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

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Monthly e-mail from Tim Congdon and John Petley – 20th December, 2021

Global money round-up in late 2021

In November the US consumer price index rose by 0.8%, taking the increase in the year to October to 6.8%. The recent fall in oil prices – related to the emergence of the Omicron variant of Covid – may moderate the CPI increase in December. All the same, the CPI increase in the year to December could exceed 7%. The numbers in other countries – notably China and Japan – have so far been less bad, but many forecasts are now being made that annual consumer inflation in the Eurozone will reach 5% and in the UK 6%. Inflation is being attributed to bottlenecks and supply shortages soon *after* the Covid pandemic, and hence as *due to* the pandemic. Further, influential economists in central banks and elsewhere take this analysis as justifying claims that the upturn in inflation will prove transitory and self-correcting. They see the rapid money growth of spring 2020 (which stemmed from the official response to Covid, particularly the central bank asset purchases) as of no great importance.

An alternative position – developed in these notes over the last 18 months – is that the current inflationary boom is the result, above all, of the excessive money growth recorded in 2020. Sure enough, money growth has moderated from recent peaks, which provides reassurance that inflation is not on an explosive upward path. But the latest three-month annualised growth rates of broad money in the USA and the Eurozone are 10.3% and 8.5% respectively, which remain inconsistent with low 2% inflation. To remind, the compound annual growth rates of M3 broad money in the decade to end-2019 were 4.1% in the USA and 3.3% in the Eurozone. Numbers as low as this – or perhaps even lower, given that trend output growth rates may have weakened – are needed if 2% inflation is to return. Inflation numbers in the 5% - 10% band will be common in 2022, implying some rises in short-term interest rates. Real money balances will be squeezed in late 2022 and early 2023. Beneath-trend growth experiences, or even recessions, are to be expected, probably in 2023, to combat inflation.

Money trends in late 2021 in the main countries/jurisdictions

The Institute of International Monetary Research focuses on the relationship between trends in the growth of the quantity of money, broadly-defined, and macroeconomic outcomes. Most of the last 18 months have been dominated by the Covid-19 medical emergency, but late 2022 should see medical normality. The Institute's consistent analysis since spring 2020 – that money growth acceleration implied an inflationary boom and an upturn in inflation – has proved correct. The new area of debate is the duration of above-normal inflation, with normality seen as an annual increase in consumer prices of 2% a year. The key principles here are that,

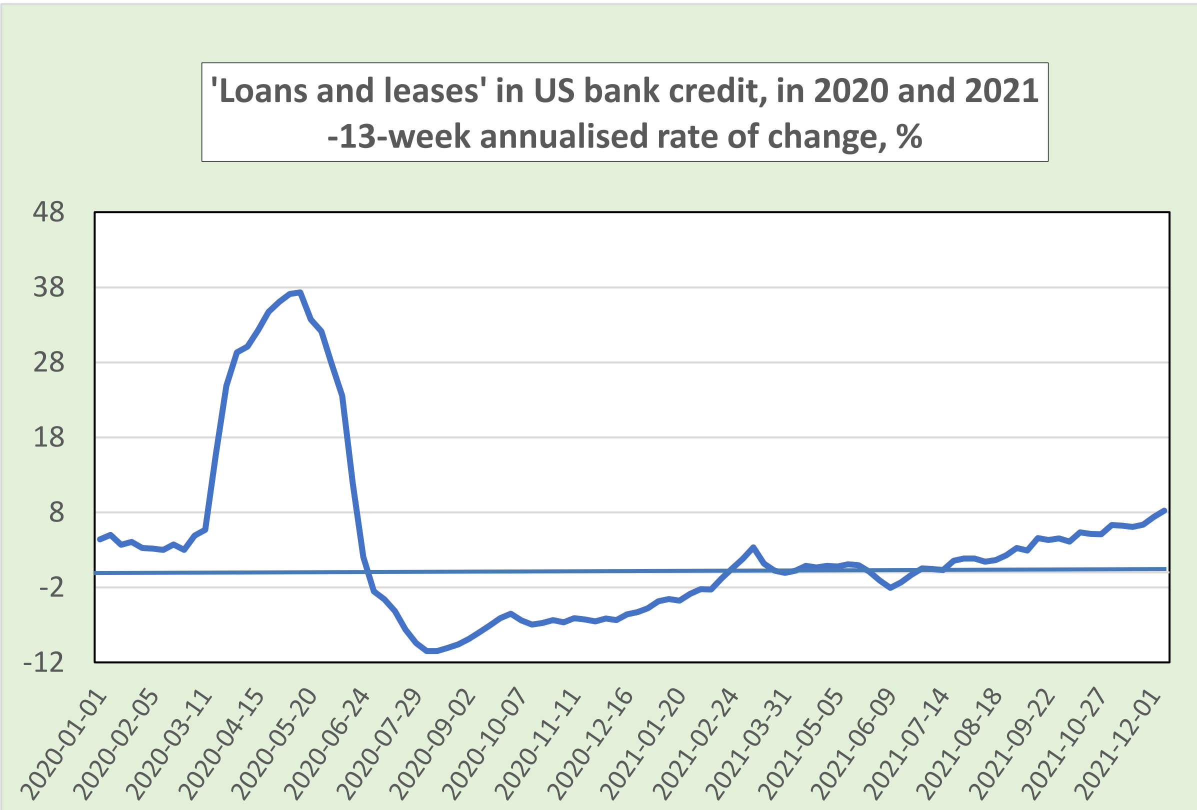
i. The rate of inflation is roughly equal to the rate of increase in nominal GDP minus that of real GDP, and
ii. Over the medium term, growth rates of broad money and nominal gross domestic product will be similar, although not identical.

Much will therefore depend on rates of broad money growth in coming months and quarters, with the table below summarizing recent patterns in the leading nations. The table shows that money growth reductions from the remarkable 2020 peaks are now evident almost everywhere. However, in the USA and the Eurozone – although not Japan – the three-monthly annualised numbers are still well above the typical figures before the pandemic and remain far too high to be reconciled with 2% inflation. Worries about inflation will persist and indeed intensify in 2022.

Name of country/ jurisdiction	Share of world output		Growth rate of broad money		Comment
	In purchasing-power parity terms, %	In current prices and exchange rates, %	In last three months at annualised rate, %	In last twelve months, %	
USA	15.1	23.3	**10.3**	**9.2**	Money growth has slowed cf. spring 2020, but is much too high for 2% Fed target.
China	18.7	16.1	**9.2**	**8.4**	Money growth moderate amid property bust scares. Talk of an easing package fades.
Eurozone	10.6	16.4	**8.5**	**7.7**	Money growth boosted by ECB asset purchases, still well above pre-Covid norms.
Japan	4.2	5.9	**2.9**	**3.6**	Credit and money growth slowing sharply, implying continuing negligible inflation in medium term.
India	7.7	3.3	**11.6**	**11.0**	Recent money growth back to double digits, with resurgent bank credit to private sector.
UK	2.2	3.4	**6.7**	**7.9**	Money growth decelerating, bank loans to corporates still very weak.

