House of Finance

SAFE

Sustainable Architecture for Finance in Europe

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About SAFE

The Research Center SAFE – "Sustainable Architecture for Finance in Europe" – is a cooperation of the Center for Financial Studies and Goethe University Frankfurt. It is funded by the LOEWE initiative of the State of Hessen (Landes-Offensive zur Entwicklung wissenschaftlich-ökonomischer Exzellenz). SAFE brings together more than 40 professors and just as many junior researchers who are all dedicated to conducting research in support of a sustainable financial architecture. The Center has two main pillars: excellent research on all important topics related to finance; and policy advice, including the dissemination of relevant research findings to European decision makers from the realms of politics, regulation and administration.

In order to promote a fruitful exchange with interested parties from politics, academia, business and the media, SAFE issues a newsletter on a quarterly basis. This aims to provide an overview of the Center's ongoing research and policy activities. The SAFE Newsletter succeeds the House of Finance Newsletter, which was published between 2009 and 2012.

SAFE is based at Goethe University's House of Finance, however extends beyond by drawing on scholars from other parts of Goethe University as well as from fellow research institutions. The Center builds on the reputation of the House of Finance institutions, serving as an interdisciplinary think tank on the issue of finance.

Content

Editorial

Wolfgang König
SAFE Executive Board

How much do we know about the implications of economic, political, and regulatory events on the real economy in Europe? And what lessons can we learn from the past? For answers, we need historical cross-country research based on comprehensive European data. Currently, the available data from before 1990 on this topic are fragmented and incomplete. Only a few largely stand-alone databases have been built by both the academic community and private companies, without concern for interoperability.

In the U.S., institutions such as WRDS (Wharton Research Data Services) or CRSP (Center for Research in Security Prices) have been investing huge resources to build and link databases suited for research over the long run. This is one of the reasons why empirical financial research in a long-term perspective is focusing today almost exclusively on US data.

The project EURHISFIRM – European Historic Finance and related Firm Data – is attempting to change that. Its long-term goal is to digitalize first stock exchange and balance sheet data, and subsequently firm-level data (e.g. legal structure, management, governance and geographical data) for Europe from 1815 onwards and to make these data available for research purposes in a machine-readable format. Besides high-quality comprehensive datasets, a central aspect and challenge in building this infrastructure is the harmonization of different data sources and formats across European countries. This infrastructure shall allow, for the first time, to conduct historical cross-country research based on comprehensive European data.

The first phase of this project is funded by the Horizon 2020 program of the European Union with about 3.4 million euros over an initial time period of three years. The objective in this phase is to produce a design study that serves as a basis for the setup of a comprehensive historical database for European finance and related firm data. The project consortium consists of eleven partners from seven European countries, and is led by Angelo Riva from Paris School of Economics. The main German contributor is Goethe University – Uwe Walz, Helmut Siekmann, Alexander Peukert, and me as a member of the whole project's executive committee – together with the SAFE Data Center (Stephanie Collet) and HeBIS (Uwe Risch).

In April, the starting signal was given for this ambitious project. At Goethe University and SAFE we are very excited to engage in this innovative endeavor in the next three years, striving for better answers to future questions derived from lessons from the past.

Yours sincerely,
Wolfgang König

Once Bitten, Twice Shy: The Power of Personal Experiences in Risk Taking

Steffen Andersen
Copenhagen Business School and CEPR

Tobin Hanspal
Goethe University & SAFE

Kasper Meisner Nielsen
Hong Kong University of Science and Technology

After the financial crisis, it seems appropriate to ask whether negative experiences will result in lower future risk taking. Do individuals have to undergo heavy losses themselves, or are common shocks a sufficient trigger to make them reduce their exposure to risky assets? Studies suggest that personal experiences make individuals refrain from opportunities to take risk. In this paper, we analyze whether these experiences are so powerful that they make individuals also change their attitudes toward risky assets. Based on data of individuals who inherit a portfolio of risky assets, we find that personal experiences indeed make individuals shy away from risk: They sell inheritances of risky assets, even when they receive large windfalls.

Heterogeneity in risk taking between individuals has been attributed to past experiences of macroeconomic shocks (e.g. Malmendier and Nagel, 2011), incidents of corporate fraud (Giannetti and Wang, 2016), and personal experiences in the stock market (e.g. Kaustia and Knüpfer, 2008). These studies suggest that personal experiences make individuals refrain from opportunities to take risk. In our study, we analyze whether personal experiences make people also change their attitudes toward risky assets.

We use an identification strategy that relies on a sample of individuals who inherit a portfolio of risky assets. The main advantage is that inheritances from estates that hold risky assets alter the active decision from one of choosing to take risk to one of choosing not to take risk. By analyzing active changes in risk taking in this setting, we can derive the consequences of personal experiences on risk preferences. To understand the effect of personal experiences, we analyze both the indirect effect on individual risk taking that comes from personal experiences of close family members and individuals living in the same local environment, and the direct effect that comes from experiences made by the individual him- or herself. This approach allows us to generate variation in the degree of personal experiences.

