



## INTERNATIONAL MONETARY RESEARCH LIMITED

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

**Monthly e-mail from Tim Congdon of International Monetary Research Ltd. –  
28<sup>th</sup> June, 2016**

### **Global money round-up in mid-2016**

The victory for the Leave campaign in the UK's referendum on EU membership has dominated financial news since 23<sup>rd</sup> June. It is of course a major event, not least because numerous forecasts of a mini-recession in the UK are now to be tested. The evidence so far is mixed, with the latest survey from the Confederation of British Industry (published a few days before 23<sup>rd</sup> June) reporting a *rise* in the balance of companies planning to expand output in the next three months. Elsewhere the main features are, first, in the developed countries continued growth of broad money at the almost ideal annual rate of 4%, and, second, in China and India signs of a slowdown in broad money growth. The slowdown in both China and India has come about suddenly, and may soon disappear from the data and not prove meaningful. On the other hand, the slowdown could last a few months, perhaps even more. Once a money slowdown/acceleration persists for six months or longer, it starts to matter to the cyclical prospect. My overall assessment is – despite the Brexit shenanigans – the global monetary background remains consistent with steady growth in world demand and output in late 2016 and into 2017. Far too much fuss is being made about Brexit. The UK's share of world output (when output is measured on a so-called "purchasing power parity" basis) is modest, less than 2½ per cent. The credit downgrades faced by British banks have created possible funding strain for them, recalling the crisis of late 2008. The problem needs to be countered by the provision of long-term refinancing facilities from the Bank of England, just as Draghi handled a similar challenge in the Eurozone in December 2011

## Money trends in mid-2016 in the main countries/jurisdictions

What are the latest money growth trends in the main countries? And what is the message for global economic activity over the next year or so, and for inflation/deflation over the medium term thereafter? The table below summarizes the key numbers. For detail, it is recommended that the reader looks at the individual country comments below. Beneath the table I make an overall assessment.

Name of country/ Jurisdiction	Share of world output, in purchasing-power- parity terms, %	Growth rate of broad money, in last three months at annualised rate, %	Growth rate of broad money, in last twelve months, %	Comment:
USA	16.1	5.3	4.2	Annual money growth moderate, at about 4% - 5% annual rate, despite regulatory attack on banks.
China	16.9	6.7	12.8	Sharp money slowdown in last two months, but perhaps temporary.
Eurozone	11.9	4.7	4.6	QE working well, with M3 growth at ideal 5% rate.
India	7.1	5.0	9.7	April and May money growth weak, but Rajan's removal may boost credit growth.
Japan	4.3	4.0	2.8	Broad money growth low, but turning upwards recently.
UK	2.3	4.1	4.2	Money growth slowing after upward blip due to stamp duty change.

In the last three months the annualised rate of growth of broad money has been between 4.0% and 6.7% in all of the world's six largest economies. With trend output growth for the world economy usually put at 3½ % a year, this sounds like a recipe for macroeconomic stability. However, money growth ought to be higher than this in the two big developing countries, to reflect their faster trend rate of output growth and the spread of the "banking habit". (See the country notes below for more detail on the countries themselves.)



28<sup>th</sup> June, 2016



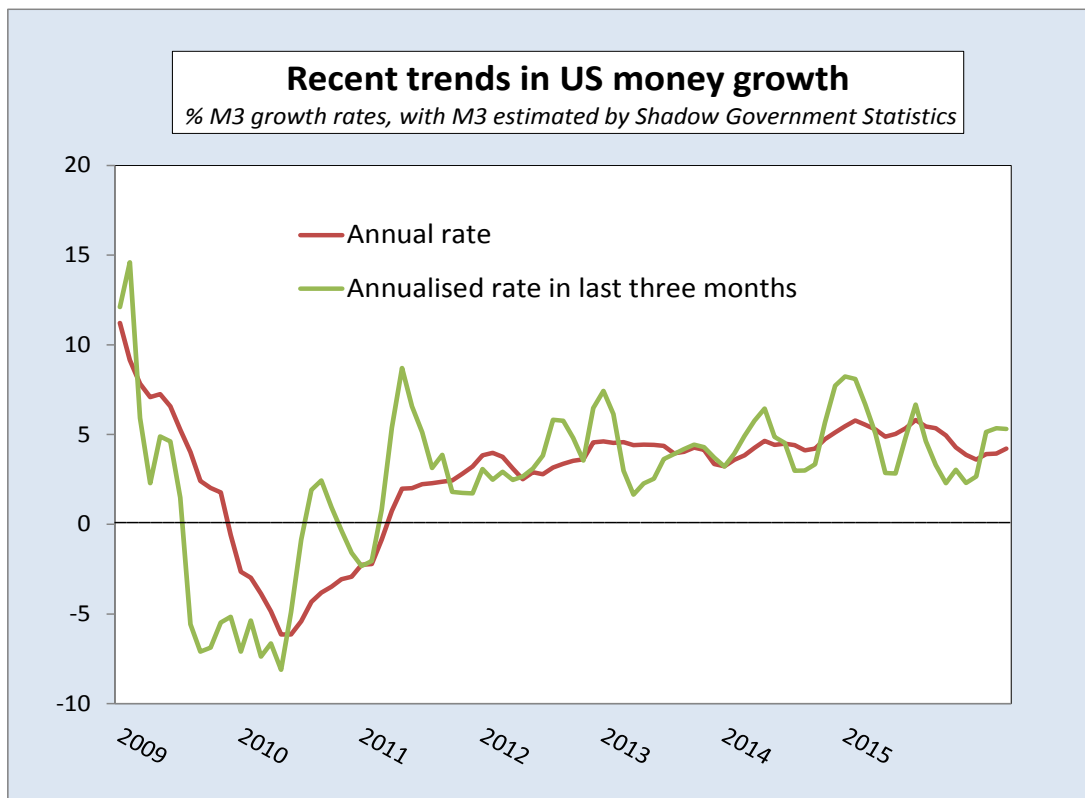
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## USA

