INSTITUTE OF INTERNATIONAL MONETARY RESEARCH

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 – 21st June, 2022

Global money round-up in summer 2022

Money growth is now falling is the main economies of the advanced "Western" nations. A particularly sharp decline seems to be under way in the USA. As discussed on p. 7 below, the M3 measure of broad money was virtually static in April, while enough is known from the Federal Reserve's weekly H8 press release to be almost certain that the stagnation of bank deposits and broad money continued into May and will persist into June. So US money growth – which was at a post-war record high two years ago – has now been replaced by torpor. With inflation still rising, real money balances are being squeezed, and asset prices and economic activity are starting to suffer. In the European Central Bank has to behave more gingerly than the Fed, because a large rise in interest rates would translate into higher government bond yields and result in much increased debt interest costs. The meaning of the ECB's much-touted "anti-fragmentation" tool remains unclear, but one possibility is that the ECB will buy even more of the debt issued by the Italian, Spanish and other governments. Eurozone money growth has dropped back, but M3 was up at an annualised rate of almost 5% in the three months to April. As inflation is higher than that, the main European economies are – like the USA – experiencing a squeeze on real money balances, but it is not so severe.

The patterns in Asia are different. In China money growth may be edging up, perhaps to provide a friendly economic backdrop to the 20th National Congress of the Communist Party. Meanwhile the Bank of Japan is largely indifferent to the slide of the yen on the foreign exchanges and at its last meeting kept its interest rate at minus 0.1%. In the year to May Japan's M3 was up by a mere 2.8%. So the drift towards monetary policy tightening is not universal. 2023 may therefore see growth in output at the global level, although not much. For reference, world output fell by 2.0% in 2009, and gained only 0.5% in 1982 and 1.7% in 2001, with all three of these years having US recessions.

Money trends in mid-2022 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. The Covid-19 epidemic is becoming less important in most countries. The Institute's consistent analysis since spring 2020 – that money growth acceleration would lead to an inflationary boom and an upturn in inflation – has proved correct. The new areas of debate are the duration of above-normal inflation, with normality seen as an annual increase in consumer prices of 2% a year, and the risk that recessions will be needed to combat high inflation. Key principles here are that,

i. The rate of inflation is equal to the rate of increase in nominal GDP minus that of real GDP,
ii. Over the medium term, growth rates of broad money and nominal gross domestic product will be similar, although only rarely identical, and
iii. Just as a correlation holds between nominal money and nominal GDP, so one holds between real money and real output, and falls in real money are often associated with asset price weakness and recessions.

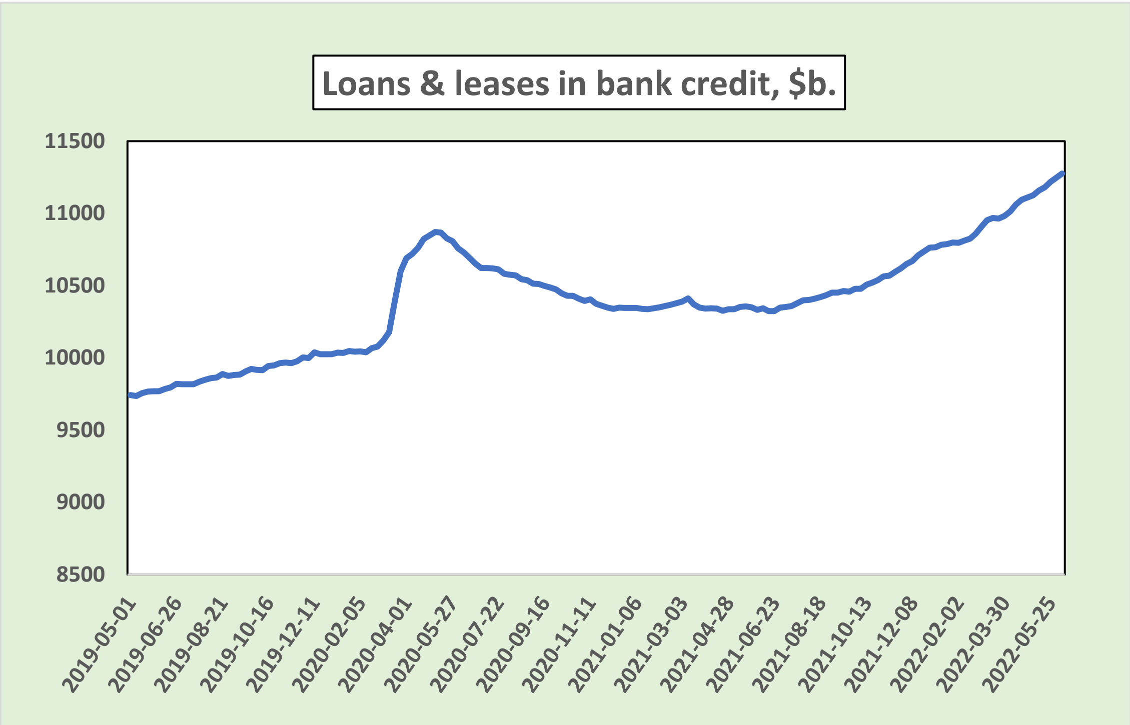
Much will therefore depend on rates of broad money growth in coming months and quarters, with the table below summarizing recent patterns in the leading nations. The table shows marked money growth reductions in the developed countries from the remarkable 2020 peaks. China is following its own path, with money growth rising slightly. In 2023 recessions in North America and Europe may still be reconciled with positive growth at the global level.

Name of country/ jurisdiction	Share of world output in 2020		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	15.4	24.7	**2.8**	**7.1**	Money growth stopped in spring 2022, implying severe squeeze on real money balances.
China	18.3	15.4	**12.3**	**10**.8	Money growth rising, amid property bust scares. Policy being eased, no official inflation concern.
Eurozone	12.1	17.4	**4.8**	**6.0**	Money growth moderating, as ECB worries about widening sovereign debt spreads.
Japan	3.7	6.0	**2.4**	**2.8**	Credit and money growth back to pre-Covid norms, implying little inflation in medium term.
India	6.8	3.1	**10.2**	**9.9**	Money growth running at roughly double-digit annual rates.
UK	2.2	3.3	**5.0**	**4.7**	Money growth low to moderate, after months of very weak bank lending to the private sector.

