

DRAFT to be updated

Financial Crises and Global Business

C.T. Bauer College of Business

Summer II: class dates June 1 to July 2, 2015 (Melcher Hall 112)

Proposed meeting times: Monday to Thursday, 4:00 to 6:30 pm

Instructor: Beverly Barrett

Contact email: bbarrett@bauer.uh.edu

Office: UCBB 402-A tel. 713-743-2592

Class: Special Topics FINA 4397-3 19582 and INTB 4397-1 18589

Financial Crises and Global Business

This class assesses the history of financial crises, the policy responses, and the impacts on business development in specific cases from Latin America (1980-1990s), Southeast Asia (late 1990s), and the United States and Europe (2008-2009). An understanding of macroeconomic conditions and the role of institutions, in the public and private sectors, provides the context for this comparative analysis of financial crises. It is a relatively small seminar style class with opportunity for discussion.

This class is open to undergraduate students of any major, and it is an elective class for students in the Bauer College of Business. The class provides credit towards the certificate in Global Studies.

Prerequisite classes are a macroeconomics course or one course in INTB.

Course Objectives:

Financial Crises and Global Business assesses the history, policy/regulatory responses, and impacts on business. An analysis of the historical circumstances surrounding financial crises provides identification of similarities and differences across crises. Financial crises vary in their underlying impetus, as they may be caused for reasons of indebtedness, currency volatility, or scarcity of credit.

The instructor worked in economic research and public affairs with the Houston Branch of the Federal Reserve Bank of Dallas during the years of the recent financial crises 2008-2009. The Federal Reserve System, in cooperation with central banks internationally, provided institutional support to the private banking system. This monetary policy action, together with bank loans directly from the government's Treasury, and fiscal policy stimulus were among actions taken by the U.S. government. This most recent case provides the contexts for a comparative analysis of previous financial crises.

After taking this class you will:

- Understand the history of financial crises, in specific cases since the 1970s
- Be able to compare crises across countries and across time
- Evaluate policy response by national and international actors
- Specify the impacts of policy responses on domestic and global businesses
- Make a comparative analysis and draw conclusions regarding national and international policy responses to crises and the effects on business development and broader economic growth

Evaluation:

Mid-term analytical and essay exam in class	20 percent	mid-June, Week 3
Final take home research project exam	30 percent	due Monday, July 6
Participation	14 percent	
(Two) discussion/presentation assignments	2 x 8 points = 16 percent	
(Four) weekly homework brief essays	4 x 5 points = 20 percent	

DRAFT to be updated

The final exam research paper project is an assessment of a historical crisis in international economics. Specific instructions will be forthcoming.

The research paper will present three parts:

- I. History of a selected financial crisis
- II. Policy Responses: National and international levels
- III. Impact on Business

Organization of the course:

I. Historical Cases:

1. Debt crises of the 1980s and 1990s
Mexico 1980s debt crises, 1990s currency crises
Latin America 1990s
Russia late 1990s and 2014
2. Currency crises of the late 1990s
East Asia 1990s
3. Credit crises in the U.S. and Europe in 2007-2009
Great Recession 2008-2009, US and Europe

II. Policy Responses

1. Domestic politics responses and electoral outcomes
2. Role of multilateral lending institutions: IMF and ECB
3. Role of multilateral advisory institutions: Bank for International Settlements, Basel Committee

III. Impact on business:

1. Economic growth
2. Currency markets
3. Financial markets
4. Credit markets

Impacts on business are assessed at national and regional levels.

Required reading assignments:

1. Reinhart, Carmen and Kenneth Rogoff. 2009. *This Time Is Different: Eight Centuries of Financial Folly*. Princeton University Press: <http://press.princeton.edu/titles/8973.html>
2. Wolf, Martin. 2014. *The Shifts and the Shocks: What We've Learned—and Have Still to Learn—from the Financial Crisis*. London: Penguin Press.
3. Select book chapters and academic articles posted to Blackboard

DRAFT to be updated

Weekly topics and assignments:

The reading assignments will be discussed on the day listed following. Students are expected to have read the material and to come to class prepared to make discussion contributions.

