

# Banking

## Module 3, 2017-2018

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## Course description

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This class covers some key themes in the commercial banking industry, including the impact of central banks and regulation. We will focus on value-creation, pricing and risk-management issues. The goal is to provide a framework for students to understand the sources of the revenue and fragilities of commercial banks as a basis for decisions and future work in economic and financial turbulence.

## Course requirements, grading, and attendance policies

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You will have three written assignments. The course grade will be based on 2 homework assignments (15 percent each), banking simulation game analysis (20 percent), and an exam (50 percent). You may discuss the assignments with other students, but you should write up each individually. Participation is not required except banking simulation game.

Students are required to adhere to the standards of academic ethics at NES.

## Schedule

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### Day 1. Introduction to Banking

- Origins and history of first banks
- The role of banks and regulation, expansion of credit
- Balance sheet
- Income statement
- Financial indicators
- Risk management framework

### Day 2. Liquidity management

- Banking system: participants and liquidity
- Measures
- Basel requirements
- Management in on-going and crisis scenarios
- History of bank runs

H/W 1: Shin, "Reflections on Modern Bank Runs: A Case Study of Northern Rock"  
(due to the beginning of the Day 3 class).

### Day 3. Capital management

- The goal of the capital requirements
- Measures
- Basel requirements
- Capital management
- Examples (why CBR have closed 25% of banks?)

Day 4. Interest rate and FX risks management

- Sources of IRFX risks
- Measures (regulatory and economic measures, gaps, behavioral adjustments, stress-tests)
- Goals and strategies
- Management (limits, hedging, balance and market instruments)
- Examples: FX explosion in Russia 1998 and 2014

Day 5. IR&FX cases. Retail banking

- IR&FX cases: Paul Volcker, the death of Savings and Loans (3-6-3 model) and the birth of interest rates derivatives
- Basic tendencies and major retail players in Russian market
- Competition from retailers, POS banking
- Client segmentation
- Product development
- Facebook, Google and Mobile operators vs banks

H/W 2: Simulation game analysis (due to the beginning of the Day 6 class).

H/W 3: Corporate loan pricing (due to the beginning of the Day 7 class).

Day 6. Pricing models and some principles of estimation banking products efficiency

- Funds transfer pricing: internal transfer rates and internal bank concept
- Basic principles of product pricing: funding and risk components, capital charges
- Basic principles of estimation banking products efficiency: scenario analysis, balance sheet dynamic modeling, cannibalization effect
- Example: loan pricing

Day 7. The past and the future of money and Banking

- What's better for banks: high rates or low rates?
- What is money?
- Digital currencies

Current trends in Fintech

**Recommended readings:**

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1. Economics of Money, Banking, and Financial Markets by Frederic S. Mishkin
2. Bank Asset and Liability Management by Moorad Choudry
3. Basel Committee on Banking Supervision Publications
4. "Strategic Risk Management in an Interconnected World" by Kroszner
5. The Economist, "Beyond Basel: America raises capital requirements for banks, widening the gulf with Europe"
6. The Economist, "Volcker Plus"
7. Ali et al. "The economics of digital currencies."
8. Andreessen, "Why Bitcoin Matters"
9. Ahamed, "Introduction" to Lords of Finance
10. Brett King Bank 3.0. Why Banking is No Longer Somewhere You Go, But Somewhere You Do

### **Academic integrity policy**

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Cheating, plagiarism, and any other violations of academic ethics at NES are not tolerated.