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## Message from the New Director, Professor Christopher Polk

I am excited to have the opportunity to be the new Director of the Financial Markets Group. Since its founding more than two decades ago, the FMG has become an international leader in academic research into financial markets, under the directorship of Professor David Webb. That reputation has been built through the cutting-edge theoretical and empirical research produced by the FMG research staff and doctoral students. These innovative ideas about financial markets originate from a variety of fields within economics and address a broad range of practical issues. As a consequence, the FMG has flourished from significant interactions with academic visitors and financial industry practitioners. Our recent and forthcoming

faculty appointments offer us the opportunity of pursuing new research grant applications and awards.

I look forward to promoting a new generation of ground-breaking financial research here at the FMG. As always, we will strive to disseminate our research, not just to the wider academic community but also to practitioners and policy makers. I hope to meet you at one of our frequent seminars and conferences soon.



**Professor Christopher Polk**  
Director, Financial Markets Group



**Professor Christopher Polk**

## Special Conference in Commemoration of Professor Antoine Faure-Grimaud

**20 November 2009**

A memorial event to celebrate the contributions of Professor **Antoine Faure-Grimaud** (1968-2009) was held in the Shaw Library. The event started with a welcome speech by David Webb, head of the Department of Finance, in which he remarked: 'It is with great sadness that we meet to remember the career of Antoine, but this event gives his colleagues, students and friends an opportunity to share recollections of what he achieved and the person he was, in the presence of Antoine's wife, children and parents.'

The conference was designed to commemorate the great contribution made by Antoine, both within the field of corporate finance and governance, and to the wider academic life at LSE and beyond. Antoine's co-authors were invited to present their joint work with him, as a tribute to his outstanding academic legacy, with an opportunity later in the day for some of his many academic friends to make more personal tributes.

*continues on page 2*



**Professor David Webb** introducing the event

## Special Conference in Memory of Professor Antoine Faure-Grimaud

continued from page 1



(left to right): **Dimitri Vayanos, Jean Tirole, Denis Gromb, Patrick Bolton, David Martimort and David Webb**

**Patrick Bolton** (Columbia University) presented the first paper of the day, entitled: 'Satisfying Contracts', which had been co-authored with Antoine during their four year collaboration. Motivated by the question of which direction the field of contract theory was heading, the paper addresses issues around control rights, the effect of conflicts on contracts, and contract incompleteness. Professor Bolton explained how he and Antoine had considered the trade-off between the advantage of thinking ahead, which allows agents to prepare for contingency, and costly complete contracts. Using a model of optimal contracting between two bounded rational agents, they had shown that optimal contracts may be incomplete and may allocate control rights to one or both parties, to give them the option to defer thinking and to let them postpone less important decisions until they become necessary.

**David Martimort** (University of Toulouse) started his talk by discussing the early years of Antoine's career, and in particular the ambitious project that had become his PhD thesis. He described how he and Antoine had first met at the University of Toulouse in 1992, and how they had then gone on to work together. At that time, partly as a result of the seminal model of collusion by Jean Tirole in 1986, the literature was covering topics such as collusion, incentive compatibility with coalitions, soft versus hard information, and coalitions with asymmetric information. Antoine was particularly interested in questions related to supervision with soft information and the convexity of agency costs, and had wanted to merge the Laffont-Tirole strand of the literature with the Bolton-Scharfstein strand, which seemed at the time to be an extremely ambitious project. Professor Martimort recalled how sceptical he had been at first; but then how successfully Antoine had managed to write a highly innovative and relevant PhD thesis. During his presentation, Professor Martimort drew a timeline from the seminal 1986 Tirole paper to more recent papers written by

Antoine; presenting Tirole's original model of collusion with hard information, exogenous transaction costs and an unusual collusion-proofness principle, and then showing Antoine's contributed to the literature in this area, which included his adding soft information and relaxing some of Tirole's initial assumptions.

Next, **Denis Gromb** (INSEAD) described how he and Antoine had started working together, and how their friendship had developed despite Antoine's suspicion of Parisians. The secrets of their partnership included their complementarity, trust and respect, he said. Recalling Antoine's wonderful sense of humour and his unique French accent, Professor Gromb gave the audience a fresh perspective on finance à la Antoine, presenting their joint paper, 'Public Trading and Private Incentives'. The paper studies the link between public trading and the behaviour of institutional investors. In their model, they explain how public trading generates prices that are more informative when information is more valuable. They also show how an entrepreneur's effort depends upon the variance of liquidity trades, the information sensitivity of the firm's stock, and the probability of a liquidity shock. He showed the implications of this work for understanding the entrepreneur's decision to go public, as well as for capital structure decisions and security design.

**Jean Tirole** (University of Toulouse) then presented on the subject: 'How to Jumpstart a Market: Thinking about Markets in the Tradition of Antoine Faure-Grimaud'. He began by discussing recent examples of evaporation of trust and market dry up, and the policy response to these events. He emphasised the need for fresh thinking if policy implications and the interaction between government intervention and the market outcome are to be properly understood, arguing that this issue is not only of theoretical interest, but is also central to the policy debate. He presented a framework



**David Webb** presenting an engraved plate to Antoine's wife, **Sönje Reiche**, on behalf of his colleagues at LSE



Antoine's drawings

showing the possible outcomes under *laissez faire* and interventionist governments. While reviewing the relevant literature, he reflected on Antoine's insight into the two-way interaction between regulation and markets, and the contribution he made to multiple areas of corporate finance, including conglomerates and cash-flow investment sensitivity, exit and securitisation mechanisms and, more generally, his contributions using mechanism design theory. In his summing up, Professor Tirole reminded the audience how creative Antoine was in his work, how generous he was to his colleagues and friends, how he was always smiling, and how he had been a scholar of the greatest integrity.

The next session of the conference consisted of personal tributes from some of Antoine's friends and colleagues.

**John Moore** (LSE) started the session by reflecting on Antoine's love for the institution of LSE and its people. Antoine was the most special of colleagues and friends, Professor Moore said, and his own decision to bring Antoine to the Department of Economics at the School had been one of the best decisions he had made. Antoine had brought fresh air to the university and was a generous colleague, he said, and his loss was a terrible one. In finishing, Professor Moore said how proud he was to have played a small part in bringing Antoine and Sönje together.

**Sridhar Arcot** (ESSEC) then presented a tribute on behalf of Antoine's PhD students. Antoine was the Department of Finance PhD programme director, and he was very close not only to the students he supervised, but also to all the students in the programme. Sridhar shared some anecdotes with the audience to illustrate the effort Antoine had put into his job, mentioning how he had lent a suit and tie to a student who had lost his luggage during the job market interviews, which was a theme that was familiar to all those who had known him. However, what was unknown to many of those in the audience was Antoine's artistic side. Sridhar presented a few of Antoine's unexpected 'comments' to his students' work in the form of the drawings reproduced here.

