

RTG1659

Interdependencies in the
regulation of markets

Syllabus “Financial Markets Regulation” (spring term 2013)

Time and location: Wed. 10am-12pm, Spandauer Str. 1, room 23

This course introduces students to the regulation of financial markets and the participants in these markets. It consists of four parts. The first two parts analyze the financial disclosure requirements of non-financial corporations and the impact of these requirements on corporate policies. The third part discusses the most relevant financial frictions that policy makers should consider when regulating financial institutions. Part four reviews the economics of financial crises and discusses what regulatory mechanisms exist to prevent financial crises.

Instructors

Prof. Dr. Joachim Gassen	HU Chair of Accounting
Prof. Tim Adam, Ph.D.	HU Institute of Corporate Finance
Prof. Lutz Weinke, Ph.D.	HU Institute of Economic Policy
Prof. Dr. Frank Heinemann	Technische Universität Berlin

Course Outline

Date	Topic	Instructor
April 10	Introduction to Course/Financial Reporting and Disclosure: An Institutional Primer	All/Gassen
April 17	Incentives for and Regulation of Disclosure	Gassen
April 24	Capital-Market Consequences of Disclosure	Gassen
May 8	no class	
May 15	Cross-Market Consequences of Disclosure	Gassen
May 22	- Uptick rule, crowded bankruptcy courts and trade credit (SPA 1, Room 23, 10-12) - SOX (DOR 1, Room 5, 12-14)	Adam/Berg
May 29	Regulation FD	Adam/Berg
June 5	Financial Frictions in DSGE Models I	Weinke
June 12	Financial Frictions in DSGE Models II	Weinke
June 19	Financial Frictions in DSGE Models III	Weinke
June 26	Basic Mechanisms of Financial Crises	Heinemann
July 3	Maturity Transformation and Systemic Risk	Heinemann
July 10	Capital Adequacy Requirements and Lender of Last Resort	Heinemann

Final Exam: TBA

Reading List

Part I: Financial Reporting and Disclosure (* indicates required readings)

* = required reading

1. Financial Reporting and Disclosure: An Institutional Primer

Ball, R. (2001): Infrastructure Requirements for an Economically Efficient System of Public Financial Reporting and Disclosure. *Brookings-Wharton Papers on Financial Services* : 127-169.

Graham, J. C. Harvey and S. Rajgopal (2005): The economic implications of corporate financial reporting. *Journal of Accounting and Economics* 40: 3-73.

2. Incentives for and Regulation of Disclosure

Beyer, A., D. Cohen, T. Lys and B. Walther (2010): The financial reporting environment: Review of the recent literature. *Journal of Accounting and Economics* 50: 296-343.

Gao, P. (2010): Disclosure Quality, Cost of Capital, and Investor Welfare. *The Accounting Review* 85: 1-29.

Goldman, E. and S. Slezak (2006): An equilibrium model of incentive contracts in the presence of information manipulation. *Journal of Financial Economics* 80: 603-626.

* Hermalin, B. and M. Weisbach (2010): Information Disclosure and Corporate Governance. *Journal of Finance* 57: 195-233.

3. Capital-Market Consequences of Disclosure

Balakrishnan, K., B. Kelly, M. Billings and A. Ljungqvist (2012): Shaping Liquidity: On the Causal Effects of Voluntary Disclosure, SSRN Working Paper.

Ball, R. and L. Shivakumar (2008): How Much New Information Is There in Earnings? *Journal of Accounting Research* 46: 975-1016.

Bhattacharya, U., A. Hackethal, S. Kaesler, B. Loos and S. Meyer (2012): Is Unbiased Financial Advice to Retail Investors Sufficient? Answers from a Large Field Study. *Review of Financial Studies* 25 (4): 975-1032.

* Kelly, B. and A. Ljungqvist (2012): Testing Asymmetric-Information Asset Pricing Models. *Review of Financial Studies* 25: 1366-1413.

