



BUSFIN 4265 –FINANCIAL INSTITUTIONS

Professor Isil Erel

Spring 2023

Meeting Times: *Section 1 (4784):* TuTh 12:45PM - 2:05PM; *Section 2 (4703):* TuTh 2:20PM - 3:40PM

Classrooms: SB 220

Professor:

Isil Erel (erel@fisher.osu.edu)

David A. Rismiller Chair in Finance,

Academic Director of the Risk Institute

<https://fisher.osu.edu/people/erel-koksal.1>

Office Hours on Zoom: Mondays 9:30AM-11:00AM (or by appointment)

Course Webpage: on CarmenCanvas (*Note: you might be seeing a different section number than your registered one as both sections are combined on Carmen*).

Course Description

This course will introduce students to financial institutions and their important economic functions. The course will examine the structure and operation of financial institutions in the U.S., with particular attention paid to the various risks and complex challenges facing these institutions. While there are no easy solutions to the challenges and problems faced by financial institutions, we will cover these issues in depth, with the objective of developing a solid understanding of them.

Required Reading

1. Course Packet [*referred to as “CP” below*], available at HBS Publishing. Please follow this link <https://hbsp.harvard.edu/import/1004761> and follow the instructions to register and download it.

2. Saunders and Cornett [*referred to as “SC” below*], *Financial Institutions Management: A Risk Management Approach*, 11th edition, McGraw-Hill. Please visit the McGraw Hill website below to view a selection of options available for rent or purchase:

11th edition (will be available to purchase online on 1/3/2023):

[Financial Institutions Management: A Risk Management Approach, 11th Edition](#)

10th edition: [Financial Institutions Management: A Risk Management Approach, 10th Edition](#)

Supplemental Readings

Articles are available on the course webpage, *referred to as “CW” in the tentative course outline below*. Also, note that these readings are OPTIONAL. Also, students are strongly encouraged to read financial press to reinforce the applicability of the topics that we cover in class.

Pedagogy

The course will be structured as a combination of lectures, discussions, and cases. **All classes will be IN PERSON, except for two lectures (on January 17th and March 28th), which will be prerecorded and posted on the course website. Please note these TWO dates on your calendar and do not show up in the classroom!**

I will post my PowerPoint slides on the course website on Canvas before each class to help you follow the lectures and take notes. Please remember that posted slides are not complete. For completeness, you should attend the lectures. Please also note that we will have a few guest lecturers throughout the semester. Please see the *tentative course outline* below for their names and affiliations.

Grading

The final course grade will be allocated as follows:

| | |
|------------------------------------|---------------|
| Individual Class Participation | 10% |
| Two Individual Assignments | 10% (5% each) |
| One Case Write-up (due last class) | 10% |
| Exam 1 | 30% |
| Exam 2 | 40% |

Please, note that I will assign the final course grade based on the final class curve, including both sections. The course grade average can vary across years (it varied between 3.3 and 3.6 in the last few years)!

Class Participation: Unless excused due to medical or other valid reasons, students are expected to attend each class in a timely fashion and take part in discussions. Class participation will be graded based on my assessment of both the quantity and quality of an individual's contribution to in-class discussions. ***Participation grades will not be shared. I will use them only to increase the final course grade when appropriate.***

Please *choose a seat for the entire term*, no later than the second-class session. This makes it easier for you to interact during class discussions and easier for me to facilitate grading for class participation.

Case Write-ups: Three cases ("GE and the Shadow Banking Landscape," "Deutsche Bank and the Road to Basel III," and "Chase Manhattan Corporation: The Making of America's Largest Bank") are available in the course packet and the last one will be assigned for formal case write-up (executive summary). Detailed instructions on the case write-up will be available on the course website at Canvas.

Students are required to form study groups to work on the cases that are assigned in the course. A study group may consist of ***up to 5 students***. You must email me a list of your group members before the first exam, and the groups may not be changed without my permission. You will have the (OPTIONAL!) opportunity to evaluate your team members at the end of the quarter. An evaluation sheet with a detailed explanation is posted on Canvas.

Individual Assignments: There will be two individual assignments. They will be posted on the course website on Canvas. **It is very important that you complete the assignment individually**, as they will help you prepare for the exams. I will also post sample problems from the textbook with solutions on Canvas.