Bank stocks: a plausible negative experience

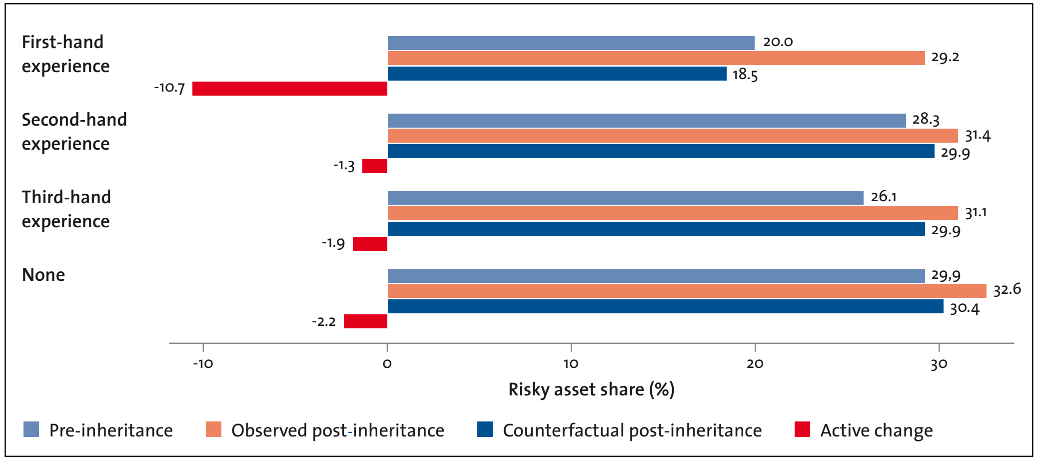
In our study we use high-quality administrative register data from Denmark to classify individuals' personal experiences and observe their allocation of liquid wealth into risky assets around inheritances. As a plausible source of negative experiences we identify individuals who invested in retail bank stocks – some of which defaulted after the crisis. These investments were often encouraged by direct marketing campaigns with a one-sided focus on capital gains, dividends, and banking privileges, with little attention to the inherent risks. Many of these investors were also deposit customers and had built up considerable trust in their bank.

Our setting is also helpful in ruling out alternative explanations for lower risk taking by individuals with personal experiences around inheritances. For example, temporary provisions by the Danish Financial Supervisory Authority fully insured the vast majority of depositors against defaults (while investments were not insured), and relatively low estate tax ensures that 85 percent of the estates (or their beneficiaries) hold sufficient cash to settle inheritance cases without selling assets.

If negative experiences affect individuals' future outlooks on investments or individuals' attitudes regarding the trustworthiness of financial institutions, we hypothesize that individuals with such personal experiences will be more reluctant to take risk in subsequent periods.

To examine the effect by the degree of personal experience, we investigate whether beneficiaries with first-, second-, and third-hand experiences behave differently than beneficiaries with common experiences when allocating inherited wealth (for definitions of experiences, see figure and explanation).

We find that third-hand experiences have a negligible effect on the level of risk taking. Investors with a second-hand experience resulting from losses within the close family reduce their allocation to risky assets marginally (compared to individuals without experiences). Investors with first-hand experiences, however, actively reduce the fraction of liquid wealth allocated to stocks by around 9 percentage points (again, relative to individuals without experiences). These effects are economically significant given a baseline allocation of liquid wealth to stocks of around 30 percent for beneficiaries who inherit. Thus, events experienced personally have much stronger effects on active risk taking than do events affecting peers and relatives.



Degree of experience and portfolio rebalancing around inheritances: This graph decomposes the change in risky asset share, measured by the fraction of liquid assets allocated to stocks and mutual funds around inheritances, into the counterfactual passive and active changes. First-hand experience is an indicator for personal experiences due to the loss of investments in a defaulted bank. Second-hand experience is an indicator for first-hand experiences in the immediate family (parent, sibling, child, or spouse). Third-hand experience is an indicator for individuals who are living in a municipality with a defaulted bank.

Macroeconomic experiences of less importance

The size of the causal effect of first-hand experiences can be estimated by comparing active changes in risk taking around inheritances, depending on the timing of the inheritance case relative to defaults. Individuals who inherit before they experience a default, on average, increase their risk taking by 3.1 percentage points, while individuals who inherit after they have experienced a default actively reduce the fraction of liquid wealth allocated to stocks by 9.2 percentage points. The difference equals 12.3 percentage points and is both economically and statistically significant.

Investors who invested in bank stocks, and subsequently lost a significant fraction of their wealth, are less willing to hold risky assets – even when they receive a significant positive windfall that more than offsets their losses. However, portfolio changes resulting from the experiences of peers and the macroeconomic climate are much smaller in magnitude. Hence, our results suggest that changes in an individual's risk taking are largely shaped by events experienced personally and only to a lesser extent by experiences of close relatives or macroeconomic conditions.