**Szuzsanna Fluck** (Michigan State University) talked about Antoine's unconventional approach to the theory of corporate finance. She also shared her experience of being Antoine's friend of more than ten years, of having the honour of being his co-author, and of having the pleasure to enjoy a meal cooked by him, praising him as a great chef.

**Sudipto Bhattacharya** (LSE) spoke next, saying that he found it impossible to say goodbye to Antoine, explaining how well their paper together, 'The Debt Hangover: Renegotiation with



Sönje Reiche, her children with Antoine, Marbod and Fereol, and Antoine's mother and step-father, Dominique and Toni Salotti

Non-contractible Investment', described their relationship, as he himself had such a great hangover of debt to Antoine. Antoine had a joy and happiness which is hard to find, Professor Bhattacharya said, and was like a younger brother to him.

**Vassilis Hajivassiliou** (LSE) added to the tributes by saying how devoted Antoine had been to his family and friends, telling the audience that shortly before he had gone into surgery he had written a document that was critical to a friend's career.

Next, **Leonardo Felli** (LSE) talked about how he and Antoine had at one point both lived in Islington, often sharing a taxi home from LSE, which meant that they were not only sharing the taxi but also the problem of how to get the taxi driver to understand their accents. Often they were not successful, and so they would pretend that they had arrived at the right place and then attempt to find their way home from where they had been dropped off. Antoine was always interesting to have around, Professor Felli said, as he always had a fresh perspective to offer. He would frequently challenge received knowledge, whether in a conference, a lecture, or even in a taxi, and it was an enormous privilege to have had him as friend and colleague.

**Patrick Bolton** (Columbia University) reflected on what an exceptional human being Antoine had been, with a huge respect for the field of economics and an awareness of his privilege to have been a Laffont student.



## Special Conference in Memory of Professor Antoine Faure-Grimaud



Sönje Reiche speaking at the conference dinner

In **Jean Charles Rochet's** (IDEI) tribute, he described Antoine as a great story teller, saying that he could talk on any topic, and was incapable of being boring.


**David Webb** (FMG, LSE) concluded the event with an overview of Antoine's time at LSE, where he had been a member of Department of Management, the Department of Economics and the Department of Finance, as well as a long-term member of the FMG, and the great contribution he had made to the life

of the school at each stage of his career. Professor Webb told the audience how Jean-Jacques Laffont had initially contacted him to bring Antoine's work to his attention, and how he had been struck by the quality of Antoine's paper. Sharing the sentiment of those who had paid tribute to Antoine before him, Professor Webb recalled how Antoine had been a great entertainer, with a marvellous sense of humour, and a fair person. He finished the final session by outlining several initiatives which would be taking place in memory of Antoine, including a number of prizes for outstanding achievement by Department of Finance MSc students and a PHD Fellowship in his name. Professor Webb then presented a silver plate to Sönje, inscribed with the words:

*To Soenje and Family*

*In memory and appreciation of Antoine from his colleagues and friends at LSE. He is greatly missed and will always be remembered.*


The event finished with a dinner, where **Sönje Reiche** had the chance to thank the event's participants, as well as some of Antoine's particularly close friends and colleagues, who she said had been of great help during his illness.



A Memorial Event to celebrate the contributions of our colleague

### Antoine Faure-Grimaud (1968-2009)

LSE in association with the Department of Finance, Department of Economics, Department of Management and FMG



Antoine was a wonderful colleague, a great teacher and a passionate believer in rigorous research and fostering this in the next generation of researchers. He had an acute intellect and a marvellous sense of humour, he was great fun. We miss him in so many ways. This event is an opportunity for us to share our recollections of what he achieved and the person he was.

The event programme

#### Curriculum Vitae

<b>1992-95</b>	PhD in Economics, University of Toulouse 1	<b>2004-09</b>	Professor in Finance, LSE
<b>1995-2002</b>	Lecturer in Management, LSE	<b>2002-09</b>	Programme Director: Corporate Finance and Governance
<b>2002-04</b>	Reader in Economics, LSE		Financial Markets Group, LSE

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#### Research Publications:

**Corporate Finance**

'The Regulation of Predatory Firms', *Journal of Economics and Management Strategy*, 6(4), Winter 1997, 849 – 876.

'Structure Financière et Concurrence Imparfaite: Modigliani-Miller 40 ans après', *Revue d'Economie Politique*, 108(1), January/February 1998, 16 – 36.

'Optimal Debt Contracts and the Single-Crossing Condition', joint work with Thomas Mariotti, *Economics Letters*, 65(1), October 1999, 85 – 89.

'Bankruptcy Costs, Ex Post Renegotiation and Gambling for Resurrection', joint work with Jean-Paul Décamps, *Finance*, 21(2), December 2000, 71 – 84.

'Optimal Debt Contracts and Product Market Competition: The Limited Liability Effect Revisited', *European Economic Review*, 44(10), December 2000, 1823 – 1840.

'The Debt Hangover: Renegotiation with Noncontractible Investment', joint work with Sudipto Bhattacharya, *Economics Letters*, 70(3), March 2001, 413 – 419.

'Dynamic Adverse Selection and Debt', joint work with Gilles Chemla, *European Economic Review*, 45(9), October 2001, 1773 – 1792.

'Using Stock Price Information to Regulate Firms', *Review of Economic Studies*, 69(1), January 2002, 169 – 190.

'Should I Stay or Should I Go? Excessive Continuation and Dynamic Agency Costs of Debt', joint work with Jean-Paul Décamps, *European Economic Review*, 46(8), October 2002, 1623 – 1644.

'Public Trading and Private Incentives', joint work with Denis Gromb, *Review of Financial Studies*, 17(4), Winter 2004, 985 – 1014.

'Conglomerate Entrenchment under Optimal Financial Contracting', joint work with Roman Inderst, *American Economic Review*, 95(3), June 2005, 850 – 861.

'The Ownership of Ratings', joint work with Elic Peyrache and Lucia Quesada, forthcoming in *Rand Journal of Economics*.

**Contract Theory**

'The Endogenous Transaction Costs of Delegated Auditing', joint work with Jean-Jacques Laffont and David Martimort, *European Economic Review*, 43(3/4), April 1999, 1039 – 1048.

'A Theory of Supervision with Endogenous Transaction Costs', joint work with Jean-Jacques Laffont and David Martimort, *Annals of Economics and Finance*, 1(2), November 2000, 231 – 263.

