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Real Money: Dollar will be cause of next financial crisis

By Rob Rikoon | For The New Mexican

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As most everyone is aware, the U.S. has been running on borrowed money for some time. Thanks to increased output from nations such as China, India and Brazil, we have been able to borrow cheaply and pay back our loans with our own currency, which is fairly easy to print. This situation will not last long. The change will come without much warning and the first hints of a vast restructuring of international trade can now be seen.

Even though U.S. consumers are saving for the first time in 20 years, we have twice as much debt per person now as we did in 1989, much of which is based on real estate values. The government's ongoing and expanding binge will push our national debt past the point of being sustainable by 2015. Falling tax revenue, the rescue of financially strapped municipalities and states, health care reform and an aging population will undermine hopes that we can grow our way out of the predicament.

With interest rates near zero, investors and taxpayers are being punished alike. As executives at big investment banks congratulate themselves on their handsome bonuses, ill begotten at the least, investors are left to protect themselves. The best strategy I know for most people is to look at high-quality corporate or municipal bonds maturing in five years or less. By investing in individual bonds that mature with regular frequency, investors can get some relief from the twin vise of low returns and higher taxes and be poised to adjust to an environment where interest rates spin out of the Federal Reserve Bank's control.

The stock market rally we are experiencing is primarily due to massive amounts of money being pumped into the financial system that has no other place to go. Longer term, only companies that are well diversified outside of the U.S. currency stand much chance of successfully dealing with the commodity-based inflation sure to come as the world's population grows and becomes more affluent, at least in some parts of the world.

Though price inflation will stay muted for some time due to the global recession, when it returns, precious metals and energy will once again be safe harbors. The U.S. dollar is the ground on which the next international financial crisis will be worked out. The Chinese, Brazilians, many Arab countries and other skeptical nations hold lots of U.S. dollars now but they are looking to get out without causing a panic.

A declining dollar hurts American consumers, but in such a way that there is no one to blame. It is an inconvenient truth that we as U.S. citizens are constrained by our own government in ways that make it difficult to diversify outside the dollar. You may want to consider investigating how you can diversify your holdings outside of U.S. currency-based investments, either through foreign stocks and bonds, commodity vehicles and energy holdings.

Don't wait too long to do your homework.

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