Our study documents that the financial crisis resulted in lower future risk taking with cohort effects primarily driven by first-hand experiences, rather than by common experiences. The welfare costs of the lower levels of risk taking are likely to be substantial and will lead to significantly lower lifetime consumption. This raises the question of how and what individuals learn from their past investment experiences. An appropriate response to negative personal experiences would be to diversify the portfolio. Instead, individuals shy away from risk taking by selling risky assets and holding cash.

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Denouncing Odious Debts: The Russian Loan of 1906

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Research Center SAFE

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Université Libre de Bruxelles

Economists have suggested it would be optimal to signal the odious character of bonds when they are issued. But since there is no international law defining such debts, it may be wondered whether markets consider odious debts any differently from other debts and whether it pays to denounce these debts as odious. This paper exploits a unique case, the 1906 loan issued by Russia, to determine markets' perception of debts presented as unfair to repay and to establish whether protests have an impact on the issuance of such loans. Although the protests could not prevent the issuance, we show that the press campaigns increased the yields of all Russian Bonds traded in Paris, and thus Russia's future borrowing costs. Once the press campaigns stopped, yields experienced a declining trend.

Legal scholars have attempted to limit the willingness to lend to dictatorship regimes by developing the doctrine of odious debt. Since the doctrine has not been recognized by any court, one could argue that denouncing odious debts is useless. However, empirical evidence shows (Peillex and Ureche-Rangau, 2016) that ethics play a role in investment decisions, suggesting that denouncing odious debts would influence the market, preventing ethical agents from buying such bonds. In this case, an odious debt label would send a clear signal.

Although literature suggests odious debts should be denounced before being issued, no paper has yet analyzed how markets react when debts are denounced as unfair to repay (Collet, 2013 is an exception, but since it analyzes the first case ever when odious debts were mentioned it may be hard to generalize its results). Empirical evidence is also missing on the effectiveness of press campaigns and organized protest against odious debts. We argue that the usefulness of denouncing debts as odious should not be judged only on the ability to prevent bonds from being issued or on their repudiation, but also on the financial costs imposed on the issuer. More precisely, one should assess whether the yields of the bonds were affected by press campaigns, or whether the yields to holders of the odious loan differed from those on other bonds issued earlier.

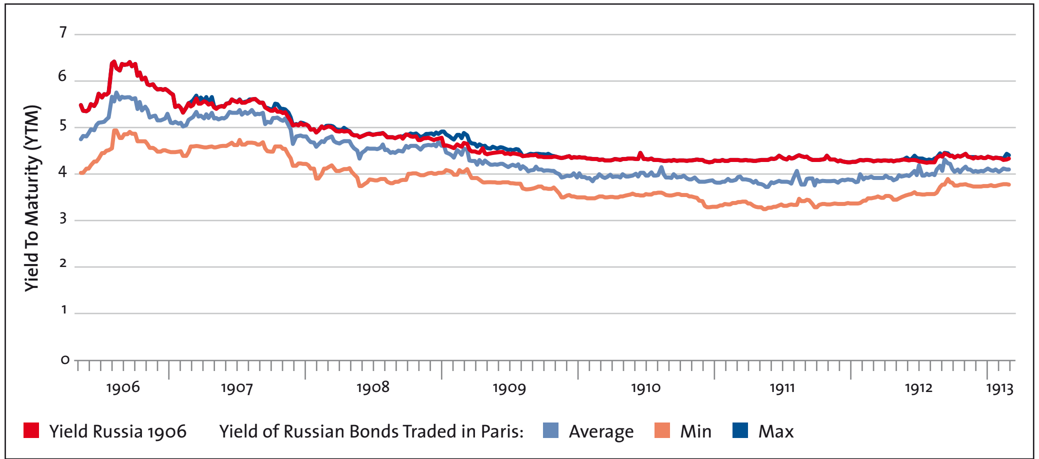
Protests against the Russian loan of 1906

To address this challenge we exploit a unique historical episode. In 1906, the Russian government floated a bond in Paris to cover the costs of its war against Japan as well as to crush the political opposition. Issued without parliamentary consent, the loan met with fierce opposition. Several Russian political parties pledged they would repudiate it should they come to power. In parallel, the flotation led to massive protests and press campaigns in Britain, France, and Germany, where it was to be listed, which led to attempts to prevent its issue.

Our paper relies on a panel of Russian bonds traded in Paris between 1906 and 1913. Taking into account the bonds' characteristics, we test if their yields were higher during the press campaigns and if the 1906 loan was penalized because of its odious character. To examine the market's reaction, we analyze the yields of Russian bonds and exploit the perceived difference between the 1906 loan and those issued previously by the Russian regime. To do so, we have constructed a panel of 13 long-term Russian bonds traded on the Paris Stock

Exchange, the main foreign market for Russian bonds at the time. The prices were collected on a weekly basis from the Cote Officielle des Agents de Change for a period stretching from May 1906 to April 1913.

