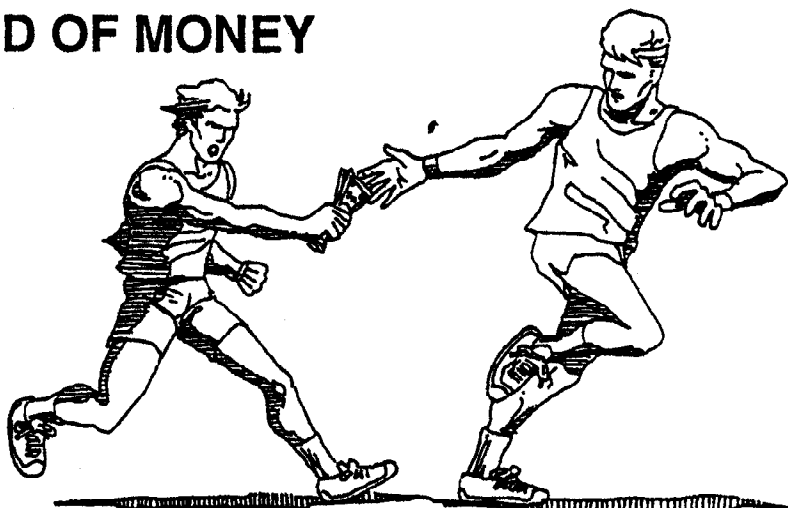


VELOCITY: THE SPEED OF MONEY



Velocity is defined as the number of times per year an “average dollar” is spent on goods and services.

$$\text{Velocity} = \frac{\text{value of transactions}}{\text{money stock}} = \frac{\text{Nominal GNP}}{\text{M1}}$$

So, if GNP = \$4500 billion, and the money stock = \$900 billion, velocity is _____.

What would speed up velocity? Anything that causes people to want to hold less cash, means money circulates faster – velocity rises.

Would the following cause velocity to rise?

- a) use of credit cards
- b) ATM's at banks
- c) people receive paychecks more frequently
- d) lower interest rates
- e) higher rate of inflation

Bonus: If velocity is rising, does the Fed have to pump in more M1 to stimulate the economy?