World economy engulfed by “debt tsunami”

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Global debt has risen to unprecedented levels since the onset of the COVID-19 pandemic in what the Institute for International Finance (IIF), whose members include over 400 banks and financial institutions, has characterised as an “attack of the debt tsunami.”

In its Global Debt Monitor report issued on Wednesday, the IIF, said global debt would set a new record and reach $277 trillion by the end of the year, equivalent to 365 percent of world GDP.

“Spurred by a sharp rise in government and corporate borrowing as the COVID-19 pandemic wears on, the global debt load increased by $15 trillion in the first three quarters of 2020 and now stands at $272 trillion,” the IIF report said.

The extent of the debt acceleration is revealed in data for individual countries and regions. Debt in the major economies jumped to 432 percent of GDP in the third quarter, up from about 380 percent at the end of 2019. Emerging market debt hit nearly 250 percent, with China at 335 percent.

In the US, total debt is on track to reach $80 trillion this year, up from $71 trillion at the end of last year. Debt in the euro area rose by $1.5 trillion in the first nine months of this year.

The IIF report said debt burdens were particularly onerous for emerging market economies, having risen by 26 percent this year as a proportion of GDP. Consequently, the share of government revenues in these countries going to make payments to international finance capital has been rising sharply.

This week Zambia became the sixth developing country to default on a loan and more defaults are expected to come. By the end of next year, some $7 trillion of emerging market bonds and syndicated loans will come due with about 15 percent denominated in US dollars.

The debt crisis for these countries is being intensified by the downturn in the world economy which, according to the International Monetary Fund, is expected to contract by 4.4 percent this year. The IMF has predicted a rebound for 2021 but that forecast was issued before the latest surge in COVID-19 infections in the US and Europe.

The surge in debt is not solely attributable to the pandemic. Even before it struck, the global economy was sliding into a downturn after a brief “recovery” in 2018 from the impact of the 2008 financial crisis.

“The pace of global debt accumulation has been unprecedented since 2016, increasing by over $52 trillion,” the IIF said.

While $15 trillion of this surge had been recorded in 2020, the debt increase from 2016 far exceeded the rise of $6 trillion between 2012 and 2016. In other words, even before the pandemic struck, the entire financial system and the global economy were becoming increasingly dependent on debt accumulation.

Emre Tiftik, the director of sustainability research at the IIF, said debt levels had risen much faster than anticipated at the start of the crisis. There is less “bang for the buck” so far as growth in the economy is concerned.

Tiftik said the increase in debt without a change in the level of economic growth “suggests that we are seeing a significant reduction in the GDP-generating capacity of debt. Aggressive support measures will be with us for some time and will inevitably increase debt significantly.”

The reasons for the divergence between debt levels and GDP growth are not hard to find. Much of the increased debt for emerging market economies is not used to boost their economies and improve health, education and other necessary measures but is used to pay interest and principal on existing debts.

In the major economies, such as the US and Europe, debt is not being incurred to provide the funds for infrastructure or health care measures. It has been used to finance massive corporate bailouts, or is being taken on by corporations to finance their speculative operations in financial markets. None of this generates an atom of real wealth but is used to increase profits obtained by financial operations.

However, if the flow of money is reduced, it threatens to set off a financial crisis, with immediate effects for the real economy as was revealed in the 2008 financial crisis.

The IIF pointed to this danger.

“There is significant uncertainty about how the global economy can deleverage in the future without significant adverse implications for economic activity,” it said.

Another record reached in financial markets earlier this month also underscores the growing instability of the entire system in the face of the “debt tsunami.”

According to the Bloomberg Barclays Global Negative Yielding Debt index, bonds worth $17.05 trillion now have a negative yield, meaning that the price of the bond is so high that an investor would make a loss if they held the bond to maturity.

Of course, no investor lays out massive amounts of money to make a loss. They are betting that the price of the bond will rise still further and lower the yield (two have an inverse relationship) and they will make a capital gain when they sell.

The bond market is only being sustained by the interventions of the world’s central banks—with the Fed alone spending $80 billion a month, almost $1 trillion a year, to buy US government debt.

As Mark Dowding, the chief investment officer at BlueBay Asset Management, told the *Financial Times*: “Central banks have been buying up more debt than governments can throw at them. That’s been pushing yields down in spite of the huge fiscal expansion.”

But low yields have completely disrupted the investment strategies of pension funds and life insurance companies, which have traditionally relied on returns from secure government bonds to meet their obligations.

The result, as Dowding noted, is to push investors into ever riskier debt financing for governments and corporations as they seek a higher rate of return. The same process has driven the stock markets to near record highs as a result of the injection of trillions of dollars by financial authorities.

The massive growth of debt has decisive and immediate implications for the struggle of the working class to defend itself against the “tsunami of death” unleashed by the refusal of capitalist governments to undertake any meaningful action to combat the pandemic.

Debt, like all other financial assets, is not in-and-of-itself value. It is a form of fictitious capital—a future claim on the surplus value extracted from the working class in the process of capitalist production.

If that process is in any way interrupted, the mountain of fictitious capital is threatened with a collapse. That was seen in mid-March when the initial impact of the pandemic, and the rising demands of workers that action be taken against it, saw a freeze in all financial markets. The potential meltdown was only prevented through the intervention of the Fed and other central banks and the accompanying back to work drive.

Now in the second and third waves of the pandemic, the demand of all sections of the financial oligarchy and their political representatives is that there must be no lockdown. That is, no effective measures will be taken to deal with the pandemic based on the closure of non-essential services and industries with compensation for the workers involved.

Surplus value must be continued to be pumped out of the working class, no matter what the cost to life.

The present situation underscores the insistence by the WSWS that the solution to the pandemic crisis lies in the development of the independent struggle of the international working class to take political power in its own hands in order to initiate a socialist program.