INSTITUTE OF INTERNATIONAL MONETARY RESEARCH

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

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[The Institute of International Monetary Research is a research institute with charitable status. This note is being e-mailed to people and organizations interested in global money trends, and the relationships between money and banking on the one hand and macroeconomic outcomes on the other. It is not business or investment advice, and the Institute accepts no responsibility for decisions taken in the light of the analysis given.]

Monthly e-mail from Tim Congdon and John Petley – 28th March, 2022

Global money round-up in spring 2022

The increase in the US consumer price index in the year to February was 7.9%, the highest for 40 years. According to the Knoema consultancy's website, the consensus view of international agencies (the OECD, the IMF etc.) is that the long-term prospect – looking out to 2030 – is for US consumer inflation to be 2.3% a year. That will clearly be exceeded by a wide margin in 2022 and 2023. The Ukraine tragedy is now giving mainstream economists a bogus excuse for their failure to anticipate the severity of the inflation upturn. Our analysis and forecasts since spring 2020 – unlike the mainstream – have been right. Money growth has been excessive in the USA, the Eurozone and the UK, and that has been the basic cause of the current inflation episode. (Money growth in the leading Asian economies has been much the same in the last two/three Covid-affected years as in the previous two/three years. Inflation in the Asian economies – China, Japan, India – will be impacted by global commodity price increases, and worldwide bottlenecks and supply shortages, in just the same way as "the West" [i.e., the USA, the Eurozone and the UK]. But it is already clear that overall inflation rates will be little changed from pre-Covid in "Asia".)

Major central banks in "the West" should pay more attention to money growth trends and take steps to restrain the expansion of *commercial* bank balance sheets. But their statements focus instead on the size of *central* bank balance sheets. At any rate, asset purchase programmes are being halted. When these measures are implemented, along with interest rate increases, broad money growth will fall. Significant reductions in money growth are therefore to be expected in "the West" in 2022 and 2023, while inflation remains high to remove the monetary overhang from the past. Real money will fall, hitting asset prices and causing beneath-trend growth and/or recessions. Whether the world economy as a whole enters recession in 2023 is unclear, because the big Asian economies are now more important as commodity importers than "the West" and do not face such severe difficulties of cyclical adjustment.

Money trends in early 2022 in the main countries/jurisdictions

The Institute of International Monetary Research focuses on the relationship between trends in the growth of the quantity of money, broadly-defined, and macroeconomic outcomes. Most of the last two years has been dominated by the Covid-19 medical emergency. Late 2022 should approximate medical normality in many countries, although China is still troubled. The Institute's consistent analysis since spring 2020 – that money growth acceleration would lead to an inflationary boom and an upturn in inflation – has proved correct. The new area of debate is the duration of above-normal inflation, with normality seen as an annual increase in consumer prices of 2% a year. The key principles here are that,

i. The rate of inflation is roughly equal to the rate of increase in nominal GDP minus that of real GDP, and
ii. Over the medium term, growth rates of broad money and nominal gross domestic product will be similar, although not identical.

Much will therefore depend on rates of broad money growth in coming months and quarters, with the table below summarizing recent patterns in the leading nations. The table shows that money growth reductions from the remarkable 2020 peaks are now evident almost everywhere. However, in the USA– although not in Japan and the UK, and perhaps the Eurozone – the three-monthly annualised numbers are still well above the typical figures before the pandemic and remain far too high to be reconciled with 2% inflation. Worries about inflation will persist and indeed intensify in 2022.

Name of country/ jurisdiction	Share of world output in 2020		Growth rate of broad money		Comment
	In purchasing-power parity terms, %	In current prices and exchange rates, %	In last three months at annualised rate, %	In last twelve months, %	
USA	15.4	24.7	**11.2**	**9.8**	Money growth has slowed cf. spring 2020, but remains far too high for 2% Fed inflation target.
China	18.3	15.4	**9.6**	**9.0**	Money growth moderate amid property bust scares. Policy being eased slightly.
Eurozone	12.1	17.4	**5.4**	**6.4**	Money growth moderating, as ECB ends asset purchases. Target2 again an issue.
Japan	3.7	6.0	**3.5**	**3.1**	Credit and money growth back to pre-Covid norms, implying little inflation in medium term.
India	6.8	3.1	**7.4**	**9.2**	Recent money falling, despite forecasts of 2022 output boom.
UK	2.2	3.3	**3.6**	**5.4**	Money growth down sharply, with very weak bank lending to the private sector.

The recent moderation in money growth in the Eurozone, Japan and the UK implies that inflation will, in these places, come down towards levels closer to the norms of the 2010s. However, the lags are such that both this year and 2023 will feature annual inflation rates typically above 5% and sometimes above 10%. The Ukraine tragedy will add some twists to the inflationary spiral, but it is certainly not the fundamental cause of the inflation of the early 2020s. This inflation episode – like others – is to be attributed to excessive growth of the quantity of money.

As noted last month, crucial to money growth in 2022 will be the behaviour of bank lending to the private sector. In the last two years high or very high money growth in the main Western economies has been almost entirely due to central bank asset purchases and monetary financing of budget deficits. The Institute's analysis has suggested that, as central bank asset purchases stop and budget deficits decline, money growth will decelerate unless bank lending to the private sector revives strongly. This point fits with the latest money growth patterns in the leading countries.

In the USA bank credit to the private sector is now growing strongly. "Loans and leases in bank credit" (mostly bank lending to the private sector, and constituting over half of US commercial bank assets) increased in the 13 weeks to 9th March at an annualised rate of 11.8%. The resumption of growth in credit to the private sector dates to the middle of last year. In the 37 weeks to 9th March "loans and leases" increased by 5.9% (or at an annualized rate of 8.4%). That 8.4% figure – and the latest three-month annualised number in double digits – are somewhat higher than in very early 2020, before Covid. Anecdotal reports of US banks' keenness to lend – and of US companies' eagerness to borrow both the rebuild inventory and to anticipate price rises – seem to be correct.

