# Falling gilt demand threatens UK finances but stablecoins offer a new way forward



Last week, the Office for Budget Responsibility (OBR) released a sobering update on the long-term outlook for UK public finances, painting a challenging fiscal future shaped by an ageing population, climate change costs, and infrastructure demands. The report projects a significant decline in demand for UK government debt—gilts—by domestic pension schemes, from nearly 30% of GDP (around £1 trillion) to just 11% by 2050, with half of this decline expected within the next five years. This fall is primarily driven by the ongoing decline of final salary (defined benefit) pension schemes, which traditionally held gilts to match pension liabilities, and the rise of defined contribution schemes, which lessen the need for such assets.

This shift is far from a niche technical issue; it holds major implications for the UK government’s cost of borrowing. With fewer pension schemes demanding gilts, prices for government debt could remain depressed and interest rates elevated, potentially increasing the government’s annual interest payments by as much as £22 billion. Such an increase would divert public funds from essential services like health and education, compounding the fiscal pressures faced by a government already borrowing over £100 billion annually.

Attempts to address this by pushing pension funds towards infrastructure and private assets while also requiring more gilt holdings risk contradictory policy goals and exacerbate investor fears of financial repression. Meanwhile, calls to reduce overall debt issuance face political hurdles and the reality of an electorate weary of tax hikes and spending cuts. The broader OBR fiscal risks report warns of a ‘daunting’ set of challenges, including growing state pension costs—which may rise from nearly 5% to 7.7% of GDP by 2070—and sluggish productivity growth, all converging to imperil the UK's fiscal flexibility and economic stability.

Against this backdrop, some have turned to more innovative financial solutions, notably stablecoins. These digital currencies are typically pegged to low-risk assets such as short-term government debt or cash and are backed by blockchain technology, offering stability combined with programmability. In theory, the development of a UK stablecoin ecosystem—backed partly by gilts or similar sovereign debt—could help spur demand for UK government assets while modernising the financial system.

Yet the UK lags behind other global financial hubs, particularly the United States, where regulatory clarity on stablecoins is advancing rapidly. The US Treasury has signalled stablecoin legislation as a key priority, exemplified by the imminent passage of the Genius Act, which will provide clearer rules for firms issuing dollar-backed stablecoins. US companies such as Circle Internet—the issuer of USD Coin—have seen soaring investor enthusiasm, reflecting confidence in digital currencies tied to stable assets. This US momentum contrasts with the more cautious stance of the Bank of England governor, Andrew Bailey, who recently voiced concerns about stablecoins’ risks to monetary policy transmission and financial stability. His focus on tokenised reserves tied closely to the domestic banking system could limit the UK's potential to become a global leader in digital finance.

Looking internationally, countries including China, Singapore, and the European Union are racing ahead with their own stablecoin or central bank digital currency projects, positioning digital finance as a geopolitical battleground where the UK risks falling behind.

Aside from macroeconomic considerations, stablecoins may also offer solutions to domestic challenges such as financial inclusion. With high street bank closures and declining cash usage leaving some populations unbanked or underbanked, stablecoins accessible via smartphones could provide low-cost, reliable digital payment options. This could empower marginalised groups, gig economy workers, and small businesses that currently struggle with traditional banking.

There are, however, important regulatory and stability concerns. The Bank for International Settlements has warned that stablecoins pose risks to financial stability and monetary sovereignty if not properly regulated, pointing out issues including their exclusion from banking know-your-customer rules and potential to disrupt safe asset markets. The UK’s Financial Conduct Authority has taken tentative steps toward loosening restrictions on certain crypto investment products, reflecting a cautious but evolving attitude, with broader regulatory frameworks for digital assets—including stablecoins—still in development under government oversight.

Meanwhile, the tokenisation of assets such as Treasury funds has gained traction in the crypto sector, with institutional players increasingly investing in tokenised mutual funds and bonds. These products offer improved liquidity and faster settlement timeframes, appealing to crypto investors who seek yield and operational efficiency. Market projections suggest that tokenised financial products could reach trillions in value, underscoring the transformative potential of digital assets.

For the UK, embracing stablecoins and other digital financial innovations could not only help modernise its financial system but also maintain demand for sterling-denominated sovereign debt amid changing investor behaviour. However, without a clear and supportive regulatory framework, the UK risks missing out on these opportunities, exacerbating existing fiscal challenges, and ceding ground to more proactive global competitors.

