

Federal Open Market Committee meeting, US Fed. 13-14/12/2022

Fed Funds rate increased by 0.5%.

The Federal Open Market Committee voted unanimously to increase the Fed Funds Rate by 0.5% during its meeting at the start of November. The cost of borrowing has now been raised from zero to 4.25% - 4.5% since the start of the year and now stands at its highest level since 2007. Significantly, this increase is smaller than the previous four rate hikes, all of which were 0.75%. The statement from the FOMC following the meeting stressed that further increases may be necessary so that inflation can be reduced to the Fed's 2% target. CPI rose by 7.1% in the year to November, the most modest annual increase this year.

The Fed remains optimistic that the US economy will enjoy a “soft landing” – in other words, for inflation to return to target without inducing a recession. In the press conference following the FOMC meeting, Fed Chairman Jay Powell pointed to the tight labour market and mentioned that although the housing market is slowing and consumer spending is also declining, the Fed currently projects that real GDP growth will be 0.5% in 2023 – modest but still positive.

He stressed that further rate rises will be accompanied by a continuation of the run-off of assets purchased during 2020, which amount to \$95b. in total every month. As has often been pointed out in these notes, today's Fed takes no interest in the quantity of money when deliberating monetary policy. If it did, its projections would look rather different. According to the Shadow Government Statistics organisation, US M3 declined by \$329b. or 4.6% in the three months to October. The annual growth rate fell to 1.4%, an 11-year low. October itself saw M3 contract by \$201b. *No single month in the Great Recession of 2008-10 saw such a massive fall in the quantity of money, broadly defined.* These notes predicted several months ago that “Quantitative Tightening” currently being implemented by the Fed could cause M3 to shrink by \$50b. each month in and of itself, regardless of any other factors and so it has proved.

Increased borrowing costs have thus far had only a modest effect on the creation of new credit by US banks. “Loans and leases in bank credit”, a set of figures produced by the Fed which corresponds to bank lending, indicates that the recent strong growth in the stock of bank loans is continuing. The level of both real estate loans and borrowing by businesses was up by more than 10% in the year to November. If these substantial increases in the Fed Funds Rate begin to deter borrowing, the decline in broad money could become more severe as the creation of new bank credit is now the main driver of M3 growth. Already, the money numbers strongly suggest that the USA will experience a recession in 2023 and if the contraction in M3 becomes more severe, so could the depth and duration of that recession.

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