Principles of Banking and Finance

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Class teachers: Artem V. Arkhipov, Evgeny V. Andreev, Anna S. Bogdyukevich, Kristina A. Budkevich

Course description

The course Principles of Banking and Finance is an introductory course on banking and financial markets for students. The course is taught in English, students need to pass an exam in external program of the LSE.

The course applies analytical approach, aimed at developing the economic way of thinking, makes the careful step-by-step introduction of different analytical models, uses a number of applications and examples from different banking systems. Prerequisites for the course are micro- and macroeconomics.

Teaching objectives

The objective of the course is to acquaint students with the principles of the financial theory, traditional and modern financial assets, types of financial intermediaries and the ways of their functioning in the modern financial markets.

The study of banking and financial markets has become one of the most interesting topics in economics. Financial markets are changing rapidly, and new financial instruments appear almost daily. The once staid financial industry has become highly dynamic. These developments in financial markets have created an integrated world economy in which events in one country’s financial markets have a major impact on financial markets in other countries. The development of the economic systems are determined by the international capital flows, channeled by banks and other financial intermediaries.

The boundaries between commercial and investment banks are disappearing while competition in financial sector is becoming global. Lots of factors, e.g. innovations, technologies, taxes and regulation, help to decrease barriers for capital flows. In 2008 these trends culminated in the world financial crisis which illuminated the most weak points in regulation, accounting, risks analysis, and other aspects off banking.

The course’s analytical framework uses a few basic economic principles to organize students’ thinking about bank management and the structure of financial markets. The basic principles are a transactions cost and asymmetric information approach to financial structure, profit maximization, basic supply and demand analysis to explain behavior in financial markets, and aggregate supply and demand analysis.

We aim to prepare students to study more complicated courses of the financial management and BORA, as well as investment portfolio management.
As a result, they must be given the principles of the investor’s behavior, of the banking regulation; taught the types of financial risks and the basic methods of their assessment and management. The seminars re based both on the detailed analysis of the banking practice and the analysis of the case studies.

Assessment

- Home assignments (14 sets)
- Intrasemester control tasks and exams
- Mock exams (150 and 180 min.)
- Winter exam (180 min.)
- External (UoL) exam

Grade determination

Students should pass the 2 intermediate Mock written exam in the end of each semester. The final exam will be held by the LSE. Each exam includes the list of 8 questions, from which the students will be asked to answer 4. Some questions may contain both numerical and essay-based parts. Each intermediate exam accounts for 20% of the final grade. Homework grades and graded received at classes account for 10% of the final grade. The rest of the final grade will be determined by the results of the final exam.

Fall semester is graded on the basis of home-assignments (15%), mock exam (25%) winter exam (50%) and class-work (10%).

Internet resources and databases

1. www.imf.org
2. www.worldbank.org
3. econ.lse.ac.uk
4. www.bis.org
5. www.nber.org
6. www.thebanker.com
Course outline

Principles of Finance

1. Consumption and investment with and without capital markets
   Consumption and investment without capital market (one person / one good economy). Production possibility frontier. The condition of the optimal allocation (utility maximization).
   Consumption with capital markets. Interest rate as the price of deferred consumption or the rate of return on investment. Fisher separation theorem. The condition of the optimal allocation (utility maximization). Types of consumers.
   Main reading:

2. Capital Budgeting and Valuation
   Methods of project’s valuation. Cash Flows. The concept of present value. Discount rate. NPV. IRR and required rate of return. Payback period. Main Reading
   Main reading:

3. Risk and return
   Main reading:
   2. Фрэнк Дж. Фабоцци. Управление инвестициями. Инфра-М, Москва 2000, Гл. 4

4. Asset pricing theories
   **Main reading:**
   2. Уильям Ф. Шарп, Гордон Дж. Александер, Джеффри В. Бэйли. Инвестиции. Инфра-М, Москва 2001, Гл. 9, 10, 12.

5. Financial Markets and Instruments
   **Main reading:**

6. Efficient markets

**Principles of Banking**
7. Economic analysis of financial structure


**Main reading:**


8. Financial intermediation


**Main reading:**


2. Фрэнк Дж. Фабоцци. Управление инвестициями. Инфра-М, Москва 2000, Гл. 8–11.


9. Bank management: retail, wholesale, investment banks

Retail banking: current account and time deposits, micro-financing, consumer loans, mortgages, asset-backed securities, payment and credit cards.

Wholesale banking: large-scale loans, trade financing, loan commitments, commercial and standby letters of credit, asset management, syndicated loans, arrangement and underwriting of corporate bonds.

Investment banks: structure of transactions, risk sharing, syndicated loans, arrangement and underwriting of bonds.

**Main reading:**


10. Risk management and internal control in banks


Interest rate margin. Interest rate risk. Fixed- and floating-rate assets and liabilities. Interest rate gaps.
Credit risk. Types of credit risk (industrial, regional and country risks). Diversification of loan portfolio.

Currency risk. Long and short open positions.

Capital adequacy. Economic capital.

Main reading:


11. Banking regulation


Banking crises.

Main reading:


12. Financial Systems Compared


Main reading:


Distribution of hours

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<th>#</th>
<th>Topic</th>
<th>Total hours</th>
<th>Contact hours</th>
<th>Self study</th>
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<td>Financial markets and instruments</td>
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