



INSTITUTE OF  
INTERNATIONAL  
MONETARY RESEARCH

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

# What does monetary analysis tell us about inflation prospects in the leading economies?

*June 2021 presentation*

*by Professor Tim Congdon CBE,*

*Chairman of the Institute of International Monetary Research*

*at the University of Buckingham*

# How wrong can you be? –

Initial responses by top mainstream economists to the Covid-19 pandemic – **The FOMC**



## A view from the Federal Reserve's Open Market Committee

- *From the Minutes of the 9 – 10 June meeting:*  
“The [forward-looking] simulations [from the Fed’s research staff] suggested that the Committee would have to maintain highly accommodative financial conditions for many years to quicken meaningfully the recovery from the current severe downturn.”
- Notice the phrase **“for many years”**.

Note that  
this comes  
from June  
**2020**



# The coronavirus pandemic is inflationary

*A presentation by Professor Tim Congdon CBE,  
Chairman of the Institute of International Monetary Research,  
in March 2020*

# The coronavirus pandemic, the quantity of money and asset prices

*May 2020 presentation  
by Professor Tim Congdon CBE,  
Chairman of the Institute of International Monetary Research  
at the University of Buckingham*

# Will the coronavirus cause an inflation

*A presentation by P  
Chairman of the Institute of  
in*

# Putting the coronavirus long-run macro

*July 20  
by Professor Tim Congdon CBE,  
Chairman of the Institute of International Monetary Research  
at the University of Buckingham*

## A quantity-theory/'monetarist' perspective

- Any quantity-theory analyst – looking at the data, and believing in the stability of underlying money-holding behaviour (for which the mean-reversion of changes in velocity, with a low mean value, is crucial evidence) – has to forecast a big rise in American inflation in 2021 and/or 2022.
- The standard macro model usually ignores money altogether, or at best adds it on as an afterthought.



A quote from a **6<sup>th</sup> April 2020**  
special e-mail from the Institute



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## Does the Fed understand what it is doing?

At some point – probably in mid- or late 2021 – the coronavirus crisis will be over...And what will then happen to the ‘excess over normal’ money balances created by public policy in 2020 and early 2021? The answer is that – as in the aftermath of wars – an inflationary boom in the world’s leading economy has to be the central forecast. **It seems to me that a major increase in inflation due to this boom is inevitable. Whether that increase is to 5% or 10%, no one knows for certain yet...**

Paul Krugman in his  
*New York Times* column  
on 21<sup>st</sup> June, **2021**



**The New York Times**

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“...[F]or those paying closer attention to the flow of new information, **inflation panic, is, you know, so last week.** Seriously, both recent data and recent statements from the Federal Reserve have, well, deflated the case for a sustained outbreak of inflation.”

- Krugman does not give a specific inflation number over any definite period, but his endorsement of the Fed has to be interpreted as agreement with the Fed’s current view.

# The Fed's current view



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The 'Press conference' material published just after the June 2021 meeting of the Federal Open Market Committee gave figures on real GDP, unemployment, consumer inflation and core consumer inflation for the years to the fourth quarter of 2021, 2022, 2023 and the 'longer run'.

- **Consumer inflation in the year to Q4 2021 is expected to be in the band '3.1% – 3.5%' and in the years to Q4 2022 and Q4 2023 in the bands '1.9% - 2.3%' and '2.0% - 2.2%' respectively.** So this is presumably also Krugman's position.