Week 1, June 1 to 4

Foundations of international economics

Relationships among Exchange Rate, Interest Rate, and Money Market

- *This Time is Different*
 - Part I: Financial Crises: An Operational Primer 1
 - Chapter 1: Varieties of Crises and Their Dates 3
 - Crises Defined by Quantitative Thresholds: Inflation, Currency Crashes, and Debasement 4
 - Crises Defined by Events: Banking Crises and External and Domestic Default 8
 - Other Key Concepts 14

The Institutional Architecture of National and International Finance

National accounting: Balance of Payments

Introduction to crises

- *This Time is Different*
 - Chapter 2: Debt Intolerance: The Genesis of Serial Default 21
 - Debt Thresholds 21
 - Measuring Vulnerability 25
 - Clubs and Regions 27
 - Reflections on Debt Intolerance 29

Overview: Recent crisis history in the US and in Europe

International Economics

- *This Time is Different*
 - Chapter 3: A Global Database on Financial Crises with a Long-Term View 34
 - Prices, Exchange Rates, Currency Debasement, and Real GDP 35
 - Government Finances and National Accounts 39
 - Public Debt and Its Composition 40
 - Global Variables 43
 - Country Coverage 43
- Krugman, Obstfeld, and Melitz, chapter 20

Week 2, June 8 to 11

Institutional Design and International Finance

Recent crisis monetary policy response to the Great Recession

Recent crisis fiscal policy response to the Great Recession

- Rodrik, Dani. 2000. "Institutions for High-Quality Growth: What They Are and How to Acquire Them." *Studies in Comparative International Development* 35: 3 (Fall), 3-31.

Historical approaches to economic development: Import-Substituting Industrialization v. Export-Oriented Development

DRAFT to be updated

Latin America:

Mexico, debt crisis of 1980s

- *This Time is Different*
 - Chapter 9: Domestic and External Default:? 128
 - Real GDP in the Run-up to and the Aftermath of Debt Defaults 129
 - Inflation in the Run-up to and the Aftermath of Debt Defaults 129
 - The Incidence of Default on Debts Owed to External and Domestic Creditors 133
 - Summary and Discussion of Selected Issues 136
- Sachs, Jeffrey. 1986. "Making the Brady Plan Work." *Foreign Affairs*. 68(3), 87-104

Argentina and Brazil in the 1990s

Selected readings, posted on Blackboard

Latin America: Mexico, currency crisis of 1990s

- *This Time is Different*
 - Chapter 10: Banking Crises 141
 - A Preamble on the Theory of Banking Crises 143
 - Banking Crises: An Equal-Opportunity Menace 147
 - Banking Crises, Capital Mobility, and Financial Liberalization 155
 - Capital Flow Bonanzas, Credit Cycles, and Asset Prices 157
 - Overcapacity Bubbles in the Financial Industry? 162
 - The Fiscal Legacy of Financial Crises Revisited 162
 - Living with the Wreckage: Some Observations 171

Week 3, June 15 to 18

Asian currency crises of the late 1990s

- *This Time is Different*
 - Chapter 12: Inflation and Modern Currency Crashes 180
 - An Early History of Inflation Crises 181
 - Modern Inflation Crises: Regional Comparisons 182
 - Currency Crashes 189
 - The Aftermath of High Inflation and Currency Collapses 191
 - Undoing Domestic Dollarization 193

Asian currency crises of the 1990s, continued

- National and international policy responses and impacts on business
- Forbes, Kristin J. 2013. "The 'Big C': Identifying and Mitigating Contagion." Federal Reserve Bank of Kansas City.