'On Some Agency Costs of Intermediated Contracting', joint work with David Martimort, *Economics Letters*, 71(1), April 2001, 75 – 81.

'Risk Averse Supervisors and the Efficiency of Collusion', joint work with Jean-Jacques Laffont and David Martimort, *Contributions to Theoretical Economics*, 2002, 2(1), Article 5.

'Collusion, Delegation and Supervision with Soft Information', joint work with Jean-Jacques Laffont and David Martimort, *Review of Economic Studies*, 70(2), April 2003, 253 – 279.

'Regulatory Inertia', joint work with David Martimort, *Rand Journal of Economics*, 34(3), Autumn 2003, 413 – 437.

'Dynamic Yardstick Mechanisms', joint work with Sönje Reiche, *Games and Economic Behaviour*, 54(2), February 2006, 316 – 335.

'Political Stabilization by an Independent Regulator', joint work with David Martimort, in Vivek Ghosal and Johan Stenik (eds.) *The Political Economy of Antitrust*, 2007, Amsterdam: Elsevier Publishers.

'Thinking Ahead: the Decision Problem', joint work with Patrick Bolton, forthcoming *Review of Economic Studies*.

'Satisficing Contracts', joint work with Patrick Bolton, forthcoming *Review of Economic Studies*.

#### Memorial Event Programme

**Friday 20 November 2009, Shaw Library**

2pm **Welcome**

2.15pm **Patrick Bolton**  
Satisficing Contracts

3pm **David Martimort**  
Collusion, Hierarchies and the Institutional Design: Antoine's Legacy and Some Steps Forward

3.45pm **Denis Gromb**  
Finance à la Antoine

4.30pm **Jean Tirole**  
How to jumpstart a market: Thinking about markets in the tradition of Antoine Faure-Grimaud

5.30pm **Presentations and Tributes**

7pm **Dinner**  
(Senior Dining Room, 5th Floor, Old Building)

#### Antoine Faure-Grimaud (1968-2009)



## Launch of AXA-LSE Research Programme on Risk Management and Regulation of Financial Institutions



# The Future of Banking and Financial Regulation

19 October 2009



(left to right): **David Webb** (FMG, LSE), **Charles Goodhart** (FMG, LSE) and **Eric Chaney** (AXA)

The FMG held a public lecture to launch its new research programme on risk management and the regulation of financial institutions, at which Chief Economist for the AXA group, Eric Chaney, Emeritus Professor of Economics at the LSE, Charles Goodhart, and Head of the Department of Finance and Director of the research programme, David Webb, discussed the future of banking and financial regulation following the global financial crisis. The crisis has revealed a distance between our understanding of the interconnected behaviour of banks, the structure of the banking systems, and layers of regulation. This new research programme aims to gain a better understanding of the weakness of the current financial architecture and to assess the scope for greater financial stability through governance and regulation.

The first speaker at the event, **David Webb** (FMG, LSE), explained that the main objectives of the research programme are to examine the reward and governance structures of financial institutions, to research the workings of complex financial networks, to develop risk models that incorporate macro factors, and to examine and suggest regulation, with a focus on forward-looking countercyclical measures. The complexity, interconnectedness and the externalities of the current financial system are issues that need to be better understood, he said, describing a model in which liquidity is endogenously determined by the interplay between investors and hedgers' demand and supply. One feature of this model is that the hedging demand may cause trades to be highly correlated. A problem with this is that, in times of stress, finding a counterparty to satisfy this correlated trade flow may be very difficult as other market participants, such as speculators, would infer prices from trading

flow, current prices and their own private information. If their inferences are negative, liquidity may disappear altogether, forcing abrupt changes in prices. This relates to banking because banks are big hedgers in the market and hence may have very correlated trades. If there is no support for prices in times of high uncertainty, this would lead to liquidity problems for banks and hence instability. Moreover, capital adequacy ratios are pro-cyclical and tend to also create correlated sells, and mark-to-market accounting tends to be counter productive in bad times as it induces correlated stop-loss orders; and these problems are exacerbated by the interconnectedness of the financial system and the use of leverage. Professor Webb also pointed out that the originate-and-distribute banking model was previously thought to disperse risks, however, all the evidence from the current crisis points to the fact that securitisation has concentrated risk in the leveraged sector. He then went on to discuss some general issues for reform, including mechanisms for identifying systemically important institutions, complexity of institutions and the fact that moral hazard and systemic risk are interconnected. He suggested some potential solutions, including measures to moderate fluctuations in leverage (such as counter-cyclical regulation, and capital targets and leverage caps), moderate fluctuations in equity (including forward-looking provisioning), and improve information (through reducing the complexity of instruments and institutions, registering counterparty exposure, and clearing platforms for CDOs and CDSs).

The next speaker, **Charles Goodhart** (FMG, LSE), discussed how it might be possible to mitigate the procyclicality in the banking system. First, he discussed some of the counter-measures currently proposed to address the problems in the banking system, arguing that direct constraints on size and activity limits may have unwanted consequences, and that size constraints may not work anyway, due to the fact that size itself may not be the problem. To support this point, he discussed the 1929 financial crisis when banks in Canada and Britain, which were larger than their US counterparts, did much better than the American banks. Furthermore, he said, large banks that are small relative to the geographical areas in which they operate may not pose a systemic risk. However, having a number of small banks, which hold the same types of securities and share the same funding models, could create a systemic risk because the failure of one bank would make similar banks suspect, as has been the case during the financial crisis.

The other direct constraint that Professor Goodhart discussed was that on activity. He noted the common tendency to assume that some financial

## Launch of AXA-LSE Research Programme



**Eric Chaney** (AXA)

would go to banks that are allowed to hold risky assets, but then in times of crisis the flow of funds would go the other way, and the procyclicality of the flows of funds would make matters worse.

The next issue discussed was remuneration, with Professor Goodhart explaining that the idea behind limiting remuneration is that it supposedly ensures that the incentives of managers are not aligned with those of equity holders. However, it is easy to see that even in cases where the incentives of managers and equity shareholders are aligned, as it is the case when managers have performance-based remuneration packages, high risks are still taken. The problem behind poor decisions therefore could be the lack of understanding about the risks embedded in different financial products.

