

**The Seeds of a Crisis: A Theory of  
Bank Liquidity and Risk-taking over  
the Business Cycle  
by Viral Acharya and Hassan Naqvi**

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- Thanks for the learning opportunity; sorry for the lack of expertise
- Just some questions and observations
- (*quick summary*) Diamond-Dybvig type 3-period model: investors “flight to quality”; banks “excess liquidity”; policy recommendation: central bank to adopt a “leaning against liquidity” approach

# Some questions for discussion...

- Did Greenspan adopt a “leaning against liquidity” policy in 1987? After “internet bubble burst”? Greenspan creates the “housing bubble”? (Taylor 2009)
- (Modeling qn): why 3-period model? What if there are infinite horizons? Would a “leaning against liquidity” lead to “bubble cycle”? (Williamson, 1987, 1988)
- (Time-consistency?) (Chang/ Ireland/ Persson/ Svensson,...)

# (other typical issues in m-policy)

- (*In-*) Determinacy issues: Lubik and Schorfheide, 2004, AER; Benhabib et al, 2001, AER;
- (idea): When agents take the monetary policy into consideration, will it “help” the market to “pin down” certain prices (including interest rates), or more confused?
- pro-active vs reactive policy? (Dupor, 2001, JET)

# **SORRY** for self-advertisement!

- Monetary policy affects different real estate related-assets differently (depending on the regime) (see Chang, Chen and Leung, JREFE, forthcoming)
- Idea: when the central bank changes the m-policy, term structure will change, which can magnify or dampen the original effect.

(figure from  
Gary  
Gorton's  
book)

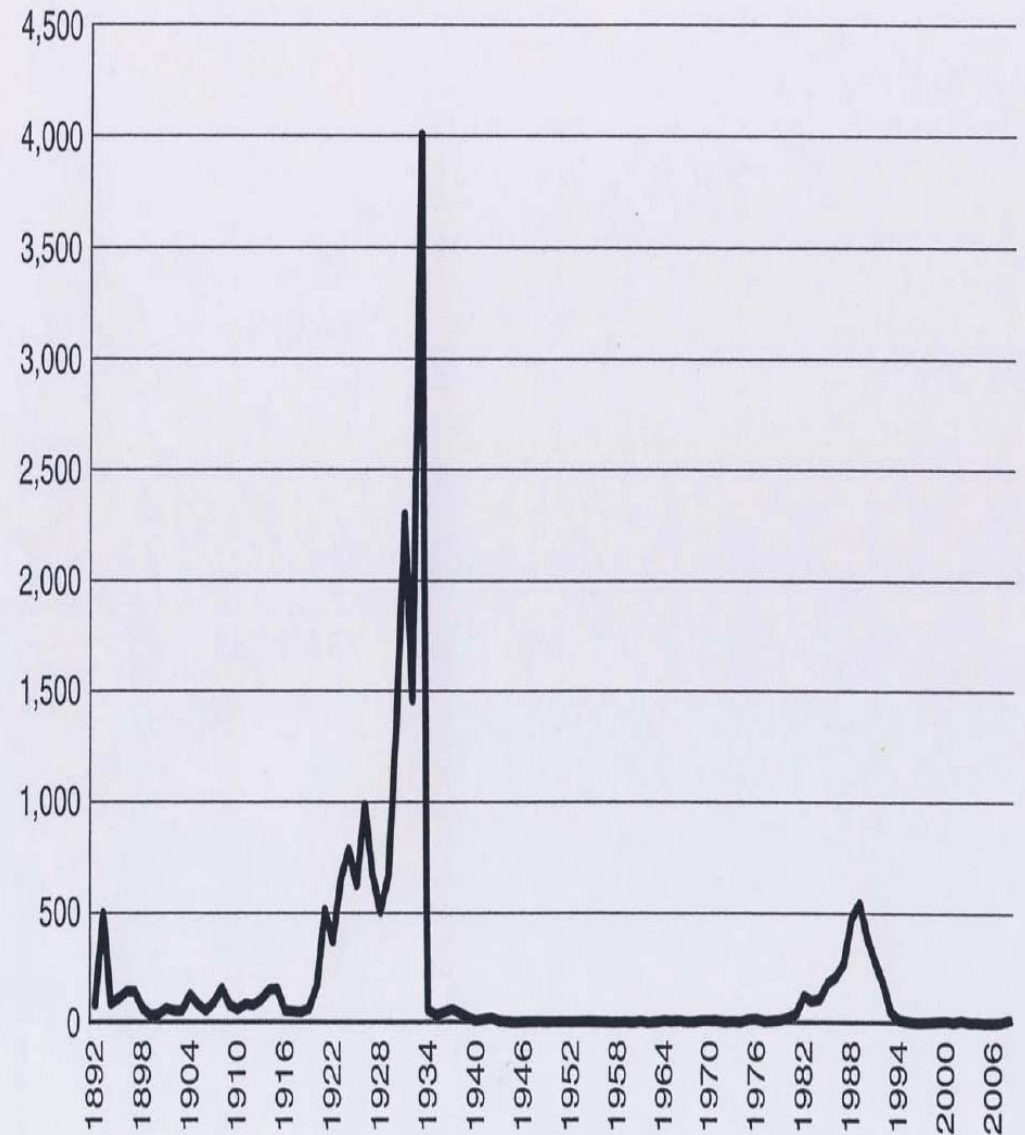


FIGURE 2.1 Number of U.S. Bank Failures, 1892–2008. Source: *Banking and Monetary Statistics* and FDIC.

# Why the recent global crisis so severe?

- Gorton (2010, p. 13-14) “Since 1934, when deposit insurance was adopted, until the current panic— a span of almost 75 years— there had been no banking panics... **What gave us almost 75 years of relative quiet in banking? What has changed?...**”

# Minor comments...

- Wage,  $w$ , seems to be missing in the maximization of p.14.



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