

## Wall Street – UH 4504

Class: Tu Th 3:30 – 4:45, in AJE 1406 (aka. “the Senior Common Room”)

Professor: Dan Simundza, Office Hours: Wed 10:00 – 11:30 at GFURR office (Kent Square building, 250 S. Main, Suite 312); also by appointment

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### Description:

This class uses the framework of political economy to study disruptions in the financial arena. We will start with arguably the most disruptive innovation: money (which, amongst other things, makes the world go ‘round, cannot buy love, and is the root of all evil). Our discussion here will focus on the precursors to money (including debt), its creation, and the effects it has had on society. We will then turn our attention to the topic of finance, and how it has shaped society. We will provide a historical background of the development of financial practices as well as a description of the modern financial industry. Central to our analysis will be a focus on the institutions (e.g. commercial banks, markets, central banks, regulatory agencies) that have developed to facilitate financial transactions.

With this historical context of money and finance, we turn to more recent developments – financialization, “fintech,” and financial crises. We will study the proliferation of finance (i.e. the growth of the traditional financial sector, and the willingness of traditionally non-financial firms to engage in financial activities), the disruptions that occur when technology firms enter the financial industry, and what happens when it all goes wrong and crisis ensues. Special attention will be paid to the regulatory and policy arenas, with an emphasis on central bank policy.

This course will involve two main components – classroom discussion and studio work (see below). The projects in these components will be complementary and will stress collaboration in identifying and describing “big questions” in the political economy of finance. Our goal is to generate methods and frameworks that can be used to solve critical, real-world problems related to policy and regulation in the monetary and financial worlds.

### Studio work:

Working collaboratively in small groups, students will strive to solve some of the big questions in the political economy of modern finance (examples below). Shoot for the moon! – we want to identify, describe, and illustrate the most critical and fundamental problems related to money and finance facing society. We will utilize students’ various training and backgrounds to collaborate in a transdisciplinary manner, approaching these questions from multiple viewpoints and perspectives. This class will stress the importance of developing a framework in which such questions can be answered. The way in which you arrive at your result is just as, if not more, important than the result itself.

Our class discussions will focus on many topics and questions appropriate for analysis, but students are also encouraged to develop questions in their areas of personal interest. To help get you started thinking about your studio project, I have listed a few possible topics below.

- Since the end of World War II, the share of the nation's GDP from the financial sector has steadily risen from roughly 2.5% immediately post-war to over 8% in the mid-2000's. How much finance is healthy for our economy?
- On a related note, we have just recently experienced the worst recession since the Great Depression, and recovery has been slow and unequal across sectors of the economy. The financial sector bounced back relatively quickly, while the labor market was slow to return to pre-crisis levels of employment (i.e. a "jobless recovery"). Are there policies that we could enact that would counteract this differential recovery? Should we?
- The lines between financial and non-financial firms are becoming more blurred over time. As an example, consider the social networking website Facebook, which makes most of its revenues through what is essentially an old-fashioned business – advertising. But now consider that Facebook was recently granted a banking license in Ireland! They are licensed to offer e-payment services across Europe, where they have over 150 million users, putting Facebook in direct competition with traditional banks, PayPal, and money transfer businesses such as Western Union. How should Facebook be regulated as it develops this new service? Should we regulate firms based on what they do, or how they are incorporated?
  - Note: not all non-financial firms are expanding into the financial arena. As an example, since 2015 General Electric has sold off the majority of the assets of its financial arm, GE Capital, in order to focus on its core manufacturing business.
- Technology is changing the marketplaces in which individuals and firms transact, both in the real economy (e.g. eBay, Uber, Airbnb) and in finance (e.g. eTrade, algorithmic trading, robo-advisors). Moreover, with the development and evolution of electronic payments and crypto-currencies like Bitcoin, the medium of exchange is also undergoing a fundamental shift. What types of policies do we need for these new marketplaces, and do we need to regulate the medium of exchange?
- Concerning the topic of money more broadly, note that while Section 8 of Article I of the US Constitution gives Congress the right to "coin money [and] regulate the value thereof," it does not specify in any terms how this is to be done. The current monetary authority in the US, the Federal Reserve, is, in the words of Nobel Prize winning economist James Buchanan, merely an "institutionally established authority charged with an ill-defined responsibility to 'do good,' as determined by its own evaluation." Should there be a monetary constitution for the United States? If so, let's write one!