Professor Goodhart also talked about the position of the current debate on banking regulation. One of the main topics of the debate is whether it is possible to create effective regulation. If it is not possible to do so then intervention may distort prices in the marketplace. In the US, many argue that instead of trying to regulate banks the government should provide incentives for them to insure themselves. One way of implementing this would be to hold debt that transforms into equity under certain conditions, and another would be to have public insurance, with the insurance price set in the market place by allowing private companies to insure small parts of the risk. The discussion in the EU and some parts in the US has gravitated towards the creation of counter-cyclical regulation such as counter-cyclical capital adequacy requirements. The main issues in this debate are to do with how counter-cyclical measures are implemented, and how sanctions are to be determined. However, the general discussion of what to do is being complicated by battles over responsibilities of home/host regulators and their national mandates.

institutions function as a combination of a casino and a utility, with a common belief being that a solution to this problem would be to split these two functions apart. However, this policy is misguided, Professor Goodhart argued, as it would mean that utility-only banks could not hold risky assets, and as a result they would offer savers less attractive yields. In good times, savers

Professor Goodhart also said that he believed it to be inevitable that we are headed towards a world with tighter requirements. This will cause a rise in the cost of banking due to costs associated with higher liquidity and capital adequacy ratios, and spreads between deposits and lend rates will adjust so as to reach an acceptable return on equity for banks. The solution may be to re-establish securitisation in a simpler, more transparent way, he said.

The last speaker of the event was **Eric Chaney** (AXA), who began by stressing the importance of understanding the causes that led to the freezing of the financial system in the aftermath of the collapse of Lehman, as this episode had a massive impact on the real economy, leading to a 20 per cent contraction in global trade. Dr Chaney argued that, following Lehman's collapse, doubts were cast on the whole banking system, and accordingly companies that had doubts about their own banks began to hoard cash, liquidate inventories, and cut investments and production. These states of affairs, when combined with a full blown credit crunch in trade finance, explains the incredible fall in global trade after Lehman's collapse. Dr Chaney estimated that it will not be until after 2013 that global trade levels will return to the levels seen before the collapse of the company.

Next, Dr Chaney spoke about regulation, saying that current levels of capital requirements seem to be set *ad hoc*. He also outlined some reasons why the new AXA-funded FMG research programme should investigate the competition between national regulators. Their incentives and national mandates may lead to coordination failures, he said, and so there is a question of how to best align incentives. Another challenge concerns the scope of the regulation, with many countries seeming to agree that micro-regulation is insufficient. However, macro-regulation poses different challenges, he said. For instance, pre-crisis global trade levels were not sustainable, and this led to an increase in asset prices that was not reflected in inflation. Central banks were very slow to recognise this rise in asset prices, the problem being that there is no cooperation when setting monetary policies. Local mandates could be the cause of the coordination problem amongst central banks, he said, with one possible solution to this problem being to ask the Bank of International Settlements to force central banks to talk about global inflation from time to time. He concluded his presentation by stressing that a more global macro-prudential regulation framework should be adopted.

# London Financial Regulation Conference

2-3 July 2009



(left to right): **Viral Acharya** (New York University), **Dave Backus** (New York University) and **Ben Katz** (Barclays)

Two major academic reports on the financial crisis have been the 2009 Geneva Report, 'The Fundamental Principles of Financial Regulation', and the Stern School of Business at the New York University book, 'Restoring Financial Stability: How to Repair a Failed System'. This conference included the key authors of both monographs, and several other leading experts, who led discussions on continuing key issues, which included liquidity, quantitative easing, and remuneration.

## The Macro-Economy and Quantitative Easing

**Tim Besley** (LSE) discussed the extent to which longer term rates have become divorced from the bank rate, and thus how far the bank rate can be used as an instrument in policy. He went on to discuss how financial frictions have a key impact on the monetary policy transmission mechanism, and will therefore affect quantitative easing. He stressed the need for an economic model to think through these issues, and he also highlighted the need for models to pay attention to quantities as well as prices. Professor Besley pointed out that we entered the downturn with inflation expectations in line with the target, with the result being that there is less inflationary risk at the time of writing. However, he said that the Taylor rule should be time-varying in order to accommodate financial frictions, and that the Monetary Policy Committee will eventually need to tighten interest rates and engage in quantitative tightening.

The next speaker was **Charles Goodhart** (FMG, LSE), who started his talk by pointing out that a zero interest rate is not the limit of monetary policy, since the balance sheet of the central bank can be expanded; this is what is generally known as quantitative easing. Professor Goodhart then went on to describe the various forms of quantitative easing used by different central banks. The Bank of Japan's use of quantitative easing in the past had aimed

at raising commercial bank reserves, while the US Federal Reserve's current aim is to ease credit conditions and intervene in certain markets that are clogged up. He also pointed out that we have seen a spike in reserves held by commercial banks, and he queried whether central banks should deter this. Professor Goodhart went on to discuss the potential impact of quantitative easing on the independence of central banks. Such an increase in central bank balance sheets brings the central bank into the fiscal sphere; in the US this could affect the relationship between the Federal Reserve and Congress, and may therefore impact the independence of the former. With this issue in mind, he made the point that the European Central Bank would find quantitative easing difficult because it would be unclear from whom they would need to get agreement regarding the fiscal implications.

**Martin Wolf** (Financial Times) ended this session of the conference by discussing the exit strategy from quantitative easing. He argued the authorities will be operating in a period of great uncertainty, and that there will be long time lags between policy changes and their effect on the economy, likening the process to pulling a brick with an elastic band. He expressed the fear that the pressure on the central bank will be to tighten too late. Mr Wolf then went on to point out that the bond market may stop operating normally, given fears over the government deficit and the banking crisis. In this event the government would have to finance the deficit by borrowing from the central bank, thus ending the independence of the latter. He concluded his talk by raising the question of whether the inflation target was too low in the lead up to the crisis, as a higher target would have left more room for manoeuvre.

## General Introduction to Work on the Financial Crisis

During the next session, **Viral Acharya** (New York University) and Professor Goodhart gave a general introduction to work on the financial crisis. Professor Acharya presented the main analyses and ideas developed in the book, 'Restoring Financial Stability: How to Repair a Failed System', based on the work of Stern School of Business, New York University members. Professor Goodhart then regaled the main recommendations of the Geneva Report, to which he had contributed, with Markus Brunnermeier, Andrew Crockett, Avinash Persaud and Hyun Song Shin.

For Professor Acharya and the New York University economists, the origins of the crisis lay in the combination of a credit boom and a housing bubble. However, Professor Acharya stressed the fact that the freezing of financial markets and the near collapse of the financial system were ultimately due to a flaw in the securitisation business of the large financial institutions, including universal and investment banks, insurance companies, and some large hedge funds. Financial institutions did not transfer risks to other



## London Financial Regulation Conference



**Philipp Schnabl** (New York University)

creditors and instead set up a shadow banking sector for regulatory arbitrage purposes by creating SIVs and conduits funded by asset-backed commercial paper, which were guaranteed by banks themselves. Exploiting a flaw in Basel II, financial institutions were thus able to expand their balance sheets without having to increase their regulatory capital.

