Analysis and insight into trends in money and banking, and their impact on the world’s leading economies

www.mv-pt.org
In his 1970 Institute of Economic Affairs pamphlet on *The Counter-Revolution in Monetary Theory* Milton Friedman, who was to be awarded the Nobel prize for economics six years later, wrote,

“Inflation is always and everywhere a monetary phenomenon in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output. … A steady rate of monetary growth at a moderate level can provide a framework under which a country can have little inflation and much growth. It will not produce perfect stability; it will not produce heaven on earth; but it can make an important contribution to a stable economic society.”
Why did inflation reach its highest-ever peacetime levels in the 1970s? Why did inflation fall in the 1980s and 1990s? Why has deflation become widespread in the leading advanced nations in 2015? The 20 years from the mid-1980s saw good economics outcomes – with steady growth and rising employment – in most countries. How is this period of ‘the Great Moderation’ to be explained? By contrast, in late 2008 and early 2009 demand and output collapsed across the world. What were the causes of this downturn, widely known as ‘the Great Recession’?

These questions are central to business life and political debate everywhere. Most observers agree that any interpretation of the Great Recession must recognize the important of banks and banking systems to the economy’s behaviour.

The newly-established Institute of International Monetary Research will promote research into how developments in banking and finance affect the wider economy. The Institute’s aims are to enhance economic knowledge and understanding, and to seek price stability, steady economic growth and high employment. Particular attention is paid to the effect of changes in the quantity of money on inflation and deflation, and on boom and bust.

The Institute is based in the United Kingdom and is associated with the University of Buckingham. However, the research and analyses are to be international in scope. Trends in the rate of growth of the quantity of money in the leading nations are to be monitored on a close and regular basis, but monetary analysis is useful in all economies, no matter how small.
The Institute will promote research into how developments in banking and finance affect the wider economy. Nowadays bank deposits are the main form of money and the principal constituent of the quantity of money. Economists have long recognised a strong relationship between changes in the quantity of money on the one hand, and changes in nominal national income and the price level on the other. This relationship is often seen as a key insight of ‘the quantity theory of money’, one of the oldest schools of economic thought. As noted by Mark Blaug, who wrote the authoritative text on Economic Theory in Retrospect, ‘painting with a broad brush, the quantity theory is supported by an overwhelming body of empirical evidence’. Further, ‘it is facts and not analytical rigour that make the quantity theory good economics’. The challenge for the Institute will therefore be to provide rigour as well as facts to the analysis of banks and money, and their wider economic effects. It will do so both historically (by looking at data from the past) and internationally (by investigating evidence from around the world).

The Institute will support:

- Research projects on the relationship between money and other macroeconomic variables, in both the short and long runs, and in many countries,
- The publication of papers and books that incorporate the results of the research projects,
- Conferences and seminars to discuss monetary and macroeconomic research, and
- Guest lectures, at which distinguished economists, policy-makers and leaders of thought can present their views on the key macroeconomic issues of the day.

Changes in the price level - through either inflation or deflation - have diverging effects on different people and companies. They can result in arbitrary shifts in income and wealth distribution, and cause social upheaval. As the great economist, John Maynard Keynes, said in his famous 1923 Tract on Monetary Reform, “...a change in the value of money...is important to society only in so far as its incidence is unequal. Such changes have produced in the past, and are producing now, the vastest social consequences, because, when the value of money changes, it does not change equally for all persons or for all purposes...Each process, inflation and deflation alike, has inflicted great injuries.”
The University of Buckingham

The Institute is associated with the University of Buckingham. Its founder and first Director, Professor Tim Congdon CBE, has given talks and seminars in the university. Some of the Institute’s research work is expected to lead to doctoral theses. The Institute’s staff will both participate in, and guide and advise the research. Two of the Institute’s three Deputy Directors – Dr. Juan Castaneda and Dr. Ali Kabiri – are members of the University’s economics faculty.