4. Cross-Market Consequences of Disclosure

* Dierynck, B., W. R. Landsman and A. Renders (2012): :Do Managerial Incentives Drive Cost Behavior? Evidence about the Role of the Zero Earnings Benchmark for Labor Cost Behavior in Private Belgian Firms. *The Accounting Review* 87: 1219–1246

* Jin, G. Z. and P. Leslie (2003): The Effect of Information on Product Quality: Evidence from Restaurant Hygiene Cards. *Quarterly Journal of Economics* 118: 409-451.

Part II: Recent Changes in Financial Markets Regulations

5. Uptick rule, crowded bankruptcy courts and trade credit

Boehmer, Jones and Zhang, 2008, Unshackling Short Sellers: The repeal of the uptick rule, Working Paper

Iverson, 2012, Get in Line: Chapter 11 Restructuring in Crowded Bankruptcy Courts, Working Paper

Barrot, 2012, Financial Strength and Trade Credit Provision: Evidence from Trucking Firms, Working Paper

6. SOX

Peter Iliev, 2010, The Effect of SOX Section 404: Costs, Earnings Quality, and Stock Prices, Journal of Finance 65(3)

Chhaochharia and Grinstein, 2007, Corporate Governance and Firm Value: The Impact of the 2002 Governance Rules, Journal of Finance

Linck, Netter, and Yan, 2009, The Effects and Unintended Consequences of the Sarbanes-Oxley Act on the Supply and Demand for Directors, Review of Financial Studies

[The Impact of the Sarbanes-Oxley Act on the Cost of Going Public \(Christoph Kaserer, Alfred Mettler, Stefan Obernberger\)](#)

7. Regulation FD

Information asymmetry, information dissemination and the effect of regulation FD on the cost of capital,

Jorion, Liu, and Shi, 2005, Informational effects of regulation FD: Evidence from rating agencies, Journal of Financial Economics

Part III: Financial Frictions and Macroeconomics

Recent research on the role of financial frictions for macroeconomic analysis has developed frameworks suitable for quantitative analysis. This is needed since many of the issues involving the role of financial factors in the business cycle and the implications for regulatory policies ultimately involve quantitative considerations.

8. Financial Frictions in DSGE models I

A quick refresher on DSGE modeling, which is at center stage in the BDPEMS course “Advanced Macroeconomic Analysis”.

Galí, J., 2008, Monetary Policy, Inflation, and the Business Cycle, Princeton University Press.

Woodford, M., 2003, Interest and Prices: Foundations of a Theory of Monetary Policy, Princeton University Press.

Setting the stage for the subsequent analysis of financial frictions in the context of an otherwise standard macroeconomic framework.

9. Financial Frictions in DSGE models II

Should financial considerations be given independent weight in monetary policy decisions? How should interest-rate policy take into account the observed movements in interest-rate spreads? Does it make sense to shift the traditional focus on interest rate policy to bank reserves as an alternative operating target for monetary policy? Is credit policy a substitute for interest-rate policy?

Cúrdia, V. and M. Woodford, 2011, The central-bank balance sheet as an instrument of monetary policy, *Journal of Monetary Economics* 58, 54-79.

10. Financial Frictions in DSGE models III

We continue with our discussion of the above mentioned questions and give an overview of other recent developments in this field.

Gertler, M. and P. Karadi, 2011, A model of unconventional monetary policy, *Journal of Monetary Economics* 58, 17-34.

Part IV: Macroprudential Regulation of Financial Markets (* indicates required readings)

11. Basic Mechanisms of Financial Crises

Allen, Franklin, and Douglas Gale (2009), *Understanding Financial Crises*, Oxford Univ. Press.

Bordo, Michael, Barry Eichengreen, Daniela Klingebiel and Maria Soledad Martinez-Peria (2001), Is the Crisis Problem Growing More Severe?, *Economic Policy* 16, 51-82, also available at <http://emlab.berkeley.edu/users/eichengr/research.html>.

