**The problem with the policy of growth through massive debt!**

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US President Teddy Roosevelt said, “nothing in the world is worth having or worth doing unless it means effort, pain, difficulty”. The resulting attributes mentioned in this quote describe quite closely Prime Minister Imran Khan’s big play and ambition about home ownership. The Pakistani Premiere recently launched a housing scheme that espouses to provide a loan for buying or building a house or flat at an interest rate of 5% per year. Imran Khan has spent quite a while in the UK and is acutely impressed by its – and US’ – mortgage industry and underlying financial system. Just like leaders in the West including the US, he perhaps also equates the increase in money circulation as a sign of growth. The problem is not growth through money circulation but growth through money circulation built on massive debt! As it can be in the case of an ‘unbridled and come what may’ home financing scheme. While home ownership itself is a noble endeavour and should be encouraged, the pitfalls of not managing it well are colossal! Consider.

The 2007 – 2008 financial crisis was predominantly a result of two factors. First, the systematic and effective sloganeering that ensured that the whole population would be geared towards home ownership, ‘come what may’. And that if someone couldn’t own a home then that person would somehow be left behind and belittled in the eyes of wider society. Second, and a corollary of the first, corporate greed and predatory lending to individuals who didn’t have the capacity to take anywhere near the level of debt being thrown at them. That put paid to the Efficient Market Hypothesis that markets are self-correcting, asset prices include all available information and an asset’s value will decline if too high! So much so that Alan Greenspan, the US Federal Reserve Chairman at the time of the crisis, said that he had spotted a flaw in his free market doctrine which guided his 18-year stewardship of US monetary policy. In his own words, “I made a mistake in presuming that the self-interests of organisations, specifically banks and others, were such that they were best capable of protecting their own shareholders and their equity in the firms”. In other words, without proper checks and balances, increased aspiration of home ownership especially along with predatory lending, will wreak havoc with the economy!

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But how and when does excessive home lending become a problem? A quick introspection of the US mortgage industry in the run up to the financial crisis of 2007 – 2008 provides some clear guidelines. The Case–Shiller index, which tracks house prices in the US, suggests that right until the 1970s there was practically no increase in house prices once adjusted for inflation. This coincided with the time when income equality was prevalent, economic gains were widely the same for all distribution groups including the top 1% and bottom 20% and the dollar was backed by gold. However, the US Federal Reserve had already started an expansive inflationary monetary policy during the 1960s and foreign governments began to redeem more and more dollars for gold leading to a very real threat that US gold holdings might eventually be exhausted. Hence President Richard Nixon decided to remove the convertibility of US dollars to gold thus a fiat currency was born where the dollar wasn’t linked to anything of intrinsic value! And, as other currencies were pegged to the US dollar since the end of World War II, they too became fiat currencies in one fell swoop! This meant that central banks everywhere had carte blanche to embark upon inflationary monetary policies underpinned by the printing of money! Without giving a second thought to the fact that they were ‘creating money out of nothing’! This resulted in debasing of currencies pretty swiftly and led to excessive inflation and four other fatal phenomenon at the backend of the 1970s. One, house prices – based on the incessant notion of always owning a home – started to climb, first slowly and then rapidly. Two, income inequality sky rocketed. The US Centre on Budget and Policy Priorities estimates that from the 1980s till around the present day, income gains of the top 1% are about 226% while those of the bottom 20% only a meagre 47%! The inequality gulf widened substantially. Three, the focus of the top 1% became asset accumulation thus igniting periodic asset bubbles across the world. Ironically, what exacerbated asset bubbles was the unwillingness of the top to increase the wages of the bottom but at the same time providing the bottom with debt laden predatory mortgages! Four, banks and lenders realised that investing in businesses and factories didn’t provide as high a return compared to providing high interest loans for home financing. Therefore, these institutions also joined the mantra of home ownership ‘come what may’! All this resulted in approximately 10-year cycles of boom and bust, of which the credit crisis of 2007 – 2008 was one occurrence.

As previously stated, Imran Khan will do well to fulfil his decent intentions of providing an affordable home to the general population. Nevertheless, such initiatives will create more problems than solutions unless he learns the following six policy lessons from his cherished Western economies. First, ignore the Efficient Market Hypothesis. Self-correcting economic mechanisms seldom exist and an interventionist approach to policy making is almost always needed. Second, an expansive monetary policy maybe a suitable start but is rarely a suitable finish. Third, license to print money is never an answer to any long run issues. Fourth, effective, independent, and competent oversight – especially that of the state bank – is a must. This should never be limited to only lip service! Five, although some realistic amount of debt may be always necessary for growth but policy stewardship should ensure that this debt is tilted towards businesses, factories, and job creation entities rather than only home mortgages. Six, do something about income inequality! Always bear in mind that this is one barometer that showcases the health of the economy as well as society. Perhaps taxation policy should be tasked with ensuring equal income gains. Without question, this is a tall order! And for a developing country, even more so! But as Hunter S. Thompson says, “anything worth doing, is worth doing right”.

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