

**Recovery and Relapse in Emerging Economies:
The role of political experience in economic crisis policy**

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Introduction

After the global recession of 2008-2009, it became clear that globalization increased the systemic risk of contagion of economic crises across all financial markets. Due to the interconnectedness of the financial markets, severe crises affected almost every region and country. Economic theory suggests that more developed economies would be better able to recover from an economic crisis because these states have greater access to credit and the ability to borrow their own currency during an exogenous shock. However, the most recent global financial crisis puzzled political scientists and economists alike as the emerging markets in Latin America and South East Asia recovered more quickly than the developed economies of North America and Europe (Haggard 2013). Within the category of emerging economies, Latin America and Eastern Asia recovered more quickly than Eastern Europe.

While existing literature examines the disparity in successful recovery between emerging markets and developed economies, there is little empirical evidence explaining successful and stunted recovery in emerging economies. What explains the successful macroeconomic recovery in Latin America and Southeast Asia after 2008 recession? I contend it is the combination of institutional change and rational choice that permitted emerging economies in Latin America and South East Asia to recover more quickly than emerging economies in Eastern Europe. More specifically, I argue that developing countries that had undergone earlier crises were in better shape to employ Keynesian policies because they enjoyed better macroeconomic fundamentals than many of the Eastern European economies due to previous economic reforms in the decades leading up to the most recent global financial crisis.

Institutional Change and Rational Choice

I define institutions as “constraints on behavior imposed by the ‘rules of the game’”. While this includes any form of social beliefs and norms that shapes human interactions, I focus on a macro systematic approach to address political and economic institutions. Therefore, when I refer to institutional change I am addressing the shift in political economic rules within a country. For instance, the move from populist policies, which guarantee a social safety net, towards capitalist policies, removes previously government sanctioned economic protection for the poor.

I define rational choice as the patterns of choices made by politicians to maximize their benefits and minimize their costs. An example of rational choice is the adoption of neoliberal structural reforms by Latin American countries in order to receive IMF monetary aid during the currency crises of the 1980s and 1990s.

Neoliberalism in Emerging Economies

Since the mid 20th century, politicians have gradually transitioned from enacting state-led economic policies to market-led policy. The neoliberalism trend is particularly visible in emerging markets, even those headed by leftist governments. Neoliberals advocate for an economy led by the market and a strong legal system to secure property rights. They support the removal of barriers to trade. The idea that government intervention disrupts the economy is fundamental to a market led economy. For this reason, neoliberals want to limit regulation and government intervention as much as possible, even during times of economic stress. For instance, neoliberal reforms

emphasize austerity during economic recessions. Emerging economies have co-opted the fundamentals of the “Washington Consensus” in order to increase trade with the United States during the age of globalization. Although most governments employ some aspects of neoliberalism, leftist governments employing neo-liberal policies are particularly strong in the regions of Latin America and Southeast Asia. Eastern European countries, on the other hand, were more likely to engage in counter-cyclical spending as they had a strong currency and low risk of default backed by the European Central Bank.

After the onset of the financial crisis of 2008, it became clear that all governments would have to respond quickly to prevent more fallout. Political economists expected political actors to react in the same way they have in previous financial crisis of the 1980s, 1990s, and early 2000s. During the 1980s, leftist Latin American governments began structural neoliberal reforms, such as encouraging privatization to lower the burden on their national treasuries. In the 1990s, these governments made neoliberal reforms more sustainable by adopting floating exchange rates. However, a puzzle emerges because many leftist governments acted as conservatives and instituted state-led reform as a response to the most recent crisis, rather than continue with pro-cyclical reforms.

