

## **Economics 5350 Banking and Financial Intermediation**

Department of Economics

Hong Kong University of Science and Technology

(Spring 2023)

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### **Course Objectives**

This course provides an introduction to banking and financial intermediation. It enables students to know the models in which banking and financial intermediation emerge as institutional arrangements to overcome some fundamental frictions of an economy. Those models help understand some common practices in financial intermediation. They are also useful to understand financial crisis and regulations.

### **Intended Learning Outcomes**

1. Know the basic models built on coalition of depositors, coalition of borrowers, delegated monitoring, etc. (PILO 1, 2)
2. Learn the complicity of the borrower-leader relationship due to costly state verification and moral hazard. (PILO 1, 2)
3. Understand some common practices in financial intermediation, financial crisis and regulations (PILO 1, 2)

**Prerequisites:** Econ 5130, 5140

### **The course material**

1. Lecture notes.
2. Reference book: Xavier Freixas and Jean-Charles Rochet, *Microeconomics of Banking*, 2nd Edition, MIT Press.

**Grading:** The grade is based on (a) the *course work* and (b) *course participation*.

1. The course work consists of homework sets (20%) and the final exam (80%).
2. The course participation applies to 6 lectures from 09/02 to 16/03. In case that you skip  $n$  of the 6 lectures and you can provide valid excuses

for  $m$  skipped lectures, the penalty is to subtract  $\max\{3(n - \max\{2, m\}), 0\}$  points from the course work.<sup>1</sup> Illness is taken as a valid excuse only if a doctor indicates by a written note that illness affects you to attend a lecture.

(2.1) When you intend to provide an excuse for a skipped lecture, the relevant document should be given to the instructor within two days after the lecture is over.

(2.2) When you attend a lecture by zoom, you should turn on video to be counted for participation—if your video is off for at least 30 minutes accumulatively during the lecture, then it will be treated as skipping the lecture.

**Academic integrity:** Cheating and plagiarism are not tolerated. Any violation will be reported to the university. See <http://www.ust.hk/vpaa0/ug-guide/integrity/> for details.

**Course outline** (subject to adjustment if necessary)

09/02 Introduction, Lecture 1

14/02 Lecture 1

23/02 Lecture 1, Lecture 2

02/03 Lecture 3

09/03 Lecture 4, Lecture 5

16/03 Lecture 6

Lecture 1: Intermediary as coalition of consumers

Lecture 2: Intermediary as delegated monitor

Lecture 3: Partial disclosure and costly state verification

Lecture 4: Credit Rationing

Lecture 5: Intermediary as coalition of producers

Lecture 6: Collateral, bank's capital, and credit crunch

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<sup>1</sup>If  $n \leq 2$ , then the penalty is zero even when you do not provide any excuse.