The recent moderation in money growth in the USA, the Eurozone, Japan and the UK implies that inflation will come down towards levels closer to the norms of the 2010s. However, the lags are such that both this year and 2023 will feature annual inflation rates typically above 5% and sometimes above 10%. The Ukraine tragedy will add some twists to the inflationary spiral, but it is certainly not the fundamental cause of the inflation of the early 2020s. This inflation episode – like all the others – is to be attributed to excessive growth of the quantity of money. The combination of falling growth in nominal money (and even the risk of outright falls in the quantity of money) and still high inflation implies declines in real money balances. A standard cyclical pattern is that such declines are accompanied by weakness in both asset prices and aggregate demand, and all too often by recessions (i.e., falls in output lasting longer than six months).

As noted here in recent months, crucial to money growth in the rest of 2022 will be the behaviour of bank lending to the private sector. In the two years to the first quarter of 2022 high or very high money growth in the main Western economies was almost entirely due to central bank asset purchases and monetary financing of budget deficits. The Institute's analysis has suggested that, as central bank asset purchases stop and budget deficits decline, money growth will decelerate *unless bank lending to the private sector revives strongly*. The patterns of bank asset acquisition have to be monitored and assessed.

In the USA bank credit to the private sector is now growing briskly, although the data are erratic from month to month. "Loans and leases in bank credit" (mostly bank lending to the private sector, and constituting over half of US commercial bank assets) increased in the 13 weeks to 8th June at an annualised rate of 12.3%. The resumption of growth in credit to the private sector dates to the middle of last year. In the year to 8h June "loans and leases" increased by 9.0%. That 9.0% figure – and the latest double-digit three-month annualised number– are higher than before Covid. The evidence behind anecdotal reports of US banks' keenness to lend – and of US companies' eagerness to borrow both the rebuild inventory and to anticipate price rises – seems increasingly correct.



If the annual rate of credit growth stays in the 8% - 10% vicinity consistently, and certainly if it moves out towards 15% annualised, the message will be that money growth has its own momentum from the private sector's behaviour. So it would continue if the Fed left its assets stock stable in value. That will affect the size of the interest rate rise needed to bring annual money growth back down to the 3% to 5% band compatible with 2% inflation. The faster is credit growth, the larger will be the required move in Fed funds rate. The degree of dynamism of private sector bank credit must be carefully watched.

Bearing in mind that Federal and state governments also have persisting deficits that must be financed, market fears of a rise in dollar interest rates in 2022 look plausible. Against that, the intended Fed sales of securities (i.e., "quantitative tightening") – of as much as $95b. a month from September– could reduce the M3 quantity of money by perhaps $50b (about 0.2%) a month. US banks' cash assets have fallen heavily in recent months, although the Fed's announcements on asset shrinkage have related to the period after 1st June. As far as the analyst is concerned, there is no alternative to checking the numbers month by month. *It needs to be emphasized that bank deposits in the US commercial banking system have been static in recent weeks. Such deposits – which constitute most of M3 broad money – were 0.4% lower on 8th June than on 9th March.*

In the Eurozone the stock of credit to the private sector was 4.8% higher in April 2022 than a year earlier. The stock of loans for house purchase was up by 5.3% in the year to April, whereas loans to non-financial corporations (i.e., industry and commerce) advanced 4.5% in the same period. Loans to all corporations, financial and non-financial, increased by 1.6% (or at an annualized rate of 6.7%) in the three months to April. European governments are still doing their best to persuade the Basel-based Bank for International Settlements, and the European Commission, that further large increases in banks' capital requirements are unnecessary and would damage the ability of their financial systems to sustain the recovery. They seem to be having some success in these efforts, despite the concurrent drives by regulatory officialdom for greater "greenery", central bank digital currencies, better corporate governance and the like. The Ukraine crisis has led to a more tolerant attitude towards lending to the European oil and gas sector.

In Japan bank lending to the private sector surged in the opening months of the Covid pandemic, but the loans have been largely repaid with the return of medical normality. Lending to the private sector is now extremely weak.

UK bank regulators seem to believe that the higher are bank capital/ asset ratios, the safer is the banking system and the better is the outlook for the economy. With inordinate amounts of capital required in commercial banking, banking groups are allocating capital to other activities. Large banks are not hiding their reluctance to commit new capital to mainstream UK commercial banking. The problem is being made worse by a decision taken by the Prudential Regulation Authority, of the Bank of England, at the end of last year, to increase from December 2022 UK banks' counter-cyclical capital buffer to 1% from zero. As explained here last month, the imposition of the extra 1% capital is – by itself – deflationary. The argument can be made that regulation has destroyed the incentive for bank stakeholders to grow their loan portfolios. (See the Institute's recent research papers – by David Llewellyn and myself – on these topics,

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https://mv-pt.org/wp-content/uploads/2021/10/2021-10-06-Research-Paper-9-Congdon-Screen.pdf

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The April money data contained a surprise. In the six months to March M4xL (i.e., bank lending excluding that to intermediate other financial corporations) averaged £5.6b. But in March itself the figure was £21.1b. The explanation was a jump in bank lending to the mainstream, non-intermediate financial sector of £13.9b., which contrasted with actual falls in the loans to this sector in the previous three months. Last month it was suggested here that an exceptional, non-recurring transaction was responsible and a new trend had not been established. That seems to be confirmed by the May data, when the mainstream, non-intermediate financial sector repaid £9.3b. of loans. The stock of bank lending is growing in the UK, but not rapidly.

