

Business Topics

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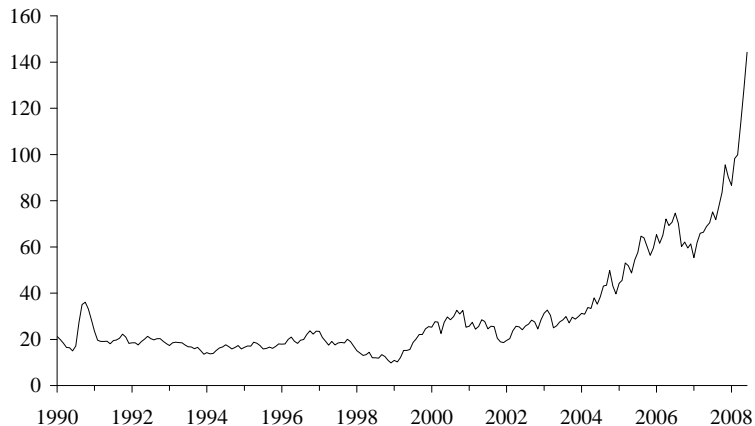
July 2008

- A Indicators and Forecasts
- B. The commodity crisis — origins and cures
- C. UK monetary muddle
- D. Europe's protectionism — latest estimates

Causes

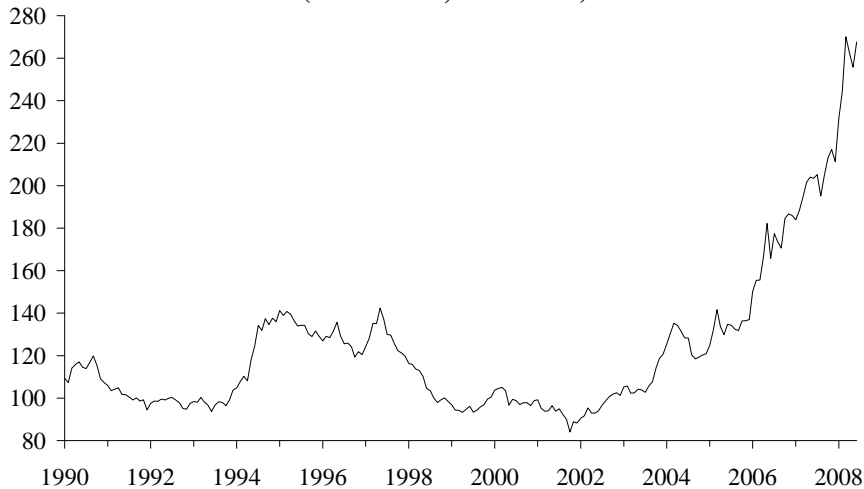
- Commodities price explosion the result of soaring demand from emerging market countries, esp China and India.
- EMC growth out of control from monetary excess; inflation now in double digits in many.
- Monetary excess comes from fixing dollar exchange rate; as dollar falls, EMCs buy dollars with own currencies, putting extra money into circulation. Attempts to offset via controls and issuing government bonds ineffective.
- So world inflation triggered by loose money linked to EMC intervention

Oil Price: North Sea Brent

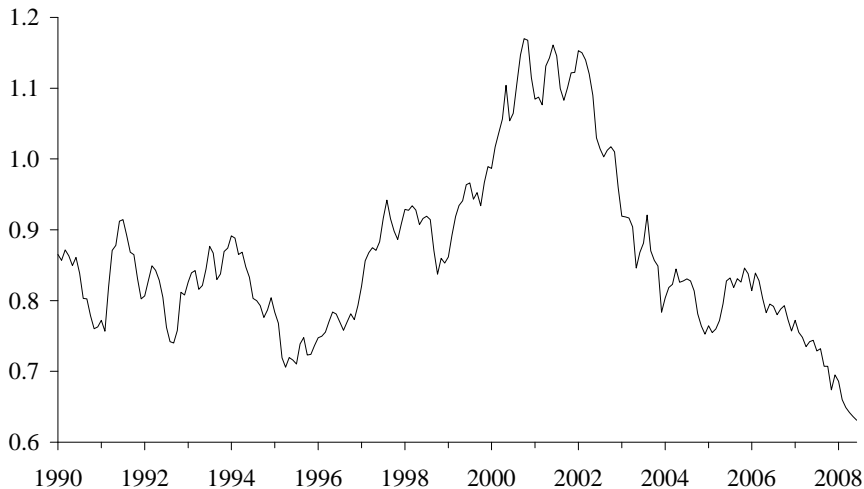


NB latest price peak is about the same in real terms as 1980 peak.

Commodity Price Index (Dollar) (Economist, 2000=100)



Euro per US dollar



Cures

- EITHER EMC can reduce money supply growth/Raise home interest rates. But this provokes inflow of money from abroad which restores monetary ease — so to avoid must let exchange rate rise. But refuse to do this because fear of job loss in exports.
- OR EMC can try controls — on bank credit and foreign inflows. But these ineffective — money 'leaks'.
- OR- US tightens money, raising dollar, tightening monetary conditions in EMC. Credit crunch has already done this but US has offset.
- OR- rest of West tightens causing world slowdown; this feeds into lower demand for EMC goods and directly into lower world demand for commodities.

Conclusions

- For world inflation to be ended, world money growth must be tightened, one way or another.
- This process is happening with credit crunch and high US inflation driving up rates in West. But not yet enough and not in US.
- Sooner or later world slowdown is coming, affecting EMCs and commodities.
- Whether soft landing depends how soon world inflation subsides — could be quite fast if commodity boom bursts but no sign yet.