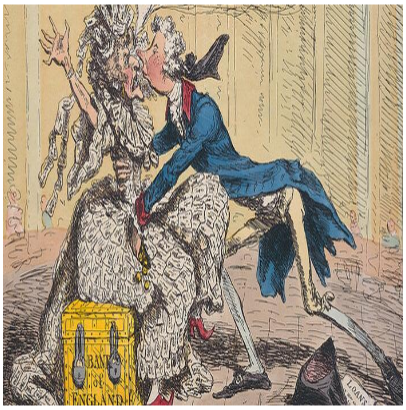

Peter Schiff: The Bank Of England Rings The Mother Of All Bells

Description

Last week, the Bank of England suddenly pivoted.

It gave up its inflation fight to rescue its pension funds and bond market. What exactly happened? And what does it tell us about the Federal Reserve's inflation fight? Peter Schiff explained it all on his podcast.

There is an old expression — "No one rings a bell" — meaning there's no warning when there is a major top or bottom in the markets. But Peter said there often *is* a bell but nobody hears it. Last week, Peter said we got the "mother of all bells."

> It was literally Big Ben that rang because the bell was in England… **The Bank of England was the first major central bank to blink in this global game of chicken.**"

Last week, the Bank of England pivoted and returned to quantitative easing.

Peter called this development "very significant." Because up until the announcement, Bank of England Governor Andrew Bailey was just as hawkish as Jerome Powell. The Bank of England raised interest rates from 0.1% last December to roughly 2.25%, including a 50 basis point rate hike in August. It was the largest BoE rate hike in 27 years.

> **He was talking tough about how resolute the Bank of England was to fighting inflation.** They've got the highest inflation in Europe. It's way above their 2% target. It's a double-digit number. It's above 10%."

Bailey even said he was committed to bringing down inflation no matter the cost and said he was willing to endure some pain, just like Jerome Powell.

> **Well, that was all a bluff because we got some pain overnight and Bailey folded like a cheap suit.** And instead of quantitative tightening, they're back to quantitative easing. The rate hikes are probably permanently on hold because the Bank of England refused to allow a potential crisis to unfold as a result of rising interest rates."

The crisis manifested itself in the UK pension system with plunging bond prices. CNBC summed up the problem.

> In order to top up the collateral on these bonds, some funds had to raise cash. But due to the speed of this crisis, many funds were caught out and were forced to liquidate their next most liquid assets, long-term bonds or gilts, causing prices of bonds to fall even more."

In order to stabilize bond prices, the BoE stepped in to buy long-term bonds, creating artificial demand and propping up prices.

This pension problem isn't exclusive to the United Kingdom. Pensions systems worldwide face the same issue, including in the United States.

When interest rates fall to zero, bond holdings in pension funds don't generate as much interest income. Pensions need this income to pay benefits. So, in order to boost their incomes, pension funds borrow money at low interest rates to buy new long-term bonds using existing bonds as collateral. They make up for lower yields by holding more bonds.

But when interest rates rise, the value of their bond portfolio collapses even as the interest on their debt rises.

> **All of the pension funds that had borrowed short to buy long-term bonds were getting crushed because the value of the bonds they owned was collapsing and the cost of servicing the debt was soaring, and they were in a position where they were**

> **going to get margin calls. Those margin calls were going to force an already collapsing bond market to fall even more and that would have wreaked havoc throughout the United Kingdom."**

In simple terms, instead of raising pension contributions or cutting pension benefits to deal with their shortfalls, pension managers took the easy, but reckless way out and borrowed money.

On top of that, the newly elected British prime minister rewarded voters with a big tax cut that threw even more gasoline on the inflationary fire.

Great Britain was looking at a potential crash in the bond market and the Bank of England rode in to save the day.

> **The Bank of England folded. They pivoted. They decided to launch a new QE program. Remember, yesterday, they were committed to quantitative tightening. Now they said they will buy whatever it takes.** They have committed to another QE infinity in order to prop up the bond market. They now have to print British pounds to buy these gilts. So, instead of fighting inflation, which yesterday was public enemy number one – it had to be brought down at any cost – now, all of a sudden, when you see the cost, well, forget about that. We're now going to create inflation."

The central bankers in England claim this is not a monetary policy decision. It was a move to avert a crisis. But as Peter said, it is most definitely a monetary policy decision.

> That's the only policy they make — monetary policy. Deciding to launch QE is monetary policy. I don't care what you want to pretend. That's what it is."

The BoE also said it just wants to maintain an orderly market.

> **Well, you can't fight inflation and maintain an orderly market because the markets have been propped up by inflation. So, if you're going to fight inflation, you'd better be prepared for a disorderly market.** And until yesterday, the Bank of England was bluffing that they were. But now that their bluff has been called, they had to show their cards, and they're holding nothing. And so, inflation won."

You might think this has nothing to do with you if you're reading this in the US. The problem is, the Federal Reserve is also bluffing. It's only a matter of time before their bluff gets called.

> **Is the Federal Reserve, when confronted with the same situation, will they make a different choice than the Bank of England?** Does the Federal Reserve have more integrity? Are these guys willing to allow a financial crisis? Because the same thing is going to happen here. We've got all sorts of leverage in our markets. We've got a bigger debt bubble than the British. It's just that the day of reckoning for us is not going to come as early as it did for them because the dollar is going up."

When that day of reckoning does come, Peter said he expects Jerome Powell to make the same decision as Andrew Bailey.

> **I don’t care how much he wants to bark about being tough on inflation. At the end of the day, he will not bite. The Fed is a paper tiger and it will fold just as quickly as the Bank of England when they’re confronted with an actual crisis.”**

by Tyler Durden

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