Major Financial Crisis of 21st Century

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My years (2003-2006) on the Executive Board of the International Monetary Fund, coincided with some of the largest financial crisis of the 21st Century. Argentina, Brazil and Turkey were the Emerging Market Economies, which were witnessing severe financial crisis. Argentina's currency crisis was so severe that the Washington Post reported that parts of the country went back to the barter system. The G7 Finance Ministers with the IMF and World Bank formulated lending policies to enable crisis-ridden countries to regain macroeconomic stability. The work I had undertaken in that period, inspired me to pursue a study on the major financial crisis of the 21st century to be presented in a series of 10 articles. The crises that I will be presenting to in the 10 part series are the Great Depression 1932; the Suez Crisis 1956; the International Debt Crisis 1982; the East Asian Economic Crisis 1997-2001; the Russian Economic Crisis 1992-97, the Mexico crisis 1990-97; the Latin American Debt Crisis in Brazil, Argentina and Uruguay 1994-2002, the Global Economic Recession 2007-09 and the European Crisis 2010-13.

Large macroeconomic imbalances represented by current account deficit and fiscal deficit contributed to vulnerability in Emerging Market Economies (EMEs). In most crisis countries, EME's financed the twin deficits with short-term foreign currency debts. A financial crisis driven by excessive loan growth was normally preceded by currency crisis, high inflation and debt defaults resulting in high capital outflows. Financial crisis also resulted from poor banking regulation, explicit government guarantees resulting in macroeconomic distortions to promote excessive investment and external shocks like commodity price volatility deteriorated a country's terms of trade. The Great Depression of 1930-31 and the Great Recession of 2007-08 were episodes in which a large number of countries simultaneously experienced crisis. The other 8 cases are largely country specific crisis. The global crisis and national crisis were preceded by elevated growth rates and collapses in the year of financial turmoil.

The October 1929 crash of the US stock market was in the backdrop of a euphoric run-up of stock market prices. The bad recession of 1929 turned into the Great Depression of 1931 following a series of banking panics which emanated from Central Europe spreading contagion to the United Kingdom, the United States of America and France eventually engulfing the whole world. In the inter-war period the

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United States was running a significant current account surplus and Germany a significant current account deficit. Public and private sectors of Germany borrowed in dollar denominated bonds and credits from United States. The German credit boom was financed through a complex web of linkages in which banks of Germany, the Netherlands and Switzerland were involved. The German Central Bank – The Reichsbank did not provide adequate credit guarantees and credit risks were not covered. The financial crisis occurred in parallel in German and Swiss Banks and the resultant capital flight set off a banking sector crisis.

Egypt's nationalization of the Suez Canal in 1956 and the failed attempt to recapture it by France, Israel and United Kingdom had significant economic consequences resulting in all four countries seeking IMF financial assistance. The military action lasted two months and in the midst of the turmoil and uncertainty, a financial crisis erupted. The pound sterling came under heavy speculative pressure and United Kingdom witnessed short-term capital outflows.

The international debt crisis began on August 20, 1982 when the Mexican Finance Minister informed the bankers assembled in New York that Mexico could not repay the loan that was due and engulfed 20 countries. At the same time, Europe's commercial banks, which had a significant exposure to Poland, were informed of the need for rescheduling the terms of repayment. Similar requests were received from Romania, Hungary and Yugoslavia. The monetary contraction in the United States in the 1970-80 period resulted in a sustained appreciation of the US dollar. It made repayments in dollar terms impossibly difficult for most countries of Eastern Europe and Latin America. The commercial debt crisis erupted in 1982 and lasted till 1989.

A major financial crisis struck many East Asian countries in 1997. The East Asian economies, which were witnessing rapid growth and improvement in living standards suddenly, got embroiled in a severe financial crisis. The crisis was largely a result of large external deficits, inflated property and stock market values, poor prudential regulation, lack of supervision and exchange rate pegs to the US dollar resulting in wide swings to the exchange rates making international competitiveness unsustainable.

Amongst the National crisis that would be covered in this series are the Russian Crisis, the Argentine crisis and the crisis in Turkey. In August 1998 Russian Federation declared a default on its debts. There were difficulties in reaching a coherent rescue plan. The banking system paralyzed, the asset prices crashed, investors fled and millions of families plunged into poverty. In 2001-02, Argentina experienced one of the worst economic crisis in its history, with a 20 percent fall in output growth over 3 years, high inflation, government defaults on debt and a banking system paralyzed. The events of the crisis imposed major hardships on the people of Argentina. An economic crisis erupted in Turkey in 2001-02 caused by weaknesses in financial and corporate sectors, magnified by high inflation, depreciation of the Turkish lira and increase in interest rates during the crisis.

The 2007 Global Financial Crisis began as a sub-prime crisis, spread to a number of economies through a combination of direct exposures to sub-prime assets. It resulted in a gradual loss of confidence in a number of asset classes and drying up of wholesale financial markets. It exposed the financial imbalances in a number of advanced economies, which had an over-reliance on funding sources by banking systems and asset bubbles in residential property markets. The Global Financial Crisis required significant international policy cooperation with the G7 group of countries expanding to work with the G20 member countries to address the challenges of global imbalances.

A series of crisis hit several Euro area countries from 2010-2013. The crisis came soon after the global financial and economic crisis of 2007-2008. It occurred in a common area comprising of highly advanced and integrated economies posing significant challenges to policy makers. The IMF concluded agreements with five euro area member countries significant among them being Greece, Ireland and Portugal.

Economic histories of Nations contain several success stories of economic reforms undertaken by them, but what are remembered most are the years of hardship suffered by millions of populations at times of economic crisis. Thankfully the global efforts for addressing financial crisis have proved largely successful despite the severe temporary hardships imposed on the population.

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