ECON 3090-002/FINN 3000-002  
Economic Policy and Financial Crises  
UNC Charlotte, Department of Economics, Fall 2014

1. Contact Information

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(Note: This telephone number is shared with other adjunct professors, as a result I may not receive your message. Accordingly, e-mail is the preferred method of communication.)

2. Important Dates & Times

Class Meetings:

Tuesday and Thursday, 9:30AM - 10:45AM  
Belk College of Business, Friday Building, Room 112

Deliverables:

Homework:

Assignment One: Handed into me by the start of Class 6, on Thursday September 4
Assignment Two: Handed into me by the start of Class 12, on Thursday, September 25

Briefing Paper: Handed into me by the start of Class 15, on Thursday, October 9

Class Presentations:

Groups 1 - 4: Class 25, on Thursday, November 13
Groups 4 - 8: Class 26, on Tuesday, November 18
Groups 9 and 10: Class 27, on Thursday, November 20

Final Exam: Thursday, December 11, 8:00AM - 10:30 AM

3. General Information

Course Description: ECON 3090/FINN 3000. Financial crises have unfortunately been regular occurrences of market economies throughout world history, including bubbles, bank
failures, and liquidity crises. This class will examine multiple crises and the governmental policy responses to them, ranging from Tulipmania, to the South Sea Bubble, to the Great Depression, to the S&L crisis, to the 1987 stock market crash, to Dot.com bubble, to the Great Recession, with a focus on the actions the federal government has taken to prevent another financial crisis (Dodd-Frank). We will examine topics including securitization, credit regulation, banking regulation, and the role of financial market actors such as hedge funds. Prerequisites: ECON 2101 and ECON 2102.

**Course Objectives:** Conversant in using the financial terms and concepts discussed, understand the major theories purporting to explain financial crises, evaluate governmental responses from a legislative and regulatory policy perspective.

**Your responsibilities:**

1) Come to class, having read and considered the assigned material and questions (listed below).
2) Actively participate in inter-active class discussions.
3) Hand in assigned homework.
4) Write an 8 - 10 page “briefing” paper with a one-page executive summary on an assigned national financial policy subject area that arguably was a factor in the creation of the "perfect storm" that lead to the Great Recession and any legislative and/or regulatory actions subsequently taken in, or as a result of, the Dodd–Frank Wall Street Reform and Consumer Protection Act (Pub.L. 111-203, H.R. 4173, found at http://thomas.loc.gov/cgi-bin/bdquery/z?d111:H.R.4173). **Further details on the paper are set forth below.**
5) Prepare and present to the class as part of an assigned team an oral 15-20 minute PowerPoint presentation with other students who have been assigned the same subject issue paper. **Further details on the team presentation are set forth below.**
6) Take the final exam

**NOTE:** Homework assignments and the briefing paper should be typed, double spaced, using Times New Roman font (size 12), with one-inch margins on all sides; citations and references must follow APA format. Include a cover page containing the title of the assignment, your name, my name, the course title, and the date. The cover page, one-page executive summary and the reference page(s) are not included in any required assignment page length. Homework assignments and the briefing paper are to be solely your own work product, without assistance of other classmates/friends, etc.

All written assignments are to be submitted in person to me and are due at the beginning of class - before I begin the day's discussion - any assignment submitted to me by any other means will not be considered for any credit!
Grading:

Class participation: 10%
Homework 10%
Written paper 30%
Team Presentation: 20%
Final Exam: 30%

Paper

Imagine you are a staff member of a newly elected Senator who has just been appointed to the Senate Banking Committee. The Senator is an independent self-made small businessman from a moderate state where political ideology must be carefully balanced against the needs and interests of the state's populous. The Senator ran for office on the platform of compromise and doing what is truly best for his/her state and the nation and wants to do everything in his/her power to live up to that promise. He/she has been advised by the Chairman of the Banking Committee that a number of hearings are planned over the course of the next year on Dodd-Frank and its implementation by the cognizant regulatory agency(s). The Chairman has also indicated that changes in Dodd-Frank are possible. He/she wants to be "up to speed and ready to go" when those hearings occur.

The Staff Director has assigned you write a paper on an assigned national financial policy subject area that arguably was a factor in the creation of the "perfect storm" that lead to the Great Recession and any legislative and/or regulatory actions subsequently taken in, or as a result of, the Dodd–Frank Wall Street Reform and Consumer Protection Act (Pub.L.111-203, H.R. 4173, found at http://thomas.loc.gov/cgi-bin/bdquery/z?d111:H.R.4173). The paper should include a background, discussion and recommendation section. The discussion section should present both sides of the issue, to include the advantages/disadvantages of the provision in Dodd-Frank. If regulations have not been issued, the Senator wants to know what action should be taken. If the cognizant regulator(s) have taken action to implement the provision, the Senator wants your assessment of that action. The recommendations section of your paper should state whether the provision should be modified (and if so how), or removed from law, as well as note any concerns with the regulatory actions taken to date.

Team Assignment

Imagine that the Senator's staff director assigned more than one staff member to independently examine the same policy area. Now, having received and reviewed each staff member's paper, the Chief of Staff has asked you and your fellow staff members to share each other's work, meet, discuss and evaluate each other's views, and develop a presentation for the Senator, comparing and contrasting any differing views, making a recommendation where there is consensus, or otherwise calling for the Senator's decision.

To facilitate the team presentation, I will be placing you in a group with several of your fellow classmates who were assigned to write a paper on the same national policy subject area. To the extent possible I will be pairing those of you who consider yourself to be of the
Chicago or Austrian school of economists (Friedman) with Keynesians. In addition, I will be paring finance majors with economic majors.

**Class structure:** This is not a lecture-format class. You need to come to class having read the assigned material and fully prepared to discuss it. We will start each class with a short introduction to the material from me. As economic and finance majors you are probably used to "numbers." This is, however, not a numbers course, it is a policy course. There will be little, if any, math. Given that this is a policy course, there will generally be no "right" answer - in fact I expect some disagreement among you and within the team groups. Furthermore, expect that I may choose to challenge your convictions.

**Course Resources:** The course does not require a textbook. I have included a listing of required readings for each class period below. For ease of reference I have attempted to provide you the URL where the document can be located wherever possible. Some readings may, however, only be available through the library and/or only be available through payment of a minor cost.