As noted here last month, crucial to money growth in 2022 will be the behaviour of bank lending to the private sector. In the last 18 months high or very high money growth has been almost entirely attributable – in the main economies – to central bank asset purchases and monetary financing of budget deficits. As central bank asset purchases stop, money growth will decelerate unless bank lending to the private sector revives strongly.

In the USA some observers believe that bank lending to the private sector will soon rebound. On 8th November the Fed published the latest *Senior Loan Officer Opinion Survey on Bank Lending Practices*. The survey's editors was particularly interested to see if credit growth would return to the pace of late 2019 before Covid-19 became a problem. To quote, "The survey included a set of special questions inquiring about the current level of demand relative to pre-pandemic levels (defined as the end of 2019) for 'commercial and industrial' and credit card loans, as well as banks' outlook for demand for such loans over the next six months. On balance, banks reported weaker levels of demand for all queried C&I and credit card loan categories compared with the end of 2019, and that they expect stronger demand for both C&I and credit card loans over the next six months." The finding that – as of autumn 2021 – people and companies were not tapping bank finance on a greater scale than before Covid is notable. With interest rates so low, and inflation on the rise, stronger demand for bank credit might be expected.



But a new trend may be imminent. The latest data suggest that bank credit to the private sector is starting to grow more strongly. The chart above relates to "loans and leases in bank credit" (mostly bank lending to the private sector) and is of weekly data; it shows the 13-week (or quarterly) annualised % rate of change. (That is, it shows the annual rate that would be recorded if the experience of one quarter continued for a year.) In the decade to end-December 2019 "loans and leases in bank credit" increased at a compound annual rate of 4.5%. Roughly speaking, a 4% annual growth rate of "loans and leases" – US banks' largest single asset category – ought to be compatible with 3% - 5% annual growth of broad money. Meanwhile 3% - 5% annual growth of broad money is in line with the average of the 2010s, when inflation was a touch beneath the 2% inflation “target”. (The Fed may not have a formal “inflation target”, but its officials talk about this sort of inflation number as acceptable.)

The chart shows that – just before the Covid-affected period – bank credit to the private sector was growing at about 5% a year. A leap then occurred, because in March, April and early May 2020 companies drew down credit lines on a huge scale ahead of (what they expected to be) a few quarters of great uncertainty when cash flows might be strained. However, Covid lockdowns were gradually eased in the following months. The deposits created by the credit drawdowns were surplus to requirements and in late 2020 they were used to repay the unnecessary borrowings. In early 2021 nothing much happened, with companies no longer in a rush to repay the emergency credit facilities, but also in no hurry to assume new financial commitments.

Finally, from July 2021 “loans and leases” have started to grow again. Indeed, in the 13 weeks to 8th December (which is the last value available) “loans and leases” increased by over 2% or at an annualized rate of 8.3%. *The 8.3% figure is higher than in very early 2020.* It suggests that anecdotal reports of US banks’ keen to lend – and of US companies’ eager to borrow both the rebuild inventory and to anticipate price rises – are correct.

One swallow does not make a summer, and a month of data does not establish a trend. All the same, the steady upward drift of the line in the chart from summer 2021 is interesting and could be important. *If credit growth reaches a 10%-a-year rate, the message will be that money growth has its own momentum from the private sector’s behaviour and does not depend on continued Fed asset purchases.* A rise in interest rates will then be necessary to bring annual money growth back down to the 3% to 5% band compatible with 2% inflation. The size of the required interest rate increases will depend on the dynamism – or lack of it – private sector bank credit.

In the Eurozone the stock of credit to the private sector was 3.7% higher in October 2021 than a year earlier. So banks have still been expanding their loan books during the pandemic, in contrast to the US situation. Mortgage lending has been dominant. The stock of loans for house purchase was up by 5.5% in the year to October, whereas loans to non-financial corporations (i.e., industry and commerce) advanced only 1.9% in the same period. However, the balance between mortgage finance and corporate loans may be shifting. In the three months to October loans to non-financial corporations increased by over 0.9% (or at an annualized rate of 3.8%). Indeed, the stock of all private sector bank credit grew at an annualized rate of 8.1% in the three months to October, not that different from the US experience. As noted here last month, it is well-known that European governments are trying to persuade the Basel-based Bank for International Settlements that further large increases in banks’ capital requirements are unnecessary and would damage the ability of their financial systems to sustain the recovery.

The latest important development on this front is that the European Union’s official green agenda is now being applied to banking. On 6th July the European Commission launched its *Strategy for Financing the Transition to a Sustainable Economy* and a proposed regulation on European green bonds; on the next day, 7th July, the European Central Bank (ECB) concluded its strategy review on the same subject and proposed significant changes. Crucially, capital weightings are to be much higher for loans to environmentally “dirty” industries (such as oil and gas development) than to the clean, renewable energy sectors. Needless to say, spokespersons for the banking industry have said that it is not ready for this drastic upheaval in asset acquisition strategies and all the attendant uncertainties. An obvious issue is whether the capital loadings are to apply retrospectively or only on newly-negotiated loan facilities.

Similar developments are likely to affect UK banks. UK officialdom, including officialdom from the Bank of England, seems to be participating in the international effort to oblige – should one say to force? – the financial system to participate in the drive for net zero carbon emissions. Mortgage lending is still growing, but bank lending to the non-bank private sector was very weak in summer 2021. But October was quite different. The stock of lending to corporates, both non-financial and financial, went up by over £12b. in the month. The UK – like the USA and the Eurozone – may be about to experience a rebound in private sector credit demand. A clash with a tightening of capital standards, courtesy of the mooted "Basel IV" rules from the BIS and an increase in the counter-cyclical capital buffer set by the Bank of England, may be in prospect. The tougher are regulations against new bank credit, the lower may be the interest rate rises in prospect in 2022 and 2023.

To repeat the point made here last month, the vigour – or lack of vigour – of bank credit to the private sector is crucial to interest rate prospects. The market consensus is that interest rate rises will occur in most developed countries – in 2022 and 2023 – once the pandemic-related weakness in aggregate demand lies in the past. Central banks may end asset purchase programmes first, but higher interest rates are widely foreseen. A reduction in money growth is a condition of the return of moderate inflation, while robust bank lending to the private sector will make it more difficult to deliver the needed reduction in money growth. But – if bank lending to the private sector is, even at virtually zero interest rates, increasing at an annual rate of 5% or less – it will be easy for central banks to keep money growth under control. Pointers to future lending growth therefore deserve to be monitored carefully in the next few months. Despite very low interest rates, and indeed extremely negative real interest rates, a big boom in private sector bank credit does not seem to be imminent anywhere. But a recovery in such credit is starting.