To repeat the point I have been making here so far this year, in 2022 and 2023 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 once the pandemic-related weakness in aggregate demand lies in the past. Central banks are now ending asset purchase programmes and in some instance are starting to reduce their asset piles. A reduction in money growth is a condition of the return of moderate inflation. Robust bank lending to the private sector is in many ways desirable, because of its contribution to wider economic efficiency.

But fast expansion of banks' loan portfolios will make it more difficult to deliver the needed reduction in money growth. 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 nominal interest rates, and indeed extremely negative real interest rates, a big boom in private sector bank credit is not imminent in Japan or the UK. But a strong recovery in such credit in the USA has begun, and the Eurozone is seeing signs of life.

21st June, 2022

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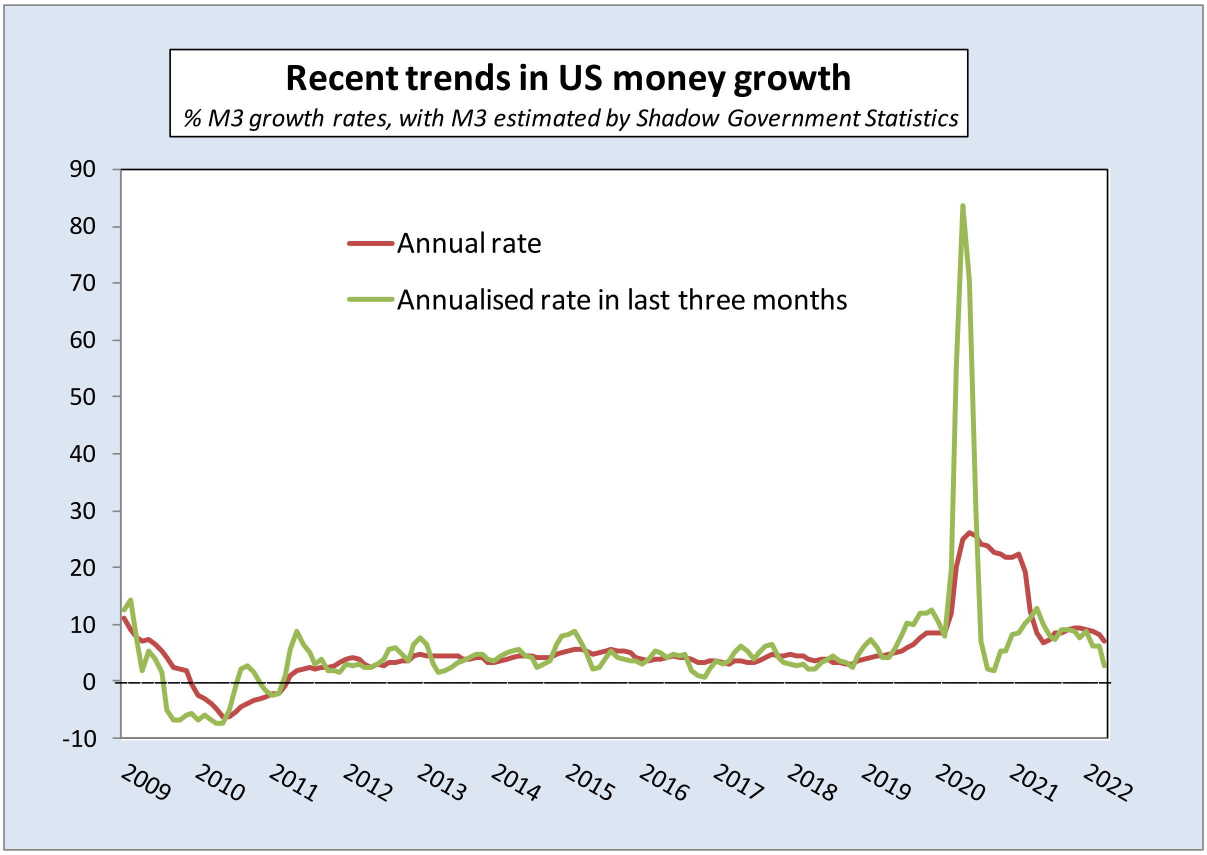
USA

	% annual/annualised growth rate:	
	M3	Nominal GDP
1961 – 2020	**7.7**	**6.3**
Ten years to 2020	**6.2**	**3.4**
Year to April 2022	**7.1**	**n.a**
Three months to April 2022 at annualised rate	**2.8**	**n.a.**

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



US broad money growth stopped in spring 2022

Summary: US broad money declined by $1b. during April. This brought down the annualised quarterly rate of M3 growth from 6.1% in March to 2,8%, the slowest rate of increase since November 2018. Meanwhile weekly data on bank balance sheets from the Fed argue that broad money was flat in May and is going sideways in June. (Our M3 data come from Shadow Government Statistics.)

US inflation has risen to levels unsurpassed since the early 1980s. This recent sharp rise in consumer prices after over two decades of relatively low inflation has become a major political issue. On 31st May, President Biden summoned Fed Chairman Jay Powell and his predecessor, Treasury Secretary Janet Yellen, to a meeting to discuss the subject. Biden insisted that fighting inflation was his top priority, albeit affirming that the conduct of monetary policy was the responsibility of the central bank. Biden seems to have abandoned a $2 trillion "Build Back Better" fiscal package due to worries about inflation. Yellen, who never made any mention of money during her tenure at the Fed, admitted that in 2021 she had been wrong about the path inflation would take. Even without this pressure from the White House, a number of senior figures at the Fed had already expressed their support for monetary tightening. His colleague, James Bullard from the St Louis Fed, expressed a desire to see the Fed funds rate raised to 3.5% by the end of the year. This may well come to pass. At its meeting on 14th - 15th June, the Federal Open Market Committee voted to raise the Fed Funds Rate by 0.75%, taking the cost of borrowing to 1.5% - 1.75%.

But the top brass at the Fed and the US Treasury say next to nothing about 2020's surge in money growth, which has been the underlying cause of the current inflation episode. Latest developments in US commercial banks must be monitored closely. The key point is that deposits of $18,068b. at US commercial banks on 8th June – the last date for which numbers are available – were *lower* than 15 weeks earlier at 23rd February, when they were $18,105b. Since such deposits are about two-thirds of M3 broad money, a fair conjecture is that money was static in May and will not grow much in June.

