

# Markets are ignoring serious risks, says Citigroup chief economist

Willem Buiter lists some of them – China, Brexit, the US economy and the EU

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FINANCIAL markets are “completely ignoring” serious downside risks to the global economy emanating from sources such as China, Brexit, the US economy and the European Union (EU), Citigroup’s global chief economist Willem Buiter has said.

Speaking at the Asian Monetary Policy Forum on Friday, he said that while this year’s global economic growth is running at a decent rate of about 3 per cent in real terms, the markets are focusing only on the most benign scenarios, without regard to the accompanying risks – and there are plenty of them.

One of the biggest relates to developments in China’s economy, which he suggested displays signs of “an accident waiting to happen”. China’s total debt now exceeds 300 per cent of its GDP, he pointed out, and the government is addressing it by adding further to the leverage, a process “which can end only one way”.

China’s economy also suffers from over-capacity in several industries, which the authorities are dealing with only in selected sectors such as coal and steel, but not in others.

The risks related to Brexit, Britain’s departure from the EU, are also underrated, said Dr Buiter. Britain stands to lose access to much of the labour that many of its industries need and which currently comes from the EU.

Going forward, this spells bad news for capital spending as well as foreign direct investment. Thus far, only the exchange rate has responded to these negative developments. The markets have stayed buoyant.

Dr Buiter pointed out that in the United States, equity markets are trading at valuations which are “hard to understand” and not justified by underlying growth of corporate earnings – a view echoed by a number of market observers. For instance, a recent study by the Bank of America found that the S&P 500, which is trading at more than 25 times current earnings, is over-valued in 18 out of the 20 most commonly used valuation metrics.

Dr Buiter also pointed out that the level of corporate borrowing, especially in the so-called “junk-bonds” (high-yield bonds), is “in dangerous territory”. The risks there, too, are underpriced. He noted that while banks have de-leveraged, household leverage in the US is rising – not through mortgages as was the case in the run-up to the global financial crisis of 2008, but through credit cards, sub-prime car loans and student loans.

“Trump risk” has also not been properly priced, said Dr Buiter. The threat of trade wars has ebbed, but the possibility of trade skirmishes, particularly with China, remain.

The break up of the euro zone also remains a risk, he added, noting that the euro currency system as it stands – with 19 central banks serving as profit-and-loss centres –



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is “not viable”. On the positive side, he pointed out that de-globalisation in the form of populism and protectionist sentiment is

not a global phenomenon, being largely confined to the United States and parts of the EU. Most emerging market economies, including large ones such as China, India and other Asian economies, Brazil and Argentina, are in fact moving in the opposite direction.

Some developed economies such as Australia, New Zealand, Canada and Japan have also not succumbed to populism. What is notable, said Dr Buiter, is that all four have low levels of income inequality and score high on inter-generational mobility. These four nations were also relatively unscathed by the global financial crisis.

The Asian Monetary Policy Forum, which was held at the Shangri-La hotel, was co-organised and funded by the University of Chicago Booth School of Business, the National University of Singapore Business School and the Monetary Authority of Singapore.