Surprisingly, the governments that utilized a hybridization of market-oriented policies and Keynesian policies were more successful than governments that only employed counter-cyclical policies. Market-oriented policies encourage competition between private companies to encourage consumption and restart the economy. Pro-cyclical policies are indicators of a tight budgetary maintenance, while counter cyclical suggests state-led spending. During times of economic crisis, pro-cyclical policies would increase credit controls and reduce government spending. Counter-cyclical policies

include targeting inflation control and stimulus packages. Also known as Keynesian policies, these strategies depend on government spending to jumpstart the economy when consumer confidence and spending is down. While Latin American and Southeast Asian governments had lacked the financial credibility to borrow from banks and other countries to engage in Keynesian policies in previous crises, the structural reforms they underwent in the last twenty years allowed them more flexibility to use a mix of both strategies.

One would have expected the leftist governments to not be very successful with market-oriented reforms. Since leftist governments rely on an electoral base that supports social safety nets, the promotion of tax cuts for private businesses rather than using tax money for public use. However, it is likely that previous experience reminded these leaders that using only expansionary, Keynesian type solutions exacerbated problems with macroeconomic stability and international opinion.

Southeast Asian leaders also implemented similar responses as Latin American politicians during their currency crises in the 1990s and early 2000s, as well as the financial crisis of 2008. Yet, there is no left within Southeast Asia, suggesting that the success of the reforms made by emerging economies were not related to a specific type of political group in power. Rather, institutional change and rational choice explains the consensus of ways to achieve successful economic recovery in Latin America and Southeast Asia and the struggle for recovery in Eastern Europe.

Explaining Economic Reform

In order to explain reform, we must investigate why it occurs in the first place.

Literature suggests that reform can be triggered in three ways. The first, “shocks,” occur because of a specific event, such as a change in power, a crisis, the establishment of a new regime, a change in global interest rates, and the amount of leverage held by international financial institutions (Krueger, 1993). Reforms can also be triggered by new information that instigates the reexamination of the costs and benefits of current government policy. This new information can also diminish uncertainty about who the winner is in a regime (Fernandez and Rodrik, 1991). For instance, Eastern Europeans shifted away from socialist policies after the fall of the USSR in the early 1990s. The leaders in these former satellites saw that the West was a stronger ally, and changed their political economic policies to reflect capitalist rhetoric. Finally, reform can occur based on the type of regime (Persson, 2002) and its policies concerning trade (Rajan and Zingales, 2003), the structure of its legal system (La Porta et al., 1997), and its ideology (Alesina and Roubini, 1992). The agent of change in this case is global governance institutions and international norms.

Implicit in these theories is the idea that reform would not occur unless a problem is present in the current system. Governments with a happy population have little incentive to change the status quo. Governments in the wake of an economic crisis, on the other hand, have myriad problems to solve. Specifically in democratic regimes, there is a very large incentive to return to times of economic growth in order to continue political party dominance. For these reasons, it is evident that reform occurs predominantly post-crisis, rather than before. One political economy study argues that this theory, known as the “crisis hypothesis” has become the “new conventional wisdom” in understanding why reform occurs (Tomassi and Velasco, 1995).

While the theory that crisis induces reform has not been seriously questioned since Rodrik, the reasoning for what indicates crisis are debatable. One empirical study of political economy suggests that cases with extremely high levels inflation will pursue strategies of lower inflation, when compared to cases that only have moderate inflation (Bruno and Easterly, 1996). This shows that inflation is a good measure of severity of a crisis. Further studies expanded the variables that indicate severity of a crisis. Another concluded that in addition to inflation, black market premiums are the best indicators of crisis, rather than current account deficits, high budget deficits, or negative per capita growth rate (Drazen and Easterly, 2001).

A distinction needs to be made between different types of reform because reform can be implemented at many different levels (Rodrik, 1996). One type of reform is macroeconomic stabilization, which is far easier to implement since there is more agreement on appropriate measures to ensure macroeconomic stability. The other type of reform is liberalization and structural reform at the microeconomic level, which is more difficult to implement because perception of ineffectiveness is harder to measure and detect. I chose to focus on the implementation of macroeconomic reform because it is a better indicator of policy choice.