Exams: There will be two exams. Dates are provided in the tentative course outline. All exams will be comprehensive in scope, including material from every part of the course. All exams will be closed book!

You can use nonprogrammable functions of a calculator. You will be provided one page of formulas (so there is no need to memorize any formula!!!).

Absences and Late Assignments

Absence from the exam or assignments will not be excused, except for the most serious circumstances. Such circumstances must be validated in writing by an appropriately accredited professional (e.g., a medical doctor). *Any unexcused absence from an exam will result in a grade of zero.* Late assignments will not be accepted for credit, except for the most serious reasons as described above. As a matter of professional courtesy, please notify me *in advance* if you are unable to attend a particular class.

Regrading Policy

Grading errors will be corrected. All regrade appeals must be submitted within *one week after the graded test or assignment is returned*.

Safety and health requirements:

All teaching staff and students are required to comply with and stay up to date on all [University safety and health guidance](#).

Academic Integrity Policy

All students are expected to abide by **the Ohio State's Academic Integrity Policy:**

Academic integrity is essential to maintaining an environment that fosters excellence in teaching, research, and other educational and scholarly activities. Thus, The Ohio State University and the Committee on Academic Misconduct (COAM) expect that all students have read and understood the university's [Code of Student Conduct](#) (studentconduct.osu.edu), and that all students will complete all academic and scholarly assignments with fairness and honesty. Students must recognize that failure to follow the rules and guidelines established in the university's *Code of Student Conduct* and this syllabus may constitute "Academic Misconduct."

The Ohio State University's *Code of Student Conduct* (Section 3335-23-04) defines academic misconduct as: <https://trustees.osu.edu/code-student-conduct/3335-23-04>. **If I suspect that a student has committed academic misconduct in this course, I am obligated by university rules to report my suspicions to the Committee on Academic Misconduct.** If COAM determines that you have violated the university's Code of Student Conduct (i.e., committed academic misconduct), the sanctions for the misconduct could include a failing grade in this course and suspension or dismissal from the university.

If you have any questions about the above policy or what constitutes academic misconduct in this course, please contact me. Other sources of information on academic misconduct (integrity) to which you can refer include: <https://oaa.osu.edu/academic-integrity-and-misconduct>.

Copyright for Instructional Materials

The materials used in connection with this course may be subject to copyright protection and are only for the use of students officially enrolled in the course for the educational purposes associated with the course. Copyright law must be considered before copying, retaining, or disseminating materials outside of the course.

Creating an Environment Free from Harassment, Discrimination, and Sexual Misconduct

The Ohio State University is committed to building and maintaining a community to reflect diversity and to improve opportunities for all. All Buckeyes have the right to be free from harassment, discrimination, and sexual misconduct. Ohio State does not discriminate on the basis of age, ancestry, color, disability,

ethnicity, gender, gender identity or expression, genetic information, HIV/AIDS status, military status, national origin, pregnancy (childbirth, false pregnancy, termination of pregnancy, or recovery therefrom), race, religion, sex, sexual orientation, or protected veteran status, or any other bases under the law, in its activities, academic programs, admission, and employment. Members of the university community also have the right to be free from all forms of sexual misconduct: sexual harassment, sexual assault, relationship violence, stalking, and sexual exploitation.

To report harassment, discrimination, sexual misconduct, or retaliation and/or seek confidential and non-confidential resources and supportive measures, contact the Office of Institutional Equity:

Online reporting form at equity.osu.edu,
Call 614-247-5838 or TTY 614-688-8605,
Or email equity@osu.edu

The university is committed to stopping sexual misconduct, preventing its recurrence, eliminating any hostile environment, and remedying its discriminatory effects. All university employees have reporting responsibilities to the Office of Institutional Equity to ensure the university can take appropriate action:

All university employees, except those exempted by legal privilege of confidentiality or expressly identified as a confidential reporter, have an obligation to report incidents of sexual assault immediately.

The following employees have an obligation to report all other forms of sexual misconduct as soon as practicable but at most within five workdays of becoming aware of such information: 1. Any human resource professional (HRP); 2. Anyone who supervises faculty, staff, students, or volunteers; 3. Chair/director; and 4. Faculty member.