However, in doing so, they

were effectively writing out-of-the-money puts on aggregate crises. The extant regulatory system, focused on individual banks, also proved unfit to mitigate systemic risk.

Professor Acharya then outlined four regulatory principles based on this diagnosis. The first of which would be to curb the risk-taking incentives induced by compensation schemes based on cash bonuses, which led traders to favour risky short-term strategies over long-term profitability. Professor Acharya expressed a preference for bonus-malus reserve accounts, which would penalise short-termism. The second principle is to prevent obvious regulatory arbitrage, such as those induced by Basel II. The implicit guarantees on government-sponsored agencies or too-big-to-fail institutions also distorted the risk-taking incentives of financial institutions and should be addressed in order to avoid a mispricing of aggregate risk. Professor Acharya's recommendation is to charge for guarantees using marking-to-market that reflects leverage in order to get a consistent price for aggregate risk. The third principle is to address not only the individual risks but also the systemic risk. To do so, Professor Acharya cited three proposals: first, to create a specific regulator for systemic institutions, or at least augment the central bank's agenda; second, to design prompt corrective action-style resolution; and third, to develop measures of systemic risk and of financial institutions' contributions to systemic risk in order to charge them, for instance, through capital requirements. Professor Acharya also said he was in favour of a public-private systemic insurance, consisting of compulsory insurance of each bank's own losses during a general crisis, with payments feeding an insurance fund used in case of a severe crisis. This system would provide a price for systemic risk (through the insurance premium) and limit both the incentives to take risks and the costs of bailouts for the public, thanks to the insurance fund. Finally, the fourth principle is to increase transparency, in particular in the shadow banking system and the over-the-counter derivatives market, by creating clearing houses and standardised products in order to minimise counterparty risk.

Professor Goodhart continued the session with a presentation of the conclusions of the Geneva Report. First, he briefly presented the framework

of the analysis, and then he discussed which proposals remain in dispute. One of the goals of the Geneva Report was to develop a more integrated macro-financial perspective on the crisis, developing the following points. The micro-prudential approach of regulation should be completed by a macro-prudential perspective, because ensuring that individual banks are safe does not necessarily lead to systemic stability. In the financial industry, more than in other sectors, negative externalities of one institution to others must be recognised and addressed by regulation. The report also details the self-amplifying mechanisms that turned relatively limited losses in the subprime corner of the US housing market into a global systemic financial crisis, and documents the importance of leverage and de-leverage over the business cycle in relation to capital adequacy ratios, stressing the desirability of counter-cyclical instruments. It advocates the need to regulate financial intermediaries that play a systemic role, as well as the banks. The authors of the Geneva Report also recommend a twin-pillar approach, granting the structural macro-prudential regulation to the central bank and the micro-prudential regulation to the financial services authorities.

A number of issues are still being debated, Professor Goodhart said, the first of which is the application of counter-cyclical capital adequacy ratios. He noted that there were competing propositions, such as the systemic insurance scheme proposed by Professor Acharya and the New York University economists, or the insurance scheme advocated by Professor Raghuram Rajan. Of these, a maximum leverage ratio may be easier to implement, he said, and could also be increased by discretion. The second debate is about the definition of systemic risk. Professor Goodhart stated his belief that a correct measure of systemic risk should be both time and state varying, although he owned that the possibility of providing a rigorous definition remains a daunting challenging for empirical economists. Another important issue is the geographical structure of regulation, because of the disparity between financial institutions, which have become global, and regulatory systems, which are determined nationally. Professor Goodhart argued, in line with the Geneva Report, that regulation should be applied at the national level, but recommended a switch from the principle of 'home' to 'host' country. He also proposed to shift the resolution of the crisis to the supra-national level, in particular for the Euro zone countries. However, he noted, international institutions are generally either entirely or partly opposed to such reforms.

### How to Revitalise the Financial System

This session was opened by **Ben Katz** (Barclays Capital), who argued that the recent large issuance and volume of outstanding Hybrid Tier 1 securities highlight their importance to the global banking sector. Banks, regulators and investors therefore need to agree on terms for this market to fully reopen. He argued that outstanding Tier 1 securities cannot be replaced with equity alone. Recent examples have shown that hybrid securities have succeeded in their role as preferential loss absorbing capital, and that despite negative valuation news, the secondary trading market for Hybrid Tier 1s is





**Andy Haldane** (Bank of England)

stabilising. Regarding these measures he pointed out that there should be greater transparency and disclosure made to investors about the capital securities they are investing in, adjustments of ratings of capital securities to incorporate the increased risk of coupon deferral, and an extension of principal payment in order to attract new investors and instruments as a write-down of triggers,

conversion to ordinary equity in stress situations and appropriate ranking in liquidation in order to improve loss absorption.

The second speaker, **Philipp Schnabl** (New York University), divided the financial crisis into two stages. In the first stage there was the liquidity crisis caused by the modern version of bank runs, with the central bank operating as the lender of last resort. In the second stage, there was the solvency crisis, triggered by the lack of capital in the financial sector and the lack of pricing for toxic assets. These two problems of the solvency crisis are linked but should be distinguished, and therefore require different interventions. He argued that an efficient bailout implemented by buying equity, guaranteeing new debt, purchasing toxic assets and the development of a new bankruptcy code is needed to solve recapitalisation, and as far as resolving the pricing for toxic assets is concerned, price discovery has to be subsidised.

The third speaker was **Dave Backus** (New York University), who pointed out that the crisis would change the markets. In the Depression of the 1930s it was argued that regulation would kill innovation, and this turned out to be the case. In his opinion, Professor Backus said, open and honest markets are needed, therefore necessitating a balance of regulation, through a combination of government spending and financial restructuring.

Finally, **Andy Haldane** (Bank of England), explained that two lessons can be drawn from the financial crisis; namely that the level of capital is too low, and the distribution of capital, too uniform. Thus the capital framework needs to better reflect balance sheet characteristics such as risk, size, connectivity and complexity, and there are three ways to approach this problem. The first one is judgement. The second is to use estimated CoVaRs in order to redistribute capital across the system. This approach is quite simple to execute and it delivers a better distribution of capital, however it does not address the level of capital, and nor does it have a structural or balance sheet basis. The third option is the system-wide Merton, which uses banks' balance sheet structures, as well as calibrated asset variances, CoVaR and exposures linkages.