If the annual rate of credit growth stays in the 8% - 10% vicinity consistently, the message will be that money growth has its own momentum from the private sector's behaviour and does not depend on continued Fed asset purchases. That will affect the size of the interest rate rise needed to bring annual money growth back down to the 3% to 5% band compatible with 2% inflation. The faster is credit growth, the larger will be the required move in Fed funds rate. The degree of dynamism of private sector bank credit must be carefully watched. Bearing in mind that Federal and state governments also have persisting deficits that must be financed, market fears of a significant rise in dollar interest rates in 2022 look increasingly plausible.

In the Eurozone the stock of credit to the private sector was 4.3% higher in January 2022 than a year earlier. Mortgage lending was the only type of credit expanding during the worst of the pandemic, but that has now changed. The stock of loans for house purchase was up by 5.5% in the year to January, whereas loans to non-financial corporations (i.e., industry and commerce) advanced 3.7% in the same period. But in the three months to January loans to all corporations, financial and non-financial, increased by 2.3% (or at an annualized rate of 9.5%). European governments are still doing their best to persuade the Basel-based Bank for International Settlements, and the European Commission, that further large increases in banks' capital requirements are unnecessary and would damage the ability of their financial systems to sustain the recovery. They seem to be having some success in these efforts, despite the concurrent drives by regulatory officialdom for greater greenery, better governance and the like.

In Japan bank lending to the private sector surged in the opening months of the Covid pandemic, but the loans have been largely repaid with the return of medial normality. Lending to the private sector is now extremely weak.

UK bank regulators seem to believe that the higher are bank capital/ asset ratios, the safer is the banking system and the better is the outlook for the economy. With inordinate amounts of capital required, commercial banks are allocating capital to other activities. Large banks are not hiding their reluctance to commit new capital to mainstream UK commercial banking. Lloyd's Bank wants to become a huge residential landlord, an activity which will divert capital from banking as such. Meanwhile HSBC has made no secret that it wants to grow the proportion of its business in Asia rather than Europe, including the UK. The problem will be made worse by a decision taken by the Prudential Regulation Authority, of the Bank of England, in December 2021. This was to increase UK banks' counter-cyclical capital buffer to 1% from zero. To the extent that capital requirements on banking in the UK are higher than elsewhere, banking business will shift from the UK to elsewhere.

UK mortgage lending is still growing, but only just. The stock of bank lending to companies and financial institutions (excluding to the awkward "intermediate other financial corporations", which are quasi-banks) was *lower* at the end of 2021 than a year earlier. In the three months to January such lending dropped by 1.0%, i.e., at an annualised rate of 4.0%. Regulation has destroyed the incentive for bank stakeholders to grow their loan portfolios.

To repeat the point made here last month, in 2022 and 2023 the vigour – or lack of vigour – of bank credit to the private sector is crucial to interest rate prospects. The market consensus is that interest rate rises will occur in most developed countries once the pandemic-related weakness in aggregate demand lies in the past. Central banks may end asset purchase programmes first, but higher interest rates are widely foreseen. A reduction in money growth is a condition of the return of moderate inflation, while robust bank lending to the private sector will make it more difficult to deliver the needed reduction in money growth. If bank lending to the private sector is, even at virtually zero interest rates, increasing at an annual rate of 5% or less, it will be easy for central banks to keep money growth under control. Pointers to future lending growth therefore deserve to be monitored carefully in the next few months. Despite very low interest rates, and indeed extremely negative real interest rates, a big boom in private sector bank credit does not seem to be imminent in Japan or the UK. But a strong recovery in such credit in the USA has begun, and the Eurozone it is seeing signs of life.

25th March, 2022

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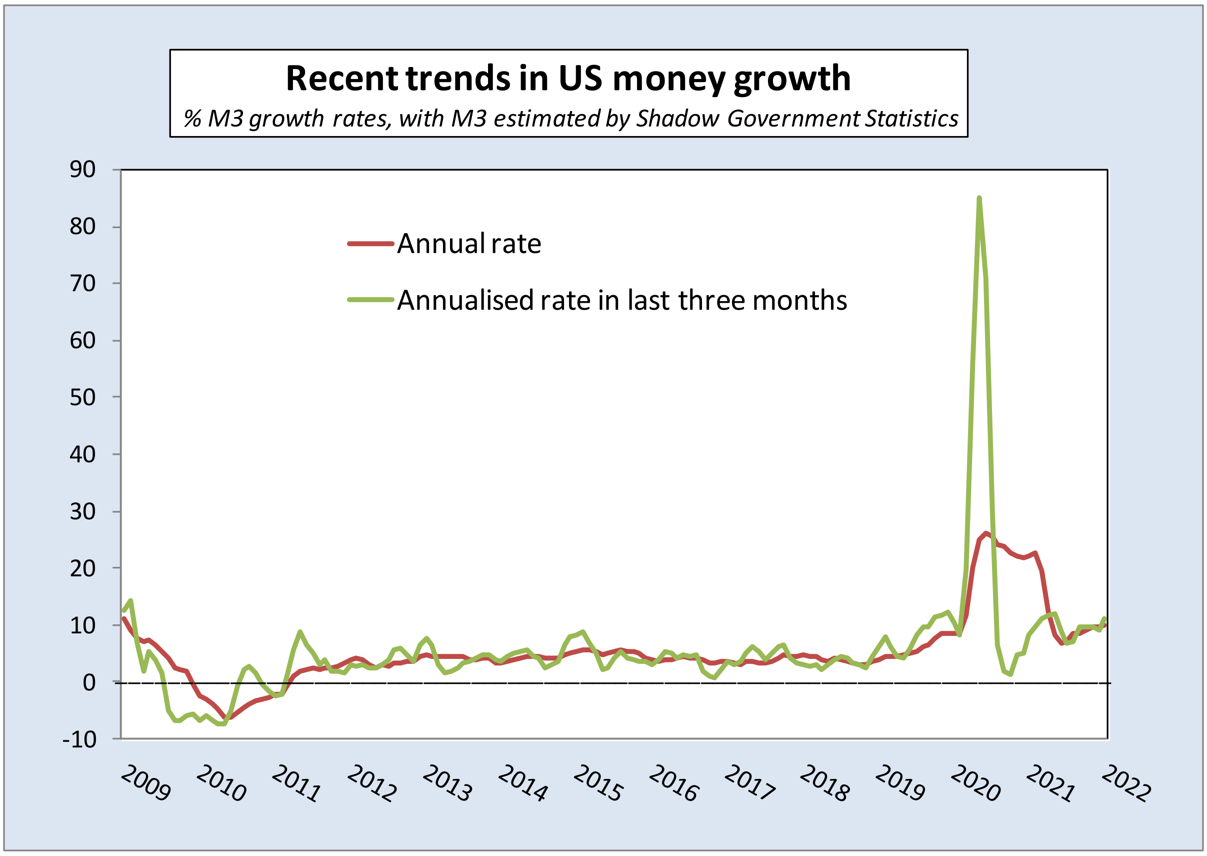
USA

