Financial Review - afr.com

Sep 20 2018 at 11:07 AM
Updated Sep 20 2018 at 5:25 PM

Australia most exposed to debt crisis: State Street

by **Patrick Durkin**

Australia's household debt to income has climbed rapidly ahead of other developed countries, leaving the country exposed to the next potential crisis, one of the world's largest investors warns.

"One of the big things that we are worried about in the coming year or so is debt levels generally," State Street Global Advisors deputy global chief investment officer Lori Heinel told a conference of some of the country's largest investors in Melbourne on Thursday.

"If you look at the increase in debt globally since 2010 it's up over 180 per cent," the visiting US fund manager told the JANA annual investor conference.

"Some of that is in pockets like government debt, for example, the US is printing trillion dollar deficits on an annual basis on the back of the tax cuts and one might argue that debt is sustainable and not a problem but if you start to have any significant uptick in rates the amount of debt servicing required could be a real problem," she said.

"So it is argued that the next downturn, the next crisis may come from a very conventional place, it may simply come from the end of the debt cycle and a debt crisis," Ms Heinel said.

Pockets of leverage

UBS head of fixed income Anne Anderson warned that tighter monetary policy would lead to higher volatility but indicators suggested the next recession is at least three years away.

"I don't think the indicators suggest the next recessions is a near and present danger," she told the conference.

"Every cycle is different...but the drivers we see are that the cycle still has room to run, the corporate sector is still very healthy but there are pockets of leverage building up," she said.

AllianceBernstein's chief economist Guy Bruten told the conference "it does seem that we are transitioning to a different phase."

"There has been no de-leveraging since the financial crisis," Mr Bruten warned, who also argued the rise of populist politics "will be a long-run phenomenon".

Trump's playbook

Ms Heinel warned that an all out trade war between the US and China is expected to knock around one percentage point off global GDP and about 2 percentage points off GDP in the US and China.

"These are really high-stakes games," she said on Thursday.

Local fund managers are less downbeat with joint managing director and chief investment officer of L1 Capital, Mark Landau predicting the current escalation would be a precursor to a deal.

"If you read Trump's playbook historically, it has been maximise leverage, put huge pressure on the opponent and then do a dealer, if we did do a deal with China or the US that would be a huge positive catalyst particularly for miners," he said.

But the local fund managers are fairly grim about the prospect for Australian shares with Mr Landau warning there is no value in the top 20 stocks because "the outlook for Aussie equities is average" and the banks, technology and retail property stocks are set to fare worst.

The banks "face all sorts of pain", Scentre Group's "best days are behind them" and "we don't think that Australia can develop the next Google or Facebook", he said.

However Los Angeles-based Sarah Ketterer, CEO of Causeway Capital with $60 billion under management, has been out here meeting with AMP, Telstra and taking a look at the banks as they search for "unpopular, undervalued" stocks. One of their biggest bets is Volkswagen hit by diesel gate in 2015.

"Any scandal which is damaging to profitability is worth analysing", she told the conference.