The stagnation of money is surprising in one respect, in that bank lending to the private sector has been buoyant. From the start of December last year to 8th June their "loans and leases" (i.e., their lending to the private sector, more or less) rose from $10,649b. to $11,274b. or by 5.9%, implying an annualised rate of increase into the double digits per cent. In the normal course of events bank make loans by expanding the two sides of their balance sheets by identical amounts, so that extra loans imply extra deposits (i.e., more money in the economy). But in recent months US banks have been shedding cash assets at a remarkable pace.

Tim Congdon and John Petley
20th June, 2022

	% annual growth rate:	
	M3	Nominal GDP
1961 – 2020	**7.7**	**6.3**
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**
2011 - 2020	**6.2**	**3.4**

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China

	% annual/annualised growth rate:	
	M2	Nominal GDP
1991- 2020	**18.4**	**14.5**
2011 - 2020	**11.7**	**10.0**
Year to May 2022	**10.8**	**n/a**
Three months to May 2022 annualised rate	**12.3**	**n/a**

Sources: People's Bank of China for M2, IMF and Institute's own estimates

Broad money growth picks up

***Summary*: In the three months to May 2022 China's seasonally adjusted M2 grew at an annualised rate of 12.3%. This is the highest reading since June 2020, a significant increase on April's 10.8% and the eighth consecutive three-month period when annualised broad money growth has been above 10%. The annual rate of increase rose from 10.4% to 10.8%, again the highest value for two years.**

While "Western" central banks continue to increase the cost of borrowing in an attempt to calm inflation, China's economy follows a different trajectory. Monetary policy has been loosened during the last two months and this has led to an increase in broad money growth. This may be partly a result of China's ongoing "zero covid" strategy which involves, if necessary, locking down entire cities to counteract any major outbreaks of coronavirus. At the end of May when extensive lockdowns in Shanghai and Beijing were lifted, things seemed to returning to normal. But a number of new cases have recently been reported and restrictions have been re-imposed in parts of Shanghai. These lockdowns have affected demand and output as well as employment. Retail sales have declined, with April's reading 11.1% lower than 12 months previous. The unemployment level rose to 6.1% in April. Apart from a short-lived spike at the very start of the pandemic in February 2020, this is the highest rate of unemployment in over 25 years. Furthermore, China's housing boom is now well and truly over. House prices only rose by 0.7% in the year to April, the weakest rise since October 2015 while the year to April saw a 47% decline in property sales.

After trying to dampen demand and in particular, to deter speculation, the People's Bank of China (the country's central bank) is now seeking to revive the housing market. The PBoC reduced the mortgage reference rate in May, the second such reduction this year. This move is typical of its current policy of targeted cuts to specific rates rather than more general cuts in interest rates. The key rates for household and business credit were left unchanged in May in spite of the weakest increase in loan growth in over a decade – a mere 10.9% in the year to April. Chinese exports nonetheless are still performing well. May saw an annual increase of 16.9%, a significant improvement on April's 3.9% increase Inflation was unchanged at 2.1% in the year to April, well below the government's 3% target. Producer prices rose at 6.4%, the slowest rate of increase in over a year.

There may be scope for further loosening, if desired. A prosperous macroeconomic background would fit into Xi Jinping's agenda, as he seeks appointment for life as chairman of the Communist Party at the party's 20th National Congress. However, many signs are emerging that the Chinese economy has lost much of the remarkable dynamism of recent decades. If the underlying trend growth rate of output has dropped to 4% a year, money growth of 10% plus will eventually prove inflationary. Admittedly, for now inflation is not a problem.

John Petley
14th June, 2022

	M2	Nominal GDP
1991 - 2000	**24.5**	**18.5**
2001 - 2010	**18.4**	**15.2**
2011 - 2020	**11.7**	**10.0**

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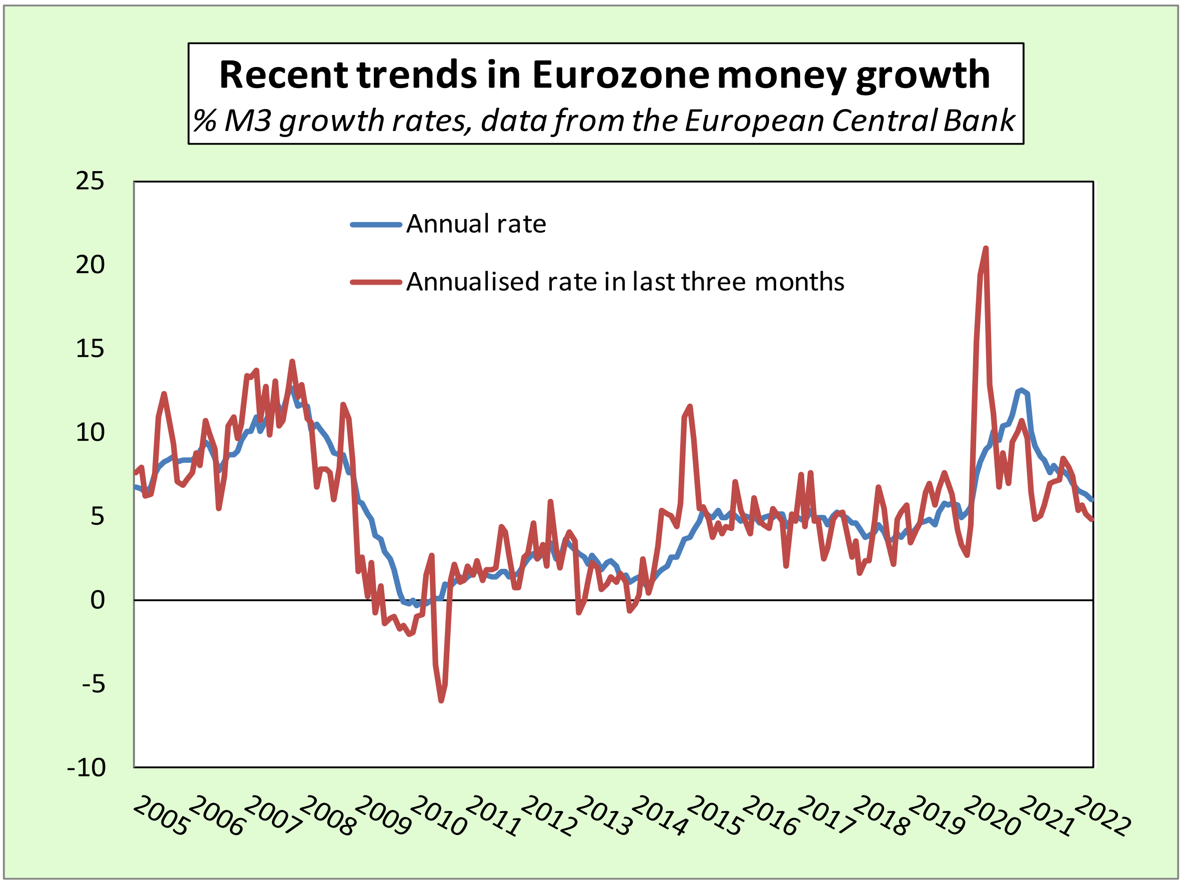
Eurozone