The University of Buckingham was originally founded as the University College at Buckingham in 1973 and received its Royal Charter from the Queen in 1983. The university’s funding is unlike that of other UK universities, as it does not receive state support. It has formal charity status as a non-profit making institution dedicated to the ends of research and education. The University of Buckingham has been top or near top of the National Student Survey (NSS) in student satisfaction since 2006. According to the 2014 Guardian University Guide, its graduates are exceptionally successful in finding work after finishing their degrees. Indeed, it ranked 1st out of 119 universities in terms of its students’ ‘career prospects’.

The Institute is located in Prebend House. A house on its site appeared in John Speed’s county map of 1610 and it is possible that some of the interior dates from that time. Like other houses on Hunter Street in the 17th century, Prebend House was probably occupied by a tanner. (The Speed map shows tanning pits in the gardens between the house and the river. The preparation of leather was an important industry in Buckingham in the past. Much of it was sent to Northampton, which became Britain’s most important centre for boot and shoe making.)
The Institute’s founder and first Director

The idea for an Institute of International Monetary Research arose in an informal conversation in 2011. Terence Kealey, then the University of Buckingham’s Vice-Chancellor, and Tim Congdon were both in London, attending that year’s Hayek Lecture by Professor Robert Barro (of Harvard University), given under the auspices of the Institute of Economic Affairs. Both found Barro’s remarks stimulating, but felt dissatisfied. They agreed that a new research organization – to understand better how banks and the financial system impact on the market economies of modern liberal democracies – was needed.

Tim Congdon spent most of his career as an economist in the City of London. Initially he advised brokerage firms’ and their clients, but in 1989 he set up Lombard Street Research as a consultancy business. At Lombard Street Research he maintained a tradition of research which had enabled him to forecast that the rapid growth in the UK’s quantity of money from 1986 to 1988 would lead to much higher inflation and a bust. These forecasts proved correct. From 1993 to 1997 Congdon served on the Treasury Panel of Independent Forecasters (also known as the ‘wise persons’), where he represented the so-called ‘monetarist’ point of view in advice to the Chancellor of the Exchequer. In 1997 he was appointed CBE for ‘services to economic debate’.

Congdon retired from the City in 2005, to have more time to write up books and papers. But he re-entered the fray at the start of 2009 when he started a small consultancy company, International Monetary Research Ltd. (turn over the page for more on the company), in response to the intensifying financial and economic crisis that became known as ‘the Great Recession’. Congdon is a prolific author of magazine and newspaper articles, academic papers and books on economic and financial topics. His most recent full-length book is the 2011 collection of his essays in Money in a Free Society, published by Encounter Books of New York.

“Tim Congdon has been Britain’s leading monetarist for about three decades... He has a sharp eye for statistics, for history, for the twists and flows of intellectual fads, and for the political arena where debate hardens suddenly into the stone of decision. He is subtle, practical, bellicose and highly articulate.”

Professor Peter Sinclair, in a review in The Business Economist of Tim Congdon’s 2007 collection of essays Keynes, the Keynesians and Monetarism
The Institute’s people

Juan Castañeda
A Doctor of Economics since 2003 (UAM University at Madrid), Juan Castañeda has experience working and researching in monetary policy and central banking. He has worked with the European Parliament’s Committee of Economic and Monetary Affairs and submitted written evidence for a UK Parliament report on the euro. He has been a visiting researcher at Cass Business School in London. He has been awarded a Bank of Spain annual scholarship to develop research on monetary history and has also developed several research projects funded by the Institute of Fiscal Studies at Madrid on fiscal policy rules.

Ali Kabiri
Dr Kabiri studied at the LSE and Cass Business School where he earned a PhD in Finance specialising in measuring asset bubbles. He has been a Visiting Research Scholar at Yale School of Management, Columbia Business School and Rutgers in the USA, and a research associate at the LSE Financial Markets Group (FMG) since 2011. He has recently released a new book, The Great Crash of 1929: A reconciliation of theory and evidence with Palgrave Macmillan.