# Equilibrium national income depends on the quantity of money and the desired ratio of money to incomes (i.e., the inverse of money velocity)

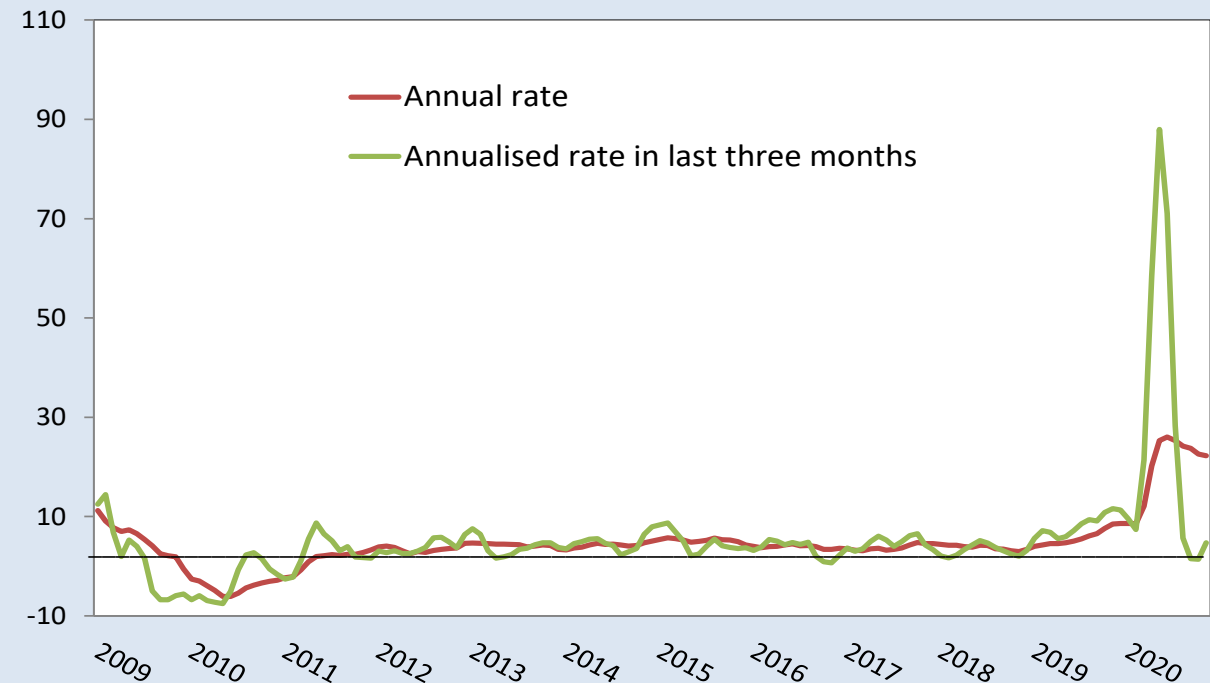
## Income velocity of M3 in the USA: actual, with an extrapolation

		Velocity - actual	Velocity - trend behaviour
1	2018	1.094	1.066
2		1.099	1.065
3		1.099	1.064
4		1.103	1.062
1	2019	1.095	1.061
2		1.090	1.060
3		1.076	1.058
4		1.057	1.057
1	2020	1.029	1.056
2		0.796	1.054
3		0.852	1.053
4		0.855	1.052
1	2021	0.857	1.050
2		?	1.049
3		?	1.048
4		?	1.046
1	2022	?	1.045
2		?	1.044
3		?	1.043
4		1.041 *	1.041

\* This value of velocity is assumed in the text.

