Index

1-year adjustable mortgage interest rate 141, 145, 146, 147, 151, 152, 182
   autocorrelation statistics 168, 169
   heteroskedasticity 170
   multicollinearity 171, 172
   regression results 175, 177, 182
   unit root tests 158, 159, 160, 162, 163, 164, 165, 167
2SLS techniques 124
10-year Treasury bond rate 101, 106, 121, 123, 128
15-year fixed mortgage rate 140, 141, 145, 146, 147, 151, 152
   autocorrelation statistics 168, 169
   GMM 179
   heteroskedasticity 170
   multicollinearity 171, 172
   regression results 173, 176
   root tests 158, 159, 160, 163, 164, 165
30-year fixed mortgage rate (MRTG) 137, 140, 141, 145, 146, 147, 151, 152
   autocorrelation 117, 118, 168, 169
   DFGLS unit root test 108, 110, 160, 165
   GMM 178
   heteroskedasticity 116, 170
   KPSS unit root test 114, 115, 159, 164
   multicollinearity 119, 120, 172
   Phillips-Perron test statistics 112, 113, 158, 163
   regression results 173, 175
AAA Corporate Bond Rate 91, 106, 120, 122, 126
ABS (asset-backed securities) 27, 28, 29
Acharya, V.V. 28
acquisitions 41, 45, 55
ADF (Augmented Dickey-Fuller) 148, 149
adjustable mortgage interest rate 145, 146, 147, 151, 152, 174–5, 177, 181–2
adjustable rate mortgages 6, 137, 139, 140, 141
Adrian, T. 144
aggregate demand 7, 8, 18, 19, 20, 25
   and interest rates 131, 144
   and monetary policy 22
AIG 32
Altunbas et al. 29–30, 32, 57
Anderson, R.G. 34–5
ANW (available net worth) 77, 80, 83
   see also net worth
asset markets 44
asset price channel 23–5
asset prices 18, 23–5, 32–3, 63–4, 78, 82, 142
   changes 77, 83, 84
determination 3
assets 4, 14, 26–7, 79, 157
   and Basel I 39, 40
   expansion 75, 81, 83
   and foreign official purchases 98
   foreign-owned in US 36, 37
   and GDP 61–2
   and margin requirements 45
   reshuffling 72
total 77, 84
autocorrelation 99, 117–18, 150, 168–9
BAA Corporate Bond Rate 91, 106, 121, 123, 127
balance sheet channel 21–2
balance sheet constraints 4–5, 17, 35, 44, 50, 57–60, 72–86
decreasing 60, 183
Central banks and financial markets

and derivative market 33
and securitization 28, 29
balance sheet expansion 4–5, 6, 8–9, 12, 54, 72, 77–8, 84–6, 183
and ANW 80
and asset price determination 3
and Basel I 40
and decreasing funding constraint 82
and haircuts and margin requirements 76
and loans 73, 75
and Regulation Q 38
and US financial markets 60–61
balance sheets 14, 18
and securitization 32
bank holding companies 42
banking capital and Basel I 39–40
Banking Holding Company Act, 1956 41
bank lending channel (bank’s balance sheet channel) 22–3
banks
commercial 28, 31, 38, 41, 63, 142
loans 22
and securitization 29–30
Barth et al. 41
Basel I 37, 39–40, 79, 80
Baum et al. 150
Bernanke, B. 15, 21, 38–9, 134, 139, 153
and the Great Moderation 3, 12, 184
and long-term interest rates 93
and Regulation Q 142
bonds 28, 41, 42, 53, 93, 157
prices 23–4
and SPVs 27
see also BAA Corporate Bond Rate
boom and bust 45
borrowings 76, 81
increase 80
short term 22
branching, interstate 55
Bureau of Economic Analysis 157
capital 45, 79, 80
core 39
for loans 75
surplus 59
capital adequacy ratios 40, 42, 58, 76, 80, 84
capital flows 35, 77, 97, 99, 101, 147–8
and interest rates 98, 149, 151, 152, 153, 183–4
capital inflows 106, 157
capital markets 32, 51, 60, 75, 77
and collateral 76
and depository institutions 48, 50
and securitization 30
capital mobility 35
capital requirements 39–40, 80, 81, 82, 84
cash financing 136, 137
cash flow 21, 22, 26
centralization 55–7, 183
Cetorelli et al. 56
Cohen, B.H. 78
collateral 21–2, 45, 76
commercial banks 28, 31, 38, 41, 63, 142
Commodity Future Trading Commission (CFTC) 43
Commodity Modernization Act (CMA) 43
competition 26, 55–7, 60, 183
consolidation 55
Consumer Price Index (CPI) 133
Consumer Price Inflation (CPI) 106, 157
core capital 39
corporate bond rate 91, 106, 120–21, 122–3, 126–7
correlations 94–5
cost of capital theory 20
counter-cyclical Fed policies 65, 184
Cowan, C. 26
credit aggregates 18
credit channel 20–23, 103, 131, 143–4
credit creation mechanism 60, 62
credit default swaps (CDS) 31–2, 40, 42, 43, 57, 58–9
credit derivative deals 57
credit expansion 5, 45, 59, 60, 82–3, 185
and endogeneity 4, 14, 64, 184
and financial assets 62–3
credit rating agencies 59
credit ratings 60
credit rationing 60, 65, 74
credit risk 40
credit standards, decreasing 65
Crotty, J. 57

