# Bond market turbulence returns amid political instability and hedge fund influence



The bond market turbulence associated with former British Prime Minister Liz Truss's brief tenure in 2022, often described as a black-swan event, has resurfaced in recent months amid volatility linked to former US President Donald Trump's actions. Over the last month, erratic statements and moves by Trump have unsettled equity, dollar, and bond markets, bringing the global financial system closer to a repeat of that significant market disruption than previously recognised.

The initial episode occurred shortly after Liberation Day on April 2, when Trump's expansive and unpredictable tariff policy, affecting more than 90 countries, shook financial markets. While the noticeable decline in equity markets drew considerable attention—largely due to its direct impact on pensions and savings—the effects on bond markets were even more alarming. Yields on ten-year and 30-year US Treasury bonds surged, and the US dollar experienced sharp depreciation, signalling deep-seated financial turmoil.

Traditionally viewed as safe havens during periods of instability, bond markets have now evolved into arenas dominated by macro hedge funds on Wall Street. Hedge funds including Ken Griffin's Citadel have become pivotal players in the US and British bond markets, emerging as the largest bidders in auctions of US Treasuries and UK gilts. These entities have also assumed the role of market makers, operating beyond the immediate regulatory sphere of central banks.

The returns on bonds can be enhanced through complex derivative strategies such as liability-driven investments (LDIs), which are commonly employed by UK pension funds. When markets become unstable, as they did after Liberation Day, rapid unwinding of these positions can generate significant volatility, provoking sharp moves like the plunge in the dollar witnessed at the time. Central banks responded by preparing to activate currency swap lines to prevent a full-scale crisis.

Concerns also arose regarding the exposure of highly leveraged hedge funds, which faced the risk of sizeable losses or failure amid the financial storm. However, authorities found some reassurance in the robust capital buffers instituted after the Great Financial Crisis, which helped to shield the banking system from direct jeopardy.

Amid this turmoil, US Treasury Secretary Scott Bessent played a key role in mediating the situation. He succeeded in persuading President Trump to impose a temporary halt on the escalating tariff wars to prevent a financial catastrophe. This move aligned with a strategy proposed several days earlier by hedge fund manager Bill Ackman, a Trump supporter, who called for a 90-day pause on “reciprocal” tariffs. Notably, some tariffs remain unchanged, including a general 10 per cent levy on imported goods into the US, as well as 45 per cent duties on motor vehicles and steel.

More recently, another market-disturbing episode unfolded when Trump publicly threatened to dismiss Jay Powell, Chairman of the Federal Reserve, whom he had labelled a “loser.” This announcement once again sent bond markets into disarray, with complex derivatives and borrowing amplifying the risk of a cascading financial crisis. Treasury Secretary Bessent intervened again, reportedly staying outside the Oval Office until other advisers left, to counsel the President on the urgent need to affirm Powell's position to stave off market collapse. Trump ultimately refrained from firing Powell, thus neutralising the threat.

These recent episodes have reawakened scrutiny over the systemic risks posed by under-regulated hedge funds, particularly given their growing influence in financial markets and potential to impact financial stability. There is mounting concern on Wall Street regarding the succession of the Federal Reserve chairmanship once Powell’s term concludes next year, with speculation about who aside from a Trump ally would be willing to accept the position amidst such volatility.

The Daily Mail is reporting on these developments, highlighting the precarious balance financial markets currently face amid political unpredictability and the expanding role of hedge funds in bond market operations.

Source: [Noah Wire Services](https://www.noahwire.com)

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