## Recent trends in US money growth

% M3 growth rates, with M3 estimated by Shadow Government Statistics



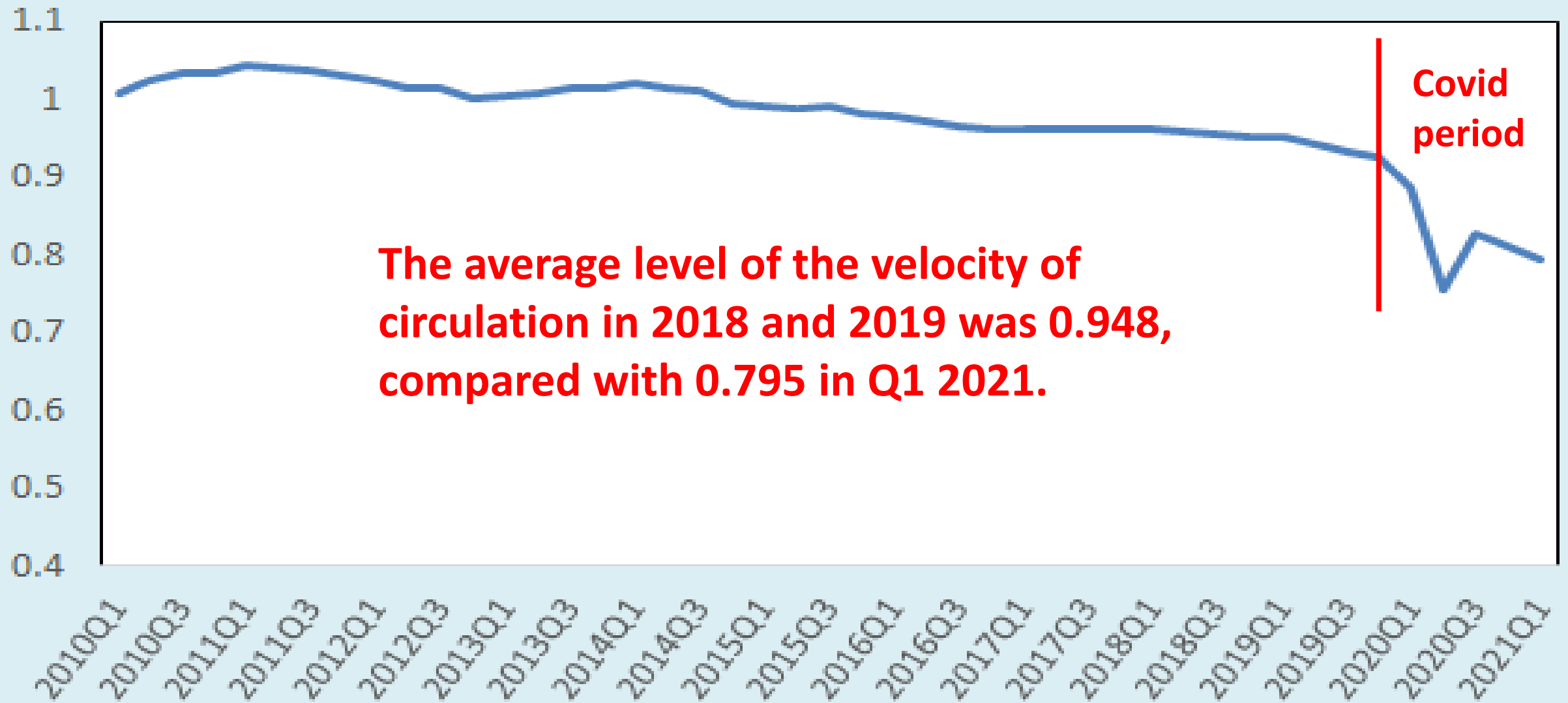


# What does that tell us about the US economy in the next two years?

- Assume that 'life returns to normal' in a medical sense by the end of next year, i.e., the fourth quarter (Q4) of 2022.
- Assume that the velocity of circulation of money, broadly-defined (i.e., M3), is **5% lower** than on average in 2018 and 2019.
- Assume that the growth of money, broadly-defined, runs at 0.4% a month (i.e., a roughly 5% annual rate) from Q1 2021 to Q4 2022.
- **THEN THE IMPLIED EQUILIBRIUM LEVEL OF U.S. NATIONAL INCOME IS ABOUT 30% HIGHER IN Q4 2022 THAN IN Q1 2021. ON THIS BASIS, THE INSTITUTE OF INTERNATIONAL MONETARY RESEARCH EXPECTS THE ANNUAL RATE OF U.S. CONSUMER INFLATION TO BE TYPICALLY IN THE 5% - 10% BAND IN THE NEXT TWO YEARS.**

