Where to now for the UK and global financial system?

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Following the Bank of England's intervention into the UK bond market to prevent a financial crash, centred on pension funds, the big question hanging over the British and global financial markets is what happens when the emergency program ends.

The BoE committed itself to spending £65 billion—£5 billion a day for 13 days until October 14—on long-dated UK government debt, that is, 10-year and particularly 30-year bonds, so-called gilts.

Over the weekend, the *Financial Times* (FT) reported that regulatory authorities responsible for the £1.5 trillion pensions sector, which came close to imploding, "have been holding daily talks with asset managers to stave off a fresh crisis" when the emergency bond-buying finishes.

The crisis erupted when pension funds, which match their income and asset holdings with their liabilities and make heavy investments in gilts to do so, were met with "margin calls"—demands for increased collateral to back the loans they had taken out to buy derivatives to balance their books as bond prices fell.

The pension funds started selling bonds, lowering their price, to raise cash to meet the margin calls. This threatened to set in motion a "doom loop," with the fall in bond prices leading to a demand for further collateral, prompting more selling, lowering prices still further, and a demand for yet more collateral.

Had the crisis continued, an estimated 90 percent of pension funds could have become insolvent.

The BoE issued a statement that the "scale and speed" of the shift "far exceeded historical moves."

Last Wednesday, the 30-year gilt yield rose at one stage by 1.27 percentage points because of the fall in bond prices (the two move in opposite directions) before coming back down after the BoE intervention. This single day movement was greater than the *annual* range in all but four of the past 27 years.

The head of UK rates strategy at the banking giant HSBC, Daniela Russell, told the FT the BoE bond purchases were a "sticking plaster" to buy time. There was a possible "cliff edge" when the intervention ended and the central bank might have to offer more support.

The newspaper reported that in the rush to raise cash, pension funds had been selling stocks and bonds, with some seeking bailouts from their corporate financial backers.

More details are thus emerging of the financial market mayhem that erupted in response to the Truss Tory government's mini-budget—which handed out £45 billion in tax cuts to the corporations and super-rich, financed by increased government debt of £72 billion. The driving forces of the crisis have come into clearer focus.

The objection of the financial elites was not that they would be showered with still more money, but that this was not accompanied by a further assault on the working class in the form of deeper cuts to health and other already eviscerated services, coupled with the suppression of the rising wages movement.

A comment by Ajay Rajadhyaksha, a leading executive at the Barclays bank, cited by Bloomberg columnist John Authers, pointed to some of the class relations motivating the adverse response of financial markets.

"Bond and currency markets have reacted so poorly since the mini-budget, at least in part due to fears that the move added new fiscal stimulus to an economy that already had 10 percent inflation and a very low jobless rate," Rajadhyaksha said.

In other words, under conditions where growing sections of the working class are demanding increased wages in the face of rampant inflation and striving to break the stranglehold of the trade union bureaucracy—the chief enforcers of the real wage cuts—the government's decision would only add fuel to the fire.

The implication of these comments, along with others that have pointed to the need to cut spending, is that the government cannot simply hand out still more money to the ultra-wealthy without suppressing the working class.

The S&P credit rating agency reinforced the demand for social spending cuts. It put the UK on a "negative outlook" on Friday, while continuing to maintain its AA rating.

S&P said that because of the package introduced by the chancellor, Kwasi Kwarteng, the UK budget deficit would increase by 2.6 percentage points of gross domestic product (GDP). This meant that "net general government debt will continue on an upward trajectory, in contrast to our previous expectation of it declining as a percentage of GDP from 2013."

Further comments have highlighted the extent of the UK crisis.

Luke Hickmore, a fixed income manager at Abrdn, a major UK-based global investment company which has been heavily involved in the British bond market for more than 20 years, told the FT there were periods on Monday and Tuesday last week when there were no buyers for long-dated gilts.

"I've never seen a move like that," he said, noting that even during the global financial crisis of 2008 there was always a market for gilts.

The present situation in the UK is only the sharpest expression of a mounting crisis in the global financial system, including the US.

Escalating rate hikes in the US, carried out in the name of fighting inflation, were implemented with the aim of inducing a recession to crush the rising movement of the working class in support of wage demands. The rate rises also boosted the value of the dollar, resulting in precipitous falls in other major currencies.

At the height of the crisis last week, the British pound traded at near parity with the US dollar and the euro went below parity. The Japanese government intervened to try to stabilise the yen for the first time in 24 years and the Chinese renminbi fell to its lowest level in more than a decade.

The US Federal Reserve hikes have led to increased tightening in the US bond market, with the rate on the 10-year bond approaching 4 percent last week. The increase in rates on government debt is making its way through the financial system. Bloomberg reported that a measure of credit stress in the US, tracked by the Bank of America, jumped to a "borderline critical zone" last week.

Last Friday, the Indian central bank raised its lending rate by half a percentage point to try to counter the fall of the rupee against the US dollar. Its governor, Shaktikanta Das, warned that after the pandemic and the war in Ukraine, the global economy was now in the midst of a third major shock, resulting from aggressive US monetary tightening.

"There is nervousness in financial markets with potential consequences for the real economy," Das said. "The global economy is indeed in the eye of a new storm."

The rise of the dollar has led to some talk in financial media circles about a possible revival of an agreement along the lines of the Plaza Accord of September 1985, in which the major economies agreed on measures to keep the dollar's value down.

There is virtually no prospect of a repeat, not least because the US does not want it. The dollar's rise, while inflationary for the rest of the world, is disinflationary for America.

Even if there were such a pact, foreign currency markets have expanded by leaps and bounds over the past 37 years. In 1985, the daily foreign exchange turnover was $200 billion. By 2019, according to the Bank for International Settlements, it had risen 40-fold to $8.3 trillion.

Such figures recall the remark by Karl Marx in the *Communist Manifesto* that bourgeois society has conjured up such gigantic means of production and exchange that it is "like the sorcerer, who is no longer able to control the powers of the nether world whom he has called up by his spells."