, growth of safer monetary liabilities such as commercial banks' savings deposits and demand deposits is contributing to an expansion of the money supply by 3.2% and 1.5%, respectively.

Figure 1. Monetary Growth and Unemployment



Source: Bureau of Labor Statistics and Center for Financial Stability.

"Interestingly the data during the past two years may show the beginnings of the reappearance of a relationship more typical since the creation of the Federal Reserve in 1913, with monetary growth leading unemployment," according to Professor and CFS Director William A. Barnett.

A chart of CFS Divisia money supply (DM4, year-over-year growth rates) and the unemployment rate may reveal changes in Fed policy regimes. Over the years, there has been a very well documented time

delay between changes in monetary growth and final targets of policy. This "causality" relationship has been evident under all Fed operating regimes, with strong causality of money to GNP with lags extending back at least two years.[1] Our chart displays a similar lagged influence of monetary growth on unemployment --- up until around 1992, after which the time delay seems to have disappeared.

Figure 1. Major CFS Monetary Aggregates and Monetary Base, % year-over-year

	2007	2008	2009	2010	2011	Apr-12	May-12	Jun-12	Jul-12
CFS DM4	7.3%	8.4%	-4.9%	-0.7%	0.9%	1.5%	0.7%	2.3%	2.9%
CFS DM4-	7.3%	2.6%	-5.0%	-0.5%	2.8%	1.8%	0.5%	2.1%	2.6%
CFS DM3	8.1%	3.0%	-2.3%	0.2%	3.6%	3.3%	1.9%	3.6%	3.7%
Monetary Base	1.5%	100.7%	22.0%	-0.4%	29.9%	5.8%	1.9%	-1.1%	-1.2%

Source: Center for Financial Stability and Federal Reserve Board (for monetary base).

Additional information is available via:
July News Release http://www.CenterforFinancialStability.org/amfm/Divisia_July12.pdf
CFS Website www.CenterforFinancialStability.org

[1] William A. Barnett and Apostolos Serletis (1990), "A Dispersion-Dependency Diagnostic Test for Aggregation Error: With Applications to Monetary Economics and Income Distribution," *Journal of Econometrics*, vol. 43, pp. 5-34; reprinted in William A. Barnett and Apostolos Serletis (2000), *The Theory of Monetary Aggregation*, Elsevier, Amsterdam, chapter 9.