Figure 1 shows that the yields of the 1906 loan were higher than the yields for other bonds. This difference is striking as the yields between bonds issued by the same sovereign are usually the same.



Yield of Russian Bonds Traded in Paris. The figure shows the yield to maturity of the 1906 loan compared to the average yield to maturity for the Russian bonds and their high and low yields to maturity.

To explain this difference we analyze the yield of the Russian loans based on a panel regression using variables linked to the protests, the odious nature of the 1906 loan, its "bad publicity" (a continuous variable counting the number of words with a negative connotation associated to the loans in the newspaper L'Humanité), as well as a set of control variables such as macroeconomic variables and the various bonds characteristics. Our main variables of interest, protest and bad publicity index, are in all specifications positive and statistically significant. Protest against the issue of the 1906 loan thus had an impact on the yields of all Russian bonds. The Odious Debt dummy variable is statistically different from zero and positive in all regressions. Being labelled as odious thus increases the yield of the bond.

In addition to our panel analysis, we rely on a structural break methodology to determine the main turning point in the spread between the yield of the 1906 loan and the average yield of the Russian bonds used in the panel regression. The paper shows that these breaks may be linked to bondholders' reassessment of the odious nature of the Russian regime.

Press plays an important role

Our results indicate that the press campaigns had an impact from the outset on all Russian loans, suggesting that, following the press campaigns, many investors considered the regime as odious. The results further show that participants were reluctant to hold the 1906 loan in particular and still preferred other loans issued by Russia. This difference of treatment disappeared once the intensity of the press campaigns diminished. Once protests and negative press reports subsided, investors began to buy "cheap" 1906 bonds. Our results highlight the importance of protests and press campaigns. While some investors would never have bought the 1906 loan, others were influenced by the negative press coverage. The press has an important role to play in terms of ethics because it can remind investors of the unethical character of "odious" debts and regimes.

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This paper is forthcoming in the Journal of Business Ethics and is available at:
http://safe-frankfurt.de/odious-debts

"Beware of Falling Prey to the Promise of Reducing Complexity"

Katja Langenbucher
Goethe University

In this interview, Katja Langenbucher, Professor of Law at Goethe University, talks about differences in legal and economic thinking and about the implications of economic transplants – concepts taken from the economic into the legal world. Langenbucher has held a full professorship for Private Law, Corporate and Financial Law in Goethe University's House of Finance since 2007 and is an affiliated professor at Sciences-Po, Paris. Her main research focuses on corporate and capital markets law and includes selected topics of European Legal Theory.

The title of your recently published book is "Economic Transplants". How do you define this concept?

In the book, I describe European law making as done from an "internal point of view." This means trying to reconstruct the legal text and to apply it to the world. By contrast, I have described a lot of US legal research as relying on an "externalist point of view." Compare this to a natural scientist or even an anthropologist, focused on observing what legal actors say and do in a certain situation and suggesting ways forward. Economic transplants are at the intersection of these points of view.

What drew your interest on that topic?

I come from a continental legal background which means we work a lot with the interpretation of text and rely on hermeneutic methods. But at the same time, if you work on corporate and financial markets law, you will be drawn to the US legal system with their long tradition of financial markets and securities law and perceiving economic insight as a natural part of law making. I wanted to understand more deeply how this interaction between law and economics works out in practice over there and why it is not commonplace over here.

Which promises do economic transplants offer?

In the book, I outline three promises. The two more philosophical promises are "measurability" and "reducing complexity." Remember that a lot of legal theory deals with how to interpret text and how to understand whether something will or should fit under a vague legal rule. In this process, words are the natural methodological tool. What did the legislator say? Did he want to capture this case? What can we find in a judge's opinion, and what are scholarly arguments on the matter? On this basis, you reach what we call a "reasoned decision". Faced with this complex, cumbersome process, economic transplants hold out a promise: It might be more attractive to look somewhere else, to use a more "hard and fast", "objective" – perhaps "scientific" – method. The last, more pragmatic promise is the offer of a "common language" for European lawmaking. Remember that today we have 27 member states in the European Union with 27 different legal orders. Economics can be an attractive common language on a "meta-level", beyond the intricacies of each jurisdiction.

You write that "communication across disciplines may face cultural problems". Can you give an example?

Financial markets law offers many examples. In the book I use, for instance, the assumption of "rational actors" in efficient capital markets as a basis of some of the theoretical models. Transplanting this idea into the law, we encounter the term "reasonable investor" in the Market Abuse Regulation of 2017. Using the concept of a "reasonable investor" decides, for example, on timely disclosure of inside information or on a prohibition to trade on the basis of such information. Take the Volkswagen scandal: When was the company obliged to tell the markets that there was a problem? Ask an economist and ask a lawyer. The economist may answer on the basis of a theoretical model – under strict assumptions trying to figure out what type of information will trigger which type of market reaction. Or he will try to find comparable empirical data or run an event study. The "externalist" lawyer might happily defer to this assessment and decide his case accordingly. The "internalist" lawyer, however, will also ask: Is this what the legislator wanted? Will deferring to economic insight fit in with more general legal rules and principles? Can we reach a fair and just result in the case at hand?

