Onward To Insolvency

By Ashok V. Desai

Pakistan has taken on so much shorter debt that is has to keep printing money, or borrow to repay loans.

It is well known that Pakistan's economy has done badly for years. The primary reason is that its balance of payments has been precarious, and that it has been living on the generosity of foreigners. One factor behind this dire situation is that its government has been most undisciplined and run enormous fiscal deficits. It has had what it thought was a good reason to do so, namely the possibility of an attack from India, and it may feel justified in its profligacy because it has so far avoided the attack. But as any Indian knows, only a lunatic would court a nuclear war with Pakistan, and India is not yet ruled by a lunatic. So it has been a pointless bonfire.

Pakistan has taken on so much shorter debt that is has to keep printing money, or borrow to repay loans.

When a country gets doles or borrows from international institutions, they expect it to use their bounty sensibly; every once in a while they come and check whether it has done so. As Wiki leaks proved, they found that it had not done so – that it had blown up America's economic aid on its armed forces. Lenders would also worry about whether Pakistan can repay its debts. To reassure them, Pakistan has published a Debt Policy statement, which is revealing in its way.

In the past six years, the ratio of Pakistan's public debt to gross domestic product has fluctuated around 55-60 percent. That is not extraordinarily high by world standards. Greece's ratio last year was 130 percent; Italy's, 115 percent. These are basket cases, but countries in no immediate danger of default have much higher ratios. For example, Germany's ratio last year was 74 percent, France's 84 percent, Singapore's 99 percent, and Japan's, 225 percent. If the debt-GDP ratio were the only criterion, it is difficult to see why Pakistan is in such trouble.

Maybe it is because Pakistan's external debt is too high. Actually, it has been somewhat smaller than domestic debt; its ratio to GDP has been 25-30 percent. This is peanuts; Sao Tome and Principle's ratio is 349 percent, Liberia's, 590 percent, and Ireland's 1,103 percent. Even if we leave out basket cases, Switzerland's ratio is 229 percent, Hong Kong's, 334 percent, and Britain's, 400 per cent.

Dividing by GDP is an elementary way of making figures for different countries comparable, but when it comes to debt, it is crude. After all, public debt is debt of the government, it has to be in a position to

repay the debt, and its capacity to repay depends on its revenue. Pakistan's public debt has been roughly four times as high as its revenue. So even if the government were to repay the debt over 20 years, it would have to use a fifth of its revenue to do so. If it were to pay 10 percent interest on the debt, its debt service ratio would come to 60 percent of its revenue; that would be drastic.

Actually, Pakistan's situation is so dire that it would not think of retiring its debt; it only has to worry about the interest payments, plus the short-term loans it has to repay. Its debt service ratio was 30 percent in 2006-07; five years later it had risen to 40 percent.

In all the above comparisons, I implicitly held the exchange rate constant. Actually Pakistan's payment situation is so dire that its Rupee is being devalued all the time; and devaluation increases the burden of the foreign debt in domestic currency. In the past year, 20 percent of the increase in debt was due to currency depreciation.

Although Pakistan's debt looks small by the world standards, its government finds it difficult to find buyers for it. In 2005-06, 22 percent of the borrowings were against what Pakistan Government euphemistically calls market-related treasury bills; in 2010-11 their share had gone up to 26 percent. These are treasury bills the government notionally sold to the State Bank of Pakistan. Since it owns the bank, these treasury bills only transfer money from one of its pockets into another. It lends to itself, more accurately, it prints money.

It can print Rupees, but it cannot print dollars or Euros; foreign loans have to be repaid on maturity. That comes to a tidy sum. Interest payments come to only about 3 percent of foreign exchange earnings. But repayments come to 15-17 percent. So about a fifth of foreign exchange earned has to be spent on debt servicing. The repayment to disbursements ration was 45 percent in 2008-09; in the next two years it rose to 71 percent; Pakistan is borrowing to repay old debts.

The fact that most foreign debt is short – to medium – terms and has to be repaid on time makes the government anxious to have foreign exchange in hand. That plus the lower interest rates on foreign loans make it eager to borrow abroad. That is what keeps the Pakistan government on a foreign exchange tight rope.

Standing Up To Europe

By Kenneth Rogoff

The IMF has so far sycophantically supported Europe; it should now stand up to the defaulting countries

As the Eurozone crisis continues to deepen, the International Monetary Fund (IMF) may finally be acknowledging the need to reassess its approach. New managing director Christine Lagarde's recent call for forced recapitalization of Europe's bankrupt banking system is a good start. European official's incensed reaction – the banks are fine, they insist, and need only liquidity support – should serve to buttress IMF's determination to be sensible about Europe.

