

Seminar

“A Liquidity-Based Intermediary Leverage”

(in English)

Professor Chen Nan-Kuang

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Biography:

Professor Chen is currently a Professor of Economics at the National Taiwan University. He holds a Ph.D. in Economics from the University of Minnesota, USA. His research focuses on the areas of Credit, Asset Markets, and Financial Intermediation in Business Fluctuations, and Asset Prices and Monetary Policy. Prof. Chen has published in Journal of Monetary Economics, Economic Inquiry, Southern Economic Journal, Journal of Housing Economics, Regional Science and Urban Economics, Oxford Economic Papers, Pacific Economic Review, International Review of Economics and Finance, as well as many others.

Date: 14 June 2017 (Wednesday)

Time: 10:30am – 12:00nn

Venue: LBYG06, G/F, B. Y. Lam Building

Abstract:

This paper studies the determination of the leverage for market-based intermediaries. We construct a three-period model in which intermediaries borrow from wholesale financiers and face a liquidity shock at the interim period. We characterize properties of the equilibrium in determining the threshold for liquidity supply, intermediary's leverage, asset prices, and investment. We find that the intermediary's leverage depends on the expected return that can be pledged to creditors, expected outlay of extra liquidity supply, and expected liquidation value of assets. We then examine how the intermediary's leverage change in response to a rise in riskiness of liquidity shock or a collateral shock on the liquidated value of assets. Both financial shocks lower the intermediary's leverage, leading to a rise in haircut, deleveraging of intermediaries' balance sheets, and investment. The results are consistent with observed evidence particularly during the 2007-09 financial crisis.