PROJECT SYNDICATE – 27 NOVEMBRE 2025

Will 2026 Bring Financial Crisis?

Over the last year, US President Donald Trump's economic policies – including a fiscal blowout, the demolition of the international trading system, threats to the Federal Reserve's independence, and erosion of the country's long-term innovation capacity – have been triggering alarm bells in the United States and globally. Add to that a frothy AI sector, the normalization of crypto, proliferating climate-related disasters, and growing public-debt burdens, and the global economy appears beset with risk.

In this Big Question, we ask ***Anat R. Admati****,* ***Hilary J. Alle****n,* ***Jayati Ghosh****,* ***Simon Johnson****,* ***Corey Klemmer****, and* ***Erin Lockwood*** *whether a major crisis is imminent, and how economies can mitigate the fallout.*

Anat R. Admati

An opaque system fraught with exploitation, excessive risk-taking, bad policies, empty promises, and outright lies is prone to major crises – especially when the deceptions and policy failures are finally exposed. Whether or not such a crisis is imminent, the system's distortions cause enormous harm, which affects us every day. Overall, the economy is moving in a deeply troubling direction.

Consider the financial system. After the 2008 global financial crisis (GFC), leaders across Western democracies promised regulatory reform and the end of taxpayer-funded bailouts. But little has changed. Not only does financial regulation remain weak, but risks have grown, with poorly supervised "financial innovations" making the system increasingly distorted and fragile. The fundamental sources of this fragility remain the same: opacity and excessive borrowing across the system, from traditional banking to private credit, private-equity markets, crypto, and stablecoins.

At the same time, longstanding anti-fraud and anti-corruption laws are not being enforced, essential banking rules have been weakened (against the views of

some former regulators and academics), and the growth of "legitimized" cryptocurrencies is raising alarms. Proceeds of crime and corruption now flow into the legitimate system, and trillions in obligations may ultimately be paid by governments and central banks under the guise of preventing a "systemic crisis." The beneficiaries of this situation are – and will be – criminals and others who have made false promises and placed reckless bets, while the rest of society will be left to absorb the losses and suffering the consequences.

Markets cannot function without trustworthy governments and effective legal systems. The greatest risks we now face stem not only from financial excesses but also from the abuse of political and economic power – and from the erosion of the institutions meant to hold powerholders to account. Even truth itself has lost its power, leaving societies increasingly vulnerable.

Hilary J. Allen

Our financial system is beset with vulnerabilities. Leverage in many parts of the non-bank financial system is at historically high levels. Ponzi-like crypto assets, which are not backed by any productive capacity, have been folded into traditional financial markets. Investing in the stock market increasingly means betting on generative-AI tools, with their intractable accuracy problems and limited demonstrable productivity gains (despite the AI industry heavily subsidizing their use). A new wave of automation, growing dependence on shared infrastructure like cloud computing, and vulnerability to major weather events and cyberattacks also create new operational risks. In short, the global financial system is a tinderbox, and any number of events could spark a conflagration.1

The US is particularly poorly positioned to deal with a financial meltdown. The best way to build resilience in the financial system is to reduce leverage and enlist highly skilled regulators to monitor emerging risks. The US is moving in the wrong direction on both fronts, loosening existing limits on leverage and slashing the number of financial regulators and supervisors.

After a meltdown starts, the damage is typically mitigated with bailouts and interest-rate cuts. As the 2008 GFC amply demonstrated, this is never a complete solution. But

it is likely to prove particularly inadequate today. Rate reductions will be limited by inflationary pressures – partly a result of Trump's trade policies. And the Trump administration may well reserve bailouts and similar emergency measures for its preferred institutions and markets, rather than extending them to those that are most crucial to financial stability. Widening budget deficits, attacks on the Fed's independence, and a general disregard for expertise may also undermine the credibility and effectiveness of any steps taken to address a panic.

Jayati Ghosh

The preconditions for a major financial crisis in the US are all in place. Financial assets are massively overvalued, based on highly leveraged AI and cryptocurrency investments, and, as was true of the run-up to the GFC, much of this leverage comes from non-bank financial institutions or shadow banks, which are subject to far fewer regulations than banks. Moreover, advanced-economy central banks are overextended, having propped up finance capital for nearly two decades. And trade uncertainties are constraining real investment, while rising inequality is reducing household demand.

In such a febrile environment, any disruption – any unwelcome news, climate shock, or shift in investor perceptions – can trigger herd behavior that leads to a bigger crisis. The question is not if, but when.

Developing countries have learned that, under such circumstances, global capital flees to "safety" – even the increasingly questionable safety of US dollar assets – generating currency devaluations and secondary crises in our economies. In the 1970s, renowned economist Charles Kindleberger pointed out that global crises occur when there is no leader willing and able to deliver liquidity to economies that need it, support countercyclical lending, and provide markets for distressed exporters. Given that this is the case today, financial instability in the US could well lead to a global downturn.