John Petley
John Petley joined Tim Congdon at International Monetary Research Ltd. in 2011 after working as a political researcher in the European Parliament. He read music at Oxford and has written two books on political issues. Besides handling the Institute’s finances, he is responsible for updating the money numbers on the website.

The Institute is an educational charity, with the status of a ‘charitable incorporated organization’. Its governance and organization are the responsibility of a board of trustees. At the time of writing the trustees are:

- Professor Tim Congdon (chairman),
- Miss Venetia Congdon (secretary),
- Professor Terence Kealey, Vice-chancellor of the University of Buckingham from 2001 to 2014, and
- Professor Martin Ricketts, Dean of Humanities at the University of Buckingham from 2001 to 2014, and
- Tim Sanderson, chairman and chief executive of Sanderson Asset Management.

The Institute has three Deputy Directors, Dr. Juan Castaneda, Dr. Ali Kabiri and John Petley. Castaneda and Kabiri are members of the University of Buckingham’s academic staff and teach economics in the School of Humanities. Petley is responsible for the Institute’s administration and finance.

The Institute’s office in Prebend House is managed by Gail Grimston, who also responds to emails on the enquiries@mv-ht.org address.
International Monetary Research Ltd: support for the Institute

Appalling macroeconomic conditions in early 2009 prompted Tim Congdon to set up International Monetary Research Ltd. Its purpose was to act as a small research and consultancy vehicle, advising financial institutions and companies on the implications of monetary developments for key economic variables. (It also served as a vehicle for the advocacy of ‘quantitative easing’, to boost economic activity.) The company provides advice to over 20 clients, mostly fund management companies, by regular e-mails and its website. The company’s research is sent also to official bodies (such as central banks), and to the financial press and media. Some of its messages are quoted in the newspapers and influence the public debate on economic policy.

International Monetary Research Ltd. has had several outstandingly good ‘calls’ in the last few years, some of which are shown on the next page. Of course, the company’s research services are of significant commercial value to subscribers.

New subscribers are welcome. Please contact us on timcongdon@btconnect.com if you would like to hear more.

- 100% of International Monetary Research Ltd.’s profits are to be donated to the Institute of International Monetary Research.
- Institutional investors who subscribe for research services from International Monetary Research Ltd. are welcome to make a donation to the Institute, to promote its work as an educational charity.
- It is hoped that, in due course, the Institute will provide subscription products for schools and universities, with the charges for these products being below cost.

(At the time of writing [March 2015] Tim Congdon is approaching his 64th birthday. He has been a successful businessman and investor, and is the main donor to the Institute. He does not take an income from International Monetary Research Ltd. and has no intention of doing so. His position as the Institute’s first Director is not full-time and is unpaid. All being well, it is planned that a full-time and paid Director will take over in 2016.)
‘Inflation worries are extraordinarily misplaced in current conditions…Nevertheless, Mr. Alan Greenspan – the revered former chairman of the US Federal Reserve – published an article in the Financial Times of 26th June under the title “Inflation is the big threat to sustained recovery”. The argument of this note is that… there is little or no risk of a significant rise in inflation until after – probably several quarters or even years after – output has returned to its trend level…’

Weekly e-mail, 2nd July, 2009, discussing the US economic situation

What happened?

Unemployment has been falling in the USA since October 2009, from 10.0% of the workforce then to just over 5.5% now, implying a period of above-trend growth. But inflation is lower now than in 2010 and 2011, and many observers are expecting an annual fall in prices (i.e., deflation) to be recorded in spring 2015. Greenspan erred, whereas International Monetary Research Ltd. was right.

‘In the late 1990s bulls of Wall Street routinely appealed to the notorious “Greenspan put”, the notion that Greenspan would do whatever might be needed in monetary policy to keep share prices high. Arguably, a “Bernanke put” of unused expansionary Fed facilities is now in existence… it is too late in the cycle to bet on further prolonged weakness in equity and real estate markets.’