A key point is that, as yet, no one is expecting interest rates over the next two years to approach the inflation rates now being seen in North America and Europe. The tiny recent move by the Bank of England – from a Bank rate of 0.1% to one of 0.25% - has caused some fuss. But bank deposits offer no meaningful return relative to an inflation rate of over 5%. In the 1970s negative real interest rates prevailed on money balances in many countries, causing a perceptible, if modest "flight from money". In other words, the ratio of money to national income and expenditure fell, and the velocity of money rose. If that pattern were to return in the next year or two, it would intensify the already evident upwards pressure on inflation.

20th December, 2021

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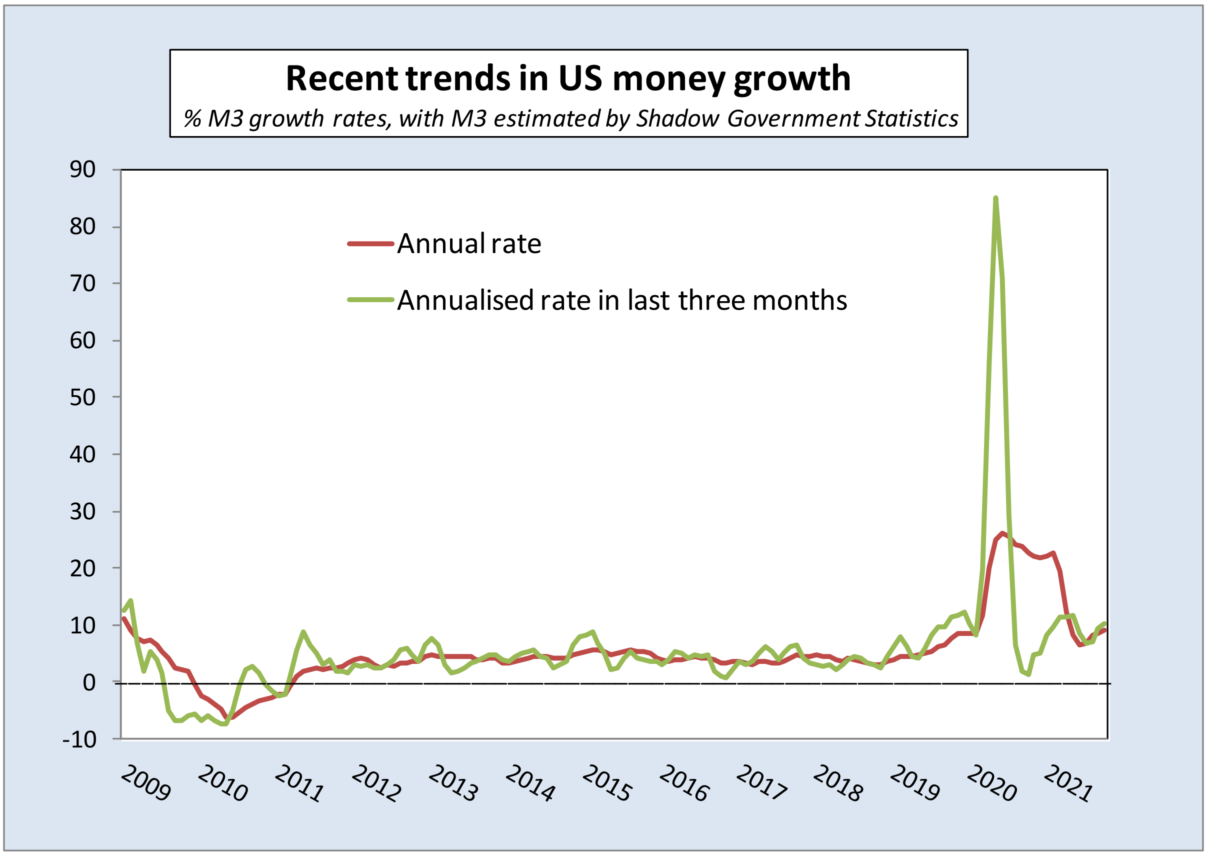
USA

	% annual/annualised growth rate:	
	M3	Nominal GDP
1961 – 2019	**7.4**	**6.5**
Nine years to 2019	**4.5**	**4.1**
Year to October 2021	**9.2**	**n.a**
Three months to October 2021 at annualised rate	**10.3**	**n.a.**

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



US broad money growth rises again, as inflation hits record levels

Summary: **US broad money growth returned to double digit levels in October. M3 grew by $200b. during the month (or by just under ¾%), which raised the annualised quarterly growth rate from 8.4% to 10.3%. This was the highest reading since May. The annual rate of growth also increased, from 8.5% to 9.2%. (Our M3 data come from Shadow Government Statistics.)**

The annual rate of consumer inflation – using the consumer price index – reached a 30-year high of 6.2% in October. Fed Chairman Jay Powell has admitted that it was "time to retire" the word "transitory" when discussing inflation. Speaking to the US Senate Banking Committee on 30th November, he predicted that the USA would suffer from high inflation well into 2022, but added that he would "use our tools to make sure that higher inflation does not become entrenched". These comments came after the Fed had announced a tapering of its asset purchase programme by $15b. per month. On 16th December, following a further rise in CPI inflation to 6.8% in the year to November, Powell announced that in January the taper would be stepped up by $30b per month and the asset purchases stopped altogether in March. The Fed funds rate remains unchanged. After a moderate third quarter (Q3), in which US GDP grew at an annualised rate of 2.1%, a number of indicators point to a more buoyant Q4.

Until recently money creation by bank lending to the private sector has been weak. Deposits arising from new bank lending were not significant in money growth in the year to mid-2021. This may be changing. In the three months to 8th December "loans and leases in bank credit" – a category in Fed statistics which corresponds roughly to bank lending to the private sector – grew at an annualised rate of 8.3%, well above the norm in the 2010s. By implication, money growth will remain positive when asset purchases cease. The other problem here will be the difficulty of avoiding the monetization of a budget deficit. The International Monetary Fund projects the USA's "general government budget deficit" to be $1,700b. in 2022 and $1,500b. in 2023, after almost $2,500b. in 2021. If $550b. of the 2022 deficit were financed from the US banking system, this would by itself add 2% to M3

In spite of monetary tightening by the Fed, yields on 10-year US Treasuries still remain below March's levels. Powell has been appointed for a second term as Fed chairman, while the new vice-chair will be Lael Brainard, who replaces Richard Clarida. Like most senior figures at the Fed, both Brainard and Clarida ignore the well-established link between the quantity of money, broadly defined, and nominal national income. Given there is often an 18-24 month time lag between a surge in broad money growth and inflation, prices are likely to rise at an even faster rate in 2022. 10% inflation is possible. Money growth will fall in 2022, but the M3 increases in the years to December 2019 and 2020 were 8.5% and 21.2% respectively. The increase in the year to December 2021 is likely to be about 9%.