The IMF has so far sycophantically supported each new European initiative to rescue the over-indebted Eurozone periphery, committing more than $100 billion to Greece, Portugal and Ireland so far. Unfortunately, the IMF is risking not only its members' money but its own institutional credibility.

Only a year ago, at the IMF's annual meeting in Washington DC, senior staff were telling anyone who would listen that the whole European Sovereign-debt panic was tempest in a teapot. Even for Greece, the IMF argued, debt dynamics were not a serious concern, thanks to anticipated growth and reforms. Never mind the obvious flaw in IMF's logic, namely that countries such as Greece and Portugal face policy and implementation risks far more akin to emerging markets than to truly advanced economies such as Germany and US.

As the situation deteriorated, one might have guessed that the IMF would mark its beliefs to market and adopt a more cautious tone. Instead, at its April 2011 interim meeting, a senior official declared that the IMF now considers troubled Spain to be a core Eurozone country like Germany, rather than a peripheral country like Greece, etc.

Simply put, Europe and US control too much power in the IMF, and their thinking is too dominant. What European leaders may want from the IMF are easy loans and strong rhetorical support. But what Europe really needs is the kind of honest assessment and tough love that IMF has traditionally offered to its other, less politically influential, clients.

The IMF's blind spot in dealing with Europe until now is only partly due to European voting power. It also stems from an "us" and "them" mentality that similarly permeates research at the top Wall Street investment houses. Analysts who have worked their entire lives only on advanced economies have learnt to bet on things going well, because for the couple of decades prior to the crisis, things mostly did go well – very well.

That is why, for example, so many keep assuming that a normal rapid recovery is just around the corner. But the financial crisis should have reminded everyone that the distinction between advanced economies and emerging markets is not a bright red line.

In his recent speech in Jackson Hole, Wyoming, US Federal Reserve chairman Ben Bernanke forcefully complained that political paralysis has possibly become the principal impediment to recovery. But analysts accustomed to working on emerging markets understand that such paralysis is very difficult to avoid after a financial crisis. Rather than slavishly believing policymaker's assurances, emerging-market researchers have learnt to be cynical about official promises. All too often, everything that can be done wrong will be done wrong.

The IMF need to bring much more of this brand of skepticism to its assessment of Eurozone debt dynamics, instead of constantly seeking strained assumptions that would make the debt appear sustainable. Anyone looking closely at Europ's complex options for extricating itself from its debt straight-jacket should realize that political constraints will be a huge obstacle no matter which route Europe takes.

Even outside Europe, the IMF has long given too much credence to sitting governments, rather than focusing on the long term interest s of the country and its people. It is doing Europe's people no favour by failing to push aggressively for a more realistic solution, including dramatic debt write-downs for peripheral Eurozone countries and reallocating core-country guarantees elsewhere.

Now that the IMF has squarely acknowledged the huge capital holes in many European banks, it shoud start pressing forcefully for a comprehensive and credible solution to the Eurozone debt crisis, a solution that will involve either partial breakup of the Eurozone or fundamental constitutional reform. Europe's future, not to mention the future of the IMF, depends on it.

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Europe’s Economic Crisis is not a Euro Crisis

What should be simple debt workout matter is in danger of spinning into a genuine catastrophe

The funny thing about the ‘euro crisis’ is that it is not a euro crisis. The currency itself is meandering along serving as a unit of account and means of payment.

Instead, we have a crisis of insolvency, first among certain profligate governments and second among banks. This has nothing to do with the euro itself.

Greece has about the same population as Los Angeles. If the government of Los Angeles defaulted on its debt, does that mean that Los Angeles must leave the ‘dollar zone’ and issue a new Los Angeles peso? The issues facing the Greek government are not really any different from those facing millions of US homeowners who borrowed more than they should have. Hard decisions must be made. But nobody suggests that those foreclosed homeowners need their own personal currency.

The other strange idea out there is that these various insolvency problems require some sort of aggressive federalization, the creation of European super state. The rationale behind this argument seems to be that the super-statists want some kind of central body of such immense stature that it can bail out the entire continent. The reasoning behind that, lenders should never take an honest loss when the losses can be foisted on the innocent taxpayer instead.