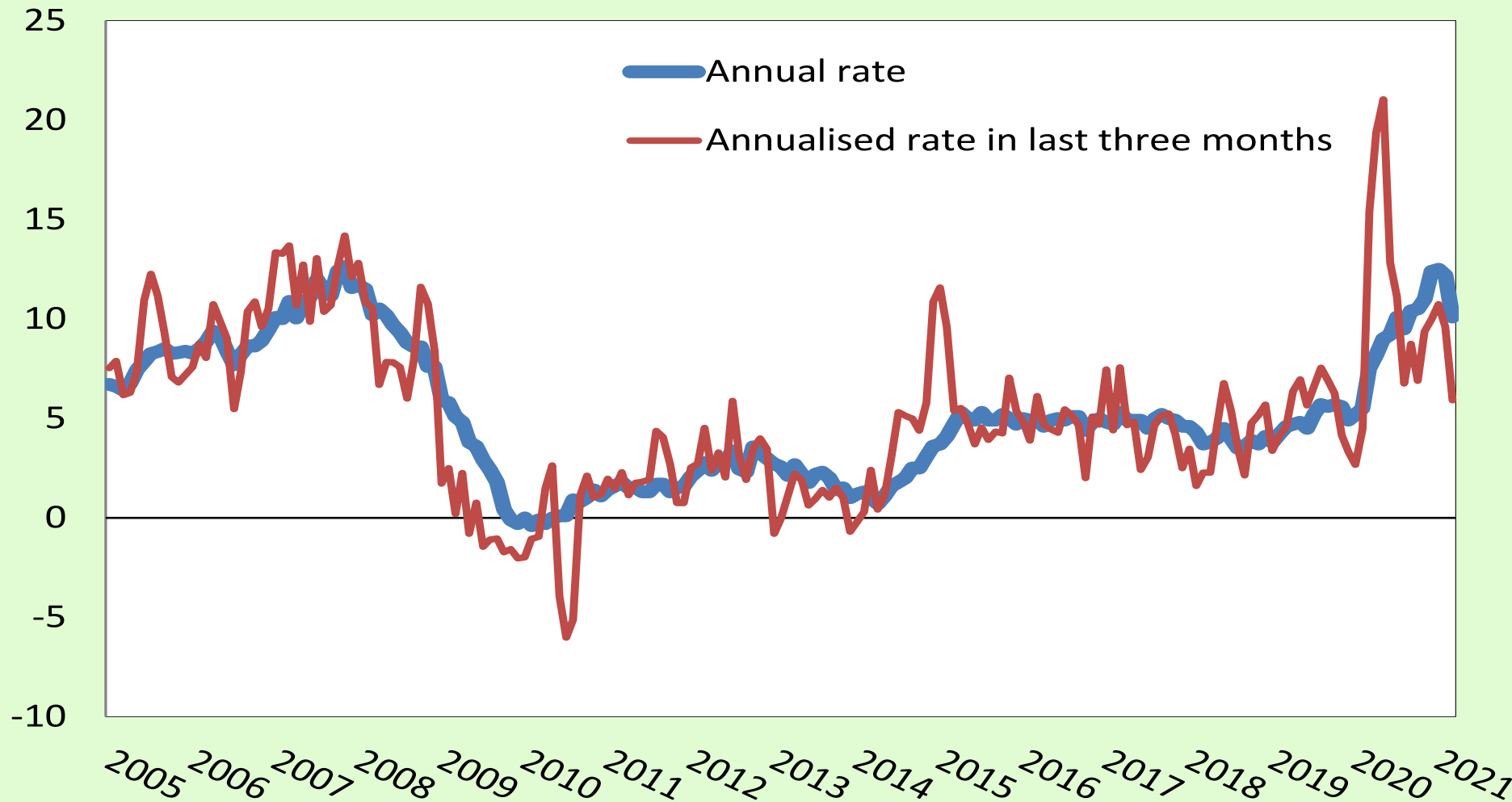


## Velocity of circulation of Eurozone M3



## Recent trends in Eurozone money growth

*% M3 growth rates, data from the European Central Bank*