Tim Congdon and John Petley
20th December, 2021

	% annual growth rate:	
	M3	Nominal GDP
1961 – 2019	**7.4**	**6.5**
1961 – 1970	**8.0**	**7.1**
1971 – 1980	**11.4**	**10.3**
1981 – 1990	**7.7**	**7.7**
1991 - 2000	**5.6**	**5.6**
2001 - 2010	**7.1**	**3.9**
Nine years to 2019	**4.5**	**4.1**

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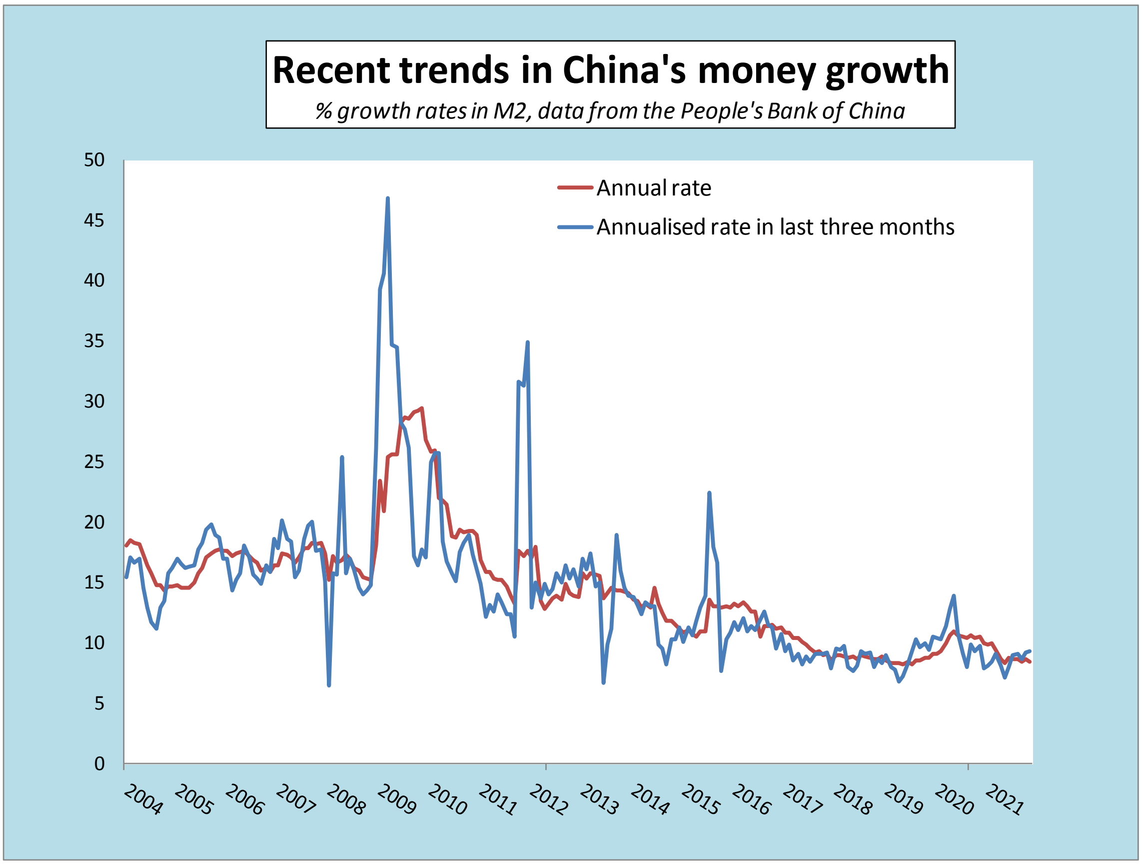
China

	% annual/annualised growth rate:	
	M2	Nominal GDP
1991- 2019	**18.7**	**14.8**
2011 - 2019	**11.9**	**10.4**
Year to November 2021	**8.4**	**n/a**
Three months to November 2021 annualised rate	**9.2**	**n/a**

Sources: People's Bank of China for M2, IMF for GDP.



Broad money growth running consistently at pre-pandemic levels

***Summary*: In the three months to November 2021 China's M2 grew at an annualised rate of 9.2%, unchanged on October's figure. The annual growth rate fell slightly, but has now remained within a narrow band between 8.3% and 9.5% for nine consecutive months. Chinese broad money growth has been remarkably stable in recent months and seems to have settled down at a level typical of the final years of the last decade.**

On 6th December, the People's Bank of China (the central bank) lowered the reserve requirement ratio for most Chinese banks by 0.5%. This was the second such reduction in 2021 and may well be a response to an expected Omicron hit to the economy. In the year to November the growth of banks' loan books stood at 11.7%, the slowest growth rate since May 2002. One factor behind the sluggish bank lending may have been the troubled state of the country's real estate sector. On 9th December, property giant Evergrande formally defaulted on its debt, according to Fitch Ratings. The company is estimated to be more than $300b. in debt. On the same day another property developer, Kaisa, also defaulted on debts totalling $12b. Although the Chinese government has been actively dampening down a boom in house prices, both new home sales and housing starts have been on a sharp upward trend since the start of the year. But house price inflation has moderated. Two years ago the regulatory authorities were clamping down on speculators and introducing tighter lending criteria in an attempt to rein in a property boom which had seen prices rising at an annual rate of more than 10%.

Away from the housing sector, China's economy is growing, but signs are emerging of the end to the long-term boom of the last 40 years which has made China the world's second largest economy (and indeed the largest, when measured in terms of purchasing-power-parity). Industrial production in October was 3.1% up on a year earlier, while industrial production in October 2020 was 6.9% higher than in October 2019, before the damage from the coronavirus pandemic. Plainly, Chinese output is well ahead of pre-Covid levels, in contrast to the situation in many more developed countries. But – by the standards of the last 40 years – a 3.1% annual gain is modest. Many observers have suggested that adverse demographics (with a falling working-age population) and Xi Pinjing's re-centralization of economic decision-making will cause the trend rate of output growth to drop to 2% - 3%, beneath that in the rest of Asia.

Inflation rose from 1.5% in the year to October to 2.3% a month later. The rise in inflation is due in part to the waning effects of falling food prices following the end of the African swine 'flu outbreak of 2019 and early 2020. It still remains below the government's 3% target, although producer prices are rising rapidly, with the annual rate of increase in November standing at 12.9%. This is actually a reduction on October's reading of 13.6% - a 36-year high. China has stepped up coal production to try to contain rising commodity prices and also to address possible energy supply issues.