The other insolvents in our drama are the banks themselves. They are busy promoting the line that any bank losses need to be made up via a taxpayer-funded recapitalization, usually on terrible terms that amount to little more than theft.

A more sensible and fair approach would be a debt for equity swap. In the simplest terms, a typical bank will have 1000 Euros of assets in the form of loans, 900 Euros of liabilities in the form of borrowed money and 100 Euros of equity. After a series of losses the bank’s assets are worth 800 Euros, but the 900 Euros of liabilities remain.

At this point, 300 Euros of bonds could be converted t equity. This would leave the baks with 800 Euros of assets, 600 Euros of borrowings and 200 Euros of equity, thus returning the bank to a state of health without the need for taxpayer funds. A huge equity cushion remains for any future losses.

Do banks know this? Of course.

They employ hundreds of sophisticated securities analysts. JPMorgan Chase’s takeover of Wahington Mutual in 2008 was done under similar conditions. The unsecured debt was eliminated, thus

recapitalizing the bank. WaMu's bank operations continued, quickly rebranded as Chase. We can only wonder why this option is not being more fully discussed across the pond.

The basic problem with the euro project is that it is in the hands of incompetents who seem to have no idea what to do when a borrower can't make the payments. The rules of capitalism on that score are clear: If the borrower is no longer able to borrow, the lender takes a loss. Both can learn from their errors and avoid them in future.

Unfortunately, what should be a simple debt workout matter is in danger of spinning into a genuine catastrophe.

The idea, repeated so often, that the euro zone needs to either break up into multiple currencies or form some sort of super state has no basis in reality.

Europe's problems are eminently solvable. However, given the very poor quality of leadership on the continent today, lots of unpleasant things that don't have to happen might indeed anyway. Equrope has no one to blame but itself.

The 1000 Genomes Project Can’t become a basis for discrimination

Eric Green, director of the US National Human Genome Research Institute, has played a key role in research aimed at decoding the human genome. He is now involved in the ‘1000 Genomes’ research project which collects, studies and profiles the genetic maps of several diverse population groups, this complex data’s destination being the public domain, Green spoke with Smita Panday about the genetic research project, the vital contributions it aims at and managing possible drawbacks around it:

What is the ‘1000 Genomes Project’?

The 1000 Genomes Project aims to study the genetic maps of 2,500 people from 27 populations around the world. The first phase was to sequence and genotype 1000 samples that were available. The goal is to find most human genetic variations, which will then be used to discover diverse genetic contributions to health and disease. The data will be helpful in determining which genes contribute to the diseases.

In the project, 300 of the samples come from populations with an ancestry from India, 100 come from Bangladesh and 100 come from Pakistan.

Have you needed to work closely with research institutes in India in order to access genetic data on populations of Indian origin?

Samples from people of Indian ancestry are coming from other countries, like the United Kingdom and the United States, to which these people migrated. Despite considerable efforts to convince Indian researchers to participate in the 1000 Genomes Project, they were unable to agree about how to collaborate in the endeavor.

How will the ambitious aim of putting genetic data in the public domain help the scientific community?

All researchers looking for genetic contributions to disease risk, protection from disease risk or response to therapies will be able to use the data for free. Researchers focusing on a specific disease will be able to compare the individuals in their study to this international reference catalogue of human genetic variants. This will accelerate research on all diseases and human traits.

Yet, so much personal data is being made public via the project. Doesn't the move hold the potential to create discrimination based on a person's genetic profile?

The 1000 Genomes Project is not collecting any medical or personally identifiable information on the people who came forward and donated blood samples. Therefore, the project itself cannot become a basis for discrimination based on genetic profiles. But countries will need to regulate the use of the

genetic risk information, so that people can utilise it productively to improve their health, rather than being afraid to use it.

In the United States, a law called the Genetic Information Nondiscrimination Act of 2008 bars the use of genetic information for decisions about employment or health insurance coverage. But regulating the use of any information - medical or genetic or otherwise - is a sovereign right for individual countries.

This has been a loaded issue through history - can your research now end up stoking sentiments of racism based on popular understandings of superior or inferior genetic profiles?

There is no evidence of the 'genetic superiority' of any population. People within populations are diverse, so some people are at higher risk for some diseases and lower risk for other diseases. Some genetic variants conferring risk for particular diseases are more common in some populations while other populations have variants conferring risk for other diseases. In the end, the balance between risk-conferring and risk-protecting genetic variants averages out across populations, so none is genetically better than any other.