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National Debt Levels: More of the same

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“History repeats itself” or “No one learns from past mistakes” are not just clichés.
They are well tested truths of all times.

Seven years after the worst financial crisis following the US banks’ debt problem, which plunged the world into Great Recession, a term now being used to distinguish from the last century’s episode of economic downturn known as Great Depression, nothing seems to have changed.

In fact, it is more of the same.

The latest study findings released last week by McKinsey Global Institute (MGI) reveal debt-to-GDP ratios have increased in all 22 advanced economies and 25 developing economies. Following the previous two reports on *Debt and Deleveraging: The global credit bubble and its economic consequences* (July 2011) and *Debt and Deleveraging: uneven progress on the path to growth* (January 2012), the report of January 2015 (the Report) on *Debt and (not much) deleveraging* laments, the ratio has gone up by more than 50 percentage points in many cases.

The Report puts together debts of all economic agents: not just governments alone, but also private sector companies, financial institutions and households. According to the Report, the total debt worldwide has gone up by $57 trillion; its ratio to world GDP has risen to 286 per cent from 269 per cent. Much contrary to the expectations that governments would deleverage, the Report says that government debt has soared in advanced economies, and private-sector deleveraging was limited. Developing countries accounted for roughly half the increase.

Unsustainable Government debt

Since the crisis in 2008, government debt has grown by $25 trillion. It is likely to increase in many countries, given the economic outlook. Partly, the rise was due to financing bailouts and fiscal stimulus programs arising out of the crisis itself; and the other reason is weak recovery despite aggressive policies.

Japan (total debt : 400 percent of GDP) tops the list of heavily indebted countries. The others are: Ireland (390 percent); Singapore (382 percent); Portugal (358 percent); Netherlands (327 percent) and Greece (317 percent). Japan’s debt which went up by 64 percent since 2007 is due to increases in government debt. As borrowing costs are low, there is low inflation and strong domestic demand for Japanese government bonds.

Lessons from the financial crisis are clear: a country with high debt levels can get into economic trouble regardless of whether its debts are heavily owed by the government (Greece, Italy), households (Spain, the U.S.), or financial institutions (Ireland, Britain).

China's debt ratio is relatively low at 217 percent of GDP as against UK's 252 percent; and USA's 233 percent. Rise in debt growth has been due to increases in corporate and household debt, besides government debt. China is facing the end of the housing boom. There are questions whether there would be any sharp corrections around the corner.

Household debts

While Ireland, Spain, the United Kingdom, and the United States have witnessed households cutting down their debt levels, in Australia, Canada, Denmark, Sweden, and the Netherlands, as well as Malaysia, South Korea, and Thailand, household debt-to-income ratios are rising. These countries would soon face property-related debt crises like those of 2008.

Fiji has contained the government debt level. Its ratio to GDP has fallen to 49 percent from an all time high of 56.20 percent in 2010. The lowest ever ratio was in 1981, when it was 33.7 percent. However, the private sector debt including household debt and housing loans are on the rise. The available data show housing loans rose from F$673.5 million in 2009 to F$ 885 million in June 2014; and total loans to households increased from F$ 824 million to F$1234.4 million. Due to fall in government's own domestic and external debt, Fiji's total debt (government, private sector companies and households) as percentage of GDP increased marginally from 104 percent in 2009 to 106 percent in 2013.

Remedies

The report prescribes remedies: heavily indebted countries require large increases in real GDP growth and strong fiscal adjustments for deleveraging. Further the Report wants fresh approaches: they are extensive asset sales, one-time taxes on wealth, and more efficient debt-restructuring programs. For management of household debts, the Report suggests flexible mortgage contracts, clearer personal-bankruptcy rules, and tighter lending standards.

So, we have been seeing changes in policies and approaches.

Familiar with the good old French saying?

" plus ca change, plus c'est la meme chose"

Translated in English, it means:

"The more things change, the more they stay the same."

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