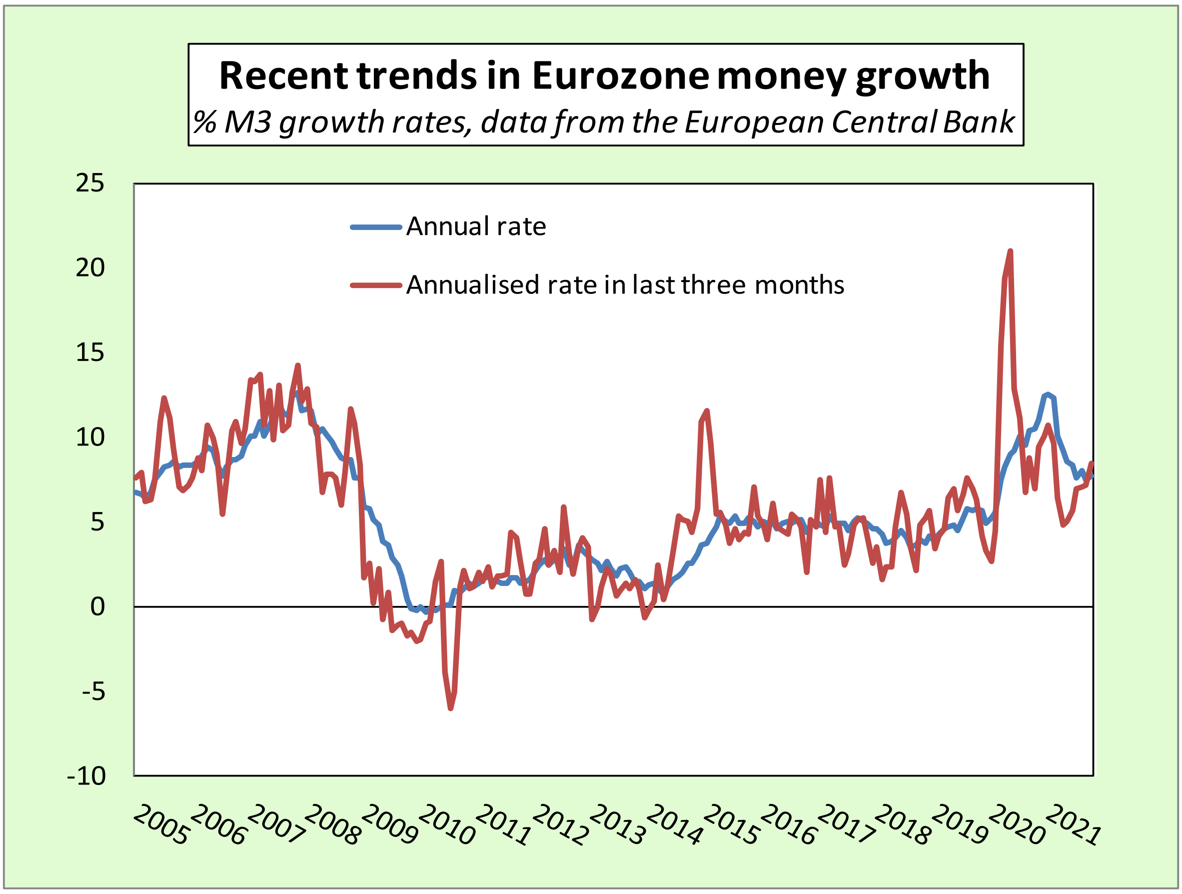
Tim Congdon and John Petley
20th December, 2021

	% annual growth rate:	
	M2	Nominal GDP
1991 - 2000	**24.5**	**18.4**
2001 - 2010	**18.5**	**15.2**
Seven years to 2017	**12.8**	**10.3**

Eurozone

	% annual/annualised growth rate:	
	M3	Nominal GDP
1996 – 2019	**5.2**	**3.1**
Nine years to 2019	**3.8**	**2.5**
Year to October 2021	**7.7**	**n/a**
Three months to October 2021 at annualised rate	**8.5**	**n/a**

Sources: European Central Bank for M3, Eurostat for GDP



Broad money growth continues on an upward trend

Summary: **In the three months to October 2021 the quantity of M3 broad money in the Eurozone grew at an annualized rate of 8.5%. On this metric (i.e., the annualized quarterly rate of increase), the 8.5% number was the highest since February and the seventh consecutive month in which it has risen. October saw M3 grow by €120b. (or by 0.8%). This was 2021's biggest one-month reading so far. Recent money growth has been much lower than in spring 2020, when the annualized quarterly rate of increase was remarkable and exceeded 15%, but it remains well above that typical in the 2010s. (The average annual rate of increase in M3 in the decade to December 2019 was 3.2%.)**

October saw prices rising at their fastest rate since the launch of the single currency. The overall rate across the 19-nation bloc was 4.9%, a notable advance on September's reading of 4.1%. Producer prices jumped by an astonishing 5.4% in the month of October, taking the increase in the year to 21.4%, another record for the Eurozone. Consumer inflation is likely to accelerate further. Germany, still the motor of the Eurozone economy, is now recording broad money growth below the average for the 19-nation bloc, while it is also seeing higher inflation. Consumer prices rose by 6.0% in the year to November, and numbers like 7% and 8% are clearly on the cards.

The ECB has no time left to tighten monetary policy this year. A page on the ECB's website dated 16th November entitled *Why is inflation currently so high*? reiterates the now familiar line that the rise in inflation reflects two influences, temporary supply-chain issues (including rising energy prices) and the one-off effects of Eurozone economies re-opening from Covid-19. No mention is made of the surge in broad money growth. The note insisted that raising interest rates now would "create unwarranted headwinds for the recovery". The ECB's stated view was that, "We are confident that inflation will decline in the course of 2022".

If the ECB winds up its Pandemic Emergency Purchase Programme (PEPP) on schedule in March next year, some moderation in broad money growth is likely. It has already started a modest "taper", as announced earlier in the year. In October, the ECB purchased €67.9b of assets under the PEPP scheme whereas the figure for July was €87.5b. The separate monthly €20b. asset purchases, introduced in 2019, are likely to continue and ECB President Christine Lagarde stated last month that she did not think that the conditions for raising interest rates would be satisfied in 2022. This statement was made before the arrival of the Omicron variant, but at a time when a number of Eurozone countries, including Germany, Austria, the Netherlands, Portugal and Belgium, were re-introducing lockdowns. These restrictions may perhaps dampen economic activity and maybe cool inflation slightly for a while if demand tails off. But any rebound in lending by Eurozone banks once these lockdowns are lifted will add further to money growth and reinforce upward pressures on inflation.