	% annual/annualised growth rate:	
	M3	Nominal GDP
1996 – 2020	**5.5**	**2.7**
Ten years to 2020	**4.6**	**1.6**
Year to April 2022	**6.0**	**n/a**
Three months to April 2022 at annualised rate	**4.8**	**n/a**

Sources: European Central Bank, Eurostat and the Institute's own estimates



Broad money growth continues to slow

Summary: **In the three months to April 2021 the quantity of broad money in the Eurozone grew at an annualized rate of 4.8%, lower than March's reading of 5.1% and indeed the weakest growth since February 2020, before the coronavirus pandemic. Broad money grew by only €23b. during April, the lowest monthly increase since August 2020.**

The ECB has not been in any hurry to raise interest rates despite rising inflation, and it has not indicated any urgency in reducing its asset pile. Money growth is slowing, but at a gentler rate than in the USA. After the meeting of the governing council on 9th June, however, it announced that the first rate hike in 11 years would follow its next meeting, scheduled for 21st July. Interest rates will be increased from 0% to 0.25%. It also stated that rates could be raised further after its September meeting and that the increase could be larger if inflation remains a problem. The ECB also confirmed that the 2019 Asset Purchase Scheme (APS) will be terminated on 1st July. This means that the €20b. worth of assets purchased this month will be the final addition to the ECB's balance sheet in the current cyclical episode. Unlike the Bank of England or the Fed, the ECB does not intend to run off or sell any of these assets for the time being. Assets purchased under the Pandemic Emergency Purchase Programme (PEPP), which expired in March, are scheduled to be reinvested until at least the end of 2024. Meanwhile those purchased under the APS will be reinvested "for an extended period of time past the date when it starts raising the key ECB interest rates".

The imminent termination of all asset purchases means that the creation of bank deposits through the extension of new credit to businesses and households will assume a greater role in driving broad money growth. At the moment, there does seem to be something of a resurgence in bank lending. The stock of loans to businesses grew by 4.5% in the year to April, a bit stronger than March's reading of 3.5%. The stock of mortgage lending in April 2022 was 5.3% higher than a year earlier. .

The retail sector also remains reasonably buoyant in spite of rising inflation. Industrial production rose by 0.4% in April, following a 1.4% decline in March. Across the 19-nation bloc, consumer prices rose by 8.1% in the year to May. This is an all-time high since the launch of the single currency. With producer prices increasing by no less than 37.2% in the year to April, inflation is likely to rise higher still as companies cannot be expected to absorb rises in production costs on this scale. The inflation figures for some individual member states are much higher than the average, although the most recent figure for Germany, 7.9%, is lower.

John Petley
14th June, 2022

	% annual growth rate:	
	M3	Nominal GDP
1996 – 2020	**5.5**	**2.7**
1996 – 2000	**4.6**	**4.1**
2001 – 2010	**6.8**	**3.1**
2011 - 2020	**4.6**	**1.6**

