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Monthly e-mail from Tim Congdon and John Petley – 24th April, 2020

Global money round-up in spring 2020

Covid-19-related lockdowns in numerous countries, including those with the biggest economies, will cause 2020 to suffer the largest fall in global output since the 1930s. **But events today are very different from those 90 years ago. From 1929 to 1933 several nations saw their banking systems implode, with contractions of balance sheets and the large-scale destruction of money balances.** The result was a persistent deflationary malaise. By contrast, today governments and central banks are engaged in a binge of so-called “fiscal and monetary stimulus”. The situation is evolving rapidly, almost week by week, but it is already clear that **the United States of America may in 2020 or early 2021 record the fastest increase in the quantity of money, broadly-defined, in its peacetime history.** The growth of US M3 (as estimated by Shadow Government Statistics) was no less than 3.9% in the one month of March, and could be 4% - 5% in April. The rate of increase in the quantity of money in a mere two-month period could be higher than in any full year in the 2010s.

Other countries have not lurched so dramatically towards “stimulus” as the USA. However, in the Eurozone Stability and Growth Pact constraints have ceased to apply, at least for a few quarters. There and in the UK budget deficits are widening and a considerable volume of monetary financing is to be expected. Even in China and Japan signs have emerged of a major move towards monetary easing. Policy-makers seem indifferent to the medium-term inflation risks inherent in monetary financing of budget deficits and the associated acceleration of money growth. In the short run this complacency about inflation will be justified by the benign effects of the oil price collapse on the main price indices. **But in 2021 and 2022 the current oil price collapse may be succeeded by an oil price surge, while excess money balances have their usual effects (on asset prices, demand, etc).**

Money trends in early 2020 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. At present the covid-19 coronavirus outbreak dominates the news, and for some weeks has caused havoc to both the world economy and global macroeconomic forecasts. The damage to travel – and then to related industries, such as hotels, leisure, catering and conferences, and also to the demand for travel-related commodities (oil, for example) – is severe and far-reaching. Moreover, the longer the lockdown continues, the greater that damage will be. The damage is not just to output, but also to budget deficits because of the consequent loss of tax revenue. At any rate, governments and central banks have taken drastic measures to mitigate the impact of losses to output and income. Budget deficits have widened sharply, while central banks have taken stimulatory action (by cutting interest rates to almost zero, and by asset purchases and monetary financing of the enlarged budget deficits). In the USA the boost to money balances in only a few weeks has been extraordinary and may be part of the explanation for a 25% surge in equity markets in a month. (At the date of writing – 24th April – the S & P 500 index is down a mere 4% on a year ago.) World output will undoubtedly fall in 2020, perhaps by between 5% and 10%, but the stabilisation of asset markets argues that in due course a good recovery should emerge. The worry then may be not the need to help laid-off workers and cash-strained businesses, but to address the inflation arising from the surges in money growth now being recorded in the main countries.

The table below shows the latest money growth numbers in the main jurisdictions. A fair comment is that the policy reaction has been most stimulatory (and probably most inflationary) in the USA, less so in the Eurozone, Japan and the UK, and stimulatory only to a small extent in China and India.

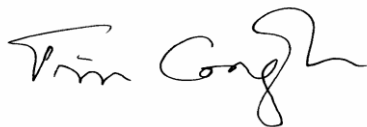
Name of country/ jurisdiction	Share of world output		Growth rate of broad money		Comment
	In purchasing- power parity terms, %	In current prices and exchange rates, %	In last three months at annualised rate, %	In last twelve months, %	
USA	15.1	23.3	22.4	12.1	Very strong money growth, partly due to monetary financing of huge budget deficit.
China	18.7	16.1	12.3	9.9	Money growth may be rising, as government favours stronger post-epidemic recovery.
Eurozone	10.6	16.4	5.5	4.5	Money growth moderate, but soon to accelerate sharply with radical ECB easing.
Japan	4.2	5.9	3.8	2.7	Doubling of BOJ asset purchases may led to much faster money growth.
India	7.7	3.3	9.7	10.0	Credit and money growth steady at high rates, amid social tension
UK	2.2	3.4	4.1	4.4	Money growth rising, before lockdown-related measures, now sharp acceleration ahead.

My verdict on prospective money growth trends has changed considerably compared with a month ago. I would now expect that by late 2020/early 2021 the annual rates of money growth in the four advanced jurisdictions will be as follows,

- The USA 15% - 20%
- Eurozone 7½% - 12½%
- Japan 4½% - 6%
- The UK 7½% - 15%

Plainly, a major acceleration of money growth lies ahead, and some quarters in 2021 and 2022 will enjoy – if “enjoy” is the right word – an inflationary boom. The monetary interpretation of inflation is everywhere neglected in central banks today, even though the evidence for its validity and effectiveness is as robust as ever. Central bankers are at present doing their damndest to indicate support for government measures to ease the massive economic pain being caused by many countries’ coronavirus lockdowns; they seem to be casual about the money creation that is implied by the generosity of these measures. (In the UK there is even an attempt by the Bank of England to refute the notion that, when it acquires more claims on the government, it is involved in “monetary financing of the budget deficit”! The Bank of England has also indicated that – when that it extends finance to the government by so-called “Ways and Means advances” [i.e., on overdraft], no inflation can result, because that type of finance is temporary, and policy-makers’ intentions are noble and benign. That raises the obvious questions, “why do policy-makers need to borrow on an overdraft basis at all?” and “if no inflation harm can result, why is there so much emphasis and fuss in officialdom’s insistence that such finance will be short-lived?”. After all, if no inflation harm can result, why not make that kind of finance permanent, as Modern Monetary Theory advocates?)