	% annual/annualised growth rate:	
	M3	Nominal GDP
1959 - 2015	<b>7.5</b>	<b>6.6</b>
Four years to 2015	<b>4.3</b>	<b>3.8</b>
Year to May 2016	<b>4.2</b>	<b>n.a</b>
Three months to May 2016 at annualised rate	<b>5.3</b>	<b>n.a.</b>

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



## M3 growth has improved from late 2015 dip

**Summary:** In the three months to May 2016 US M3 grew at an annualised rate of 5.3%. April itself saw an increase in M3 of almost \$70b., close to the recent average. US broad money growth is reviving from a dip in late 2015, which was due to the Fed's preparedness to run down the stock of assets acquired in its "quantitative easing" operations. Bank credit to the private sector continues to be quite buoyant, despite the regulatory attack on big commercial banks. (Note that the M3 data used in this note are from the Shadow Government Statistics research company.)

Late 2015 saw a dip in US broad money growth, which was attributed in the analysis here to the Fed's preparedness to run off some of the assets acquired by the Fed in its QE programmes. If the Fed had sustained its stock of QE assets, broad money growth would have been higher and short-term macro conditions more positive. For four years now, the important driving force behind money growth has been bank lending to the private sector. In May banks' cash assets were more or less stable. With bank credit to the private sector still moving ahead and the Fed's activities being neutral for money expansion, broad money increased by about \$70b.(or 0.4%) in the month.

Quarter-by-quarter wobbles in broad money growth have been associated since 2011 with steadiness in the annual growth rate. As the chart shows, the annual rate of growth of broad money has been impressively stable. In the 53 months from January 2012 to May 2016 the average annual rate of growth of M3 has been 4.3%, with a high of 5.8% in a couple of months in 2015, and a low of 2.5% in May 2012. By long-run past standards the last four/five years are remarkable for both the lowness and stability of money growth. As Milton Friedman would have expected, the low and stable growth of money has been accompanied by negligible inflation, and steady growth in demand and output, while unemployment has dropped.

In these notes concern has been expressed that the ongoing regulatory attack on the banks might cause them to check the expansion of their risk assets, particularly their loans to the private sector. The data need to be watched, but so far such fears have been misplaced. "Loans and leases to the private sector" at all US commercial banks advanced by 0.4% in March, 0.6% in April and a touch above 0.5% in May (i.e., at annualised rates of 4.8% , 7.7% and 6.7% respectively). Credit expansion is resilient, despite continued worries about lack of capital in the banking system. A 25 basis point increase in Fed funds rate was widely expected at the June meeting of the Open Market Committee, but has been postponed at least until next month.

*Tim Congdon*  
17<sup>th</sup> June, 2016

	% annual growth rate:	
	M3	Nominal GDP
1960 – 2014	<b>7.6</b>	<b>6.7</b>
1960 – 1970	<b>7.7</b>	<b>7.7</b>
1971 – 1980	<b>11.4</b>	<b>10.7</b>
1981 – 1990	<b>7.7</b>	<b>7.7</b>
1991 - 2000	<b>5.6</b>	<b>5.6</b>
2001 - 2010	<b>7.1</b>	<b>3.9</b>
Four years to 2015	<b>4.3</b>	<b>3.8</b>



