INSTITUTE OF
INTERNATIONAL
MONETARY RESEARCH

Federal Open Market Committee meeting, US Fed. 31/01-01/012/2023

Fed Funds rate increased by just 0.25%.

The Federal Open Market Committee voted unanimously to increase the Fed Funds Rate by 0.25% during its first meeting of 2023. In the space of a year the cost of borrowing has now been raised from zero to 4.5% - 4.75% and now stands at its highest level since 2007. After scaling back from a run of 0.75% increases to 0.5% in December, the FOMC was unanimous in backing a smaller increase in borrowing costs, but Chairman Jerome Powell stressed that further increases would be appropriate in the forthcoming months. The statement from the FOMC following the meeting stressed that the Fed still stands by its commitment to bring inflation down to the official 2% target. The CPI rose by 6.5% in the year to December, well above this target but nonetheless a welcome slowing from June's peak of 9.1%.

The US labour market is still tight and average mortgage rates have actually fallen back from a peak of over 7% in November. Statistics like these have led to optimism both within the FOMC and the wider commentariat that the recent below-trend growth in the US economy in recent months will not turn into a recession.

The monthly $95b. run-off of assets purchased during 2020-22 will continue. The Fed appears to be oblivious that this is causing a very sharp decline in broad money. In the final quarter of 2022, M3 shrank at an annual rate of 3.9%. December also saw the *annual* rate of money growth drop into negative territory. This has not happened since 2009-10. What is particularly worrying is that this period was characterised by a loosening of monetary policy including reductions in the Fed funds rate. The current decline on broad money is taking place against a background of *increasing* borrowing costs and there is no indication that the Fed intends to change its policy until inflation drops back close to 2%. (Powell emphasised that he wanted to stop higher inflation expectations becoming anchored). Given that there is still a monetary overhang in the wake of the huge growth in M3 during 2020, it looks likely that it will take much of 2023 for this objective to be realised. The outlook therefore would appear to be a several further months of broad money shrinkage. Given the substantial evidence which the Institute of International Monetary Research has gathered emphasizing the link between changes in the quantity of money and their effects on asset prices, inflation and GDP, our assessment of the US economy is much less positive than that of the Federal Reserve. In other words, the money numbers strongly suggest that the USA will experience a recession, possibly before the end of 2023. Furthermore, if the Fed continues with its current policy, that recession could turn out to be quite protracted.

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/