Institutionalist Theory

In addition to looking at economic reform literature, historical institutionalism theory is important to explain how similar economic reform occurred within two regions with distinct political factors at around the same time. One theory of historical institutionalism suggests that political institutions are sticky and policy change is very

difficult to achieve. When it does occur, it can be explained as a response to exogenous shocks and significant failures of policy (Krasner 1988). This theory relies on the belief that change results from a “critical juncture” in policy (Baumgartner and Jones 1993).

However, other theorists believe that institutional change can take place more gradually. Smaller events can change policy dramatically, but their effects can only be felt over time (Mahoney and Thelen 2010). Gradual, cumulative change best explains the adoption of the similar economic policies by Latin American and Southeast Asian leaders over time. It also explains the small variances in counter-cyclical policies across each regime, as small and gradual policy adaptations to globalization do not shift the fundamental character of each regime.

Causal Relationship

I argue that it is endogenous factors of the middle-income developing countries that led to discrepancies in the success of recovery. I contend there is a historical path dependent argument between successful macroeconomic reform and previous experience such as prior macroeconomic crises that led to subsequent reform that improved better macroeconomic statistics so that Keynesian reflation was possible in 2008. I argue that there is a causal connection between successful macroeconomic recovery in the most recent global recession and the type of reform previously implemented. In Latin America and Southeast Asia, neoliberal reforms had already been tried in response to the debt and currency crises of the 1980s, 1990s, and early 2000s. The results of the reforms taken in response to these crises were stronger currencies, current account surpluses, and a declining fear of default risk. Developing countries were in a much better position to try

reflationary policies, regardless of political orientation, because of the previous structural changes. Furthermore, political leaders that were capable of forgoing austerity and utilizing Keynesian policies were more likely to retain their leadership.

Eastern Europe, on the other hand, was constrained by the austerity measures forced on them by the core countries of the Eurozone. Joining the Euro gave Eastern European countries the ability to borrow money cheaply, increasing their current account deficits. A current account deficit implies that a government is relying on borrowed money to finance its actions. When the financial recession hit, the ability to make any macroeconomic decisions was severely constrained by the ECB. This is important because it can explain the puzzle of why emerging markets in Latin America and East Asia recovered more quickly than emerging markets in Eastern Europe. It can also illuminate a possible new consensus of economic policy during times of crisis for all types of governments, regardless of the economic ideology of the reigning political group.

Research Design

In order to explore the relationship between successful macroeconomic recovery and previous macroeconomic reform experience, I will test my hypothesis by exploring eight case studies from three different geographic regions of emerging markets.

Argentina and Brazil make up the Latin America subset. Indonesia, Malaysia, South Korea, and Thailand account for the case studies in East Asia. The Eastern and Southern European case studies are Greece, Poland, and Spain. The large number of cases account for the diversity of the global market as a whole, particularly due to the range of

geographical regions and the state of their financial markets. Furthermore, the vast majority of these countries have accessible and consistent reports of data.

The variables include political and economic variables. Macroeconomic variables like current account deficit, inflation rate, GDP per capita growth, and sovereign debt rates are from the World Bank. Other variables, such as type of currency regime and IMF agreements are from the IMF. Furthermore, I will explore case studies comparing the 1980s, 1990s, and 2000s to the most current crises, I hope to show a correlation between successful macroeconomic reform and previous crises experience.

Dependent Variable

The dependent variable is health of the overall economy in the years after the Great Recession. It is operationalized by GDP growth rate gathered from the World Bank. I have broken this down into three different categories of recovery in Table 1.¹ Group I is little to no recovery where GDP growth is below 3%. Group II is moderate recovery, where GDP growth is between 3-6%. Group III is quick recovery where GDP growth is 6% and higher.

Independent Variable

The independent variable is policies enacted in response to the crisis. These policies include banking regulations, central bank goals, and exchange rate regimes. These policies affect factors such as current account deficits, unemployment, inflation, and bank lending policies, liquidity, and political risk. This is operationalized by policy type, which is made up of expansionary, contractionary, or mixed economic policy.