Economics is often perceived as "hard science". Is the legal world too uncritical?

To the extent that lawyers expect economics to give us "objective" and "tested" answers to legal intricacies, I do think so. And moving beyond the legal world in a narrow sense towards the broader regulatory and parliamentary areas of law making, we still encounter this challenge. Transforming an economic argument into either a strictly legal or a more political argument risks losing complexity. In the book, I call such transplants "economic clichés". We find them, for instance, when we see references to economists' papers without carefully pointing out the underlying assumptions, potential biases, or even flaws. If economic transplants enter the legal – or the political – dialogue in this way, they cannot live up to any of the promises they hold out. In that sense, a lawyer must beware of falling prey to the promises of measurability and reducing complexity.

To what extent do economic transplants have an impact on adjudication and law making in Europe?

On judges, the impact is relatively small. Obviously, judges are not trained in economics. In one case, I show the ensuing risks of applying economic transplants without such training in assessing empirical data. In another case, by contrast, I portray a conscious judicial decision to reason from an "internal point of view" instead of deferring to economic transplants. For the legislator, things are different. Economic transplants often play a role in promoting certain policy goals. A case I discuss in the book is the regulation of shareholder activism. In other instances, economic transplants can offer help to understand how a specific goal might be achieved by highlighting, for example, certain incentive structures. They may also, in the form of so called "regulatory impact assessments", help us to figure out whether regulation passed was successful in achieving its goals.

You write that economic transplants might help rationalize legal and political debate. How optimistic are you about that?

Can political debate ever be rationalized? But seriously, even if I am skeptical, it is not as bad as it looks. Law making is not only done in parliament but involves careful legal drafting by highly trained staff in ministries. They will often face the tricky task of fitting the goals stemming from a certain economic policy into one legal order. They have to make sure an isolated change in the law does not cause unwanted "ripple effects" elsewhere in the legal universe.

Should lawyers get more economic training, or should they rely more often on experts?

We should probably distinguish between different legal actors. If this is about practicing lawyers and judges, I am hesitant. Quite pragmatically, I do not see how we could ensure meaningful and up-to-date economic training of large parts of the legal profession nor do I consider this a necessary part of their work. As to relying on experts in the way we see them in, for example, a medical malpractice suit, this applies only to questions of fact. However, many economic transplants are questions of law, such as, for instance, the "reasonable investor". For these, experts are not an option. As to regulators and lawmakers, I am more hopeful – maybe not for training in economics in the strict sense, but for more transparency. Avoiding the "economic clichés" I referred to earlier requires carefully distinguishing between what we can robustly infer from an economic study and what is being claimed as a seemingly "scientifically proven" policy goal. We can only try to get better at this important communicative endeavor, working towards ever more transparency.

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Discussing the New Role of Central Banks

In recent years, central banks, such as the European Central Bank (ECB), the U.S. Federal Reserve, and the Bank of England, have been attacked for stretching their mandates or for implementing an alleged wrong monetary policy. The rise of populism in different countries has intensified this debate, and the independence of central banks has been put into question more than once. Have central banks become too powerful? What can be done to hold them accountable for their decisions? These issues were debated in two Policy Lectures at the House of Finance.

Better Judicial Control

Rosa María Lastra from Queen Mary University of London presented her ideas about populism and central bank independence in a Policy Lecture on 26 April. She argued that a specialized chamber within the European Court of Justice could improve the legal control of the ECB. “Having dedicated specialized judges with expertise in financial and monetary matters when adjudicating cases related to the ECB would enhance the legal framework of ECB accountability in light of the significantly expanded mandate of the ECB,” she said. According to Lastra, populists see central banks as a part of the “political establishment.” They wanted faster growth and, at the same time, called for protectionist measures, such as limits to immigration, Lastra said. Furthermore, she added that inequality fed popular discontent. “Those who feel disenchanted, with little to lose, will vote, rebel or protest against the ‘political establishment’,” Lastra argued. She said that populist attacks on central banks have damaged the “social legitimacy” of central banks. “Populism is a reality we need to face,” Lastra said.

Also, the mandate of central banks has become “fuzzier, broader, and more complicated” in recent years, Lastra pointed out. This has increased the pressure on the debate of whether a central bank abides by its mandate and of who holds the central bank accountable. Although Lastra believes that parliamentary accountability remains important, she is not convinced that politicians are properly performing this function

Rosa María Lastra from Queen Mary University of London

right now. Instead, a better judicial control of central banks could help boost public confidence in central banks. With regard to the European Union, she proposes to set up a specialized chamber within the European Court of Justice where specialized judges would deal with central bank-related issues. Also, central banks needed to communicate more effectively with the public. “They were not very good at communicating in the past. Much more has to be done,” Lastra said.