	% annual/annualised growth rate:	
	M3	Nominal GDP
1961 – 2020	**7.7**	**6.3**
Ten years to 2020	**6.2**	**3.4**
Year to January 2022	**9.8**	**n.a**
Three months to January 2022 at annualised rate	**11.2**	**n.a.**

Sources: Shadow Government Statistics research service for M3 after 2006 and US Bureau of Economic Analysis for GDP



US broad money growth remains strong, but will decelerate

Summary: US broad money grew at an annualised rate of 11.2% in the three months to January 2022. In January itself M3 increased by $293b., the second highest reading since June 2020. By comparison, the average monthly M3 increase was $61.2b. in 2018 and even in 2019, when broad money growth accelerated, the average was $135.4b. The annual rate of growth nudged up from 9.6% in December to 9.8%. (Our data come from Shadow Government Statistics.)

The acceleration in broad money growth in the second half of 2021 was caused partly by a significant resurgence in lending by US banks. (When banks extend new loans, they usually create new deposits [i.e., money] on the other side of the balance sheet.) The resurgence took place while the Fed's asset purchases were ongoing. The asset purchases have been reduced since November and will cease at the end of March. The increase in "loans and leases" (i.e., bank lending to the private sector) faded slightly in January and February, perhaps because of the Omicron variant. But another upturn has occurred in recent weeks. In the 13 weeks to 9th March loans and leases grew at a high annualised rate of 11.8%.

Since loans and leases are the largest single category of bank assets, the message is that US money growth will continue when the Fed asset purchases stop. That conclusion is reinforced by the Treasury's need to finance its continuing deficit. According to the International Monetary Fund, the USA's general government deficit was 10.8% of GDP in 2021, and will still be 6.9% of GDP this year and 5.7% in 2023. In the year to 9th March holdings of Treasury and agency securities at US commercial banks climbed by a remarkable 18.2%, from $3,956b. to $4,675b. The increase reflected the large imbalance in Federal finances, which could no longer be blamed entirely on the Covid emergency. The Biden administration has committed to extra infrastructure spending. Understandably, in the partisan political debate Republicans are claiming that the alarming jump in inflation is due to government over-spending.

Money growth will slow down from here, despite the vigour of bank credit to the private sector and some monetary financing of the budget deficit. High inflation will persist, as the lags between money and inflation are – to recall Milton Friedman – "long and variable". Inflation on the consumer price index was 7.9% in the 12 months to February, the highest reading in over 40 years. A rise to double digits in the coming months is inevitable, not just because of the impact of the Ukraine tragedy on energy and food prices, but also because product and labour markets in the USA are overheating. Responding to the rise in prices, the Federal Open Market Committee announced a 0.25% increase in the Fed Funds Rate at its meeting on 15th and 16th March. Its next meeting will include a statement about plans to run down the assets purchased in the last two years. Two weeks before the FOMC meeting, Fed chair, Jerome Powell, told Congress that high inflation was not related to the surge in broad money growth.

Tim Congdon and John Petley
21st March,2022

	% annual growth rate:	
	M3	Nominal GDP
1961 – 2020	**7.7**	**6.3**
1961 – 1970	**8.0**	**7.1**
1971 – 1980	**11.4**	**10.3**
1981 – 1990	**7.7**	**7.7**
1991 - 2000	**5.6**	**5.6**
2001 - 2010	**7.1**	**3.9**
2011 - 2020	**6.2**	**3.4**

China

	% annual/annualised growth rate:	
	M2	Nominal GDP
1991- 2020	**18.4**	**14.5**
2011 - 2020	**11.7**	**10.0**
Year to February 2022	**9.0**	**n/a**
Three months to February 2022 annualised rate	**9.6**	**n/a**

Sources: People's Bank of China for M2, IMF and Institute's own estimates

Broad money growth settles at pre-pandemic levels

***Summary*: In the three months to February 2022 China's seasonally adjusted M2 grew at an annualised rate of 9.6%. This is lower than January's reading of 10.1%, although still higher than any of the figures in the first half of 2021, which ranged between 7.0% and 9.0%. The annual growth rate declined from 9.5% to 9.0%. This is above the average increase for 2021, although not by much.**

For the better part of a year the Chinese money numbers have been similar to those in the two/three before the pandemic. The fiscal and monetary stimuli of 2020 were relatively modest and short-lived. Consequentially, although the stock market surged in 2021, the effect on inflation has been negligible thus far. Consumer prices rose by only 0.9% in the year to February, unchanged from January's reading. Food prices are falling. The increase in producer prices, which rose by 13.5% in the year to October, is easing, which suggests that much of the cost surge has been absorbed by industry. Indeed, there appears to be a slowdown in several sectors of the economy. Property prices in China's 70 largest cities increased by only 2.3% in the year to January, the slowest rate of increase in over six years. Admittedly, part of this slowdown has been deliberately engineered by the Chinese government, which is keen to exclude speculators from the market. But the recent well-publicised woes of some of the country's largest property developers argue that the housing market is likely to remain subdued.