Latin America

Latin America was primarily affected by the Great Recession through trade and the financial market. Countries that relied heavily on the US as a trading partner, like Mexico, suffered a greater fall in exports and commodity prices than countries like Brazil, Chile, and Argentina (Haggard 2013). Diversification of trade had a large impact on the health of the economy. In the financial markets, countries with higher political risk premiums, like Venezuela and Argentina had higher sovereign debt yields. Investors desired greater compensation for the risk that these countries would fall into turmoil. Despite these conditions, Latin American countries not only rebounded quickly compared to previous Latin American crises, but also were in better economic shape than the advanced industrialist states (Haggard 2013).

I argue this is due to their previous financial crisis experience and subsequent reforms made in response. Sovereign debt crises plagued Latin America in the early 1980s. Mexico, Brazil, and Argentina had been borrowing money cheaply from foreign investors for years to develop infrastructure (Calvo 2000). As their countries' economies were booming, few leaders were paying attention to the massive amount of loans policymakers has signed off on. When the global economy went into recession in the late 1970s, interest rates on bond payments rose as Latin American currencies depreciated. Once it became clear that these countries could not repay their bills, Latin America underwent years of stagnated growth as a result of contagion. Leaders eventually turned to the IMF for a bailout and instituted pro-market reforms as well as austerity programs (Calvo 2000). In addition, new securities such as Brady bonds were created to convert

distressed sovereign debt into new bonds (Wolfson and Epstein 2013). Through these methods, Latin American countries in distress were able to reduce their debt.

The second round of crises occurred in 1994, notably commencing with the Tequila crisis of 1994. A sudden devaluation of the Mexican peso, spurred by the loosening of tight currency controls put in place by Ernesto Zedillo's predecessor, President Carlos Salinas, created a massive interest rate crisis (Calvo 2000). The rationale behind the shift in economic policy was to increase Mexico's fiscal capacity, but ended up raising Mexico's risk premium. As a result, the peso fell by nearly 50% in one week. Although the US government stepped in with a 50 billion dollar bailout by guaranteeing Mexican loans, debt yields were still at 11% (Calvo 2000). The bond crisis spread throughout the entire region, particularly in Argentina. The speed of effects of contagion throughout the area became very worrisome as it resulted in a dramatic collapse of market activity. Confidence started to build up again after a few years and Mexico was able to repay all of its US Treasury loans by reforming further.

The economic policy reforms made during these two financial crises would soften the effects of the Global Recession by enabling Latin American governments more flexibility. These changes include a shift towards more flexible exchange rate regimes, pro-cyclical policies, diminished government debt, and a new emphasis on domestic borrowing (Wolfson and Epstein 2013). Flexible exchange rate regimes are an important change in economic policy as it gives policy makers monetary authority. It also makes the currency and interest rates far more sensitive to investor confidence. Pro-cyclical policies encouraged leaders to spend in during economic booms and initiate austerity during recessions. This gave foreign investors more confidence in Latin America's

emerging markets as they were following policies similar to the “Washington consensus.” Governments were also borrowing significantly less than they had in the past, resulting in diminished government debt, if not a surplus in some countries. Finally, while foreign investors are still an important capital source for emerging markets, Latin America began focusing on domestic borrowing through bonds and securities (Wolfson and Epstein 2013). This lowers the capital flight risk, which can have a significant effect on the sovereign debt bond yields. What is most remarkable is that this pattern emerged across most of Latin America, regardless of political orientation.