Steps:

- 1) Discover and define a problem facing society within the thematic boundaries of money and finance.
- 2) Characterize and describe the problem utilizing the diverse backgrounds of your group's members. This will likely require research, data collection, modelling, and

analysis. Each group will present their problem to the class – you must convince us that this is a significant problem, worthy of our attention.

- 3) Develop a framework to solve the problem. You may have to learn and/or generate new methods (e.g. statistical analysis, programming, network design) in order to do this. This step will likely involve multiple iterations, and you may feel that the outcome of your efforts is uncertain at best. There is also the possibility that some of your attacks on the problem will lead to nothing – do not let failure slow you down! Instead, learn from all of your efforts.
- 4) Provide a solution to the problem and illustrate how it will work. Solutions are likely to take the form of policy proposals. You could propose a new policy, modify regulations, change laws, etc. Students will present the results of their semester-long collaboration to the class. Please keep in mind that your classmates come from diverse backgrounds, and your presentation should aim to communicate your results in engaging and intuitive ways.
- 5) As a final project, you will identify a diverse group of stakeholders with interest in your problem, and devise a strategy to disseminate your proposed solution to this group of stakeholders. This could take the form of preparing a presentation for a conference or submitting a short “white paper” to a think-tank or policy research organization.

#### Student responsibilities:

My expectations for students in this class are high. I expect students to prepare thoroughly, contribute to class discussions and debates, and to seek help when they need it.

- Classroom participation [25%] – The easiest way for you to do well in this class is to actively participate. Learning is not accomplished via osmosis; it requires costly effort. I provide incentives for effort by giving credit for participation in classroom discussions. The most important thing you can do in order to learn the material, and an easy way to earn participation credit, is to ask questions. Questions (and answers) are public goods, and as such are underprovided by the free market. Providing participation credit is intended to prevent this market failure. Please ask questions – if you are confused, I guarantee someone else is as well.
  - Skills/abilities learned: communication; team work; reflective and critical analysis
- Presentations [25%] – Each module of our class offers opportunities for students to present in small groups and to engage in debate on a topic of critical, real-world significance. These exercises require students to discover, define, and analyze issues and problems related to the development of our economy and financial system. You will be evaluated on your knowledge of the subject matter, your analysis of the issue (including any use of data and theories discussed in class), and your ability to persuasively and clearly communicate the results of your investigation. The goal of these exercises is to get students from diverse disciplines to collaborate on substantial problems, and to work creatively towards a solution.

- Skills/abilities learned: transdisciplinary collaboration and communication; public speaking; identifying and addressing problems
- Midterm exam [10%] – There will be an in-class exam on Thurs Oct 19 that will require students to use the concepts discussed in class and apply them to a new situation. This is not merely a test of your knowledge – rather, it is a test of your ability to use what you have learned to critically analyze and address a real-world problem.
  - Skills/abilities learned: analytical knowledge of political economy and finance
- Studio project [40%] – Approximately one quarter of our class meetings will be devoted to your policy project. The final draft will be due at the end of the semester. You will be graded on the completeness and creativity of your final submission.
  - Skills/abilities learned: data management; programming; transdisciplinary collaboration and communication; research methods and analysis

Policies:

*Accommodation* – Students with need of special accommodations due to a documented disability should provide the appropriate accommodation letter from Services for Students with Disabilities by Tue September 19.

*Behavior* – Very simply, your actions cannot negatively impact or interfere with the learning opportunities of other students. Please be courteous.

