We are living on borrowed (money) time

By **Vern Gowdie**, The Daily Reckoning, 13 October 2016

The Dow fell 1% on concerns over a possible rate hike and lower oil prices. And the real fear is central banks may have decided to throw in the towel on QE. The prospect of markets standing or falling on their two feet was enough to take some money off the table last night.

The market's fears are unfounded.

Central banks, for all their talk about it being time for governments to do the heavy lifting with fiscal policy, are secretly addicted to their experiment.

They oh so desperately want their theories to work.

In central banker land (a far off and distant place inhabited solely by economic PhDs with fairy wings and pixie dust) the thinking goes something like this: All we need is more time, more money, even more negative interest rates, the abolition of cash and, if that still isn't enough, to have the power to command the military to threaten people at gunpoint to borrow and spend. Then the world will see we were right all along.

The world watches their every move. They've had a taste of real power. The celebrity status that's accorded to them is feeding egos. Heads of government court them. Central bankers are not about to go quietly into the night. You can bet your bottom dollar (and that's all some people will be left with when this is over) the central bankers will continue their experiment until the bitter end.

The warnings on debt overload have come thick and fast in the past week.

First we had the 'better late than never/continually adjusting growth projections downward' IMF (and no, it is not an acronym for Idiots, Morons and Fools) telling us — surprise, surprise — the world has an unsustainable level of debt.

Shock horror…we never saw that one coming.

The Guardian's coverage of the 'big' announcement ran with the headline: 'IMF urges governments to tackle record global debt of $152tn'.

McKinsey Global Institute published a report in February 2015 (21 months ago) titled: ‘Debt and (not too much) Deleveraging’. In the report, McKinsey identified the world had added another US$57 trillion in debt since 2007. According to McKinsey, the total debt pile as at 2014 was US$200 trillion. The IMF reckons it’s at US$152 trillion.

My money is on McKinsey being closer to the mark.

Anyway, when you’re that far in the red, we can put the difference down to a rounding error.

Back to *The Guardian* article:

‘*The International Monetary Fund has urged governments to take action to tackle a record $152tn debt mountain before it triggers a fresh global financial and economic crisis.*

‘*Warning that debt levels were not just high but rising, the IMF said it was vital to intervene early in order to mitigate the risks of a repeat of the damaging events that began with the collapse of the US sub-prime housing bubble almost a decade ago.*

‘*It said that new research in its half-yearly fiscal monitor covering 113 countries had shown that debt was currently 225% of global GDP, with the private sector responsible for two-thirds of the total.*’

Does the IMF seriously think this is some sort of revelation? If they do, what hope have we got?

Brace for impact folks.

What makes me laugh is the line, ‘*Warning that debt levels were not just high but rising...*’

Of course debt levels are rising.

What do you expect the outcome will be when the cost of borrowing is zero or, if you’re lucky, investors will actually pay you for the privilege of lending you money? Go figure, debt levels are rising.

Even our own RBA acknowledged the borrowing incentive provided by low interest rates.

Up until recently, the RBA's monthly statement on the cash rate included this sentence: '*Monetary policy has been accommodative for quite some time.*'

That's central banker speak for 'We are keeping interest rates low for long enough to make borrowing money — to stimulate growth — look like a no-brainer'.

The RBA have dropped this sentence from recent statements…perhaps they got sick of stating the obvious.

Given this *accommodative* policy, it comes as no surprise that the head of S&P Sovereign Ratings Committee issues a warning earlier this week over our foreign debt levels.

According to *The Australian* on 10 October 2016:

'*Australia's foreign debt has hit "extreme" levels that match the worst in the world, according to a startling warning from ratings agency Standard & Poor's that will intensify the dispute over budget repair after years of political deadlock on major savings.*

'*The global S&P executive who signs off on Australia's credit rating has rung the alarm over the nation's debt, suggesting the Turnbull government will need to find substantial new savings to avoid losing its coveted AAA rating.*'

Foreign debt is money we've borrowed from overseas investors to fund our lifestyles.

We are living well beyond our means, but, what the heck; we're the envy of the world.

'*Mr* [Scott] *Morrison attended the annual meetings of the International Monetary Fund and World Bank in Washington last week.*'

'*"There is not an economy in the G20 or otherwise that would not want to be Australia at the moment and would not want to have the strong financial and banking system that ensures that we can have the resilience to ensure we underpin jobs and growth in this country," he told parliament on Monday* [9 October 2016].'

— Yahoo7 News

They said the same about the Spanish economy in 2007. Look how that debt-financed property bubble economy turned out.

In the blue corner we have the IMF and S&P Ratings saying ‘whoa, time to rein in the debt’; in the red corner we have central banks and governments saying ‘we need to keep rates lower to accommodate more borrowing so we are the most envied economy in the world’.

Imagine the four parties sitting around a table; the conversation would go something like this:

CB and Govt.: We need more debt to grow the economy.
IMF and S&P: We have too much debt already in the economy.
They all ask: Then, how do we grow the economy?
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They all ask: Then, how do we grow the economy?

This is the bind we are in.

For far too long, debt has been the sole economic driver in the global economy.

We are utterly dependent on it for a statistical measurement of ‘growth’.

The creaks and groans of the world’s debt load are becoming so loud even the IMF can hear it in their soundproof Washington DC offices.

The last time the system took a break from shouldering more debt was in 2008/09. Here’s the Federal Reserve chart on total US debt since 1945. That minor, teeny-weeny disruption in the extrapolating debt trend resulted in the greatest economic upheaval since the Great Depression. That’s a serious dependency issue. Since 2008, the only thing additional debt has bought us is a stay of execution.

We are literally living on borrowed time.

When the debt load collapses under its own weight, envy is going to turn to pity.

Pity those poor Australians (literally) who believed their own BS about being recession-proof, who have borrowed to the max to fund lifestyles well above their pay grade.

Our total national debt (public, corporate and private) is $6 trillion — four times the size of our economy. We have never been more exposed to an external shock. This could get real ugly.

When the authorities — ratings agencies and the likes of the IMF and Bank of International Settlements — start issuing warnings, while at the same time government ministers strut around like peacocks telling us 'how good we are', you know it will have gone past the point of no return.

That's why central banks will plumb new lows to keep the whole thing upright for as long as possible.

The end result will be the US share market going to new highs — the classic suckers' rally awaits.

Cheers,

Vern Gowdie, for *The Daily Reckoning*