These reforms made it possible for Latin America to be in better shape than other emerging countries in Europe that did not have the fiscal, nor the monetary freedom to pursue the same policies. Exchange rate flexibility allowed governments to depreciate their currency, making exports more desirable in other countries. Furthermore, low levels of government debt permitted policymakers to respond with countercyclical measures, which wouldn't have been possible had their currency still been pegged. Additionally, almost all major countries in the region announced fiscal stimulus, with the exception of Colombia (Haggard 2013). While political orientation affected the form of the stimulus, whether it be conservative pro-cyclical policies in Chile or populist policies in Brazil, fiscal stimulus were seen across the board. This is in great contrast to previous reform strategies of the 1980s and 1990s, suggesting that Latin America is no longer constrained to a pro-cyclical response to financial crises.

Southeast Asia

Like Latin America, Southeast Asia's previous crisis led to reforms that better prepared them for the global recession. In the 1997 the Thailand baht collapsed when the Thai government switched from a pegged currency board to a floating rate (Coursetti 1999). Thailand's significant foreign debt bankrupted the country and investor confidence fell in the entire region. The financial crisis spread to all the countries in the region, although South Korea, Indonesia, and Thailand were the most affected. Nevertheless, financial contagion resulted in devalued currencies, stock market crashes, a rise in private debt, and a loss of demand (Haggard 2000). As Asia had attracted almost half of total capital inflow of other developing economies, the fall in confidence was a big hit to the region's economies and resulted in stagnant growth.

In response to the crisis, the governments of Asia appealed to the IMF, just as Latin American leaders had done the decade before. The IMF initiated a 40 billion dollar relief program to stabilize South Korea, Thailand, and Indonesia. The structural adjustment packages (SAP) required nations to reduce government spending and deficits to restore confidence in fiscal authority (Goldstein 1998). Furthermore, it stipulated that governments must let insolvent banks fail, as it would promote accountability in the banking sector. Finally, governments were required to raise interest rates to promote their currency. In addition to these contractionary policies, the IMF also encouraged liberalization of the financial sector through the elimination of restrictions on capital flows, high interest rates to encourage domestic borrowing, and re-pegged national currencies to the dollar to prevent currency risk (Goldstein 1998).

Similarly to Latin America, Southeast Asian countries pursued radically different policies in the most recent recession due to an increase in economic flexibility. Instead of pro-cyclical efforts of the late 1990s, central banks provided liquidity and instituted policies of monetary easing (Ananta 2011). This resulted in exchange rates depreciating to make exports more competitive. Furthermore, fiscal stimulus packages were the norm across governments of all ideologies, including authoritarian and semi-authoritarian regimes (Haggard 2013). The most popular strategy were social expenditure measures, although tax cuts were popular in Indonesia and the Philippines. As Southeast Asian economies continue to increase competitiveness with more advanced economies, they have shifted their pursued policies to reflect not just export interests, but also the interest of consumers.

Eastern Europe

Eastern Europe took significantly more time to recover from the global recession due to economic constraints of the Euro, pressures from the core countries, and poor fiscal decisions made after joining the Eurozone. In order to join the Euro, nations were required to limit their government debt levels following the Growth and Stability Pact (Pop-Eleches 2008). Nearly every country broke these guidelines. Particularly in Eastern Europe, where credit had been difficult to obtain due to high risk premiums after dissolution of the USSR, joining the Eurozone meant easy credit (Pop-Eleches 2008). Governments could borrow at very cheap rates. Furthermore, the EU encouraged the idea of Europe as an identity and provided a large fund to help Eastern Europe assimilate to Western Europe.

A distinction needs to be made in the degree of monetary autonomy each nation possessed during the aftermath of the crisis. Greece, Ireland, and Portugal are members of the Eurozone, and very constrained by the core countries of Germany, France, and Belgium. Hungary, Romania, and Bulgaria are members of the EU, but had not adopted the Euro. Finally, many former Soviet satellite countries including Armenia, Belarus, Bosnia and Herzegovina, Georgia, Kosovo, Serbia, and Ukraine are outside of the EU all together. The first group, in addition to being constrained by the core countries' economic authority, are also at the center of a banking crisis because of overleveraged banks and complicated financial instrument markets. As they had no monetary autonomy, pro-cyclical policies were forced upon them.