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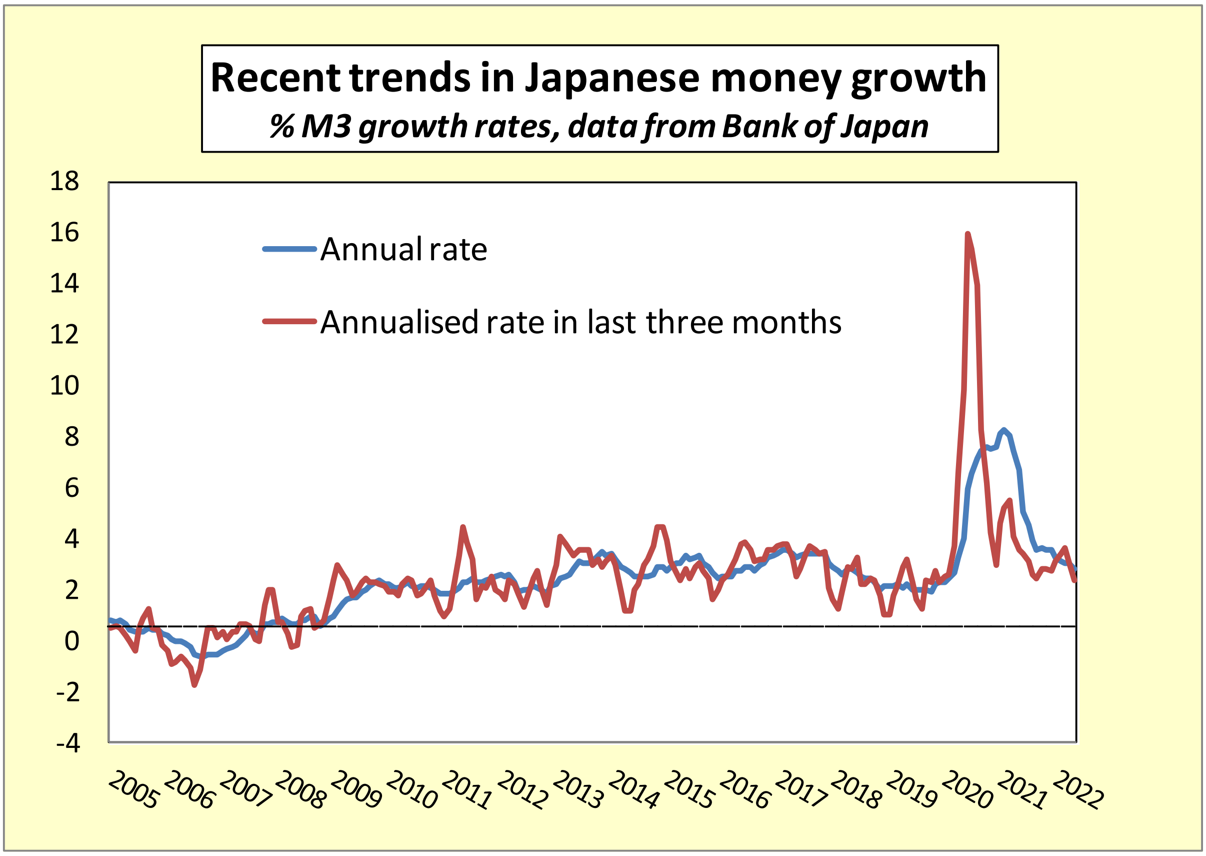
Japan

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2020	**3.9**	**1.7**
Ten years to 2020	**3.2**	**0.3**
Year to May 2022	**2.8**	**n/a**
Three months to May 2022 at annualised rate	**2.4**	**n/a**

Sources: Bank of Japan for M3 and IMF for GDP



Broad money growth falls back to pre-pandemic levels

Summary: **The three months to May 2022 saw Japanese M3 increase at an annualised rate of 2.4%, a drop from April's figure of 3.1% and the lowest reading since September 2021. The annual rate of growth also fell, declining from 3.0% in March to a two-year low of 2.8%. Broad money growth was particularly weak in May itself, with an increase of only 12 trillion yen, in contrast to April's downwardly revised figure of 43 trillion.**

Consumer prices rose by 2.5% in the year to April, the first time in seven years that it has not undershot the Bank of Japan's 2% target. There is little likelihood that the BoJ will deviate from its very loose policy settings. It may even be relaxed about inflation above 2%, after so many years of price stagnation/stability. The BoJ indeed has increased its purchases of long-dated Japanese government bonds as it fights to prevent yields rising above its 0.25% announced yield cap for 10-year bonds. With the BoJ now increasingly itself rather out of step with other central banks in not tightening monetary policy, the yen continues to weaken. It fell to a 24-year low against the US dollar in June and has declined in value against the American currency by nearly 20% since March.

The weakness of the yen has pushed up producer prices, which rose by 9.1% in the year to May. Although April's reading was higher at 9.8%, these high values point to inflation remaining at elevated levels by Japanese standards for some months. But the prospect of double-digit inflation is remote. The ultimate cause of inflation is excessive money growth, as the last two years of experience in North America and Europe have demonstrated with marked clarity. Money growth did accelerate in Japan in 2020, but the annual rate of increase never much exceeded 8%. Furthermore, money growth fell back to more typical Japanese levels of less than 4% by the spring of 2021. This suggests that inflation will remain moderate in Japan, while the countries of North America and Europe experience inflation at or close to double-digit annual rates.

Looking further ahead, Japanese money growth could well revert to similar levels to those of the previous decade. The Bank of Japan continues to focus on boosting the monetary base, in spite of its relatively modest effect on broad money growth – or indeed, on the wider economy. With growth in new bank credit currently at a very low level, there will be little boost to broad money by the creation of new bank deposits from new loans. Since the summer of 2021, loan growth has consistently remained at 1% or lower. The BoJ's bond purchases and monetary financing of the budget deficit have instead been the key factors at work in creating new money balances. New monetary initiatives from the BoJ do not seem very likely, especially with some MPC members expressing concern a year ago that an ultra-loose monetary policy cannot be continued indefinitely. The new Japanese Prime Minister, Fumio Kishida, is keen to use fiscal policy to stimulate the economy, but so far his relatively big spending budgets have had little effect. Japanese GDP shrank by 0.1% in the first quarter of 2022 and the money numbers do not suggest that any uptick is imminent.

