Finance 321: Financial Institutions

Fall 2012

Professor Sheffield C. Richey, Jr.

Classes: Mondays and Wednesdays 5:55pm to 7:00pm.
Office: Enterprise Hall, 2nd Floor, Finance Department; Office Hours by Appt., M and W, one hour before class
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Consider this syllabus an agreement. There are no "extra credit" assignments. Unless otherwise stated, students are responsible for all text material, whether covered in class or not. Class notes are the students' responsibility.
Absences are treated consistent with University policy. Conflicts due to professional commitments must be indicated in advance; obligations will be due on or prior to original due dates. Makeup exams will only be given by prior arrangement or in case of a significant illness. Any University cancellation of class will result in the assignment or obligation being due the next scheduled class meeting.


Recommended: Wall Street Journal (Highly Recommended), Business Week, The Economist, Fortune, Financial Times, American Banker

Outside Reading: Outside assignments will be announced in class and made available in class, on this website or at the Copy Center.

Honor Code: Students are expected to follow the honor code as presented in the University's Catalog.

Grading: Midterm Examination 30 percent
Final Examination 30 percent (non-cumulative)
Paper 40 percent
(NOTE: Class participation and discussion are expected.)
Schedule for the Semester

Class  Subject (Chapters) and Important Dates

INTRODUCTION

Major Financial Intermediaries and Their Role in the Economy
8/27  Chapter 1 PPT - Why Are Financial Institutions Special?
      Chapter 2 PPT – Financial Services: Depository Institutions

Institutionalization of Saving, Financial Intermediation, the Financial System and Reforms
8/29  Chapter 3 PPT – Financial Services: Insurance

9/3   Chapter 4 PPT - Financial Services: Securities Brokerage and Investment Banking

9/5   Chapter 5 PPT – Financial Services: Mutual Funds and Hedge Funds

9/10  Chapter 6 PPT – Financial Services: Finance Companies

RISK MEASUREMENT

9/12  Chapter 7 – Risks of Financial Institutions

9/17  Chapter 8 – Interest Rate Risk I
9/19  Chapter 9 – Interest Rate Risk II
9/24

9/26  Chapter 10 – Market Risk

10/1  Chapter 11 – Credit Risk: Individual Loan Risk

10/3  Chapter 12 – Credit Risk: Loan Portfolio and Concentration Risk

10/8  NO CLASS

10/10 MIDTERM

10/15  Chapter 13 – Off-Balance-Sheet Risk
RISK MANAGEMENT

10/31 Chapter 18 – Liquidity and Liability Management
11/5 Chapter 19 – Deposit Insurance and Other Liability
11/12 Chapter 20 - Capital Adequacy
11/14 Chapter 21 - Product and Geographic Expansion
11/19 Chapter 22 – Futures and Forwards
11/21 THANKSGIVING
11/28 Chapter 23 – Options, Caps, Floors, and Collars
12/5 Chapter 24 – Swaps
12/10 Chapter 25 – Loan Sales
12/12 Chapter 26 – Securitization

Research/Position Paper

- A. Must be typewritten, double-spaced, type no larger than 12 point, 1 inch margins or less.
- B. About 8-10 pages in length, not including references, title page, figures, or tables.
- C. Papers should thoroughly provide history of topic or issue discussed, discuss pros and cons where appropriate, and then give the author’s opinion on the subject (e.g. how a crisis could have been handled differently; how you would have improved regulations or legislation; how you would improve on the matter/issue; what mechanisms could have been put in place, etc.).
  - 1. Executive Summary of results and conclusions (less than 1 page).
  - 2. A brief overview of the case and a statement of the problem to be addressed.
  - 3. A discussion of your analysis.
4. Summary and conclusions.

All ideas, hypotheses, conclusions not original with the author must be accompanied by appropriate citations. Use the style for citations followed in the text. Internet citations should include the name of the author(s), complete URL, date of the posting or publication, date of access, publisher and city, state and country. Papers are the product of the student and should be kept by him throughout the course. Be sure to retain a copy of the paper before it is submitted.

Interesting and Provocative Topics in Financial Institutions:

Professor Hanweck’s Suggested Topics:

- 1. Federal Deposit Insurance Corporation - purposes, effects, and prospects
- 2. The international debt crisis - causes, consequences, and remedies
- 3. The U.S. agricultural financial crisis - causes, consequences, and remedies
- 4. Prudential regulation - its future in a deregulated environment and relationship to federal deposit insurance
- 5. The S&L crisis of the late 1980s - causes, consequences, and remedies
- 6. Interstate banking: Issues of competition and expansion of customer base
- 7. Electronic payment systems - their impact on the scope of depository institutions markets
- 8. Proposed deregulation and its past and future impact on financial institution behavior and performance (choose a financial institution)
- 9. Free Banking - historical perspective and policy issues in the context of the current debate on banking deregulation. What is “free banking?”
- 10. Issues related to expanded powers for depository institutions - e.g., securities and insurance underwriting, equity investments, brokerage services, commercial activities
- 11. "Too-Big-To-Fail" doctrine - purposes and consequences
- 12. • 13. Financial Market Crises: Their causes, consequences and remedies
- 13. Alternative Mortgage Instruments, the primary and secondary mortgage markets, and the S&L industry
- 14. Internationalization of Financial Markets and Exchanges: Analyze the development of these markets in Tokyo, London, Hong Kong, Singapore, etc. and how they are coordinated to provide competition for financial intermediaries in the U.S. Consider also European economic integration-EC ’92 and adoption of the EURO in January 1999.
- 15. The U.S. Government Securities markets' organization and the implications of monopolistic practices for pricing and stability of these markets
- 16. FIRREA (Financial Institutions Reform, Recovery, and Enforcement Act of 1989) and its effects on the future of S&Ls and the industry.
- 17. The RTC (Resolution Trust Corporation) and its effects on real estate markets and as a means of conducting the disposition of failed depository
institutions’ assets.

- 18. **Securitization of depository institutions' assets.** Requires little liability issue since assets are not held, but it requires the depository institution to provide a market for these instruments.

- 21. **The "Credit Crunch."** Define. Was there a "credit crunch" in the early 1990s or was there only a lack of borrowers of good credit quality that needed financing.

- 22. **FDICIA (Federal Depository Insurance Corporation Improvement Act of 1991).** Significant mandates to protect the FDIC Insurance Funds from being depleted (suggestion 6 above is related), established Prompt Corrective Action, capital standards for market, exchange rate, and interest rate risk, and risk-based deposit insurance premiums.

- 23. **Reigle-Neal Interstate Branching and Banking Efficiency Act of 1994.** Permits interstate branching for the first time throughout the U.S. unless specifically blocked by state law. Effective June 1997. The effect of this act may have been dissipated over the previous 14 years of interstate banking or it may be a strong impetus to banking consolidation, efficiency and competition.

- 24. **Bank for International Settlements: Basle Accord and Revisions since 1989.** Established the first international agreement on capital adequacy standards leading to the current proposals for a "models-based" identification for required capital for a banking and investment banking companies.

- 25. **Asian Crisis Beginning in 1997.** The collapse of the Thai baht in 1997 began the Asian Crisis that led to a collapse of several southeast Asian economies (e.g., Indonesia) and crippled the South Korean economy.

- 26. **Russian Default and Devaluation of August 1998.** Led to a major flight to quality threatening the stability of global financial markets and the $3.6 billion bailout of Long Term Capital Management by major banks and investment banks in the U.S. and abroad that had interests in and loans to LTCM.


- 29. **Dodd-Frank Wall Street Reform and Consumer Protection Act, July 2010**

Professor Richey’s Suggested Topics:

- 30. **Moral hazard and FIs (e.g. FDIC insurance or Fannie Mae and Freddie Mac);**
- 31. "Success" rate of major IPOs in the past;
- 32. **Basel Accords - setting banking capital standards;**
- 33. Up front and hidden costs of annuities. Are they worth it?;
- 34. Recent JPM $2b trader loss and attempts by FIs to hedge risks in their proprietary portfolios;
- 35. Use of Dutch auction in an IPO; discuss GOOG IPO;
36. Compare and contrast the use of the Repricing model (Ch. 8) versus the Duration model (Ch. 9) by FIs in reducing interest rate risk; pros and cons;
37. Discuss the role AIG and the Credit Default Swaps it underwrote had in Financial Crisis;
38. Discuss why hedge funds unlike other FIs are not regulated and proposals (law, regs) and attempts to regulate them. Would such laws/regs crimp their style?;
39. Discuss loan portfolio diversification and Modern Portfolio Theory;
40. Discuss liquidity risk faced by life and property and casualty insurers and how they cope with it;
41. Discuss the Glass-Steagall Act, the Financial Markets Modernization Act of 1999 which repealed it, and the pros and cons of another Glass-Steagall type law being reenacted by Congress;
42. Discuss some facet of the 2010 "Dodd-Frank" financial markets law (run by me). Would the portion of the law you discuss hurt the affected FI's ability to compete and earn profits?;
43. Mark-to-market versus book value (historical accounting) of an FI's assets and the debate over it by regulators and banks during the financial crisis;
44. Discussion of capital assets (leverage) ratio and risk-based capital ratios; pros and cons;
45. Pros and cons of the conversion of on-balance-sheet mortgages to securitized mortgages - can discuss main loan originators (commercial and mortgage banks), FNM/FRE, and Collateralized Debts Obligations packaged by the investment banks during the financial crisis.