**Readings:** The readings are probably longer in pages per class than many other economic or finance classes. Somewhat mitigating is that many readings (a) are physically small, relatively large type face sources that are double-spaced, (b) contain many graphs, (c) need not be read with the same intensity you would read a textbook, and (d) are logically written. Furthermore, in circumstances where you are familiar with certain concepts, such as “CDO” or “securitization,” you will be able to quickly review the material. Because academic research and literature on the Great Recession continues to actively evolve, I have not been able to find a single text that is authoritative and objective (over two decades passed before an authoritative text was written on the Great Depression). As much of the literature has a distinct point of view, multiple sources ensure more than one opinion is presented.

The entire syllabus has been provided at course inception in recognition of your personal schedule and to enable reading in advance. I am aware that many of you work. I am also not unaware of the fact that UNC Charlotte now has a intercollegiate football team. This is, however, the first time this course has been taught at UNC Charlotte and the first time I have taught this course. In that vein, I reserve the right and privilege of changing and/or modifying the syllabus as we proceed through the semester. I also welcome your comments and suggestions as to particular areas you would like to focus on.

**General Rules**

**Attendance:** Classroom attendance is mandatory. We will be covering a substantial amount of material and the easiest way to keep up will be to attend class and actively participate in the discussion. Be on time and stay for the duration. If you do not plan to attend the entire lecture, please see me in advance or refrain from coming to class.

**Communication:** Communication with those outside of class while class is in progress is not acceptable. (In other words, turn off all communication devices prior to the start of
class.) Check your UNC Charlotte e-mail (username@uncc.edu) for correspondence and updates.

**Academic Integrity:** Academic misconduct (cheating) will NOT be tolerated. In addition, you have the responsibility to know and observe the requirements of University Policy 40 (The Code of Student Academic Integrity). This code forbids cheating, fabrication or falsification of information, multiple submissions of academic work, plagiarism, abuse of academic materials, and complicity in academic dishonesty. Academic evaluations in this course include a judgment that your work is free from academic dishonesty of any type; and grades in this course therefore should be and will be adversely affected by academic dishonesty. Students who violate the code can be expelled from UNC Charlotte. The normal penalty for a first offense is zero credit on the work involving dishonesty and further substantial reduction of the course grade. In almost all cases, the course grade is reduced to U. Copies of the code can be obtained from the Dean of Students Office. Standards of academic integrity will be enforced in this course. You are expected to report cases of academic dishonesty to me.

**Statement on Diversity:** The Belk College of Business strives to create an inclusive academic climate in which the dignity of all individuals is respected and maintained. Therefore, we celebrate diversity that includes, but is not limited to ability/disability, age, culture, ethnicity, gender, language, race, religion, sexual orientation, and socio-economic status.

**Tentative Course Schedule**

Below is a tentative schedule (as noted, there is no guarantee that we follow the schedule precisely). We may deviate from the schedule as the course progresses depending on time and it is your responsibility to keep up with adjustments made throughout the course.

Classes 1 & 2 (August 19 & 21) - **Introduction - Impact of the Great Recession**

Our first priority is to get organized. I want to learn about you and your career goals and I will give you the opportunity to learn about me. I will be handing out index cards asking for some information about you, your career goals, etc. From the information you provide I will be making team assignments and a seating chart (I know some would prefer not to have assigned seating, but I think assigned seating will be beneficial).

As you will learn, as a CEO of a Washington, D.C. financial trade association, I experienced the great recession first hand - it had a momentous impact on the industry my staff and I were hired to represent. I will spend a class session going through that with you. It was an experience I would never want to repeat or wish upon anyone else. I hope that my discussion of the real world impact will serve as not only as an introduction to the course, but also heighten your interest in this course.
Class 3 (August 26) - **Financial Crises - A Historical Perspective - Tulipmania**

**Readings:**

Knight, T. (2014)
Peculiar Facts From 500 Years of Finance
*American Association of Individual Investors Journal*
*(Copies will be distributed in advance of class)*
Was tulipmania irrational?
*The Economist*
http://www.economist.com/blogs/freeexchange/2013/10/economic-history

Garber, P.M. (1989)
Tulipmania
*The Journal of Political Economy*
http://ms.mcmaster.ca/~grasselli/Garber89.pdf

The tulipmania: Fact or artifact?
University of California, Los Angeles

New Evidence of the First Financial Bubble
Yale International Center for Finance

As a foundation, we will spend several class sessions discussing the financial crises that have occurred through-out history. As we do so, think about what a crisis is – is it a set of economic conditions? A failure of governance? The result of bad choices, or of uncontrollable forces? Can such events ever be prevented? If so, what are the consequences from a business perspective? Look for parallels.

The first documented financial crisis ("Tulipmania") occurred in the early 1660's in Holland. Knight attempts to provide history's lesson as a template to investors (note that the article is from the *American Association of Individual Investors Journal*). Garber presents a relatively comprehensive look at tulipmania, discussing the traditional view of its causes, and suggesting that the pricing for rare bulbs reflected normal pricing behavior while offering no explanation for the speculation in common bulbs. Thompson takes a different approach. In a rather densely written, but precise account he argues that the market for tulips was an efficient response to changing financial regulation. In a more recent paper, Frehen, Goetzmann and Rouwenhorst suggest that innovation was the key driver.
Discussion Questions:

1) What is a “financial crisis”? Is it any crisis involving money? A crisis involving regulatory failures? When GDP drops by some percentage? Is it something that we can only define as, "We know it when we see it?" How, if at all, would you distinguish a crisis from a bubble? Is it necessary we come to joiner on a formal definition?

2) What do you believe was the cause(s) of tulipmania?

3) Do you believe irrationality can ever be employed to describe the basis for a financial crisis or is there always some rational explanation?

4) Is the "irrationality" explanation "one of laziness" as asserted in The Economist?

5) Who is right, Gardner or Thompson?

6) Do you agree with Knight - is there a history lesson to be learned? If so, why haven't we learned it, or have we?

7) Was innovation a factor in tulipmania? If so, from your basic knowledge of the Great Recession can you draw any parallels?