D’Arista, J. 16, 17
debt 39, 40, 54
decoupling, dual 4, 5, 6, 8, 14, 60–64, 65, 153, 183, 185
de facto measures of financial integration 35
demand deposits 38, 79
deposit/depository institutions 47, 51, 52, 53, 54, 55, 58
and capital markets 50
and discount window operations 46, 48, 49
deposits 52, 83
and demand 79
expansion 82
increase 80, 81
and loans 51
long term 54
and reserves 75
deregulation 16, 26, 38, 41, 183
derivatives 30–33, 43, 52, 56, 58, 59, 106, 157
direct regulatory cushions 77
disintermediation in the financial system 30
Dokko et al. 133–4
Draghi, M. 2
dual decoupling 4, 5, 6, 8, 14, 60–64, 65, 153, 183, 185
Ducoudre, B. 93
Durbin-Wu-Haussman endogeneity test 99, 149
earnings, retained 77, 78, 83
endogeneity 98, 99, 124, 148, 149, 184
and credit expansion mechanism 60, 62, 64
and expansion of balance sheets 3, 4, 5, 8–9, 12, 14, 73, 78, 84, 86
of money supply 16–17
Epstein, G. vii, 66
equity 45, 77, 78, 79, 83, 84
Eurodollar borrowing 45
evolutionary-institutionalist economic school of thought’s methodology 6
excess reserves 79, 80, 81
low 82
exchange rate channel 23
expectation channel 59
expectations theory 93
exports 23

the Fed
and CDS 31
counter-cyclical policies 65
and dual decoupling 12, 13, 14, 183
and housing 142–54
and monetary policy 130, 131, 133, 134, 143
and overnight interest rates 18
regulatory framework 13, 37–50
and regulatory requirements 59
and securitization 32
see also Fed rate
Federal Deposit Insurance Corporation (FDIC) 42
Federal Housing Finance Agency 157
federally related mortgage pools 53
Federal Reserve Bank of Philadelphia 157
Fed rate 6, 14–15, 62–4, 142–4
and the housing boom 132, 135
and long-term interest rates 89–129, 134
and mortgage interest rates 6, 132, 144–52
and rate targets 48, 50
and short-term funds 22, 23
fee income 52
Feinman, J.N. 45
Feldstein, M. 14
financial assets 4, 14
and GDP 61–2
price 3
see also assets
financial crisis, 2008 130–54
financial derivatives 106, 157
see also derivatives
financial innovations 25–35, 39–40, 43, 55–6, 58, 82
central banks and financial markets


financial integration 13, 15, 26, 35–7, 82, 183
financialization 15, 35
financial prices and the Fed’s interest rate 63–4
financing, cash 136, 137
firm balance sheet channel 21–2
fixed mortgages 137, 139, 145, 151, 173, 175–6, 178–9
downward trend 140, 141
flexibility 54, 59, 74
and OTC contracts 30
and Regulation Q 39
and securitization 32, 41–2, 52
Flow of Funds Accounts 137
foreign capital flows 99, 149
and interest rates 151, 152, 153, 183–4
foreign funds 106, 132, 157
foreign official purchases 98, 149
FRB/US Dynamic Stochastic General Equilibrium models 133–4
Friedman, B.M. 1–2, 11, 15–16, 17, 58
Friedman, Milton 7
funding constraints 58, 82, 83
funding corporations 53, 54
funds
availability of 74, 82
foreign 106, 132, 157
increasing 58
GDP (gross domestic product)
and balance sheet growth 76
and financial assets 61–2
and gross capital flows 35
Geithner, T. 15, 51
General Theory (Keynes) 24
Gertler, M. 15, 21, 153
Glass-Steagall Act 41, 42, 55
GLBA (Gramm-Leach-Bliley Act) 41, 43
global financialization 15, 35
GMM (General Methods of Moments) 98–9, 124–5, 126–9, 148, 149, 150, 178–82
Gnos, C. 73
Goderis et al. 32
Goodfriend, M. 3, 12, 20
Government Sponsored Enterprises (GSE) 53