There is also a slowdown in the growth of lending by Chinese banks. An 11.4% increase in new credit in the year to February is the lowest figure in some 20 years. In order to boost the stock of new loans, the People's Bank of China has reduced two of its main lending rates since the start of 2022 after having cut banks' cash reserve ratios by 0.5% in November 2021. Yi Gang, the central bank's governor, insisted that monetary policy would remain accommodative. Given that the inflation target is 3%, there is scope for further loosening if it is felt necessary.

Although China held a ceremony as far back as September 2020 to commemorate the end of the pandemic in the country, the celebrations have proved premature. Several Covid-19 outbreaks have since occurred in several parts of the country and been dealt with by localised but strict lockdowns. In mid-March 2022 no fewer than 30 million people were locked down, including 12.5 million in the technology centre of Shenzhen. If further outbreaks continue to be recorded, this could slow the economy in the coming months. Thus far, the manufacturing sector has remained buoyant, with production 7.5% higher in February 2022 than 12 months earlier. Retail sales also continue to record strong growth.

John Petley
15th March, 2022

	% annual growth rate:	
	M2	Nominal GDP
1991 - 2000	**24.5**	**18.5**
2001 - 2010	**18.4**	**15.2**
2011 - 2020	**11.7**	**10.0**

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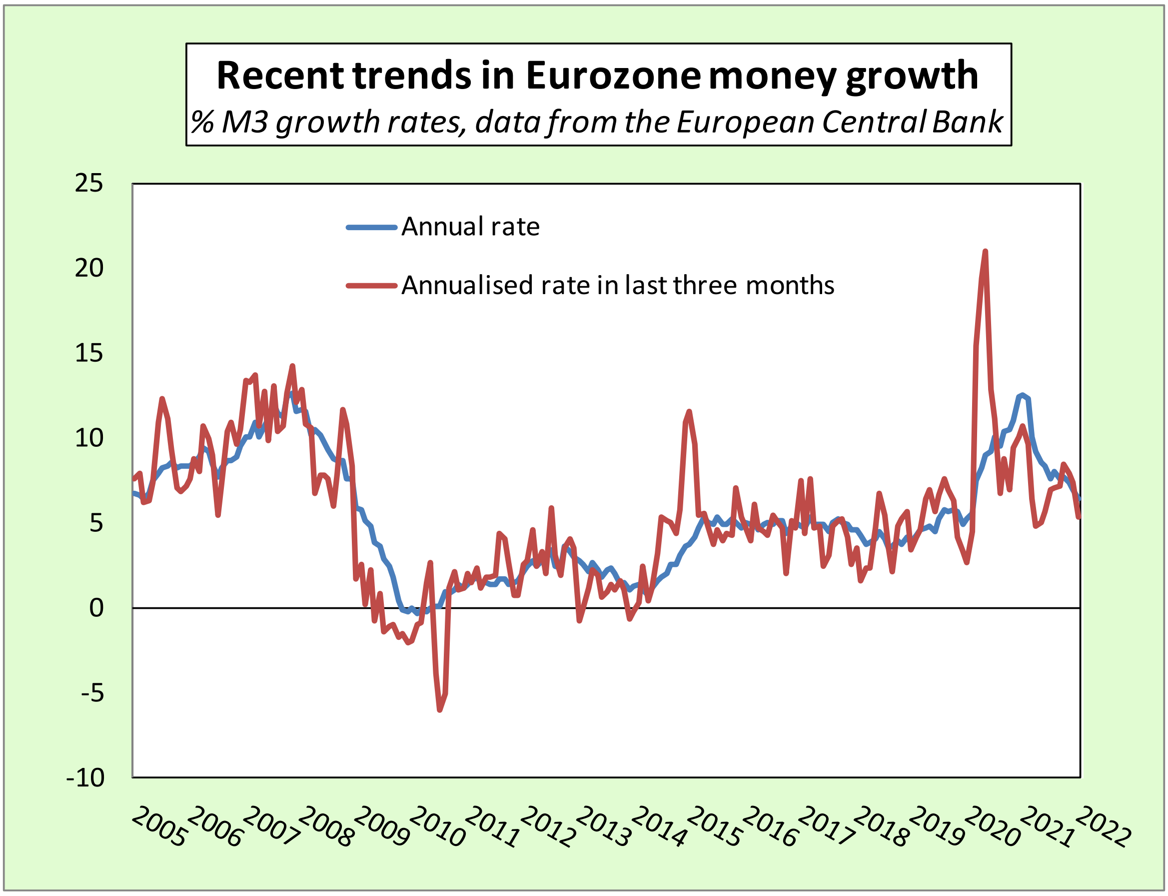
Eurozone

	% annual/annualised growth rate:	
	M3	Nominal GDP
1996 – 2020	**5.5**	**2.7**
Ten years to 2020	**4.6**	**1.6**
Year to January 2022	**6.4**	**n/a**
Three months to January 2022 at annualised rate	**5.4**	**n/a**