Class 4 (August 28) - Financial Crises - A Historical Perspective - The Mississippi and South Sea Bubbles

Readings:

Riding the South Sea Bubble
American Economics Review

Walsh, P (2012)
Writing the History of the Financial Crisis: Lessons from the South Sea Bubble,
School of History and Archives, University College Dublin,
http://www.academia.edu/1564001/Writing_the_History_of_the_Financial_Crisis_Lessons_from_the_South_Sea_Bubble

Temin and Toth provide a case study of a well-informed investor in the South Sea bubble, arguing that from the perspective of a sophisticated investor, it was profitable to ride the bubble. Drawing on his research on Ireland and the South Sea Bubble, Walsh seeks to explore how historians have dealt with past economic and financial crises and where possible glean any lessons learned.

Discussion Questions:

1) What do you believe was the cause or causes of the South Sea Bubble?

2) Is an understanding of the human impact of financial crisis, as asserted by Walsh important?
3) Do you believe, as postulated by Temin and Toth, that investors in many cases knew that the South Sea Stock was overvalued? If so, why did they continue to buy shares in the stock?
4) What is synchronization risk and how, if at all, did it lead, or contribute, to the crisis?
5) Do you agree with Walsh that the global financial crisis of 2007 ("The Great Recession") was not as unprecedented as some have postulated?
6) Why would politicians and policy makers find it attractive to take the position that the Great Recession was unprecedented and could not be foreseen?
7) Can you draw any parallels to tulipmania?

Class 5 (September 2) - Financial Crises - Historical Perspective - The Bank Panic of 1907

Readings:

Lessons from the Panic of 1907
Economic Review

Tallman, E.W. (November 2012)
The Panic of 1907
Federal Reserve Bank of Cleveland

Watch the video: The Panic of 1907: Lessons Learned from the Market's Perfect Storm
http://millercenter.org/scripps/archive/forum/detail/3838

Tallman summarizes the academic literature on the panic, noting that despite the fact the panic occurred over 100 years ago, research continues to uncover data and underexploited connections between institutions. Tallman and Moen examine the circumstances leading to, and the intervention measures taken during, the panic. In the video Robert Bruner, Dean of the University of Virginia's Darden Graduate School of Business Administration and Sean Carr, Director of Corporate Innovation Programs at the Darden School's Business Institute, discuss the panic of 1907 and the financial crisis of 2008.

Discussion Questions:

1) What caused the crisis of 1907?
2) Do you agree that failure in financial markets is like a vortex in a sink - a pernicious reinforcing downward cycle that gains in momentum and force the longer it runs with ever increasing velocity? If so, how can they be stopped?
3) Drawing on your basic knowledge of the Great Recession, what are the differences between the panic of 1907 and the Great Recession?
4) Do you agree that investors and depositors get with they deserve? If so, from your basic knowledge, was that the case in the Great Recession?
5) What role did financial intermediaries play in the 1907 panic?
6) Did the lack of regulation of some entities contribute to the panic?
7) What intervention measures were taken? How effective were the intervention measures?
8) What role did any unequal regulation of financial institution play in the panic?
9) What role did trust companies play in the panic?
10) Why did the panic of 1907 lead to the creation of the Federal Reserve?
11) Do you agree with Roosevelt's assessment of businesses?
12) What regulatory failures, if any, can be attributed to the crisis?

Classes 6 & 7 (September 4 and 9) - Financial Crises - A Historical Perspective - The Great Depression

Homework Assignment One:

Research and provide a listing and brief summary of the laws enacted during and immediately following the Great Depression passed and signed into law to facilitate the nation's recovery and/or improve the nation's financial system. Be prepared to discuss each.

Due at the beginning of class 6, on September 4.

Readings:

Roosevelt, T.R. (1933)
Fireside Chat
http://www.mhric.org/fdr/chat1.html

The Nation in Depression
Journal of Economic Perspectives 7(2), 19-39
http://eml.berkeley.edu/~cromer/great_depression.pdf

Where Is There Consensus among American Economic Historians?
Journal of Economic History, 55(1), 1439-154
http://employees.csbsju.edu/jolson/econ315/whaples2123771.pdf

Butkiewicz (2002)
Reconstruction Finance Corporation
EH.Net Encyclopedia
http://eh.net/encyclopedia.article.butkiewicz.finance.corp.reconstruction
Money, Gold and the Great Depression
Remarks at the H. Parker Willis Lecture on Economic Policy, Washington and Lee University

Romer, C. (1992)
What Ended the Great Depression
*The Journal of Economic History* 52(4), 757-784
http://eml.berkeley.edu/~cromer/What%20Ended%20the%20Great%20Depression.pdf

An interview with Christina Romer on Learning from the Great Depression (2012)
Five Books
http://fivebooks.com/interviews/christina-romer-on-learning-great-depression
An interview with Robert Barrow on Lessons from the Great Depression (2012)
Five Books
http://fivebooks.com/interviews/robert-barro-on-lessons-great-depression

There is a plethora of material on the Great Depression. Former Federal Reserve Board Chairman Ben Bernanke wrote his doctoral thesis on it. Unfortunately, our time to discuss it is limited. The FDR fireside chat is also available in an audio file at http://www.presidency.ucsb.edu/mediaplay.php?id=14540&admin=32 and interesting as an example of an initial response to a crisis. Listen to it as well as read it – the tone of FDR’s voice is an important part of its effectiveness.

Romer (The Nation in Depression) examines he ways in which the U.S. experience resembled, and fundamentally differed, from that of other countries. Whaples (p 143 - 144 and 149) presents the results of a survey of American economic historians on causes of the Great Depression. Butkiewicz provides an overview of the activities of the Reconstruction Finance Coproation (RFC).

In his remarks at Washington and Lee University, Bernanke discusses the causes of the Great Depression and offers a number of lessons learned. Romer (What Ended the Great Depression) examines the source(s) of recovery from the Great Depression. The Five Books interview with Romer briefly addresses Romer’s thoughts on the lessons of the Great Depression and provides her recommendations for five books on the Great Depression. The interview with Barrow takes issue with some of the common assumptions about the Great Depression, while also providing his thoughts on the Obama administration’s Great Recession stimulus package.

**Discussion Questions:**

1) What are the competing explanations for the Great Depression? Which do you find most convincing? Why?
2) What do you believe was the cause, or causes, of the Great Depression?
3) What regulatory failures, if any, can be attributed to the Great Depression?
4) What is your personal view on each of the questions Whaples asked?

5) Does it matter that economists have not been able to reach consensus on the causes and cure for the Great Depression?

