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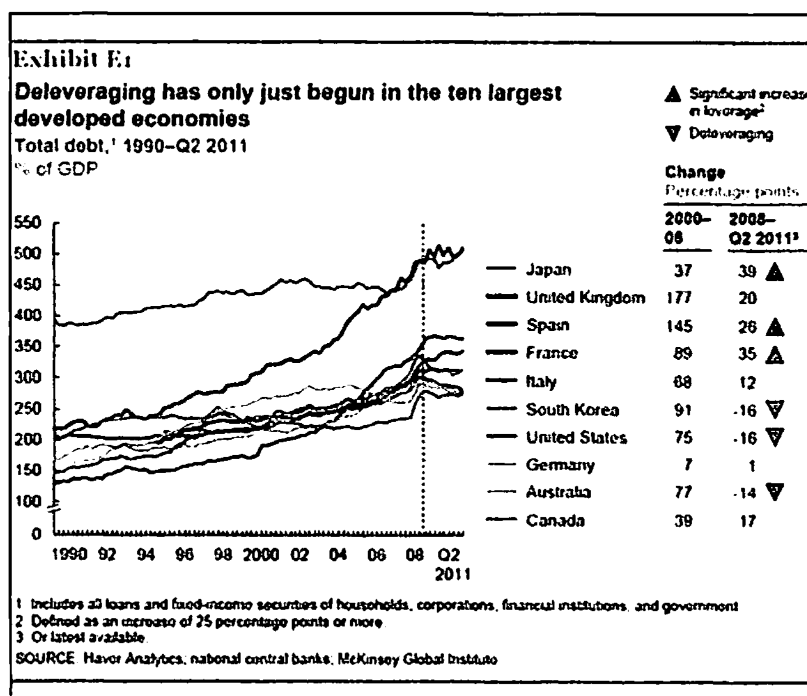
U.S. DELEVERAGING, UNLIKE SOME

McKinsey Global Institute has produced an interesting report on international debt and deleveraging. It finds that a few of the world's largest economies, including the U.S., have made significant progress in reducing debt since the second quarter of 2008, while others, mostly in the EU, have continued amassing more debt. This chart requires a little study; it shows total debt (government, household, financial institution and non-financial corporate) for ten countries from 1990 to the present. Debt is expressed as a percentage of GDP. It shows that total U.S. debt has declined since 2Q 2008 by 16%. All of that is due, of course, to the efforts of families and businesses, as government debt has skyrocketed:



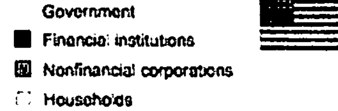
This one shows what McKinsey calls "rapid private sector deleveraging" in the United States:

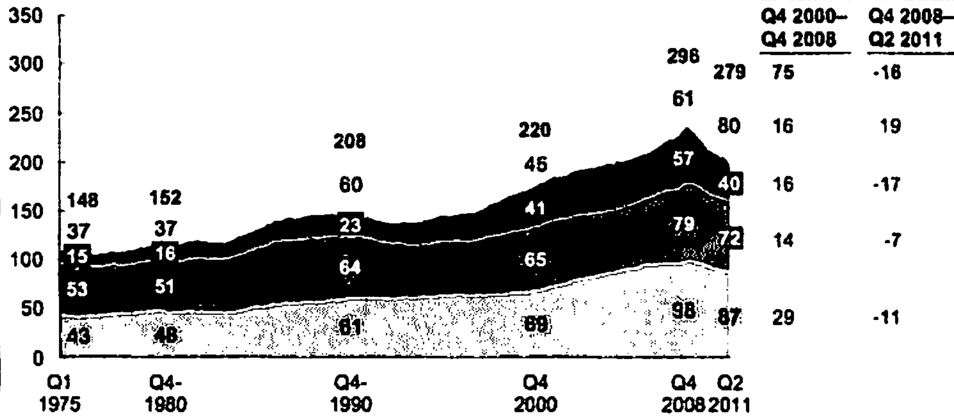
Exhibit 5

The United States has undergone rapid private-sector deleveraging since 2008

Debt[1] by sector, 1975–2011

% of GDP





1 Includes all loans and credit market borrowing (e.g., bonds, commercial paper), excludes asset-backed securities to avoid double counting of the underlying loan.

NOTE: Numbers may not sum due to rounding.

SOURCE: US Federal Reserve Flow of Funds; McKinsey Global Institute

It is worth noting that McKinsey standardized its measure of government debt across the ten countries in the study, and did not include, among other things, the federal debt that is held by the Social Security Administration as "assets." This chart shows what was and was not included:

Exhibit A4

Total US government debt ranges from 80 to 140 percent of GDP, depending on what is included

Government debt, Q2 2011

$ trillion

		$ trillion	% of GDP
Included in our government debt figures	Federal publicly held debt	9.7	80
	State and local debt	2.5	
	Federal debt in government accounts	4.6	31
	State and local unfunded pension liabilities and health benefits for retirees[1]	1.2-4.4	8-29
	Total government debt	**18.0-21.2**	**119–140**

1 Amount of unfunded liabilities varies according to the measurement metric depending on discount rate, assets market value, and cost allocation between past and future service.

SOURCE: Federal Reserve; Government Accountability Office, US Department of the Treasury, Financial Management Services, McKinsey Global Institute

In the Telegraph, Ambrose Evans-Pritchard draws conclusions that are favorable to the U.S., not so much to Great Britain: "America overcomes the debt crisis as Britain sinks deeper into the swamp."

Three years after bubble burst, the UK has barely begun to tackle the crushing burden left by Gordon Brown. The contrast with the United States is frankly shocking.

[T]otal public and private debt in the UK is still hovering at an all-time high. It has risen from 487pc to 507pc of GDP since the crisis began. ...

It is a very different picture in the US where light is emerging at the end of the tunnel. American banks, firms, and households have been chipping away at their debts, more than offsetting Washington's double-digit deficits.
The total burden has dropped to 279pc, down from 295pc at the peak of the boom. Households have purged roughly a third of the excess, roughly tracking the historic pattern of post-bubble deleveraging.

One is tempted to ask what all the fuss was about in the US. The debt of financial institutions is just 40pc, compared to the UK (219pc), Japan (120pc), France (97pc), Germany (87pc) and Italy (76pc). Bank debt has dropped from $8 trillion to $6.1 trillion — accelerated by the Lehman collapse — as lenders rely more on old-fashioned deposits.

Tim Congdon from International Monetary Research said US banks were never as damaged as claimed and now have the highest capital ratios in over thirty years. The rate of loan write-offs has dropped from 3.2pc to 1.9pc, a faster improvement than after the financial crisis of the early 1990s.
...

In hindsight, the US property boom was was remarkable modest compared to what happened in Spain, or what is happening now in China now where the house price to income ratio in Beijing, Shanghai, and Shenzhen is near 18. America's ratio peaked at 5.1 and is already back to its modern era average of three. The excesses have been unwound.

Personally, I am coming to the conclusion that the US crisis in 2008-2009 was largely a case of botched monetary policy and could easily have been avoided. The growth of M3 money — which the Fed stopped tracking thanks to a young Ben Bernanke — was allowed to balloon in the bubble, then collapse in 2008.

I can't judge whether the latter claim is true or not, although it is a widely held view. My main takeaway from these data is that the U.S. could get back on the path to economic growth rather quickly if we could only get our inept federal government under control.