Is it time to replace the bond market with something su...

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One of the best uses for AI that I currently know is to ask it to summarise the arguments in an article or paper.

This does not, I suggest, mean that reading the article is not necessary. However, it does save time in working out just what an author means, provided the AI output is checked for consistency with the paper just read. This addresses the problem that all too often authors fail to express themselves very clearly, making the construction of counterarguments to what they have to say a great deal harder, even if doing so is desirable. To put this another way, AI cts the crap.

I did this with an FT article this morning. The article in question was by someone called Philip Coggan, and was entitled 'The bond market maths does not add up for governments'.

The article, as far as I was concerned, was lacking in imagination, seeking to find problems without considering possible solutions or counterarguments. However, I wished to summarise just what issues the author was seeing in the world he apparently spends his life observing before seeking to tackle what it seemed that he was saying. This is how ChatGPT summarised his arguments:

Core Argument:

Governments in developed countries are struggling to find reliable buyers for the rapidly growing volume of debt they are issuing — and this is pushing up borrowing costs, with serious fiscal implications.

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1. Rising Debt Burden

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OECD governments will issue $17 trillion in bonds in 2025, up from $14 trillion in

2023.

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Total debt is projected to reach **$59 trillion, or 84% of OECD GDP**.

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Much of this debt is short-term: **45% will mature by 2027** and will need refinancing at higher interest rates, raising fiscal costs.

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Interest on debt is already 3.3% of GDP on average — higher than defence spending.

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2. Political Constraints

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Cutting deficits is politically difficult: voters oppose spending cuts or tax rises, and populist movements are gaining strength.

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Populist governments may worsen deficits with spending promises and less fiscal discipline.

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3. Demand for Government Bonds Is Weakening

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During the 2010s, bond demand was strong — even negative yields were accepted.

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Central banks played a key role via QE, buying bonds in secondary markets and reassuring investors.

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Now, **central banks are reversing course via QT** (quantitative tightening), selling

off bonds:

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Central bank holdings of government debt fell from **29% (2021) to 19% (2024)**.

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QE is unlikely to return soon — rate cuts would precede it.

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4. Pension Fund Demand Is Changing

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Traditional defined benefit (DB) pensions invested heavily in government bonds.

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Now, **defined contribution (DC) pensions dominate** (59% of global pension assets), and they invest less in bonds.

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This shift reduces steady long-term domestic demand for bonds.

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5. Rising Reliance on International and Speculative Buyers

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With central banks and pensions retreating, foreign investors (e.g., hedge funds) are becoming more important:

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Their share of bond holdings rose to **34% in 2024**, up from 29% in 2021.

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These investors are **return-sensitive and volatile**.

6. Risk from Japanese Yield Rises

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Albert Edwards notes that rising Japanese bond yields (10-year up from 0% to 1.6%) may trigger instability.

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This undermines the **“carry trade”**, where investors borrow in yen to buy higher-yielding foreign bonds.

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As Japanese yields rise, **leveraged investors must unwind positions**, potentially triggering bond sell-offs globally.

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7. Consequences: Higher Yields, Higher Costs

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The basic supply-demand balance in bond markets has worsened: more issuance, less steady demand.

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Result: **bond yields will likely rise further**, increasing borrowing costs.

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This **tightens fiscal space** and **makes governing more difficult**.

Conclusion:

The developed world faces a structural problem: growing debts, declining sources of reliable finance, and rising costs of borrowing. Without radical shifts in fiscal or monetary policy — or new, dependable buyers — the maths of modern government is becoming unsustainable.

To be candid, I found that a lot more useful than the original piece, and one that was much easier to use as a basis for preparing a counter-narrative.

This is the counter-narrative I prepare.

Philip Coggan's claims as to the problems of government funding in the FT are deeply misleading. In his article, he ignores the structural failures of the financial system, misrepresents the nature of government finance, and clings to outdated ideas about how public funding should be raised in a modern economy.