6) To what extent was monetary policy a factor in the Great Depression?

7) How did the Roosevelt Administration respond to the Great Depression? What lessons on how to handle a crisis are there from that response?

8) Some have argued that when a financial crisis occurs, it is important for government to “do something” even if the “something” isn’t particularly well thought out or executed. (This is often referred to as the “throw money out of helicopters” theory and why former Federal Reserve Board Chairman Ben Bernanke was nick-named, "Helicopter Ben.") Was that true in the Great Depression? Why/why not?

9) How was the Great Depression being used in the debate over our financial crisis? (No reading on this, just think about what you may have seen/and/or heard/or read.)

10) Imagine you have read these materials and are an aide to President Bush in September 2008. The President asks you what he can do to avoid being thought of as a “second Herbert Hoover” – what is your advice?

11) What were the source(s) of recovery from the Great Depression?

12) What changes in U.S. federal regulatory structure occurred as a result of the Great Depression?

13) What parallels exist to the Great Recession? If you believe there are parallels between the Great Depression and the Great Recession, why didn't we learn from them?

Classes 8 & 9 (September 11 and 16) - Financial Crises - A Historical Perspective - The Saving and Loan Crisis

Readings:

The S&L Crisis: A Chrono-Bibliography
The Federal Deposit Insurance Corporation
http://www.fdic.gov/bank/historical/s&l/

Rothchild, J. (1993)
A Wonderful Life: S&L Hell: The people and the politics Behind the $1 Trillion Savings and Loan Scandal
Los Angeles Times Book Review
http://articles.latimes.com/1993-05-09/books/bk-33020_1_kathleen-day
Bode, K. (1993)
Where the Streets Are Paved With Depositors
*The New York Times*
http://www.nytimes.com/1993/05/16/books/where-the-streets-are-paved-with-depositors.html

Laughlin, R.J. (1991)
Causes of the Savings and Loan Debacle
Fordham Law Review 59(6), S301-S321
http://ir.lawnet.fordham.edu/cgi/viewcontent.cgi?article=2920&context=flr

Cassak, L. (2011)
How Governments React to Financial Crises: The Saving and Loan Crisis as a Test Case
The Foundation for Law, Justice and Society in affiliation with The Centre for Socio-Legal Studies
University of Oxford
https://www.academia.edu/1328422/How_Governments_React_to_Financial_Crises_The_Savings_and_Loan_Crisis_As_a_Test_Case

The Savings and Loan Crisis and Its Relationship to Banking
Federal Deposit Insurance Corporation
http://www.fdic.gov/bank/historical/history/167_188.pdf

The U.S. Banking Panic of 1933 and Federal Deposit Insurance
Harvard Business School Case Study
http://hbr.org/product/The-U-S--Banking-Panic-of/an/799077-PDF-ENG

Start with the FDIC's chrono-bibilography, it provides a great reference point from an historical perspective. Kathleen Day, a reporter for *The Washington Post*, broke many of the major stories on the S&L crisis. She later took a leave of absence to write *S&L Hell: The People and the politics behind the $1 Trillion savings and loan scandal*. *S&L Hell* offers a comprehensive account of the causes of the crisis, spotlighting the role of the regulators, thrift operators, lobbyists, and politicians. Day's book could be a course into itself. The book reviews gives you a glimpse. Laughlin provides a nice overview of the crisis. Cassak details the regulatory responses as the crisis unfolded. The Harvard Business School case study is taught relatively early in the schools required course *Business, Government and the Information Economy* and serves as a foundation for the analysis of modern financial crises.

**Discussion Questions:**

1) What did commercial banks do in the 1920s?
2) What do you believe were the causes of the S&L debacle?
3) How would you judge the government's reaction to the crisis?
4) What role did deposit insurance play in the crisis?
5) Should Roosevelt have agreed to deposit insurance?
5) Does deposit insurance (note it is now at $250,000) create systemic risk? If so, how?
6) Does the separation of investment and commercial banking make sense?
7) What regulatory failures, if any, can be attributed to the crisis?
8) Do you agree with Laughlin that timely action could have avoided the crisis?

Class 10 (September 18) - Financial Crises - A Historical Perspective - The 1987 Crash

Readings:

Ritholtz, B. (2012)
Art Cashin: Black Monday, An Unforgettable Single Day
The Big Picture
http://www.ritholtz.com/blog/2012/10/art-cashin-black-monday-an-unforgettable-single-day/

Fraim, R. (2012)
Revisiting the 1987 Crash
The Big Picture
http://www.ritholtz.com/blog/2012/10/revisiting-the-1987-crash/

Vigna, P. (2012)
Crash of ’87 Recollections: "My Singularly Worst-Day Ever"
The Wall Street Journal
http://blogs.wsj.com/marketbeat/2012/10/19/crash-of-87-recollections-my-singularly-worst-day-ever/

Ritholtz, B. (2011)
October 19, 1987: Dow Down 22%
The Big Picture

What Caused the 1987 Stock Market Crash and Lessons for the 2008 Crash
Social Science Research Network

Crash-Testing the Efficient Market Hypothesis
National Bureau of Economic Research 3, 277-286
http://www.nber.org/chapters/c10957.pdf
Skim the first 4 articles that are included to give you a sense of the impact of the 1987 crash.

McKeon and Netter assert that the large three-day drop from October 14 to October 16 led to the Monday morning crash of October 19, 1987. Shiller provides the results of a survey sent to individuals and institutional investors inquiring about their behavior during the crash. Carlson reviews the events surrounding the crashes and discussed the Federal Reserve's response.

Discussion Questions:

1) Imagine that you were running the floor for PaineWebber on Monday morning, October 19, how would you have reacted that day?
2) Should the crash have been anticipated given the substantial market downturn the Thursday and Friday immediately preceding?
3) How do you interpret the results of Shiller's survey?
4) How do you judge the Federal Reserve's response? Did it save the day?
5) Do you believe in the efficient market hypothesis? If so, how do you rationalize the October 1987 crash?

Class 11 (September 23) - Financial Crises - A Historical Perspective - The Dot.com Bubble

Readings:

A Behavioral Model of the Dot.com Bubble and Crash
Routhledge Publishing
Redhead examines market bubbles and crashes and suggests that psychology and sociology are, at a minimum, as important as financial and economics in explaining such events. Morris and Alam document the decline in the relationship between market value and traditional accounting information during the bubble, while recognizing irrational exuberance and the aggressiveness of financial analysis forecasts as possible explanations for the Dot.com bubble. Goodnight and Green assert that economics and rhetoric should switch places.