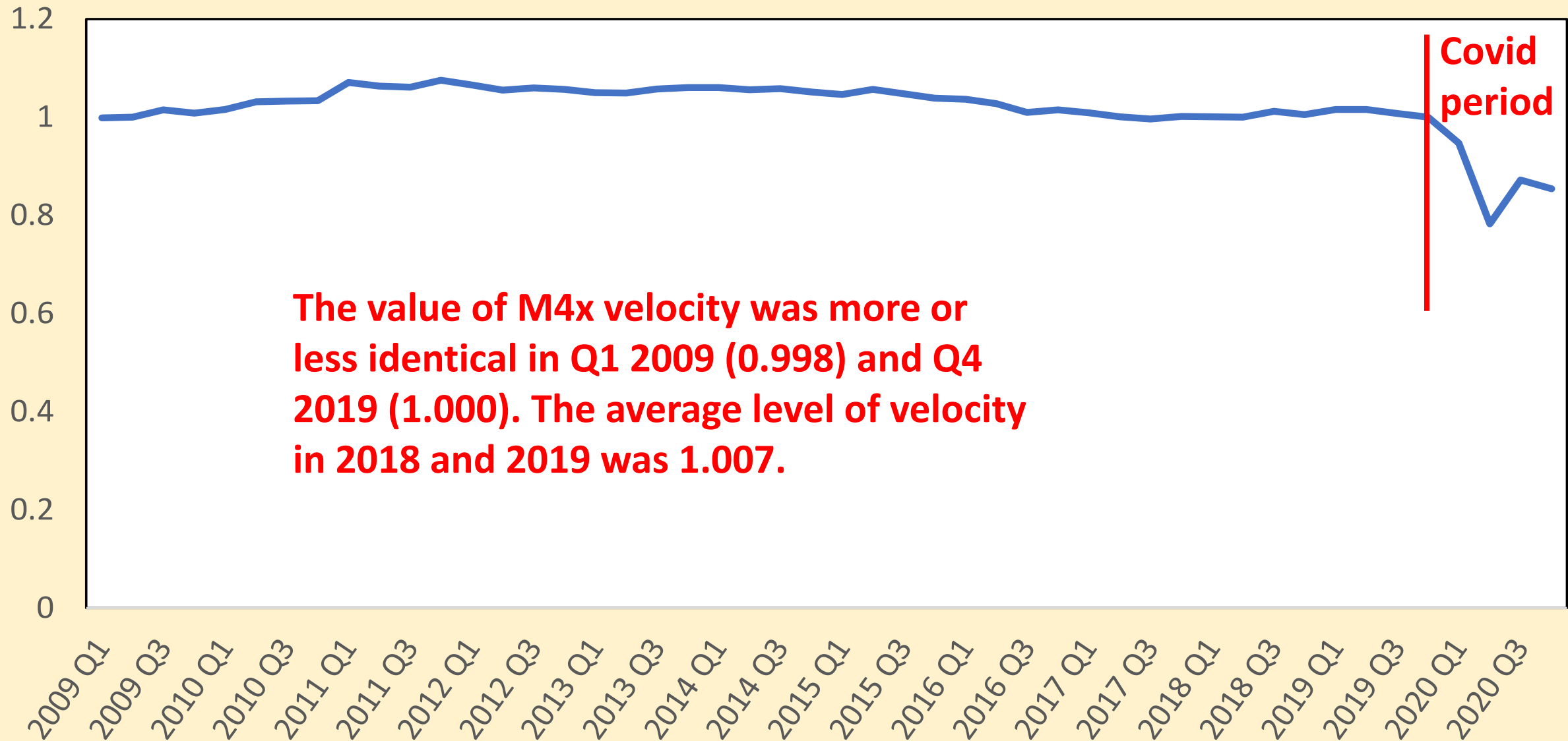
The annual M3 growth rate has recently been the highest since the euro was created in 1999, although only slightly above that in late 2007.

