

CHARTICLE

First Thailand. Then Malaysia, Indonesia, Korea, the Philippines and Brazil. Next Venezuela? Argentina? China? Poland?

By **JAMES R. BARTH, DAN BRUMBAUGH and GLENN YAGO**

Currency contagion: less than meets the eye?

"Contagion" is the bogeyman of the hour. By most accounts, the currency crises that swept through Asia of irrational fears. Sure, all the affected economies had problems, but the immediate cause of the capital flight was panic as investors followed the herd into dollars and yen and D-marks. No emerging economy will be safe until the herd is back in the corral.

Or so the story goes.

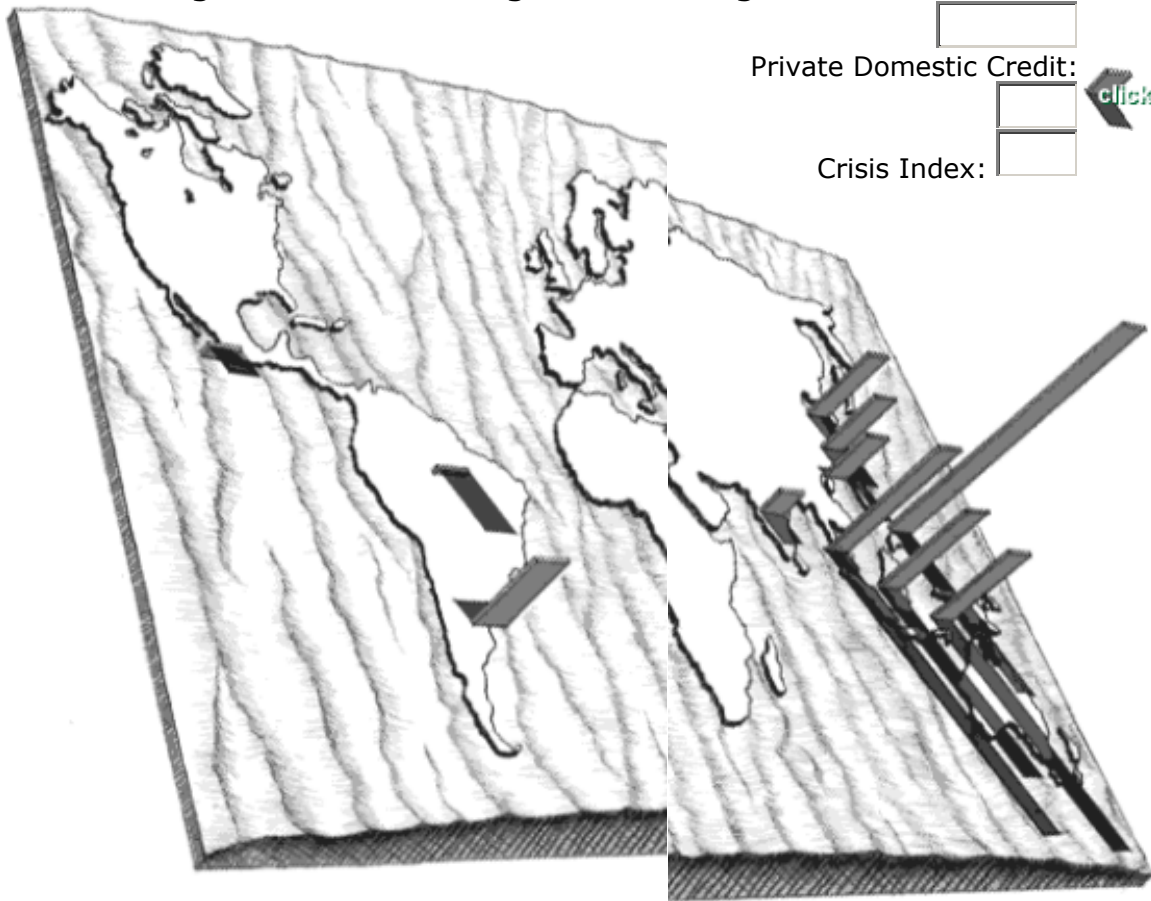
There's just one catch: events long before the collapse of the Thai baht seem to predict the severity of the currency crisis in a variety of countries. Check out our (admittedly crude) Crisis Index.

The index is calculated as the sum of the percentage depreciation of the local currency plus the percentage of foreign exchange reserves lost from May through November of 1997. Now compare the crisis index to the percentage change in outstanding domestic credit from 1992 through 1996.

The growth of (mostly bank) lending looks like a pretty good proxy for the accumulation of bad debt on lenders' balance sheets.

Maybe there was method to investors' madness. Maybe investors deserted emerging markets with the most serious problems and stayed the course in markets that had kept a lid on crony capitalism such as Hong Kong and India.

Profligate Bank Lending Cast A Long Shadow Over Asia



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