Weekly e-mail to clients on 17th July, 2009, discussing prospects for the American stock market

What happened?

The five years from mid-2009 saw large gains in the American stock market, with the S & P 500 index doubling in value.

In March 2010 Jurgen Stark, the ECB’s chief economist, warned that the ECB should withdraw its credit facilities to weak banks (or ‘non-standard measures’) in order to avoid risks of more inflation. International Monetary Research Ltd. said, ‘The ECB’s exit from the non-standard measures certainly appears premature… Contrary to Stark’s analysis, the main threat to Eurozone monetary stability is now deflation, not inflation. To worry about rising medium-term inflation risks when the quantity of money has stopped growing is “inflation nuttiness” of an extreme kind…’

Weekly e-mail from International Monetary Research Ltd. on 19th March, 2010

What happened?

Banks in the Eurozone periphery continued to have severe funding difficulties over the next five years. Money growth and inflation remained very low, and in late 2014 most Eurozone member states were experiencing falls in the price level, i.e., deflation. The ECB’s chief economist was wrong, whereas International Monetary Research Ltd. had the correct prognosis.
The Institute’s work and thinking will be conveyed by a variety of means, including research papers, conferences, lectures and seminars. It is also hoped that, when sufficient resources are available, the Institute will prepare an educational service (on how banks work, how money affects the economy and so on) for other learning institutions. One of the Institute’s objectives will be to inform the debate on public policy, and to help in maintaining price stability and high employment. But perhaps an even more important long-run aim will be to improve financial awareness and the understanding of economics in schools and sixth-form colleges, and of course other universities.

However, initially, the website will be the main vehicle for spreading the research ideas and findings. The website address www.mv-pt.org reflects the Institute’s purpose. It refers to the so-called ‘equation of exchange’, \( MV = PT \), where \( M \) stands for ‘the quantity of money’, \( V \) for its velocity, \( P \) for the price level and \( T \) for the number of transactions. The identity was first proposed by Simon Newcomb, an American astronomer and physicist, in 1885. It was developed by Professor Irving Fisher of Yale University in a famous 1913 book on The Purchasing Power of Money. The website will in due course contain educational webcams. These webcams will explain both

- how money is created by the banking system, and
- how money relates to the rest of the economy.
When the monetary regime is working well, it is easy to forget how much trouble disorder in a nation’s banking system and public finances can cause. The most celebrated economist of the early Victorian era, John Stuart Mill, wrote in his classic text *Principles of Political Economy*,

“There cannot...be intrinsically a more insignificant thing in the economy of society, than money...It is a machine for doing quickly and commodiously, what would be done, though less quickly and commodiously, without it: and like many other kinds of machinery, it only exerts a distinct and independent influence on its own when it gets out of order.”
The new Institute of International Monetary Research, which is associated with the University of Buckingham, will promote research into how developments in banking and finance affect the wider economy. Nowadays bank deposits are the main form of money and the principal constituent of the quantity of money. Economists have long recognised a strong relationship between changes in the quantity of money on the one hand, and changes in nominal national income and the price level on the other. This relationship is often seen as a key insight of ‘the quantity theory of money’, one of the oldest schools of economic thought. As noted by Mark Blaug, who wrote the authoritative text on Economic Theory in Retrospect, ‘painting with a broad brush, the quantity theory is supported by an overwhelming body of empirical evidence’. Further, ‘It is facts and not analytical rigour that make the quantity theory good economics’. The challenge for the new Institute of International Monetary Research will be twofold,

• to compile data, and to dig up the facts about how developments in banking and finance impact on the economy as a whole, and

• to be rigorous in analysing those data and facts, and conducting research on the main policy messages.

The Institute is an educational charity. Its work will inform the public debate on economic policy, enhance knowledge about how the economy works and provide support for the teaching of economics in educational institutions, including schools and sixth-form colleges.