After the Bank of England intervention financial turmoil continues

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Turbulence in global financial markets is continuing in the wake of the Bank of England's intervention in the UK bond market crisis, which threatened the solvency of pension funds and a crisis in the financial system on a scale of, or possibly even greater than, the meltdown of 2008.

Bond yields in the UK market have come down somewhat as bond prices have risen (they move in opposite directions) and sterling has clawed back some of its losses against the US dollar, after it threatened to fall to parity with the US currency.

Yesterday, a leading article in the *Wall Street Journal* warned: "Mounting volatility in government bond markets is intensifying fears on Wall Street that this year's wild swings in the world's safest assets could destabilize already rocky financial markets."

It noted that before the BoE intervention, the yield on the 10-year US Treasury note, which is regarded as benchmark for the US and global financial system, had risen to above 4 percent for the first time in more than a decade.

The upward movement "marked the latest explosion in normally placid debt markets, raising investor concerns that the year-long selloff in bonds has entered a new and more dangerous phase."

The rise in bond yields is already having an impact on the economy with the report yesterday that the average interest rate on a 30-year home mortgage is now 6.7 percent, more than double the level of 3.01 percent just a year ago. One of the fears is that rising mortgage rates will precipitate a sharp fall in the housing industry.

So far this year, major bond indexes in the US have had their biggest ever losses and the stock market continues to gyrate as it moves down, with the key S&P 500 index losing 22 percent so far this year.

After a surge on Wall Street following the BoE intervention on Wednesday, there was a selloff yesterday with the S&P 500 closing at its lowest point for 2022 as the yields on Treasury bonds reached some of their highest levels for the year. As one portfolio manager commented to the WSJ: "This volatility is quite breathtaking."

Chris Turner, global head of markets at the financial giant ING, told the newspaper that central banks remained "wholly focussed" on taking rates higher "even if that means causing a recession."

He said the "massive intervention" from the BoE, in which it has committed to spend £65 billion buying up UK government debt, "stabilized things for 12 hours, but obviously they haven't addressed the fundamental challenges."

Some of those "fundamental challenges" emerge from an examination of the way the crisis erupted in response to the Tory government's "smash and grab" mini-budget last Friday, which gave a £45 billion handout to the corporations and the super-rich.

The adverse reaction of the financial markets was not to the handout, but because the additional money flow, which they always welcome, was not accompanied by further deep attacks on social spending, but was to be financed by increasing government debt to the tune of £72 billion.

The prospect of a further rise in debt, increasing the supply of bonds, produced a rapid drop in their prices, sending their yield skyrocketing. The immediate impact was on pension funds, which are among the largest purchasers of government debt.

Pension funds pursue what is known as liquidity-driven investment (LDI). That is, they generally do not engage in speculative measures aimed at securing higher returns that "beat" the market.

They seek to ensure that their income flows and the value of their assets will cover their liabilities to retirees. But to do this they need to undertake derivative trades, financed by borrowing, to hedge against market movements to ensure this is the case.

This borrowing is backed by the collateral they hold in the form of government bonds and cash. But when the price of the underlying asset, government bonds, falls precipitously, as it did at the start of the week, the lender demands more cash.

To meet these demands, the pension funds must sell bonds,

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sending their price down even further, thereby precipitating a "doom-loop." It reached a point where one analyst warned that had the BoE not intervened, 90 percent of pensions funds could have been rendered insolvent.

In a comment on the crisis, *Financial Times* columnist Robin Wigglesworth made some important observations about what had been revealed.

He noted it had hammered home a truism derived from past experiences: that "the greatest damage is often caused by supposedly stolid investments that turned out to be anything but," and "truly cataclysmic financial debacles tend to involve investment strategies [such as LDI] and financial securities that everyone thought were boring."

"What else like this may be lurking out there?" he continued. "What is the next debacle within some unlikely corner of the global financial system. We are likely going to find out soon."

Throughout the present crisis the word "confidence" has been used repeatedly. The capacity of the financial system to continue to siphon wealth to the upper echelons of society depends on confidence that its operations will not be impeded either by maladministration on the part of governments or the struggles of the working class.

Over the past decades of growing financial turbulence, going back to the stock market crash of October 1987, confidence has been restored by the intervention of the Fed and other central banks as they pumped more money into the system. But these operations—each one bigger than the last—were able to be carried out in conditions vastly different from those of today.

Inflation was at historic lows and the movement of the working class was suppressed by the trade unions—strike activity, the most basic indicator of the class struggle, was at historic lows—and real wages were on a continuous downward trajectory.

Today inflation is at a four-decade high, and the working class is striving to break out of the grip of the trade union bureaucracy, most notably in the UK and the US as other sections also start to move into action in support of wage demands and an end to increasingly intolerable conditions of exploitation.

This means the restoration of confidence cannot take place through the methods employed by central banks in the past.

It requires a massive assault on the social position of the working class, to suppress wages and drive up exploitation to new levels to increase the flow of surplus value into the financial system and sustain the mountain of debt and fictitious capital built up over decades.

The outlines of this class war are already clear. The central banks are raising interest rates, not to bring down inflation, but to induce a recession and suppress wage demands. At the same time, the knives are being sharpened for major attacks on social services, health and education spending, which represent a deduction from the pool of surplus value available for appropriation by finance capital.

The UK Tory government of Prime Minister Liz Truss, responding to the criticism of its mini-budget, has issued statements that "iron discipline" must be imposed on public spending.

The unions know very well what is ahead. A letter signed by 18 unions said austerity would be an "act of national vandalism." But at the time, while writing letters to the Tories, they are working night and day to suppress the struggle by workers to bring down the Truss government.

The same class mechanics are on display in the US where the unions are trying might and main to sell out every strike.

In financial circles, the response to the latest data on initial jobless claims, which showed they had fallen to their lowest levels since April, was that the Fed would have to be even more aggressive on rate hikes.

As one investment strategist told the WSJ; "The Fed is trying very hard to inflict pain on the jobs markets and it's not working. That maintains the narrative that the Fed is going to have to be tighter for longer."

The ruling classes in the US, the UK and around the world have a counter-revolutionary strategy which they intend to impose as the only solution to the deepening crisis of the profit system over which they preside.

The working class cannot defeat them through half measures—least of all through letter writing—but only through an opposed strategy, worked out to the end. It must assert its great social power through the development of independent rank and file committees to break the grip of the union bureaucracy, develop an independent perspective, and advance the struggle for socialism.

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