The government faces the complex task of balancing innovation with financial stability, ensuring that digital assets bolster rather than undermine public finances. The evolving stance of both the Bank of England and Chancellor Rachel Reeves, especially in forthcoming statements such as the Mansion House speeches, will be crucial in signalling the UK’s direction in this fast-changing financial landscape. In this digital finance race, the UK's ability to act decisively could shape its economic resilience and global standing for decades.

### 📌 Reference Map:

* Paragraph 1 – [[1]](https://www.thetimes.com/business-money/economics/article/falling-gilts-demand-threatens-uk-finances-stablecoins-offer-hope-0c23330hq), [[2]](https://www.ft.com/content/261fa8ce-47a8-4180-870e-82331b61d03a), [[4]](https://www.ft.com/content/650576d0-408d-4dca-a8e8-88915d52bdca)
* Paragraph 2 – [[1]](https://www.thetimes.com/business-money/economics/article/falling-gilts-demand-threatens-uk-finances-stablecoins-offer-hope-0c23330hq), [[2]](https://www.ft.com/content/261fa8ce-47a8-4180-870e-82331b61d03a), [[4]](https://www.ft.com/content/650576d0-408d-4dca-a8e8-88915d52bdca)
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* Paragraph 9 – [[1]](https://www.thetimes.com/business-money/economics/article/falling-gilts-demand-threatens-uk-finances-stablecoins-offer-hope-0c23330hq), [[2]](https://www.ft.com/content/261fa8ce-47a8-4180-870e-82331b61d03a), [[4]](https://www.ft.com/content/650576d0-408d-4dca-a8e8-88915d52bdca), [[5]](https://www.ft.com/content/24133257-62eb-41f5-9778-0be200fd3b7d), [[6]](https://www.ft.com/content/4026da6b-43e6-47eb-9282-838aa841905a)

