

Current Topics and Modern Financial Markets

Syllabus

Approved by the Program Academic Council
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Protocol # 3

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Course information

Course Website: my.nes.ru

Instructor's Office Hours: Room 2.11, Friday 11:00-12:00

Class Time: ---

Course description

The overall purpose of the course is to engage students into the discussion of current issues and challenges that global financial markets are facing in the aftermath of financial crisis. The course will touch on numerous public policy issues, many of which are politically controversial and most of which are likely to continue to be important for years to come. A goal of the course is to provide students with a framework within which these public policy issues can be addressed in a useful manner.

Course requirements, grading, and attendance policies

The course grade will be based on the following: participation in class, tests, regular homework assignments, and a final exam. Homework will be assigned every week. There is no textbook.

Readings: Students should read assigned materials before each class.
In-class Tests: At the beginning of each lecture (except the very first one), there will be short 10-minute tests with a question about material of the previous lecture. A goal of these tests is to help students not to fall behind on the material and to keep track of attendance. Make sure that you come on time.

Homework assignments: Each week students have to read required material and submit a short writeup with their answers on the questions. Don't expect to find all answers in the readings.
NOTE: Many readings represent official reports and documents, some of them are very long; as in real life, there is no need to read them line by line, rather those documents can be skimmed through but more important parts must be read carefully.

Case write-ups should be succinct and self-contained. Long write-ups are not necessarily good writeups. Good business writing makes points in a manner that respects the reader's time. Typically, the answers to questions will not be heavily mathematical, but mathematical intuition will often be required to address some of the questions. Write-ups should be uploaded onto mynes at the beginning of class, including the very first class. Students have to submit at least 5 out of 7 assignments.

If students submit all 7 assignments, then the best 5 are counted towards their final grade.

Students should be prepared to discuss and defend the ideas in their write-ups in class. Students should be prepared to discuss and defend the ideas in their write-ups in class. For some questions, there is no “right” or “wrong” answer, in the sense that finance and economics professors themselves are likely to disagree about the answers to the questions. Students may talk to other students about the assigned questions, but each student should prepare a write-up individually, without looking at the write-ups of other students. Each student should list on the write-up the names of the other students with whom the student discussed the write-up.

Class participation: Class attendance and participation are required. Each class several related financial concepts or theories will be discussed; students should review what they learned about these topics in other courses.

Final Test: A final 90-minute test is in-class and closed-book. One double-sided A4 cheat-sheet is allowed.

Grading: Grading will be based on case write-ups (20%), in-class tests (18%), class participation (12%), and a final test (50%). Missing class is strongly discouraged. Case write-ups are graded on a scale with the following interpretation: 0=missing, 1=okay, 2=good; 3=great

Methodology

Students are expected to read material before the class, submit write-ups on assigned questions, and participate in class discussions.

Sample of Test Questions

Label each of the following statements as TRUE, FALSE, or UNCERTAIN. For each statement, justify your answer with a few sentences or a brief paragraph.

Warren Buffett's and AIG's derivatives strategies were similar in that both firms conceptually sold disaster insurance, hoping that a disaster would not occur.

Questions for Case Write-Up:

1. According to Cunningham, what is the main difference between Berkshire and KKR?
2. Does Buffett believe that banks are more deserving of bailouts than other types of companies? Why or why not?
3. What are the similarities between Buffett's strategies and carry trades?
4. Explain similarities and differences between Warren Buffett's business model, AIG's business model, and Yale's investment strategy. Issues to consider include leverage, marking-to-market, hands-on management of companies, and perhaps other things (but save option writing for the next question).
5. One type of business model involves writing out-of-the-money options and hoping to make a profit from doing so. Writing insurance is an analogous strategy. According to Buffett, is this the way Berkshire Hathaway makes most of its money? Is this the idea behind Gary Gorton AIG's strategy, according to the FCIC report?
6. Compare Buffett's letter to shareholders for 2009 (published 2010), p.16 with the financial crisis inquiry

report, pp. 243-244. What does Buffett think about AIG management?
7. What does Buffett think is wrong with the Black-Scholes model? Is he correct?

Academic integrity policy

Cheating, plagiarism, and any other violations of academic ethics at NES are not tolerated.

Course contents

I. Abacus Deal, Financial Crisis 2008-2009

- Abacus deal as an example of a structured product
- Causes of financial crisis: Different views

II. Derivatives - Buffett vs AIG:

- Buffett's business model
- AIG business model
- Buffett's critique of Black-Scholes model

III. London Whale Case - Regulations after Financial Crisis

- Dodd-Frank Act in the US, MiFID in Europe, Basel III
- Bank regulations, banking industry sanitation
- London Whale case
- Stress testing
- Asset management industry as SIFIs and systemic risk

IV. Commodities Markets and Hedging:

- Current and future oil prices, how to interpret forward curves
- Hedging: Metallgesellschaft hedging debacle
- Price manipulations in commodities market
- Cash settlement and fixings
- Corners and squeezes: Silver crisis of 1981, VW squeeze in 2008
- Risk Management in Russia, barrier options

V. Structuring of Retirement Systems:

- Pension Systems, main issues
- Russian Pension System
- Debt crisis in Europe and US

VI. Government Finance:

- State loans and guarantees
- Public finance and option pricing

VII. Sovereign Wealth Funds and Review

- Sovereign wealth funds
- Lybia vs Goldman Sachs; DB mirror trades

Course materials

Required textbooks and materials

The course will require a lot of reading of various papers, reports, and official documents. Some of the readings are very long; there is no need to read them entirely from the first page to the last page, those readings can be just skimmed through, but most relevant and important parts have to be read carefully.

REQUIRED READING:

Last Berkshire-Hathaway Annual Report: <http://berkshirehathaway.com/letters/letters.html>

Board of Governors of Federal Reserve System, Dodd-Frank Act Stress Test 2016: Supervisory stress test methodology and results, June 2016:

<https://www.federalreserve.gov/newsevents/press/bcreg/bcreg20160623a1.pdf>

Dodd-Frank Act (full text): www.sec.gov/about/laws/wallstreetreform-cpa.pdf

VIDEO: (Senate Hearings on Goldman Sachs Case)
www.c-span.org/video/?293196-3/investment-banks-financial-crisis-goldman-sachs-chair-ceo
www.c-span.org/video/?293196-1/investment-banks-financial-crisis-directors
Warren Buffett's interview, www.youtube.com/watch?v=FPkX7S5z5t0
Senate Hearings on AIG:
www.c-span.org/video/?281644-1/aig-bailout-oversight-hearing-panel-1
www.c-span.org/video/?281644-2/aig-bailout-oversight-hearing-panel-2
Выступление Эльвиры Набиуллиной на XXV Международном Финансовом Конгрессе <https://www.youtube.com/watch?v=w153NjW2w8Q>
Round table on pension reform: <https://www.youtube.com/watch?v=5Bz9hxIK5gU>
David Swensen's lecture at Yale, "Guest Speaker David Swensen"
www.youtube.com/watch?v=wRdx7kVNQ_E

Special Equipment and Software Support:

The following software programs from local HSE network (by contract) will be used in class:

- Microsoft Windows 7 Professional RUS or
- Microsoft Windows 10 or
- Microsoft Windows 8.1 Professional RUS

The multi-media projector will be required for presentations as well.