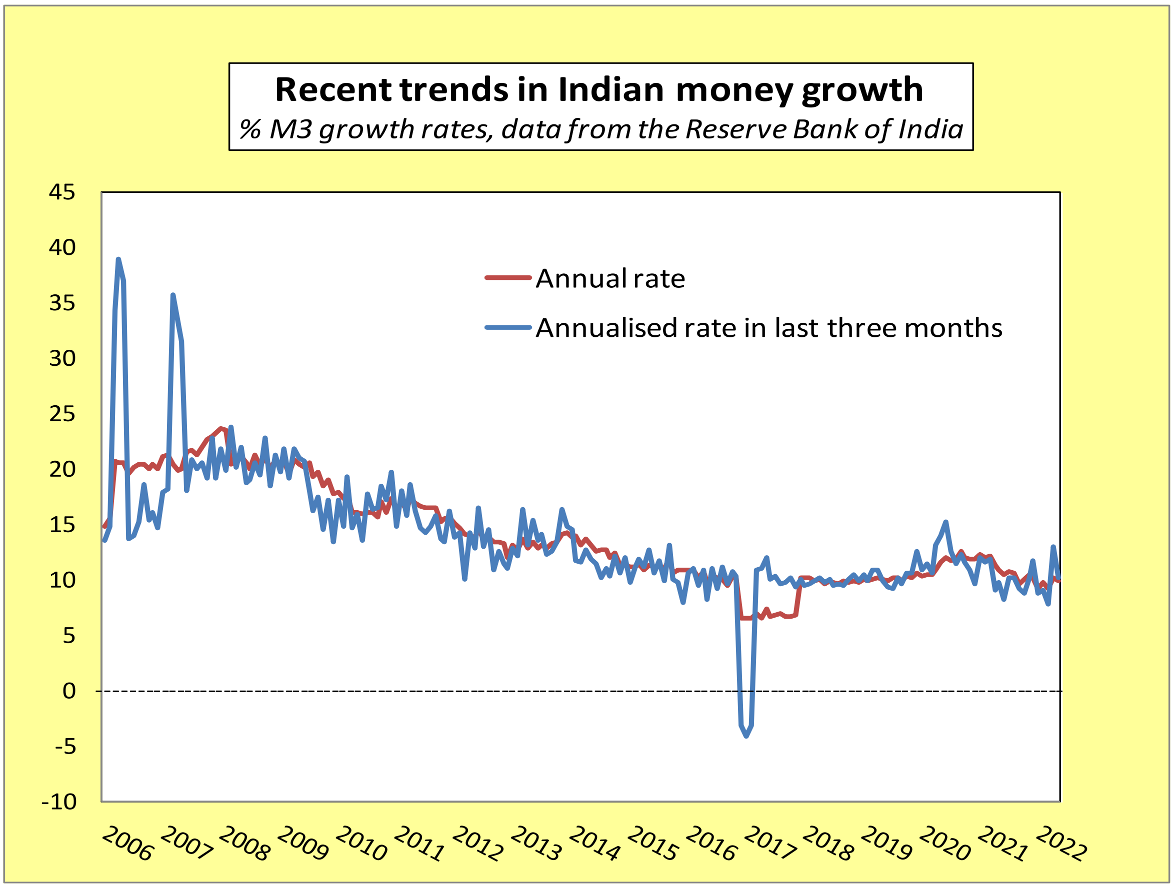
John Petley
16th June, 2022

	% annual growth rate:	
	M3	Nominal GDP
1981 – 1990	**9.2**	**4.6**
1991 - 2000	**2.4**	**1.1**
2001 - 2010	**1.0**	**0.8**
2011 - 2020	**3.1**	**0.3**

India

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2020	**15.8**	**12.9**
Ten years to 2020	**11.3**	**9.8**
Year to May 2022	**9.9**	**n/a**
Three months to May 2022 at annualised rate	**10.2**	**n/a**

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



Broad money growth slows again

Summary: **In the three months to May 2022 India's seasonally adjusted M3 grew at an annualised rate of 10.2%. This is substantially lower than the 13.2% recorded in April. April itself saw very strong broad money growth which caused the annualised quarterly growth rate to rise sharply from March's figure of 7.8%. However, this trend did not continue into May. The annual growth rate also fell back, from 10.2% in April to 9.9%.**

An acceleration in the growth of bank credit to the private sector has occurred since 2020. The stock of such credit is now showing annual growth rates into the double digits, whereas in 2020 the rate of increase was typically in the mid- single digits. Another influence on the relatively strong broad money growth of recent months has been the monetization of government debt. Fiscal expenditure rose steadily for most the past year, driven largely by substantial infrastructure projects.

India's central bank, the Reserve Bank of India, is now tightening monetary policy, amid concerns about persistently high inflation. As far back as 5th April it insisted in public statements that it would focus on reducing inflation, even if this meant slower growth. At its regular meeting on 8th June, it announced that the cost of borrowing would be raised by 0.5%. This follows hot on the heels of a 0.4% increase announced at a non-scheduled meeting less than a month earlier. The annual consumer inflation rate actually fell from 7.8% in April to 7.0%, but this is the fifth consecutive month in which it has been higher than 6%, the top end of the RBI's target range. India's commercial banks have also been under pressure from the RBI to write off bad debts while at the same time it is demanding that they operate with capital levels close to the international norms determined by the Bank of International Settlements (the so-called Basel III rules). The RBI's determination to clean up India's banks – and in particular, to address their excessively relaxed approach to loan defaults – is understandable, but these reforms may well reduce banks' enthusiasm for risk and thus cause broad money growth to slow further.

As a major energy importer, India has also faced the double problem of rising commodity prices and a weakening rupee, which is currently trading at an all-time low against the US dollar. With the USA now firmly committed to drastic monetary tightening, the rupee is likely to weaken further. India has been selling some of its foreign exchange reserves in an attempt to stop the rupee's decline. Approximately $30b. has been sold since March. The increases in interest rates have affected bond yields, which have continued to climb, with that on the 10-year government bond reaching a three-year high of 7.6% in June. The Indian government has nonetheless announced a substantial $26b. fiscal package, including tax cuts on fuel and agricultural subsidies. If this is again financed through the banking system, it should to a degree compensate for the effects which higher interest rates and tighter banking regulation will have on broad money growth.