## Securitisation

This session was chaired by Professor Goodhart and had the participation of Dr Schnabl and **Marke Raines** (Taylor Wessing LLP). Dr Schnabl presented his paper, 'Securitization without Risk Transfer', in which he enumerates some of the most popular explanations for the financial crisis, which include the complex design of mortgages, the originate-to-distribute model of securitisation, and the rating agencies' rubber stamping of 'AAA' products. He argued that these are not sufficient explanations, and to address the issue of the explanation gap he characterised and compared the 'old' and the 'new' model of banks. In the old model, the main role of banks was to accept deposits and to act on behalf of depositors monitoring loans, with equity holders rather than depositors bearing the cost of any equity losses. The role of the regulator in this model was to ensure that this was the case. In the new model, securitisation appears as a powerful mechanism that banks can use to avoid costly capital, and efficiently transfer risk to investors.

Next, Dr Schnabl briefly characterised the evolution of asset-backed commercial paper conduits, and showed the relative importance of these products for the three largest sponsors before the crisis: Citibank, ABN Amro and Bank of America. He also pointed out the main implications of different accounting approaches for these products, namely the fact that these assets may or may not be reflected on banks' balance sheets, which has crucial implications for financial ratio analysis. In the context of the subprime crisis of summer 2007, he showed the positive correlation between banks' exposure to conduits and a drop in stock prices, and the three main consequences for the banks that held these types of products: the small banks went under and some had to be bailed out, some other banks had to take these assets back on their balance sheets, whilst others still extended their guarantees. In this context, he suggested an alternative model for asset-backed securities, which would enable an increase in the level of assets on the balance sheets of banks, but without necessarily increasing the level of risk. Finally, he discussed three lessons to be taken from the financial crisis: the need for more regulation and disclosure of these products, the need for using more than a single ratio to evaluate capital requirements and the financial health of banks, and the need to focus more sharply on systemic risk.

Next, Mr Raines discussed the history of the concept of securitisation, of which the earliest record in the UK dates from 1769, despite the fact the first formal security deal did not take place until 1970 in the US and 1985 in the UK. He also expressed his belief that the causes of the crisis emanated from Basel II, fraud, bank mistakes and fair value accounting, finally pointing out that the decrease in financial institutions' values were not consistent with the real losses they had suffered.

Conference organised by: **Charles Goodhart** (FMG, LSE) and **Viral Acharya** (New York University, London Business School, CEPR and NBER)

# Too Big to Fail, Too Interconnected to Fail?

15 September 2009



(left to right): **Malcolm Knight** (LSE and Deutsche Bank), **Howard Davies** (LSE), **Gillian Tett** (Financial Times), **Charles Goodhart** (FMG, LSE) and **Patrick Raaflaub** (FINMA)

The FMG hosted a successful one-day conference entitled, 'Too Big to Fail, Too Interconnected to Fail?' in September. The purpose of the conference was to identify the specific characteristics of financial institutions that pose potential risks to the financial system as a whole, and to review the ways in which these elements of systemic risk have been addressed in the past. There was also some reflection on the consequences of this analysis for the prudential regulatory principles and supervisory measures, as well as for the design and functioning of deposit insurance schemes, clearing and settlement systems, and other elements of the system that impact on financial stability.



**Philipp Harle** (McKinsey & Co) discussed the role of clearing and settlement infrastructure in today's complex, interconnected financial industry, in the context of limiting

**Avinash Persaud** (Intelligence Capital)

interdependence and contagion. He argued that any discussion about the future of financial architecture should be based on a few fundamental assumptions. Firstly, banks should assume risks and leverage with less insolvency risk, although he owned that removing insolvency risks completely would seriously hamper economic growth. Secondly, banks should be primarily privately owned and compete with one another. Competition is important for innovation and for keeping the cost of financial products low, and banks should be allowed to operate internationally to cater to the globalised economy. Now that the immediate threat of meltdown has passed, the effectiveness and impact of suggested measures must be assessed in detail. Some of the dimensions to take into consideration include difficulty of implementation, enforceability and national costs versus international benefits. He went on to discuss how central clearing and settlement (CCP) infrastructure plays a critical role in reducing systemic risk. He suggested that market participants should make maximum use of these central clearing and settlement systems. Where central systems cannot be used, they should increase the share of collateralised transactions through third party agents. While concentration of flows in one CCP has cross-margining and netting efficiency advantages, several CCPs reduce the systemic risk concentration in CCPs, and foster innovation and efficiency through competition. Given that the increasing



**Patrick Pearson** (European Commission)

use of central systems increases systemic risk relevance, their setup and operations should be strictly regulated and supervised. Central systems can be operated by private owners, but authorities should have the right to seize management control immediately when necessary, he argued.

**Michele Faissola** (Deutsche Bank) then discussed the issue of central counterparties, outlining the several phases of the current crisis. The first phase was first-order meltdown, which mainly affected mortgages, the second phase was systemic risk, the third phase

was the impact on the real economy, and the fourth phase was normalisation. He also touched upon the general agreements around the causes leading to the crises, and then discussed the current state of OTC derivative regulation in detail, which he observed is in a state of flux, although he noted that regional positions are starting to crystallise. He compared the US and European positions on various issues, such as the standardisation of OTC derivatives, central counterparties, electronic trading and exchanges, price transparency, applicability, data repositories and trade reporting; commenting that infrastructure changes will be important in reducing both actual and perceived systemic risk. In conclusion, he said that we all share the common goal of financial stability, and so it is important that we make significant progress on market infrastructure. There is a need for further dialogue between legislators, regulators and users, as the unintended consequences of poorly defined legislation will be significant. However, we must also be wary of the unprecedented level of change that is contemplated by some, as this too may be dangerous.

The title of the presentation by **Thomas Huertas** (FSA) was, 'Too Big to Fail, Too Complex to Contemplate: What to do About Systemically Important Firms'. Dr Huertas observed that



**Hugo Banziger** (Deutsche Bank)

the financial crisis challenges the very basis of our economic and financial system, and that the acid test for a cure to what ails the financial system is whether it will work with respect to financial

institutions that are considered 'too big to fail'. These are the large, complex, cross-border financial institutions that are the principal players in financial markets, the principal users of payment, clearing and settlement systems, and a major source of credit to consumers and corporations around the world. He suggested that we should take steps to improve macroeconomic policy, resolution, deposit guarantees, regulation and supervision, and to encourage them to work in harmony with one another. We also need a mechanism to handle these large, complex, cross border financial institutions, he argued, so that they can die by the market without killing the market. Stricter capital, stricter liquidity, contagion control and living wills are important steps in that direction. These steps formalise the lessons that regulators and supervisors have been drawing from the crisis – that capital must be able to absorb losses whilst the bank remains a going concern, and that banks must prepare in advance for economic and financial stress that may occur.