Midterm exam in class, 1.5 hours

DRAFT to be updated

Week 4, June 22 to 25

The Great Recession in the U.S. and Advanced Economies

– *This Time is Different*

- Chapter 13: The U.S. Subprime Crisis: An International and Historical Comparison 203
- A Global Historical View of the Subprime Crisis and Its Aftermath 204
- The This-Time-Is-Different Syndrome and the Run-up to the Subprime Crisis 208
- Risks Posed by Sustained U.S. Borrowing from the Rest of the World: The Debate before the Crisis 208
- The Episodes of Postwar Bank-Centered Financial Crisis 215
- A Comparison of the Subprime Crisis with Past Crises in Advanced Economies 216
- Summary 221

The Aftermath of the Great Recession in the U.S. and Advanced Economies

- *This Time is Different*

- Chapter 14: The Aftermath of Financial Crises 223
- Historical Episodes Revisited 225
- The Downturn after a Crisis: Depth and Duration 226
- The Fiscal Legacy of Crises 231
- Sovereign Risk 232
- Comparisons with Experiences from the First Great Contraction in the 1930s 233
- Concluding Remarks 238

The policy responses: A closer look at national and international institutions

The roles of International Financial Institutions

The IMF, the Central Banks, and the Basel Committee

- Selected readings on Blackboard

Recent crisis impact on financial and credit markets in the five years following

- *This Time is Different*

The impacts on business

Chapter 17: Reflections on Early Warnings, Graduation, Policy Responses, and the Foibles of Human Nature 277

On Early Warnings of Crises 278

The Role of International Institutions 281

Graduation 283

Some Observations on Policy Responses 287

The Latest Version of the This-Time-Is-Different Syndrome 290

DRAFT to be updated

Week 5, June 28 to July 2

Class 13

Vulnerabilities of developing countries

Institutional weakness and dollarization liabilities

- Krugman, Obstfeld, and Melitz, chapter 22
- Raghuram G. Rajan and Ioannis Tokatlidis. 2005. "Dollar Shortages and Crises." *International Journal of Central Banking* (September 2005), 177-220.

Class 14

Conclusions and research projects focus

- What have we learned?
- Comparing regional crises
- The sources of financial crises over time
- Research presentations

Final exam – research paper for exam – due via TurnItIn on Monday, July 6

Additional Selected Readings:

(*Available on Course Reserve in library (two-hour to scan/copy); articles posted on Blackboard)

*Blinder, Alan. 2013. *After the Music Stopped: The Financial Crisis, the Response, and the Work Ahead*. New York: Penguin Press.

Forbes, Kristin J. 2013. "The 'Big C': Identifying and Mitigating Contagion." Federal Reserve Bank of Kansas City.

*Frieden, Jeffrey and Menzie D. Chinn. 2011. *The Making of America's Debt Crisis and the Long Recovery*. New York: W.W. Norton & Company.

Claessens, Stijn, Richard J. Herring, Dirk Schoenmaker. 2010. A safer world financial system: Improving the resolution of systemic institutions. Available from:

http://www.voxeu.org/article/safer-world-financial-system?quicktabs_tabbed_recent_articles_block=1

*Haber, Stephen. 2014. *Fragile by Design: The Political Origins of Banking Crises and Scarce Credit*. Princeton: Princeton University Press.

Krugman, Paul R., Maurice Obstfeld, and Marc J. Melitz. 2015. *International Economics: Theory & Policy*, 10th edition. Pearson. Chapters 20 and 22.

Oatley, Thomas. 2012. *International Political Economy*. Pearson Longman. Chapters 14 and 15.

Rajan, Raghuram G. and Ioannis Tokatlidis. 2005. "Dollar Shortages and Crises." *International Journal of Central Banking* (September 2005), 177-220.

*Rodrik, Dani. 2011. *The Globalization Paradox: Democracy and the Future of the World Economy*. New York: W.W. Norton and Company, Inc.

*Rodrik, Dani. 2007. *One Economics, Many Recipes: Globalization, Institutions, and Economic Growth*. Princeton: Princeton University Press.

Sachs, Jeffrey. 1986. "Making the Brady Plan Work." *Foreign Affairs*. 68(3), 87-104

The Economist interactive essay: The slumps that shaped modern finance

Available from: <http://www.economist.com/news/essays/21600451-finance-not-merely-prone-crises-it-shaped-them-five-historical-crises-show-how-aspects-today-s-fina>

The years 1792, 1825, 1857, 1907, and 1929 - that shaped modern finance - are featured in this essay. More recent crises are 2008 (sub-prime mortgage lending), 2001 (dot.com), 1997 (Asian crisis), 1987 (black Monday), and 1973-1974 (oil crisis with OPEC embargo to US)