Discussion Questions:

1) Define an economic bubble?
2) Was the Federal Reserve's monetary policy responsible for the Dot.com bubble? To what extent?
3) In 1997 Congress passed the Taxpayer Relief Act of 1997 lowering the maximum tax on capital gains for individual investors from 28 percent to 20 percent for assets held more than 18 months. The dividend tax rate was left unchanged. Might this have impacted the desire for, and volatility of, growth stocks?
4) Are psychology and sociology as important as finance and economics in explaining events such as the Dot.com Bubble and crash?
5) To what extent was the Dot.com bubble attributed to the decline in market value and traditional accounting? To the irrational exuberance theory? To the aggressiveness of financial analysts' forecasts? Should economics and rhetoric switch places as postulated by Goodnight and Green?
6) What regulatory failures, if any, can be attributed to the crisis?

Class 12 (September 25) - The Financial Regulatory System

Homework: Write a short (3-5) page briefing paper for your Congressman explain the financial system in the United States, noting the concerns that Senator Paul and others have raised regarding the Federal Reserve system. Make a recommendation as to any restructuring you might deem appropriate.

Due at the beginning of class 12 on September 25
Readings:

Kaplan, T. (2009)
The Federal Reserve: What the Hell Is It?
*Vanity Fair* Politics and Power Blog,

Voakes, G. (2012)
Infographic: Uncovering The Fed
*Business Insider*

Hudson Telic, L. (2008)
The U.S. Financial Regulatory System
Council on Foreign Relations

Jickling, M. and Murphy, E V. (2010)
Who Regulates Whom? An Overview of U.S. Financial Supervision
Congressional Research Service
http://www.fas.org/sgp/crs/misc/R40249.pdf

Statement of Gene L. Dodaro
Acting Comptroller General of the United States
Financial Regulation: A Framework for Crafting and Assessing Proposals to Modernize
the Outdated U.S. Financial Regulatory System
Testimony Before the Congressional Oversight Panel
GAO-09-310T (2009)
http://digital.library.unt.edu/ark:/67531/metadc291487/m2/1/high_res_d/121456.pdf

Eichengreen, B. (2010)
The Last Temptation of Risk
*The National Interest*
http://nationalinterest.org/article/the-last-temptation-of-risk-3091

Now that we have completed our historical review, let's take a look at the federal financial regulatory system. As you read these materials, imagine you are a congressional staff member to a new member of Congress, who has just been assigned to the House Financial Services Committee. This new member of Congress is a small business person who has no background in financial services other than that with respect to the operation of his/her small business. He/she needs to learn about the regulatory structure overseeing the financial services industry and has heard a lot about concerns with the Federal Reserve. The staff director has asked you to "dig into all this" and brief your congressperson on the crisis. Think about how you would summarize the financial system for a busy lawmaker.
Kaplan provides a capsule overviews of the Federal Reserve. In his infographic, Voakes explores the controversy over the Federal Reserve, including some interesting facts. Dodaro's statement provides a suggested framework for modernizing the U.S. financial regulatory system. Eichengreen (an influential and important macro-economist) attempts to explain why economics let us down in predicting/preventing the crisis.

Discussion Questions:

1) Now that we have completed our historical look at crises prior to the Great Recession, lets again discuss: What is a “financial crisis”? Is it any crisis involving money? A crisis involving regulatory failures with respect to financial issues? When GDP drops by some percentage? Is it something we only know when we see it? Is a formal definition useful? How, if at all, would you distinguish a crisis from a bubble? Has your opinion on any of these questions changed since the course first began?

2) What is the Federal Reserve? Why does it exist? Imagine you work for a Member of Congress who asks you, "setting aside the politics is there any substance to Rand Paul's concerns?" How do you answer?

3) Think about the different regulatory agencies described by Jickling and Murphy. Why do we have so many regulators? Are there too many? Does the number of overlapping regulators provide the opportunity for regulatory arbitrage? What is different about the various agencies? Which ones, if any, failed (and how), based on your current understanding of the economic events and policies leading to Great Recession?

4) Do you agree with Eichengreen that economists failed us by not being able to predict the crisis? If so, how do we avoid another crisis?

5) What changes, if any, would you make in the U.S. financial regulatory system and why?

Class 13 (September 30) - Background on derivatives, hedge funds, short selling and collateralized mortgage obligations

Readings:

Credit Default Swaps (CDS) Primer 
Nomura Securities International, Inc  
http://www.securitization.net/pdf/content/Nomura_CDS_Primer_12May04.pdf

Nomura Securities International, Inc  
Some argue that hedge funds, derivatives and short selling played a role in the Great Recession. These readings introduce some of the crucial financial instruments arguably involved in the financial crisis. Our goal is for you to have an understanding of (1) why these instruments appeared; (2) why their use may have become problematic; and (3) what regulatory steps might be appropriate and which ones might not be. The Whitten and Adelson articles are clear, concise explanations of what CDO and CDS instruments are. Note that these were written before the crisis by a firm that sold CDS and CDO products. (How does that affect how you read these articles?) The Hawkesby piece endeavors to describe derivatives in simple terms. The Shadab article is a post-crisis, skeptical analysis of regulatory efforts plus a good description of how the CDO-CDS market works. (Shadab is one of the best writers on financial regulation around.)

Discussion Questions

1) What should be the goals of regulation of hedge funds and derivatives?
2) Why haven't hedge funds, short selling, and derivatives been regulated to prevent the problems critics think exist with them?
3) Suppose you wanted to regulate one or more of these products, how would you do it? What agency would be responsible?
4) Why did regulators propose/adopt the measures described by Shadab despite the problems with these solutions (also described by Shadab)? What does this tell us about the political process and “fixing” financial regulation?
5) What problems should regulators being trying to solve with respect to CDS/CDO markets? What problems should they leave to market mechanisms? Who should regulators protect in regulating CDS/CDO markets?

6) Given the need for risk management described by Stowe, what new problems might regulating CDS/CDO markets create? What can regulators do to avoid these problems?

7) Given the global nature of financial markets, can one country effectively regulate such entities? Even if most countries cannot, can the United States?

