Some Expect Disruptions; Optimists Spend Freely; Rates Could Rise in 2000

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WASHINGTON—In trying to ensure a smooth run-up to the year 2000, Federal Reserve officials might be helping create the potential for economic bumps down the road.

Thanks in part to Fed policies that are making money more readily available, businesses and individuals appear to be loading up on cash, much of it borrowed, some analysts say. That is helping to swell values on U.S. securities markets, heating up an already strong economy, some analysts believe. But what happens after the Y2K phenomenon has come and gone?

Some analysts say that, at a minimum, the big bucks suddenly sloshing around in the economy could provide further encouragement for Federal Reserve officials to tighten monetary policy again after January, particularly if the increases continue.

"If the growth rates in money supply stay high, it will be another reason for the Fed to raise rates," says Marc Wansel, vice president and financial economist for J.P. Morgan Inc. in New York.

Don Hays, president of Hays Market Focus Inc., a Nashville, Tenn., newsletter and consulting company, thinks such a rate increase could bring on a significant money-supply contraction. In the past, such contractions have led to market corrections, he says.

In November, the Fed's broadest measure of money in the economy, the M3 supply, grew by about 18% on an annual basis, compared with 9.7% for the first six months of the year.

Fed officials used to pay more attention to trends in money supply, believing that sharp increases, like the recent one in M1, could spur inflation. Now they rely less on monetarism, which had its heyday in the 1970s and 1980s. Many economists believe it has proved to be a less-than-reliable indicator of larger economic conditions. But some Fed officials still keep a close eye on money supply.

Several specific measures of bank lending have soared even higher in recent weeks. According to the Fed, loans for securities, typically to dealers, have swelled by 24.5%, or some $28.1 billion, since the be...
Money Supply Soars as Y2K Nears

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The beginning of November. Lending tends to add to the money supply by creating new deposits.

Oddly, Y2K seems to be pumping up the money supply for opposite reasons, according to some analysts following the issue. On one hand, a lot of people are worried about economic disruptions in case computers crash. They are loading up on cash, as are the businesses that serve them, such as banks and brokerage firms. In a new Wall Street Journal/NBC News poll, 38% of those surveyed said they plan to prepare for any potential Y2K problems by taking extra money out of the bank before New Year's Day. Some businesses also worry that companies they do business with, especially overseas, will experience big disruptions and won't be able to pay bills.

But a lot of investors as well as banks also are beginning to think that the Y2K phenomenon might not be so bad. That is helping to turn them from more cautious Y2K investment strategies to more aggressive ones, and leading to more securities deals, including transactions financed by bank loans. That in turn is driving the money supply up even more.

The Fed itself, in an effort to ensure that the economy keeps working smoothly, may have contributed to the money supply's swelling, some analysts say, by making money more available to banks and securities dealers in the event that Y2K disruptions prove to be substantial.

That has helped buoy confidence in relatively riskier loans and investments, Mr. Wurzelbacher says, adding that it appears to be driving up demand for money as well. "The flight to quality that many anticipated hasn't happened," he says. "It's because of those Fed actions."

A third, related factor causing the money pool to grow is generally rising confidence in the economy's strength in the fourth quarter, thanks to continued strong consumer spending and low inflation.

For now, it is all helping make for a strong economy this month. Some analysts see no reason that won't continue after Jan. 1. They note that money-supply numbers are notoriously volatile, and often rise and subside without having much discernible impact on the overall economy. They think the recently rising tide of cash doesn't bode well or ill. "It's hard to believe it means much," says Bruce Steinberg, chief economist for Merrill Lynch & Co. in New York.

Even some analysts who have publicly pointed to the change in credit and money supply aren't sure it has much long-term significance. Ian Steeples, chief U.S. economist for High Frequency Economics in Valhalla, N.Y., chalks up a lot of the money-supply increase to defensive Y2K preparedness: "Does it mean anything for the economy? No, not really. It will not make much difference, except to get some excitable economists excited."