Tim Congdon and John Petley
20th December, 2021

	% annual growth rate:	
	M3	Nominal GDP
1996 – 2019	**5.2**	**3.1**
1996 – 2000	**4.6**	**4.1**
2001 – 2010	**6.8**	**3.1**
Nine years to 2019	**3.8**	**2.5**

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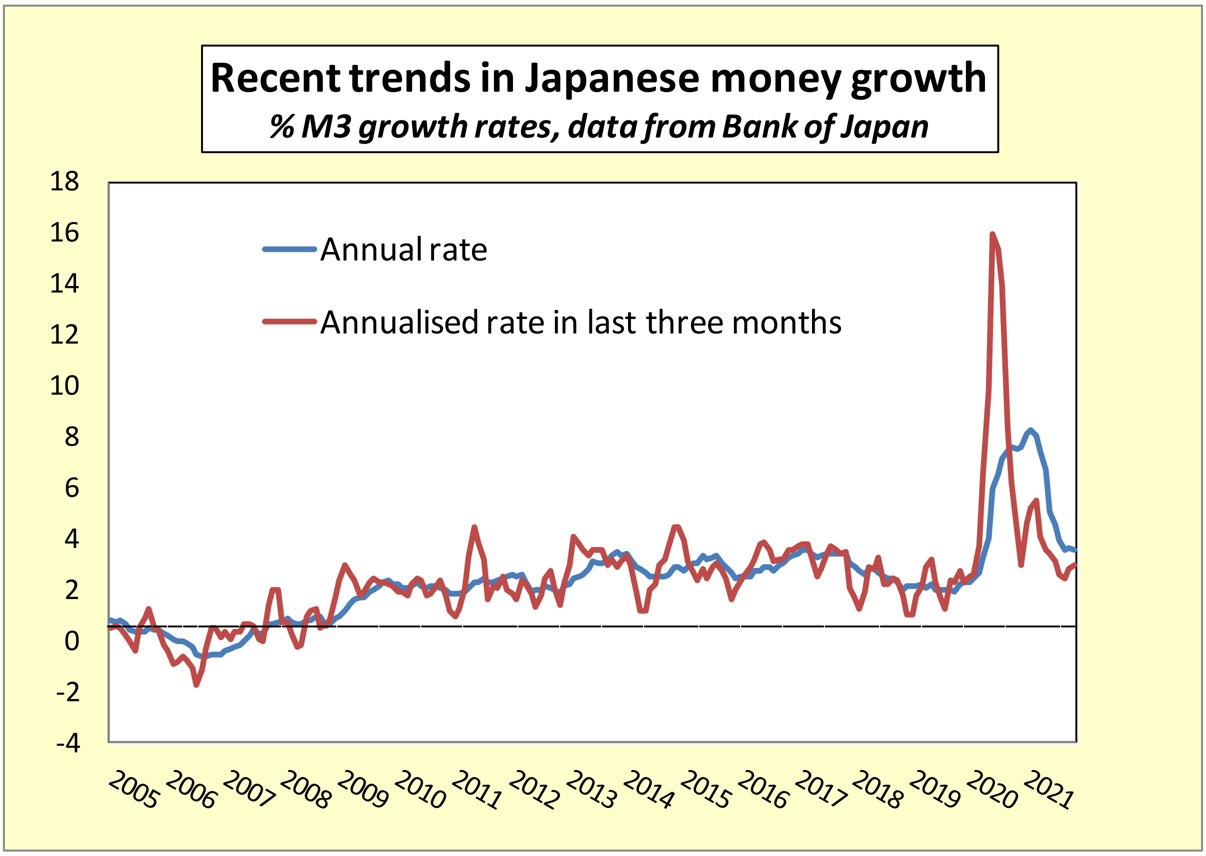
Japan

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2019	**3.9**	**1.9**
Nine years to 2019	**2.7**	**0.9**
Year to November 2021	**3.6**	**n/a**
Three month to November 2021 at annual rate	**2.9**	**n/a**

Sources: Bank of Japan for M3 and IMF for GDP



Broad money growth very low, but picks up slightly

Summary: **The three months to November 2021 saw Japanese M3 increase at an annualised rate of 2.9%, slightly higher than October's reading of 2.8%. These figures are significantly lower than the exceptional ones seen in spring 2020. The annual growth rate was little changed, falling from 3.7% in October to 3.6%.**

Japan has now recorded two consecutive months of positive inflation, albeit at a very modest level. Consumer prices rose by 0.1% in the year to October, following September's 0.2% increase. Producer prices rose by 9.0% in the year to November, the highest number for 40 years. December has seen the yen strengthen slightly against the US dollar after declining in October and November. With November also seeing a fall in the price of oil, upward pressure on manufacturers' costs may decline slightly. Thus far, most of the extra costs have been absorbed in the supply chain and have not yet reached the consumer. However, an inflation spike is inevitable in the next few months, which may enable the Bank of Japan finally to achieve its ambition of a 2% rise in consumer prices over a twelve-month period. On 15th November Governor Kuroda stated that he expected inflation to rise to 1% by the middle of next year. For once, the BoJ may be underestimating the strength of upward pressures on prices and costs. Three weeks later, his deputy, Masayoshi Amaiya, stated that Japan does not need to follow other central banks in tightening monetary policy for now.

He too acknowledged that prices were likely to rise in 2022, as companies passed on extra commodity and energy costs to consumers. He also said that a decision on whether or not to phase out the remaining pandemic relief programmes in March 2022 as planned would be taken at the January MPC meeting. The BoJ may be under-estimating inflation in 2022, but Maiya is likely to be correct that the scale of inflation is also going to be much lower in Japan than in most developed countries. Money and fiscal stimuli were smaller than elsewhere, and did not cause as great a spike in broad money growth.

Japanese GDP contracted by 0.9% in Q3 2021, following a modest 0.4% increase in the previous three months. The retail sector has been very weak, with consumer spending falling by 1.3% in Q3, which coincided with the peak of the coronavirus outbreak in the country.Thus far, the reduction in new cases and the easing of restrictions have not resulted in any significant increase in retail sales. Exports have performed well, however. They increased by 9.4% in the year to October, despite microchip-related problems in the automotive sector.

Bank credit to the private sector remains stagnant. The stock of bank loans was up by a modest 0.6% in the year to November, down from 0.9% in October. Part of the explanation may well be the surge in lending early in 2020 as Japanese companies sought to build up a buffer of cash as a contingency to tide them over the pandemic. Fumio Kishida, the new Prime Minister, has announced plans for a fiscal so-called stimulus package to boost the economy, amounting to 56 trillion yen (or about \$500b. at current exchange rates).

