

Seminar in Financial Institutions

OBJECTIVES

This seminar provides an exposure to the recent papers in a few of the interesting topics in banking, and more generally financial intermediation. During this semester, the topics covered will be grouped under the following topics (1) Theory of Banking (2) Bank Regulation, (3) Loan Contracting, (4) Contracting and Architecture, (5) Relationship Lending, (6) Securitization, (7) Contagion and Systemic Risk, (8) Banking and the Economy (9) Credit Risk, and (10) Banks and Corporate Governance. In addition to the papers assigned for presentation and detailed discussion in class, an extensive reading list of other related papers and surveys on each topic are also included.

GRADING

Final grades will depend on the quality of class participation and paper presentation, as well as a class paper that seeks to review and synthesize research in a particular area of financial intermediation. This paper must be submitted by February 2007.

Background Reading:

- Book:** Friexas and Rochet (1997), *The Microeconomics of Banking*, Cambridge and MIT Press.
1. O'Hara, M., 1983, "A Dynamic Theory of the Banking Firm," *Journal of Finance*, vol. 38, no. 1, 127-140.
 2. Boyd, J. and E. Prescott, 1986, "Financial Intermediary-Coalitions," *Journal of Economic Theory*, vol. 38, 211-232.
 3. Diamond, D., 1984, "Financial Intermediation and Delegated Monitoring," *Review of Economic Studies*, vol. 51, 393-414.
 4. Diamond, D. and P. Dybvig, 1983, "Bank Runs, Deposit Insurance, and Liquidity," *Journal of Political Economy*, vol. 91, no. 3, 401-419.
 5. Allen, F. and D. Gale, 1998, "Optimal Financial Crises," *Journal of Finance*, vol. 53, no. 4, 1245-1284.
 6. Bhattacharya, S. and A. Thakor, 1994, "Contemporary Banking Theory," *Journal of Financial Intermediation*, vol. 3, 95-133. **(Survey)**
 7. S. I. Greenbaum, 1996, "Twenty-Five Years of Banking Research", *Financial Management*, Summer, 86-92. **(Survey)**.
 8. Boot, A., 2000, "Relationship Banking: What Do We Know?" *Journal of Financial Intermediation*, vol. 9, 7-25. **(Survey)**

SEPT. 11: Organization and Assignments

SEPT. 18: Theory of Banking: Why do banks exist?

1. Diamond and Rajan, "Liquidity Risk, Liquidity Creation, and Financial Fragility: A Theory of Banking", *Journal of Political Economy*, 109,2, 287-
2. Philip Bond, "Bank and Nonbank Financial Intermediation", *Journal of Finance*, December 2004, 2489-2529.

SEPT. 25: Bank Regulation

1. Lucy White, "Is Deposit Insurance a Good Thing, and if so, Who Should Pay for It?" working paper.
2. F. Allen, E. Carletti, and R. Marquez, 2006, "Credit Market Competition and Capital Regulation," Wharton working paper.

Background Papers:

3. Hauswald and Senbet, "Public and Private Agency Conflict in Banking Regulation," November 1999.
4. Marshall and Prescott, "Bank Capital Regulation With and Without State-Contingent Penalties," September 2000.
5. Morrison, "Banking Licenses, Bailouts and Regulator Ability," July 2002.

OCT. 9: Loan Contracting I

1. J. Qian and Philip Strahan, "How Law and Institutions Shape Financial Contracts: The Case of Bank Loans," QJ and working paper January 2005.
2. E. Von Thadden, 1995, "Long-Term Contracts, Short-Term Investments and Monitoring," *Review of Economic Studies*, 62, pp. 557-575.
3. M. Garmaise and T. Moskowitz, "More Banks, Less Crime? The Real and Social Effects of Bank Competition," Working Paper (forthcoming *Journal of Finance*?)