Two specific medium-term worries should be mentioned in the present context. The first is that the current oil price fall will lull policy-makers into believing that the more serious risk from the pandemic recession is deflation, not inflation. The second is that – even as inflation does become evident, perhaps more in 2021 than in 2020 – central bankers will rely on their non-monetary theories of inflation to dispute, or even to deny altogether, that the cause of inflation is unduly rapid growth of the quantity of money.



24th April, 2020



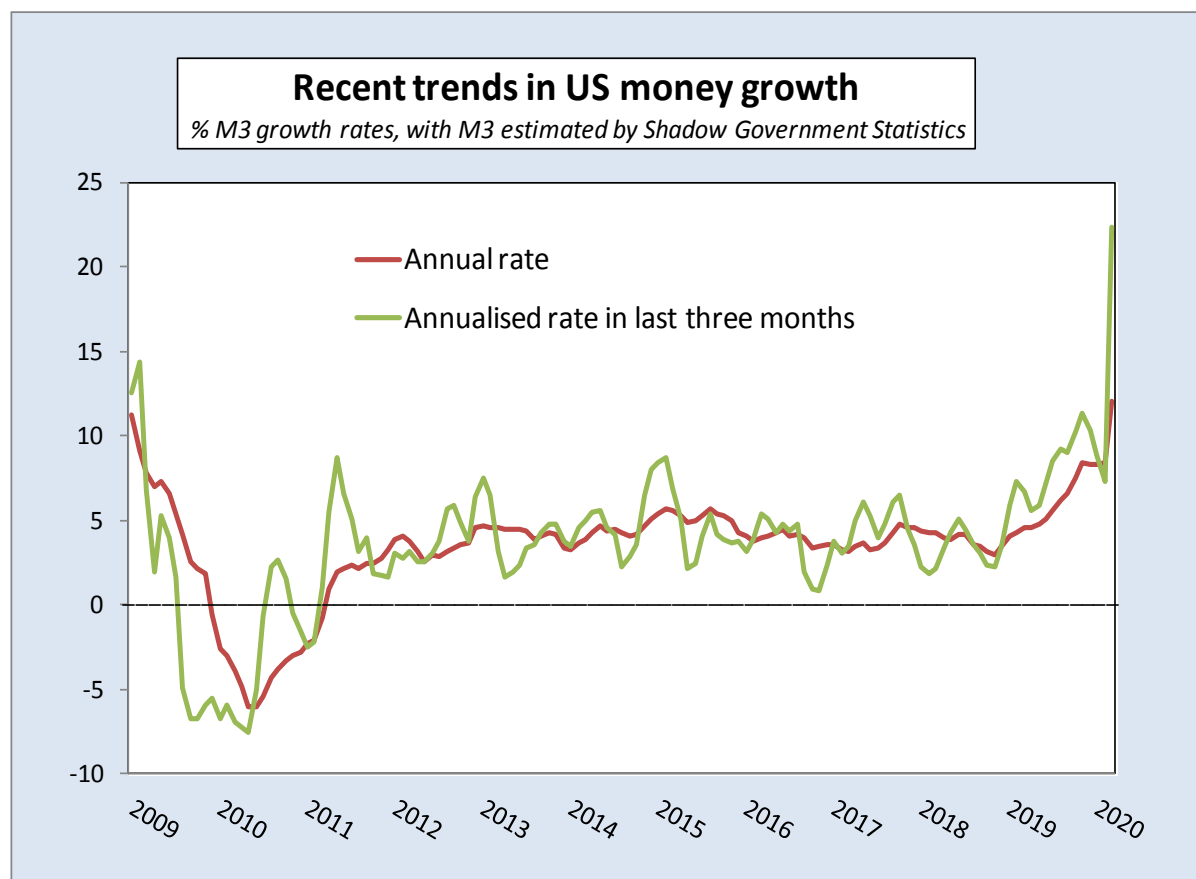
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USA

	% annual/annualised growth rate:	
	M3	Nominal GDP
1960 – 2018	7.4	6.5
Eight years to 2018	4.0	4.0
Year to March 2020	12.1	n.a
Three months to March 2020 at annualised rate	22.4	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 very sharply, to record levels

Summary: In the three months to March US M3 broad money grew at an annualised rate of 22.4%, the highest reading since October 2007. In March itself the quantity of money rose by \$814b. or 3.9%. The average increase in broad money between May 2019 and February 2020 was \$150b., high by the standards of the last decade. But March's reading was more than *five times* this amount. The annual growth rate also rose sharply from 8.4% to 12.1%, again a figure unsurpassed since before the Great Recession. (Note that our M3 data come from Shadow Government Statistics.)

The Federal Reserve's response to the coronavirus pandemic stands in sharp contrast to its behaviour during the Great Recession of 2008-10. Then, the US authorities insisted that banks must operate with higher capital/asset ratios. Banks responded by reducing the size of their risk asset portfolios, lending less or even calling in loans. A contraction of loan assets meant the destruction of bank deposits and money balances. Eventually, thanks to three rounds of "quantitative easing" (i.e., Fed asset purchases) money growth picked up. The coronavirus pandemic is different, as it is primarily a supply-side disruption rather than a collapse of demand, but some of the policy response has been similar.

