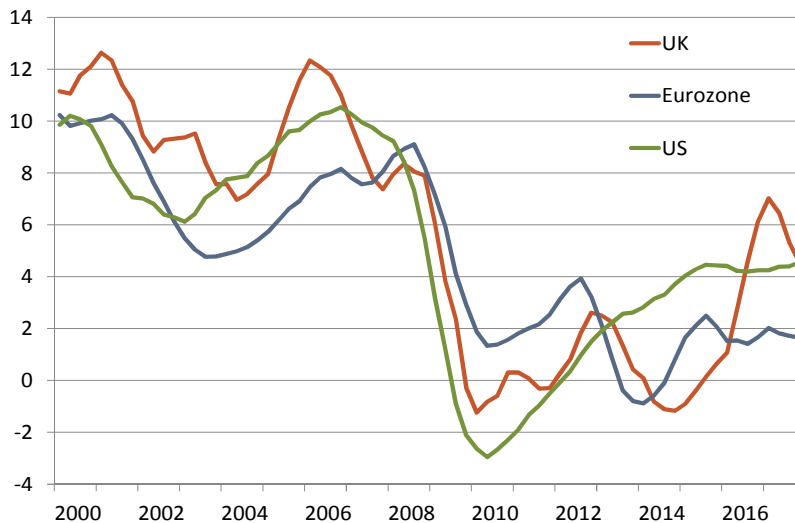


14 September 2018

10 years after Lehman – can it happen again?

The big credit excesses are over for now: credit to private sector, yoy change in %



Credit to the non-financial private sector, including debt securities, quarterly data, eurozone 2015 adjusted for one-off surge due to a re-classification of some debt. Sources: BIS, Haver Analytics

- **From exuberance to despair:** 10 years ago, Lehman triggered the worst recession in the western world since the 1930s. Can it happen again? As usual, the economist's reply has to be "yes and no". Yes, bouts of euphoria followed by overdone despair are part of human nature. Excesses and the subsequent painful cleansing will happen again. But no, a replay of the post-Lehman mega-crisis looks unlikely in the western world for the time being.
- **Less tinder today:** The bursting of credit bubbles in the US and, far less importantly for the world, in the UK, Spain and Ireland had been the root cause of the 2008/09 crisis. In the subsequent recovery, credit growth has remained much more moderate (see chart). In an upturn marked by unusual caution, we do not yet find excesses in credit, inflation or investment that look serious enough to take down the global economy if they should correct.
- **Lessons learned:** Banks have bigger buffers, and policymakers are watching financial stability risk and contagion hazards more diligently. They have established procedures for winding down stricken banks in an orderly way instead of triggering contagion by simply closing them Lehman-style. See "[10 lessons from the financial crisis](#)".
- **Anglo debt migration:** Following their pre-Lehman credit excesses, the US and the UK needed much more deleveraging than the eurozone. Over the last 10 years, households reduced their debt by 21ppt from 99% to 78% of GDP in the US and by 10ppt from 101% to 91% of GDP in the UK. The debt of financial institutions has fallen even more significantly by 38ppt in the UK (from 223% to 185%) and the US (from 120% to 82% of GDP). Policymakers have facilitated the process by allowing a large rise in public debt by 46ppt in the UK (from 42% to 88% of GDP) and by 43% in the US (from 65% in 2007 to 108% of GDP in 2017), well ahead of the rise by 22ppt to 87% in the eurozone.
- **Public debt is a long-term problem:** The rise in public debt will have to be reined in with painful policy choices in the future. But as Japan shows, for largely healthy economies with responsible central banks, the public debt ratios reached in the US, the UK and the eurozone are not the stuff for debt crises. Weak Italy might be different, though.
- **Volatile markets, resilient economies:** Finance has changed in many ways. Many brokers take less risk onto their own books, investors use more exchange traded funds, algorithm-driven trading is on the rise. That can sometimes add to market volatility. But with more stable finance, the potential impact on the real economy now looks smaller.
- **Excesses elsewhere – but they are less dangerous:** To some extent, leverage has migrated to shadow banking systems and emerging markets. But potential problems there are less likely to cause a dangerous crunch in bank credit in the developed world. China can still cope with its debt due to its high savings rate. Some other emerging markets are in trouble. Fortunately, they are simply not big enough to cause a big new global crisis.

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