“Expertise is not just inside independent institutions”

This view is shared by Sir Paul Tucker. “The worst thing independent institutions can do is to take action and not talk to the public,” Tucker said in a lecture on 30 April at the House of Finance. He is the former Deputy Governor of the Bank of England with responsibility for financial stability and Chair of the Systemic Risk Council today. In a joint lecture of the Institute for Law and Finance (ILF) and Center SAFE

Sir Paul Tucker

Tucker talked about his ideas. The core of his interest is the delegation of power to technocrats or institutions which have no democratic legitimation and the consequences of such independence for these institutions. In his lecture, Tucker examined the arguments in favor of such delegations of power. One central consideration is expertise: Politicians give over decisions to experts which is supposed to lead to better results. In Tucker´s view, this is a flawed argument. “Expertise is not just inside independent institutions,” Tucker argued. Clearly, it would also be possible to separate expertise and policymaking, Tucker said.

However, one major problem of such delegations of power is the lack of democratic control. Tucker argued that two things are vital when delegating power to an independent institution. Firstly, the design of policy making needs to be effective. Looking at the ECB, Tucker said that the Governing Council was too big to take decisions effectively. Also, the voting behavior of its members should be transparent to make them more accountable. Tucker also sees the ECB´s mandate of monetary policy and banking supervision critically. The problem of having two missions at the same time is that one receives more attention than the other, Tucker stated.

Secondly, strict rules for the delegation of competencies are needed. Independent institutions should be accountable for their actions and monitorable for the public.

Delegation of power should be done with diligence, Tucker said. Otherwise “we would strengthen the argument that the government becomes undemocratic.” Also, independent institutions like central banks should use their power with care. “They have the duty to do the least to deliver their missions,” Tucker said.

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Selected Policy Center Publications

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„Why the Initial Regulation of Financial Innovations is Decisive – Regulatory Arbitrage and Off-Balance-Sheet Leasing in Germany”,
Policy Letter No. 69.

Goldmann, M. and G. Pustovit (2018)
“Governing Cryptocurrencies through Forward Guidance?”,
Policy Letter No. 68.

Kasinger, J. and L. Pelizzon (2018)
“Financial Stability in the EU:
A Case for Micro Data Transparency”,
Policy Letter No. 67.

The SAFE Working Papers can be downloaded at
http://safe-frankfurt.de/policy-publications

News

Lorenzo Bini Smaghi: "Purple Bonds" as an Alternative to Eurobonds

What can be done to strengthen the euro area architecture? In a Policy Lecture in May, Lorenzo Bini Smaghi, Chairman of the Board of Société Générale, put forward his idea of "Purple bonds". This concept aims at protecting national bond stock from disruption, encouraging fiscal discipline, and lowering funding costs for the periphery. Essentially, the idea is that the Fiscal Compact (European Fiscal Stability Treaty) requires member states to reduce general government debt above 60% of GDP by one twentieth every year. Any refinancing needs that incur debt in excess of this limit should be done in "Red bonds" that would carry a high risk premium, he suggests. The debt at or below the yearly limit of the Fiscal Compact would be "Purple" and protected from any debt restructuring that could otherwise be required as part of an eventual program of the European Stability Mechanism. The no restructuring guarantee would not apply if a member state were to leave the euro area. Starting from today, all existing government debt would be labelled "Purple", declining to 60% of GDP by the end of the 20-year period. For Bini Smaghi, "Purple bonds" have an important advantage. "They could give national governments an incentive for more fiscal discipline," he said.

Ardo Hansson: Side Effects of ECB's Monetary Policy May Get Stronger

During the last years, the European Central Bank (ECB) employed several unconventional monetary policy tools to jump-start economic growth and spur demand. Has the euro area monetary policy been effective and what have been the side effects of unconventional monetary policy, especially of the asset purchase programs? In a Policy Lecture in April, Ardo Hansson, Governor of the Eesti Pank (Bank of Estonia) and member of the ECB Governing Council, pointed out that non-standard measures of ECB monetary policy have mostly achieved their intended outcomes. However, the longer the accommodative monetary policy lasted, the higher the probability of significant side-effects was, Hansson warned.

Joachim Wuermeling: A European Digital Financial Center

The United Kingdom's withdrawal from the European Union is an opportunity for continental Europe, including Ireland, to set up a technologically first-class financial hub and to become a highly relevant global player. In a Policy Lecture in February, Joachim Wuermeling, Member of the Executive Board of Deutsche Bundesbank and Member of the SAFE Policy Council, presented some preliminary thoughts on the idea of a European digital financial center. He noted that the European Union already provides most of the qualities required for such a center although at the moment Europe's potential is spread over various locations across the continent. Wuermeling sees a chance in new digital technologies, such as real-time communication, distributed ledger technology, platforms, and co-working to set up a technologically first-class financial hub from scratch. Policymakers could serve as catalysts by bringing the key players together, he said.

