A Great Deal of Ruin

A Great Deal of Ruin provides an accessible introduction to the enduring problem of financial crises. Illustrated with historical analysis, case studies, and clear economic concepts, this book explains in three parts what financial crises are, how they are caused and what we can learn from them. It begins with a taxonomy of crises and a list of factors that increase the risk for countries experiencing a financial crisis. It then examines five of the most important crises in modern economic history, beginning with Great Depression and ending with the Subprime Crisis in the United States and its evolution into a debt crisis in the Eurozone. The book concludes with a set of lessons that can be learnt from the crises of the past. It will appeal to university students as well as general readers who are curious to learn more about the recent Subprime Crisis and other financial crises.

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Financial Crises since 1929

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UNIVERSITY PRESS

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Shaftesbury Road, Cambridge CB2 8EA, United Kingdom

One Liberty Plaza, 20th Floor, New York, NY 10006, USA

477 Williamstown Road, Port Melbourne, VIC 3207, Australia

314–321, 3rd Floor, Plot 3, Splendor Forum, Jasola District Centre, New Delhi – 110025, India

103 Penang Road, #05–06/07, Visioncrest Commercial, Singapore 238467

Cambridge University Press is part of Cambridge University Press & Assessment, a department of the University of Cambridge.

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www.cambridge.org
Information on this title: www.cambridge.org/9781108739900

DOI: 10.1017/9781108608589

First published 2019

A catalogue record for this publication is available from the British Library

ISBN 978-1-108-49734-3 Hardback
ISBN 978-1-108-73990-0 Paperback

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Preface

In the 1970s, problems of economic instability and crisis began to be pushed into the background of the discipline of economics and replaced by a focus on economies in stable equilibria at full employment. This viewpoint has ample theoretical justification, but as an economist with a background in historical studies, I have a natural skepticism toward stories of long run equilibrium, or quick recoveries from a collapse of the macroeconomy. In the first years of my career, I was continually puzzled by the fact that twenty miles from where I worked was another world where the Mexican economy took nearly a decade to emerge from a crisis that cut wages in half and threw millions back into poverty. Plus, there was the problem of Japan in the 1990s. After several decades of spectacular growth on what appeared to be a stable trajectory that would soon surpass the United States in GDP, Japan fell into a lost decade of intractable economic problems. Solid institutions and competent macroeconomic management did not seem to be enough to avoid a prolonged crisis. While Japan was struggling to emerge from its problems, a group of institutionally strong, fast growing, stable models of economic development in East Asia experienced sudden and catastrophic breakdowns and then came the Subprime Crisis that many thought could never happen.

Watching the difficulties of regaining growth in Latin America, Europe and the United States, puzzling over the lost decade in Japan, and studying the collapse in East Asia, confirms my view that market economies have more than a little instability baked in, and that the natural tendency to return to full employment after a recession or a crisis could be obstructed by far more than simple human error or misguided government policies. If history teaches anything, it is that the world is a lot messier and more complex than the one described by economic theories emphasizing equilibrium and full employment.

Economic theory is a powerful tool for understanding the world but it requires institutional and historical context, as well as a sense of the limits to theoretical models, in order to avoid falling into scholasticism. I am fortunate that both my undergraduate and graduate programs were in universities where economic history was valued and taught beyond the bare minimum. And, in the university where I teach, I had the luck to become the "accidental director" of the Latin American Studies program. That good fortune gave me the opportunity to travel in Latin America, especially Mexico, to talk with scholars and friends abroad, and to think about the problems of economic instability from outside the lens of the US economy.

In 2009, colleagues in La Paz, Mexico, invited me to give a paper on the Subprime Crisis as part of a conference on that topic. I want to thank Antonina Ivanova, Alba Eritrea Gamez, and Manuel Ángeles for the opportunity to begin developing some of the ideas in this book. Shortly thereafter, I created a course on the subject of financial crises which enabled me to develop a set of topics for teaching about the Subprime Crisis and other historical episodes. I thank my colleagues for the space to develop this course. I benefited greatly from the several semesters of students who read earlier pieces of this work and provided feedback and discussion. In 2012, Rosio Barajas and Eduardo Mendoza at the Colegio de la Frontera Norte invited me to give a paper on the Eurozone Crisis and lessons from Mexico's experiences with debt and currency crises. I am thankful to them for their invitation and their spirit of collaboration. My colleague and friend Miguel Montoya at the Tecnológico de Monterrey, Campus Guadalajara, let me try out ideas as an invited lecturer in his Masters in Engineering Management program and the results became the genesis of the present work. The book took further shape when my friend Tom Passananti suggested we collaborate on an historical comparison of the financial sector policies of Mexico and Brazil in the 1890s. Tom later suggested we look at the impact of the Panic of 1907 on the Mexican Revolution.

I am grateful for these opportunities and for the friendship and support of my colleagues. Needless to say, I alone am responsible for the mistakes and errors of the current volume.

Academic colleagues and friends are essential but even more so is the support of my wife, Marion. For her patience, her enthusiasm, and her love, I am forever indebted.