A significant tremor in the bond markets

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Stock markets continue to surge, reaching new record highs in the US on a regular basis. Nevertheless, the fragility of the global financial system, built on a mountain of debt, was illustrated this week by tremors that went through the bond markets.

The yield on the benchmark 10-year US Treasury surged to just below 2.6 percent on Wednesday following a report by Bloomberg that China, the second largest holder of US debt after the US Federal Reserve, was planning to cut back its purchases.

This was the highest level since last March and some 50 basis points above the level reached at the end of the year. The 2.6 percent figure represented a full 1 percent increase over the yield in mid-2016.

The Bloomberg report cited anonymous high-placed Chinese sources. They said US bonds had become less attractive compared to other financial assets and pointed to growing trade tensions with the US as a reason to cut back purchases.

The report was quickly denied by Chinese financial authorities. But it set off a round of selling, sending the price of bonds down and yields up (the two move in inverse relationship to one another), because it fed into other concerns about how long the bull run in bonds, which has kept global interest rates at historic lows, could continue.

The sell-off was also fuelled by reports that the Bank of Japan (BoJ) is reducing its purchases of bonds in the Japanese market and the European Central Bank (ECB) may be moving to cut its purchases of financial assets in the wake of a strengthening European economy.

The wider concerns centre on the impact of moves by the world's major central banks to back off from the historically unprecedented monetary policies initiated in the wake of the global financial crisis of 2008 and the ongoing stagnation in the world economy.

Massive purchases of bonds by the Fed, the ECB and the BoJ have kept interest rates at or near zero, and have been the central factor in the rise of equities and other financial assets to the benefit of the global financial oligarchy.

One measure of the extent of their intervention can be seen in the fact that in the past few years virtually all the new debt issued by governments in the major advanced economies has been purchased by central banks. Three key central banks hold a combined total of some $14 trillion in financial assets they have bought since 2009.

While the bond market has calmed since Wednesday's sell-off, reports in the financial press indicate nervousness about what it could signify. One immediate concern is the impact of the tax cuts of the Trump administration, which will have to be financed by the issuing of more government debt under conditions where investors appear to be making something of a retreat.

The *Wall Street Journal* said the bond market has received an "early alarm call" for 2018. It said the big threat lies in the resurgence of inflation, which would send bond prices lower and interest rates (yields) higher.

The *Financial Times* described the sell-off as "fierce," while the *New York Times* said investors had been "spooked" at the spectre of central banks halting their bond-buying spree.

The *Times* also pointed to another concern in the financial markets--the resurgence of the class struggle, as workers, battered by years of falling living standards, start to push for higher wages.

The most immediate fear, it said, was that a sharp fall in bond prices would "rattle" equity markets that have been trading at record highs. "Beyond that, there is a looming concern that as the global economy heats up, inflation, a bond investor's main worry, will start to inch up, fed by higher wage demands on the part of workers everywhere."

The focus on the revival of class struggle is not misplaced. Its suppression over the past three decades and more has been central to the prolonged bull run in bond markets that started in the mid-1980s.

The defeats inflicted on the working class in the 1980s by the Reagan and Thatcher governments, aided and abetted at every turn by the trade union bureaucracies, and the "restructuring" of labour relations and working conditions around the world since then have been a key factor facilitating the orgy of financial speculation—a process that was intensified even further in the wake of the financial crisis of 2008.

Underscoring the significance of the bond market bull run, the economics correspondent for the British *Telegraph*, Ambrose Evans-Pritchard, wrote that when the tide turned, it would be "immensely powerful" and the world economic system would face "nothing less than a regime change."

Apart from their impact on equity markets, rising interest rates will have major ramifications for the economy as a whole.

In its *Global Financial Stability Report* of last April, the International Monetary Fund drew attention to the fact that, according to at least one measure, the ability of US companies to cover interest payments is at its weakest since the 2008 financial crisis. US corporations have taken on an additional $7.8 trillion in debt and other liabilities since 2010, with smaller firms, holding 22 percent of total assets, facing possible bankruptcy as a result of a sharp rise in interest rates.

The growth of debt, facilitated by ultra-low interest rates, is a global phenomenon. The ratio of global debt to GDP (gross domestic product) now stands at more than 330 percent, an increase of 56 percentage points since the financial crisis of 2008. Governments and corporations in less advanced countries that have taken out dollar-denominated loans are extremely vulnerable to even a small rise in global rates.

This economic situation has decisive political implications. It signifies that as workers begin to move into struggle against decades of social and economic devastation, they are going to be directly confronted with a crisis of the entire capitalist system.