

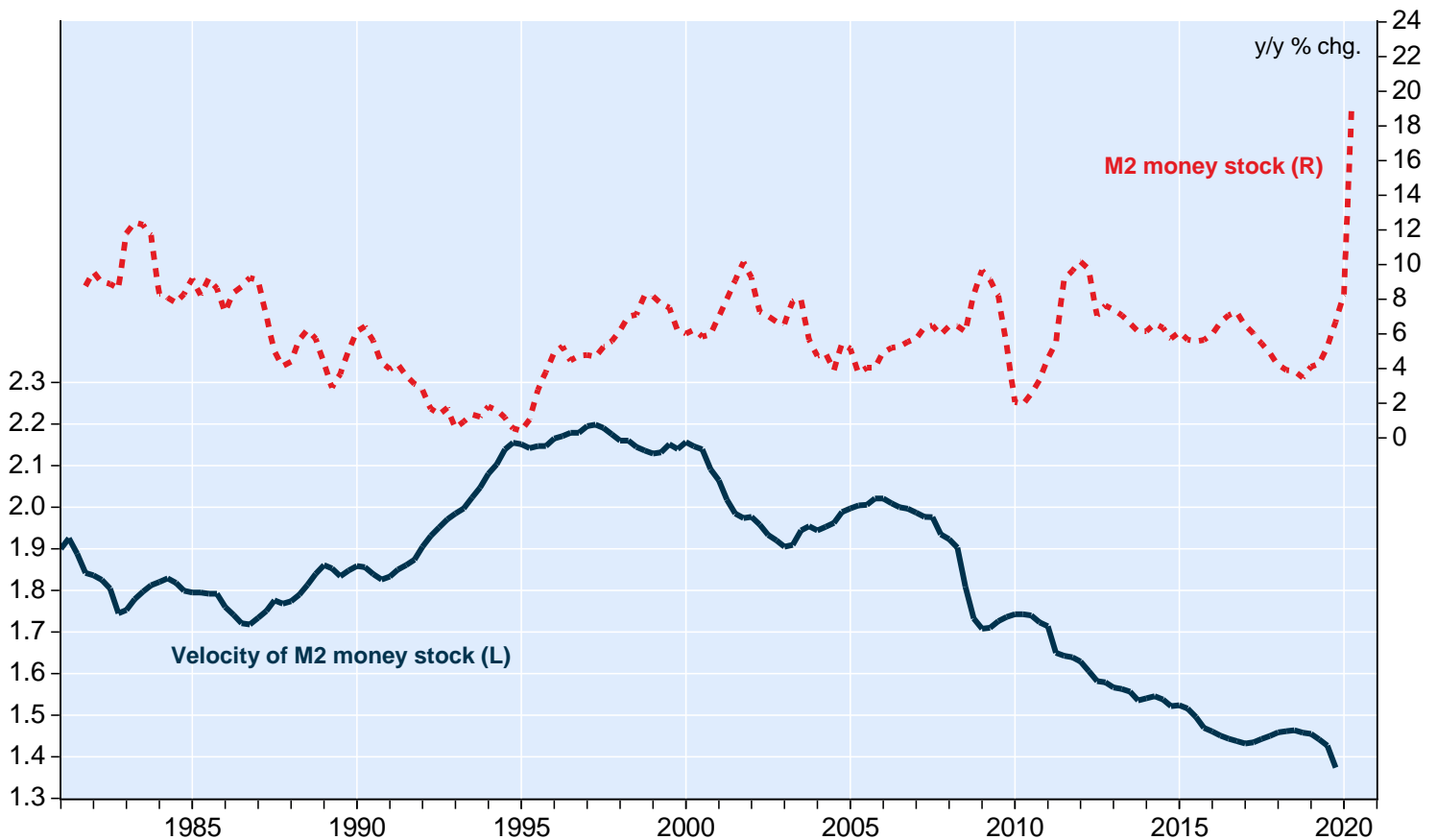
U.S. Watch

By Krishen Rangasamy

Earlier this week, the Federal Reserve reiterated its message that low interest rates are here to stay and that asset purchases would continue "at least at the current pace". As today's *Hot Chart* shows, unprecedented liquidity injections by the Fed have caused money supply to soar at a record pace, with the M2 measure on track to grow nearly 20% year-on-year in the current quarter. Which begs the question – could the Fed's ultra-loose policy stance cause the annual inflation rate to surge above its 2% target? That's unlikely in our view, at least over the near to medium term. The negative output gap stemming from the coronavirus recession is weighing on prices as evidenced by latest data showing the **largest decline ever recorded for core inflation**. Moreover, risks of an inflation surge are low as long as the velocity of circulation of money, i.e. frequency of monetary transactions in the economy, remains low. The record low velocity of money should not be surprising amid a dull economic outlook (which encourages cash hoarding by the private sector) and rock bottom interest rates (which give investors incentives to adjust their portfolios towards cash). But should that change for some reason, look for the Fed to promptly adjust its message.

U.S.: Will surge in money supply fuel inflation?

M2 money stock and Velocity of money



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