
The Aftermath of Global Financial Crises

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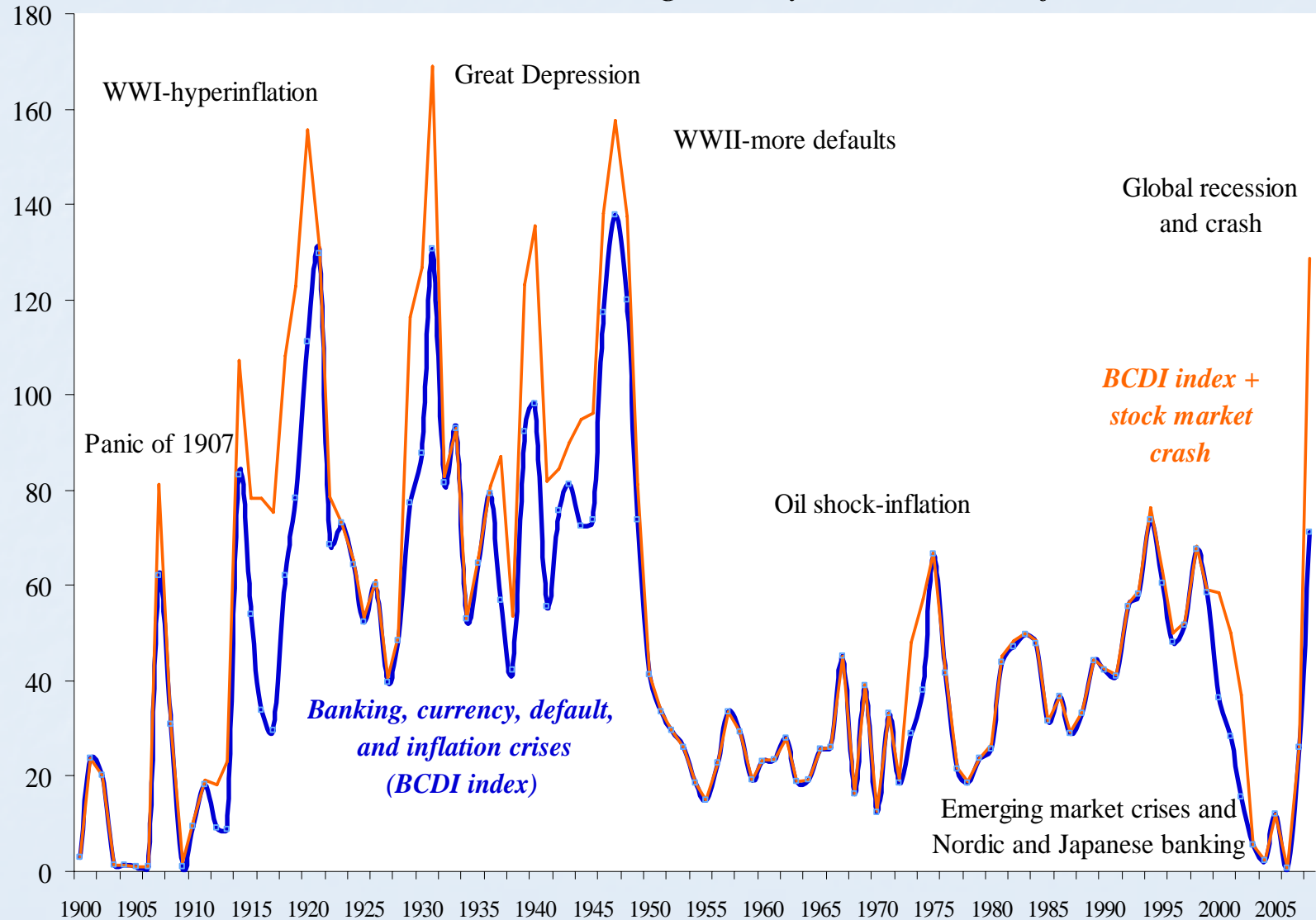
This talk is based on several works with Kenneth Rogoff:

- **“Banking Crises: An Equal Opportunity Menace”**
NBER Working Paper 14587, December 2008.
- **“The Aftermath of Financial Crises,”** *American Economic Review*, forthcoming, May 2009.
- ***This Time its Different: Eight Hundred Years of Financial Folly*** (Princeton University Press, 2009)

**Where are we at present
in a historical global
context?**

Varieties of crises: World aggregate, 1900-2008

A composite index of banking, currency, sovereign default and, inflation crises, and stock market crashes (weighted by their share of world income)



Reinhart and Rogoff

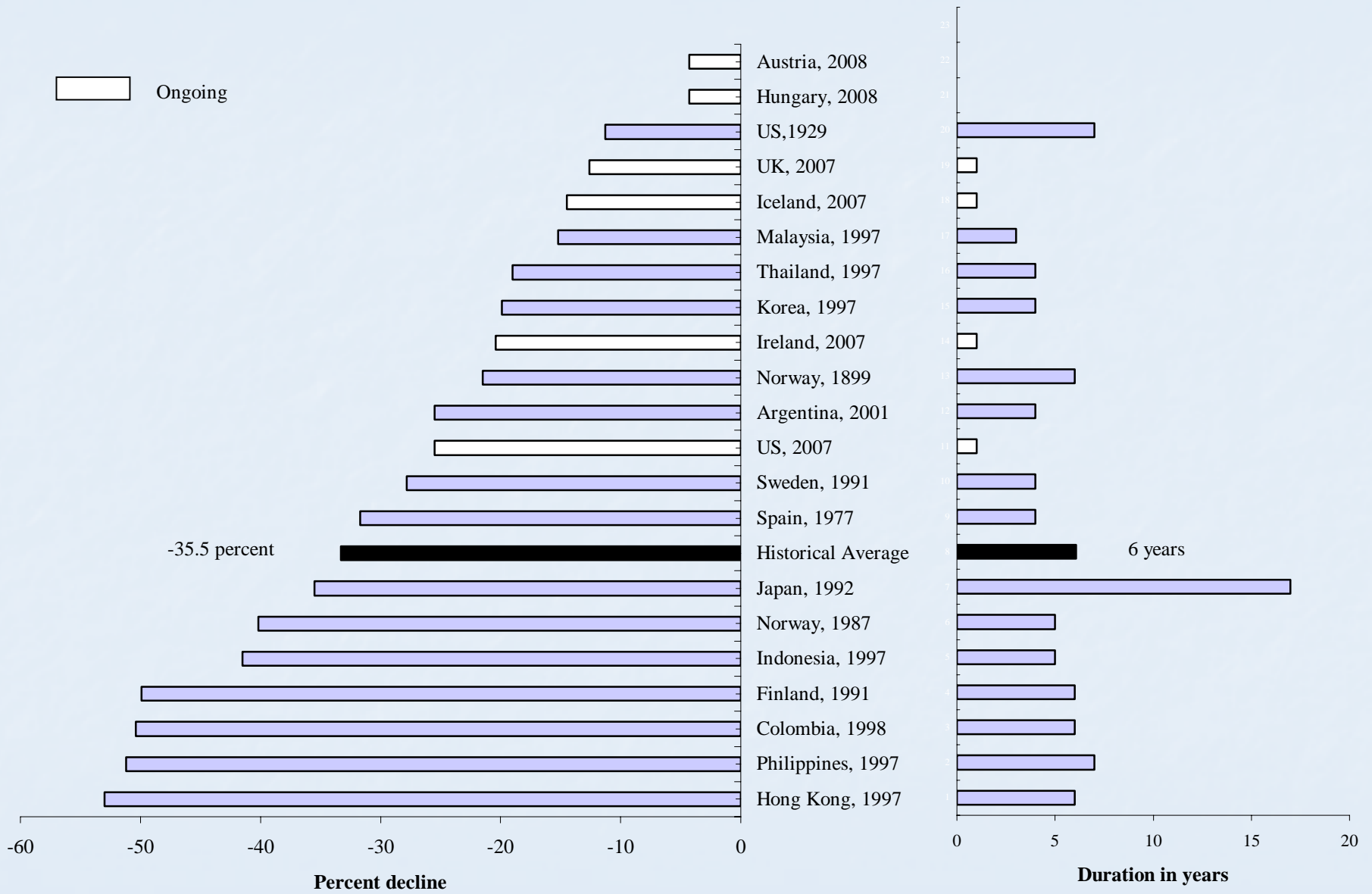
**The incidence and number
of banking crises is quite
similar in high and middle-to-low
income countries...**