Sources: European Central Bank, Eurostat and the Institute's own estimates



Broad money growth deceleration continues

***Summary*: In the three months to January 2021 the quantity of M3 broad money in the Eurozone grew at an annualized rate of 5.4%. Seven consecutive months of accelerating broad money growth saw the three monthly annualised rate reach 8.5% in October 2021 before the quite recent decline to a more moderate figure. The annual growth rate also continued to slow, falling from 6.9% in December to 6.4%, the lowest reading since February 2020.**

Broad money growth remained buoyant until last autumn, but is now moderating. It may decline further. At its meeting on 10th March the ECB's Governing Council reaffirmed its commitment to end the Pandemic Emergency Purchase Programme (PEPP) at the end of the month. (The PEPP had been a response to the Covid 19 emergency, which began in March 2020.) Asset purchases have been "tapered" for several months now. In July the ECB purchased €87.5b. in assets; by December the monthly purchases had fallen to €49.4b.; and February's figure was €40.2b. A separate asset purchase programme dating from 2019 was to have been boosted by €20b. for three months starting in April as a precautionary measure. Now, after the purchase of €40b, in assets in April, the figure will decline to €30b. in May and €20b. in June, after which it too may be terminated. The ECB does not plan to run off these assets until the end of 2024 at the earliest, nor does it plan to raise interest rates until (to quote) "some time after the end of asset purchases".

Consumer prices rose by 5.8% in the year to February, the highest inflation rate since the launch of the single currency. This figure is likely to be surpassed in coming months. Above-target inflation is likely to persist for several quarters, despite the current deceleration in broad money growth. The problem – as in other developed economies where the central banks indulged in asset purchases to meet the Covid-19 threat – is the time lag between monetary policy actions and the inflationary response. Milton Friedman usually referred to a lag of two years, but in practice it can be even longer. On 10th March Christine Lagarde, the ECB President, acknowledged that "inflation had continued to surprise on the upside". She made no reference to the double-digit annual growth rate of money recorded in early 2021, but instead highlighted an unexpected surge in energy costs.

If the ECB wishes to avoid a serious and continuing overshoot of its 2% inflation target, the annual rate of broad money growth needs to be between 1% and 5%. Since March 2020, it has been higher than this in every month apart from April 2021, sometimes considerably so. While the war in Ukraine and the resultant sanctions on Russia has pushed up energy costs, it needs to be stressed, first, that they were rising before the conflict began and, second, countries which did not see such significant surges in broad money growth in 2020 and 2021, such as China, South Korea and Japan, are not seeing anything like the same increases in consumer inflation. High inflation may result in the ECB facing considerable pressure to tighten monetary policy drastically, especially from member states currently suffering higher inflation than the Eurozone average. (Prices rose by no less than 14.2% in Lithuania in the year to February, 12.0% in Estonia and 7.6% in Spain.)

John Petley
14th March, 2022

	% annual growth rate:	
	M3	Nominal GDP
1996 – 2020	**5.5**	**2.7**
1996 – 2000	**4.6**	**4.1**
2001 – 2010	**6.8**	**3.1**
2011 - 2020	**4.6**	**1.6**

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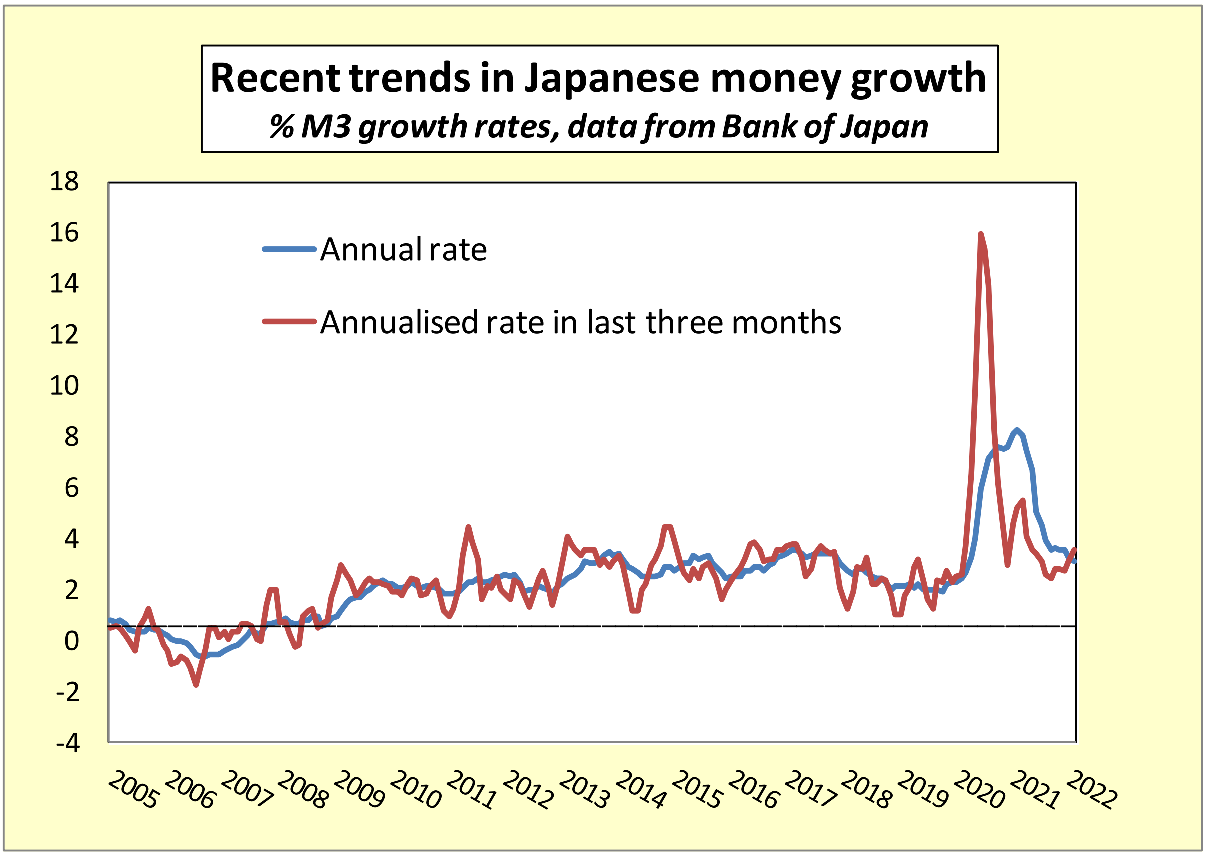
Japan

