# Air of crisis overhangs central bankers' meeting

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When the annual conclave of central bankers gets underway at Jackson Hole, Wyoming on Friday, the main focus of financial markets will be on the speech delivered by Federal Reserve Chairwoman Janet Yellen. They will be searching for clues as to if and when the Fed might start raising interest rates.

The Fed made the first increase in its base rate for a decade last December, lifting it by 0.25 percentage points. It indicated that a further rise would come in 2016, but has since kept it on hold. However, last week Fed Vice Chairman Stanley Fischer pointed to changes in the jobs market and inflation, saying the Fed might be getting close to its target on these two indices, remarks interpreted as favouring a rate rise.

But overshadowing the conjecture about short-term decisions on monetary policy is a growing sense in ruling circles that the quantitative easing (QE) program of pumping trillions of dollars into the financial system has completely failed. What's worse, it is creating the conditions for a new crisis.

In an article on the upcoming meeting, the right-wing British *Daily Telegraph* said there were three tough questions central bankers needed to ask themselves: is quantitative easing actually working, has the banking system been broken by the spread of negative interest rates, and is it time to update an economic model that "no longer tells us much about the real world."

The rationale for QE, which bailed out the banks and financial institutions responsible for the 2008 crisis and fostered further speculation, was that lower rates would stimulate finance capital to invest in the real economy. This has not happened.

Eight years on, investment worldwide is well below where it was before 2008 with no sign of any uplift. This has been coupled with a downturn in the rate of productivity growth because of the reduction in capital spending, as funds accumulated by major corporations are channelled into speculative activities such as share buy-backs and mergers. So sharp has been the decline that productivity in the US could well be in negative territory.

The chief effect of quantitative easing has been to increase financial asset prices. Share values in the US are at or near record highs under conditions where economic recovery is taking place at the slowest rate for any period since World War II. In major cities around the world, cheap money has fuelled a property boom.

The most significant impact of QE has been in the bond market. It has created a situation where some $13 trillion worth of government bonds are trading with negative yields, meaning the price of the bond is so high, and the yield so low (the two move in an inverse relationship to each other), that an investor purchasing a bond would receive a negative return if he held the bond to maturity. Bonds, however, continue to be purchased in the expectation that their price will rise even higher, leading to capital gains. But such has been the escalation in prices that there has been a series of warnings from hedge fund and bond traders of a massive bubble heading for collapse, sooner rather than later.

But even as these warnings are made, the financial madness continues. This week the *Wall Street Journal* reported, in an article entitled "Credit Markets: Stimulus Efforts Get Weirder," that, as part of its quantitative easing program, the European Central Bank is inducing investment banks and companies to create new forms of debt.

Having turned money lending on its head by moving to negative interest rates, the article said, central banks were now "all but inviting private actors to concoct specific things for them to buy so they can continue pumping money into the financial system.” While the ECB arrived late to QE, it had now “embraced bond-buying with fervor.”

When the US Federal Reserve began its QE program, its then-chairman, Ben Bernanke, predicted its actions would turn the situation around, lifting inflation and returning the capitalist economy to its previous growth path. “We have a technology called the printing press,” he said in a major speech on deflation in 2002.

The contradictions of the capitalist system, however, have proven to be more powerful than even the most powerful of central bankers.

Despite QE, inflation is running at below historical norms in the US and the UK and close to zero in Japan and the eurozone. Far from overcoming the crisis, QE has exacerbated it.

Ultra-low and even negative interest rates have directly impacted on one of the pillars of the global financial system. Pension funds and insurance companies are now facing a situation where their returns on secure assets, principally government bonds, are so low that their entire funding model is under threat.

Former UK pensions minister Baroness Altmann has said the entire system is at a “crisis point,” blaming the policies of the Bank of England for driving down yields, while the *Financial Times* this week reported on the growing crisis facing pension funds that rely on steady returns from secure investments in government debt. It noted that pension funds run by companies in the S&P 500 index were underfunded by $562 billion at the end of last month, an increase of $160 billion over the past seven months because of low bond yields.

Apart from indications about future interest rate movements, one of the issues that will be most closely studied in Yellen’s remarks will be what she has to say about the so-called neutral rate of interest. This is the rate at which it is judged that the economy is in equilibrium—with interest rates neither too low to lead to high levels of inflation nor too high, resulting in recession and unemployment.

There is a growing fear this rate has fallen so low, largely because of a slowdown in US economic growth, that interest rates cannot be raised much further. This is of concern because without an increase in rates, the Fed has no room to manoeuvre downwards in the event of another recession.

On top of this there are concerns that the bond markets have been inflated to such a degree that any increase in real growth rates will put upward pressure on interest rates, bringing a fall in inflated bond prices. This will result in significant losses for investors and speculators who have bought into the market at already high levels, expecting that prices will rise even further. The Fitch ratings agency has calculated that even a return to the market conditions of 2011, when interest rates were already at very low levels, would bring losses totalling some $3.8 trillion. In other words, even a small “success” in moving back to more “normal” conditions could have the effect of triggering a financial crisis.

The central bankers and financial authorities gathered at Jackson Hole have no economic answer to the crisis of the profit system over which they preside. Their only “solution” is ever deeper attacks on the working class coupled with the development of more authoritarian forms of rule aimed at suppressing the social struggles this will produce.