**On the duration and depth of
the post-banking crisis crash for
selected indicators.**

**Financial crises are protracted
affairs...**

Past and Ongoing Real House Price Cycles and Banking Crises:

Peak-to-trough Price Declines (left panel) and Years Duration of Downturn (right panel)



Indices of total building activity in selected countries
(1929 = 100)

Country	Indicator	1932
South Africa	Buildings completed (value)	100
Argentina	Permits (area)	42
Australia	Permits (value)	23
Belgium	Permits (number)	93
Canada	Permits (value)	17
Chile	Permits (area)	56
Colombia	Buildings completed (area)	84
Czechoslovakia	Buildings completed (number)	88
Finland	Buildings completed (cubic space)	38
France	Permits (number)	81
Germany	Buildings completed (rooms)	36
Hungary	Buildings completed (number)	97
Netherlands	Buildings completed (dwellings)	87
New Zealand	Buildings completed (value)	22
Sweden	Buildings completed (rooms)	119
United Kingdom	Permits (value)	91
United States	Permits (value)	18
Average		64
Memorandum item:		
United States	Permits (number)	
September 2005 peak = 100		23 ¹

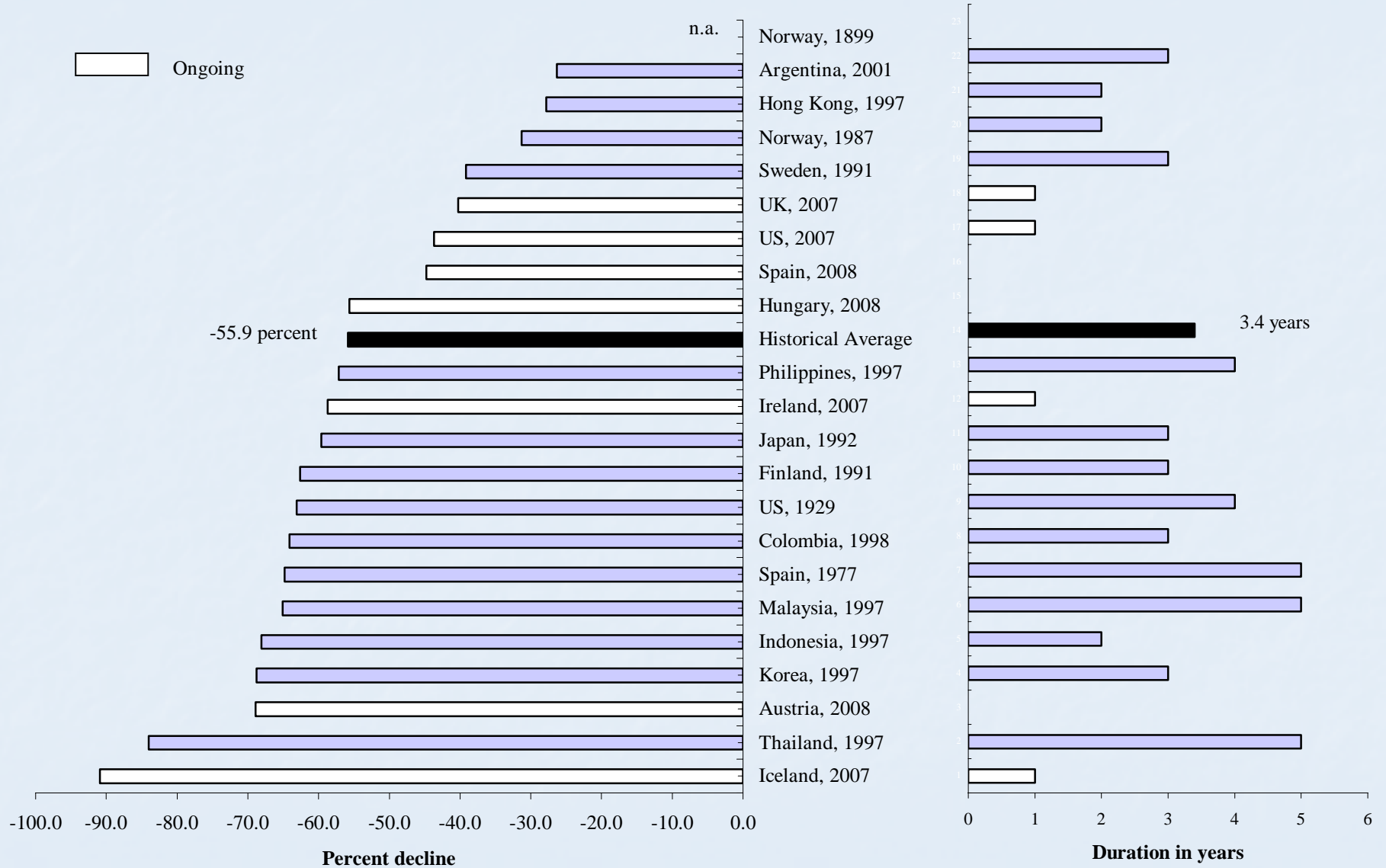
Sources: League of Nations, *World Economic Survey* (various issues), Historical Statistics of the United States (2003).