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## Bibliography

1. <https://www.thetimes.com/business-money/economics/article/falling-gilts-demand-threatens-uk-finances-stablecoins-offer-hope-0c23330hq> - Please view link - unable to able to access data
2. <https://www.ft.com/content/261fa8ce-47a8-4180-870e-82331b61d03a> - This article discusses the significant decline in UK pension funds' demand for government bonds (gilts). The Office for Budget Responsibility (OBR) projects that pension fund ownership of gilts will decrease from nearly 30% of GDP in 2025 to just 11% by 2074. This reduction is attributed to the ongoing shift from defined benefit (DB) to defined contribution (DC) pension schemes, leading to a decrease in the need for assets like gilts that match pension liabilities. The decline in demand could result in higher interest rates on UK government debt, increasing annual interest costs by approximately £22 billion.
3. <https://www.ft.com/content/adfd7fe4-d06e-40e3-a26c-a80828dc2fb4> - The UK's Office for Budget Responsibility (OBR) has issued a stark Fiscal Risks report highlighting the unsustainable state of Britain's public finances. Key concerns include escalating debt, mounting state pension costs driven by increased life expectancy, and a declining ratio of working-age taxpayers to pensioners. The pensions triple lock, originally aimed at reducing pensioner poverty, has become significantly more expensive and politically difficult to reform. Neither the Conservative nor Labour parties appear prepared to address rising fiscal challenges seriously, with election strategies avoiding tax increases or spending cuts. Both parties have made unfunded promises, further constraining economic flexibility. Essential service costs are rising, yet long-term funding solutions are lacking. Continued reliance on borrowing, stealth taxes, and politically motivated spending decisions reflect a systemic reluctance to present hard fiscal truths to voters. Unless addressed, these policies risk burdening future generations and provoking market instability akin to the brief crisis during Liz Truss's tenure. With no credible plan for debt reduction, the UK is at risk of financial and policy paralysis. The article emphasizes the urgent need for honest political discourse and tough fiscal decisions to address long-term economic sustainability.
4. <https://www.ft.com/content/650576d0-408d-4dca-a8e8-88915d52bdca> - The UK faces significant fiscal challenges, with the Office for Budget Responsibility (OBR) warning of 'daunting' risks due to rising public debt and limited capacity to handle future shocks. Despite efforts, the UK's fiscal stability has only seen temporary improvements, and debt levels are projected to rise amid low economic growth and higher interest rates. The OBR highlights the UK as having one of the highest debt, budget deficits, and borrowing costs among 36 advanced economies. Contributing factors include pension strain, continued triple lock pension commitments, and declining pension fund investments in government gilts, potentially increasing interest spending by £22bn annually. The state pension cost alone may rise from nearly 5% to 7.7% of GDP by 2070. Additionally, risks from global tensions, climate costs, and sluggish productivity growth loom large. The OBR cautions that even a slight drop in productivity growth forecasts could eliminate fiscal flexibility. With Chancellor Rachel Reeves under pressure, the government acknowledges the fiscal challenges but defends its policies aimed at long-term economic stability.
5. <https://www.ft.com/content/24133257-62eb-41f5-9778-0be200fd3b7d> - Crypto companies and traders are increasingly investing in tokenised Treasury and money market mutual funds, with assets in such products surging 80% in 2025 to $7.4 billion, according to RWA.xyz. Major funds from BlackRock, Franklin Templeton, and Janus Henderson Anemoy have experienced rapid growth, driven partly by crypto investors seeking higher-yield alternatives to traditional stablecoins. These tokenised products offer yield, ease of use, and faster settlement—often in minutes rather than days—making them attractive as collateral in crypto derivatives trading. This shift is supported by evolving market infrastructure and enthusiasm following the election of pro-crypto U.S. President Donald Trump. Analysts note the tokenised funds offer more liquidity and lower costs. McKinsey projects the tokenised market for mutual funds, bonds, and exchange-traded notes could hit $2 trillion. Adoption is being further driven by stablecoin issuers parking reserves in yield-bearing tokenised Treasuries, exemplified by Janus Henderson Anemoy's $409 million fund backed by Sky Money. While applications in collateral management are expanding, broader market adoption remains in early stages, hindered by occasional liquidity gaps. Industry leaders and institutions, including Digital Asset and JPMorgan Chase, are developing platforms to facilitate tokenised collateral transfers and trading outside traditional banking hours.
6. <https://www.ft.com/content/4026da6b-43e6-47eb-9282-838aa841905a> - The UK's Financial Conduct Authority (FCA) has proposed lifting its ban on retail investment in exchange-traded notes (ETNs) linked to cryptocurrencies, such as bitcoin and ethereum, signaling a shift in its previously cautious approach to digital assets. The ban has been in place since January 2021, but the FCA now argues that the market has matured and that investors should be allowed to make informed decisions about high-risk investments. The proposed changes are currently under consultation until July 2025. This move comes as global competition to attract the crypto industry intensifies, particularly following the reelection of a pro-industry U.S. President Donald Trump. UK Chancellor Rachel Reeves has also outlined plans to enhance regulatory frameworks and cooperate with the U.S. in digital assets oversight. However, other restrictions remain, including bans on crypto derivatives and exchange-traded funds for retail investors. Companies offering crypto-linked securities will be subject to strict financial promotion rules to ensure consumer protection, although investments in crypto ETNs will not be covered by the government’s compensation scheme. The broader UK regulatory framework will address stablecoins, trading platforms, brokers, lending, and give the FCA new enforcement powers.
7. <https://cincodias.elpais.com/mercados-financieros/2025-06-24/el-bis-carga-contra-las-stablecoins-y-las-ve-un-riesgo-para-la-estabilidad-financiera-y-la-soberania-monetaria.html> - In its 2025 annual economic report, the Bank for International Settlements (BIS) warns about the risks posed by stablecoins to financial stability and monetary sovereignty. The organisation considers these cryptocurrencies, whose value is linked to traditional assets like the dollar or euro, not to be a solid form of money and highlights potential risks if they are not adequately regulated. While acknowledging their utility in cross-border payments and as an entry point to the crypto ecosystem, the BIS points out their lack of compliance with banking know-your-customer regulations and their inability to guarantee one-to-one conversion. Additionally, it notes that their growth could generate tensions in safe asset markets and displace other investors. The BIS also alerts to the negative effect they could have on emerging economies, such as the loss of monetary sovereignty. However, the BIS defends the tokenisation of assets and money as a positive evolution of the financial system, calling on central banks to collaborate with the private sector to advance towards a more efficient and integrated monetary infrastructure.