8) Although CDOs and CDSs are both instruments of credit risk transfer and often analyzed together, Shadab's identifies several institutional, regulatory, and economic distinctions between CDOs and CDSs, and notes how these differences explain the differing outcomes experienced by the instruments during and after the crisis. Can these distinctions even be further developed, or may they not be as important as Shadab implies?

Classes 14 and 15 - (October 2 & 9 (Student Recess October 6 & 7)) - **Background on the Great Recession**

**Readings:**

Gorton, G. and Metrick, A (2012)
Getting Up to Speed on the Financial Crisis: A One-Weekend-Reader's Guide
Yale University and the National Bureau of Economic Research

Lo, A.W. (2012)
What An Economist Learned From Reading 21 Books About The Crisis

Temin, P. (2010)
The Great Recession and The Great Depression
National Bureau of Economic Research

Reinhardt, C. and Rogoff, K (2009)
Preface: This Time It's Different: Eight Centuries of Financial Folly
Munich Personal RePEc Archive
http://mpra.ub.uni-muenchen.de/17451

Book Review: This Time It's Different: Eight Centuries of Financial Folly
*The Region* September, 66-71
https://www.minneapolislfed.org/publications_papers/pub_display.cfm?id=4540&
Steward, J.B. (2009)
Eight Days, The battle to save the American Financial System
*The New Yorker*
http://www.newyorker.com/magazine/2009/09/21/eight-days

Greenspan, A. (2010)
The Crisis
Brookings Paper on Economic Activity, Spring 2010, 201-246
http://www.brookings.edu/~/media/Projects/BPEA/Spring%202010/2010a_bpea_greenspan. PDF

Yandle, B. (2010)
Lost Trust: The Real Cause of the Financial Meltdown
*The Independent Review*, 14(3), 341-361
http://www.independent.org/pdf/tir/tir_14_03_02_yandle.pdf

Ritholz, B., (2013)
Barry Ritholz o Causes of the Financial Crisis
*Five Books*

Acharya, V.V, Philippon, T., Richardson, M., and Roubini, N.

Let's now turn to the Great Recession. We will be debating the causes for decades (as we are still debating the causes of the Great Depression). Gorton and Metrick cover the key facts and mechanisms in the build-up of risk, the panics in the short-term debt markets, the policy reactions and the real effects of the crisis. Lo reviews a diverse set of twenty-one books, some written by academics, some by journalists and one by a former Treasury Secretary. Temin discusses the parallels between the Great Depression and the Great Recession. The title to Reinhardt and Rofoff's book, This Time It's Different: Eight Centuries of Financial Folly, says it all. *The New Yorker* article pieces together an account of the crisis from interviews with participants and observers, Greenspan asserts that heavy securitization of the subprime mortgage market triggered the crisis, Yandle blames politicians and the Fed. Ritholz blames regulatory changes and the Fed Acharya, Philippon, Richardson, and Roubini call for a redesign of the regulatory overlay of the global financial system.

**Discussion Questions:**

1) What do you believe was (were) the cause(s) of the Great Recession?
2) Was there a single spark that lit it off?
3) Why can't economists come to joinder on the cause(s)?
4) What does the fact economists cannot come to joinder on the cause(s) indicate about the profession?
5) Was the Great Recession a case of people losing their fear in the climate of prosperity, thereupon becoming more relaxed (like someone who has had a little too much to drink), becoming lulled in a false sense of security, safety and prosperity, thereafter cutting corners and building in the kind of risks that end in financial crisis?
6) Was the Great Recession no different than any other financial crisis, or was it truly different?
7) To what extent did technology and innovation play in the crisis?
8) Why didn't the greatest financial minds in the country (Greenspan, Bernanke) see it coming?
9) Should Lehman have been saved?
10) What parallels can you draw to the Great Depression?

Class 16 – (October 14) - The Housing Bubble, Subprime Mortgages & Securitization

Readings:

Katz (2010)
The Rise and Fall of Fannie Mae: A Timeline
AOL Real Estate

A Brief History of Fannie Mae and Freddie Mac
Time Magazine
http://content.time.com/time/business/article/0,8599,1822766,00.html

Averting Financial Crisis
Congressional Research Service
http://assets.opencrs.com/rpts/RL34412_20080321.pdf

Fannie Mae and Freddie Mac in Conservatorship
Congressional Research Service

Kosar, K. (2007)
Government Sponsored Enterprises (GSEs): An Institutional Overview
Congressional Research Service
http://fas.org/sgp/crs/misc/RS21663.pdf
Housing, Global Finance, and American Hegemony: Building Conservative Politics One Brick at a Time
Comparative European Politics 6, 262-284

Managing a $700 Billion Bailout: Lessons from the Home Owners’ Loan Corporation and the Resolution Trust Corporation
http://www.businessofgovernment.org/sites/default/files/ManagingtheBailout.pdf

Doherty, B. (2009)
The Housing Boom and Bust
Reason.com

Cardan, A. (2010)
The Booked Review: "The Housing Boom and Bust"
Forbes

Thomas Sowell on the root causes of the mortgage lending crisis
Wintery Knight Blog (2011)

Gintis
Review of Thomas Sowell, The Housing Boom and Busy (sic)
University of Massachusetts Amherst

Democrat Barney Frank admits his role in causing the recession (2010)
Wintery Knight Blog

Watch The You Tube Video: SubPrime Mortgage Mess Explained
https://www.youtube.com/watch?v=q8hjUei-Nwo

Watch the Video
Thomas Sowell on the root causes of the mortgage lending crisis
The CRS studies outline some of the basics issues and facts involved in the subprime/housing bubble. The timeline from AOL Real Estate provides a brief history of Fannie and Freddie. The *Time* article, published just before the September 2008 conservatorship of Fannie and Freddie, provides a further historical synopsis and overview of the 2 main government actors. The book reviews of Sowell’s *The Housing Boom and Bust*, summarize Sowell's conservative, free-market assessment of the problem. The Schwartz article is a left-wing critique of the causes of the crisis. These readings should (a) give you an overview of the issue and (b) provide examples of quite different explanations for the solutions offered by those who favor markets and are suspicious of governments and those who find markets questionable and put more trust in the public sector.

