

WORLDWIDE TRENDS IN MONETARY AGGREGATES OVER RECENT YEARS

Over recent years, monetary trends in the major industrialised countries have exhibited many similarities. This box analyses the development of broad money in the five largest developed economic areas since the early 1980s. It also presents a global monetary aggregate (constructed as a simple sum of the monetary aggregates of the euro area, the United States, the United Kingdom, Japan and Canada converted into euro) in order to investigate the linkages between money and other macroeconomic variables at the global level.

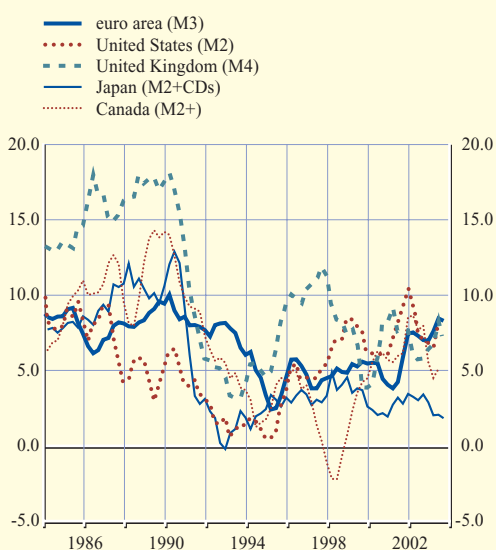
Developments in broad money in the largest developed economic areas

Chart A plots the annual growth rate of a key monetary aggregate for the euro area, the United States, the United Kingdom, Japan and Canada in domestic currency.¹ Over longer periods, some broad co-movements are apparent. The 1980s, in particular, were characterised by high monetary growth, which was followed by a significant decline in the early 1990s and some renewed increase thereafter.

Chart B illustrates in more detail recent developments in the euro area, the United States and the United Kingdom.² In all three economic areas, monetary growth has been rather high over

Chart A Broad money growth in the euro area and abroad

(annual percentage changes; quarterly data)

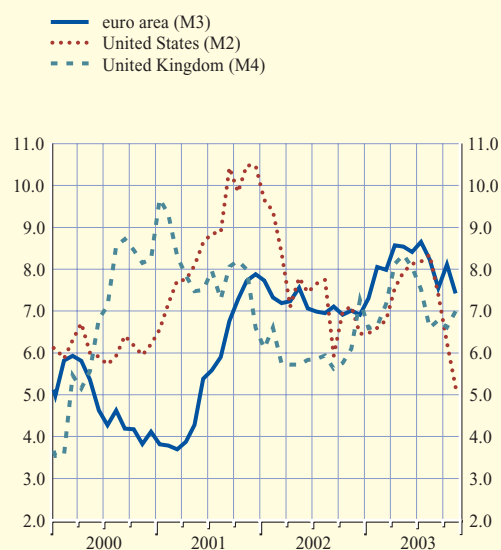


Sources: ECB and BIS.
Note: Underlying data are in domestic currency.

- 1 The monetary aggregates are M3 for the euro area, M2 for the United States, M4 for the United Kingdom, M2 plus certificates of deposit for Japan and M2+ for Canada.
- 2 In Japan and Canada developments seem to have been largely influenced by domestic factors and show less similarity with those of the euro area, the United States and the United Kingdom.

Chart B Broad money growth in the euro area, the United States and the United Kingdom

(annual percentage changes; monthly data)



Sources: ECB and BIS.
Note: Underlying data are in domestic currency.

recent years, especially considering the low level of inflation. In the United Kingdom, M4 growth started to increase in 2000. In the United States and the euro area, broad monetary aggregates increased strongly in 2001, driven in both cases by portfolio shifts away from financial markets. While country-specific factors partly account for these trends, important common factors also played a role. These included heightened stock market volatility, a protracted decline in stock prices, and rising economic uncertainty, not least that triggered by the terrorist attacks of 11 September 2001.