Disability Services:

The university strives to make all learning experiences as accessible as possible. If you anticipate or experience academic barriers based on your disability (including mental health, chronic, or temporary medical conditions), please let me know immediately so that we can privately discuss options. To establish reasonable accommodations, you should register with Student Life Disability Services (<https://slds.osu.edu>). After registration, please contact me as soon as possible to discuss your accommodations so that they may be implemented in a timely fashion.

Accessibility of Course Technology

This online course requires use of CarmenCanvas (Ohio State's learning management system) and other online communication and multimedia tools. If you need additional services to use these technologies, please request accommodations as early as possible (<https://it.osu.edu/help>)

Tentative Course Outline

This outline is tentative and subject to changes. Please refer to the course website on Carmen for updates on readings, sample problems, and case assignments. It is the students' responsibility to check the course website for updates and announcements.

Class 1 Course Overview

Jan 10

Topics: Course Organization and Requirements

Classes 2&3 Introductions to Financial Institutions, Depository Institutions (Commercial Banks)

Jan 12 & 17

Note: We will have an in-person class on January 12, but the class on January 17 will be pre-recorded and posted on Zoom (so, no in-person class on January 17!)

Topics: Introduction to Financial Institutions
 Functioning of the Commercial Banks

Required Readings:

Saunders & Cornett: *Financial Markets and Institutions: A Risk Management Approach* (“S&C”) Ch. 1-2

Supplemental Readings:

Some examples of recent academic research, on Canvas course website [CW]:

Does FinTech Substitute for Banks? Evidence from the Paycheck Protection Program (Isil Erel and Jack Liebersohn), 2020, NBER Working Paper.

A Theory of Risk Capital (Isil Erel, Stewart Myers, and James Read, Jr.), 2015, *Journal of Financial Economics*, 118/3, 620-635.

Why did Holdings of Highly-Rated Securitization Tranches Differ So Much Across Banks? 2014, (Isil Erel, Taylor Nadauld, and Rene Stulz), 2014, *Review of Financial Studies*, 27/2, pages 404-453.

Governance, Risk Management, and Risk-Taking in Banks (Rene Stulz), 2014, Ohio State University Working Paper.

Class 4 Commercial Banks (Cont.)

January 19

Topics: Financial Statements and Analysis
 Governance of Commercial Banks

Required Readings:

S&C Appendix 2A, and Appendix 2B

Supplemental Readings:

A Syndicated Loan Primer [CW]

How do Banks Manage Liquidity Risk? [CW]

Lessons from the Great Credit Crisis, S&P [CW]

Corporate Governance and Banks: What Have We Learned from the Financial Crisis? (Hamid Mehran Alan Morrison Joel Shapiro), 2011, Working Paper.

Classes 5&6 Bank Regulation (Deposit Insurance & Capital Requirements)

January 24 & January 26

Topics: Creation of FDIC
 Moral Hazard due to Deposit Insurance
 Savings and Loan Crisis
 Capital Requirements (Basel Capital Accords)

Required Readings:

S&C Ch. 20 and Ch. 21

Supplemental Readings:

Basel “IV”: What’s next for banks? *McKinsey&Company Global Risk Practice*, April 2017 [CW]

Class 7 A Case on Basel III

January 31

Note: The Case “Deutsche Bank and the Road to Basel III” is a must-read before class (no write-up necessary)!

Required Readings:

Case: Deutsche Bank and the Road to Basel III [CP]

Supplemental Readings:

Deutsche Bank: Still Struggling on Capital, *WSJ* [CW]

Deutsche Bank: What to Know, *WSJ* [CW]

Class 8 Federal Reserve System

February 2

Guest Speaker: Mark Meder, First Vice President and Chief Operating Officer, Federal Reserve Bank of Cleveland

Classes 9 Other Lending Institutions

February 7

Note: First Individual Assignment is due at the beginning of the class!

Topics:

Saving Institutions

Credit Unions

Finance Companies

Required Readings:

S&C Ch. 2 and Ch.3

Supplemental Readings:

Savings and Loan Crisis (Ely), *The Concise Encyclopedia of Economics* [CW]

Class 10 Shadow Banking

February 9

Note: The Case “GE and the Shadow Banking Landscape Case” is a must-read before class (no write-up necessary)!

