Currency and Banking Crises in Emerging Markets (IBUS 6290), Winter 2013
Thursdays 16:30-19:00 Duques 256

Instructor: Prof. D. Leipziger (DLeipzig@gwu.edu)
Duques 450b 202-994-8202
TA: Matt Prizinsky (MPrizinsky@gwu.edu)

Class Objectives: A financial crisis can be extraordinarily damaging to a country’s economic growth, public finances, and international credibility. Given the high costs of a crisis, one would imagine that policymakers would take the utmost care to avoid them. Unfortunately this is not always the case and some crises are clearly avoidable. That said, a particular set of circumstances, domestically or globally, can trigger a currency or banking crisis, and in that event, policymakers need to utilize available tools and best practice to manage the crisis, shorten rather than lengthen its duration, and attempt to limit the spillover costs that can damage the pace of recovery. This course will examine what causes a financial crisis and how various countries have responded to their specific crises. Cases will include Argentina, Mexico, Korea, and Greece. Readings will accompany cases and selected guest lecturers may be invited for particular cases where they were involved in the management of the crisis.

Learning Objectives:

• To better understand the causes and impacts of financial crises on emerging market economies and the economic agents operating in these markets
• To drill down on the economic implication of crises and the alternative ways of dealing with specific shocks to the financial sector
• To examine specific country cases and ascertain how governments dealt with their crises and to assess the effectiveness of those measures in a public policy sense
• To gain basic lessons from financial crises and improved understanding of the measures being proposed to limit their frequency and associated contagion

Prerequisites:

Students taking the class should have had a solid macroeconomics course as part of their graduate course of study at GWU so that the analytic links between financial issues and macroeconomic fundamentals can be further developed.
Class Expectations:

Students should be conversant with the fundamentals of macroeconomics and the links between macro-economic management tools and the foreign exchange and money/bond markets. Towards this end, it would be wise to review your macro comprehension and consult either Mankiw and Ball or an equivalent macroeconomic text. Readings need to be completed before each class and the Instructor reserves the right to quiz students on selected reading assignments. There will be two short written assignments for the class, consisting of a three page Note on how a particular financial crisis could have been handled better and three page Note to your bank CEO alerting him/her to the potential warning signals of an impending financial crisis. You may reference a real country case or make one up. We will have a short in-class final exam concerning aspects learned during the class.

Course Materials:

Required and Recommended readings will be available via the class Blackboard webpage. Links for the HBS cases will also be provided via Blackboard. Students are not required to purchase a textbook for this class, however students will be expected to purchase and read four assigned HBS case studies (approximately $7 each).

Strong recommendation:

Read the FT every day and bring in relevant articles to be discussed in class.

Grading:

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<thead>
<tr>
<th>Assignment</th>
<th>Percentage</th>
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<tr>
<td>Note 1 (due Jan 31)</td>
<td>30%</td>
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<tr>
<td>Note 2 (due Feb 21)</td>
<td>30%</td>
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<tr>
<td>Final Exam (Mar 7)</td>
<td>40%</td>
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Class 1: INTRODUCTION: January 17, 2013

Required Readings:

Caprio, G and D. Klingebiel, “Bank Insolvency: Bad Luck, Bad Policy, or Bad Banking?” Annual World Bank Conference 1996


Recommended Readings:

Chapters 5, 18 and 19 or equivalent macro text covering exchange rates and capital flows, banking, and financial crises.


World Bank, *Global Development Finance* (2012), Overview Chapter

Topics for Discussion:

The basic facts of current global finance and causes of crises
The analytic links between financial markets and the macro-economy
The costs of financial crises in the short, medium and long term
The international financial architecture
What have we learned since Kindleberger?