Notes: Note differences in the definition of the indicator cross-country.

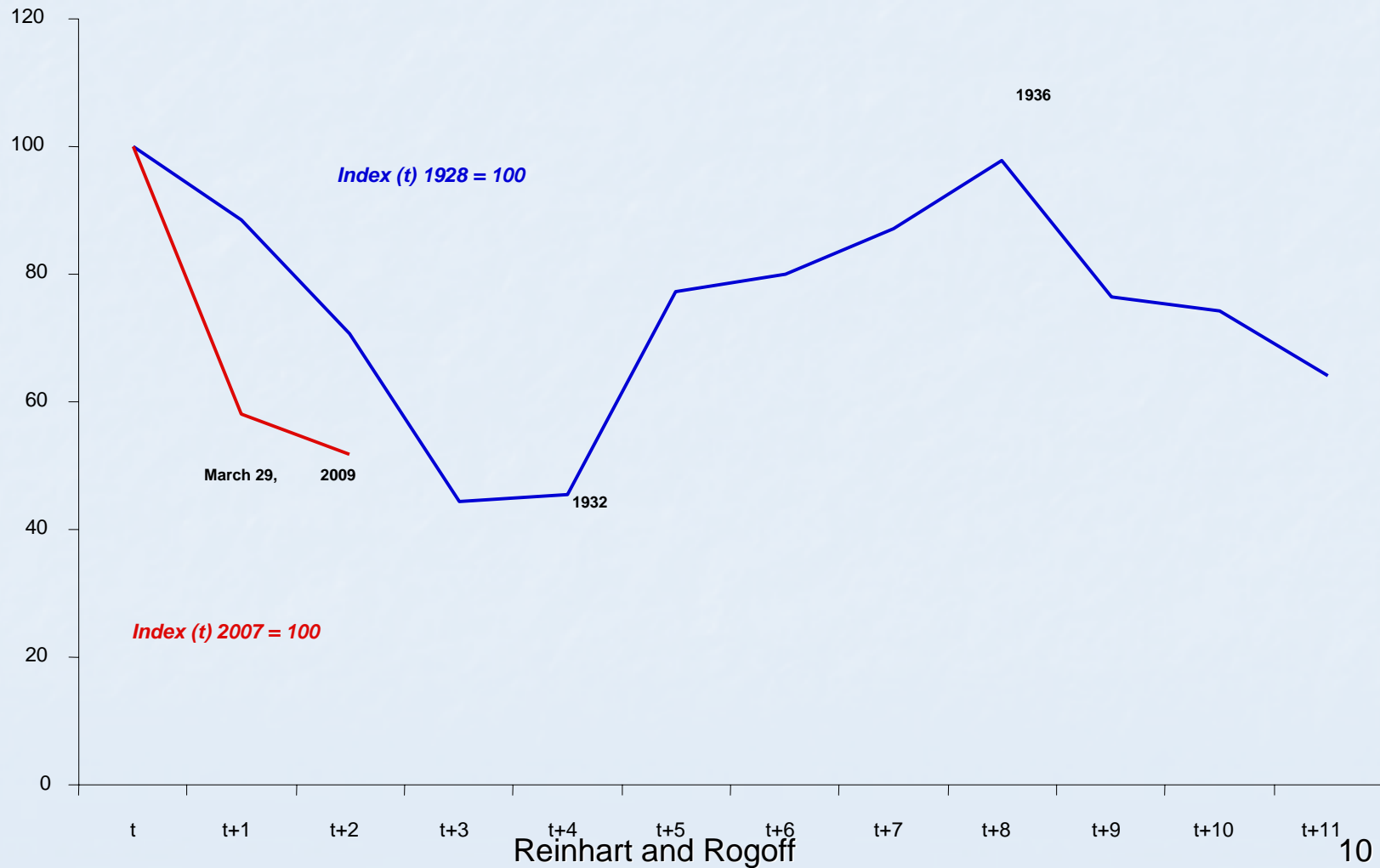
¹ Through March 2009.

Past and Ongoing Real Equity Price Cycles and Banking Crises:

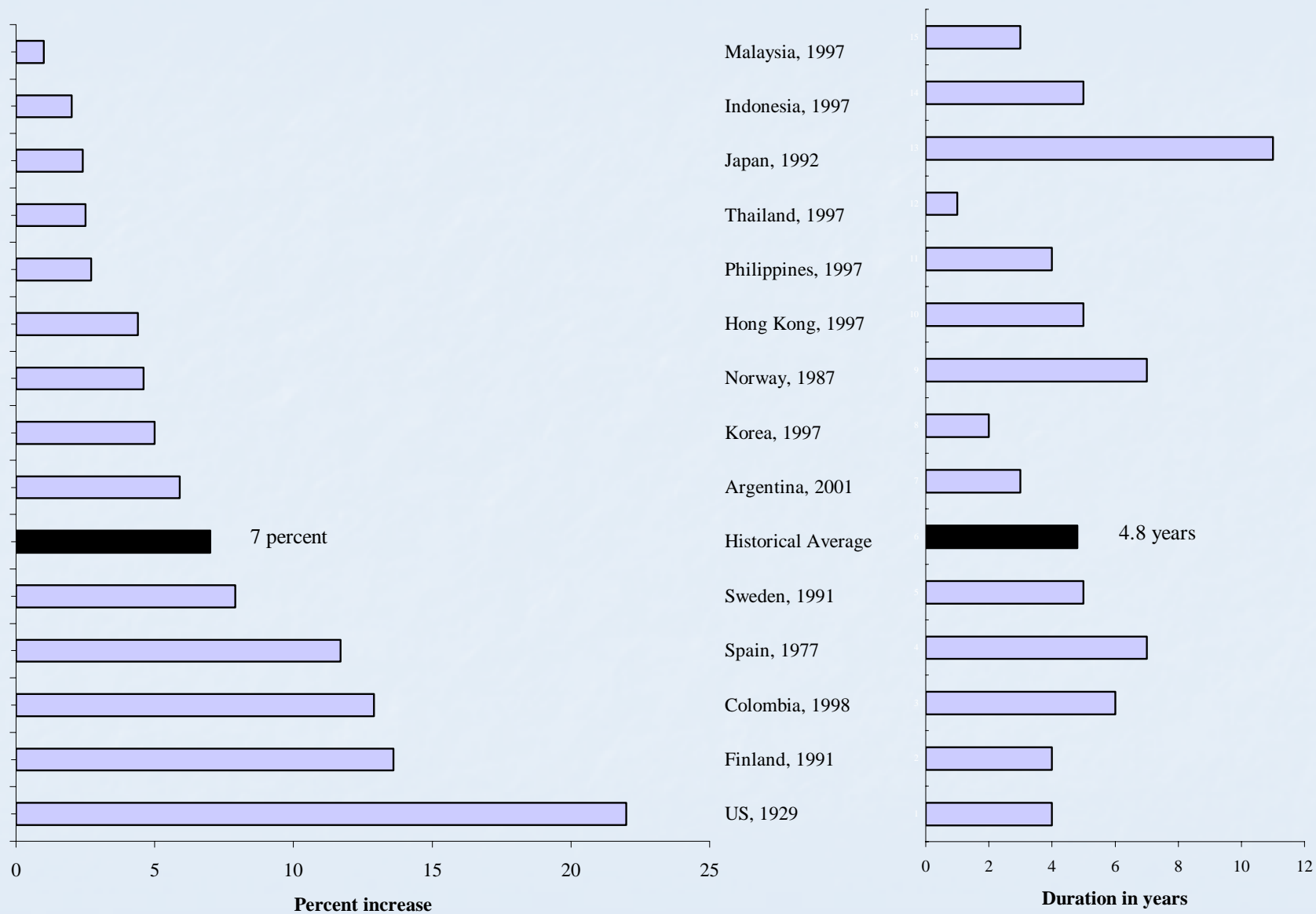
Peak-to-trough Price Declines (left panel) and Years Duration of Downturn (right panel)