**Discussion Questions:**

1) What were the causes of the housing bubble/subprime crisis?
2) What role did securitization play in the crisis?
3) Did Freddie and Fannie contribute to the problem? If so, what might be done to prevent such problems in the future?
4) What is the role of Congressional oversight in supervising GSEs like Freddie and Fannie? Do some research in news archives – what sort of complaints do people have about how Congressional oversight was handled? What criticisms have been raised about the role of individual Congressmen and Senators with respect to oversight of Freddie and Fannie?
5) What is the role of Executive branch in supervising GSEs? Should GSEs be treated differently than administrative agencies directly responsible to the President (e.g. the Department of Housing and Urban Development)? Was the GSE structure appropriate for Freddie and Fannie?
6) What kind of solutions do Schwartz and Sowell suggest to prevent the problems that produced the housing bubble and subprime crisis in the future? Which is more convincing? Why?

Classes 17 and 18 (October 16 and 21) - **The Financial Crises Inquiry Report**

The Financial Crisis Inquiry Report (2011)

The Financial Crisis Inquiry Report is over 600 pages in length with appendices. Reviewing the report in its entirety would take a semester. That said, as noted in a January 2011 article by Gretchen Morgenson in the *New York Times*, the report is in and of itself, "A Bank Crisis Whodunit with Laughs and Tears." The commission was created "to examine the causes of the financial and economic crisis in the United States." Its statutory instructions set out twenty-two specific area for inquiry and called for the examination of the collapse of major financial institutions that failed, or world have failed if not for exceptional assistance from the government. The commission was not asked to offer policy recommendations or
evaluate federal law (TARP) (evaluation of TARP was undertaken separately by the Congressional Oversight Panel and the Special Inspector General for TARP). The Commission members were appointed to an independent 10-member panel, six members appointed by the Democratic leadership of the Congress and four members by the Republican leadership. As you might, therefore, surmise, there was disagreement on the final report, with dissenting views. Focus on the preface (pp. xi-xii), the Conclusion of the Commission (p. xv - xxviii), and the dissenting views (pp. 411-439 and 443-538 (read the introduction and summary of Wallison's dissent, skimming the remainder (485-538)). Note that not even the dissenters agreed!

Discussion Questions:

1) There is disagreement among the commissioners as to the extent that the lack of federal regulations and federal regulatory supervision contributed to the crisis. Which side do you take? Why?
2) Do you believe, as the majority asserts, that with proper federal regulation and supervision the crisis could have been avoided?
3) What do you believe were the essential causes of the crisis? To what extent did each cause contribute to the crisis? Said another way, had any cause or causes been eliminated or mitigated in some way, could the crisis have been avoided?
4) Was there a "spark" that lit the crisis? If so what was it?
5) Do you agree with Wallison that given that the Congress moved forward with the passing of Dodd-Frank before the completion of the commission's work, "Why have the commission at all?"
6) Wallison assets that none of the reasons cited by the commission alone, or in combination, caused the crisis? Do you agree? If so, what do you think cause the crisis?
7) Why couldn't the commissioners reach an agreement?
8) What does the fact the commissioners could not reach agreement portend for the country?
9) What role(s) should government play in housing policy?
10) Was the government's housing policy a contributing factor to the crisis? If so, to what extent?
11) To what extent did the Federal Reserve's monetary policy contribute to the crisis?
12) What is the difference between a bubble and a crisis? Does every bubble lead to a crisis?
13) What is a non-traditional mortgage (NTM)? To what extend did NTMs contribute to the crisis? If NTMs had not existed would the crises have been avoided?
14) Was the crisis a "perfect storm?" If so, can perfect storms ever be avoided? If so how? Is avoiding a perfect storm tantamount to removing risk from the financial market place?
Classes 19 and 20 - (October 23 and 28) - **Troubled Asset Relief Program (TARP)**

**Readings:**


While not a lengthy as the Financial Crisis Inquiry Report, the Final Report of the Congressional Oversight Panel on TARP (196 pages), is a lot to digest (the commission held over 20 hearings across the country). Read the Executive Summary (pp. 1-4) and Introduction (pp. 5 - 21). Then read the lessons learned under each subsection and the Conclusions and Lesson Learned (pp. 151 -160).

**Discussion Questions:**

1) Was TARP necessary?
2) In a crisis, is it always necessary for the government to be seen as doing something?
3) Think about each of lesson learned subsections - what are your thoughts on each?
4) Did TARP prevent another Great Depression? Why or why not?
5) Did TARP increase moral hazard?
6) Does TARP deserve the public stigma that exists when the "four letter acronym is mentioned?
7) How important is communication to the public when legislation such as TARP is created?
8) Did TARP only benefit Wall Street or where there also benefits to main street?
9) Think back to the South Sea Bubble and to the Frehen, Goetzmann and Rouwenhorst paper, New Evidence of the First Financial Bubble. To what extent was innovation in the securities market a contributor to the Great Recession?

Classes 21 and 22 - (October 30 and November 4) - **The Enactment of Dodd-Frank**

**Readings:**

*The Washington Post*

Irwin, N (2013) Robert Kaiser on Dodd-Frank: 'This example of Congress working also illuminated why it works so rarely'
*The Washington Post* Wonkblog
Before we dive into the substance of Dodd-Frank itself, we should review the Senate floor debate on Dodd-Frank. Illuminating of the political process is the book by Robert Kaiser, 'Act of Congress': How America's Essential Institution Works, and How It Doesn't. We do not have time to read the book, but it does provide an interesting account of how "sausage was made" in the passage of Dodd-Frank. The Congressional Record is long (over one-hundred pages). Note, however, that interspersed among the debate on Dodd-Frank are numerous other items - skip those in your reading.

Discussion Questions:

1) What were the arguments in favor of the passage of Dodd-Frank?
2) What were the arguments against the passage of Dodd-Frank?
3) Do you believe that Dodd-Frank should have been enacted? If you were a Senator or Congressman, setting aside party politics, would you have voted for it?
4) Are there any provisions that are of particular concern to you?
5) If you were Cam Fine would you have gone along with Frank?
6) Was as Kaiser asserts, Dodd-Frank an example of Congress working? Why or why not?