Conference organised by: **Charles Goodhart** (FMG, LSE), **Malcolm Knight** (LSE and Deutsche Bank) and **David Webb** (FMG, LSE)



# Job Market Candidates



### Cláudia Custódio

Cláudia Custódio is a PhD student in the Department of Management at LSE, and has been a member of the FMG since June 2007. She graduated from IBS (ISCTE Business

School) in Lisbon, where she also taught financial accounting and corporate finance. At the FMG she has contributed to the Corporate Finance and Governance research programme, and the RICAPE2 project.

Her main research interests include corporate finance and corporate governance, and she is currently working on corporate diversification and CEO characteristics. Her other research interests include cash holdings and capital structure.

In her job market paper she shows that M&A accounting can explain the diversification discount as measured with Tobin's  $q$ . The typical M&A accounting procedure inflates the book value of assets and creates a mechanical drop in the common measure of acquirers'  $q$ . Because diversified firms are more acquisitive than standalones, their  $q$  is likely to be lower, generating a spurious diversification discount. After adjusting  $q$  for goodwill, by excluding it from the book value of assets, she finds no significant diversification discount in most of her specifications. As an alternative to the goodwill correction, she makes use of a change in the M&A accounting rules in 2001 as a natural experiment to test this hypothesis.



### Aytek Malkhozov

Aytek Malkhozov is a PhD student in the Department of Finance, and has been a member of the FMG since 2005 when he joined as a Deutsche Bank fellow. He completed his undergraduate studies in

Financial Economics in France, and then gained an MSc degree in Finance and Economics at LSE.

His research focuses on asset pricing theory, macro-finance and derivatives.

His job market paper, co-authored with former FMG member Maral Shamloo, examines how

changes in macroeconomic expectations and macroeconomic uncertainty affect asset prices in general equilibrium. More specifically, he examines the implications of introducing anticipated productivity shocks for the ability of a real-business-cycle model to explain asset prices. Incorporating anticipated shocks, or news, creates a persistent predictable component in consumption growth, often referred to as long-run risk in the finance literature. Thus, in conjunction with Epstein and Zin (1989) preferences and under plausible parameter calibrations, news shocks help explain key observed asset pricing facts. Furthermore, news shocks improve the prediction for the co-movement of macroeconomic and financial variables, and explain the asset returns' lead over the business cycle.



### Kalin Nikolov

Kalin Nikolov is a Department of Economics PhD candidate and has worked at the Bank of England since 1999, during which time he has worked on building the Bank's new forecasting model and the

Quantitative Easing programme.

His main research interests lie in the macroeconomic implications of credit market imperfections, however he has also worked on monetary economics and optimal monetary policy.

His job market paper examines whether a benevolent government can improve on the free market allocation by setting capital requirements for private borrowers in a stochastic model with collateral constraints. Previous theoretical studies have found that when asset prices enter into borrowing constraints, pecuniary externalities between atomistic agents can make the *laissez faire* equilibrium constraint inefficient. For reasonable parameter values he finds that, quantitatively, the answer is 'no' – private and government leverage choices coincide. Limiting private leverage by imposing capital requirements has the beneficial effect of dampening the effects of the 'collateral amplification mechanism'. This reduces 'fire sales' in recessions and limits the negative externality that individual

asset sales have on other credit constrained borrowers. However, capital requirements are a blunt tool; they tax the activities of highly productive entrepreneurs and reduce the amount they produce in equilibrium. This reduces total factor productivity and steady state consumption. In the end, society faces a choice between high but unstable consumption in the free borrowing world, and low but stable consumption in the regulated world.



### Andrea Vedolin

(visiting student)

Andrea Vedolin is a PhD student at the University of Lugano, who is visiting the FMG. Before starting her PhD she received an MA in Economics from the University of Zurich.

Her research interests include theoretical and empirical asset pricing, derivatives pricing, portfolio choice and financial econometrics. Her current research agenda focuses on understanding the impact of uncertainty on bond, credit and equity markets in equilibrium models. She expects to receive her PhD in Spring 2010.

Her job market paper studies volatility risk premia in the cross-section of individual stocks. She develops an economy with multiple assets where each firm is subject to default. The profitability of each firm is unknown. Since expected cash flow growth is unobservable, agents estimate it from a common set of observable variables, and agree to disagree. In order to estimate a firm's expected growth rate of cash flows, they observe a firm-specific signal and a systematic signal. The systematic signal is linked to the aggregate state of the economy. In the economy, two rational manifestations of uncertainty are: (i) agents' disagreement about the future profitability of firms and a business-cycle indicator, and, (ii) time-varying volatility of fundamental growth rates which are allowed to have a bearing on risk premia in equilibrium. Calibrating the model, the results show that the interplay between leverage and the two sources of uncertainty add a crucial component to the understanding of both the time-series and cross-section of individual volatility risk premia.

# Discussion Papers



DP 632 (PWC4)

## Rents, Learning and Risk in the Financial Sector and Other Innovative Industries

Bruno Biais, Jean-Charles Rochet,  
Paul Woolley

We study innovative industries subject to two risks. First, it is uncertain whether the innovation is strong or fragile. Second, it is difficult to monitor managers, which creates moral hazard and agency rents. As time goes by and profits are observed, beliefs about the industry are updated. As long as no default occurs, confidence builds up. Initially this spurs growth. But increasingly confident managers end up requesting large rents, curbing the growth of the industry. If rents become too high, investors give up on incentives, and failure rates rise. If the innovation is fragile, eventually there is a crisis. Our model captures stylized facts of the recent financial innovation wave and generates new implications for risks, returns and rents.

DP 633

## Ambiguity, Information Acquisition and Price Swings in Asset Markets

Antonio Mele, Francesco Sangiorgi

This paper studies asset markets in which ambiguity averse investors face Knightian uncertainty about expected payoffs. The same investors, however, might wish to resolve their

uncertainty, although not risk, by just purchasing information. In these markets, uninformed and, hence, ambiguity averse, agents may coexist with informed agents, as a result of a rational information acquisition process. Moreover, there are complementarities in information acquisition, multiplicity of equilibria, history-dependent prices, and large price swings occurring after small changes in the uncertainty surrounding the asset expected payoffs. Our model suggests the importance of uncertainty, as a new channel for episodes of extreme price volatility, media frenzies and media glooms.

DP 634

## Endogenous Technological Progress and the Cross Section of Stock Returns

Xiaoji Lin

I study the cross sectional variation of stock returns and technological progress using a dynamic equilibrium model with production. In the model, technological progress is endogenously driven by R&D investment and is composed of two parts. One part is product innovation devoted to creating new products; the other part is dedicated to increasing the productivity of physical investment and is embodied in new tangible capital (eg, structures and equipment). The model breaks the symmetry assumed in standard models between in- tangible capital and tangible capital, in which the accumulation processes of tangible capital stock and intangible capital stock do not affect each other. The model explains qualitatively

and in many cases quantitatively well-documented empirical regularities: (i) the positive relation between R&D investment and the average stock returns; (ii) the negative relation between physical investment and the average stock returns; and (iii) the positive relation between book-to-market ratio and the average stock returns.