Global stock markets during global crises: Composite real stock price index (*end-of-period*)

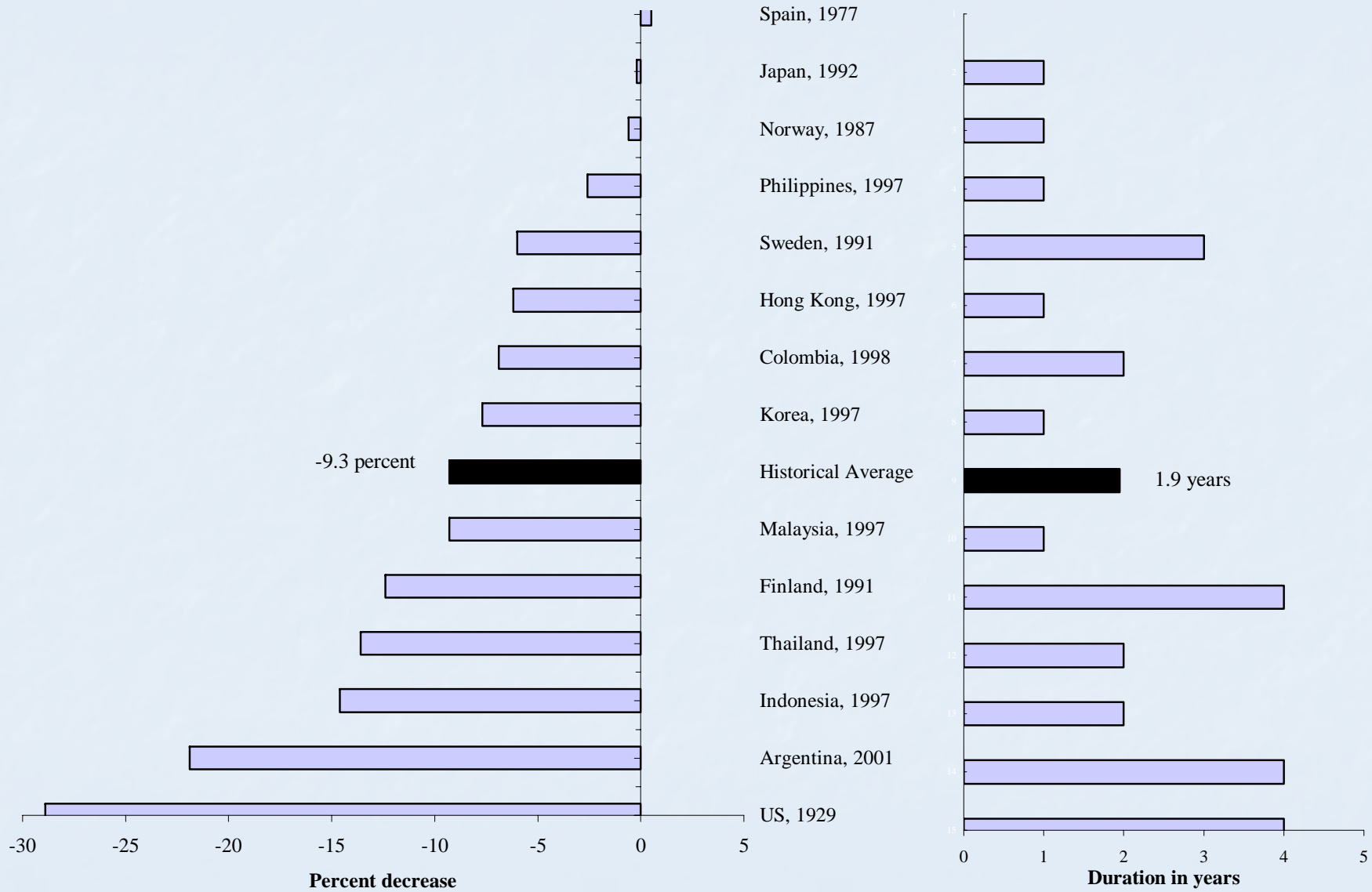


**Past Unemployment Cycles and Banking Crises: Trough-to-peak
Percent Increase in the Unemployment Rate (left panel) and Years Duration of Downturn (right panel)**

