ICEF, Higher School of Economics, Moscow
Master Programme, Academic Year 2016-2017

Banking
Course Syllabus

Lecturers: Dr. Luca Gelsomini (e-mail: lgelsomini@hse.ru)
Dr. Vladimir N. Sokolov (e-mail: vsokolov@hse.ru)

Part 1. Banking: Theoretical part

Lecturer: Dr. Luca Gelsomini (e-mail: lgelsomini@hse.ru)

Objective

Part 1 of the course aims to provide an overview of the theoretical aspects of banking.

Outline

- Why financial intermediaries exist.
- The asymmetric information justifications of financial intermediation.
- The industrial organization approach to banking.
- The equilibrium of the credit market.
- Bank runs and the lender of last resort.
- Regulation and its justifications.

Methods of Learning

The following methods and forms of study are used in the course:

- Lectures
- Self-study

Literature

1. Readings:

Freixas X. and J.-C. Rochet, 2008. Microeconomics of Banking, Second Edition. Cambridge, Mass.: MIT Press.
Garber, P., and S. Weisbrod, 1992. The economics of banking, liquidity and money. Lexington, Mass.: D. C. Heath.
Greenbaum, S. I., and A. V. Thakor, 1995. Contemporary financial intermediation. Fort Worth, Texas: Dryden Press.
Mishkin, F. S., 1992. The economics of money, banking and financial markets. London: Scott, Foresman.

2. Further readings:

Hellwig, M., 1991. Banking, financial intermediation and corporate finance. In European financial integration, ed. A. Giovannini and C. Mayer. Cambridge: Cambridge University Press.

Prerequisites

As far as Part 1 of the course is concerned, a good knowledge of game theory and the basic concepts of modern finance is recommended.

Evaluation

Your performance in this course will be evaluated on the basis of the following criterions:

- Attendance
- In-class performance
- Exam

Grade Determination

For what concerns the first component (taught by Dr. Gelsomini):

- Weight of the attendance mark = (1/3)x(15%) of the overall mark
- Weight of the in-class performance mark = (1/3)x(15%) of the overall mark
- Weight of the final examination mark = (1/3)x(70%) of the overall mark

Banking: Empirical part

2nd year MSc Course
ICEF, NRU-Higher School of Economics

Lecturer: Vladimir Sokolov, Ph.D, e-mail vskolov@hse.ru: **-** Offce: 3420

Course Objective

This part of the banking course will cover the main empirical contributions that have been recently published in the academic journals. This material will illustrate how banking theories introduced in the first part of the course stand against the empirical evidence. The chosen topics are also intended to advance the students' understanding of the main regulatory debates regarding the role of banking industry in the economy.
The course starts with a review of the banks' financial statements and definitions of concepts that will be used in the following lectures. Then it covers the main activities of banks – lending and attracting deposits. The issues of credit rationing and relationship banking that have received a lot of focus in the academic literature will be highlighted. When covering the deposit attraction activities of banks the concept of bank runs and liquidity risk will be reviewed. This motivates assessment of the popular regulatory policy implemented in many countries - deposit insurance. We will discuss studies that investigate the moral hazard and risk shifting problems that arise due to deposit insurance policies. The last several lectures are related to the very active debate on prudent regulation of the banking industry that gained a lot of attention following the recent financial crisis. The banking theories often provide contradictory answers to the following questions that are very important to the regulators: Does policy of promoting higher competition among bank lead to banking sector stability? Do we need large or small banks? Do higher capital requirement imposed on banks lead to lower risk-taking by banks? What ownership structure leads to better corporate governance? The broad range of empirical papers that shed light on these questions will be discussed. In the end of the course each student will be present one academic paper on the issues covered in the course.

Grade determination for the empirical part of the course

5 %   Class participation
30 % Student presentations
65 % Final Exam

Grade determination for the whole course

40 % Theoretical part
60 % Empirical part

Main Readings

1. Degryse, H., Kim, M., Ongena, S., Microeconometrics of Banking: Methods, Applications and Results, Oxford University Press, 2009. (D)

2. Freixa, X., and Rochet, J-C., Microeconomics of Banking, The MIT Press, 2008. (F)

3. Academic journal articles listed below the corresponding topic

Course outline

- **Week 1. Overview of the bank's financial statements, measures of market power and bank's soundness**

  Non-performing loans, Bank reserves, Net interest rate margin, Hirschmann-Herfindahl index, CR3, Panzar-Rosse H-statistic, Lerner index, Z-score

  Readings: (D) Ch. 3; (F) Ch. 1-2
  Journal Readings:

1. Laeven, L., Levine, R., 2009. Bank governance, regulation and risk taking. J. Financial Economics 93 (2), 259–275.

2. Panzar, J.C., Rosse, J.N., 1987. Testing for monopoly equilibrium. Journal of Industrial Economics 35 (4), 443–456.

3. Roy, A.D., 1952. Safety first and the holding of assets. Econometrica 20 (3), 431–449.

4. Zhang, D., Cai, J., Dickinson, D., Kutan, A., (2016). Non-performing loans, moral hazard and regulation of the Chinese commercial banking system, Journal of Banking and Finance 63, 48-60.

- **Week 2. Bank lending**

  Loan pricing, Credit rationing, Adverse selection, Relationship lending, Risk overhang

  Readings: (D) Ch. 4-5; (F) Ch. 4-5
  Journal Readings:

1. Cenni, S., Monferra, S., Salotti, V., Sangiorgi, M., Torluccio, G., (2015). Credit rationing and relationship lending. Does firm size matter? Journal of Banking and Finance 53, pp. 249-265.

