Forbes Magazine's Portfolio Strategy columnist and Fisher Investments chief executive Ken Fisher argues that, as long as the return on assets markedly exceeds borrowing costs, debt will contribute to an increase in gross domestic product

Why debt is good for growth

The Western World is massively under-indebted when everyone thinks just the reverse. That's bullish. Last month I briefly mentioned this while citing statistics showing that increased budget deficits in the US and Britain lead to higher stock returns in historically significant ways. More interesting is that no one – simply no one – stops to ask the basic question: "What's the right amount of debt for our society to have?"

Instead, everyone assumes more debt is worse and less debt is better. It derives from 3,000 years of evolving cultural and moral values assuming debt is bad. In finance, however, there must be a right amount of debt and if we have less than that we're under-indebted and benefit when our indebtedness increases. That's basically why big budget deficits in history are followed by improving markets and surpluses by bad markets – the deficits are moving us closer to where we should have been all along.

Most debt bears fixate on the US. Any way you figure it, its total net assets, of all types, are something shy of $100 trillion (£52 trillion). Total debt is $45 trillion. Debt to equity is about one to one. General Motors' debt to equity is 10 to one. Gross domestic product is $12 trillion. So, the return on assets exceeds 12% while average net borrowing costs are below 5%.

As long as the return on assets markedly exceeds borrowing costs, society benefits if folks borrow more to get assets that increase gross domestic product. You may scoff – arguing that much borrowing isn't aimed at that, but instead consumption? Less so than you think. Consumer loans and federal debt total less than 15% of the US's total debt.

The biggest chunk, rather obviously, is banking system debt. But even when the government borrows and does so stupidly, which is more often than not, it can only spend the money by avalanching it on individuals and corporations who the next time around spend the same money relatively normally.

The average person spends their money averagely. Anyone can walk into a bank, detail their financial circumstances and have the bank detail what they will or won't lend you. It's a very mature catechism and, generally, it ends up with an amount whose net annual interest and principal repayments total about 50% of annual income.

The US exists today at about 10% of those levels even though it must be a safer bet than any single borrower. We need more debt. Next month I'll detail why current account and trade deficits aren't a problem but a benefit. Meanwhile, buy stocks such as the following.

Virtually unknown, the US's **Jakks Pacific** is the hottest new toy firm, thriving where others shrivel. Because the sector is cold, Jakks sells at only 10 times my estimate of 2005 earnings. Its speciality is reintroducing forgotten classics to a new generation of kids. But it also sports hot new classics such as Sponge Bob Square Pants and its new TV Games is a blockbuster technology twist injecting a vast mass of classic games into your TV. The stock also suffers from implied scandal from a pending lawsuit. To me this is opportunity, not risk.

Chevy Chase's unforgettable movie character, Fletch, once famously said, "It's all ball bearings these days". Well, as the global economy picks up so will ball bearings and you can own the world's clear leader at 11 times 2005 earnings in the shape of Sweden's **SKF AB**. Operating in 70 countries with a widely diversified customer base it's also the industry innovator and gains market share by both organic growth and acquisition. It's cheap.

France's **Thomson** is ideally postured to capitalise on the broadband access revolution ahead through its 41,000 patents and daunting global position in technologies and services for the media and entertainment industries. Yet it is priced like a consumer electronics play at 50% of annual revenue and 13 times 2005 earnings. When it receives technology valuations, you will have made good money.

Sounds similar but, here in Britain, **Tomkins** seems boring with a wide area of engineered industrial and construction products. But it isn't – which is why it is cheap at half of book value and 13 times earnings. Like SKF, it grows through new industrial technology and acquisition. The market fears rising commodity prices will tank it, but I think that's already priced into the stock with better times ahead. Take a look.

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