Bank of England launches emergency operation to stave off financial collapse

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The Bank of England (BoE) has launched an emergency operation to prevent a collapse of the UK bond market. This threatened to make pension funds insolvent and spark a meltdown of the financial system akin to the "Lehman moment" that set off the global financial crisis of 2008.

The BoE intervention came on Wednesday morning when its Monetary Policy Committee (MPC) said it was reversing its previously announced policy of selling off long-term bonds, or gilts, scheduled to begin next month, and would resume purchases.

The bond market selloff started following the Tory government's smash and grab mini-budget last Friday which handed out £45 billion worth of tax cuts to the corporations and super-rich to be financed by an increase of £72 billion in government debt.

It said the central bank would carry out "temporary purchases" of long-dated government bonds to "restore orderly market conditions," on "whatever scale is necessary to effect this outcome" and the operation would be "fully indemnified" by the Treasury.

The BoE later confirmed it expected the bond-buying program would total £65 billion at the rate of £5 billion a day for the next 13 days.

The move came after it became clear pension funds, which form a base of the long-term bond market, were faced with insolvency. As part of their operations, these funds use derivatives to hedge their financial positions.

With the fall in the price of bonds they were facing increased margin calls from investment funds that finance their operations for which they did not have the cash on hand. They started to sell off some of their holdings to meet these demands, threatening to set off a vicious circle in which these sales drove bond prices even lower and yields higher.

Comments from senior figures in the banking and financial system indicate the extent of the crisis. An unnamed senior London-based banker told the *Financial Times* (FT) that at one stage on Wednesday morning there were no buyers for long-dated UK government bonds.

"At some point this morning I was worried this was the beginning of the end. It was not quite a Lehman moment. But it got close," the banker said.

Kevin Rosenberg, the chief executive for Cardano Investment, which manages strategies for about 30 UK pension schemes, with a total of around £50 billion, told the FT the organisation had written to the BoE warning of the developing crisis.

"If there was no intervention today, gilt yields could have gone up to 7-8 percent from 4.5 percent this morning and in that situation around 90 percent of UK pension funds would have run out of collateral. They would have been wiped out," he said.

The BoE seems to believe that the immediate crisis can be resolved through its bond market intervention over the next two weeks.

But there is no guarantee of that. Its policy is shot through with contradictions and is being made up on the run. As recently as last Thursday it confirmed that sales of gilts would start on October 3.

The selloff of long-dated government bonds, now flipped, was part of the BoE's monetary policy tightening program which has seen hikes in interest rates.

It says this part of its agenda will remain. The bank stated in yesterday's announcement that the "MPC will not hesitate to change interest rates by as much as needed to return inflation to the 2 percent target sustainably in the medium term."

But its intervention in the bond market, through which it is effectively financing the Tory government's handout to the wealthy and the corporations, is inherently inflationary.

The BoE and the government have said they will co-ordinate their policies. But as PNB economist Paul

Hollingsworth remarked: "It is hard to appear co-ordinated when fiscal policy has its foot on the accelerator and monetary policy on the brake."

Even before the crisis engulfed pension funds, there was evidence of mounting problems in the financial system. A significant number of banks, including HSBC and Santander, suspended the issuing of new mortgages, along with a series of other lenders, including Virgin Money and Halifax, because they did not know what the cost of funding would be.

Whatever the immediate outcome of the present crisis, the cost of mortgages will rise significantly with warnings that the worst-case scenario of a housing market crash is now becoming the "main assumption," according to one industry analyst cited in the FT.

Following the BoE intervention, bond prices started to rise and there was some marginal increase in the value of the pound against the US dollar.

The most significant reaction came in the US where, after an initial fall in the futures market, Wall Street surged when the market opened. The Dow finished up by 550 points for the day, 1.9 percent, the S&P 500 was up by 2 percent, with the NASDAQ rising by 2.1 percent.

The surge in the market, coming after a "near death" experience in the UK financial system, appears to have been motivated by the belief it will add pressure on the Fed to ease up on its restrictive monetary measures. But there are growing concerns about the state of the US economy as sentiment on Wall Street swings wildly between fear and greed.

"There's fear that the whole system collapses and demand is not able to withstand this amount of rate hikes," Agnes Belaisch, a strategist at Barings Investment Institute told the *Wall Street Journal*, noting that there was evidence of a recession.

The immediate origins of the UK crisis lie in the unrestrained greed of the financial elites, represented by the grotesque figure of Prime Minister Liz Truss and her Treasurer Kwasi Kwarteng. But the underlying driving forces lie in the explosion of parasitism in the global financial system over decades, accelerating after the crisis of 2008.

The guiding philosophy of Fed chief Jerome Powell and other central bankers is that inflation can be brought under control in the same way it was achieved under Fed chairman Paul Volcker in the 1980s.

They aim to drive up interest rates and induce a recession to crush the wage demands of the working class confronted with daily cuts in living standards flowing from the highest inflation rate in four decades.

But much has changed since the 1980s, above all in the level of debt and the mechanisms of the global financial system. And the central bankers confront a resurgent working class.

In 1982, at the height of Volcker's class war under the Reagan administration, gross public debt was 34.3 percent of gross domestic product. It had risen to 127 percent by 2021.

Globally, as a result of corporate bailouts during the pandemic, the total of public plus non-financial debt rose by 28 percentage points to 256 percent of global GDP in 2020, according to the International Monetary Fund.

The government debt market has undergone a vast transformation. According to the Bank for International Settlements, as much as 30-50 percent of marketable government debt is now held overnight. This means that the bond market, in which this debt is traded, is highly vulnerable to shifts in financial conditions which can precipitate a far-reaching crisis, as seen in the UK.

This situation has vast implications for the working class all over the world.

It lives under conditions where a sword of Damocles hangs over its head as the insatiable drive for enrichment by the financial elites and their political representatives threatens, virtually overnight, to bring about mass unemployment, the wiping out of pension funds and a crisis for home buyers, on top of the blows already being inflicted by rampant inflation and cuts in social services spending.

The only way to end this madness is the international struggle for socialism by the working class to take the economy and its financial system out of the hands of a rapacious ruling class and establish an economy based on human need not the dictates of private profit.