



Roubini's Worry List

So far this year, the investment markets have held up pretty well, which doesn't always happen after a year of big returns like we experienced in 2013. But based on experience, it seems likely that something will spook investors during the year.

Professional investors have learned to create a mental "watch list" of possible market-shaking events, and they were helped recently when Noriel Roubini, chairman of Roubini Global Economics, former Senior Economist for International Affairs at the U.S. Council of Economic Advisors, compiled his own worry list. Roubini said that we're past the time when people should be fearful of a breakup of the Eurozone, or (for now) any Congressional tinkering with the debt ceiling. The public debt crisis in Japan seems to be fading in the optimism of Japanese Prime Minister Shinzo Abe's monetary easing and fiscal expansion, and the war between Israel and Iran over Iranian nuclear technology, once thought to be imminent, now appears to be on the back burner.

So what does today's worry list look like? Roubini starts off with China, which is trying to shift its growth away from exports toward private consumption. Chinese leaders, he says, tend to panic whenever China's economic growth slows toward 7% a year, at which time they throw more money at capital investment and infrastructure, creating more bad assets, a lot of industrial capacity that nobody can use, and a bunch of commercial and industrial buildings which sit empty along the skyline. Eventually, something will have to be done about the growing debt at the same time that investors face a potential crash in inflated real estate prices. Think: five or six 2008 real estate crises piled on top of each other, all of it happening in one country.

Numbers two and three on Roubini's worry list involve the U.S. Federal Reserve, which could (worry #2) cease its massive purchases of real estate mortgages and government bonds too quickly, causing interest rates to rise and sending financial shockwaves around the world. Or, on the other hand (worry #3) the Fed might keep rates low for so long that the U.S. experiences new bubbles in real estate, stocks and credit--and then experiences the consequences when the bubbles burst.

Roubini also worries about emerging market nations being able to manage their debt and capital inflows if interest rates go up, and of course the situation in the Ukraine has significant market-spooking potential. Finally, he notes that China has significant unresolved territorial disputes with Japan, Vietnam and the Philippines, which could escalate into military conflict. If the U.S. were drawn into a maritime confrontation, alongside Japan, with Chinese warships, investors might think it's a good time to retreat to the sidelines.

None of these scenarios are guaranteed to happen, and some of them seem unlikely. But these periodic, headline-related spooking comes with the investment territory. If and when one of these events grabs the global headlines, it might be helpful to remember that the stock markets have weathered worse and come out ahead. Think: World War II, a presidential assassination, two wars in the Middle East, 9/11 and a Wall Street-created global economic meltdown. If we can survive and even profit, long-term, from a stay-the-course investment mentality through those events, then we might be able to weather the next big headline on (or off) the worry list.