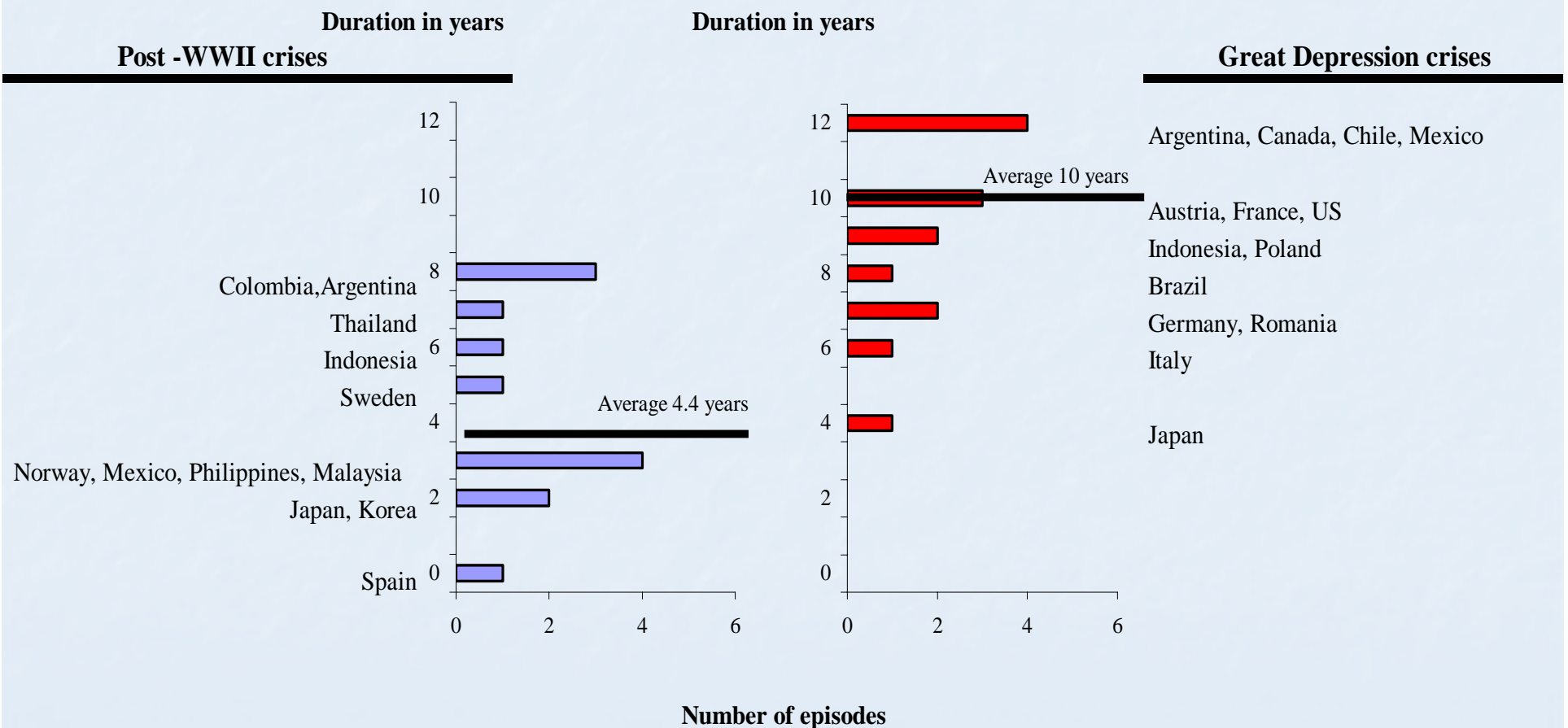


Past Real Per Capita GDP Cycles and Banking Crises: Peak-to-trough

Percent Decline in Real GDP (left panel) and Years Duration of Downturn (right panel)



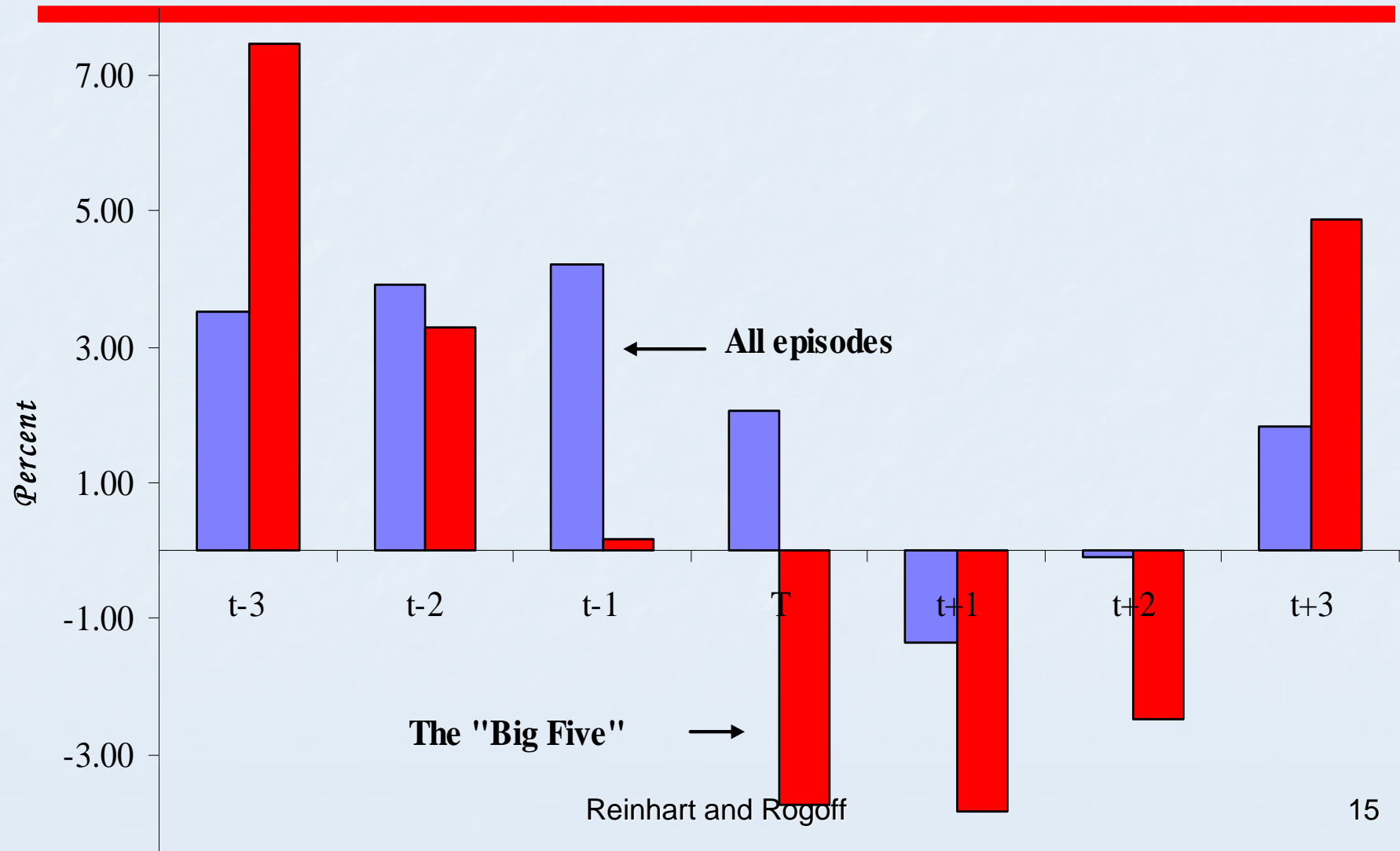
The duration of major financial crises since the Great Depression: The downturn, peak-to-pre-crisis peak in real per capita GDP in 28 episodes



As to the fiscal **aftermath** of banking crises, we find:

