

Macro Roundup Article

Headline: [Markets Go Calm: A Lehman Pause or the Real Thing?](#)

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Tweet: [@johnauthers](#) cites work by [@willdenyer](#) of Gavekal Research whose gauge of financial conditions suggests that financial conditions are now extremely tight.

Summary: How exactly should financial conditions be measured? It proves to be a difficult issue. The most widely cited benchmarks incorporating a range of market indicators, produced by Goldman Sachs and by Bloomberg, both suggest that conditions were relatively easy until very recently, and then tightened rapidly. Neither is particularly extreme. But what exactly are we (and Goldman) measuring? Will Denyer of Gavekal Research suggests that these indexes are of limited use. Discussing the Bloomberg index, he said: "It comprises credit spreads in the money and bond markets, the S&P 500, and volatility measures including the VIX index. As a result, it is probably better thought of as an indicator of financial market risk appetite, rather than as a measure of whether or not conditions in the real economy are conducive to credit growth." He offers his own gauge, which he dubs the "true financial conditions index," an ambitious undertaking that incorporates money supply growth, the yield curve, metrics of vitality in the banking sector, the spread between the rate of return on corporate investments in real assets and the real cost of financing those investments, and measures of housing affordability (using real mortgage rates, deflated by inflation expectations). Put all of this together, and it looks like money was already very tight last week, ahead of the Credit Suisse weekend, when this chart was produced.

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