

BONNER & PARTNERS

Why QE Hasn't Led to Inflation

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Q: Why hasn't QE caused consumer price inflation?

A: Because QE “money” is just a drop in the ocean of the overall money supply.

American economist Milton Friedman famously said, “Inflation is always and everywhere a monetary phenomenon.”

He meant that the more money there was chasing goods and services, the higher the prices of those goods and services would rise.

So the logic goes that, if the Fed is “printing money,” prices should be rising...

What most folks struggle to understand is that there are two types of “money” in the system.

There's the “money” the Fed creates when it engages in QE.

This “state money” (aka the monetary base) is made up primarily of commercial banks' reserve deposits with the Fed... plus currency in circulation. It accounts for about 20% of the money in the economy, as broadly measured.

Then there is “money” private banks create when they make loans. This “private money” makes up the other roughly 80% of the money in the economy.

The Fed can boost the amount of “state money” in the system through QE. But only banks can increase – through new lending – the supply of “private money.”

And due to its relative size, it's private money that counts when it comes to consumer price inflation.

And therein lies the rub...

As Steve Hanke, a professor of applied economics at Johns Hopkins University and an expert in currencies, pointed out last year:

Since August 2008, the month before Lehman Brothers collapsed, the supply of state money has more than quadrupled, while bank money has shrunk by 12.1% – resulting in an anemic annual increase of only 4.5% in the total money supply.

That's less than half the annual increase in the total money supply reached in 2008.

Bottom line: The Fed can pump up the monetary base. And it can nail interest rates to the floor to

encourage folks to borrow. But until bank lending starts to lift the overall money supply, consumer price inflation won't respond.

P.S. Here's that link again to access Braden's report on the "Great Wave" he believes is building in US stocks. Learn how to protect yourself [here](#).