# What does that tell us about the Eurozone economy in the next two years?

- Assume that 'life returns to normal' in a medical sense by the end of next year, i.e., the fourth quarter (Q4) of 2022.
- Assume that the velocity of circulation of money, broadly-defined (i.e., M3), is then **5% lower** than on average in 2018 and 2019.
- Assume that the growth of money, broadly-defined, runs at 0.4% a month (i.e., a roughly 5% annual rate) from Q1 2021 to Q4 2022.
- **THEN THE IMPLIED EQUILIBRIUM LEVEL OF EUROZONE NATIONAL INCOME IS ALMOST 25% HIGHER IN Q4 2022 THAN IN Q1 2021. ON THIS BASIS, THE INSTITUTE OF INTERNATIONAL MONETARY RESEARCH EXPECTS THE ANNUAL RATE OF EUROZONE CONSUMER INFLATION TO EXCEED 5% AT SOME POINT IN THE NEXT TWO YEARS.**



# Velocity of M4x circulation in the UK



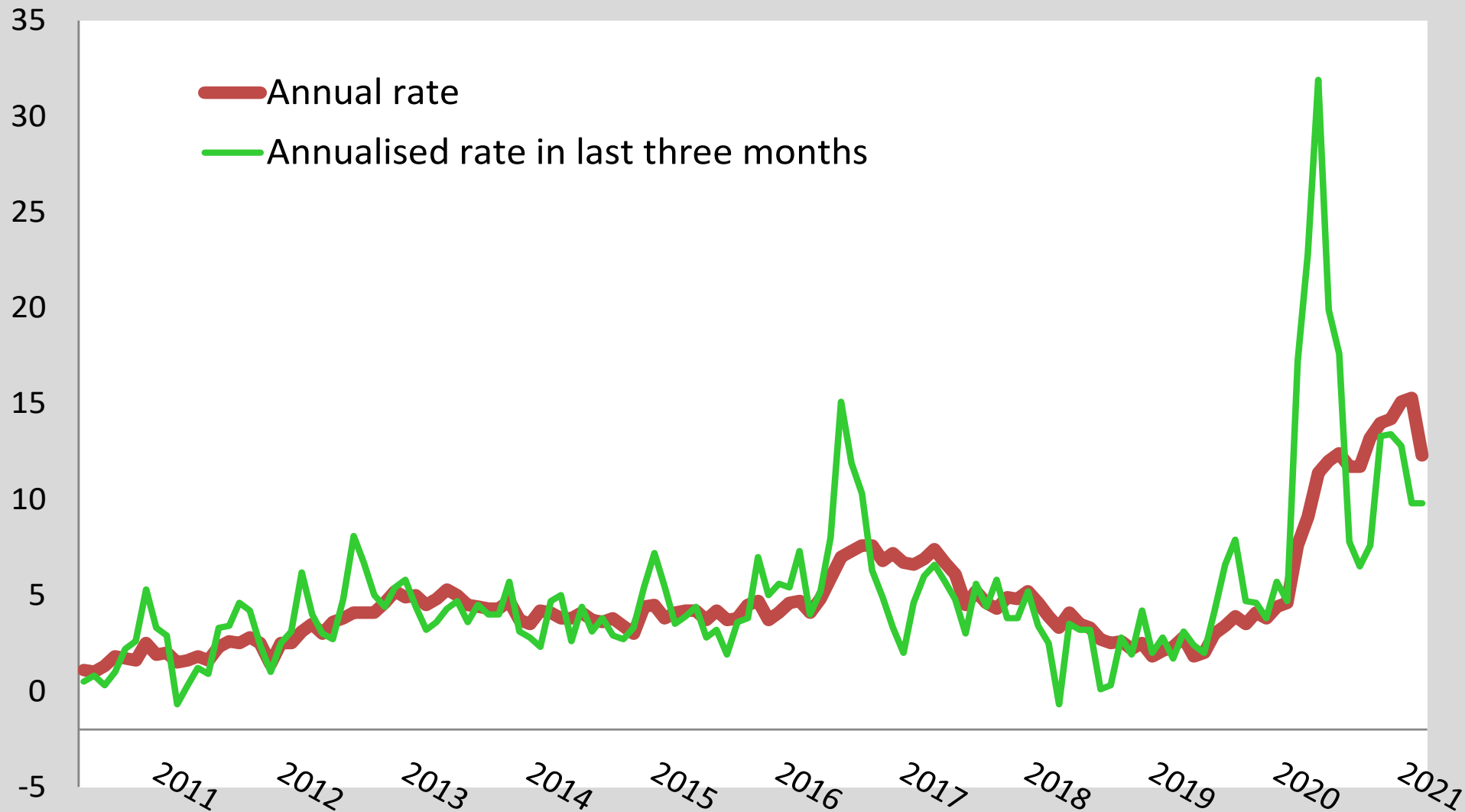
## Recent trends in UK money growth

% M4x growth rates, data from the Bank of England



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The annual M4x growth rate has recently been the highest in the period for which M4x has been calculated. In fact, recent broad money growth has been the highest since the 1980s.

# What does that tell us about the UK economy in the next two years?

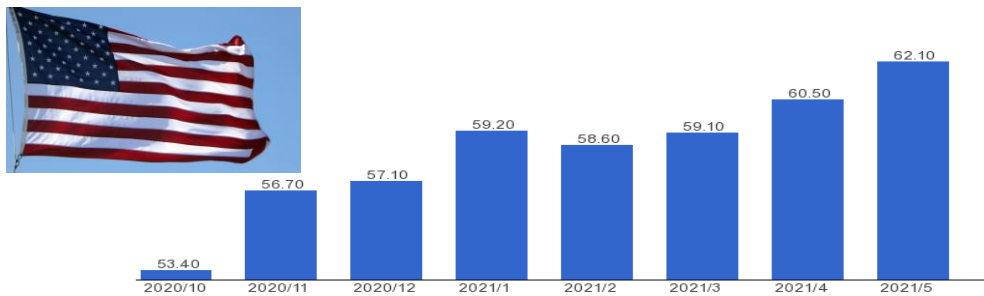