The asset purchase programme, which had already been restarted in late 2019, has been scaled up dramatically. The Trump administration, like Obama's before it in 2009, has embarked on huge increases in Federal expenditure and opened up a vast budget deficit. But, in contrast to 2009, the capital ratio requirements for US banks have been loosened. This will tend to promote bank lending to the private sector and hence broad money growth. Further, ample liquidity is being provided to commercial banks by the Fed and the administration to enable them to provide loans for struggling businesses. Meanwhile the Fed, along with commercial banks, has shown itself prepared directly to finance much of the huge US budget deficit. The net result has already been a surge in the quantity of money, which – even in late 2019, before the pandemic emergency began – was growing at the highest rate in a decade. Although the surge of deposits in the final three weeks of March slowed in the first week of April, this month sees payment of the vast majority of "stimulus checks" (i.e., the \$1,200 per person payment) and an associated enormous issuance of Treasury bills, which will mainly be bought by the banks. Bank deposits will jump again, so that the M3 quantity of money could rise by 4% - 5% in the one month of April. The annual rate of M3 increase may exceed 15%. The USA has suffered from Covid-19, with more infections and deaths than any other country in the world. Macro data for the next two months will be even worse than those for March, but it is the long- term consequences of the enormous recent increase in broad money which need to be kept in mind.

John Petley
16th April, 2020

	% annual growth rate:	
	M3	Nominal GDP
1960 – 2018	7.4	6.5
1960 – 1970	7.7	6.8
1971 – 1980	11.4	10.3
1981 – 1990	7.7	7.7
1991 - 2000	5.6	5.6
2001 - 2010	7.1	3.9
Eight years to 2018	4.0	4.0



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China

	% annual/annualised growth rate:	
	M2	Nominal GDP
1991- 2018	19.2	15.1
2010 - 2018	13.6	11.2
Year to March 2020	9.9	n/a
Three months to March 2020 annualised rate	12.3	n/a

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



Broad money growth edges higher

Summary: In the three months to March 2020 China's seasonally adjusted M2 grew by 3.1% or at an annualised rate of 12.3%. This is the highest reading since August 2016, apparently a reflection of officially-supported monetary loosening which has followed the coronavirus outbreak. The annual growth rate rose from 9.0% to 9.9%, a value unsurpassed since April 2017. March's data may signal a change from a long period of stable broad money growth in China. The annual growth rate had remained within the 8% - 9% band for 18 consecutive months.

On 4th April a state ceremony was held to mourn the Chinese victims of the Covid-19 virus. Very few cases have been reported since then and even fewer deaths. Restrictions on large gatherings remain in place, but – according to government statements (which may be “false news”) – the country is well down the road to normality and a new wave of infections has not been triggered thus far. After cutting base rates by 0.2% to a record low of 3.85% on 20th April, market sources say it is unlikely that the central bank, the People's Bank of China, will announce further interest rate moves. (Among other recent moves, the PBOC has made a substantial reduction to the interest rate on its medium-term lending facility while reducing banks' cash reserves ratios by 0.5% on 15th April and indicating a further 0.5% reduction for 15th May. The PBOC has also cut the interest rate on financial institutions' excess reserves, the first such reduction in 12 years. These moves have been made to encourage China's banks to lend more.)

But more important than interest rate changes are the official guidelines on the quantity of new credit banks can extend. The increase in money growth in March may hint at a policy shift, with the state authorities concerned to maintain demand and output after the calamitous fall in gross domestic product in the first quarter. Growth in the stock of lending by Chinese banks picked up from an annual rate of 12.1% in January and February to 12.7% in March. But a big spike in money growth – of the kind seen in the early months of 2009 – seems unlikely. .

The rise in food inflation caused by an outbreak of African swine fever appears to have peaked, with overall annual consumer price inflation falling back from 5.2% in February to 4.3% in March. Food inflation is slowing, although pork prices continue to rise by over 100% year on year. Over four times as many new cars were registered in March as in February, which saw a decline of roughly 85% on January's figure. With China's main export markets hit hard by the Covid-19 outbreak, exports are down, but a 6.6% annual decline in March is an improvement on the 17.2% fall registered in the first two months of 2020. Domestic demand also fell sharply, with retail sales falling by 15.8% in the year to March. These figures should improve shortly, but demand for Chinese goods abroad is likely to remain subdued for some months due to ongoing factory and shop closures in many countries.

