EC3001: The Economics of Banking

2019/20

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Aims
The course's aim is to provide a theoretical economic analysis of the economics of banking and the potential fragility of the financial system. The course will include analysis of why banks exist and why bank runs may occur. The course's textbook will be Freixas and Rochet "Microeconomics of Banking", but will also use "Understanding Financial Crises", Clarendon Lectures in Finance by Franklin Allen and Douglas Gale.

Learning Outcomes
Upon completion of this course students should be able to:

- Explain the economic meaning of the terms liquidity and solvency in the context of financial intermediaries, analyse these concepts using simplified frameworks and be able to answer problems based on these frameworks
- Discuss why banks exist and the role that they play in the modern economy.
- Describe and apply models of equilibrium bank runs and be able to answer problems based on these frameworks
- Discuss the implications of imposing capital structure controls and/or liquidity controls on financial intermediaries

Course Delivery
The course is a one semester course which will be given in the Spring semester. There will be one two-hour lecture per week and one seminar per week. The lectures will be used primarily for expounding the economic theory and the seminars for going through problem sets although there may be some reversal of this demarcation of lectures and seminars in some weeks. You are advised that solving the problems will be of enormous help in examinations and tests, although they will not be part of the formal method of evaluation. You should prepare answers to the problems before the weekly seminars and expect to present them to the rest of the group. As with all courses in the department, failure to attend seminars can lead to students being awarded an Attendance Fail (AF; please see the college regulations for more information).

Note that lecture notes and homework answer sheets are NOT given out or placed on Moodle in this course. This is because I have found that students engage more with the course when handouts are not available. This benefits everyone attending lectures and seminars. This has been a successful policy in previous years and will not be changing this year. Please note that while seminar attendance is compulsory and is monitored by the department, attendance at lectures is also an essential part of the course. If you do not want to regularly attend lectures or write up your own homework answers then you should seriously consider taking an alternative course.
Assessment
This course is assessed 100% by an unseen examination in the summer term. There will be a mid-term test but this is to provide students with feedback and exam practise and will not contribute to the final grade. Please refer to the student handbook for the scheduling of the summer exam.

Communication and Office Hours
I will endeavour to answer emails within three working days during term time. Most questions will be answered by going over the material at the start of the next lecture or seminar so that all students can benefit. However if you do want to go through something directly with me then you can email to arrange a slot during my office hours. Please note that I do not answer homework questions directly by email.

Textbooks
Microeconomics of Banking, Xavier Freixas and Jean-Charles Rochet, MIT Press (2008)
Understanding Financial Crises, Clarendon Lectures in Finance by Franklin Allen and Douglas Gale
OUP (2009)

COURSE OUTLINE
We will cover most of the following topics

- Microeconomic Models of Banking
- Why Banks Exist
- Liquidity Insurance, Narrow Banking
- Bank Runs
- Policies to Prevent Bank Runs
- Banking Regulation
- Contagion and Financial Stability