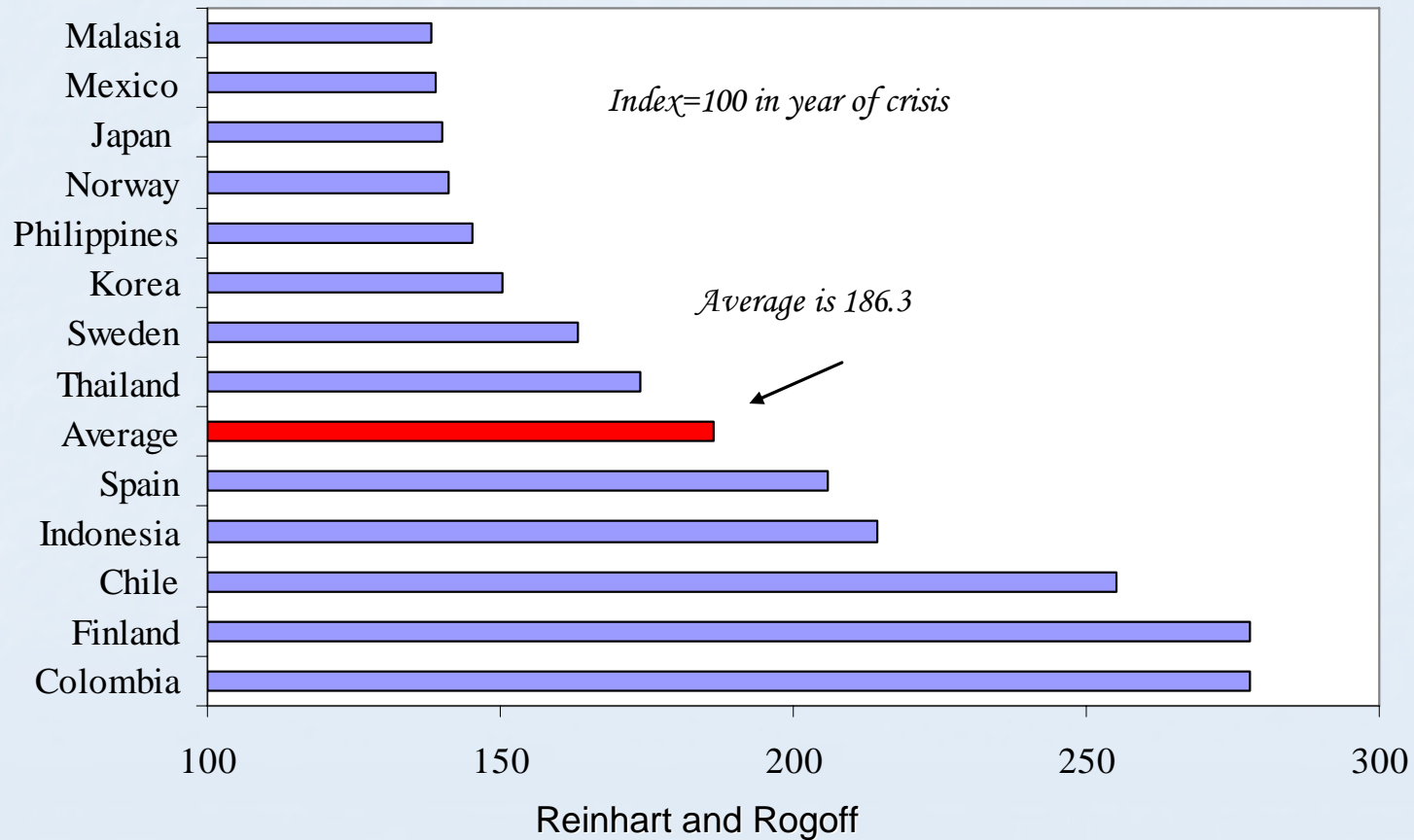
- That the nearly universal focus on calculations of **bailout costs** as the centerpiece of the fiscal consequences of banking crises is **misguided and incomplete**.
- Banking crises weaken fiscal positions beyond the costs of bailouts, as **government revenues contract and stimulus plans find favor**.

*Real Government Revenue and Banking Crises,
Advanced Economies, 1815-2007
(annual percent changes)*