John Petley
18th April, 2020

	% 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



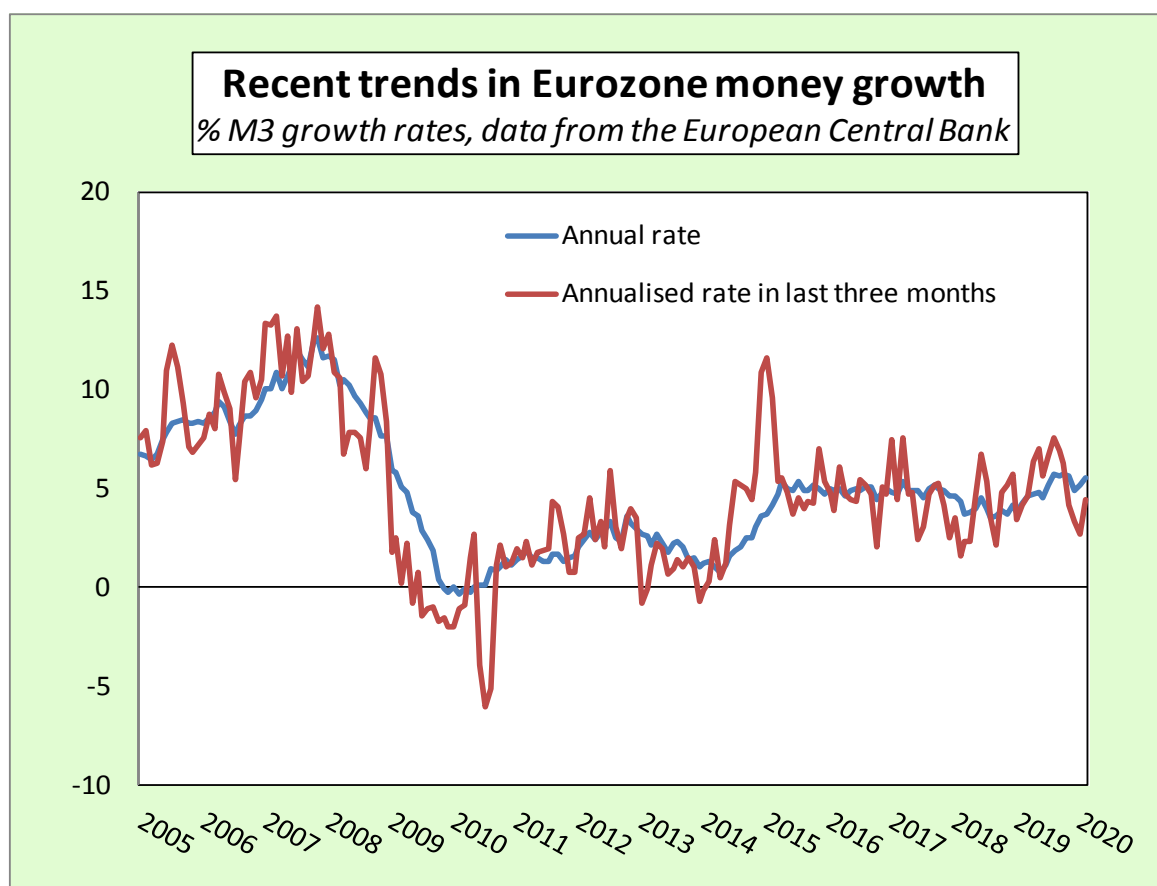
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Eurozone/Euroland

	% annual/annualised growth rate:	
	M3	Nominal GDP
1996 – 2018	5.2	3.1
Eight years to 2018	3.7	2.5
Year to February 2020	5.5	n/a
Three months to February 2020 at annualised rate	4.5	n/a

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



Money growth was picking up ahead of stimulus

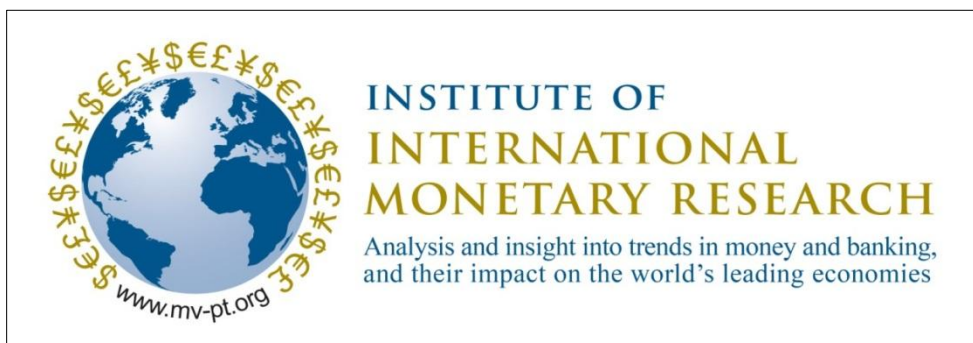
Summary: In the three months to February 2020 annualised broad money (M3) growth in the Eurozone rose to 4.5%, a gain on January's reading of 2.7%. In February the quantity of money grew by €98b. or more than 0.7% (i.e., at an annualised rate of more than 8%), the highest number since August. The coronavirus outbreak has ushered in a radical shift in policy, with March seeing the European Central Bank announcing a huge expansion of its asset purchase programme, along with other easing measures. The effects of these moves may start to become evident in March's money figures.

In the week ending 27th March the ECB bought €20b. of sovereign debt, the largest asset purchase in a single week in the last two years. €11.8b of Italian sovereign debt was purchased in March as a whole. These moves should boost broad money across the Eurozone, but especially in countries where M3 growth has been weak. Italian annualised quarterly M3 growth, for example, had turned negative in February. The ECB has had less scope for monetary easing than other central banks. As its deposit rate is already negative and its refinancing rate at zero, the ECB has less scope to cut interest rates than other central banks, but it remains true that asset purchases can be on a larger scale than so far announced. Further, Eurozone banks have been offered huge bank loan guarantees and loans at favourable rates from the ECB and state agencies, in the hope that small businesses in particular will take advantage of low-cost credit facilities. Any upturn in bank lending to the private sector is likely to be modest in scope, at least initially. The ECB seems to be focussed on the survival of banks, with the postponement of stress tests planned for later this year. Following on from the sluggish broad money growth in late 2019, the rate of money growth will increase – perhaps substantially – following the ECB's actions, but probably not to the very high levels currently seen in the USA. A rise in asset prices (and inflation) is nonetheless likely in 2021-22.

Christine Lagarde, the ECB president, stated in an article in the *Financial Times* (of 20th March) that “economic activity across the euro area will decline considerably.” In the first half of this year cash flow strains in some sectors (hotels, travel, restaurants) are likely to be followed by bankruptcies, loan provisions and some loan write-offs. Still, unlike the Great Recession of 2008, the ECB has responded quickly with a substantial loosening of monetary policy. The Covid-19 crisis has, however, exacerbated existing political tensions within the 19-nation bloc. Resistance to “Eurobonds” in some north European countries remains as strong as ever. The Dutch government, supported by Germany, Finland and Austria, refused to support plans for an emergency “coronabond”, which would have driven down borrowing costs for the nations of the south. In their view community debt issuance would be unfair on countries that had saved money for such an emergency. Nevertheless, the Dutch government's line provoked criticism not only from Italy and Portugal, but also from Nout Wellink, a former governor of de Nederlandse Bank, the Dutch central bank. The reaction from Italy was even stronger. Matteo Salvini, leader of the Lega Party, which currently tops the opinion polls, has said of the EU that, “A far cry from being a union, this is a den of snakes and jackals.”

