

Definitions of the monetary aggregates

Last year the Bank ceased to publish certain monetary aggregates, including M3, following the conversion of the Abbey National to a bank. At that time it was recognised that the conversion, together with other developments, called for a re-examination of the definitions of the broader monetary aggregates in general.⁽¹⁾

The Bank undertook a study of the arguments in principle for making changes to the definitions of the various aggregates, which culminated in a paper in the *Discussion paper* series.⁽²⁾ This *Discussion paper* was given a wide circulation: in addition to the usual recipients, copies were sent to a number of analysts and commentators known to have a particular interest in the subject, and further copies were sent to enquirers whose interest was aroused by the reference in the 'Red Book'⁽³⁾ or by articles in newspapers and journals. In all, some 1000 copies were distributed.

The paper made a number of proposals, which are summarised below. Readers of the paper were invited to comment upon these proposals, as well as to make more general comments; they were asked to respond by the end of May.

Proposals in the Discussion paper

These can be summarised as follows:

- (a) Non-interest-bearing M1 ('nib M1') should no longer be published as an aggregate, though its components should still be published.
- (b) M2 might be redefined slightly so as to make it a subset of M4 (or, less attractively, M4 might be redefined to achieve the same effect).
- (c) The current definition of M2 is hard for banks and building societies to apply; the Bank would explore alternative definitions with reporting institutions.
- (d) Neither personal sector M4, nor M4 held by individuals, seemed an adequate replacement for M2; they should continue to be published, but not as a substitute for M2.
- (e) If a robust redefinition of M2 (as in (c)) proved impossible to find, a 'hybrid' (ie one that is not consistent between banks and building societies) might be published alongside M2.

- (f) Despite their theoretical interest, there seemed to be significant problems with the construction and interpretation of 'Divisia' money indices. But the Bank was open to representations, if there were good solutions to the problems.
- (g) The definition of M4 should remain unchanged.
- (h) Except for part of the period when the 'Corset' was in operation, M5 has not conveyed a message significantly different from that of M4. Many liquid assets are now excluded from M5, but data for these assets are not all available in a frequent and timely fashion. It was proposed to cease publication of M5, and publish instead such information about individual liquid assets as is available, so that important developments in broader liquidity are not overlooked.

Response to the paper

Despite the wide circulation of the paper and the considerable interest that the definition of the monetary aggregates often arouses, the response to the paper was limited. In all 14 replies were received, although some of these represented the views of a group of individuals. The Bank is grateful to the respondents, who made a number of useful comments and suggestions.

There was no single common theme to the responses received. Although respondents were asked to offer their views on the proposals summarised above, not all of them did so. Nobody disagreed with the suggestion that nib M1 and M5 should cease to be published ((a) and (h) above). Although most respondents who considered the proposal that M2 be made a subset of M4 ((b) above) were in favour of it, there was no agreement about how this might be achieved, nor about the merits of possible substitutes for M2 ((c), (d) and (e) above). Several respondents argued strongly in favour of a 'Divisia' measure of money ((f) above); it was implicit in most of their responses that they were indifferent to the Bank's proposals for the existing monetary aggregates.

The Bank's reaction

The Bank proposes to implement the proposals made in the paper in due course. In particular, the definition of M4 will not be changed; the definition of M2 will be changed slightly so as to make M2 a subset of M4; and nib M1 will no longer be published as an aggregate. These changes are

(1) See the August 1989 *Bulletin*, pages 352-3.

(2) 'Monetary aggregates in a changing environment: a statistical discussion paper', Bank of England *Discussion paper* No 47, March 1990.

(3) *Financial Statement and Budget Report 1990-91*, HMSO, March 1990.

largely self contained and are relatively easy to implement. It is proposed to make these changes later this year, probably with the publication of the full monetary data for October or November (ie on 29 November or 7 January), and thereafter in the *Bulletin* in February 1991.

Although it is intended to cease publishing M5, it is important that information about a range of liquid assets is published as a substitute. This body of data might take a little longer to assemble. Until then, M5 will continue to be published.

Little was said about the aggregate M4c in the *Discussion paper*, but the arguments for ceasing to publish M5 apply equally well to M4c. Publication of M4c will therefore

cease at the same time as publication of M5 ceases, though the data for the liquid assets included in M4c will continue to be published thereafter.

Discussions are continuing with the banks and building societies about the definition of deposits which are included within M2. It is hoped that these discussions will be completed within the next few months, but it may take rather longer to implement any major changes that might result.

The Bank will give further thought to the points made by the proponents of 'Divisia' measures of money. A number of theoretical and practical issues remain, which call for further investigation.