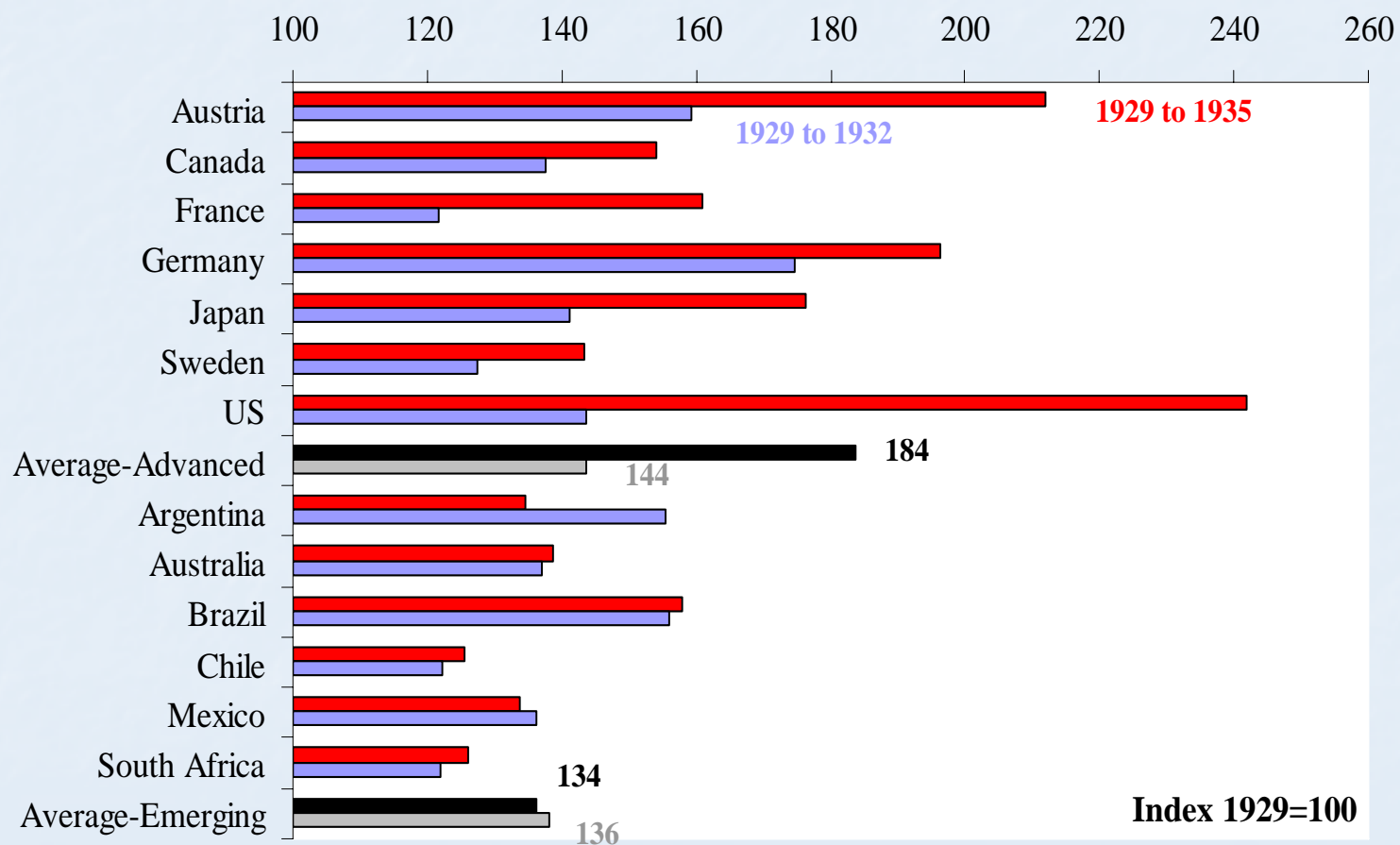


Thus, the true legacy of financial crises is **more government debt...**

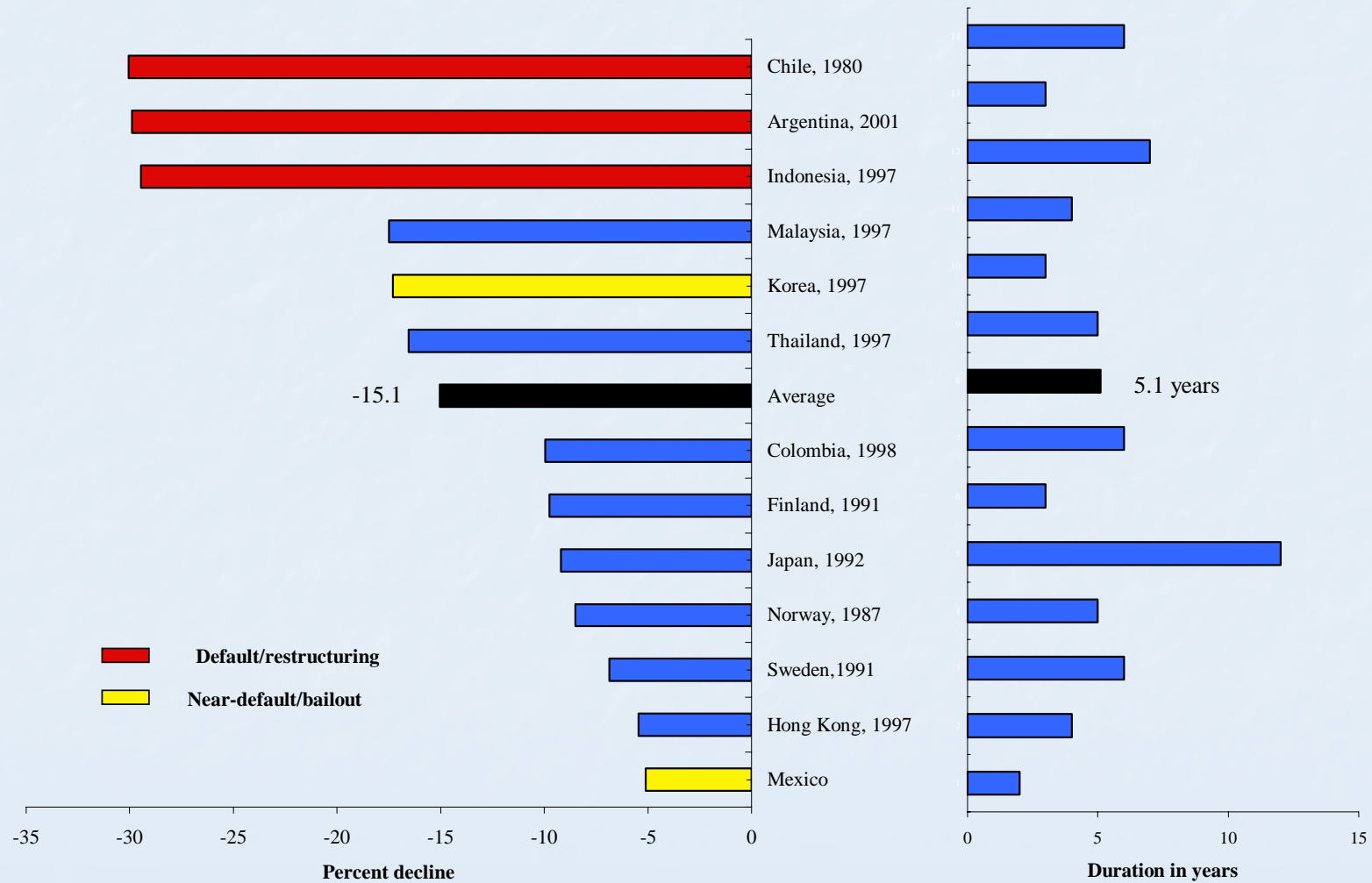
Cumulative increase in public debt in the three years following the banking crisis



Cumulative increase in real public debt in three and six years following the onset of the Great Depression, 1929