*Academic integrity* - The undergraduate Honor Code pledge that each member of the university community agrees to abide by states:

“As a Hokie, I will conduct myself with honor and integrity at all times. I will not lie, cheat, or steal, nor will I accept the actions of those who do.”

Students enrolled in this course are responsible for abiding by the Honor Code. A student who has doubts about how the Honor Code applies to any assignment is responsible for obtaining specific guidance from the course instructor before submitting the assignment for evaluation. Ignorance of the rules does not exclude any member of the University community from the requirements and expectations of the Honor Code. For additional information about the Honor Code, please visit: <https://www.honorsystem.vt.edu/>

Readings:

There is no required textbook for this class. Instead, readings for each module will consist of selections from books, academic articles, and news articles (with the odd video thrown in for good measure).

Depending on your background, however, you may wish to take a look at the following three books which provide historical context on the development of economic thought. The theories

they discuss provide the lens through which we will cast modern economic and financial developments.

Heilbroner, R. (1999) "[The Worldly Philosophers: The Lives, Times and Ideas of the Great Economic Thinkers](#)," 7<sup>th</sup> Ed.

Kocka, J. (2016) "[Capitalism: A Short History](#)"

Kurz, H. (2016) "[Economic Thought: A Brief History](#)"

### Key:

[B] Book

[A] Academic article

[V] Video

[N] News/popular press article

*Note:* specific readings will be assigned when appropriate. The below is subject to change based on class discussions

### Module 1: Money

- Theories: a liquid medium of exchange; the only payment that can satisfy tax liability
- Types: commodity, representative, fiat, commercial bank, digital currency
- Policy: central banks, (hyper)inflation
  - *Student presentations:* Cryptocurrencies

#### *Primary resources:*

[B] Graeber, D "[Debt: The First 5,000 Years](#)"; online [here](#) (Ch 1, 2, and 3)

[B] Goetzman "[Money Changes Everything: How Finance Made Civilization Possible](#)" (Introduction & Part I)

[A] Radford (1945) "[The Economic Organisation of a P.O.W. Camp](#)"

[A] Neiburg, F. (2016) "[A True Coin of Their Dreams: Imaginary Monies in Haiti](#)" (read the intro, Geographies of Monies and Calculation, and the conclusion)

[V] NOVA film "[Secrets of Making Money](#)"; the focus seems to be on anti-counterfeiting, but there is a section on the history of money

#### *Additional resources:*

[B] Ferguson, N "[The Ascent of Money: A Financial History of the World](#)" (Ch 1) (*Note:* you didn't hear it from me, but there is a video based on this book available on YouTube – the book is better, but the video is adequate)

[B] Davies, Glyn "[A History of Money: From Ancient Times to the Present Day](#)"; online [here](#)

[B] Sprang "[Stuff and Money in the Time of the French Revolution](#)"

[N] Irish Times 4/15/2015 "[Woman fired for being a prostitute by Dutch central bank](#)"

## Module 2: Finance & Financialization

- Historical view of the financial industry
- Modern finance (guest lecture by George Morgan)
  - *Student presentations*: Be a private wealth management analyst for a day!
    - Working in small groups, sell us on an investment – equity, debt, FX, etc.
- Financialization
  - Growth of the financial sector & financial services
  - Infiltration of non-finance companies into the financial industry
- Inequality - “the 1%”
  - Wealth and wages
  - Tax treatment of financial assets

### *Primary resources:*

- [B] Goetzman “[Money Changes Everything: How Finance Made Civilization Possible](#)” (Parts III and IV)
- [B] Ferguson, N “[The Ascent of Money: A Financial History of the World](#)” (Chs 2, 3, & 6)
- [A] Krippner, G (2005) “[The financialization of the American economy](#)”
- [N] Smith, N. “[How Finance Took Over the Economy](#),” Bloomberg View
- [V] “The Men who Built America”
- [V] Merchant of Venice – watch the [Welles film](#), and [Geanakopolos’s](#) discussion thereof