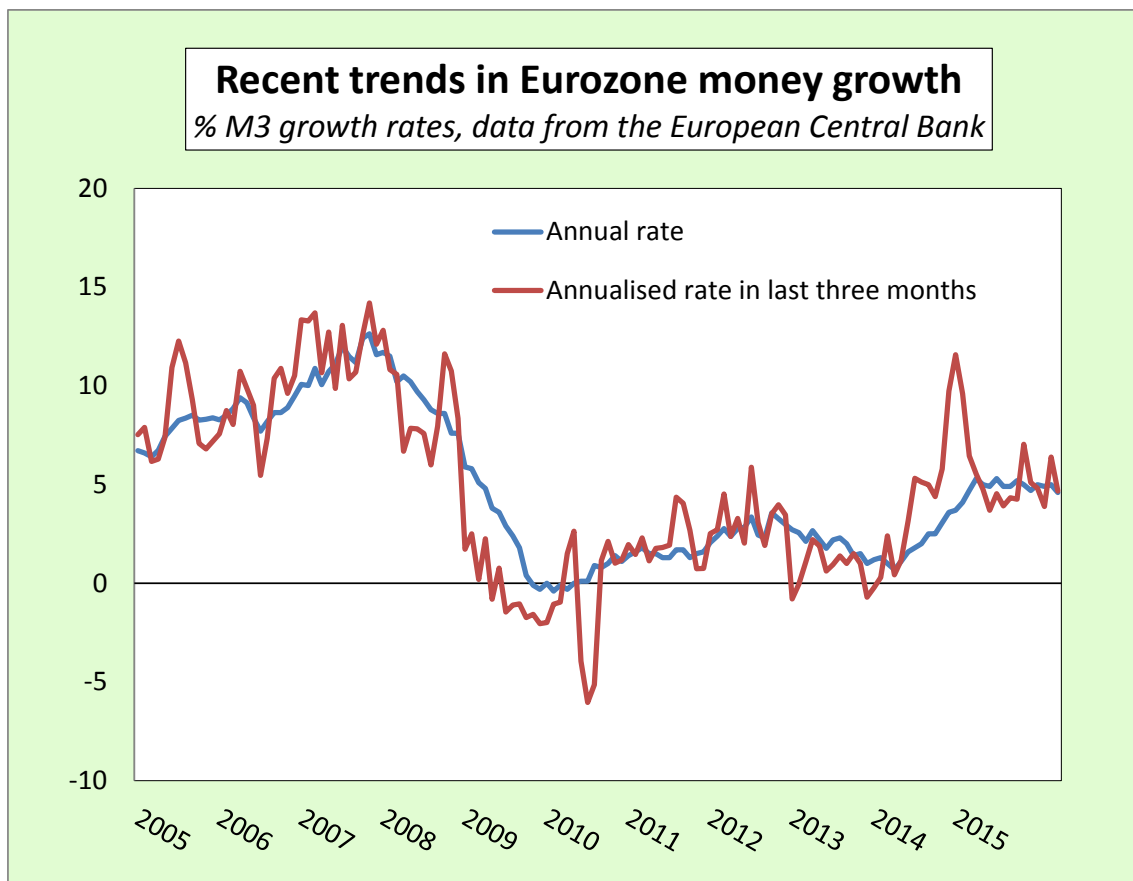
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## Eurozone/Euroland

	% annual/annualised growth rate:	
	M3	Nominal GDP
1995 – 2015	<b>5.3</b>	<b>3.1</b>
Five years to 2015	<b>3.0</b>	<b>1.6</b>
Year to April 2016	<b>4.6</b>	<b>n/a</b>
Three months to April 2016 at annualised rate	<b>4.7</b>	<b>n/a</b>

Sources: European Central Bank and International Monetary Research Ltd. estimates



## Money growth very satisfactory in mid-2016

**Summary:** In the three months to April 2016 the Eurozone's M3 quantity of money grew at an annualised rate of 4.7%. Meanwhile the annual rate of broad money growth has remained at about 5% - a more or less ideal number in view of the persisting deflation fears – since spring 2015. The ECB's "quantitative easing" programme has been successful. Annual broad money growth has risen from its 2009 – 2013 average (of a mere 2% or so), helping the Eurozone to achieve a clear cyclical rebound. The Germany economy, in particular, is seeing robust domestic demand.

The comentariat (of journalists, investment bank analysts and so on) continues to lambast the ECB, on the grounds that Eurozone demand growth is too weak, with persisting deflation worries. In fact, the ECB's QE programme has worked almost to perfection. Since its announcement in February 2015 the annual growth rate of M3 has moved up to 5% and stayed there with some consistency. In the five years to end-2014 the annual growth rate of M3 had averaged under 2%. The contrast in money growth between the pre- and post-QE-announcement periods is clear. Further, the credit counterparts data show that the money growth upturn reflects increased bank acquisition of government securities, just the pattern to be expected with a large-scale QE programme.

