

## BOX 18.4

## UK AND EUROZONE MONETARY AGGREGATES

## CASE STUDIES AND APPLICATIONS

## How long is a piece of string?

## UK measures

There are two main measures of the money supply in the UK: cash in circulation (i.e. outside the Bank of England) and M4. Cash in circulation is referred to as the 'monetary base' or 'narrow money' and M4 is referred to as 'broad money' or simply as 'the money supply'. In addition, there is a measure called 'Retail deposits and cash in M4' (previously known as M2). This measure excludes wholesale deposits.

The definitions are as follows:

**Cash in circulation.** This is all cash held outside the Bank of England: in other words by individuals, firms, banks and the public sector.

**Retail deposits and cash in M4.** Cash in circulation with the public (but not cash in banks and building societies) + private-sector retail sterling deposits in banks and building societies.

**M4.** Retail deposits and cash in M4 + private-sector wholesale sterling deposits in banks and building societies + sterling certificates of deposit.

Table (a) gives the figures for these aggregates for the end of December 2008.

(a) UK monetary aggregates, end December 2008 (not seasonally adjusted)

	£ million
<b>Cash in circulation</b> (i.e. outside the Bank of England) <sup>a</sup>	54 399
– Cash in banks and cash held outside the country <sup>a,b</sup>	–9 531
+ Private-sector retail bank and building society deposits	1 077 872
= <b>Retail deposits and cash in M4</b>	<b>1 122 740</b>
+ Private-sector wholesale bank and building society deposits + CDs	827 097
= <b>M4</b>	<b>1 949 837</b>

<sup>a</sup> Cash in circulation is calculated mid-month and thus the figure slightly understates the end-month value.

<sup>b</sup> Row 4 minus rows 3 and 1.

Source: Based on data in Monetary and Financial Statistics, *Bankstats*, January (Bank of England 2009), Tables A1.1.1 and A2.2.1.



Why is cash in banks and building societies not included in M4?

## Eurozone measures

Although the ECB uses three measures of the money supply, they are different from those used by the Bank of England. The narrowest definition (M1) includes overnight deposits (i.e. call money) as well as cash, and is thus much broader than the UK's narrow money measure. The broadest eurozone measure (M3) is again broader than the UK's broadest measure (M4), since the eurozone measure includes various other moderately liquid assets. The definitions of the three eurozone aggregates are:

**M1.** Cash in circulation with the public + overnight deposits.

**M2.** M1 + deposits with agreed maturity up to two years + deposits redeemable up to three months' notice.

**M3.** M2 + repos + money-market funds and paper + debt securities with residual maturity up to two years.

Table (b) gives the figures for UK money supply for each of these three ECB measures – again, for the end of December 2008.

(b) UK money supply using ECB measures: end December 2008 (not seasonally adjusted)

	£ million
Currency in circulation	45 577
+ Overnight deposits	983 487
= <b>M1</b>	<b>1 029 063</b>
+ Deposits with agreed maturity up to 2 years	222 665
+ Deposits redeemable up to 3 months' notice	624 565
= <b>M2</b>	<b>1 876 293</b>
+ Repos	207 683
+ Money market funds and paper	85 262
+ <b>M3</b>	<b>2 169 238</b>

Source: Monetary and Financial Statistics, *Bankstats*, January (Bank of England 2009), Table A2.3.



What are the benefits of including these additional items in the broad measure of money supply?

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Table 18.4 The initial effect of an additional deposit of £10 billion

Liabilities	£bn	Assets	£bn
Deposits (old)	100	Balances with the central bank (old)	10
Deposits (new)	10	Balances with the central bank (new)	10
		Advances	90