Classes 23 and 24 - (November 6 mad 11) - Dodd-Frank

Readings:

Brief Summary of the Dodd-Frank Wall Street Reform and Consumer Protection Act
United States Senate Committee on Banking, Housing, and Urban Affairs
http://www.banking.senate.gov/public/_files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf
The Dodd-Frank Act: a cheat sheet
Morrison & Forester (2010)

Dodd, C. (2012)
Why Dodd-Frank is Necessary
Político

Greenspan, A. (2011)
Dodd-Frank Fails to Meet test of our times
Financial Times
http://www.ft.com/intl/cms/s/0/14662fd8-5a28-11e0-86d3-00144feab49a.html#axzz39ufrv7ai

The Editors (2010)
Ten Reasons to Oppose Dodd Frank
National Review online
http://www.nationalreview.com/articles/243407/ten-reasons-oppose-dodd-frank-editors

Does Dodd-Frank Work? We asked 16 experts to Find out
The Washington Post Wonkblog

Konczal (2014)
Ignore the Naysayers: Dodd-Frank Reforms Are Finally Paying Off
New Republic
http://www.newrepublic.com/article/118814/dodd-frank-reforms-are-finally-paying

"Failing To End Too Big To Fail": An Assessment of Dodd-Frank Four Years Later (2014)

Boggs, J.C., Foxman, M. and Nahill, K.
Dodd-Frank At One Year: Growing Pains
Harvard Business Review online

Dodd Frank is over 2,000 pages in length and, four years later, is still fully implemented. Regulations issued total over 14,000 pages. Studying it in depth would encompass a course of several semesters. Davis Polk puts out a monthly progress report on its implementation.
(http://www.davispolk.com/Dodd-Frank-Rulemaking-Progress-Report). In its July 2014 report, Davis Polk noted that as of July 1, 2014, a total of 280 Dodd-Frank rulemaking requirement deadlines have passed. Of these 280 passed deadlines, 127 (45.4%) have been missed and 153 (54.6%) have been met with finalized rules. In addition, 208 (52.3%) of the 398 total required rulemakings have been finalized, while 96 (24.1%) of the rulemaking requirements have not yet been proposed.

Given that it is a law that is in existence and that Democrats see no threat of repeal, immediately or otherwise, it is much easier to find articles in opposition of Dodd-Frank than it is to find articles in favor. The reading list is therefore somewhat imbalanced.

Discussion Questions:

1) Was Dodd-Frank necessary?
2) Should Dodd-Frank be repealed?
3) Should Dodd-Frank have gone further in overhauling the financial regulatory system?
4) If you were Senator Scott Brown would you have voted against Dodd-Frank?
5) Does Dodd-Frank, as suggested by Alan Greenspan, fail to meet the test of our times?
6) What does the fact that nearly half of the rule-making remains say about the regulatory agencies?

Class 25 (November 13) - Presentations Groups 1 - 4

Class 26 (November 18) - Presentations Groups 4 - 8

Class 27 (November 20) - Presentations Groups 9 and 10

Class 27 - (November 20) - A Global Perspective

Readings:

Bordo, M. D. (2000)

Serven, L and Nguyen, H (2010)

China's Holdings of U.S. Securities: Implications for the U.S. Economy Congressional Research Service
Bordo focuses on the globalization of financial markets from an historical perspective of the past one-hundred-and twenty years. Serven and Nguyen survey the academic and policy debate on the role of global imbalances, their role in the inception of the global crisis and their prospects in the aftermath. The CRS report describes one important consequence of globalization – the United States’ dependence on foreign capital, particularly Chinese capital.

Discussion Questions:

1) How is the world financial system more global today than in the past? What are the advantages and disadvantages of that?
2) What kind of governments benefit from increased globalization? What kinds are harmed?
3) Should Americans care about the U.S. reliance on Chinese capital? Why/why not? Is this more, or less, important during a time of crisis?
4) In 2009 the British government advised the Caymanian government that “It would be unwise … to expect that the Cayman Islands’ prosperity can presume on an offshore tax haven status.” Does the financial crisis mean the end of tax competition?
5) Do you agree with Bordo that the role of an international crisis manger should be limited to providing liquidity to countries that cannot access the private capital makers and then to lend short-term on the basis of sound collateral and at a penalty rate? Why or why not?
6) Do you foresee an increase or decrease in global imbalances in the future? Why or why not?

Classes 28 and 29 (November 25 and December 2) - Financial Regulation

Readings:

A Short History of Financial Deregulation in the United States
Center for Policy and Research

Chairman, United Kingdom Financial Services Authority
The Financial Crisis and the Future of Financial Regulation
The Economist's Inaugural City Lecture
International Center for Monetary and Banking Studies and The Centre For Economic Policy Research

Princeton University Press

W.G. Hart Legal Workshop Institute of Advance Legal Studies

Journal of Economic Literature, 49(1), 120-128
http://www.aeaweb.org/atypon.php?return_to=/doi/pdfplus/10.1257/jel.49.1.120

Sherman provides a summary of the major regulatory changes over the past three decades. Lord Turner, the chair of the UK’s financial regulatory agency, in a controversial speech in 2009, argued that financial crisis revealed that Britain’s financial industry is too large and needs to be downsized. Brunnermeir, Crockett, Goodhart, Persaud, and Shin provide key recommendations on macro-prudential measures, as well as other minor issues such as the role of stress tests (focus on the conclusions and recommendations (pp. 63 - 66) and the Appendix: The Boundary Problem in Financial Regulation (pp.67 - 73). The Squam Lake Report, crafted by a group of 15 leading economists, provides specific policy recommendation on specific issues that might have mitigated the financial crisis (focus on Chapter 1, the introduction (pp. 5 -17) and Chapter 11, the conclusion (pp. 79-87). The articles by Glinavos and Hoshi discuss financial regulation in the context of the financial crisis.

Discussion Questions:

1) What regulatory changes instituted over the last 3-decades contributed to or exacerbated the crisis?
2) Is the financial industry too large? If so, should it be downsized as suggested by Lord Turner?
3) Be prepared to discuss each of the general conclusions and recommendations of Brunnermeir, Crockett, Goodhart, Persaud, and Shin. Do you agree? Are the recommendations politically feasible? Why or why not?
4) Do you agree with the principles set forth in the Squam Lake Report?
5) Would the financial crisis have occurred if the recommendations in the Squam Lake Report had been in place?
6) Are there limits to modern market capitalism as suggested by Glinavos?
7) Is there, as suggested by Glinavos, a direct link between the receding reach of the state and market instability?
8) How does one distinguish between the health of an individual financial institution and the stability of the entire financial system?