In April itself M3 growth was slightly weaker than typical in the last 15 months. M3 went up by €31b. or just under 0.3%. The relative weakness was not because the QE programme was ineffective, since the ECB's credit counterparts data show that in April bank credit to general government was a strong €51b. The influence holding back monetary expansion continues to be sluggish bank credit to the private sector, which was more or less flat in the two months, March and April, after a good rise in February. The stock of credit to the non-government Eurozone residents was up by a mere 1.2% in the year to April.

One feature at present is that money growth in Germany is above money growth in other Eurozone member states. In the year to March Germany's M3 advanced by 7.7%, whereas it went up only 4.0% in the rest of the Eurozone. A 3<sup>rd</sup> June Bundesbank press release was headlined, "Brisk domestic activity driving robust upswing". A bit more than a week later Bundesbank president, Jens Weidmann, said at a symposium that "the current environment does not warrant a further monetary loosening". For example, the German office market is very active, with prices moving ahead nicely against a background of continually falling vacancy rates.

*Tim Congdon  
17<sup>th</sup> June, 2016*

	% annual growth rate:	
	M3	Nominal GDP
1995- 2015	<b>5.3</b>	<b>3.1</b>
1995 – 2000	<b>4.5</b>	<b>4.0</b>
2001 – 2010	<b>6.7</b>	<b>3.4</b>
Five years to 2015	<b>3.0</b>	<b>1.6</b>



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## China

	% annual/annualised growth rate:	
	M2	Nominal GDP
1991- 2014	<b>20.3</b>	<b>15.8</b>
2010 - 2014	<b>15.2</b>	<b>12.8</b>
Year to April 2016	<b>12.8</b>	<b>n/a</b>
Three months to April 2016 at annualised rate	<b>6.7</b>	<b>n/a</b>

Sources: People's Bank of China for M2 and International Monetary Research Ltd. estimates



## Broad money growth slows, reflecting concern over too much debt

**Summary:** In the three months to April 2016 China's M2 expanded by 1.6%, or at an annualised rate of 6.7%. This compares with an increase of 2.5% (and an annualised rate of increase of 10.4%) in the preceding three months, i.e., the three months to January. These numbers are somewhat below the typical growth rates of the last decade. However, money growth in late 2015 was higher than in late 2014. The intentions of Chinese monetary policy-making have become unclear, with key figures in the ruling Communist Party expressing concern about too much debt.

Money growth in China has a seasonal pattern, with the first quarter tending to see faster growth than the rest of the year. Much of the Chinese banking system is state-owned and subject to bureaucratic direction. The start of each year sees the allocation of credit limits for particular borrowers (themselves also often state-owned) and a burst of money expansion. 2016 has been no exception. When allowance is made for the seasonal pattern, Chinese money growth has decelerated in recent months. In the three months to April M2 was up by only 1.6%, i.e., at an annualised rate of 6.7%.

This may be a blip. Money growth has indeed been markedly volatile in China in the last two years, as the chart opposite demonstrates. But a wider debate on money and the banking system is under way at the top of Chinese society. Official anxiety is being expressed about over-indebtedness, even though rapid growth of debt has been a long-standing feature of the Chinese boom. According to *The Economist*, an "authoritative person" warned in a recent article in *The People's Daily* that future growth of demand and output must not rely too much on debt. Observers surmised that this "authoritative person" was Liu He, who is an economic adviser to Xi Jinping, China's president. If so, the larger message is that banks must not step extending easy credit to the wasteful state-owned sector. If this precept is being translated into action, it may be an explanation for the money slowdown in the date.

The correlation between the growth rates of money and nominal GDP in China is clear. Persisting slow money growth in China would therefore imply persisting deflation at the wholesale level (i.e., "at factory gates"). It would also be bad news for China's demand for commodities. However, scares about Chinese policy have been recurrent in recent years. In the end pragmatism prevails, as the Chinese leadership does not want a recession. Xi Jinping and his associated are said to be distrustful of prime minister, Li Keqiang, who is allegedly more relaxed about turning on "the credit taps" if growth falters.