John Petley
8th April, 2020

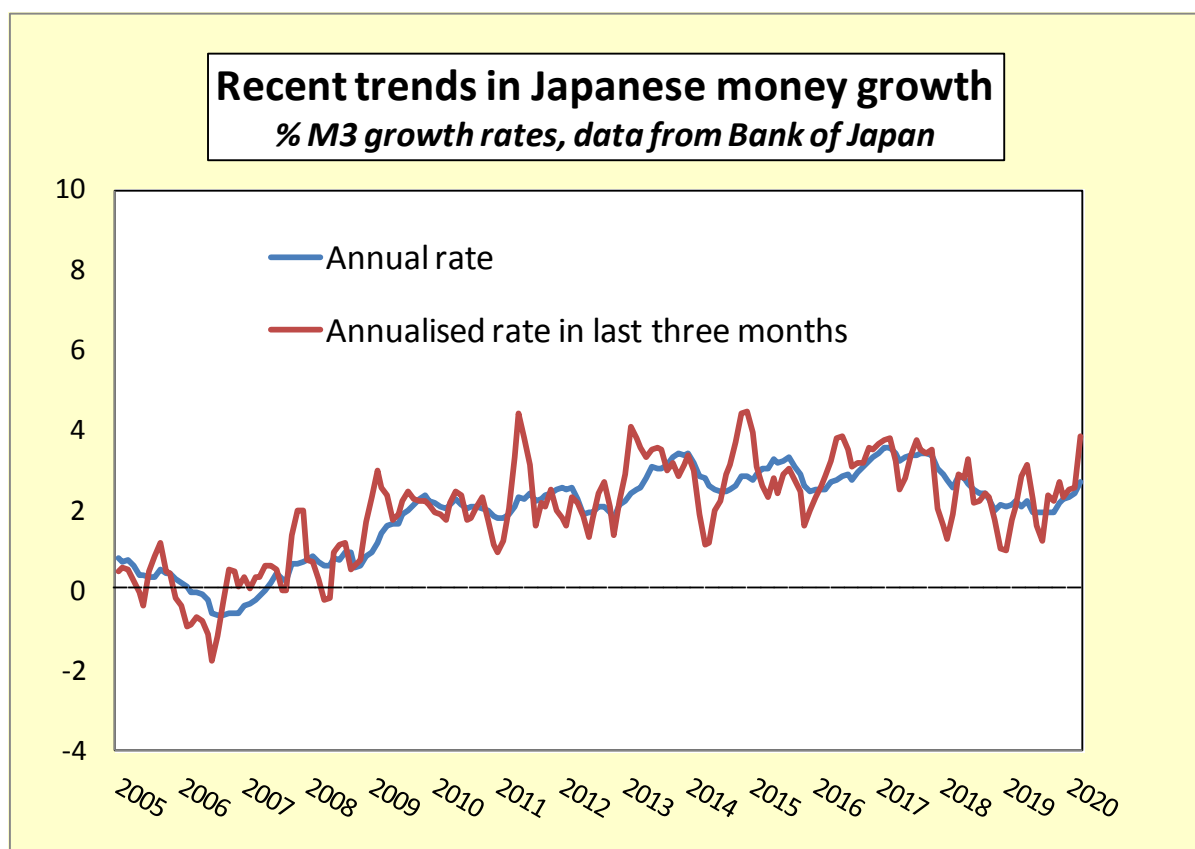
	% annual growth rate:	
	M3	Nominal GDP
1996 – 2018	5.2	3.1
1996 – 2000	4.6	4.1
2001 – 2010	6.8	3.1
Eight years to 2018	3.7	2.5



Japan

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2018	4.0	1.9
Eight years to 2018	2.8	0.6
Year to March 2020	2.7	n/a
Three months to March 2020 at annualised rate	3.8	n/a

Sources: Bank of Japan for M3 and IMF for GDP



Broad money growth picks up

Summary: In the three months to March 2020 Japanese M3 broad money rose at an annualised rate of 3.8%. This is the highest reading since January 2015, but still only moderate by international standards. The annual growth rate rose from 2.4% to 2.7%, the most elevated figure since May 2018. March saw the quantity of money, broadly defined, jump by 62 trillion yen, the largest one-month number in over 15 years.