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2020	**3.9**	**1.7**
Ten years to 2020	**3.2**	**0.3**
Year to February 2022	**3.1**	**n/a**
Three months to February 2022 at annualised rate	**3.5**	**n/a**

Sources: Bank of Japan for M3 and IMF for GDP



Broad money growth picks up slightly

Summary: **The three months to February 2022 saw Japanese M3 increase at an annualised rate of 3.5%. Since the start of 2022, broad money growth has picked up, increasing by 61 trillion yen in January and 45 trillion in February. These figures are higher than the typical numbers in the previous decade, but nowhere near as high as the exceptionally high growth in M3 in the spring of 2020. The annual rate of M3 growth fell from 3.5% to 3.1%.**

After suffering a rise in coronavirus cases in January and February, Japan intends to lift all restrictions on 21st March. The country has avoided full-blown lockdowns, with businesses largely remaining open throughout the last two years. The economy grew by a modest 1.1% in the final quarter of the year, with the retail sector expanding for the fourth consecutive month. Inflation remains very low. Consumer prices rose by only 0.5% in the year to January, a decline from December's 0.8%, which was the highest reading in two years.

The continuation of very low inflation in Japan – despite the yen's decline by over 15% against the US dollar during 2021 and the rise in commodity prices – offers a strong argument in favour of broad money being the principal determinant of nominal national income and wealth. As Japan is the world's fifth largest importer of crude oil, the recent surge in energy prices plus the weaker yen should have pushed up producer prices significantly. February indeed saw an annual rate of increase of 9.3%, the highest since May 1985. Thus far, however, companies have absorbed much of the extra costs, and prices in the shops and on websites have not changed greatly. However, a rise in inflation is likely and the Bank of Japan may finally – later in 2022 – reach its long-standing target of a 2% annual increase in consumer prices. But the figure will be modest compared with the double-digit inflation to be envisaged in other advanced economies. The importance of money growth to inflation over the medium term finds further confirmation.

At a time when other economies have started tightening monetary policy, the Bank of Japan has confirmed its intention to continue with its very accommodative policy. Growth in new credit to businesses is extremely weak. The stock of loans by Japanese banks grew by a mere 0.4% in the year to February, the lowest rate of growth in almost a decade. Japanese exports are performing well, up by 19.1% in the year to February, but the rest of the economy is only growing at a moderate rate. Retail sales were up by 1.6% in the year to January and the growth in housing starts seems to be slowing after surprisingly a strong showing in 2021, given the country's demographics. Unemployment stands at a mere 2.8%, although this is higher than the 2.4%- 2.5% typical of the two years before the pandemic. There is little upward pressure on wages, in spite of a steady increase in job vacancies during 2021.

John Petley
16th March, 2022

	% annual growth rate:	
	M3	Nominal GDP
1981 – 1990	**9.2**	**4.6**
1991 - 2000	**2.4**	**1.1**
2001 - 2010	**1.0**	**0.8**
2011 - 2020	**3.1**	**0.3**

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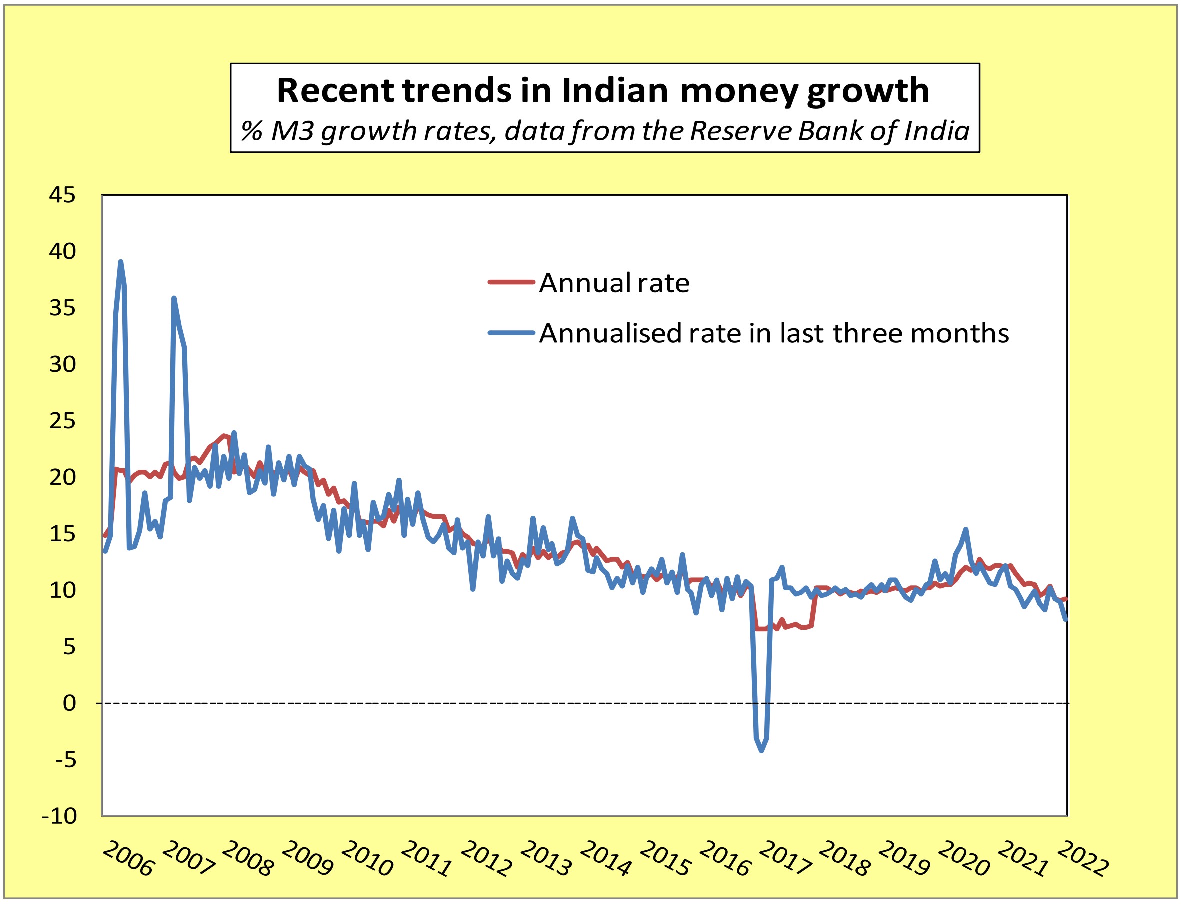
India