Tim Congdon  
27<sup>th</sup> June, 2016

	% annual growth rate:	
	M2	Nominal GDP
1991 - 2000	<b>20.3</b>	<b>15.8</b>
2001 - 2010	<b>15.2</b>	<b>12.8</b>
Four years to 2014	<b>14.1</b>	<b>11.6</b>



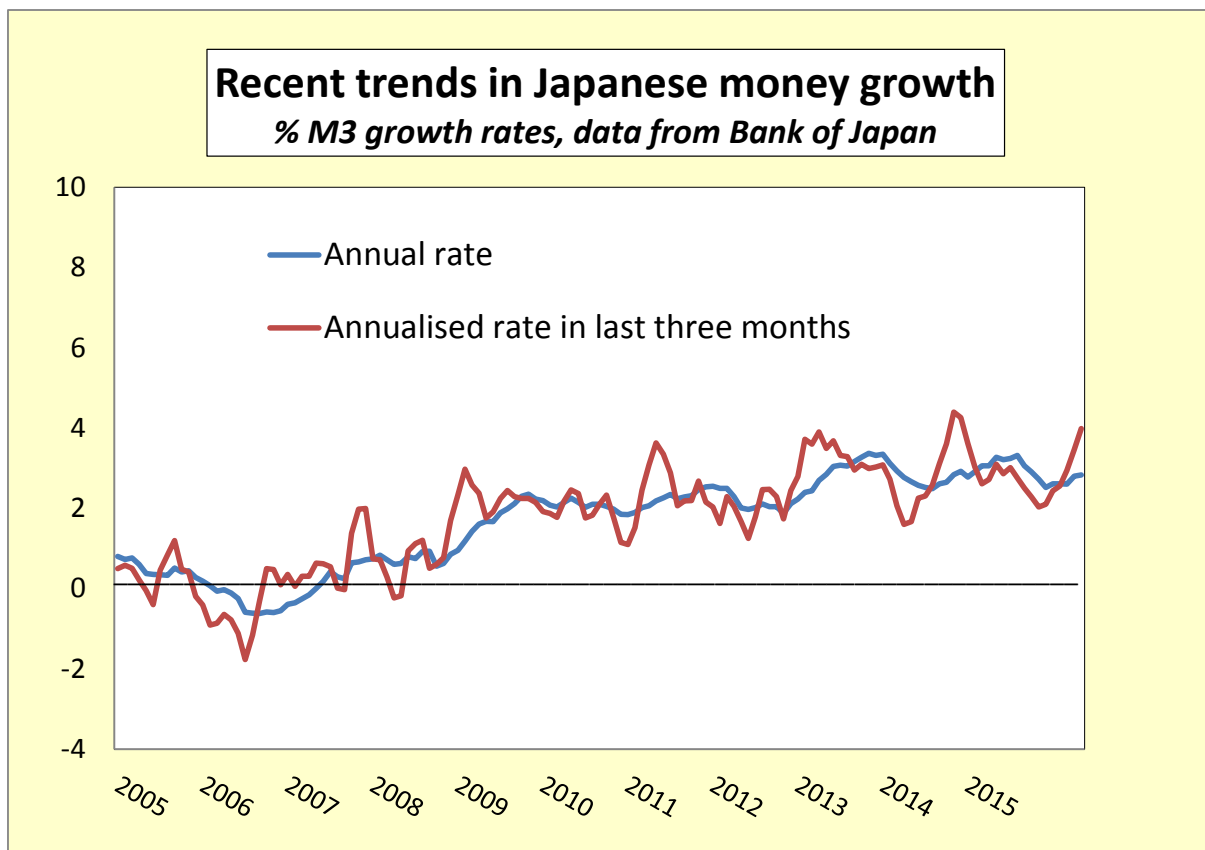
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## Japan

	% annual/annualised growth rate:	
	M3	Nominal GDP
1971- 2015	<b>6.3</b>	<b>4.3</b>
Five years to 2015	<b>2.7</b>	<b>0.4</b>
Year to May 2016	<b>2.8</b>	<b>n/a</b>
Three months to May 2016 at annualised rate	<b>4.0</b>	<b>n/a</b>

Sources: Bank of Japan for M3 and IMF for GDP



## Broad money growth is moderate and perhaps edging up

**Summary:** In the three months to May 2016 Japanese M3 grew at an annualised rate of 4.0%. (In May itself M3 was up by just under 0.4%, i.e., at an annualised rate of 4.4%.) These numbers are a tad higher than those seen for most of 2015 and in that sense are an improvement. The Bank of Japan persists with its programme of so-called “quantitative and qualitative easing”, now with “negative interest rates” tacked on. QQE consists mostly in central bank asset purchases. The BOJ has been criticised for its apparent indifference to yen strength, but has made no new policy moves in the last few weeks.

Financial markets were disappointed by a 16<sup>th</sup> June announcement from the BOJ. In theory one of its key objectives is to raise inflation to 2% at an annual rate. However, the recent advances of the yen on the foreign exchanges have dampened inflation pressure and the BOJ said that consumer prices are likely to fall slightly this year.

The BOJ has said that it plans to meet its inflation objective by boosting the monetary base, an approach which is understood to be one of the three “arrows” of “Abenomics”. The monetary base has indeed soared since the inception of the latest QQE programme in April 2013, but the quantity of money as such (i.e., the broadly-defined M3 measure) has responded less than might have been expected. At first QQE involved BOJ asset purchases of 60 – 70 trillion yen a year, but since October 2014 this has been increased to 80 trillion yen a year. (At an exchange rate of 100 yen to the \$, a trillion yen is equal to \$10 billion) This compares with a figure for total M3 of about 1,250 trillion yen.

