# Another financial crisis is certain. The only question is when and how

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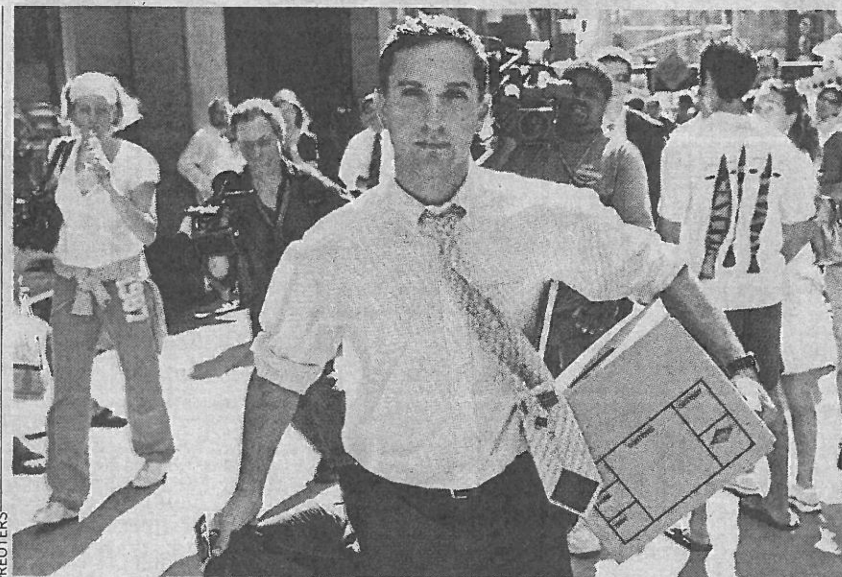
In introducing the annual Michel Camdessus Lecture this week, Christine Lagarde, managing director of the International Monetary Fund, insisted that a number of important goals had been achieved since the financial crisis nearly ten years ago. "The crisis was overcome; a deflationary spiral avoided; and – at long last – a broad-based global recovery is under way. A hat trick of sorts".

Quite so. But have the lessons been learnt? Some, perhaps. For one, the banking system has been made safer, at least in Western economies. Yet whereas an exact repeat of the last crisis now seems quite unlikely, it would be most unwise to assume that we've at last got the measure of these events. In responding to them, there is a sense in which we are always doomed to fighting the last war. All financial crises admittedly have common elements, yet each will inevitably be significantly different from the last one. Like flowing water, finance finds a way around whatever obstructions may be put in place, and creating new hazards.

Today we have a relatively good understanding of the immediate causes of the 2008-09 crisis; steps have been taken to shore up the system against a replay. But as likely as not, we've repeated the mistakes of the Maginot Line; we've built the fortifications to protect ourselves from a past threat. Next time, the nemesis will come from a different direction.

A new analysis by the markets team at Deutsche Bank finds that far from getting better at preventing and managing financial crises, we've actually got a great deal worse; since the breakdown of the Bretton Woods fixed exchange rate regime in 1973, these events have become a lot more frequent than they were before. Here's a list of some of the most high profile ones – the UK secondary banking crisis (1975); the two oil price shocks of the 1970s; the UK fiscal crisis of 1976, culminating in an IMF bail-out; numerous emerging market defaults (mid-1980s); mass failures in the US savings and loans sector (late 1980s/early 1990s); various Nordic financial crises (late 1980s); the bursting of the Japanese stock and property bubbles (1990); various emerging market shocks/devaluations (1992); the Mexican tequila crisis (1994); the Asian crisis (1997); the Russian and LTCM crisis (1998); the dot.com crash (2000). Nor did it end with the Global Financial Crisis of 2008-09. This was quickly followed by the eurozone sovereign debt and banking crises.



REUTERS

A Lehman Brothers worker leaving his building in New York in the heat of the financial crisis that took hold in 2008. The crisis is only one of a long list in modern times

It is almost as if financial crisis is now the world's more natural state. The present condition of apparent calm may instead be the aberration. The Deutsche analysis takes a quite old-fashioned view of the underlying causes of this rising tide of financial instability.

Burgeoning budget deficits, ballooning debts, unbridled credit creation, ultra loose monetary policy, financial deregulation, the build-up of global imbalances – all these things have been on the rise, the analysis argues, since the final break with the gold standard in the early 1970s and its replacement by a fiat currency world. For Deutsche, the coincidence is impossible to ignore. Since nothing has been done about the underlying money system, the analysis concludes, we can only expect more of the same.

There may be some truth in this assertion, yet there is also an even greater cause, overarching, as it were, the ill discipline of the modern currency system. This, in all its various forms, is globalisation. I don't mean by this simply the free movement of capital across borders, a phenomenon that has come to act like a lightning rod, such that trouble in one market quickly spreads to other economies. Rather, I mean the wider, disinflationary effects. Explosive growth in international trade and migration has had many positive consequences, raising millions in the developing world out of poverty, but has also caused downward pressure on wages and prices in advanced economies, driving interest rates to record lows in the process. Growth in credit has become a lazy substitute for growth in wages.

Each successive financial crisis, has, moreover, been met with more of the same – ever greater levels of policy stimulus. The excess is thereby never properly purged. "By continually using stimulus to deal with crises and not letting creative destruction take over," observes Deutsche, "subsequent crises become more likely by passing the problem along to some other part of the global financial system, and usually in bigger size".

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Persistent central bank money printing since the financial crisis has puffed up asset prices to dangerously high levels, thereby almost certainly sowing the seeds for the next crisis. So hooked on the steroids have markets become, that merely stopping them, let alone unwinding them and returning monetary conditions to "normal", might trigger a panic.

It's impossible to know what form Britain's next financial crisis might take, or its timing. But here is one scenario.

Mark Carney, Governor of the Bank of England, this week referred to Brexit as an example of "de-globalisation". He acknowledged that many supporters of Brexit do not think of it as such, but as an opportunity to enhance trade with the rest of the world. Yet before those supposed benefits kick in, there is bound to be some diminution of trade with the EU. If globalisation is disinflationary because of the impact of global competition, it follows that Brexit will temporarily at least be inflationary, in that disengaging from the EU will reduce some of these disinflationary forces. For a while, Britain will become a somewhat more closed economy. This way of thinking has helped persuade key Bank of England policymakers that some increase in interest rates may now be necessary.

In itself, the sort of Brexit-inspired deglobalisation Carney talks of would be very unlikely to trigger a financial crisis. But mix it in with the hard left policies of Jeremy Corbyn's Labour, and all the ingredients for a catastrophic loss of international confidence in the UK economy would be in place. Brexit and Corbyn together would be a peculiarly toxic combination. Fully blown balance of payments and fiscal crises, requiring recession inducing rises in interest rates, would not be long in coming.

All Labour governments are eventually destroyed by fiscal and financial crisis. With Mr Corbyn, it would at least be swift.