Background Papers:

4. Rajan, 1992, "Insiders and Outsiders: The Choice Between Informed and Arms-Length Debt," *Journal of Finance* 47(7), 1367-1400.
5. Hackbarth, Hennessy, Leland, "The Optimal Mix of Bank and Bond Debt: An Asset Pricing Approach, September 2002.
6. Hubbard, Kuttner and Palia, "Are There Bank Effects in Borrowers' Cost of Funds? Evidence from a Matched Sample of Borrowers and Banks," *Journal of Business*, 2002, 75, 4, pp. 559-581.

OCT. 16: Loan Contracting II

1. Sufi, "Information Asymmetry and Financing Arrangements: Evidence From Syndicated Loans," October 2004, forthcoming *Journal of Finance*.
2. V. Ivashina, "The Effects of Syndicate Structure on Loan Spreads," working paper, June 2006.
3. M. Roberts and M. Bradley, "The Structure and Pricing of Debt Covenants," May 13, 2004, Duke University working paper.

Background Papers:

4. Hubbard, Kuttner and Palia, "Are There Bank Effects in Borrowers' Cost of Funds? Evidence from a Matched Sample of Borrowers and Banks," *Journal of Business*, 2002, 75, 4, pp. 559-581.
5. Berlin, M. and L. Mester, 1992, "Debt Covenants and Renegotiation," *Journal of Financial Intermediation*, 2, 95-133.
5. James, C. and Houston, J., 1996, "Bank Information Monopolies and the Mix of Private and Public Debt Claims," *Journal of Finance*, vol. 51, no. 5, December 1863-1889.

OCT. 23 Contracting and Architecture

1. M. Burkart, T. Ellingsen, M. Giannetti, "What You Sell is What You Lend? Explaining Trade Credit Contracts," November 2005 working paper.
2. D. Paravisini, "Constrained Banks, Constrained Borrowers: Bank Liquidity Constraints and Firm Access to External Finance," Columbia Working Paper, 2005.
3. Isil Erel, "The Effect of Bank Mergers on Loan Prices: Evidence from the US," MIT working paper, June 2005.

Background Papers:

4. Rajan and Petersen, "Does Distance Still Matter? The Information Revolution in Small Business Lending," March 2001.
5. Dell'Ariccia and Marquez, "Information and Bank Credit Allocation," *Journal of Financial Economics*, 2004, 185-214.
6. Stein, J., 2002, "Information Production and Capital Allocation: Decentralized vs. Hierarchical Firms," *Journal of Finance*, October.

OCT. 30: Relationship Lending I

1. Fields, Fraser, Berry and Byers, "Do Bank Relationships Still Matter?" *Journal of Money, Credit and Banking*, August 2006, pp. 1195-1210.
2. L. Mester, L. Nakamura, M. Renault, "Transactions Accounts and Loan Monitoring," forthcoming *Review of Financial Studies*.

Background Papers:

3. Berlin, M. and L. Mester, 1999, "Deposits and Relationship Lending," *Review of Financial Studies*, Fall, vol. 12, no. 3, 579-607.
4. Boot and Thakor, "Can Relationship Banking Survive Competition", *Journal of Finance*, April 679-713.
5. Madhavan, Marx, and Panchapagesan, 2003, "Relationship Markets and the Decision to Go Public" Washington University Working Papers

NOV. 6: Relationship Lending II

1. S. Ongena and D. Smith, "The Duration of Banking Relationships," *Journal of Financial Economics*, 2001.

2. Yasuda, “Do Bank Relationships Affect the Firm’s Underwriter Choice in the Corporate-Bond Underwriting Market?” *Journal of Finance*, vol. 60, issue 3, June 2005
3. Drucker, Steven and Manju Puri, 2005, “On the Benefits of Concurrent Lending and Underwriting,” *Journal of Finance*, vol. 60, issue 6, December 2005

Background Papers:

4. Detragiache, E., P. Garella, and L. Guiso, 2000, “Multiple Versus Single Banking Relationships: Theory and Evidence,” *Journal of Finance*, June, vol. 55, no. 3, 1133-1161.
5. Jean-Baptiste, “Information Monopoly and Commitment in Intermediary-Firm Relationships,” February 2001.