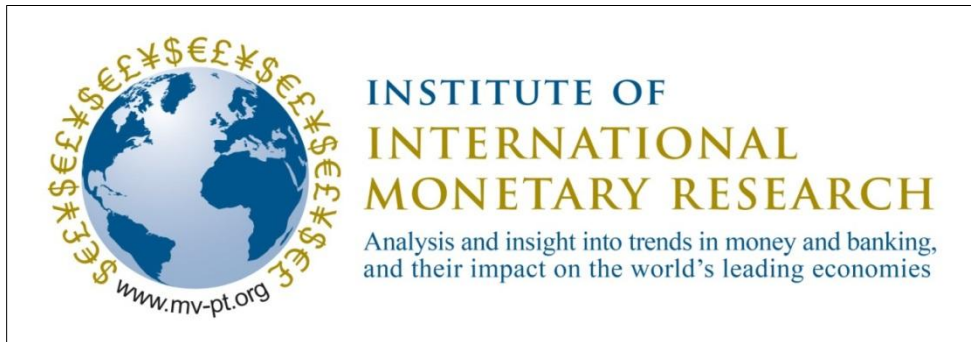
The Bank of Japan's Monetary Policy Committee responded to the coronavirus crisis at its regular meeting on 16th March by doubling its monthly purchase of Japanese government bonds (JGBs). In addition, the Bank will provide a new loan facility for companies affected by the downturn, which will be available for the next six months. The statement issued by the MPC, however, stressed that it would "not hesitate to take additional easing measures if necessary". This may be a meaningful change of course to a more expansionary monetary policy, but – given the disappointing record of the BOJ in the last 30 years – outsiders will have a wait-and-see attitude. The Japanese government has been proactive. It announced a stimulus package amounting to 108.2 trillion yen (i.e., \$1,000b., roughly), with most of this money being used to protect jobs in the SME sector. Further, on 17th April it stated that every citizen would be provided with a cash handout of 100,000 yen (about \$900). This comes on top of an earlier announcement that households experiencing a large drop in income would be eligible for a handout of 300,000 yen. The legislation for the latest move has yet to be signed off by Japan's parliament, however, which may delay the payments for one or even two months.

Few restrictions on movement have been imposed. Japanese businesses remain open, perhaps because of fears of a major recession after the Japanese economy shrank by 1.6%, equivalent to an annual rate of contraction of 6.3%, in the final quarter of 2019. Nevertheless, a month-long "state of emergency" was introduced in major cities on 7th April and extended to the whole country nine days later. Even so, this is not a full lockdown. The measures urge people to stay at home, but do not force them to do so. Thus far, Japan, with its elderly population, has escaped lightly with just over 10,000 cases and only 171 deaths reported as on 20th April.

The current money figures do not yet reflect the effect of the policy developments arising from the coronavirus outbreak. Even so March did see the largest one-month increase in broad money for many years. If April's figures see a further increase in the growth of broad money, change may be afoot, and there is at least a chance that asset prices and inflation will rise when "normality" returns. This is not to deny that the BoJ's programme of so-called "quantitative and qualitative easing", negative interest rates and "yield curve control" have been beneficial. M3 growth has probably been higher than would otherwise have been the case, although the effects have been marginal. With the postponement of the Tokyo Olympics to 2021, that potential boost to Japan's economy will not now happen this summer.

John Petley
16th April, 2020

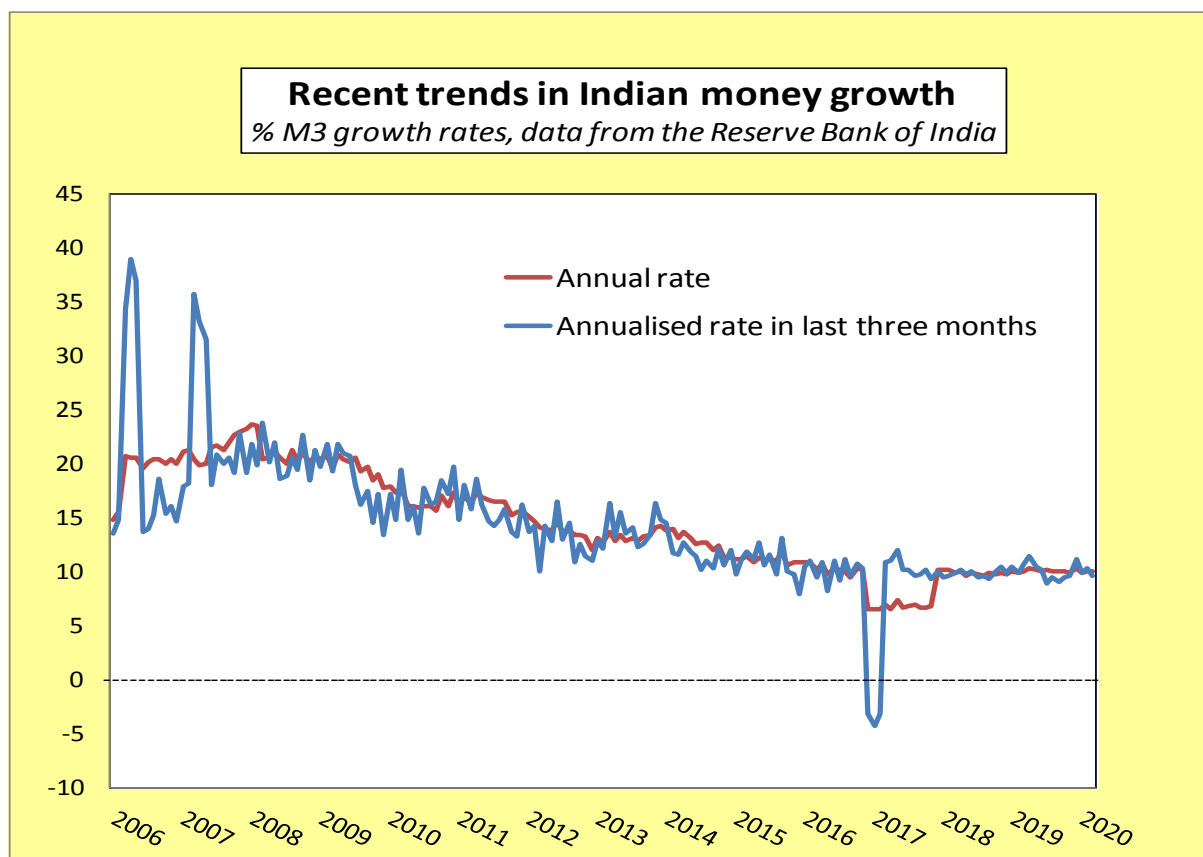
	% annual growth rate:	
	M3	Nominal GDP
1981 – 1990	9.2	4.6
1991 - 2000	2.5	1.1
2001 - 2010	1.1	0.8
Eight years to 2018	2.8	0.6