On the face of it, 80 trillion of asset purchases ought to boost M3 by about 6% a year. A proportion of the 80 trillion yen asset purchases is indeed from non-banks, which directly boosts M3. But much of the bond buying is from banks, with no immediate effect on non-banks’ deposits (i.e., M3 money). Anyhow the typical annualised three-monthly growth rate of M3 in the three years before April 2013 was about 2¼%, whereas subsequently it has been about 3%. In that context the latest number, 4.0%, is satisfactory or even encouraging.

Bank lending to the private sector has been not been responsive to the excess bank cash reserves created by QQE. Throughout the programme Japanese banks have been sitting on their greatly-increased cash assets. Nevertheless, the BOJ asset purchases are having important effects. For example, these purchases have included buying of “real estate investment trusts” which are now priced on the stock market at a 40% premium to underlying value. REITs on other stock markets are at far less fancy valuations.

*Tim Congdon*  
*17<sup>th</sup> June, 2016*

	% annual growth rate:	
	M3	Nominal GDP
1981 – 1990	<b>9.2</b>	<b>6.2</b>
1991 - 2000	<b>2.4</b>	<b>1.3</b>
2001 - 2010	<b>1.1</b>	<b>-0.5</b>
Five years to 2015	<b>2.7</b>	<b>0.4</b>



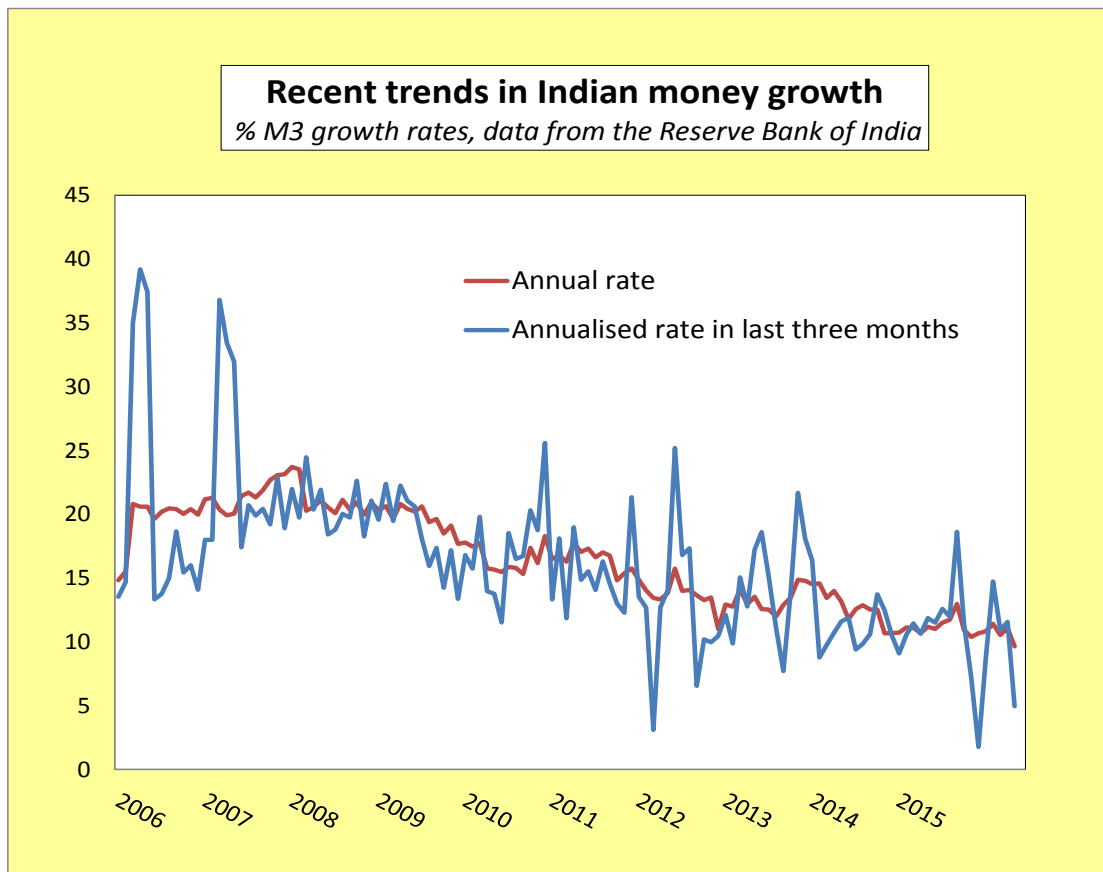
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## India