Class 2: Financial Crises in High-Growth Regions: January 24, 2013

Required Readings:

HBS Case on East Asian Financial Crisis (Case 9-074-045)


Topics for Discussion:

The structure and financing of the Korean economy
The causes and consequences of the Korean financial crisis
The links between corporate restructuring and the Korean crisis
The management of contagion and the role of IFIs
Lessons from the workouts in Thailand, Korea, and Indonesia
The idiosyncratic policies of Malaysia
The Chiang-Mai Initiative
Class 3: Argentina’s Currency Board and Its Eventual Demise: January 31, 2013

Required Readings:


The 2000 Crisis in Argentina, HBS Case # 9-704-004

Recommended Readings:


Assignment # 1: Note on What Argentina Should Have Done Differently OR What Korea Could Have Done Differently (3 pages single spaced).

Topics for Discussion:

The benefits and costs of a currency board
What does a currency board imply for macro-policy?
Why did Argentina Fail?
The mechanics of the exit from the pegged exchange rate: winners and losers
Observations from the ground and legacy issues

Class 4: Exchange Crises and Financial Crises: February 7, 2013

Required Readings:


Mexico: The Tequila Crisis, HBS Case # 9-702-093
**Recommended Readings:**


International Monetary Fund, “The Effectiveness of Capital Controls and Prudential Policies in Managing Large Capital Inflows, *IMF Discussion Note* by Habermeier, Kokenyne and Baba, August, 2011

**Topics for Discussion:**

The Tequila Crisis and its Aftermath
How does contagion work?
What lessons are there for banks?
What lessons are there for central banks?
What lessons are there for policymakers?
What are the similarities with exchange crises elsewhere?

**GUEST SPEAKER:** **DR. FERNANDO MONTES-NEGRET, SENIOR ADVISOR, IMF AND FORMER DIRECTOR FOR FINANCIAL SECTOR, WORLD BANK AND LEAD FINANCIAL ADVISOR FOR THE WORLD BANK IN MEXICO**

**Class 5: The Current European Crisis: February 14, 2013**

**Required Readings:**


De Grauwe, Paul, “Crisis in the Eurozone and How to deal with it,” *CEPS Policy Brief* No. 204 (February, 2010)

**IMF paper on Greece** (to be distributed)
Topics for Discussion:

What lessons from emerging markets did the Europeans not internalize?  
How to manage a debt restructuring?  
What options faced Greece and its partners in 2009?  
What are the options today and what affects the fate of the Euro?  
What do we learn from the optimal currency area literature?  
What do we know about the fixed exchange rate literature and its implications?  
(POSSIBLE GUEST SPEAKER ON GREECE AND THE EURO)

CLASS 6: Predicting and Preventing Crises: February 21, 2013

Required Readings:

A redacted Financial Sector Assessment Program (FSAP) Report


Assignment # 2: A Brief of 3 pages (single-spaced) to your CEO outlining factors that could be associated with a higher probability of a financial crisis in selected countries in 2013-2014. What warning signs should he/she be alert to catching?

Topics for Discussion:

What is the role of an FSAP (Financial Sector Assessment program)?  
What factors are associated with financial crises?  
How did Canada manage to avoid the US financial crisis in 2009-2010?  
What contributes to prudent financial supervision: Chile vs. Spain  
The links between banks and financial crises: review the Glass-Steagall debate  
Taking a look at Glenn Hubbard (video)

GUEST SPEAKER: DR. AUGUSTO DE LA TORRE, CHIEF ECONOMIST, LATIN AMERICA AND CARIBBEAN REGION, WORLD BANK, FORMER CENTRAL BANK GOVERNOR, ECUADOR, AND AN FSAP TEAM LEADER

Required Readings:

Macro-Prudential Policy Tools and Frameworks: Progress Report to the G-20, Financial Stability Board (October, 2010)
Capital Controls in Chile in the 1990s, HBS Case # 9-705-031

Speech by Mark Carney, Governor of the Bank of Canada (to be distributed)

Topics for Discussion:

The changing roles of Central Banks, the IMF, World Bank, and the BIS
The Financial Stability Board
The Innocent Bystander Problem
Lessons for policymakers from Chile, Brazil, and Argentina
Unsolved issues of international coordination in crisis management

FINAL EXAM: MARCH 7, 2013