

U.S. Inflation Since Early 2020: The Impact of Broad Money Growth.

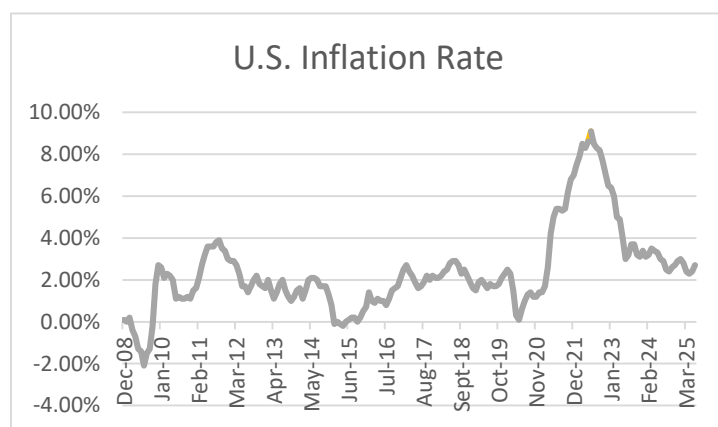
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Introduction

The U.S. Inflation Rate averaged just 1.5% from the end of 2008 to the end of 2020, rising to 7.2% at the end of 2021, and hitting a record high of 9.1% in June 2022. It has since then fallen to 3.4% in December 2023 and even further by the end of 2024 to 2.9%. The U.S inflation currently stands at 2.7% for June 2025, up from 2.3% and 2.4% in April and May, respectively. Despite the decline, the U.S. Inflation Rate remains above the appropriate 2% FED target.

Figure 1: U.S. Inflation Rate, U.S Bureau of Labor Statistics.



Economists have proposed several reasons to explain the rising average prices, including the incidence of wars, profiteering, and other special circumstances that most often will affect relative prices rather than average prices. So far, Milton Friedman's explanation, as fancied in a famous phrase, "inflation is always and everywhere a monetary

phenomenon", stands out.

The Case for Broad Money Measure

At this point, it is essential to note that while all Monetarists agree that inflation is primarily caused by monetary movements, they may differ in their definition of money, whether narrowly or broadly defined. Broad money measure provides a superior forecasting ability for inflation because it encompasses a wider range of financial assets, including savings and time deposits, which better reflect the total purchasing power in an economy. Broad money (M2 or M3) captures the liquidity of assets that can readily influence spending and price levels. Congdon argues that broad money's comprehensive scope aligns more closely with the quantity theory, providing a stronger correlation with nominal GDP and inflation over time.

Changes in Broad Money and Inflation

Since 2020, U.S. inflation has risen and fallen, largely due to fluctuations in the broad money supply (M2). The U.S. broad money supply during the period between 2020 and 2021 experienced rapid growth, increasing by about 26% due to unprecedented fiscal stimulus, CARES Act, for instance, and the Federal Reserve's monetary easing, which both injected trillions into the economy through direct payments, enhanced unemployment benefits, and quantitative easing. This money explosion, coupled with supply chain disruptions and pent-up demand after COVID-19 lockdowns, drove inflation, peaking at 9.1% in June 2022, the highest in 40 years. Reactionary as always, the FED aggressively raised interest rates and reversed quantitative easing with a quantitative tightening policy across 2022 and 2023, which saw M2 growth stall, contracting slightly by mid-2022, marking the first decline since the Great Depression. This contraction, along with supply constraints, cooled inflation to around 3% by mid-2024. However, M2 resumed in late 2023, reaching \$21.94 trillion by May 2025 with a 4.5% year-on-year growth rate, the highest since July 2022, which might cause renewed price pressure.

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