John Petley
10th December, 2021

	% annual growth rate:	
	M3	Nominal GDP
1981 – 1990	**9.2**	**4.6**
1991 - 2000	**2.4**	**1.1**
2001 - 2010	**1.0**	**0.8**
Nine years to 2019	**2.7**	**0.9**

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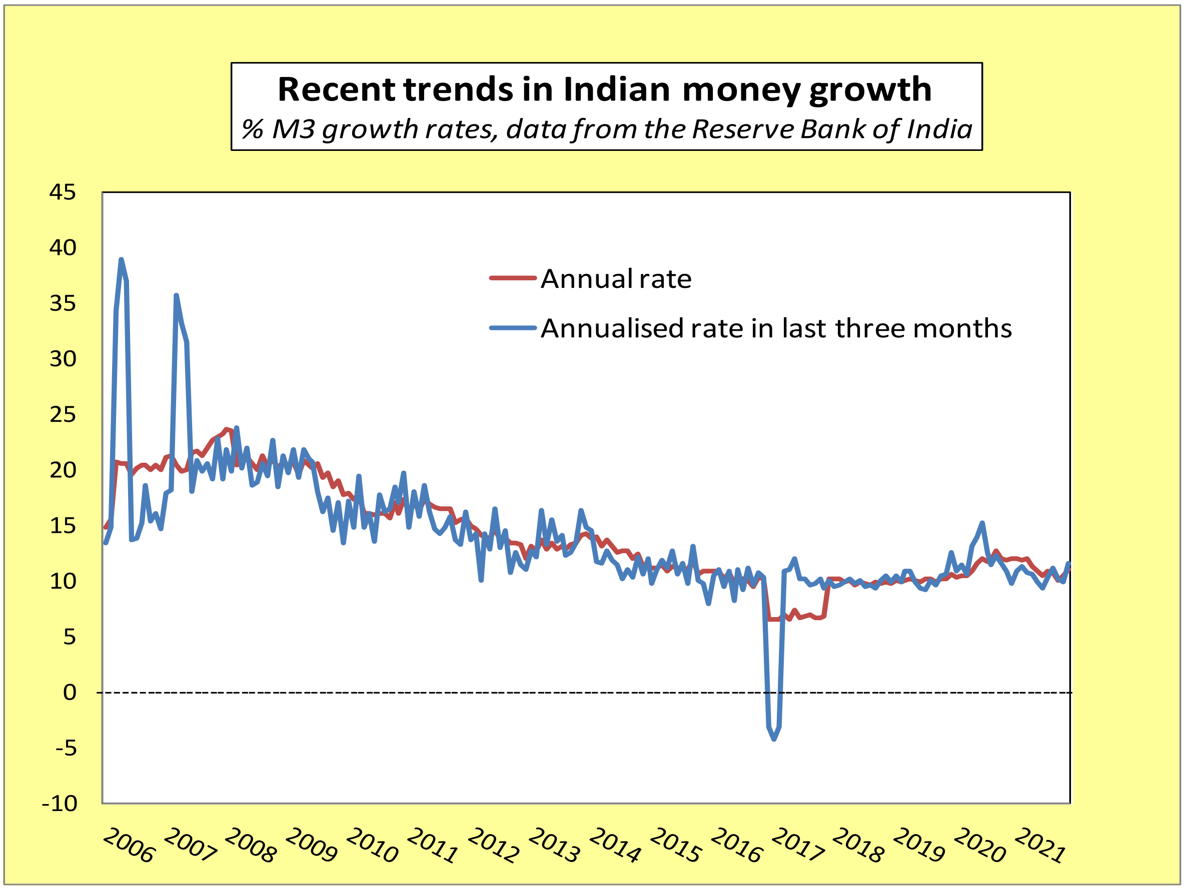
India

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2019	**15.8**	**13.4**
Nine years to 2019	**11.2**	**11.9**
Year to November 2021	**11.0**	**n/a**
Three months to November 2021 at annualised rate	**11.6**	**n/a**

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



Growth of bank credit and broad money strengthens

Summary: **In the three months to October 2021 India's seasonally adjusted M3 grew at an annualised rate of 11.6%, a significant increase on October's reading of 10.0% and the highest figure since May 2020. The annual growth rate picked up from 10.4% to 11.0%, the highest value since April.**

The dominant feature of the India monetary scene in the 18 months to mid-2021 was a squeeze on domestic credit coinciding with the Covid-19 medical emergency. "Bank credit" (almost entirely to the private sector) is a category in the Reserve Bank of India's twice-monthly release on scheduled banks' *Statement of Condition.* On 5th June 2021 it stood at 105,857b. rupees (roughly $1,500b.), little higher than at the end of 2019. (The 6th December 2019 value of "bank credit" was 102,537b. rupees.) The stagnation of bank credit in this period contrasts with the five years to end-2019, when it expanded at a compound annual rate of 9.5% and was the main driver of monetary expansion. Money growth nevertheless remained strong in the 18 months to mid-2021, partly because banks were required to finance a budget deficit much enlarged by Covid-19 and partly because the banking system increased its external assets. (The RBI's foreign exchange reserves advanced markedly.)

In the last six months bank credit to the private sector seems to have revived dramatically. The RBI's "bank credit" figure was 116,190b. rupees on 3rd December this year, up sharply – by 9.8% – from the corresponding June number.). (The 9.8% figure relates to six months and implies an annualized rate of increase of 20.6%.) The development may be temporary, but is striking. The RBI has in recent years been engaged on a mission to eliminate bad debts from India's banks and to boost their capital levels closer to the internationally-endorsed levels set by the Basel-based Bank for International Settlements. The mission appeared to be re-affirmed on 15th December, when the RBI published a statement that banks would from 1st April 2023 need to measure capital in accordance with the BIS's "standardized approach". The subject is political to some degree, because compliance with international rules will constrain banks' assets. The current Modi government, which does not conceal that it practices economic nationalism, is keen for Indian banks to support faster economic growth.

India saw the number of new coronavirus cases fall below 10,000 daily in early December, a sharp contrast from May and June when over 300,000 infections were being recorded on some days. Although the new Omicron variant has already appeared in the country, for now no hints of new restrictions are being announced. Inflation is on the rise, with higher fuel prices and a weather-related spike in food prices boosting the annual rate to 4.9% in the year to November, up from 4.2% the previous month. This is still within the government's 2%- 6% target range, but producer prices have now been climbing at over 10% per annum since April. November's producer price reading of 14.2% was the highest since 1988. In the 2020-21 financial year the government deficit was 9.3% of GDP, compared with a target figure for 2021-22 of 6.8%.