Required Readings:

Case: GE and the Shadow Banking Landscape [CP]

S&C Ch. 18

Supplemental Readings:

Why Do Firms Borrow Directly from Nonbanks? (Chernenko, Sergey and Erel, Isil and Prilmeier, Robert), 2020, Fisher College of Business Working Paper

Thinking Critically about Nonbank Financial Intermediation, The Brookings Institution, 2015 [CW]

Class 11 Review Session

February 14

Review Past Midterms

Class 12 Exam 1
February 16

Classes 13&14 Off-Balance-Sheet Banking & Loan Securitization

February 21 & February 23

Topics: Off-Balance-Sheet Assets/Liabilities
Loan Commitments
Securitization of Mortgages
Fannie Mae and Freddie Mac

Required Readings:

S&C Ch. 16 and Ch. 26-27 (*skim through*)

Supplemental Readings:

The Economics of Structured Finance (Coval, Jurek, and Stafford), 2009 [CW]

Understanding the Securitization of Subprime Mortgage Credit (Ashcraft and Schuermann), 2008 [CW]

Fussing and Fuming over Fannie and Freddie: How Much Smoke, How Much Fire? (Frame and White), 2005 [CW]

Classes 15&16 Measuring Interest Rate Risk

February 28 & March 2

Topics: The Case of Homeside Lending
Repricing GAP
Duration and Convexity

Required Readings:

S&C Ch. 8&9

Supplemental Readings:

NAB Lesson in How to Burn \$3 billion (Hooper), *Radio National*, 2001 [CW]

Class 17 Consumer Lending, Recent Changes in Banking and Bank Regulation

March 7

Guest Speaker: Monique Riccobelli and Steve Walsh (Huntington Bank)

Supplemental Readings:

Dodd-Frank Act Stress Test [CW]

Classes 18 Mutual Funds, Hedge Funds, Private Equity

March 9

Required Readings:

S&C Ch. 5

Supplemental Readings:

Investment Company Fact Book, *Investment Company Institute* [CW]

SPRING BREAK WEEK: March 14-18th

Class 19 Investment Banks

March 21

Topics: Investment Banks and Securities Firms
Securities Underwriting
Book building
Underpricing of IPOs

Required Readings:

S&C Ch. 4

(*Skim Through*) Role of the Investment Bank (Connelly, Fox, and Klausner), UBS, 2005 [CW]

(*Skim Through*) Initial Public Offerings: Going by the Book (Benveniste and Wilhelm), *Journal of Applied Corporate Finance*, 1997 [CW]

Optional Readings:

IPO Statistics (Ritter) [CW]

Secondary Market Stabilization of IPOs (Wilhelm), *Journal of Applied Corporate Finance*, 1999 [CW]

Classes 20&21 Measuring Credit Risk

March 23&28

Note: We will have an in-person class on March 23, but the class on March 28 will be pre-recorded and posted on Zoom (so, no in-person class on March 28!)

Topics: Calculating Return on a Loan
CreditMetrics of JP Morgan (VaR)
RAROC Models

Required Readings:

S&C Ch. 10 and Chapter 11 (only the VaR calculation)

Supplemental Readings:

Cycles and the Credit Culture (Henry Mueller) [CW]

Optional Reading:

If you want to learn about Moody's KMV, which is not covered in this class: Modeling Default Risk (Crosbie and Bohn), *Moody's KMV*, 2003 [CW]

Class 22 Credit Risk from a Practitioner's Perspective

March 30

Guest Speakers: Jeff Weaver, EVP & Director Qualitative Risk Assessment, KeyBank

Class 23 Insurance Companies

April 4

Topics: Risk and Insurance

Required Readings:

S&C Ch. 6

Supplemental Readings:

A Lively Market in 'Death Bonds' (Pleven and McDonald), *WSJ*, 2007 [CW]

Class 24 Trends and Challenges in the Insurance Industry

April 6

Guest Speaker: Klaus Diem, Senior Vice President, Chief Risk Officer, Nationwide

Note: Second Individual Assignment is due at the beginning of the class!

Class 25 Review Session

April 11

Review of the past exams

Class 26 Exam 2

April 13

Class 27 Pension Funds

April 18

Guest Lecturer: Brian Grinnell, Chief Actuary, STRS Ohio

Class 28 Case Discussion: Chase Manhattan Corporation

April 20

Note: Case write-up is due at the beginning of the class!

Topics: Bank Mergers
Value Creation in Corporate Restructurings

Required Reading:

Case: Chase Manhattan Corporation: The Making of America's Largest Bank [CP]