Thomas Mosk Awarded ECB Lamfalussy Fellowship

Thomas Mosk, Assistant Professor at SAFE, has been awarded a Lamfalussy Research Fellowship at the European Central Bank (ECB) for his research proposal "Limits to Monetary Policy Transmission: Evidence from Corporate Loan Pricing." In a joint project with Rainer Haselmann, Program Director of the research area "Financial Institutions" at SAFE, Mosk aims to assess the interest rate pass-through of monetary policy to loan rates using a unique hand-collected dataset on newly originated corporate term loans and interest negotiations of a large commercial bank in the Netherlands produced between 2007 and 2013.

Selected Publications

Ioannidou, V., Mosk, T. and J. Sturgess (2018)
"Intended and Unintended Consequences of Government Credit Guarantee Programs",
Finance and Investment: The European Case, Oxford University Press.

Elsinger, H., Schmidt-Dengler, P. and C. Zulehner (2018)
"Competition in Treasury Auctions",
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Donadelli, M., Paradiso, A. and M. Riedel (2018)
"A Quasi Real-Time Leading Indicator for the EU Industrial Production",
forthcoming in The Manchester School.

Lambert, C., Noth, F. and U. Schüwer (2018)
"How Do Banks React to Catastrophic Events? Evidence from Hurricane Katrina",
forthcoming in Review of Finance.

Brennan, M. and H. Kraft (2018)
"Leaning Against the Wind: Debt Financing in the Face of Adversity",
forthcoming in Financial Management.

Bursian, D. and E. Faia (2018)
"Trust in the Monetary Authority",
forthcoming in the Journal of Monetary Economics.

Caporin, M., Pelizzon, L., Ravazzolo, F. and R. Rigobon (2018)
"Measuring Sovereign Contagion in Europe",
Journal of Financial Stability, Vol. 34, pp. 150–181.

Collet, S. and K. Oosterlinck (2018)
"Denouncing Odious Debts",
forthcoming in Journal of Business Ethics.

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"On the Fintech Revolution: Interpreting the Forces of Innovation, Disruption, and Transformation in Financial Services",
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Lehman Ten Years On

Harold James
Princeton University

This year, Harold James holds the Visiting Professorship of Financial History at Goethe University´s House of Finance. His research focuses on Economics and Financial History and Modern European History, especially on Germany and the European Monetary Union. He is Claude and Lore Kelly Professor in European Studies, Professor of History and International Affairs, and Director of the Program in Contemporary European Politics and Society in Princeton University, Furthermore, he holds the position of Official Historian at the International Monetary Fund.

Why should we care about the tenth anniversary of the Lehman failure? Aren't there more important issues to worry about, and more dramatic events to commemorate? 2018 brings many reminiscences, such as the hundredth anniversary of the end of the First World War. What are the claims of a medium-sized bank failure to rival in importance the end of a conflict that destroyed European civilization?

Lehman was not an extraordinarily large bank. It was probably not insolvent when it collapsed. It is hard to see how Lehman should have been able to take down the economy of the United States or the world financial system. But sometimes the flapping of a butterfly's wings transforms the world. During the European financial crisis that erupted after 2010, Lehman was constantly invoked, especially by Europeans, and applied to the threat of state bankruptcies and defaults.

The financial crisis had three big effects, fundamentally shifting the general basis of the narrative told by opinion-shapers and policy-makers. One: The Lehman crisis made a particular kind of financial history popular, which went along with a financial theory – that of Charles Kindleberger, who drew very explicitly on the work of Hyman Minsky on financial cycles. It was read as a warning against "market fundamentalism."

Second, Lehman apparently revealed that not just the story of the old business cycle was relevant, but that the Great Depression was contemporary. Ben Bernanke, the Federal Reserve chair, recalled that his response to the Lehman developments was to think of the Austrian Creditanstalt in 1931: "My mind went back to my own studies of the Great Depression of the 1930s." In the Great Depression, especially in Germany and the US a liquidationist attitude had prevailed, following the dictum of Andrew Mellon: "Liquidate labor, liquidate stocks, liquidate the farmers, liquidate real estate." By contrast, in the Great Recession, debt – especially public debt – was used to replace insecure private debt. Because of low interest rates, that may be sustainable, at least for some time.

The third new story was that the butterfly of Lehman was the signal of the end of American capitalism. The German finance minister, Peer Steinbrück, explained that "The US will lose its status as the superpower of the global financial system." The crisis was widely seen as a quintessentially American affair, emanating from a combination of testosterone-driven finance and a political penchant for promoting real estate even for those who could not really afford it. It was only gradually that analysts such as Hyun Song Shin and Tam Bayoumi pointed out the transatlantic nature of the crisis, and the essential part played by badly regulated and over-sized European banks in the build-up of risk. One of the most widely used Chinese terms in the wake of Lehman was xìng zai lè huò, best translated as "Schadenfreude": somebody else – some other society – tripped on an enormous political banana skin.