First, we are not short of funds. We are awash with them. As Martin Wolf **has often pointed out** **in the FT, we live in a world of persistent and chronic excess saving. This is a vital observation. The financial system is flooded with money looking for a safe home. If governments are struggling to find buyers for their bonds, the problem is not with the amount of debt that they are seeking to fund, or with deficits, but is instead the consequence of financial markets having stopped functioning effectively in their primary role, which is connecting surplus savings to useful investment.**

Second, quantitative tightening is a choice, and a damaging one. This issue exacerbates the problem Philip Coggan observes at present. The reversal of quantitative easing (QE) programmes by central banks at this moment through so-called quantitative tightening (QT) is not a necessity. It is a political decision, rooted in misplaced and dogmatic fears about inflation and government deficits.

Third, QE worked. It lowered borrowing costs, stabilised markets, and underwrote investment. It could and maybe should be used again, although the technicalities would need to be revised, as I note below. There is actually nothing that prevents central banks from reversing QT and resuming bond purchases. In fact, doing so would make sense at this moment in a world where financial markets are proving incapable of allocating capital toward productive, long-term public goals.

Fourth, governments have other tools at their disposal. The idea that governments are financially constrained in the same way as households is economic nonsense. They issue the currency. They can, if they so choose, borrow directly from their central banks to fund critical spending, especially in times of crisis. There is nothing illegal about this in the UK. It might well be better to do this than repeat QE.

Fifth, governments can and should raise more tax revenue from those most able to pay. The wealthy, who have benefited most from asset inflation and tax cuts, are not paying their fair share of taxes. If there is a need to manage inflationary pressures while sustaining public investment, taxing wealth is the most logical tool.

Sixth, cutting spending is not viable and nor is it necessary. The FT piece suggests that politicians face hard choices; either find new buyers for bonds or cut spending. But cutting government spending is not a real option. It would worsen economic hardship, deepen inequality, and threaten society, and all to satisfy a broken bond market. That makes no sense at all, especially since, seventh, the problem lies in the structure of the market and not in excessive public sector economic activity.

I stress, this is not a crisis of economic overreach. This is a crisis caused by our failure to reform outdated financial structures. Gilt markets, like many aspects of modern finance, are based on assumptions often made centuries ago about the nature of money, the savings needs of society, and about inflation, risk, and monetary discipline. They are designed to benefit speculators, not society. Most especially, they are not designed to meet the modern needs of either savers or the government, so the real question is, why perpetuate them? Governments should not be beholden to the whims of hedge funds or the bond vigilantes. If the current system of bond issuance is failing, it is time to reform it.

So, eighth, it's time for purpose-driven public finance. Rather than issuing generic gilts for speculative saving and trading, governments should offer modern, purpose-driven savings products aimed at consumer markets when pension funds have departed the bond markets. These could include:

- **Green New Deal bonds targeted at climate infrastructure.**

- **NHS bonds designed to fund health investment and training.**

- **Local resilience bonds aimed at supporting regional renewal.**

Such bonds would appeal to domestic savers, and most particularly those holding the excess funds Martin Wolf describes, who want security, purpose, and social return on their capital. These are the modern equivalents of the post-war savings movements that helped rebuild Britain. They could do the same again.

In conclusion, the story we are being told is that governments are running out of financial road, but the truth is that the road is being narrowed, not by public spending, but by ideologically driven constraints on government finance. We do not lack money. We lack the courage to reimagine how to use

it. It is time to reject the panic about public debt and build a financial system fit for the future: one that works for both people and the planet, and not just institutional savings portfolios.

In summary, AI plays a role in focusing arguments.

Now, the question is:

[poll id="159"]

An AI-generated summary is available here.

Taking further action

If you want to write a letter to your MP on the issues raised in this blog post, there is a ChatGPT prompt to assist you in doing so, with full instructions, **here. Just remember to copy and paste my arguments, not the discussion on AI.**

One word of warning, though: please ensure you have the correct MP. ChatGPT can get it wrong.