

## CFA Trending Topics | March 19, 2018

### Corporate debt to GDP near all time highs...is it a reason to worry?

Despite a rosy economic backdrop, several measures of domestic corporate leverage are at their highest in the modern era, such as non-financial business debt-to-US-GDP rising above 73%, its highest level since the pre-1980 timeframe. We note:

- Rising interest rates coupled with new interest deductibility limitations could exacerbate downturns.
- S&P recently published a report warning of high debt levels in a rising interest rate environment.
- However, Moody's appears more optimistic in contrast, citing strong economic growth and shrinking number of low quality high-yield companies.
- Debt is also not as industry-concentrated as pre-2008, and more fixed-rate debt has been locked in at low rates.

#### Key Takeaways

- While increased cash flows post tax reform can support further increases in leverage, management teams should stress test counterparty credit risk.
  - Downsides could be exacerbated by rising rates, limited interest deductibility, and contagion.
- Recession risk models are sensitive to market dynamics such as growth and borrowing rates, and may not fully incorporate potential heightened downside risk

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