India

	% annual/annualised growth rate:	
	M3	Nominal GDP
1981- 2018	14.8	12.4
Eight years to 2018	11.2	6.9
Year to March 2020	10.0	n/a
Three months to March 2020 at annualised rate	9.7	n/a

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



Sustained double-digit annual rate of broad money growth continues

Summary: In the three months to March 2020 India's seasonally adjusted M3 grew by 2.3% or at an annualised rate of 9.7%. This is slightly down on February's reading of 10.3%, but the overall pattern of Indian money growth has been remarkably stable. The annual growth rate, unchanged at 10.0%, has been within a narrow band – from 9.6% to 10.3% - for 28 consecutive months.

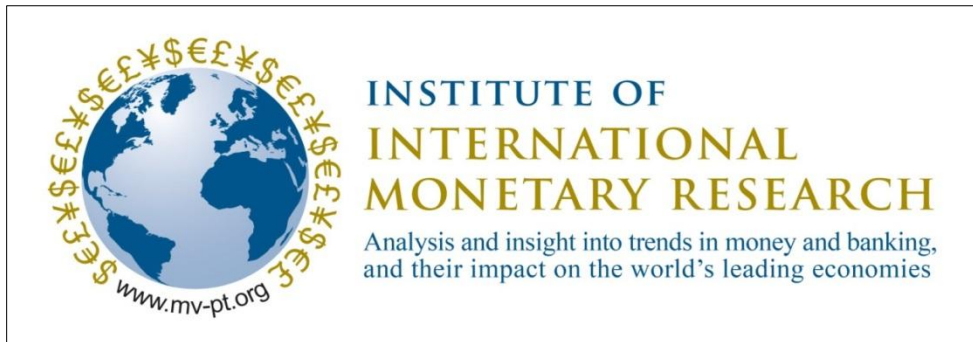
These figures do not reflect developments in the country following the leap in coronavirus cases reported from early March. The entire country was placed under lockdown from 24th March. Even grocery shops were closed in one of the tightest set of restrictions seen anywhere in the world. Currently, less than 600 deaths and 20,000 infections have been reported, but the number of infections has started to rise significantly since the middle of April. The authorities are concerned that the country's health system would be unable to cope if the number of cases increases still further.

The Indian economy had been going through a period of sluggish growth before the lockdown. The stock market fell by over 35% between a peak in late January and mid-March. The annual growth in lending by Indian banks fell to 6.1% in March, the lowest reading since the November 2016 demonetisation exercise. The Reserve Bank of India cut interest rates by 0.75% – from 5.15% to 4.4% – at the meeting of its Monetary Policy Committee on 27th March. The same day, the government announced an aid package amounting to \$22b. to help the poor. These measures may prove grossly inadequate if the lockdown has to be extended. Even the cut in base rates may do little to boost bank lending, since commercial banks have been notoriously slow to pass on previous rate reductions to borrowers. On 17th April the RBI cut its reserve repo rate by 0.25%, another move to encourage banks to lend. A week earlier the RBI provided \$6.5b. in extra funding to enable India's commercial banks to lend to the struggling shadow bank sector and small businesses. Also the strict rules on non-performing loans, introduced in the last couple of years in an attempt to address the poor loan quality of India's banks, have been relaxed.

The annual rate of consumer price inflation has now fallen for two consecutive months, although at 5.9%, it remains well above the government's 4% target. Of course, such is the severity of the shock to the economy from the lockdown that inflation is likely to be the least of the RBI's concerns.. With further measures possible if the number of cases continues to increase or the lockdown is extended, the overall impact on broad money growth is hard to estimate at the moment. The measures brought in thus far are more modest in scale than those of more developed economies. Even so, India has a large budget deficit and the next M3 figures are likely to show that broad money growth has increased. Thankfully, there have been no further reports of bank failures after the collapse of Yes Bank in early March, although there are concerns about the shadow banking sector. Meanwhile, the sectarian rioting in Delhi, which claimed more than 50 lives in February, has subsided, although tensions persist between the Hindu and Moslem communities.