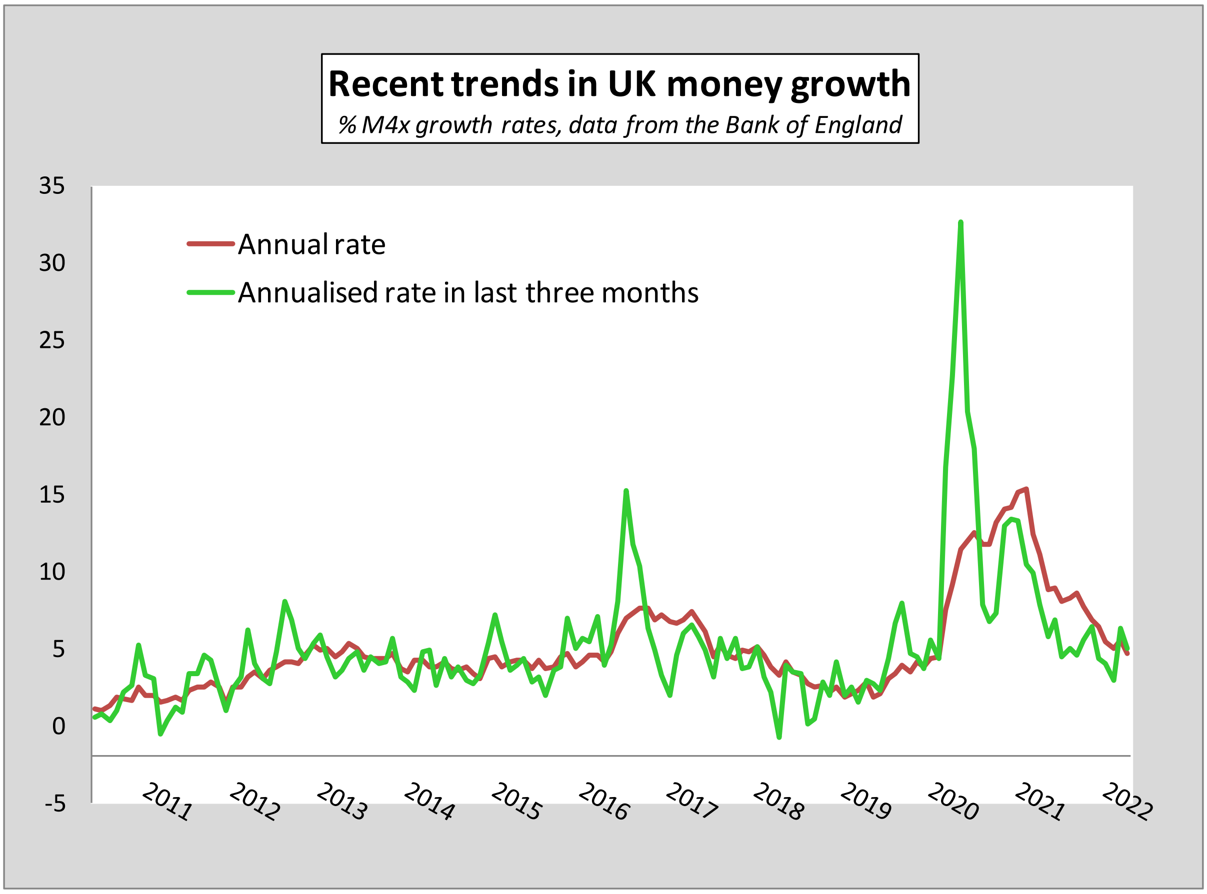
John Petley
16th June, 2022

	% annual growth rate:	
	M3	Nominal GDP
1981 - 1990	**17.3**	**14.7**
1991 - 2000	**17.2**	**14.1**
2001 - 2010	**17.3**	**13.6**
2011 - 2020	**11.6**	**9.9**

UK

	% annual/annualised growth rate:	
	M4x/M4 before 1997	Nominal GDP
1961 – 2020	**9.3**	**7.6**
Ten years to 2020	**5.2**	**2.3**
Year to April 2022	**4.7**	**n/a**
Three months to April 2022 at annualised rate	**5.0**	**n/a**

Sources: Bank of England and Office for National Statistics



Broad money growth slows down

***Summary*: In the three months to April 2022, UK M4x broad money increased at an annualised rate of 5.0%, significantly lower than March's reading of 6.3% After March's strong growth of over £25b., broad money rose by only £1.1b. in April. This also brought down the annual rate of growth from 5.5% to 4.7%, the slowest in more than two years.**

March's strong money growth proved to be a one-off. It has been followed by the smallest increase in M4x since August 2020. Broad money growth is likely to slow further in the coming months. On 16th June, the Bank's Monetary Policy Committee voted by 6 to 3 to raise the Bank rate by a further 0.25%, taking it to 1.25%. This is the fifth consecutive hike in borrowing costs and comes in the wake of annual consumer price inflation rising to 9.0% in April. Significantly, the three dissenting MPC member wanted a 0.5% increase. The statement issued after the meeting hinted that further increases may be implemented if inflation proves to be persistent. Indeed, the BoE itself now predicts that inflation will not peak until the final quarter of the year after climbing to double-digit levels. The BoE also intends to reduce its balance sheet by "running off" assets as they mature.

These moves come at a time when the growth in bank credit to the private sector is appears to be stalling. April saw a £9.3b. decline in the stock of bank lending to the financial sector after March's remarkable £13.5b. increase. Bank lending to the non-financial sector also declined. Households are continuing to borrow, but April's £5.7b. increase in new loans was lower than the figures for any of the three previous months.

In its statement following June's MPC meeting, the MPC offered an analysis of the causes of the current inflationary spike. Global energy price shocks and the war in Ukraine were mentioned, along with the tight domestic labour market. No mention was made of the surge in board money during the spring of 2020. Speaking in Vienna last month at a conference hosted by the Austrian Central Bank, BoE Governor, Andrew Bailey, denied responsibility for the high rate of inflation. One of his concerns may have been criticism from one of his predecessors, Lord Mervyn King, in a November 2021 lecture to the Institute of International Monetary Research. King argued that the asset purchase programme which was launched to counter the economic effects of the coronavirus pandemic (and which caused broad money growth to grow so dramatically) was unnecessary. This suggests that no notice will be taken of a possible contraction in broad money growth in coming months. The Bank's decision in March to delay the implementation of the remaining Basel III standards until January 2025 at least puts back one deterrent to new bank lending by two years. Likewise, the Prudential Regulation Authority's removal of an extra capital buffer requirement – introduced as a precautionary measure during the coronavirus pandemic – will benefit any expansion plans the banks may have.

John Petley
13th June, 2022

	% annual growth rate:	
,	M4/M4x	Nominal GDP
1961 - 2020	**9.3**	**7.6**
1991 – 2000	**6.4**	**6.0**
2001 – 2010	**6.5**	**3.9**
2011 – 2020	**5.2**	**2.3**