	% annual/annualised growth rate:	
	M3	Nominal GDP
1991- 2014	<b>16.5</b>	<b>13.8</b>
2010 - 2014	<b>14.2</b>	<b>14.4</b>
Year to May 2016	<b>9.7</b>	<b>n/a</b>
Three months to May 2016 at annualised rate	<b>5.0</b>	<b>n/a</b>

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



## Abrupt money slowdown in spring 2016, amid policy-making tensions

**Summary:** Indian money growth has a seasonal pattern. Comment here is on a seasonally-adjusted series estimated by the Institute of International Monetary Research from Reserve Bank of India data. **The annual rate of broad money growth – which has been mostly in a 11% - 14% corridor in recent years – is slowing. Indeed, in the last three months the annualised rate of increase has been only 5.0%. Tensions between the RBI Governor, Raghuram Rajan, and the commercial banking industry seem to lie behind his decision not to seek another term. The banks resisted his demands for increased loan loss provision, hoping that resumed inflation would boost asset prices and help their profitability.**

The Reserve Bank of India has pursued an anti-inflationary monetary policy in recent years, with gradual but persistent declines in the rate of broad money growth. (See the chart opposite.) The current RBI governor, Raghuran Rajan, a former chief economist at the International Monetary Fund, assumed office in September 2013 during a period of rupee depreciation and anxieties about rising inflation. He is regarded as a successful governor, as the rupee has stabilized and inflation has moderated.

However, Rajan is not seeking a second term, which would have begun in September 2016. He seems to have been pressing an agenda similar to that of central bank leaderships in the advanced economies, with increased capital ratios and the “tidying-up” of balance sheets, including the early writing-off of bad debts. In G7 economies subject to close surveillance from the Bank for International Settlements (and the Financial Stability Board under Mark Carney), the Rajan agenda would be widely supported. But the message has to be that in India top bankers have the ability to influence the government and to dissuade it from pursuing policies that are against their best interests. (Given the plight of commercial banks in the G7 nations, bankers’ hostility to the Rajan agenda is understandable.)

The last few weeks have seen a marked deceleration in broad money growth, perhaps because banks have been implementing part of the Rajan agenda. In the three months to May M3 increased by little more than 1%, or at an annualised rate of 5.0%. The slowdown – from the double-digit annual growth rates that have applied consistently over the last 30 years – is marked and significant. As the box above shows, the annual rates of increase in M3 and nominal GDP have been very similar in the last 15 years. If M3 growth were to remain at an annual rate of 5%, the rate of increase in nominal GDP would move towards that sort of figure. Since the trend rate of increase in real output is usually put at 6% or above, the message has to be that current policy would lead – eventually – to deflation. Perhaps it is not altogether surprising that Rajan has been asked to move on.

*Tim Congdon*  
27<sup>th</sup> June, 2016

	% annual growth rate:	
	M3	Nominal GDP
1991 - 2000	<b>16.9</b>	<b>14.4</b>
2001 - 2010	<b>17.3</b>	<b>13.6</b>
Four years to 2014	<b>13.4</b>	<b>12.9</b>