John Petley
17th April, 2020

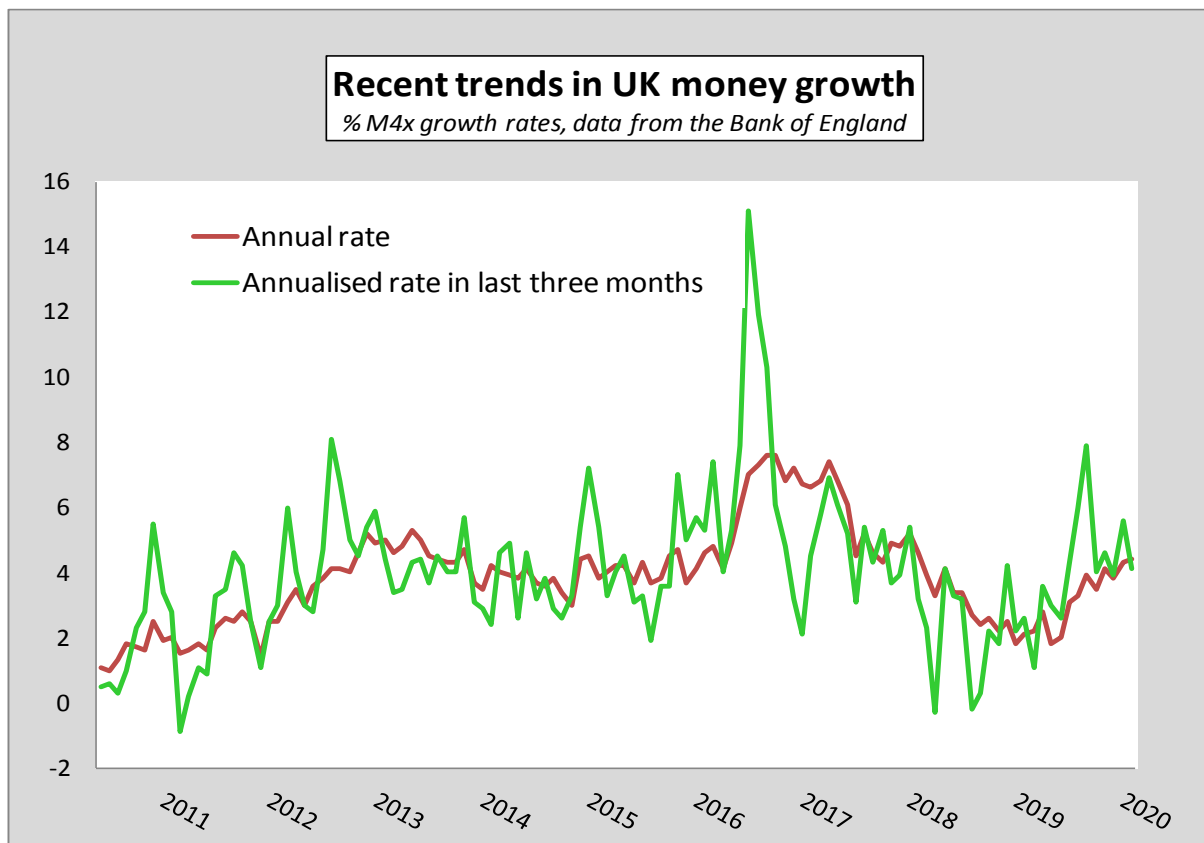
	% annual growth rate:	
	M3	Nominal GDP
1981 - 1990	17.1	15.5
1991 - 2000	17.4	14.0
2001 - 2010	17.3	14.8
Eight years to 2018	11.3	11.8



UK

	% annual/annualised growth rate:	
	M4x/M4 before 1997	Nominal GDP
1964 – 2017	9.8	8.2
Eight years to 2018	4.1	3.7
Year to February 2020	4.4	n/a
Three months to February 2020 at annualised rate	4.1	n/a

Sources: Bank of England and Office for National Statistics



Broad money growth on upward trend, with acceleration ahead

Summary: In the three months to February 2020 UK M4x grew at an annualised rate of 4.1%, down on January's reading of 5.6%, but above the average for 2019. The lower figure was caused not by particularly weak broad money growth in February itself, but rather because October's very strong growth (£14.3b.) dropped out of the calculations. (M4x money grew by £6.4b. in February.) The annual growth rate ticked up from 4.3% to 4.4%, the highest reading on this metric since February 2018.

With the commencement of a "lockdown" on 23rd March, many sectors of the economy other than the hospitality and travel industries have suffered a significant reduction in business. In the short term unemployment will rise, while inflation will fall, helped by the slump in the oil price. The housing market recorded its best month in over six years in February, with over 73,500 new mortgages approved. It will now be frozen, at least for March and perhaps for April and May. No statistics for March have yet been released, but the short-term gloom needs to be put in context. The drastic actions taken by both the Bank of England and the Chancellor will mitigate the worst effects of the crisis.

The quantity of money will have increased during March, while the annual growth rate may soon reach double digits. Excess money balances will tend to keep asset price stronger than would otherwise have been the case, with positive effects on confidence and behaviour. In the background the huge increase in the budget deficit poses new issues for policy-makers. "Net public borrowing" was originally intended (in the Budget on 12th March) to be £54.8b. in 2020/21, but in less than three weeks the lockdown and related policy measures caused the number to soar to over £200b., perhaps even to end up in the £250b. - £300b. range. In 2019/20 financing by issuance of medium- and long-dated gilts, and of index-linked gilts, was £94.0b., and surely cannot be much higher in 2020/21. It seems plausible that short-dated financing – by the issue of short-dated gilts and Treasury bills, to be taken up mostly by the banking system – will total at least £150b. in 2020/21. That will add about 7% to the quantity of money. (The new Governor of the Bank of England, Andrew Bailey, wrote an article in the *Financial Times* on 5th April acknowledging the need to maintain public confidence in UK monetary policy, but without once mentioning the quantity of money. His focus was on government borrowing from the central bank, whereas the effect of official actions on broad money matters to the economy.)

The Bank of England has also committed to a £200b. so-called "quantitative easing" programme, in which it will purchase a mixture of government and corporate bonds, and high-quality commercial paper. If all of that is implemented in the next 12 months, that is another 10% or so on broad money. It is also important that – in welcome contrast to their decisions in 2008 – regulators have loosened banks' capital and liquidity ratios. Rapid money growth will help asset prices and a recovery, but risks inflation in 2021 (and perhaps 2022) at well above the 2% target.

Tim Congdon and John Petley
21st April, 2020

	% annual growth rate:	
	M4/M4x	Nominal GDP
1964- 2017	9.8	8.2
1991 – 2000	6.4	5.0
2001 – 2010	6.5	3.9
Eight years to 2018	4.1	3.7