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monday is 6 week

UNIVERSITY OF CHICAGO
Graduate School of Business

Business 336
Financial Markets
and Institutions

Douglas W. Diamond
Winter 1984

COURSE OUTLINE

Text: Branch and Stigum, Managing Bank Assets and Liabilities, Dow-Jones, Irwin, 1983. (S-B, below)

"()" denotes readings which are recommended, but not required.

I. Financial Intermediation and Banking: Regulation and Markets.

1. Banks as intermediaries. Banking as a typical industry.

Readings: Wood, Ch. 1, 4
S-B, Ch. 1, 2

it • Fama, "Banking in the Theory of Finance." *chapter 12.*

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direct finance
indirect "
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Model.

2. Money market instruments. (Only brief class discussion of this section).

Readings: **S-B** Ch. 3, "The Instruments in Brief."
Ch. 4, "Discount and Interest Bearing Securities."
Wood, Ch. 3, "Financial Innovation and the Demand for Money."

Stigum, Ch. 12, "Repos and Reverses."
real **Dann and James**, "Impact Of Deposit Rate Ceilings on the Market Value of Thrift Institutions," (handout in class).

Section 3

3. Compensating balances, the prime rate.

Readings: S-B, Ch. 5, "Domestic Banking."
BIRNS, "Compensating Balance Requirements."
(Black, "Bank Funds Management in an Efficient Market.")
Merris, "The Prime Rate."
S-B, Ch. 6, "Eurobanking."
Haydon National Bank (case).

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balance
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4. Regulation and the setting today.

Readings: **Campbell**, "The Regulation of Commercial Banks."
S-B, Ch. 7, "The Setting Today."
(J. Karaken, "Deregulating Commercial Banks.")

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5. Liquidity and the benefits of deposit insurance. The liquidity service provided by intermediaries.

Readings: Wood, Ch. 6, "Characteristics of Securities." DFA model

S-B, Ch. 8, "Liquidity Management."

(Lückett, "Approaches to Bank Liquidity Management.")

J¹⁰ Diamond-Dybvig, "Bank Runs, Deposit Insurance and Liquidity."

(Schweitzer, "Bank Liability Management.")

Stigmon, ch. 11, "The Federal Funds Market" p2. Section 5

6. Interest rate risk and duration.

Readings: S-B, Ch. 9, "Interest Rate Exposure." → Duration

Wood, Appendix 5.D - Duration. *SD DFA-1*

Ingersoll, "Is Immunization Feasible? Evidence from the CRSP data." ○ Paper sub

(Miller, Class Notes 1, 2, 8.) TFA

7. Interest rate risk: Futures markets.

Readings: S-B, Ch. 12, "Futures Strategies."

Keen, "Interest Rate Futures: A Challenge for Bankers."

II. Agency Problems and a More Fundamental View of Financial Intermediation

1. Agency problems and corporate finance.

Readings: *15* Miller, class note 13.

Diamond-Verrecchia, "Optimal Managerial Contracts and Equilibrium Security Prices." (Don't read the math).

Class note - "Optimal Contracts."

~~Buckeye Pipeline Company (case).~~

2. Asset side services: Covenants and delegated monitoring. + Bond holder (to check on cost)

Readings: Smith-Warner, "On Financial Contracting." (EIR & F&E)

Class note, "Financial Intermediation and Delegated Monitoring."

3. Deposit insurance's costs: risk taking, and capital structure implications.

Readings: *2* Buser-Chen-Kane, "Federal Deposit Insurance, Regulatory Policy and Optimal Bank Capital."

J. Kareken, "Deregulating Commercial Banks."

Class note on deposit insurance (FDIC annual report.)

4. Long run capital structure policy.

Readings: ~~Ordler-Taggart, "Implications of Corporate Capital Structure Theory for Banking Institutions."
 Marius, "The Bank Capital Decision: A Time Series Cross Section Analysis."
 Wells Fargo (case).
 (Bedford, "Income Tax of Commercial Banks.")
 (Skelton, "The Relative Pricing of Tax-Exempt and Taxable Debt.")~~

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Essay (1 week ahead)
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