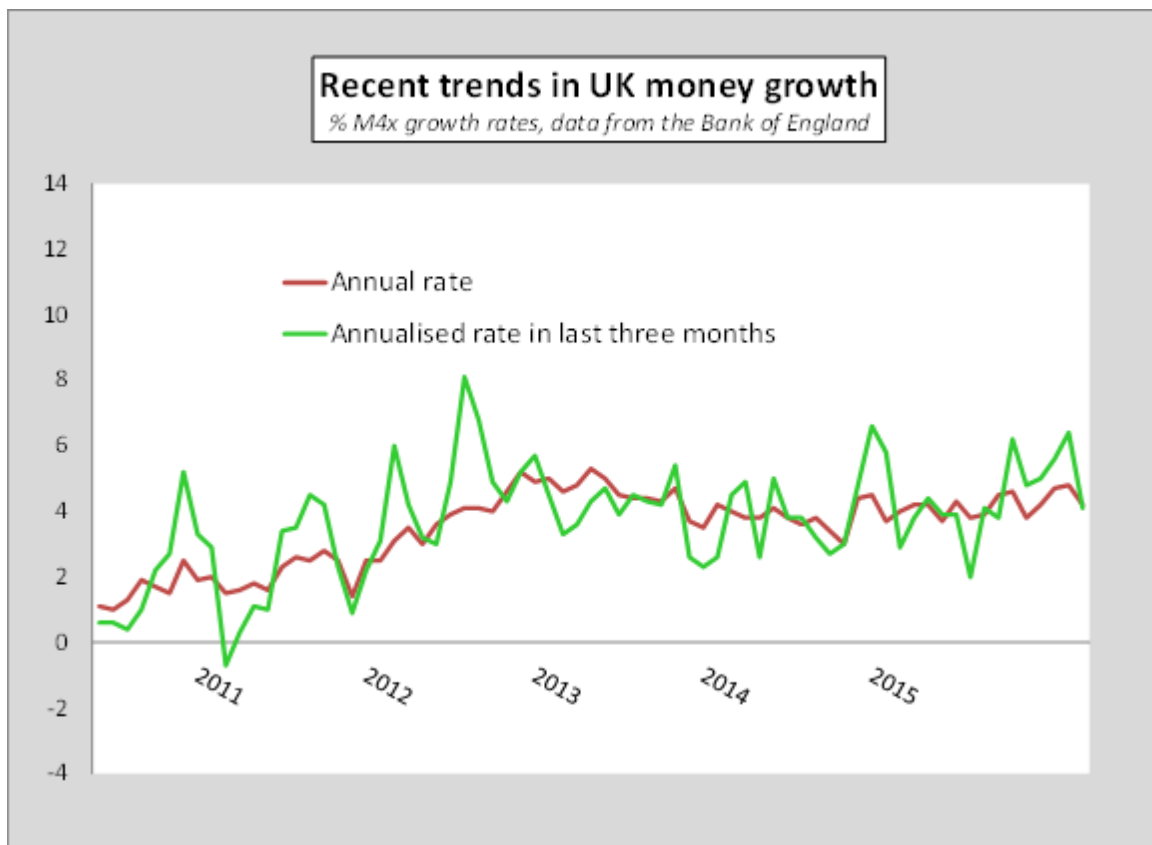
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## UK

	% annual/annualised growth rate:	
	M4x/M4 before 1997	Nominal GDP
1964 – 2015	<b>10.0</b>	<b>8.2</b>
Five years to 2015	<b>3.7</b>	<b>3.6</b>
Year to April 2016	<b>4.2</b>	<b>n/a</b>
Three months to April 2016 at annualised rate	<b>4.1</b>	<b>n/a</b>

Sources: Bank of England and Office for National Statistics.



## April dip in M4x growth after strong first quarter of 2016

**Summary:** M4x was virtually unchanged in April, after three months of high growth in the first quarter. The buoyancy of broad money growth in Q1 was attributable to a lending surge as buy-to-let investors borrowed from the banks, to beat the stamp duty change on 1<sup>st</sup> April. The annualised quarterly rate of broad money growth in April was 4.1%, down noticeably from March's 6.4%. The blip upwards in money growth in Q1 seems like to prove temporary.

For much of the period since the end of QE in 2012 the annual rate of M4x growth has been remarkably stable. It has fluctuated within a narrow 3% - 5% band. The monetarist argument is that low and stable money growth over the medium term would result in low inflation, with demand and output growth steady. This is what has happened. In fact, the last few years have seen the lowest increases in both nominal GDP and the price level, over a sustained period, since the 1930s.

Early 2016 saw buoyancy in credit to the private sector, related to borrowing to beat the increase in stamp duty for buy-to-let home-buying. In the three months to March bank lending (excluding lending to intermediate "other financial corporations" [i.e., quasi-banks]) jumped by 2.6%, or at an annualised rate of 10.9%. But in April the stock of loans actually dropped, if by only £2.1b. or 0.1%. Much-hyped fears about "Brexit" ought to have prompted the use of overdraft facilities by companies, ahead of a possible sterling depreciation, but that seems not to have happened. In fact, companies repaid bank debt on a small scale in both March and April. Indeed, without the buy-to-let effect, bank lending to the private sector would have been weak so far in 2016.

Money growth indicators are healthy for the UK economy, and argue against pessimism about growth in demand and output in the rest of 2016. Although widely-quoted forecasting bodies (such as the National Institute) have endorsed government alarmism about the consequences of Brexit, little hard evidence is available that previous accessions to and departures from customs unions had marked cyclical impacts on aggregate demand. Newspapers blamed poor retail sales figures in the spring on Brexit, but a 0.9% jump in retail sales in May was then recorded. Business surveys have not so far registered any significant dent from all the Brexit talk. If there has been a problem so far in 2016, it has been a rather slow international economy rather than anything much the matter with UK domestic demand.

*Tim Congdon*  
17<sup>th</sup> June, 2016

	% annual growth rate:	
	M4/M4x	Nominal GDP
1964- 2015	<b>10.0</b>	<b>8.2</b>
1991 – 2000	<b>7.5</b>	<b>5.9</b>
2001 – 2010	<b>7.0</b>	<b>4.2</b>
Five years to 2015	<b>3.7</b>	<b>3.6</b>