2. DeYoung, R., Gron, A., Torna, G., Winton, A., (2015), Risk Overhang and Loan Portfolio Decisions: Small Business Loan Supply before and during the Financial Crisis, The Journal of Finance, pp. 2451-2488.

3. Kirschenmann, K., (2016). Credit rationing in small firm-bank relationships, Journal of Financial Intermediation 26, pp. 68-99.

4. Berg, T., Saunders, A., Steffen, S., (2016). The total cost of corporate borrowing in the loan market: Don't ignore the fees, The Journal of Finance 71, pp. 1357-1392.

- **Week 3. Bank funding and liquidity risk**

  Deposit contracts, Market discipline, Bank runs, Liquidity insurance, Deposit insurance

  Readings: (D) Ch. 8; (F) Ch. 8
  Journal Readings:

1. Brown, M., Guin, B., Morkoetter, S., (2016). Deposit withdrawals from distressed commercial banks: the importance of switching costs, University of St. Gallen Working Paper 2013/19

2. DeYoung, R., and Jang, K., (2015). Do Banks Actively Manage Their Liquidity? CBE Research Paper 2015-1.

3. Iyer, R., and Puri, M., (2012). Understanding Bank Runs: The Importance of Depositor-Bank Relationships and Networks, American Economic Review 102, 1414-1445.

- **Week 4. Deposit insurance and banks' risk taking**

  Moral hazard, Liquidity regulation, Liquidity risk management, Liquidity coverage ratio

  Readings: (D) Ch. 7; (F) Ch. 9
  Journal Readings:

1. Anginer, D., Demirguc-Kunt, A., Zhu, M., (2014). How does deposit insurance affect bank risk? Evidence from the recent crisis, Journal of Banking and Finance 48, pp. 312-321.

2. Lambert, C., Noth, F., Schwer, U., (2016). How do insured deposits affect bank risk? Evidence from the 2008 Emergency Economic Stabilization Act, Journal of Financial Intermediation.

3. Boyle, G., Stover, R., Tiwana, A., Zhylyevskyy, O., (2015). The impact of deposit insurance on depositor behavior during a crisis: A conjoint analysis approach, Journal of Financial Intermediation 22, 590-601.

- **Week 5. Competition, risk taking, capital requirements**

  Competition-fragility hypothesis, Competition-stability hypothesis, Franchise or charter value of banks, risk-shifting problem, rationale for capital requirements, screening of borrowers

  Readings: (D) Ch. 7; (F) Ch. 3
  Journal Readings:

1. Beck, T., De Jonghe, O., and Scepens, G., (2013) Bank Competition and Stability: Cross-country Heterogeneity, Journal of Financial Intermediation 22, 218-244.

2. Boyd, J.H., De Nicolo, G., 2005. The theory of bank risk taking and competition revisited. Journal of. Finance 60 (3), 1329–1343.

3. Hellmann, T.F., Murdock, K.C., Stiglitz, J.E., 2000. Liberalization, moral hazard in banking, and prudential regulation: are capital requirements enough? American Economic Review 90 (1), 147–165.

4. Martinez-Miera, D., Repullo, R., 2010. Does competition reduce the risk of bank failure? Review of Financial Studies 23 (10), 3638–3664.

- **Week 6. Banks' size, Too-Big-to-Fail**

  Economy of scale, Too-Big-to-Fail (TBTF)

  Journal Readings:

1. Bertay, A., Demirguc-Kunt, A., Huizinga, H., (2013). Do we need big banks? Evidence on performance, strategy and market discipline. Journal of Financial Intermediation 22, 532-558.

2. Davies, R., Tracey, B., (2014). Too Big to Be Efficient? The Impact of Implicit Subsidies on Estimates of Scale Economies for Banks, Journal of Money, Credit and Banking 46, 219-253.

3. Hughes, J., and Mester, L., Who said large banks don't experience scale economies? Evidence from a risk-return-driven cost function, Journal of Financial Intermediation 22, 559-585.

4. Wheelock, D., and Wilson, P., (2012). Do Large Banks Have Lower Costs? New Estimates of Returns to Scale for U.S. Banks, Journal of Money, Credit and Banking 44, 171-199.

- **Week 7. Bank capital and regulation**

  Capital structure of banks, capital regulation, regulatory capital, Basel accords, risk-weighted assets

  Readings: (D) Ch. 9; (F) Ch. 9
  Journal Readings:

1. Berger, A., DeYoung, R., Flannery, M., Lee D., and Öztekin, O,. (2008). How Do Large Banking Companies Manage Their Capital? Journal of Financial Services Research 34, 123-149.

2. Berg, T., and Gider, J., (2016). What determines the leverage between banks and non-banks? Journal of Financial and Quantitative Analysis.

3. Gropp, R., and Heider, F. (2010), The determinants of bank capital structure, Review of Finance 14, pp. 587-622.

4. Mariathasan, M., and Merrouche, O., (2014), The manipulation of Basel risk-weights, Journal of Financial Intermediation 23, 300-321.

- **Week 8. Bank ownership and governance**

  Government ownership of banks, cooperative banks, corporate governance of banks

  Journal Readings:

1. De Haan, J., and Vlahu, R., (2015). Corporate governance of banks: A survey, Journal of Economic Surveys, pp. 1-50.

2. Laeven, L., and Levine, R., (2009), Bank governance, regulation and risk taking, Journal of Financial Economics 93, 259-275.

3. Micco, A., Panizza, U., and Yanez, M., (2007), Bank ownership and performance. Does politics matter? Journal of Banking and Finance 31, 219-241.

4. Sapienza, P., (2004), The effect of government ownership on bank lending, Journal of Financial Economics 72, pp. 357-384.

- **Week 9-10. Student's presentations of academic papers**