



When Will The Next Global Financial Crisis Strike?

Description

It is almost a decade since the global financial crisis commenced. It created chaos for the world economy and, for a time at least, a full-scale financial meltdown seemed to be a very real possibility. Although this was avoided, a wide range of industries and companies have not yet fully recovered from the crisis. Banking stocks, for example, are still struggling in some regions, while some companies have ceased trading altogether due to the financial pressure they experienced during the recession.

Looking ahead, another economic crisis seems inevitable. After all, the world economy moves in cycles and, according to history, the current uptrend will not last forever. In fact, the current monetary policies being adopted across the globe could be the cause of the next crisis.

Policy issues

Of course, the near-zero interest rates and quantitative easing policies which have been pursued by a range of major economies in recent years were completely understandable given the challenges faced during the financial crisis. A period of global deflation was successfully avoided, while lending by banks continued to a higher extent than it otherwise would have. This helped to improve economic activity levels and generate improved GDP growth. Undoubtedly, the financial crisis was shorter and less harmful because of the loose monetary policies which were pursued.

However, those policies could now be sowing the seeds of the next financial crisis. The world economy has delivered relatively impressive growth for a number of years, and yet interest rates in the US and Europe, for example, are still near-zero. While this has created improved economic conditions for businesses and individuals, it has also created significant asset price growth. In fact, it may even be described as a bubble, since in many cases it is now difficult to justify current valuations.

Furthermore, a loose monetary policy which is in place for too long can also cause inflation to rise. While this has not occurred yet, plans for a loose fiscal policy in the US under President Trump may cause the price level to increase at a faster pace across the globe.

The trigger

Clearly, pinpointing a trigger to set off the next financial crisis is challenging. However, a rising interest rate could be the catalyst to cause a downturn in global economic activity. Many investors seem to have priced in a period of continued low interest rates. Therefore, they may become much more risk-averse if interest rates are forced higher by an inflation rate which is significantly above the current level.

When this will occur is clearly difficult to judge, but since it is nearly a decade since the start of the last crisis it seems likely to commence in the medium term. As ever, seeking out companies with wide margins of safety and diversifying among different industries and regions could be a sound move for Foolish investors.

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