Political Economy of Finance - Perceptions 10 Years After the Crash

A retrospective summary

With this Seminar we want to add to existing efforts in understanding the financial meltdown that first culminated in the Lehman Brothers liquidity crunch in 2008. Thus, ten years after the crash, we will revisit institutions and concepts that led up to the crisis and critically evaluate following regulation as well as political aftermath. In this seminar we will acquire a basic understanding of banking and finance and build intiuition on finance-related issues such as risk-management, liquidiy-transformation, balance-sheets, lending and securitization. Within the basics-subsection we will also discuss both Keynesian and Minskyan approaches to financial (in-)stability. We will then examine regulation as in Basel III and Shadow Banking entities. Using this as grounds of discussion, we will follow up with issues of financial stability, financialization, crisis and monetary policy after the crash. Both interdisciplinary and post-keynsian approaches will be center of discussions. All sessions will be based on weekly reading and will in some cases be attended by field-experts. This is a reading-intensive course. We encourage students from all fields to join in the discussion of crisis, crash and political implications. Some background in accounting or finance will be helpful. We will, however, offer access to all topics with little prior knowledge. Interested students can get ahead of things with Perry Mehrling's online lecture noted in Course Outline 2.

Course Outline

It may be noted here that this course tried to prepare students for discussions through teaching "vocabulary" to use. Finance isn't difficult in itself. It merely uses strange words and concepts. It made sense to really focus on the basics. Students had little exposure to concepts of banking throughout their previous studies and are quickly overwhelmed with fiananace-vocabulary and mechanics. Next to "explaining vocabulary" and going at finance from a "learning a language"-perspective this course relied heavily no balance sheet notations. My experience with this course is, though, that its contents might have been a little overwhelming to some and this course's pace a little to fast.

Sessions were often structured in a way where students would discuss given study questions within groups of two or three for twenty minutes. Following, the whole class would try answering them alongside the current reading. There were also students' presentations as well as an external presentation by an ECB economist.

Students in their feedback highly appreciated the open learning atmosphere during the course, diving into "the classics" (reading of Hawtrey, Keynes, Minsky) and the vocab-driven approach. It simplified concepts to "studying vocabulary".

1. Hawtrey, R. G. (1919). Currency and Credit. "Capter I: Credit without Money". In Longmans, Green and Co.
    - Distinction of money and credit
    - Money as "final means of discharging debt"
    - Introduction to liquidity, "dealing in debts",
2. Perry Mehrling, Online-Course, coursera.com, Week 1: "The Four Prices of Money", "The natural Hierarchy of Money"
    - Introduction to balance sheets
    - Introduction to four prices of money
    - Introduction to hierarchical structure of money
    - Study Qestions:
        - How is par relevant to your daily life?
        - What happens if net worth of a bank is lower than zero? (Show in a balance sheet)
        - Are deposit accounts money?
        - Show Hierarchy of Money (Gold-Standard) in Pyramid and Balance-Sheets
        - What takes the place of gold in a Post-Gold-Standard world?
3. Overview: Fixed Income, Govt-Bonds, Securitization, Forms of credit
    - Introducing debt instruments
    - Especially to economics students these real-world instruments are very little known
    - Treating "coupon", "yield", "maturity", etc. as vocabulary
    - Visualization with outstanding debt of Germany, Greece, Apple
    - Visualization of yield courves to show maturity/yield nexus
4. Keynes, J. M. (1937). The General Theory of Employment. The Quarterly Journal of Economics, 51(2), 209–223.
    - Keynes' reply in the QJE is a great summary of his just previously published work
    - Introduces further into liquidity preference
    - Study Qestions:
        - What is the fundamental difference between Ricardian and Keynsian economics?
        - What description does Keynes find for the rate of interest?

- What is ”liquidity preference”, how does it interact with the rate of interest and how can you relate in real life?
- What monetary transmission does Keynes suggest as a means of steering price-level?

5. Financial Instability and Liquidity: Financial Instability Hypothesis”, Hyman Minsky, 1992, Working Paper No 74, Levy Economics Institute of Bard College
   - Not the best text on financial instability but short
   - Study Qestions:
     - What is Minsky’s point of departure? Inductive Reasoning vs. neoclassical axiomatic reasoning
     - What are the steps Minsky uses to argue his point?
     - What is his point?
6. Financial Regulation: Basel III
   - Presentation of two business administration graduate students on Basel III
   - Focus on Capital Buffers, Liquidity Coverage Ratio, Leverage Ratio
   - Introducing Basl III important to get a feel for real-life balance sheets and liquidity/solvency issues
   - Possible reading: Duffie, D. (2016). Why Are Big Banks Offering Less Liquidity To Bond Markets? Forbes
7. First-Half-Recap
   - Recapping the basics section of this seminar, students were really glad to be able to go over all points again
   - Students discussed the attached overview (see below) in small groups and formulated questions to the lecturer
8. Shadow Banking, Shadow Money: Perry Mehrling, Online-Course, coursera.com, Week 10: ”Banking as Advance Clearing”, especially from ”Financial Evolution: Indirect Finance to Direct Finance” onwards
   - Student-Presentation on Securitization
   - “Money market funding of capital market lending.” (Perry Mehrling)
   - Visualization of indirect finance
   - Usage of Zoltan Poszar’s Shadow Banking Map
9. Shadow Banking: Gabor, D. (2016). The (impossible) repo trinity: the political economy of repo markets. Review of International Political Economy, 23(6), 967–1000.
   - Presentation of ECB economist

- Role of Repo-Transactions in today's finance
- Position of Central Banks in rise of repo-funding
- Repo-Trinity as political tool, supposed to strengthen financial markets, but as Gabor shows prone to fail

10. Shadow Banking: Gorton, G., & Metrick, A. (2012). Securitized banking and the run on repo. Journal of Financial Economics, 104(3), 425–451
    - Small-group-discussions: Comparison of reasoning in Gorton/Metrick (2012) vs. Gabor (2016)
    - Each student recieves a quote from each of the papers
    - Each student then presents their quote and draws on differences and similarities in both
11. Mehrling, P. (2013). Elasticity and Discipline in the Global Swap Network., 44, 311–324.
    - Introction into "unconventional monetary policy" that isn't discussed regularly
    - Study Qestions:
      - What is a Central Bank Currency Swap line?
      - What do we use "onshore" and "offshore" for (in this context)?
      - Why is it (was it in the financial crisis) relevant if you are (were) an on-/offshore bank?
      - How is the FED an "indirect backstop" in the Eurodollar market?
      - Why is the emergence of the Central Bank Swap Network noteworthy? (historically, politically)
      - How does a CB-Swap differ from commercial currency swaps?
12. Political Economy of Risk: de Goede, M. (2004). Repoliticizing financial risk. Economy and Society, 33(2), 197–217.
    - Exploring topics of Gender and Risk
    - Discussion on interdisciplinatory approaches towards questions of finance and risk