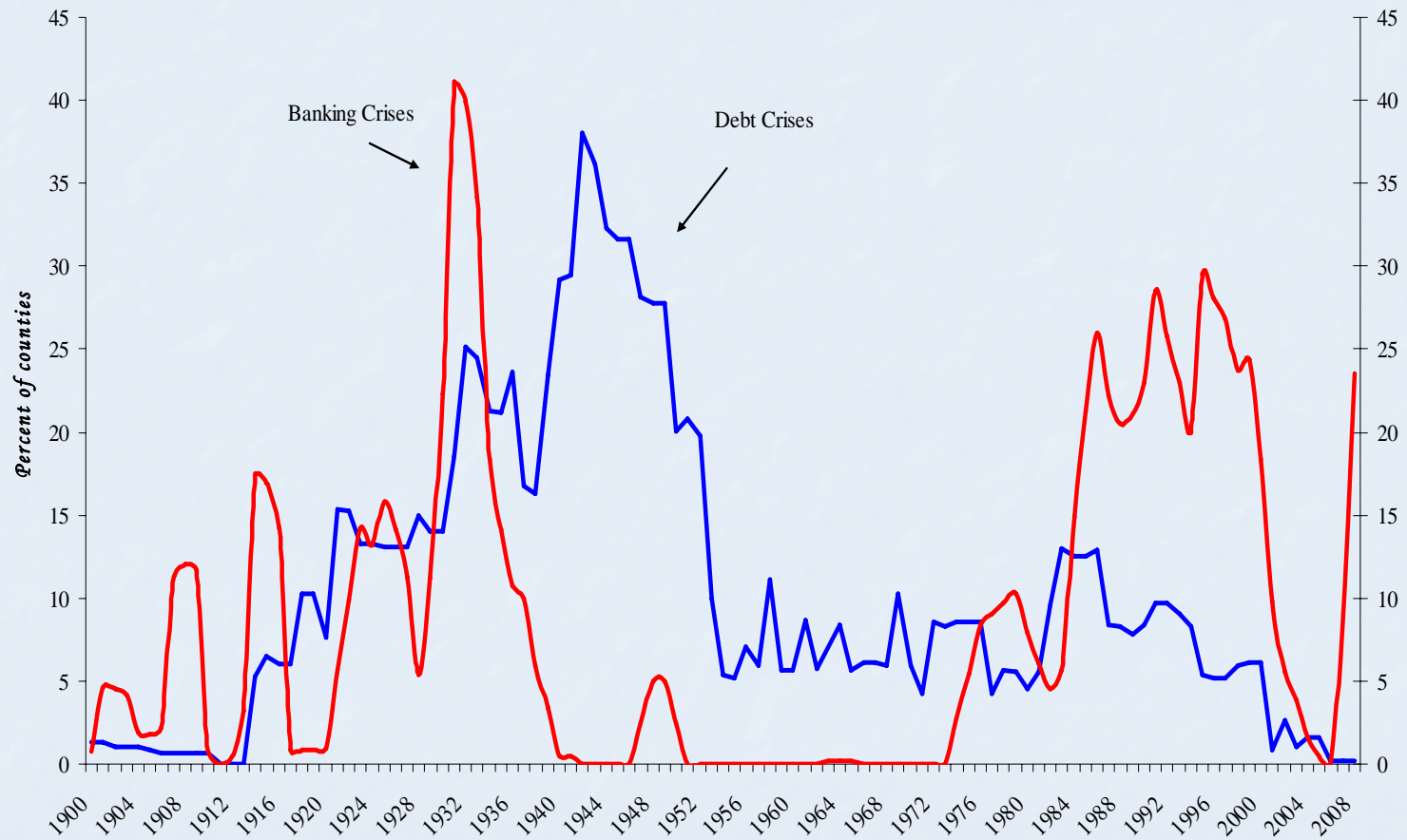
Institutional Investor sovereign ratings cycles and banking crises:
 Peak-to-trough index declines (left panel) and years duration of downturn (right panel)



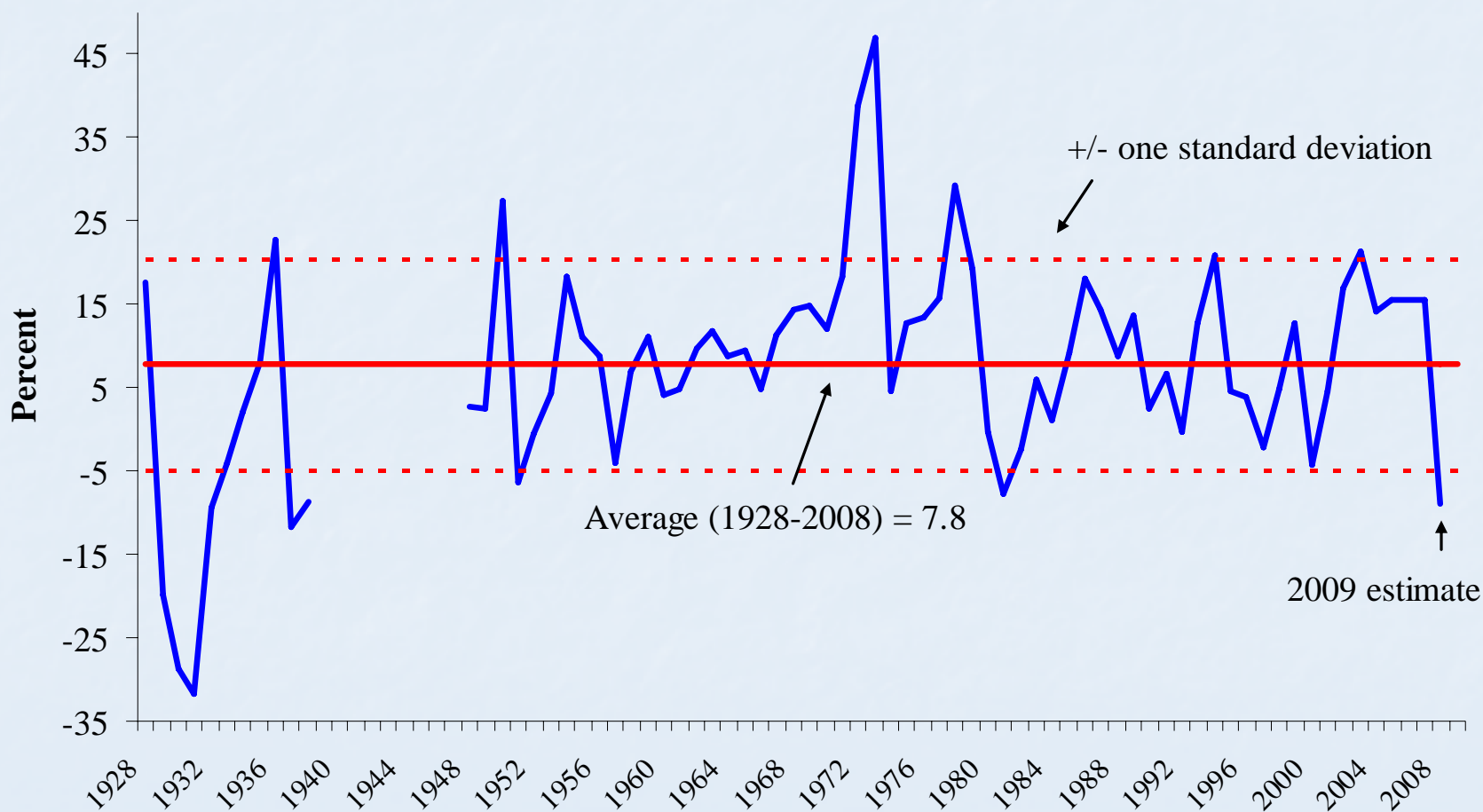
Banking crises and default cycles on external debt

- **This lull in sovereign defaults may also be temporary.**
- **A high incidence of global banking crises (such as at present) has historically been associated with a high incidence of sovereign defaults on external debt...**

*Proportion of Countries with Banking and Debt Crises
Weighted by Their Share of World Income*



World export growth, 1928-2009 (annual percent change)



Policy issues going forward

- **Swift** implementation is critical—delays are terribly **costly** in both terms of the economy and of the **cost** of the crisis (**speed** should take precedence over **polish**)
- **Soaring debt**: Policy makers should be concerned about the debt levels (explicit and implicit) that it is likely to take on as it works its way out of the crisis.
- Financial crises are “hardy perennials”-- **regulation** needs to be constantly revised and revisited to “**keep up**” with market innovation.