

Abstract

Could the cost of the 1994 Mexican banking crisis have been lower had the government reacted differently and, if so, how much lower? This paper addresses this question by looking at the Mexican crisis in comparative perspective. Forty crisis episodes around the world were statistically analyzed and the results used to evaluate the Mexican case. A robust association was found between crisis fiscal costs and government policy. Measures such as liquidity support, re-capitalization, and relaxation or non-enforcement of regulation/supervision significantly increase fiscal costs. There is also empirical support for the hypothesis that the nature of the regulatory environment may exercise a negative effect on the capacity of banks to quickly recover from crisis situations. Finally, evidence was found to support the idea that certain policies may lead to even more expensive crises when they are implemented in unreliable legal environments. The Mexican case is, overall, no exception in these regards. The fiscal cost of the 1994 Mexican crisis could have been lower had the government opted for a more limited policy strategy. Better systems of property rights protection and contract enforcement could have also induced a less expensive crisis.