### *Additional resources:*

- [B] Wright and Sylla (2015) “[Genealogy of American Finance](#)”
- [B] Epstein, G (2006) “[Financialization and the World Economy](#)”
- [A] Cochrane, J. (2013) “[Finance: Function Matters, not Size](#)”
- [A] Geanakopolos – “[The Leverage Cycle](#)”
- [N] The Atlantic “[The Quiet Coup](#)” Simon Johnson
- [N] Thomas Philippon’s short [blog post](#) on the size of the financial industry over time; some good links
- [N] Mutual fund managers from poor families outperform their wealthy-descendent peers, from [Bloomberg](#)

## Module 3: Disrupting Banking

- Fintech
  - *Student presentations*: identify a start-up firm in fintech, describe it and its environment, explain its products/services and how they will affect the banking/financial industry.
- The distributed ledger (guest lecture by Manu Sporny)
- Financial inclusion

*Primary resources:*

- [B] Schumpeter “[Capitalism, Socialism and Democracy](#)”
- [B] Yunus, M “[Banker to the Poor: Micro-Lending and the Battle Against World Poverty](#)”
- [N] The Economist survey “[The disruption of banking](#)”

*Additional resources:*

- [A] Kirilenko & Lo (2013) “[Moore’s Law versus Murphy’s Law: Algorithmic Trading and Its Discontents](#)”
  - [N] The Clearing House & S. Markovich on “[Creative Destruction in Banking](#)”
  - [N] IBM “[5 disruptive technologies that are challenging the traditional banking model](#)”
- NOTE: There is a [Millennial Disruption Index](#), but it seems to be incomplete; let’s complete it!
- [N] [Bitcoin and Decentralized Networks are the Future, Says University Professor](#)

Module 4: Quantitative Easing and Financial Regulations (4 guest lectures by Kwok Ping (Byron) Tsang)

- How do central banks work?
- Implementation and goals of monetary policy
- Quantitative easing and other unconventional policy tools
- Financial regulations since the Crisis
- Class discussion 1: Is there a trade-off between central bank independence and limitation of power?
- Class discussion 2: Are financial regulations beneficial overall?

*Primary resources:*

- [A] Excerpts from The Squam Lake Report: Fixing the Financial System
- [A] Four Stories of Quantitative Easing by Brett W. Fawley and Christopher J. Neely
- [A] Reading About the Financial Crisis: A Twenty-One-Book Review by Andrew Lo
- [A] Challenges for Cost-Benefit Analysis of Financial Regulation by John Cochrane
- [N] Improving the Oversight of Large Financial Institutions, speech by Janet Yellen
- [N] Financial Sector Reform: How Far Are We?, speech by Stanley Fischer
- [N] Monetary Policy since the Onset of the Crisis, speech by Ben Bernanke

Module 5: Financial Booms & Busts

- The roaring 20’s
- The Great Depression
- The 2007/8 crisis (2 guest lectures by Giselle Datz)
- Speculative bubbles – tulips, housing (2008), identification, causes

- “Rational” bubbles?
- Bank runs – fractional reserve banking, role in depression
- US Savings & Loan crisis
- Scandals – Maddoff; LIBOR interest rates; Enron; Martha Stewart
  - *Student presentations*: From which country will the next financial crisis come?

*Primary resources:*

[B] Shiller, R (2015) “[Irrational Exuberance](#)” 3<sup>rd</sup> edition

[B] Sorkin “[Too Big to Fail: The Inside Story of How Wall Street And Washington Fought to Save the Financial System – and Themselves](#)”

[A] Goolsbee & Krueger (2015) “[A Retrospective Look at Rescuing and Restructuring General Motors and Chrysler](#)”

[V] Inside Job (2010)

[V] The Big Short (2015)

*Additional resources:*

[N] Bloomberg 4/27/16 “[Venezuela Doesn’t Have Enough Money to Pay for Its Money](#)”

[V] It’s a Wonderful Life