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Measuring and Forecasting Financial Stability

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Comments on „Twin Crisis: An Examination of the Empirical Links“

Comments on:

**Twin Crises: An Examination of the
Empirical Links**

by Jürgen von Hagen and Tai-kuang Ho

Data

- 49 countries, 1980-2004 , unbalanced(?)
- 85 currency, 63 banking, and 27 twin crises
- Quite much: on average: a crisis every 5 years
- Crisis definition:
 - EMPI and IMP (von Hagen&Ho 2007)
 - Symmetric treatment of BC and CC
 - less sample bias than market event indices
- Sensitivity analysis (?)

Main Results

1. Banking crises: high in early 80s and 90s, low between (i.e. **not** a **new** phenomenon)
2. Banking crises are **equally likely to lead or to follow** currency crises, and vice versa
3. Banking crises and currency crises are **symmetric** in helping to predict follow-up crises of the other kind.

Timeline

- (1) Most empirical literature finds less crises in the early 80s
- (2) von Hagen & Ho's results differ from the result of other empirical studies
- Are the results driven by the crises in the 80s?
- Naiv question: (a) Are the crises of the 80s structurally different or (b) is the environment of the 80s different from the 90s?
- (a) different balance sheets in the 80s, less hedging instruments (positive or negative)
- (b) e.g. new/stronger contagion channels

Empirical results

- Definition of recovery: return to trend growth
What if growth remains a little lower?
- Two-step algorithm to estimate simultaneous equations: Endogeneity problem
- Currency crises are have larger output losses than twin crises. Why? Endogeneity problem?
Suggestion:
 - Control for macro variables
 - Business cycle component / change in growth

Summary

- Very interesting paper
- A pleasure to read
- New and important results
- Comprehensive and exact empirical analysis
- High potential to dig deeper and find even richer results