Financial Crises (YOU DON'T NEED TO KNOW THE STUFF IN PARENTHESES!)

<table>
<tr><td colspan="3">Mexican Financial Crisis: 1994</td></tr>
<tr><td colspan="3">Boom Trigger: Financial liberalization led to large inflows of portfolio investment (including reduction of mandatory reserve ratio from 50% to 10%).</td></tr>
<tr><td colspan="3">Bust Trigger: The December Mistake--new president devalued peso slightly despite earlier promises not to.</td></tr>
<tr><td colspan="3" align="center">Tension Points</td></tr>
<tr><td>Currency Price Divergence (gap between pegged and free-market/mental-model value of currency)</td><td>Financial Returns (gap between financial/expected and real returns)</td><td>Financial Fragility (factors putting agents in precarious financial situations)</td></tr>
<tr><td>• Booming asset market kept peso strong so that government didn't have to support it
• All non-financial variables favored the dollar
• Ratio of foreign reserves to current-account deficit fell (from ≈ 200% to ≈ 20%)</td><td>• Real stock market returns far exceeded increases in real GDP (real share prices rose by ≈ 30% while real GDP rose by ≈ 4%)
• Large increase in share of GDP created by finance and real estate (percent of GDP created by industry fell slightly while that in finance and real estate rose by over 50%)</td><td>• Domestic debt/GDP rose (almost 400%)
• External debt increased (bank FX exposure rose by 30%, such that 1/3 of all loans being made were in FX)</td></tr>
<tr><td colspan="3">Consequences:
• Peso lost 60% of its value vs. dollar in two weeks
• Non-performing loans exceeded the equity capital of entire Mexican banking system (double!)
• Large contraction in real GDP (6%)</td></tr>
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Asian Financial Crisis: 1997 (focus on Thailand)		
Boom Trigger: Financial liberalization led to large inflows of portfolio investment .		
Bust Trigger: Government report indicating oversupply of housing; major land developer defaulted.		
Tension Points		
Currency Price Divergence (gap between pegged and free-market/mental-model value of currency)	*Financial Returns* (gap between expected/financial and real returns)	*Financial Fragility* (factors putting agents in precarious financial situations)
• Booming asset market kept baht strong so that government didn't have to support it • GDP falling and current account deficit rising • Ratio of foreign reserves to current-account deficit fell (from ≈ 400% to ≈ 250%)	• Ratio of financial investment inflows to GDP rose (almost 1000%) • Central city land prices rose (by 500%) • Meanwhile, GDP declining	• Short-term debt as a percent of long term increased (doubled) • External debt increased (by ≈ 40%)
Consequences: • Thai baht fell by 50% • Collapse in real estate prices meant that developers could not repay banks • GDP fell catastrophically (by 40%)		

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