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2021	**15.7**	**13.1**
Ten years to 2021	**11.0**	**10.0**
Year to February2022	**9.2**	**n/a**
Three months to February 2022 at annualised rate	**7.4**	**n/a**

Sources: Reserve Bank of India for M3 and IMF for GDP



Broad money growth has been falling, despite bullish 2022 GDP forecasts

Summary: **In the three months to February 2022 India's seasonally adjusted M3 grew at an annualised rate of 7.4%. After increasing by 10.2% in the three months to November 2021, M3 growth has declined in each subsequent month and now stands at its lowest level since February 2017. The annual growth rate which had also been slowing since November, steadied in February however. It rose slightly from 9.1% to 9.2%.**

After suffering badly from the coronavirus pandemic in the first half of 2021, the Indian economy recovered strongly in the latter part of the year, particularly in the third quarter, which saw growth of 12.7%. But these oscillations need to be set in a medium-term context. According to the International Monetary Fund database, GDP grew by on average by an impressive 7.4% in the five years 2014 – 18 inclusive. But 2019, before Covid, reported a more modest increase of 4.0%. Covid was then largely responsible for a GDP plunge of 7.3% in 2020. The IMF gives a 2021 GDP rise of 9.5%. So the average GDP growth rate in the three years to end-2021 was mediocre, at under 2%. The IMF then envisages a 8.5% gain in 2022, and robust growth thereafter at about 6% a year. The Indian stock market certainly agrees with this optimism, as it soared in late 2020 and 2021 from a Covid-related low in April 2020.

The bullish case for India is well-known, with its young population and striking economic dynamism since the liberalizations of the 1990s. However, worries have grown about the increasingly narrow-minded "Hindutva" (i.e., Hindu nationalist) agenda of the BJP, the governing party, and Narendra Modi, who has been prime minister since 2014. The BJP's economic policies are meant to be supportive of the free market, and the government has – for example – taken courageous and unpopular decisions to reduce misguided agricultural subsidies. But it has also imposed new restrictions on imports, even failing to participate in regional free trade programmes. On 10th March the BJP enjoyed electoral success in the important Uttar Pradesh state election and it has extra momentum from that.

Given the numerous forecasts of GDP growth of 8% or more in 2022, the reduction in money growth now being reported just does not fit. As inflation has been consistently 5% or so for several years, and is expected to be somewhat higher in 2022 because of global commodity price developments, 8% real GDP growth implies a nominal GDP increase of, say, 15%. In India – as elsewhere – nominal GDP and the quantity of money are related, because of the stability of agents' money-holding preferences. The explanation for the money slowdown seems to be mostly that the Reserve Bank of India is putting pressure on commercial banks to recognise non-performing loans and to operate with capital/asset ratios that are nearer to international norms (i.e., higher than before), particularly norms laid down by the Bank for International Settlements. A recent admission by the Punjab Bank that it has suffered from a total of 1,142 defaults totalling 239b. rupees (over \$3b.) comes as a reminder of the strains in Indian banking. The RBI sees itself as having the task of improving the banking culture without denying the economy the liquidity and dynamism it needs.