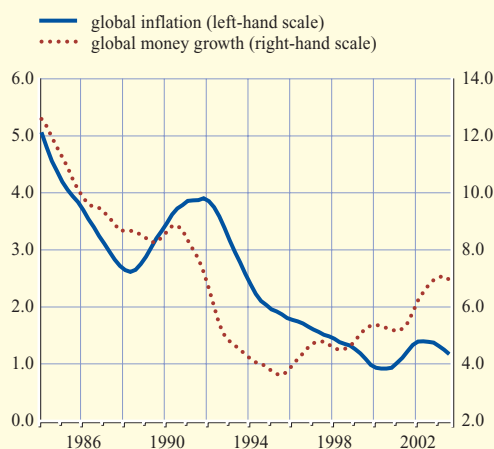
In early 2003 a similar parallel upward movement among the three monetary series can be observed, probably triggered by rising investor uncertainty related to the then prevailing geopolitical situation. The relatively low level of interest rates also contributed significantly to the increase in monetary growth. Despite this, monetary growth appears to have stabilised more recently and shows some signs of moderation, as some portfolio shifts back to the stock market took place in an environment of less volatile market conditions.

Link between global monetary growth and other global macroeconomic variables

Chart C shows developments in the annual growth rate of a global monetary aggregate (in nominal terms) and the global inflation rate (measured by the GDP deflator). Although there are several episodes where developments in the two variables appear only weakly related, overall there is a positive correlation between global inflation and global monetary growth. The chart suggests that the decline in the growth of global money preceded the disinflationary period in the first half of the 1990s. However, the relation between the two variables from mid-1995 onwards is less clear. While the growth of global money increased from the mid-1990s, global inflation continued to decline and has only started to rise since 2001.

Chart C Global money growth and global inflation

(two-year moving average of annual percentage changes; quarterly data)



Sources: ECB, Eurostat, BIS and OECD.

Note: Global money is the simple sum of broad monetary aggregates in the euro area, the United States, the United Kingdom, Japan and Canada converted into euro using purchasing power parity exchange rates; global inflation is the weighted average of the inflation rates (measured by the GDP deflator) in the euro area, the United States, the United Kingdom, Japan and Canada constructed using GDP weights.

Chart D compares developments in the global monetary aggregate in real terms with those in global real GDP. As in the case of inflation, a positive correlation emerges between the growth of real global money and the growth of global real economic activity: periods when global real GDP growth is relatively high appear to coincide with periods where the growth of real global money is also relatively high, and vice versa. The main exception is the period from mid-2001 onwards, during which the annual growth of real global money increased substantially, while global real GDP growth declined significantly. This is another indication that the strong turbulence in financial markets (related to the heightened global economic, financial and geopolitical uncertainty over recent years) has led to an

increased preference of economic agents for holding liquid and safe assets, such as those included in the broad monetary aggregates. The gap between real money growth and real GDP

Chart D Global real GDP growth and real global money growth

(two-year moving average of annual percentage changes; quarterly data)



Sources: ECB, Eurostat, BIS and OECD.

Note: Global real GDP growth is the weighted average of real GDP growth rates in the euro area, the United States, the United Kingdom, Japan and Canada constructed using GDP weights; real global money is nominal global money deflated by the euro area GDP deflator.

growth on a global scale (in terms of two-year moving averages) peaked at 3.4 percentage points in the first quarter of 2003 and diminished only slightly in the following two quarters.

Overall, the comparison shows that the recent apparent decoupling of monetary growth from nominal GDP developments was not a phenomenon restricted to the euro area. Indeed, it seems that many common factors were at work in causing similar trends in other major economies. Looking ahead, it is uncertain how the current high excess liquidity will be used. Although it is possible that a higher liquidity preference of agents in their portfolio allocation will become a structural phenomenon, there are also risks of the excess liquidity leading to higher global inflation and/or renewed global asset price bubbles in the future.³ For this reason, further developments in these monetary holdings need to be monitored carefully.

³ See also the box entitled “What could happen with the accumulated excess liquidity in the euro area?” in the October 2003 issue of the ECB’s Monthly Bulletin, pp. 8-10.