gradualism 63
Great Moderation 3, 12, 64, 184
Greenspan, A. 43, 92–3, 133, 134
gross capital flows 35
Group Ten 55

haircuts 60, 74–5, 76
Hansen J test 98, 149
hedging 59, 130
Henderson, D.R. 133
heteroskedasticity 99, 116, 170
Hicks, J. 6–7
Hirtle, B. 32
home mortgages 136–7, 138, 139
see also mortgage interest rates; mortgages
homoskedasticity 94, 99, 149
Honda 80
housing boom 5, 6, 131, 133–44, 151
Hummel, J.R. 133
Idier et al. 93
imports 23
income statement of financial institutions 84
inflation 23, 96, 106, 157, 171–2, 184
low 3, 26
innovations 13, 17, 57
financial 16, 25–35, 39–40, 43, 55–6, 58, 82, 183
technological 12
institutionalist-evolutionary school 6
institutional structure of US financial market 25–50
Instrumental Variable (IV) 98, 149, 150
insurance companies 53
integration, financial 13, 15, 26, 35–7, 82, 183
interest, decreasing importance 52
interest paying checking accounts 26
interest rate ceilings 55, 142
interest rate channel 6, 18–20, 103, 104, 131, 144
interest rate derivatives 30
interest rates 2, 4, 5, 7–8
and capital flows 98, 149, 151, 152, 153, 183–4
and the Fed rate 6, 14–15, 132
high 22
and the housing boom 131, 134, 135
Index

long-term 64
low 26
medium term 147
and Regulation Q 38
smoothing 63
see also overnight interest rates
The International Convergence of
Capital Measurements and
Capital Standards (Basel I) 39–40
see also Basel I
interstate banking and branching 41, 55
investment demand 19
issuers of asset-backed securities 53, 54
IV techniques 124, 125
Jorgenson, Dale W. 20
JP Morgan 57
Keynes, J.M. 24
King, M. 15–16
KPSS unit root test 98, 114–15, 148, 149, 159, 164
Kregel, J. 30, 52–3
leakage rate, low 82
legal capital adequacy ratio 80
leverage 31, 59, 63, 76, 84
Levine, R. 42, 43, 153
liabilities 77, 79, 81, 82
life insurance companies 55
liquidity 29, 31, 33
loan creation 73, 81
loan demand 76
loan-deposit nexus 50–54, 76
loans 22, 52, 80, 143–4
and CDS agreements 40
expansion 59–60, 75–6, 82, 83
illiquid long term 58
increase 81
mortgages 57
see also mortgages
and Regulation Q 38
loan to value ratio 60
long-term debt arrangements 54
long-term interest rates 5, 15, 20, 183–4
and the Fed rate 64, 89–129, 134
and mortgages 6, 133, 134, 144, 147
long-term loans, illiquid 58
low interest rates 5, 26, 133
low leakage rate 82
low margin requirements 60
macroeconomic modeling 184
macroeconomic variables 96
margin calls 45
margin loans 45
margin requirements 1, 44–5, 59, 74–5, 76, 80
low 60
market interest rates 14–15, 19, 20, 25, 130, 143
effect on currency 23
and ceilings 38, 142
decoupling 5
see also interest rates
market prices 8, 14, 33, 64, 153
Marx, K. 57
medium term interest rates 147
mergers 55
Miles, W. 54
Minsky, Hyman 16
Mises, von L. 132–3
Mishkin, F.S. 11, 65, 133
monetarism 7
Monetary Control Act (MCA) 38, 45–6, 55, 142
monetary policy 22, 96
and the Fed 130, 131, 133, 134, 143
and inflation 23
influence 26
and investment decisions 24
money base and ratio with financial
assets 62
Money Market Deposit Accounts
(MMDA) 33, 55
money market mutual funds 54
money markets 76, 77, 83
borrowings 22, 85
money multiplier analysis 86
money supply, endogeneity 16–17
mortgage interest rates 106, 122, 124, 129, 157, 173–82, 183
and the Fed rate 6, 131, 132, 133, 134, 144–52
mortgage pools, federally related 53
mortgages 27–8, 57, 136–41
and Regulation Q 38–9
MRTG see 30-year fixed mortgage rate
(MRTG)
multicollinearity 100, 119–20, 148, 150, 171–2
Mundel-Fleming model 97, 147–8
mutual funds 54