Two of these popular stories are not really right. The financial crisis showed up problems of complexity, of the intertwining of dysfunctional and highly intransparent private and state institutions, and not of markets as such. And the world was not near to another Great Depression. Intransparency, as rapidly became clear, was not a unique property of the U.S.. The combination of these two stories had a massive effect on perceptions, and contributed greatly to the third story, which is quite real: the loss of the United States' financial and political preeminence.

Events

June

2 June – 21 July	**GBS Open Program** **Bank Management** Speaker: Axel Wieandt, WHU – Otto Beisheim School of Management
5 June 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Angelo Ranaldo, University of St. Gallen
5 June 2.15 – 3.45 pm	**Frankfurt Macro Seminar – Joint with SAFE** Speaker: Kristoffer Nimark, Cornell University
8 June 11.00 am – 5.30 pm	**Joint Goethe University, SAFE and IBF Research Conference** **Lehman – 10 years after** Program Chair: Harold James
11 June 5.00 pm	**EFL Jour Fixe** **Fund Savings Plans Choices with and without Robo Advice** Speaker: Konstantin Bräuer, E-Finance Lab
12 June 2.15 – 3.45 pm	**Frankfurt Macro Seminar – Joint with SAFE** Speaker: Nicolas Crouzet, Northwestern University
12 June 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Byoung-Hyoun Hwang, Cornell University
15 June 2 – 2.15 pm	**Frankfurt Macro Seminar – Joint with Deutsche Bundesbank and SAFE** Speaker: Frank Schorfheide, University of Pennsylvania
15 – 16 June	**SAFE Conference** **Firms in the Labor Market: Recruitment, Wages and the Role of Financing Conditions** Keynote speaker: Steven Davis, University of Chicago
16 June – 6 July	**GBS Open Program** **FinTech in Retail Financial Services** Speaker: Andreas Hackethal, Goethe University
19 June 12.15 – 1.45 pm	**SAFE Policy Lecture** Speaker: Pentti Hakkarainen, European Central Bank
19 June 2.15 – 3.45 pm	**Frankfurt Macro Seminar – Joint with SAFE** Speaker: Steven Davis, University of Chicago
19 June 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Michael Hasler, University of Toronto
22 June 12.15 – 1.45 pm	**SAFE Policy Lecture** Speaker: Ashoka Mody, Princeton University
26 June 2.15 – 3.45 pm	**Frankfurt Macro Seminar – Joint with SAFE** Speaker: Bart Hobijn, Arizona State University
26 June 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Casey Rothschild, Wellesley College

July

2 July 5.00 pm	**EFL Jour Fixe** **From Crowdfunding to Crowdsales: An Exploratory Study of Token Sales and Initial Coin Offerings** Speaker: Daniel Blaseg, E-Finance Lab
3 July 2.15 – 3.45 pm	**Frankfurt Macro Seminar – Joint with SAFE** Speaker: Silvio Petriconi, Bocconi University
3 July 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Francesco D'Acunto, University of Maryland
10 July 2.15 – 3.45 pm	**Frankfurt Macro Seminar – Joint with SAFE** Speaker: Basit Zafar, Arizona State University
10 July 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Harjoat Bhamra, Imperial College, London
12 July 12.30 – 2 pm	**SAFE Policy Lecture** Speaker: Theodor Weimer, Deutsche Börse
6 – 21 July	**GBS Open Program** **Bank Risk Governance and Regulation** Speaker: Carsten Lehr, Westend Bank AG
7 – 28 July	**GBS Open Program** **Financial Stability and Regulation** Speaker: Norbert Metiu, Deutsche Bundesbank
14 – 28 July	**GBS Open Program** **Household Finance** Speaker: Stefan Meyer, Leibniz Universität Hannover
20 – 27 July	**GBS Open Program** **International Finance** Speaker: Loriana Pelizzon, Goethe University
28 July – 11 August	**GBS Open Program** **Mergers & Acquisitions** Speaker: Volker Brühl, CFS

August

20 – 21 August	**2018 CEBRA Annual Meeting** Co-organized by SAFE
20 – 21 August	**SAFE Conference** **2nd SAFE Market Microstructure Conference**
28 August 4.15 – 5.30 pm	**Finance Seminar – Joint with SAFE** Speaker: Andriy Shkilko, Wilfrid Laurier University, Ontario

CFS Center for Financial Studies
EFL E-Finance Lab Frankfurt am Main
GBS Goethe Business School
IBF Institut für Bank- und Finanzgeschichte
ILF Institute for Law and Finance

Please note that for some events registration is compulsory.

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