Quick Recovery

The countries that fall into the quick recovery category are Brazil, Malaysia, Indonesia, and Poland. These countries carried out similar policies that greatly contributed to the success of their recovery. Foremost, these countries all displayed a trend of strong government fiscal responsibility. This is linked to previous policies from the 1990s. In Latin America and Southeast Asia, IMF funds were contingent on cyclical fiscal spending. Fiscal responsibility is related to austerity measures, which is the second common policy of quick recovery countries. Since the IMF bailouts of the 1990s stressed pro-market reforms and austerity programs, these countries continued the practice even after the SAPs had ended (Wolfson and Epstein 2013). Indonesia, in particular, underwent a structural readjustment plan in response to the Asian financial crisis. As a result, these countries were running a surplus leading up to the Great Recession. This is

essential to their recovery policies as they had the ability to engage in counter-cyclical policies without raising their risk of default. Brazil, Malaysia, Indonesia, and Poland also had the ability to pursue hybrid policies that mixed structural reforms with industrial policies and slight capital controls. For instance, even Brazil had a stimulus package that increased its GDP growth significantly in the years following the Great Recession (Haggard 2013).

Other factors that lay the foundation for a quick recovery are diversification of trade, an emphasis on domestic borrowing, and strict banking policies. All of these countries had enough sectors of their economy that a collapse in one did not lead to a collapse in overall trade. Furthermore, these countries had made the transition from primarily relying on foreign investors to encouraging domestic borrowing. Domestic borrowing lowers the risk of speculative attacks on domestic currency since domestic investors are less likely to pull out in times of turmoil. These emerging economies learned the troubles of flighty foreign investors responding to political risk after the Latin American currency crisis and the Asian financial crisis, prompting them to encourage domestic borrowing. Likewise, stricter banking policies limits systemic risk in the banking system and lowers the threat of contagion (Abidad and Moody 2005). Poland and Indonesia have very strict banking policies as a result of previous structural adjustments, which insulated their economies from the damaging assets that overleveraged banks in Europe had accumulated.

The last factor that contributed to a quick recovery is still debated by political economists (Calvo 2000). Exchange rate regimes, whether floating or fixed, are limited by the “Trilemma” where it is only possible to have two of the following circumstances:

a fixed exchange rate, free capital flow, and sovereign monetary policy. I contend that the quick recovery countries were able to respond to the crisis more quickly because they had free-floating exchange regimes which encourage more foreign investment and an increase in free capital flow. The central bank's ability to devalue money through open operations is crucial to emerging economies that rely on exports as a big source of their GDP. By expanding the money supply, the central bank devalues the domestic currency relative to foreign currencies. This drives up demand for exports and lowers demand for imports, which boosts GDP growth.

Moderate Recovery

South Korea best exemplifies a moderate recovery of between 3 – 6% GDP growth due to a mix of successful and failed policies. South Korea's biggest failure was a loss of competitiveness. As the Japanese yen fell against the won in the past two years due to Japanese stimulus programs, the South Korean won appreciated, significantly hurting the South Korean export sector of the economy (Wolfson and Epstein 2013). The won itself is currently experiencing volatility as the central bank has attempted to increase competitiveness through dollar-buying to weaken the won against the yen.

Nevertheless, South Korea does have the economic fundamentals to withstand the monetary stimuluses of the US and Japan. South Korea accumulated a large amount of foreign currency reserves to insulate its currency from speculative strikes (Wolfson and Epstein 2013). Like the quick recovery countries, South Korea accumulated a low external debt load from previously running a surplus before the devaluation of the yen. As the 4th largest Asian economy, South Korea also had a steady current account surplus

from its trades with the US. These conditions lay the groundwork for South Korea's ability to engage in monetary easing during the first year after the Great Recession. As the Central Bank lowered interest rates and the government enacted a stimulus program, it is clear that South Korea engaged mainly in expansionary policy, which contributed the majority of its limited success.