- Assume that 'life returns to normal' in a medical sense by the end of next year, i.e., the fourth quarter (Q4) of 2022.
- Assume that the velocity of circulation of money, broadly-defined (i.e., M4x), is **then 5% lower** than on average in 2018 and 2019.
- Assume that the growth of money, broadly-defined, runs at 0.4% a month (i.e., a roughly 5% annual rate) from Q1 2021 to Q4 2022.
- **THEN THE IMPLIED EQUILIBRIUM LEVEL OF U.K. NATIONAL INCOME IS ALMOST 25% HIGHER IN Q4 2022 THAN IN Q1 2021. ON THIS BASIS, THE INSTITUTE OF INTERNATIONAL MONETARY RESEARCH EXPECTS THE ANNUAL RATE OF U.K. CONSUMER INFLATION TO EXCEED 5% AT SOME POINT IN THE NEXT TWO YEARS.**



# The verdict of business surveys?

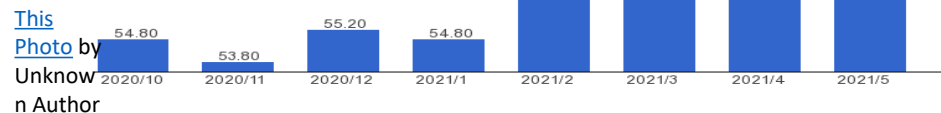
## Purchasing Managers Index (PMI), manufacturing in the USA

**May 2018 - May 2021:** For that indicator, we provide data for the USA from May 2018 to May 2021. The average value for the USA during that period was 53.11 index points with a minimum of 36.1 index points in April 2020 and a maximum of 62.1 index points in May 2021. Click on the following link to see the values of [Purchasing Managers Index \(PMI\), manufacturing](#) around the world.



