

Stockholm School of Economics / Swedish House of Finance

Doctoral Mini-Course

New Ideas in Banking and Corporate Finance

Enrico Perotti, UvA and CEPR

2019

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Location: Room “Fama” at Swedish House of Finance

Dates: April 1 – 3, 2019 (detailed schedule TBA)

This course is for 3.75 ECTS. Mode of assessment TBA.

Course Outline

The course reviews some classics and novel work in financial intermediation and related and related themes in corporate finance. It combines a classic contractual approach with recent work on system-wide risk creation.

Drawing from the lesson of the crisis, it focuses on the risk transformation role of banks and shadow banks and the sources of endogenous credit risk.

Topics include debt optimality and induced moral, external effects of bank funding and credit, maturity and liquidity risk transformation, endogenous risk cycles, and the novel literature on demand for safety. Recent work on firm demand for credit completes the broad framework. Time allowing, we will cover the implications for capital and liquidity regulation.

Requirements

None. Recommended: Contract Theory, Corporate Finance

Course Material

No stars indicate complementary readings. * One star indicates mandatory readings to be studied carefully outside technical details. ** Two star readings require understanding technical derivation.

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Advanced mandatory reading (before the first class)

- Myerson, Roger B. "Rethinking the Principles of Bank Regulation: A Review of Admati and Hellwig's The Bankers' New Clothes." *Journal of Economic Literature* 52.1 (2014): 197-210.

Lecture 1

Cost of Bank Equity & Optimality of Debt

Debt Enforcement: Bank Monitoring & Monitoring the Bank

- * Dang, Tri Vi, et al. "Banks as secret keepers." *The American Economic Review* 107.4 (2017): 1005-1029.
- * Gale, D, and M Hellwig (1985), "Incentive Compatible Debt Contracts: The One Period Problem," *Review of Economic Studies*, 52, pp 647-663
- Hart, O. and J. Moore (1998, February). Default and renegotiation: a dynamic model of debt, *Quarterly Journal of Economics* 93(1), 1–41.
- ** Holmstrom, B, and J Tirole (1997), "Financial Intermediation, Loanable Funds, and the Real Sector," *Quarterly Journal of Economics*, 112, p 663-691
- Diamond, D. W. and Rajan, R. G. (2001), 'Liquidity risk, liquidity creation, and financial fragility: A theory of banking', *Journal of Political Economy* 109(2), 287–327.

Lecture 2

Optimal Demandable Debt & Bank Runs

- ** Diamond, Douglas and Philip Dybvig (1983), "Bank runs, deposit insurance and liquidity," *Journal of Political Economy*, 91: 401-419
- ** Brunnermeier, Marcus, and Martin Oehmke (2012): "The Maturity Rat Race," *Journal of Finance*, (2013)
- * Brunnermeier, Markus, "Deciphering the Liquidity and Credit Crunch 2007–2008",
- Goldstein, Itay "Empirical Literature on Financial Crises: Fundamentals vs. Panic", in *Evidence and Impact of Financial Globalization*, edited by Gerard Caprio (Elsevier, Amsterdam), pp. 523-534, December 2012
- Goldstein, Itay and Ady Pauzner, Demand Deposit Contracts and the Probability of Bank Runs", *Journal of Finance*, vol. 60(3), pp. 1293-1328, June 2005
- Matta, Rafael and Enrico Perotti (2018), "Efficient Mandatory Stay", mimeo, University of Amsterdam

Lecture 3

Demand for Safety

- Caballero, Ricardo, and Emmanuel Farhi. "The safety trap." *The Review of Economic Studies* (2017): rdx013.
- ** Caballero, R. and A. Krishnamurthy. Global imbalances and financial fragility. *American Economic Review*, 99(2):584–88, 2009.
- ** Krishnamurthy, Arvind and Vissing-Jorgensen, Annette, (2012), The Aggregate Demand for Treasury Debt, *Journal of Political Economy*, 120, issue 2, p. 233 - 267
- * Ahnert, Toni and Enrico Perotti. Intermediaries as Safety Providers. University of Amsterdam Working Paper, 2017.
- Ahnert, Toni and Enrico Perotti. Cheap but Unstable, University of Amsterdam Working Paper, 2015

Lecture 4

Systemic Risk and Correlated Distress

Principles of Macroprudential policy

Aggregate Risk Externalities and Liquidity Regulation

- * Adrian, T and H Shin (2010), "Liquidity and leverage," *Journal of Financial Intermediation*, 19, 418-437
- * Perotti, E, and J Suarez (2011), "A Pigovian Approach to Liquidity Regulation", *International Journal of Central Banking*

Assessing Excess Credit and Long Term Trends

- * Doettling, Robin and Enrico Perotti, E "Long Term Trends", Uva mimeo; revision of CEPR DP 2017
- * Enrico Perotti and Magda Rola-Janicka, "Funding Shocks and Credit Quality", Uva mimeo
- * Philippon, Thomas, and German Gutierrez, 2016, Investment-less growth: An empirical investigation, New York University working paper.
- Philippon, Thomas and German Gutierrez, 2017, Declining competition and investment in the US, New York University working paper.
- Martinez-Miera, David & Suarez, Javier, 2012. "A Macroeconomic Model of Endogenous Systemic Risk Taking," CEPR Discussion Papers 9134