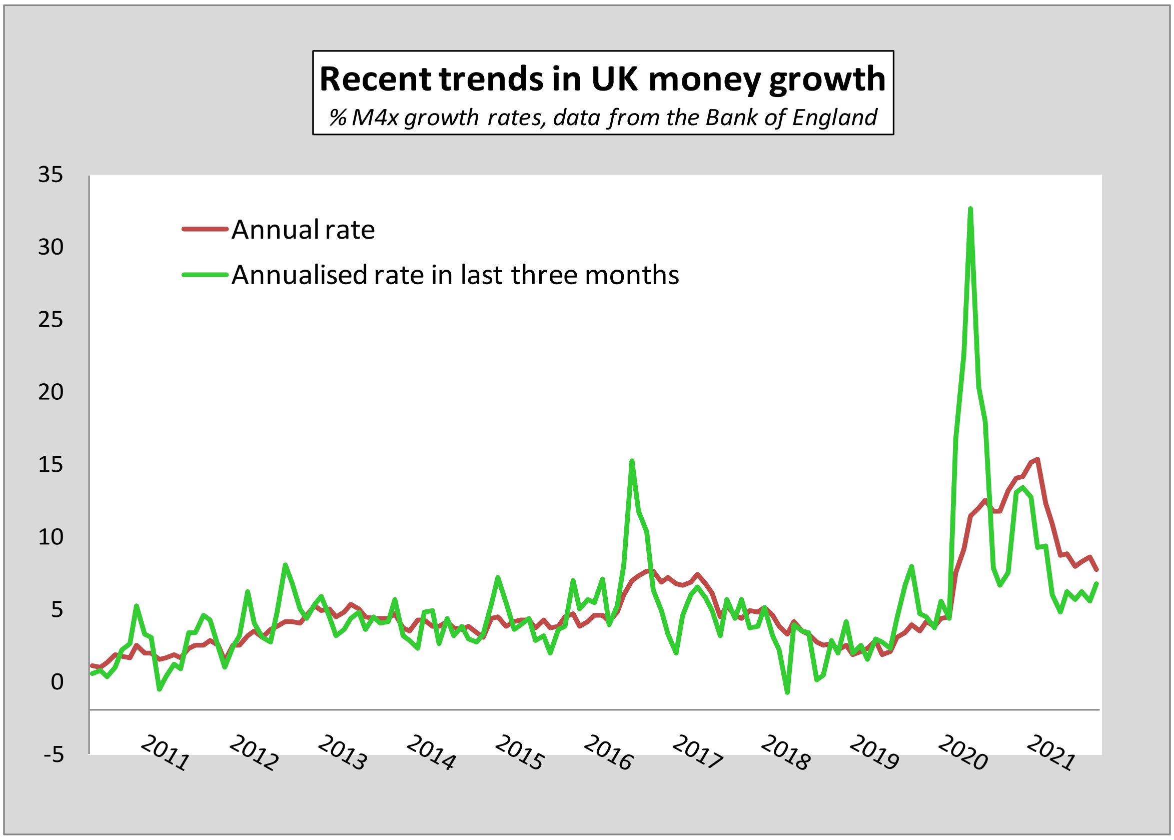
Tim Congdon
20th December, 2021

	% annual growth rate:	
	M3	Nominal GDP
1981 - 1990	**17.1**	**14.7**
1991 - 2000	**17.4**	**14.1**
2001 - 2010	**17.3**	**12.9**
Nine years to 2019	**11.2**	**11.9**

UK

	% annual/annualised growth rate:	
	M4x/M4 before 1997	Nominal GDP
1964 – 2019	**9.6**	**8.0**
Nine years to 2019	**4.0**	**3.7**
Year to October 2021	**7.9**	**n/a**
Three months to September 2021 at annualised rate	**6.7**	**n/a**

Sources: Bank of England and Office for National Statistics



Broad money growth remains at an elevated level

Summary: **In the three months to October 2021 UK M4x grew at an annualised rate of 6.7%. This was up on September's figure of 5.5% although considerably lower than the exceptional readings in the Covid emergency period between March 2020 and March 2021. A number of 6.7% is still above that typically recorded in the 2010s. (The average annual growth rate of M4x in the decade to 2019 was 3.8%.) In an economy where the trend rate of output growth is low, perhaps only 1% a year, annual money growth needs to be only 3% - 5% if the 2% inflation target has any hope of being met over the medium term.**

The Bank of England puzzled markets when it failed to raise interest rates in November, after having given signals that it would do so. It was then shocked by the announcement, on 15th December, of a 5.1% increase in the consumer price index in the year to November. A modest move in Bank rate, from 0.1% to 0.25%, came the next day.

Rising energy costs have been an important contributory cost factor, but higher prices both for food and second-hand cars have also added – in an arithmetical sense – to the upward pressure on inflation. With the annual increase in producer prices reaching 9.1% in November, a 13-year high, inflation will rise even higher in coming months. But, in an underlying causal sense, the explanation for the rise in inflation is to be sought in money growth numbers over the Covid-affected period. In the 20 months from February 2020 to October 2021 the M4x measure of broad money climbed by 19.8%, whereas in the preceding 20 months (from June 2018 to February 2020) it went up by only 5.8%. Growth rates of money and nominal GDP are related, even if they are not identical. The contrast between money growth for several years before the Covid emergency and during the Covid emergency is blatant. The Bank of England has only itself to blame for both above-target inflation and the criticisms it is now facing. In particular, the decision of its Monetary Policy Committee on 4th November 2020 to inaugurate another £150b. of "quantitative easing" has to be condemned as highly misjudged and inflationary.

Crucial will be the Bank's ability to dampen money growth in coming quarters, with the omicron variant adding to the difficulties in policy-making. Asset purchases (or QE) will surely stop soon. Much will then depend on how bank lending to the private sector behaves. A major part of it is mortgage lending, which is treated far more leniently in the Basel III bank capital regime than lending to corporates, particularly lending to small businesses. The "stamp duty holiday" for house-buyers finally ended on 30th September. Unsurprisingly, mortgage approvals fell by roughly 4,700 to 67,199.in October. Net mortgage lending (i.e., gross lending minus repayments) fell from £10.2b. in September to a mere £1.0b. in October. But signs of intense competition in the mortgage market are evident, and net mortgage lending of perhaps £5b. a month looks plausible in 2022. Much will therefore depend on bank lending to the corporate sector. One factor behind the sharp jump in broad money growth in October was an increase in net borrowing of £8.7b. by non-intermediate, non-bank financial companies.

John Petley
15th December, 2021

	% annual growth rate:	
,	M4/M4x	Nominal GDP
1964 - 2019	**9.6**	**8.0**
1991 – 2000	**6.4**	**6.0**
2001 – 2010	**6.5**	**3.9**
Nine years to 2019	**4.0**	**3.7**