# Banking Theory

## Syllabus

**Teacher:** Silvio Petriconi, Bocconi University

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**Schedule:** April 30th, May 2nd and May 4th, 9:00-11:00am.

**Location:** 420 Uris Hall

**Prerequisites:** graduate-level microeconomics

## Course Description

This is a short "workshop-style" compact course in banking for PhD students in applied macroeconomics and finance. The course has two fundamental objectives:

1. *to give an introduction to the banking literature* with particular emphasis on aspects that I consider important for macro-financial research.
2. *to enable young researchers to develop their own applied theories.* I plan to discuss techniques relevant to the construction of theory models that incorporate nontrivial aspects of banking.

## Course Structure

1. Asymmetric Information and the Existence of Banks
2. Liquidity and Runs
3. Screening and the (Mis-)Allocation of Credit
4. Capital Structure and Capital Regulation
5. Financial Linkages, Contagion and Systemic Risk

6. Banking and Monetary Policy Transmission

## Textbook

No textbook is required. However, highly recommended references are:

- X. Freixas and C. Rochet, *"Microeconomics of Banking"*, 2nd edition, MIT Press, 2008
- Degryse, H., M. Kim and S. Ongena, *"Microeconometrics of Banking"*, Oxford University Press, 2009

## Literature

We will discuss many, but likely not all, of the papers in the literature list that follows below. Particularly central papers are marked with asterisk (*).

### 1. Asymmetric Information and the Existence of Banks

- Leland, H., and D. Pyle (1977), "Information asymmetries, financial structure, and financial intermediation". *Journal of Finance* 32, 371-388.
- Diamond, D., (1984) "Financial intermediation and delegated monitoring". *Review of Economic Studies* 51, 393-414.
- (*) Sharpe, S. A. (1990), "Asymmetric Information, Bank Lending, and Implicit Contracts: A Stylized Model of Customer Relationships". *Journal of Finance*, 45, 1069-1087.
- Gorton, G., and G. Pennacchi (1990) "Financial Intermediaries and Liquidity Creation.". *Journal of Finance*, 45 (1), 49?71.
- Donaldson, J. and G. Piacentino, "Warehouse Banking" (2018), forthcoming in *Journal of Financial Economics*

2. **Liquidity and Runs**

- (*) Diamond, D., and P. Dybvig (1983), "Bank runs, deposit insurance, and liquidity". *Journal of Political Economy* 91, 401-419.
- Malherbe, F. (2014), "Self-fulfilling Liquidity Dry-ups". *Journal of Finance*, 69, 947-970.
- Morris, S. and H.S. Shin (2001), "Rethinking Multiple Equilibria in Macroeconomic Modeling". in: Macroeconomics Annual Vol. 15, MIT Press.
- Goldstein, I. and A. Pauzner (2005), "Demand–Deposit Contracts and the Probability of Bank Runs.". *Journal of Finance*, 60: 1293-1327.
- Diamond, D. and Rajan, R. (2001), "Liquidity Risk, Liquidity Creation, and Financial Fragility: A Theory of Banking". *Journal of Political Economy* 109 (2), 287-327

3. **Screening and the (Mis-)Allocation of Credit**

- (*) Stiglitz, J., and A. Weiss (1981), "Credit rationing in markets with imperfect information". *American Economic Review* 71: 393-410
- De Meza, D. and D. Webb (1987), "Too Much Investment: A Problem of Asymmetric Information". *Quarterly Journal of Economics* 102 (2): 281–292
- (*) Ruckes, M. (2004), "Bank competition and credit standards". *Review of Financial Studies* 17, 1073-1102
- Petriconi, S. (2015), "Bank Competition, Information Choice and Inefficient Lending Booms". Working Paper
- Vanasco, V. (2017), "The Downside of Asset Screening for Market Liquidity". *Journal of Finance* 72 (5), 1937-1982

4. **Capital Structure**

- (*) Allen, F.; E. Carletti and R. Marquez (2015), "Deposits and bank capital structure". *Journal of Financial Economics*, 118 (3), 601-619.
- Gale, D. and P. Gottardi (2017), "Equilibrium Theory of Banks' Capital Structure". CESifo Working Paper Series No. 6580.

**5. Financial Linkages, Contagion and Systemic Risk**

- (*) Allen, F., and D. Gale (2000), "Financial contagion". *Journal of Political Economy* 108, 1-33.
- Caballero, R. and A. Simsek (2013), "Fire Sales in a Model of Complexity". *Journal of Finance* 68 (6), 2549-2587
- Farboodi, M. (2017), "Intermediation and Voluntary Exposure to Counterparty Risk". Working Paper, Princeton University.

**6. Banking and Monetary Policy Transmission**

- Hachem, K. (2011), "Relationship Lending and the Transmission of Monetary Policy" *Journal of Monetary Economics*. 58(6-8), 590-600.