NOV. 13: Securitization

1. Peter DeMarzo, 2005, “The Pooling and Tranching of Securities: A Model of Informed Intermediation, *Review of Financial Studies*, 18,1,
2. Ayotte and S. Gaon, “Asset-Backed Securities: Costs and Benefits of ‘Bankruptcy Remoteness,’” May 2006 Working Paper.

Background papers:

3. Arping, “Playing Hardball: Relationship Banking in the Age of Credit Derivatives,” May 2002 working paper.
4. Bodnar, de Jong and Macrae, “The Impact of Institutional Differences on Derivatives Usage: A Comparative Study of US and Dutch Firms,” April 2002 working paper.

NOV. 20: Contagion/Systemic Risk

1. N. Chan, M. Getmansky, S. Haas, A. Lo, “Systemic Risk and Hedge Funds,” October 14, 2004 working paper.
2. Allen, F. and Carletti, 2006, “Credit Risk Transfer and Contagion” *The Journal of Monetary Economics*, 53, 89-111.
3. Yaron Leitner, “Financial Networks: Contagion, Commitment, and Private Sector Bailouts”, *Journal of Finance*, vol. 60, issue 6, December 2005.

Background papers:

4. Acharya and Yorulmazer, “Information Contagion and Inter-Bank Correlation in a Theory of Systemic Risk,” November 2002 working paper.
5. Bernardo and Welch, “Financial Market Runs,” September 2002.
6. Elsinger, Lehar, and Summer, “Risk Assessment for Banking Systems” August 2002 working paper.

NOV. 27: Banking and the Economy

1. Bo Becker, “Geographical Segmentation of US Capital Markets,” working paper.

- I.Serdar Dinc, "Politicians and Banks: Political Influences on Government-Owned Banks in Emerging Markets," *Journal of Financial Economics*, 2005, pp. 453-479.

Background papers:

- Kashyap, A. and J. Stein, 2000, "What Do A Million Observations on Banks Say About the Transmission of Monetary Policy?" *American Economic Review*, vol. 90, no. 3 June 407-428

DEC. 4:Credit Risk

- V. Acharya, S. Bharath, and A. Srinivasan, "Understanding the Recovery Rates on Defaulted Securities," April 2004 working paper.
- P. Collin-Dufresne, R. Goldstein, S. Martin, "The Determinants of Credit Spread Changes," *Journal of Finance*, December 2001.
- Frank de Jong and Joost Driessen, "Liquidity Risk Premia in Corporate Bond Markets," Working Paper November 14, 2005.

Background papers:

- Von Thadden, Berglof, and Roland, 2003. "Optimal Debt Design and the Role of Bankruptcy" Unversite de Lausanne Working Papers.
- Brunner and Krahen, "Multiple Lenders and Corporate Distress: Evidence on Debt Restructuring," July 2002.
- Gilsen, John, and Lang, "Troubled debt restructurings—An empirical study of private reorganization of firms in default" *Journal of Financial Economics* 26 (1990) 000-000. North-Holland.

DEC. 11:Banks and Corporate Governance

- Caprio, Laeven and Levine, "Governance and Bank Valuation," Working Paper. 2004.
- Santos and Rumble, "The American Keiretsu and Universal Banks: Investing, Voting and Sitting on Nonfinancials' Corporate Boards," Forthcoming in the *Journal of Financial Economics*.
- Allen, Franklin, Bartiloro, Laura and Kowalewski, Oskar, "Does Economic Structure Determine Financial Structure?" (February 2006). AFA 2007 Chicago Meetings Paper Available at SSRN: <http://ssrn.com/abstract=891313>

Background:

- Allen and Gale, "Banking and Markets," November 2000 working paper.
- Demirguc-Kunt and Levine, "Bank-Based and Market-Based Financial Systems: Cross Country Comparisons," 2004.