* Heinemann, Frank (2012), [Understanding Financial Crises: The Contribution of Experimental Economics](#), *Annals of Economics and Statistics* 107-108, 7-29.

Kindleberger, Charles P., and Robert Z. Aliber (2005), *Manias, Panics, and Crashes: A History of Financial Crises*, 5th edition, Palgrave Macmillan.

Minsky, H.P. (1972), Financial Instability Revisited: the Economics of Disaster, http://fraser.stlouisfed.org/historicaldocs/dismech/download/59037/fininst_minsky.pdf

Reinhart, Carmen, and Kenneth Rogoff (2009): *This Time is Different*, Princeton Univ. Press.

Abreu, D., and M. Brunnermeier (2003), "Bubbles and Crashes", *Econometrica* 71, 173-204.

* Banerjee, A.V. (1992), "A Simple Model of Herd Behavior", *Quarterly Journal of Economics* 107, 797-817.

12. Maturity Transformation and Systemic Risk

* Hellwig, M. (2008), "The Causes of the Financial Crisis", *CESifo Forum* 9, 1- 21.

* Cooper, Russell W. (1999), *Coordination Games: Complementarities and Macroeconomics*, Cambridge University Press, Cambridge, UK, pp. x-xiii, 19-45, 126-131.

* Diamond, P, and P. Dybvig (1983), "Bank Runs, Liquidity and Deposit Insurance," *Journal of Political Economy* 91, 401-419.

Obstfeld, Maurice (1996), "Models of Currency Crises with Self-Fulfilling Features," *European Economic Review* 40, 1037-1047.

Milgrom, P. and J. Roberts (1990), "Rationalizability, Learning, and Equilibrium in Games with Strategic Complementarities," *Econometrica* 58, 1255-1277.

Vives, X. (1990), "Nash equilibrium with strategic complementarities," *Journal of Mathematical Economics* 19, 305-321.

13. Capital Adequacy Requirements, Liquidity requirements, and Lender of Last resort

* Bank for International Settlements (2006), *Basel II: International Convergence of Capital Measurement and Capital Standards: A Revised Framework – Comprehensive Version*, available at <http://www.bis.org/publ/bcbs128.htm>.

* Brunnermeier, M., A. Crockett, C. Goodhart, A. Persaud, and H.S. Shin (2009), *Geneva Report on the World Economy 11: The Fundamental Principles of Financial Regulation*, International Center for Monetary and Banking Studies (ICMB), Genf.

Brunnermeier, M., and L. Pedersen (2009), "Market Liquidity and Funding Liquidity," *Review of Financial Studies* 22, 2201-2238.

* Cifuentes, R., G. Ferruci, and H.S. Shin (2005), "Liquidity Risk and Contagion" *Journal of the European Economic Association* 3, 556-566.

Diamond, D., and R. Rajan (2001), "Liquidity Risk, Liquidity Creation and Financial Fragility: A Theory of Banking." *Journal of Political Economy*, 109, 287–327.

Hellwig, M. (1994), "Liquidity Provision, Banking, and the Allocation of Interest Rate Risk", *European Economic Review* 38, 1363 - 1389.

Hellwig, M. (1995), "Systemic Aspects of Risk Management in Banking and Finance", *Schweizerische Zeitschrift für Volkswirtschaft und Statistik* 131, 723 - 737.

Hellwig, M. (1998), "Banks, Markets, and the Allocation of Risks", *Journal of Institutional and Theoretical Economics* 154, 328-351.

* Rochet, J.-C., and X. Vives (2004), "Coordination Failures and the Lender of Last Resort: Was Bagehot Right after all?" *Journal of the European Economic Association* 2, 1116-47.

Further References

Journal of Regulatory Economics: <http://crri.rutgers.edu/jre/>

International Centre for Financial Regulation (ICFR): <http://www.icfr.org/Home.aspx>

List of financial regulatory authorities (Wikipedia):

http://en.wikipedia.org/wiki/List_of_financial_regulatory_authorities_by_country