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What Explains the Speed of Recovery from Banking Crises?

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Highlights

- This paper uses event history analysis in order to identify factors that are related with the speed of recovery from banking crises (i.e. the time it takes to reach pre-crisis income levels)
- Regarding domestic factors, simultaneous currency crises, large financial sectors, primary deficits and overvalued currencies are correlated with later recovery
- Regarding external factors, a low growth of world trade as well as indicators of uncertainty in financial markets are associated with later recovery
- Global interest rate shocks are harmful for the speed of recovery among middle income countries

Abstract
While a large body of research has explored the causes and effects of banking crises, less is known about what determines recovery from banking crises, despite large variations in post-crisis performances across countries. In order to identify local and global factors that determine the length of recovery (i.e. the time it takes until countries reach their pre-crisis level of per capita GDP), this exploratory paper employs event-history analysis on 138 incidents of banking crises between 1970 and 2012. Regarding domestic factors, the simultaneous occurrence of currency crises, large financial sectors, overvalued currencies and large primary deficits are associated with later recovery, whereas higher debt-to-GDP ratios or inflation levels do not exhibit a negative effect on post-crisis performances. Regarding external factors, a low growth of world trade as well as indicators of uncertainty in financial markets are correlated with later recovery. Global interest rate shocks are particularly harmful for the speed of recovery among middle-income countries with a strong reliance on external capital. The results are similar when using the length of recessions as an alternative indicator of post-crisis performances.
Keywords: banking crises; recovery; duration analysis

JEL Classification: H12, E44, O23

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