Bank for International Settlements report charts a financial system in crisis

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The annual report of the Bank for International Settlements (BIS), the global umbrella organisation of the world's central banks, provided details of a world financial system wracked by deepening problems any one of which could set off a crisis on the scale of the 2008 crash or even greater.

A key feature of the report is that in portraying the present situation it makes clear that measures taken by governments and central banks at one point in time, which appeared to be a rational response to overcome dangers to financial stability, only created the conditions for the eruption of even more severe turbulence.

The report, which was issued at the weekend, begins: "The global economy has reached a critical and perilous juncture. Policymakers are facing a unique constellation of challenges. Each of them, taken in isolation, is not new; but their combination on a global scale is."

These words, coming from the horse's mouth, should perhaps be emblazoned across the computer screen of every journalist, columnist and academic who has denounced the Marxist movement for its alleged "catastrophe mongering" and "exaggeration" in its exposure of the irresolvable contradictions of capitalism.

The report places at the centre of its analysis the combination of high inflation and rising financial vulnerabilities—unprecedented in the post-war period—resulting from the increase in debt, both public and private. These problems have emerged in the past but never together. In the 1970s and early 1980s high inflation was not accompanied by financial instability and when financial dangers developed, as in 2008, they occurred in a low-inflationary environment.

The report noted that the "rather unique combination of high inflation and widespread financial vulnerabilities is not simply a bolt from the blue" and not just a product of the COVID-19 pandemic and the war in Ukraine. The roots of the problems go deeper as "debt and financial fragilities do not appear overnight; they grow over time."

Pointing to these issues, it stated: "The challenges the global economy is now facing reflect in no small measures, a certain 'growth illusion,' born out of the unrealistic view of what macroeconomic stabilisation policies can achieve… The unintended result has been reliance on a de facto debt-fuelled growth model that has made the economic system more fragile and unable to generate robust and sustainable growth."

Debt creation did not begin yesterday, or even the day before, but goes back almost four decades when the US Fed made a decisive turn in response to the Wall Street crash of October 1987.

The Fed determined that henceforth its task was not to prevent the development of speculative financial bubbles, many of them financed by debt, but rather to engage in a clean-up operation when they burst by pumping more money into the financial system to enable speculation to continue.

This led to the financial crash of 2008 and then to the market meltdown of March 2020, when the pandemic struck. Governments and central banks responded with corporate bailouts and the provision of trillions of dollars of essentially free money to the financial markets, boosting the fortunes of the financial oligarchy to stratospheric heights.

Just as the financial authorities thought instability had been contained, it erupted again in March with three of the four largest banking failures in US history.

The report noted that while the global economy withstood the "strong headwinds" better than expected over the past year "signs of strain started to emerge. In particular, financial stress rattled the financial system engulfing both banks and non-bank financial institutions and prompting a forceful response to limit contagion.

"The strains share a common cause: the system is under stress following the era of low-for-long interest rates."

The stresses that have most recently manifested themselves are far from over, as the report outlined.

"There are widespread macro-financial vulnerabilities in the system. Public and private debt levels are historically high. Asset prices, notably those of real estate, have started softening on the back of rich valuations. Interest rates may need to stay higher and for longer than financial markets are

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pricing in. The strains that have emerged so far reflect interest rate risk, but credit losses are still to come. This will further test the resilience of the financial system."

This situation has arisen because the policy measures taken by governments and central banks at one point to alleviate a crisis and prevent a financial meltdown, while they have provided an immediate solution, have only created the conditions for its eruption in a higher form.

The BIS acknowledged this, to some extent, with the introduction of the concept of a "region of stability identified as the set of fiscal and monetary combinations which are consistent with macroeconomic and financial stability."

But the concept has no analytic value because the boundaries of the "region" are characterised as fuzzy and indistinct. In other words, those in charge of the regulation of the capitalist economy have no real idea of what effect their emergency measures will have over the longer term.

As the report put it: "A policy conduct that may appear stabilising in the near term can, over time, inadvertently shrink the region and take policies towards the boundary. The economic system may appear stable for a long time until, suddenly it is not."

This latter phrase is repeated several times in the report and underscores the central problem facing the would-be regulators. The problem lies not in their lack of computing power or information but is rooted in the very nature of the capitalist system itself.

The private ownership of the means of production and finance mean that economic and financial processes operate as a powerful force behind the backs of market participants, giant corporations, banks, and finance houses. Within their operations there is a degree of conscious control but outside in the broader economy and financial system anarchy reigns, which, despite all efforts to regulate it, repeatedly erupts in the form of a crisis.

While the BIS analysts are bereft of any solutions to contain the contradictions of the profit system and its inherent anarchy, they are guided by a sure class instinct and decades of experience when it comes to what must be done—the working class must be made to pay.

This is set out in the two policy prescriptions outlined in the report. First, it said: "The priority for monetary policy is to bring inflation back to target."

As has become ever clearer over the past year, the "fight against inflation" is directed to slowing economic growth, even to the extent of inducing a recession, to suppress the wage demands of the working class. This policy must be continued even when, as the report acknowledged, wage increases are well behind the level of inflation and one of the chief causes of inflation is profit gouging by corporations.

"While nominal wage growth has not been exceptionally strong so far," the report said, "this should not provide too much comfort.… Some catch-up is on the cards particularly given the strength of labour markets."

In other words, while the wages struggles of the working class have been somewhat contained by the trade union bureaucracies in every country, that situation may not endure, thus requiring the battering ram of interest rate hikes.

The second arm of policy directed against the working class is cuts in government spending. As usual with such reports this is couched in language aimed at disguising its essential class content.

"The priority for fiscal policy is to consolidate," the report said pointing to the growth of government debt to historic highs.

Under conditions where all major governments are expanding their military budgets, this means deep cuts in social spending directed against the working class. Cuts would also work to slow the economy thereby putting downward pressure on wage demands and lessen the need for steeper interest hikes which adversely impact on the financial system.

"Consolidation," the report said, "would provide critical support in the inflation fight. It would also reduce the need for monetary policy to keep interest rates higher for longer, thereby reducing the risk of financial instability."

The BIS report makes clear that for all the declarations about the "stability" and "resilience" of the financial system its underlying historic crisis is deepening. There is no prospect of some kind of restoration of "normalcy" because, as the historical record shows and as the report itself acknowledged, measures taken at one point to rescue the financial system have only created the conditions for even greater instability.

There are only two alternatives. Either ruling classes are able to impose the historic crisis of the profit system on to the backs of the working class, plunging it into social devastation, or the working class, armed with internationalist and socialist program puts an end to capitalism.

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