

Problem set 2: Seminars – ECON 4335 Economics of Banking
March 2 & 4 – 2010 (week 9)

1. Consider a profit-maximizing bank, as in 3.1.3 in F&R, taking all interest rates (r_D, r_L, r) as given. How will, the bank's positions (D, L, m) be affected by:
 - A higher capital requirement α
 - A higher rate of interest in the interbank market

2. How is the competitive structure of equilibrium interest rates in 3.1.4 in F&R affected by:
 - A higher capital requirement
 - Open market operations through a change in B (the stock of government bonds)
 - A more efficient banking industry, say by lowering the constant marginal costs $C_L = a$ and $C_D = b$ to ka and kb for some $k < 1$.

3. Without relying explicitly on formal models, you are asked to provide arguments in favor and against more competition in the banking industry.