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## This Time It's Not Different

By **Kenneth Rogoff**

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Feb. 16 issue - From the way money is now pouring into middle-income countries, like Brazil, China and Turkey, people must believe that we won't see another international debt crisis until the next sighting of Halley's comet. Has everybody forgotten about Mexico (1994); Thailand, South Korea, Indonesia and others (1997); Russia (1998); Brazil (1999); Argentina (2001); Turkey (2001), and Brazil (2002)? They shouldn't. According to a foreboding study issued last fall by the International Monetary Fund (when, incidentally, I was still chief economist there), at least a dozen other emerging markets have more debt than they can handle. Simply put, the average emerging-market country has a debt-to-income burden similar to that of a rich country, pyramided on lower exports and a tax base less than half as large. A recipe for catastrophe.

Yes, there are exceptions. Brazil, for example, has gotten pretty good at collecting taxes. And yes, the task of judging whether a country can outgrow its debt burden is not a science. Country defaults have complex social and political dimensions, and I have yet to see any framework that can convincingly name the time or place of the next big crisis. But one didn't have to be Nostradamus to foresee Argentina's recent collapse. Facing persistent budget deficits and volatile world prices for its goods, Argentina fought in vain to maintain a rigid currency peg to the dollar. Only the United States can print dollars.

Are the investment geniuses of the world concerned? It is hard to see it in the interest rates they are charging corporations and governments in emerging markets. When Brazil was on the brink of collapse in August 2002, and before it was bailed out by a \$45 billion loan from the IMF, it had to pay a whopping 24 percent premium above U.S. Treasuries. Now? Just above 4 percent extra, not that much larger than the spread many individuals pay on their mortgages. Does that make sense, given these countries' checkered credit histories? Let me tell you, it is *a lot* easier for the local bank to seize your house or car than it is for Citibank to get to a deadbeat sovereign debtor.

Some say this time is different. Exchange rates are more flexible, global markets are deeper—something akin to Fed chairman Alan Greenspan's remarkably sanguine view about why the world shouldn't worry about voracious American borrowing. Well, as University of

Maryland professor Carmen Reinhart has quipped, "this time is different" has oft proved the four most expensive words in the English language. Debt crises are as old as international lending, and call me crazy, but I don't think we are going to have to wait too long for the next one.

Do people really think the post-1994 period was an aberration? Do they know that Argentina has defaulted five times since its birth in the 1820s, Brazil seven times, Mexico eight times, Turkey seven, Venezuela nine, etc.? Speaking of Venezuela, I can sort of understand why investors are inspired by leftist turned centrist Brazilian President Luis Inacio Lula da Silva. But why are they equally inspired by Venezuela's erratic Hugo Chavez? Right now they are charging both countries similar interest rates. Somehow I don't think there is a lot of discrimination across borrowers going on here.

What, then, underlies this apparent collective insanity? Yes, there have been some good policy changes, but the main factor, I am afraid, is that rich-country interest rates are still stunningly low, even allowing for global disinflation. Craving higher returns, global-portfolio funds are increasingly washing up on the shores of distant emerging markets. With growing world demand once again soaking up emerging-market exports, and with low interest rates making debt finance easy, debtor countries have the best of both worlds. But it is not going to last. Eventually rich-country interest rates have to climb, and when they do, some developing countries are going to get slammed.

So what is to be done? Investors ought to realize that last year's 55 percent average return on emerging-market debt was an aberration. Developing-country leaders need to realize that borrowing is like taking steroids: it gives countries a short-term performance boost but leads to insidious long-term problems. Look at the modern history of most Latin American countries. And rich-country leaders need to start thinking about ways to make it more difficult for foreign creditors to enforce claims in rich-country courts and make it harder for developing countries to borrow. Some good proposals have been out there for 25 years. Last but not least, institutions like the IMF have to try to relitigate themselves from the last round of crises (that is, get repaid by some countries) in order to get ready for the next round. This time it's different? Sure, right.

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