Little to No Recovery

Policy makers and economies are still struggling to find sustainable economic solutions for Hungary, Greece, Spain, and Argentina today. These countries suffer from a few conditions that have constrained their ability to recover. All of these countries have seen changes in their political parties and the rise of extremists. In Argentina, the populist leadership has pulled the country deeper into crisis due to meager reserves, a stagnant economy, and rising inflation without economic growth. Fewer dollars are available due to capital plugs to prevent flight risk, but as a result imports have fallen which have further dragged overall economic activity. The reliability of the government has also been called into question with its attempts to avoid paying investors on its sovereign debt bonds and unreliable economic data.

In Europe, Hungary, Greece, and Spain are suffering from large current account deficits and balance of payment crises (Pop-Eleches 2008). As Greece and Spain are constrained by the Eurozone and unable to devalue the Euro, they are unable to pay back their debts. Unemployment has skyrocketed and austerity programs have been forced upon them, which further reduce GDP growth (Pop-Eleches 2008). These peripheral countries have realized that their historical trend of borrowing has led to more difficult

economic and political adjustments, particularly in the shift of regimes. Political trends have shown that as the right likes to borrow, the left ends up paying back through austerity measures, causing further public unrest and a shift in the political climate.

Conclusion

While it is interesting to note that political decisions and not just the market affect the macroeconomic recovery, there is room for more research on the matter. Future research on the global recession should include variables that account for the complexity of the financial system, as less developed economies often do not have the same derivatives available that caused the most recent financial crisis. Trade relations and its impact on recovery would also be an interesting topic to explore, as nations that had less contact with the US generally improved more quickly than those that had heavily integrated economies. Furthermore, it is difficult to understand the entire plausibility of this theory until more time has passed and all of the economies have fully recovered from the global recession. Current fiscal and monetary policies have a lag effect; so until more time passes many trends will not be as apart. Missing data could be supplemented with more qualitative research on specific cases through interviews with policy makers. With this in mind, theories will need to be revised and expanded as the long-term effects of macroeconomic reform are realized.

It is clear that emerging economies need several factors to better insulate themselves from future financial crisis. First, investor confidence is necessary. Traditionally foreign debt lenders have power to shift interest rates significantly by

flooding the markets with national currencies, but emerging markets can remedy this problem through strong domestic borrowing. Second, low levels of government debt are important to sustain counter-cyclical policies. Not only do low levels of government debt lower the political risk premium, but past surpluses allow governments to borrow more cheaply in times of need to stimulate spending. The success of fiscal stimuluses in Latin America and Southeast Asia and the failure of austerity programs in Eastern Europe highlight the disparity in successful recovery. Finally, monetary autonomy is necessary for monetary easing. Latin America and Southeast Asia were able to devalue their currencies, increasing the attractiveness of exports while lowering interest rates, thus engaging in quantitative easing. Much of Eastern Europe was constrained by the strength of the Euro. Unable to lower their current account balances through currency manipulation, interest rates remained too high for constituents during a recession and private debt skyrocketed.

Nevertheless, there is opportunity in crisis. If Eastern European countries were to emulate the steps taken by other emerging economies in past decades, they could better prepare their fiscal and monetary capacity and limit political and economic fallout in the next downturn. Addressing these issues is of the utmost importance as emerging economies prepare for the US to begin tapering interest rates and the strengthening of the dollar.

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¹ Table 1.

Growth Rate	Case Studies	Policies
Quick Recovery > 6% GDP growth	Brazil, Malaysia, Indonesia	Hybrid, structural, industrial, capital controls
Moderate Recovery 3-6% GDP growth	South Korea, Thailand	Monetary autonomy, foreign currency reserves
Little to No Recovery < 3% GDP growth	Argentina, Greece, Hungary	Populist, global governance constraints