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Modeling the Demand for M3 in the Unified Germany

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Abstract

An error correction model for the demand for real M3 money is constructed for the period of 1976–1994 with real GNP, the GNP deflator, as well as a short-term and a long-term interest rate as explanatory variables. Quarterly, seasonally unadjusted data are used in estimating the model. It is found that there is a clear structural break due to the German unification in 1990. On the other hand, once this structural break is accounted for, a stable relation is found which resists a series of specification tests. These include a number of recent tests of parameter constancy and linearity. Our specification is at variance with findings reported by some other researchers, notably the Deutsche Bundesbank.

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