The course focuses on systemic risk, banking crises, financial stability and macroprudential policies. An emphasis will be on systemic risk and prudential policies in peripheral economies. Peripheral economies is defined here as peripheral European economies and emerging economies.

The course will start with an overview of the concepts of systemic risks and financial stability. Underlying reasons for banking crises which are (1) liquidity (fractional banking), (2) structural weakness and (3) leverage cycles. First is liquidity and bank runs and the role of the Central Bank as a liquidity provider and a lender of last resort. Before the last Global Financial Crises the underlying causes of financial crises in emerging economies was frequently structural weakness. Second we will look at the history of financial crises in emerging economies to gain an understanding of banking crises arising from structural weakness. Last we will look at the theory of credit and leverage cycles and some case studies of banking crises that seem to be caused by excessive growth in credit and leverage.

The next stage of the course will focus on most pressing threat to financial stability for peripheral economies. Capital surges and sudden stops. Excessive pro-cyclical capital flows may increase financial instability and this is a potential risk that emerging economies and peripheral economies face as they open up capital markets to the world. We will look at the risks associated with excessive capital flows, empirical evidence and innovating efforts to manage excessive pro-cyclical capital flows.

In the third phase of the course we will look at the Global Financial Crises of 2007-2008. Underlying causes and how they unfolded. The Sovereign debt crises that followed, including the crises in Greece. How regulation and supervision may have failed and how it is being overhauled now, including both new microprudential policy and the new macroprudential policies.

We will end the class with capital flow management which is one of the more pressing issues for peripheral and emerging economies that are opening up their capital account. Many countries have used prudential policies in an attempt to manage excessive pro-cyclical capital flows, such as Korea, Brazil and Chile. We will study the motivation for these policies, empirical evidence and the most recent research in this area.

Prerequisite: Introductory microeconomics and macroeconomics.

[Also GLBL311b and GLBL781b]