Funding the Future

The Bank of England is using quantitative tightening to...

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As the FT notes this morning:

The Bank of England's vast sale of government bonds is causing a shortage of cash in corners of the money markets and may need to end, investors have warned.

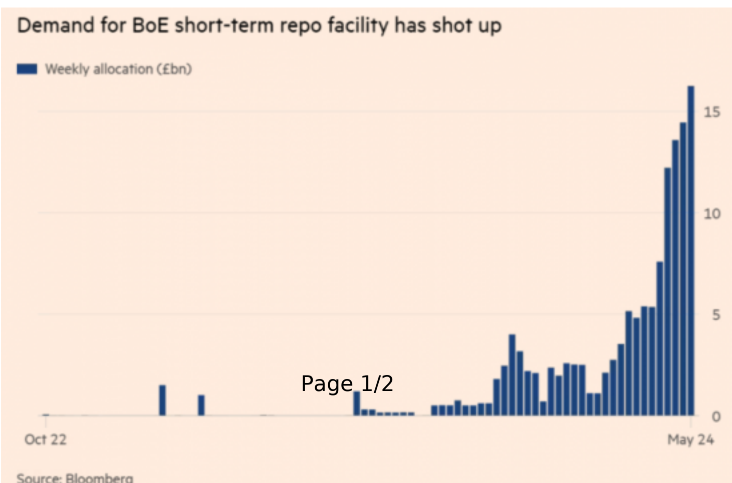
Over the past two years, the BoE has shrunk its balance sheet from nearly £1tn to about £760bn largely by reducing its holdings of government debt it bought under numerous rounds of quantitative easing stimulus.

As I have noted many times here, quantitative tightening happens to reduce the UK's government-created money supply.

Supposedly, this reduces the rate of inflation. There is not the slightest shred of evidence that this has worked in the UK, where our inflation rate has remained above that of countries and the EU, that have not used the aggressive form of QT that the Bank of England has.

The other reason for QT is to keep interest rates up. By reducing the money supply the aim is to keep up the price of using it. And as the FT notes, this is exactly what has happened.

Shortages of liquidity have developed in financial markets as a result of increasing QT over the last year or so, forcing financial institutions to borrow overnight from the Bank of England using the repo (bond-backed) facilities that it offers. The quantity has increased like this:



That indicates a significant growth in the demand for cash to match overnight payment demands by banks and others of late, which can only be because their central bank reserve accounts are being forced too low. The result has been an increase in interest rates:

As I have always suggested, it is clear in that case that the QT programme has always existed as a mechanism for forcing higher interest rates into financial markets and not to reduce the size of the Bank of England balance sheet, which is in itself a matter of total inconsequence, as Japan has proved.

So, what we are really seeing is the Bank of England deliberately increasing stress in financial markets so that the stress on householders via mortgage rates, businesses via loan rates, and renters via increased rental demands continues.

And, as I have always said, all this is for no economic gain, because inflation passes anyway.

So, what is the Bank of England doing? The only explanation is that they are declaring war on the productive economy and households, all to keep rates high for reasons that neither they nor anyone else can explain.

Incompetence on this scale requires the abolition of the Bank of England's independence. But that's not going to happen with Rachel Reeves in charge.