Description: This course is an introduction to modern monetary and banking theory at a graduate level. The literature in this area is very large. In the course we shall concentrate on the theory of financial intermediation and banking, the role of banks in regulation, supervision and conduct of monetary policy, the transmission mechanism of monetary policy, bank runs and financial crises, securitization, and the recent 2007-2008 financial crisis. If time permits there will also be a discussion of the modern search theoretic theory of money. For a large part of the course, the strategic interaction between different economic agents and the role of asymmetric information will be stressed.


Supplementary Texts:


Assessment:
The course is assessed by a final examination (40%); Mid-term examination (20%), and 2 Homework Assignments (10% each), and a Term Paper (20%).

Reading List and Course Outline: The earlier material is well covered in textbooks, the later material is evolving and will be based on journal articles. While the material is largely self-contained, students will be expected to know economics at the level of EC5101, EC5102, and EC5104.

1. *Introduction and overview: Financial Intermediation* (Week 1-3)
   Transaction costs, liquidity provision, information sharing, delegated monitoring and intertemporal smoothing.
   1. Freixas and Rochet (2008), Ch. 1-3.
2. *The Borrower-Lender Relationship* (Weeks 4-5)
   Costly state verification, strategic debt repayment, moral hazard, and incomplete contracts.
   1. Freixas and Rochet (2008), Ch. 4.

3. *Credit Rationing* (Week 6)
   Credit rationing due to adverse selection and moral hazard.
   1. Freixas and Rochet (2008), Ch. 5.
   2. Walsh (2010), Ch.10.

4. *Transmission of Monetary Policy* (Week 8)
   Money channel, credit channel, foreign exchange channel, banking channel.
   1. Freixas and Rochet (2008), Ch. 6.
   2. Walsh (2010), Ch.10.

5. *Bank Runs and Systemic Risks* (Week 9)
   Liquidity insurance, fractional reserve system, bank runs, lender of last resort.
   1. Freixas and Rochet (2008), Ch. 7.

6. *Credit, Liquidity and Financial Crises* (Week 10-11)
   Credit cycles, liquidity, mark-to-market.
   1. Freixas and Rochet (2008), Ch. 9.

7. *Central Bank Independence and Conduct of Monetary Policy* (Week 12)
   Time inconsistency problem, central bank independence.
   1. Walsh (2010), Ch. 7.
   2. Blinder (1998), Ch. 3.

8. *Monetary-Policy Operating Procedures* (Week 13)
   Goals, targets and instruments of monetary policy.
   1. Walsh (2010), Ch. 11.
   2. Blinder (1998), Ch. 1, 2.