

Written Exam at the Department of Economics summer 2024

Economics of Banking

Final Exam

28.5.2024

(3-hour written aids allowed/no aids allowed)

Answers only in English.

This exam question consists of 3 pages in total

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- Or if you otherwise violate the rules that apply to the exam

1. As a consequence of the climate problems, there is political consensus for support of green alternatives to ready-made food and similar products of animal origin. The producers of such innovative types of food face an initial barrier of consumer resistance. If they succeed to pass this barrier, they will have satisfactory level of income, but the chance is expected to vary considerably among the new producers.

The new firms have in general had an acceptable access to credits, but since the green transition is a matter of social concern, it is proposed that the government subsidizes bank credits to all new enterprises producing green alternatives. Give a theoretical assessment of whether this particular intervention in the credit market is the right way to achieve the overall goal and which side effects it may have.

After of few years, the consumers have become accustomed to green food which can now be marketed in the same way as traditional food. Also the technologies in both production and marketing have been refined so that the prospective income depends mainly on the competences and energy of the entrepreneur. What will be the implication of these changes for the assessment of government subsidies?

2. A bank wants to attract capital from investors who want to participate with rather large amounts of money in start-ups of enterprises in the field of AI, but who are waiting due in part to a general economic downturn and in part to uncertainty about the final legal conditions for commercial AI. The investors want their deposits to be accessible rather quickly so that they can react if the business conditions allow it, and they expect to get at least a small interest on their deposits. The bank also wants to obtain some positive profit from this engagement, so they must find a suitable placement of the deposits.

The bank proposes to use a standard deposit contract. Give a theory-based assessment of whether this is a reasonable solution for both parties and whether there are inherent risks that the deposits may be lost.

The Financial Inspection of the country decides that the bank is not allowed to carry out its proposal. Give a suggestion as to how the contracts could be reformulated so as to satisfy the demands of the Financial Inspection.

3. In a country with a banking sector consisting of predominantly middle-sized banks it is decided that liquidity problems in banks should be solved within the banking sector itself, typically by having one of the other banks taking over the bank in troubles. There has however been some opposition to this policy, based on the argument that in a period of financial unrest it will lead to a concentration of the

banking sector, something that will increase riskiness in the financial sector. Give a theoretical assessment of this argument.

In view of the political controversies, it is decided that banks should rely on themselves rather than being bought up by other banks or helped by a lender of last resort. On the other hand, defaults should be avoided since this would result in losses for the creditors of the bank even if the problems were only related to liquidity. How can this be achieved?