Developing economies can and should act now to strengthen their resilience and ensure that they do not bear the brunt of any future downturn. This includes efforts to develop domestic markets and generate domestic revenues, prepare

countercyclical policies, and cultivate alternative trade partnerships. Crucially, developing-economy governments must adopt financial rules aimed at reducing the sector's fragility, including limiting or banning opaque private cryptocurrencies, developing central bank digital currencies, regulating shadow banking, and, above all, restricting volatile cross-border capital flows.

Developing economies cannot control what happens in the US. But they can and must avoid their own past mistakes.

Simon Johnson and Corey Klemmer

A dark shadow stalks the land: private credit. Precise definitions and numbers vary depending on whom you ask, but the general impression is that private investment funds, exempt from both the rules of bank supervision and the disclosures of publicly listed companies, could now (or soon) pose a threat to financial stability.

There is nothing inherently wrong with credit expanding to support economic growth. In fact, one of the Fed's goals, according to the 1913 Act that created it, is "to furnish an elastic currency" (an old-fashioned expression for a perfectly modern idea). And private credit funds promise high returns – and often show them on paper. During good times, that is enough for investors, who do not bother too much with the details, reasoning that a rising tide lifts all boats. It's only when sentiment turns more cautious that everyone looks for "who has been swimming naked."

We are not there yet, but when that moment comes, three pointed questions about private credit will stand out. First, in what condition are the funds that took the most extreme risks? How much did they lend (relative to borrowers' equity) and how much did they borrow (relative to their own equity)? Second, are the credit ratings of these private credit funds (and their assets) appropriate in a stressed scenario? Third, and most important, would the failure of any private credit fund impose significant losses on one or more banks at the financial system's core?

After the 2008 GFC, legislation and regulation succeeded in pushing risk away from the insured banking sector, toward capital markets. But big banks still wanted a piece of the action, so they worked their way back in through their exposure to private funds. The consequences of that exposure remain to be seen.

Erin Lockwood

Having studied the GFC, and the role that inadequate risk models and minimal regulation played in fueling it, I am increasingly concerned about financial risk. While a crisis may not be imminent, the ingredients are certainly there.

At the heart of the 2008 crisis were highly correlated defaults that far exceeded risk models' projections for maximum losses. These upended investment strategies, triggered credit-derivatives payments, forced margin calls, and left highly leveraged firms without the liquidity to make good on their debts. Regulators had left it up to financial institutions to measure their own risks and allocate capital buffers accordingly. As a result, those institutions failed, triggering a crisis that spilled over into the real economy.

The AI industry – which accounts for a rapidly growing share of the US and global economy – exhibits some of these same features. Asset-price movements and downside risks are probably highly correlated within a dense network of investments, many of them circular. For example, Nvidia recently invested $100 billion in OpenAI, to fund the company's investments in Oracle data centers, which are powered by Nvidia graphics processing units (GPUs). This kind of equity investment in one's own customers drives valuations higher, while creating interlocking liabilities and concentrating risk. The correlation of downside risks is further exacerbated by the relative lack of differentiation among AI service providers.

Given the astronomical mismatch between AI firms' revenues and the projected costs of computing power, the industry depends on huge amounts of securitized debt and derivatives to hedge the debt's default risk. The pricing of these contracts depends on the accurate measurement of risk and the appropriate allocation of capital to weather market downturns. But while post-2008 regulation tied capital requirements to standardized measures of risk among regulated financial institutions, much of the credit flowing into the AI industry is funneled through unregulated lending vehicles designed to keep debt off firms' balance sheets. Are these shadow banks accurately pricing the risks associated with an AI bubble collapse and holding adequate capital reserves? There is little way to know.

Given the circular investments rampant in the AI industry, if the bubble bursts, and creditors prove not to be adequately capitalized, there is a very real risk of systemic contagion. While bankruptcies among a handful of highly leveraged special purpose vehicles would not necessarily spell financial collapse, tight ties (to the tune of $1 trillion) between the shadow banking sector and conventional investment banks raises the possibility of spillovers.

Economies' ability to navigate the fallout of a crisis will depend on four factors. The first is the size of the AI sector: economies with large AI sectors (as a share of the economy) will fare worse than those that are less exposed to the industry.

The second factor is the strength of banking regulation. Strong resolution and recovery regimes, in particular, are crucial to prevent the contagion from spreading beyond the AI sector and to limit dynamics that would fuel a broader systemic crisis.

The third factor is the state's approach to bailing out the AI sector. While governments in countries with large AI sectors might be tempted to funnel public money into ailing AI firms, this will generate substantial political and macroeconomic costs.

The final factor is the distribution of wealth and income. In the US, the economic gains from the AI boom have been concentrated at the top of the US income distribution. But robust recovery will depend on the state's use of fiscal and monetary policy to shape a more equitable society.