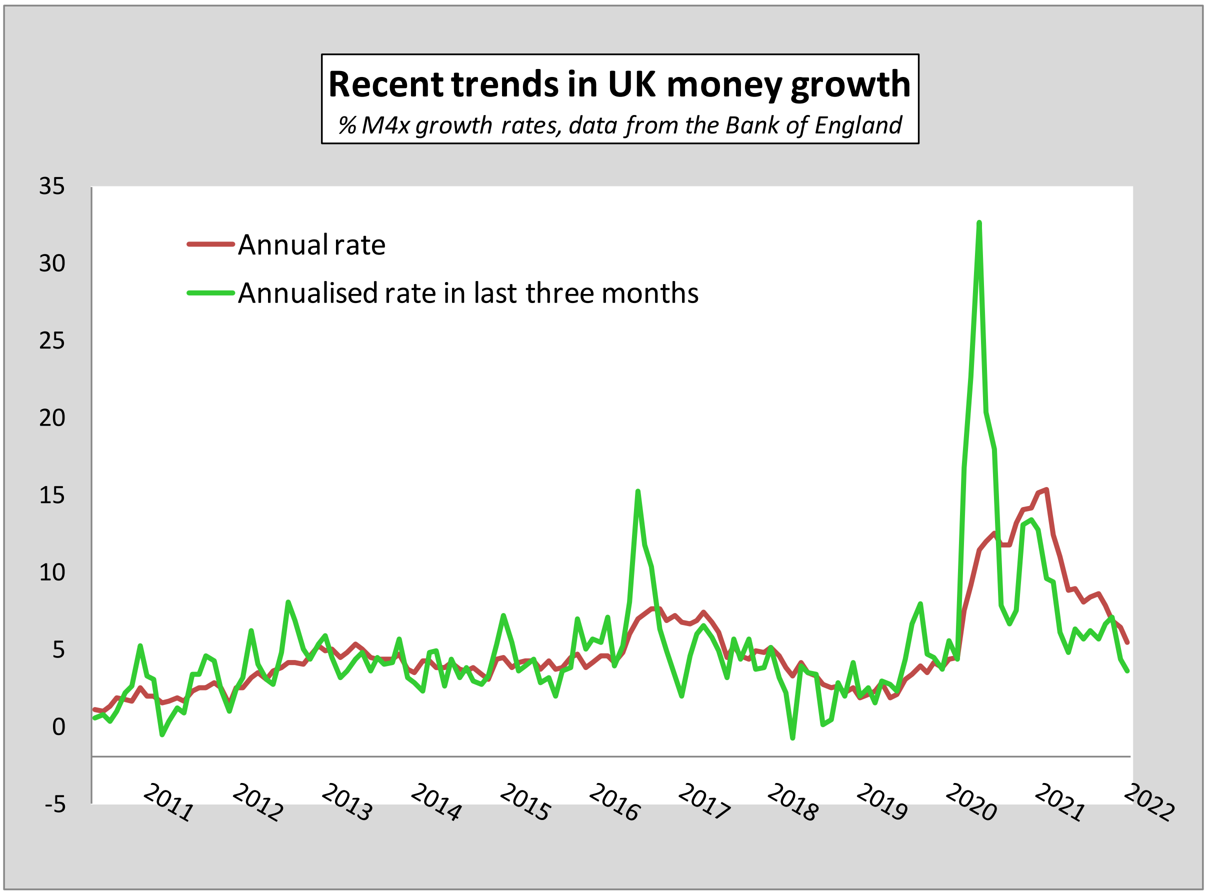
Tim Congdon
21st March, 2022

	% annual growth rate:	
	M3	Nominal GDP
1981 - 1990	**17.3**	**14.7**
1991 - 2000	**17.2**	**14.1**
2001 - 2010	**17.3**	**13.6**
2011 - 2020	**11.6**	**9.9**

UK

	% annual/annualised growth rate:	
	M4x/M4 before 1997	Nominal GDP
1961 – 2020	**9.3**	**7.6**
Ten years to 2020	**5.2**	**2.3**
Year to January 2022	**5.4**	**n/a**
Three months to January 2021 at annualised rate	**3.6**	**n/a**

Sources: Bank of England and Office for National Statistics



Broad money growth back to pre-pandemic levels

Summary: **In the three months to January 2022, UK M4x broad money increased at an annualised rate of only 3.6%. This is the smallest increase – on the three-month annualised measure – since June 2019, nine months before the start of the coronavirus pandemic.**

The coming months are likely to see higher inflation, but much lower broad money growth. The UK economy at present provides a classic illustration of the time lag between changes in the quantity of money and the resultant effects on consumer prices. The dominant causal influence on the current upturn in inflation – evident in the rise of 5.5% in consumer prices in the year to January – is the acceleration in broad money growth in 2020. To remind, the annual increase in M4x – which had averaged 4.4% in the five years 2015 – 2019 inclusive – reached 15.1% in January 2021 and was still 8% last autumn. Three Bank rate increases have been announced since December, but inflation will remain on an upward trend for a few quarters. The economy remains very busy as people and companies compensate for work not done during the Covid-19 emergency, while the damage from international commodity price rises will be aggravated by the Ukraine tragedy.

The inflationary surge may not subside until 2023, but by then the UK economy may be facing another problem. On 13th December 2021, the Bank of England increased the countercyclical capital buffer for UK banks by 1%, with the decision to take effect in December 2022. The Bank's website states that this tool is used when "it judges that risks are building up" and provides banks with "an additional cushion of capital". However, the requirement for extra capital also acts as a disincentive for banks to lend. (It also may cause banks to shift capital to foreign businesses or to UK non-bank activities.) Already January's money and credit statistics showed weakness in credit growth. The stock of loans to non-financial companies increased by only £1.0b. in January after falling by £0.6b. in December, and in January 2022 it was a mere 0.2% higher than a year earlier. Total bank lending to the UK economy did increase in that year, but this was due entirely to lending to households, mostly for mortgages. Money growth arising from new bank credit to the private sector will be weak in 2022, and may well remain so while the regulatory regime – based on the Basel III capital rules – is so hostile.

The Bank of England is now reducing its holdings of government securities, built up by the asset purchases of 2020 and 2021. It has already run off approximately £28b. of the government bonds it purchased in the last two years, which will to some extent lower the quantity of money. The risk is now that money growth falls too soon and too sharply, so that boom becomes bust. Rishi Sunak's November 2021 Budget, with its increase in National Insurance (to raise £12b. a year), suggests that he wants to bring government spending under control.

Tim Congdon and John Petley
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	% annual growth rate:	
,	M4/M4x	Nominal GDP
1961 - 2020	**9.3**	**7.6**
1991 – 2000	**6.4**	**6.0**
2001 – 2010	**6.5**	**3.9**
2011 – 2020	**5.2**	**2.3**