



## CENTER FOR FINANCIAL STABILITY

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### HIGHLIGHTS

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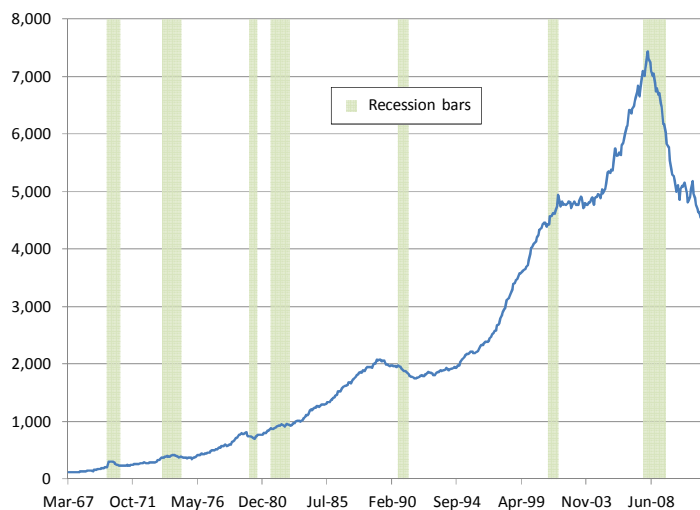
## SHADOW BANKING AND THE FED: CENTER FOR FINANCIAL STABILITY MONEY SUPPLY STATISTICS DATA FOR OCTOBER 2012

Center for Financial Stability (CFS) [money supply data for October 2012](#) suggests that the economy has bottomed. However, below potential growth remains vulnerable to the upcoming fiscal cliff.

Participants in the financial economy continue to seek safety in insured institutions. In contrast, the shadow banking system has been hit hard.

“The shadow banking system is vital to corporations and the overall economy,” according to CFS President Lawrence Goodman. The shadow banking system embedded in the CFS monetary data contains institutional money market funds, commercial paper, and repurchase agreements. CFS data evaluate the levered transactions – which helped to topple the US economy. However, the commercial paper and institutional money fund markets provide the funding or fuel for growth in corporate America. Unfortunately, these sources are presently plagued by domestic and international regulatory and policy uncertainty.

**Figure 1. CFS Shadow Banking (Real, September 2012 billions \$)**



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

The CFS measure of the shadow banking system is down a stunning 40% in real terms from peak to trough in the recent financial crisis. In contrast, previous adjustments typically associated with recession or bursting market bubbles coincided with a 13% to 25% collapse in shadow banking during the period from 1967 to the present.



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## Observations this Month

CFS Divisia M4 (DM4) for October advanced by 4.4% on a year-over-year basis. As the performance of the broadest money supply measure was clouded by large issuance of Treasury bills to fund the budget deficit, the broad money supply excluding Treasury bills (DM4-) provides a clearer picture of the private sector. DM4- gained a low, but improving, 3.9% on a year-over year basis relative to 2.2% one year earlier. Historic real trend growth of 3 ¼% is typically associated with broad money growth of 6% to 6.5%.

**Figure 2. 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>Jun-12</u>	<u>Jul-12</u>	<u>Aug-12</u>	<u>Sep-12</u>	<u>Oct-12</u>
<b>CFS DM4</b>	7.3%	8.4%	-4.9%	-0.7%	0.9%	2.2%	2.9%	3.3%	4.3%	4.4%
<b>CFS DM4-</b>	7.3%	2.6%	-5.1%	-0.6%	2.8%	1.9%	2.5%	2.5%	3.7%	3.9%
<b>CFS DM3</b>	8.1%	3.1%	-2.3%	0.1%	3.6%	3.4%	3.6%	3.3%	4.3%	4.5%
<b>Reserves</b>	0.1%	1801%	38.8%	-5.4%	48.2%	-6.6%	-6.7%	-5.1%	-7.7%	-6.9%

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.

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Additional information:

[www.CenterforFinancialStability.org](http://www.CenterforFinancialStability.org)

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