DP 635

## Lessons from the Global Financial Crisis for Regulators and Supervisors

Willem Buiter

This lecture is a tour d'horizon of the financial crisis aimed at extracting lessons for future financial regulation. It combines normative recommendations based on conventional welfare economics with positive assessments of the kind of measures likely to be adopted based on political economy considerations.

DP 636

## Negative Nominal Interest Rates: Three Ways to Overcome the Zero Lower Bound

Willem Buiter

The paper considers three methods for eliminating the zero lower bound on nominal interest rates and thus for restoring symmetry



to the domain over which the central bank can vary its policy rate. They are: (1) abolishing currency (which would also be a useful crime-fighting measure); (2) paying negative interest on currency by taxing currency; and (3) decoupling the numéraire from the currency/medium of exchange/means of payment and introducing an exchange rate between the numéraire and the currency which can be set to achieve a forward discount (expected depreciation) of the currency vis-a-vis the numéraire when the nominal interest rate in terms of the numéraire is set at a negative level for monetary policy purposes.

DP 637

### Endogenous Liquidity and Contagion

Rohit Rahi, Jean-Pierre Zigrand

Market liquidity is typically characterized by a number of ad hoc metrics, such as depth, volume, bid-ask spreads etc. No general coherent definition seems to exist, and few attempts have been made to justify the existing metrics on welfare grounds. In this paper we propose a welfare-based definition of liquidity and characterize its relationship to the usual proxies. Our analysis rests on a general equilibrium model with multiple assets and restricted investor participation. Strategic intermediaries pursue profit opportunities by providing intermediation services (ie, 'liquidity') in exchange for an endogenous fee. Our model is well-suited to study the contagion-like effects of liquidity shocks.

#### Correction

In the July 2009 issue of the Quarterly Review DP 624, entitled 'Best Ideas', was incorrectly listed as being authored by Suddipto Bhattacharya and Sergei Guriev, when in fact it was authored by Randy Cohen, Christopher Polk and Bernhard Silli. The editors apologise for this mistake.

# Special Papers

SP 184

### A Pragmatic Approach to the Phased Consolidation of Financial Regulation in the United States

Howell Jackson

The financial crises of the past year have put the issue of financial regulatory structure on the front burner of public policy for the first time in many years, making possible reforms on a scale not imaginable since the Great Depression. Dramatic increases in market volatility, unprecedented interventions by the Federal Reserve Board to sustain securities firms, palpable failures to protect consumers in mortgage lending markets, and lingering concerns over the competitiveness of the American financial services industry have all combined to put regulatory reorganization on

the national agenda. While the United States employs more financial regulators and expends a higher percentage of its gross domestic product on financial oversight than any other major country, events of the past few years suggest that the country has not obtained a higher quality of supervision than other jurisdictions. Indeed, to the extent the current credit turmoil had its origins in the United States, one could quite plausibly claim that our regulatory structure has done a good deal worse than other more streamlined systems in protecting consumers and ensuring market stability. As the rest of the world has moved towards more consolidated forms of regulatory oversight, a natural question posed by recent events is whether the United States should also undertake such a regulatory reorganization and, if so, how such a reorganization should be accomplished.

## Forthcoming Discussion and Special Papers

Discussion Papers

DP 638

### Organizational Diseconomies in the Mutual Fund Industry

Fabian Garavito

DP 639 (PWC 5)

### Liquidity and Asset Prices: a Unified Framework

Dimitri Vayanos and Jiang Wang





DP 640

**Regime Switching in Volatilities  
and Correlation between Stock and  
Bond Markets**

Runquan Chen

**Special Papers**

SP 185

**The Value of Interest Rate Forecasts?**

Charles Goodhart and Wen Bin Lim

# Visitors to the FMG

## July-October 2009

**Ron Bird** (University of Technology, Sydney)

**Marvin Goodfriend** (Carnegie Mellon and NBER)

**Jens Hilscher** (Brandeis University)

**Cristian Huse** (Stockholm School of Economics)

**Otmar Issing** (University of Wuerzburg)

**Jiro Kondo** (Northwestern University)

**Peter Kondor** (Central European University)

**Samuel Lee** (New York University)

**David Marsh** (London and Oxford Capital Markets)

**Ian Martin** (Stanford University)

**Antoinette Schoar** (Massachusetts Institute of Technology)

**Raman Uppal** (London Business School)

**Andrea Vedolin** (University of Lugano)

**Svitlana Zhylenko** (Charles University)





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The screenshot shows the FMG website with a blue header and a background image of a modern building interior. The main content area is divided into two columns. The left column is titled 'Events this week @ FMG' and lists two events for Wednesday, 15th October 2008. The right column is titled 'In the news' and lists two news items. At the bottom, there is a navigation menu with links to home, about, events, news, publications, research, people, be involved, mailing list, contact, and Corporate Partnership Programmes. There is also a search bar and logos for LSE and RLAB.

**FMG**  
Financial Markets Group

The Financial Markets Group Research Centre at LSE is one of the leading centres in Europe for academic research into financial markets. [more about FMG](#)

### Events this week @ FMG

**Wednesday, 15th October 2008 - at 1.00-2.00pm**

**Lunchtime Workshop** | The Effect of Credit Rationing on the Shape of the Competition-Innovation Relationship | Jan Bena (FMG/LSE)  
location: R407, FMG, 4th Floor, Lionel Robbins Building, LSE

**Wednesday, 15th October 2008 - at 5.00pm**

**Capital Markets Workshop** | Smooth Ambiguity Aversion Toward Small Risks and Continuous-Time Recursive Utility | Costis Skiadas

### In the news

Special London Financial Regulation Seminar announced - Howell Jackson (Harvard Law School) **13 Oct 2008**

Professor Howell Jackson (Harvard Law School) will give a special lunch seminar as part of the London Financial Regulation Seminar.

Managing International Financial Instability Public Lecture - **9 Oct 2008**

Conference slides available

Date: Tuesday 7 October 2008 Time: 6-7.30pm Venue: Sheikh Zayed Theatre, New Academic Building Speaker

**In the press: Jon Danielsson provides an analysis on "What happened to Iceland"** - Jon Danielsson (FMG/LSE) investigates the factors that caused the Icelandic financial crisis.

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## FMG Review

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