Nadauld, T.D. 42
national average adjustable mortgage rate 145, 146, 147, 151, 174, 177, 181
national average mortgage rate 145, 146, 147, 151, 174, 176, 180
NBER (National Bureau of Economics) 93, 145
negative credit multiplier 45
net worth 76, 80, 81, 82, 84
changes 77–9, 83, 85
New Consensus 3, 6, 7, 8, 20, 104
new equity issuance 77, 78
Newey-West procedure 99, 150
Niggle, C.J. 16–17
non-deposit/non-depository institutions 53, 54, 60, 76
non-interest income 52
non-OECD banks, debt 40
null hypothesis 98, 148
objective balance sheet constraints 58, 74, 75, 77, 84–5
objective funding constraint 74
OCC (Office of the Comptroller of the Currency) 30, 32, 42
OLS (Ordinary Least Squares) 94–5, 97–8, 99, 101, 120–24, 148, 149–50
open market operations 1, 18–19, 44, 48, 50, 142, 143
options 30, 31
“originator and seller” banking model 52–3
orthogonality condition 98, 149
OTC (over-the-counter) contracts 30
overnight interest rates 2, 3, 4, 18, 19, 20
decoupling with market prices 14, 64
and long-term interest rates 5, 89–129

Paden, D.W. 7
Papademos, L. 15
pen-market operations 18
Personal Consumption Expenditure (PCE) index 133
Phillips-Perron test statistics 112–13, 148–9, 158, 163
Poole, et al. 50
pools of funds, increasing 58, 77
positive credit multiplier 45
post-Keynesian models 20, 104
post-Keynesian monetary theory 6, 8
post-Keynesians 3, 73
Prasad et al. 35
prices 63–4
bonds and stocks 23–4
changes 84
competition 55
and financial assets 3
Primary Mortgage Market Survey 157
procyclicality in financial markets 65, 184
profits 25, 26, 57, 59, 72, 84
quantity target 142
Rasche, R.H. 34–5
ratings, high 59
recessions 94, 145
redundancy test 98, 149
Regulation Q 26, 33, 38–9, 55, 59, 142
regulatory constraints 74, 82
replacement cost 24
required capital 80
required credit ratings 60
required reserve ratios 1, 33, 45–6, 59, 82, 142, 143
required reserves 16, 33, 58, 59, 75, 79, 80, 81
reserves 64, 76, 79, 80, 81, 82
reshuffling assets 72
retained earnings 77, 78, 83
Riegle-Neal Interstate Banking and Branching Act 41, 55
risk 40, 130
risk premium 97, 147, 157
risk weighted assets 58, 79–80, 81
rolling regression coefficients 101–3
Rudebusch et al. 93
Sachs, Jeffrey 130–31
Schnabl, P. 28
Index

Schumpeterian theory of industrial innovation 57
Securities Exchange Act, 1934 44
securitization 26, 28, 29–30, 32, 41–2, 52, 58, 59
Security Exchange Commission (SEC) 42, 43
self-imposed cushions 77, 82
Sellon, G.H. 14–15, 38
Sherlund, S.M. 42
Shiller, R.J. 44, 135
Shin, H.S. 78, 144
short-term debt 40
short-term funds 22
short-term interest rates 18, 20, 91, 93, 133, 134
and the Fed 6, 15, 151
short-term market rates 22, 144
short-term mortgage rates 144, 145
speculation 32–3
SPVs (Special Purpose Vehicles) 27, 30, 40
stock prices 23–4, 45
subjective balance sheet constraints 58, 59, 74–5, 77, 84–5
subsidiaries of banks 42
super senior 32
supply side developments in financial markets 65, 185
surplus capital 59
Survey of Professional Forecasters (SPF) 106, 157
swaps 30, 31–2
sweep accounts 26, 33–5, 58
sweep programs 46
Taylor, J.B. 23, 130, 133, 134
technological changes 26
Thornton, D. 50, 93
Tier 1 capital 39
Tier 2 capital 39
Tietmeyer, H. 15
time deposits 38
time series data 98, 148
Tobin, J. 24, 35
transmission mechanism 18–25, 51, 131, 185
treasury bond rate 121, 123, 128
trusts 27, 54
uncertainty 23
underwriting 55
US financial system, institutional structure 25–50
Vector Auto Regressive (VAR) models 133–4, 150
volatility 3, 26, 97, 184
Volcker, Paul 3
Warnock, F.E. 147, 148
Warnock, V.C. 147, 148
weak identification tests 98, 149
wealth effect channel 24–5
Wolf, Martin 133
Woodford, M. 2, 8, 15
Zywicki, T. 133