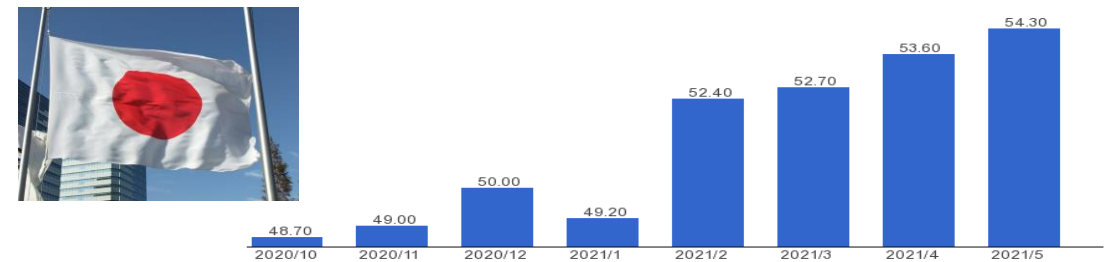
## Purchasing Managers Index (PMI), manufacturing in Euro area

**April 2019 - May 2021:** For that indicator, we provide data for Euro area from April 2019 to May 2021. The average value for Euro area during that period was 50.21 index points with a minimum of 33.4 index points in April 2020 and a maximum of 63.1 index points in May 2021. Click on the following link to see the values of [Purchasing Managers Index \(PMI\), manufacturing](#) around the world.



## Purchasing Managers Index (PMI), manufacturing in Japan

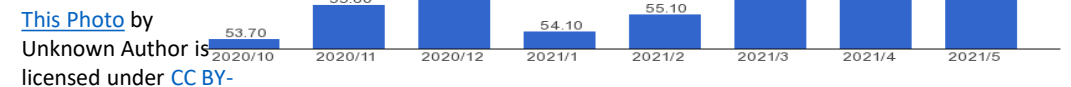
**June 2018 - May 2021:** For that indicator, we provide data for Japan from June 2018 to May 2021. The average value for Japan during that period was 49.17 index points with a minimum of 38.4 index points in May 2020 and a maximum of 54.3 index points in May 2021. Click on the following link to see the values of [Purchasing Managers Index \(PMI\), manufacturing](#) around the world.



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## Purchasing Managers Index (PMI), manufacturing in the United Kingdom

**May 2018 - May 2021:** For that indicator, we provide data for the United Kingdom from May 2018 to May 2021. The average value for the United Kingdom during that period was 52.03 index points with a minimum of 32.6 index points in April 2020 and a maximum of 65.6 index points in May 2021. Click on the following link to see the values of [Purchasing Managers Index \(PMI\), manufacturing](#) around the world.



# The Fed's current view



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The 'Press conference' material published just after the June 2021 meeting of the Federal Open Market Committee gave figures on real GDP, unemployment, consumer inflation and core consumer inflation for the years to the fourth quarter of 2021, 2022, 2023 and the 'longer run'.

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# The Fed's current view



# A digression?

- **Consumer inflation in the year to Q4 2021 is expected by the FOMC to be – in the middle of its range – 3.3%.**
- ***But the increase in the US consumer price index\* between December 2020 and May 2021 was 3.3%!***
- **So the forecast made by the FOMC in June 2021 – in the middle of a big boom, with business surveys reporting very high price-raising intentions by companies – is that consumer prices won't change in the last seven months of the year! (I don't know whether Paul Krugman agrees with this.)**

\* I have used the seasonally unadjusted series. On the adjusted series the increase in the five months was 2.9%.