

Part IIB Paper 6
Banking and Finance
Paper Co-ordinator: Dr T Cavalcanti

Paper Content

The global financial crisis has highlighted the importance of the hidden wiring of banking and finance that underpins intermediation between savers and borrowers. This paper is designed for those interested in issues banking and finance, asset pricing, corporate decision making under uncertainty, financial intermediation, as well as the role of banks and credit in a modern capitalist economy.

Aims

The paper provides an introduction to banking, financial asset valuation and its application to corporate decision-making. We will cover current research on the evolving nature of financial intermediation, and issues in the design of financial regulation. We will cover both micro and macro topics.

Objectives

Students should be able to understand important basics of asset valuation and its relevance for understanding financial markets and corporate finance. They should also be able to use small models to understand the concept of financial accelerator, and to interpret the behaviour of households, firms, and financial intermediaries. This course is ideal for students who wish to enter career in the City or in a central bank or finance ministry. It is also a course that will support those who want to pursue research on these key topics.

Lecture Courses

Introduction to Corporate Finance (Dr S Reiche, 8 hours, weeks 5-8, Michaelmas Term)

Finance and Asset Pricing (Prof J Chadha, 8 hours, weeks 1-4 Michaelmas Term;)

Credit and Banking (Dr T Cavalcanti, 8 hours, weeks 1-4, Lent Term)

Credit and Financial Development (Dr T Cavalcanti, 8 hours, weeks 5-8, Lent Term)

Lecture topics

Corporate finance topics include: Capital structure; Debt vs Equity financing; Asymmetric information and outside financing (hidden action and hidden information); Diversification; Debt overhang and renegotiation; Monitoring.

Finance and asset pricing topics include: Facts: Time Variation and Business Cycle Correlation of Expected Returns; Predictability and Forecasting and Review of the Efficient Market Hypothesis; Factor Pricing Models - Capital Asset Pricing Model (CAPM) and consumption-based CAPM; Equity-Premium puzzle; Mean-Variance frontier and Beta representations.

Credit and Banking topics include: Theory of banking; credit rationing and deposit insurance; financial accelerator and credit channel; bank runs, banking crises and lender of last resort; and regulation.

Credit and Financial Development topics include: Microfoundations for credit constraint; the role of credit market in fostering entrepreneurship (theory and evidence); Macro effects of financial frictions on productivity and development (theory and evidence).

Readings

(This is indicative reading and students should not buy any books until they have seen the detailed reading lists provided for each lecturer)

Bailey, R. E. (2005). "The Economics of Financial Markets", Cambridge University Press.
Campbell, J., A. Lo, and C. MacKinlay. The Econometrics of Financial Markets. Princeton, NJ: Princeton University Press, 1997.

Copeland, T. and F. Weston, Shastri, K. Financial Theory and Corporate Policy. (Fourth edition) Pearson 2005

Hull, J. Options, Futures, and Other Derivative Securities, 2nd edition. Englewood Cliffs, NJ: Prentice Hall, 1993.

Tirole, J. (2005). The Theory of Corporate Finance, Princeton University Press.

Ross Westerfield, Jaffe and Roberts, Corporate Finance, McGraw-Hill Ryerson, 2003.

Xavier Freixas and Jean-Charles Rochet, Microeconomics of Banking, 2nd edition, 2008, MIT Press.

K Matthews and J Thompson, "The Economics of Banking" Wiley, 2008.

AN Berger, P Molyneux, and JOS Wilson "The Oxford Handbook of Banking" eds, OUP, December, 2009.

Hull, J. Options, Futures, and Other Derivative Securities, 7th edition. Englewood Cliffs, NJ: Prentice Hall, 2008.

Hillier, D., M. Grinblatt, and S. Titman. Financial Markets and Corporate Strategy European Edition 1st edition. McGraw-Hill, 2008. Parts I and II only.

Banerjee, A. and E. Duflo (2011). "Poor Economics: A Radical Rethinking of the Way to Fight Global Poverty", MIT Press.

Sheinkman, J. A. (2014). "Speculation, Trading, and Bubbles", Columbia University Press.

Shin, H. S. (2010). "Risk and Liquidity", Oxford University Press.

Journal articles to read will be announced during each lecture course.

Prerequisites

Students are expected to be proficient in quantitative methods at the level of Part I Paper 3, but it is not necessary to have done Paper 6 in Part 2A. In addition, this Paper builds on Part 2A Paper 1 and Paper 2, in particular the Economic of Uncertainty and Information, and Monetary Economics.

Supervisions

The suggested supervision assignments will be posted on by the course lecturers over the course of the term, as well as classes with the teaching associate. Supervisions are organized by your Director of Studies.

Examination

The exam consists of 4 Sections and each Section carries equal weight. Each Section contains 2 questions of each course module and students are required to answer 1 question from each Section.