INSTITUTE OF
INTERNATIONAL
MONETARY RESEARCH

Federal Open Market Committee meeting, US Fed. 03-04/05/2022

FOMC increases the Fed Funds Rate by 0.5%.

Confronted with consumer price inflation at a 40-year high of 8.5% in the year to March, the FOMC followed up its 0.25% increase in the Fed Funds Rate last March with a further increase, this time of 0.5% on 4th May, taking borrowing costs up to 0.75% - 1%. It also announced that on 1st June, it will stop fully re-investing maturing assets purchased over the last two years. For three months, $30b. worth of Treasuries and $17.5b. of mortgage-backed securities will be "run off" and from 1st September, these quantities will be doubled. Fed Chairman Jerome Powell indicated that further rate rises were likely before the end of 2022, "Inflation is much too high and we understand the hardship it is causing, and we're moving expeditiously to bring it back down", he said at the Press Conference following the FOMC meeting, adding that "It anticipates that ongoing increases in the target range will be appropriate."

Broad money growth is declining and this trend is likely to accelerate in the coming months. Annualised quarterly M3 growth stood at 6.1% in the three months to March 2022, the final month in which the Fed purchased any assets. The annual growth rate fell to 8.2%, the lowest reading since October 2019. The Fed rightly recognises that raising interest rates and running off its asset purchases will bring down inflation, but because it takes precious little interest in the money supply, it is in danger of "closing the stable door after the horse has bolted." The seeds of the current inflationary spike were sown two years ago when broad money growth accelerated at a rate unparalleled since the end of the Second World War. As Milton Friedman observed, there is always a lag between a surge in the money supply and its effect on prices. No matter how drastically the Fed tightens monetary policy now, it will take a while for inflation to subside – indeed, high inflation may well persist into 2024 or even 2025. The biggest concern is that in its frustration over the failure of inflation to come down rapidly, the Fed may push up the Fed Funds Rate too rapidly and provoke a serious recession.

You can access further details on the latest monetary developments in the USA in our latest **monthly report and video** at https://mv-pt.org/monthly-monetary-update/