
BOOK REVIEWS

Systemic Financial Crises: Containment and Resolution Edited by Patrick Honohan and Luc Laeven, Cambridge University Press, 2005, pages 384+XI

Increase in inflation variability and exchange rate volatility after 1971, and financial and macroeconomic liberalization in weak institutional environment during the last three decades increased the vulnerability of banking system more than other sectors. Banking crises of systemic importance increased in frequency and in severity, during the last quarter of the previous century as compared with earlier historic periods. The costs of the banking crises have been large, part of which has been borne by shareholders and depositors but most of it have been assumed by the governments. In addition to that fiscal cost, banking collapses have contributed to prolonged economic downturns and worsening of poverty. Predicting systemic banking crises is by no means an easy task even in the existence of some sophisticated models as they have proved to be unable to predict crises out of sample with any degree of success.

Systemic banking crises are not all the same but they are not all the different either and thus have a lot to learn from the way they have been handled to minimize their spread and diminish the losses caused by them. *Systemic Financial Crises: Containment and Resolution*” edited by Patrick Honohan and Luc Laeven presents the experiences of scholars most of which have been directly or indirectly involved in various financial sector assistance programs of various types for distress countries.

Nine chapters of the book are divided into four parts. In Part I, Patrick Honohan and Luc Laeven, drawing on the findings of the rest of the book, trace the decision points of the typical banking crisis. They offer a brief review of the scale and intensity of recent crises, distinguish the containment and resolution phases of the crisis, and discuss the theoretical and empirical models. Given the institutional weakness that contribute to both the frequency and depth of banking crises, this part of the chapter emphasize on the structural reforms in order to build an environment that can resist the crisis or at least ease it resolution.

Part II of the book deals with the containment and resolution of the crisis. The analyses presented in three chapters of this part of the book serve to emphasize the difficulties of implementing an effective containment and resolution strategy. Because the best policy actions depend on the nature of the crisis as well as the state of the national institutions, and because many irreversible decisions are

necessarily taken at speed under pressure of events, authors have emphasized the importance of having maximum information (especially about the condition of the banks), a good contingency plan (in terms of institutional lines of authority) and a clear cut picture of trade-offs that may be expected.

Though the diversity of banking crises means that case study approach is best for learning the lessons but in this book help has also been sought from theory and econometrics. Chapters 5 and 6 which constitute Part III of the book provides an insight using mathematical modeling and cross country econometric study. The complexity of the behavioral interaction between bankers, their customers and regulator is such that theory often generates ambiguous predictions. Thus, there is no substitute for looking at the available data.

Part IV highlights some of the distinctive structural features and financial reforms that may influence country's ability to weather a financial shock or prevent future crises. The presence or not of foreign banks, their entry in response to crisis, and their preparedness to ride out trouble is one of these dimensions. Another is the nature of the bankruptcy law. The last chapter, by Joe Peek and Eric Rosengren, presents as a case study of Japan which is often seen as being stuck in a chronic banking crisis. In the end of the book 'Banking Crisis Database' compiled by Gerard Caprio, Daniela Klingebiel, Luc Laeven, and Guillermo Noguera is also given which is extremely useful for further research in the area of financial crisis as the lessons of experience are complex and may not yet be fully distilled.

Systemic Financial Crises: Containment and Resolution is an excellent reading equally for policy makers in central banks as well as in finance ministries and for academia as it guides through how policy makers facing systemic financial crises made difficult decisions under pressure. Those who are lucky like Pakistan and have not faced any such crises during the period considered in this book can also learn from the lessons of others and continue to be lucky in this regard.

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