Contents

Acknowledgments List of Figures List of Tables	
1. Nature of Financial Risk	1
2. Value-at-Risk and Capital	16
2.1 Portfolio Choice under VaR Constraint	19
2.2 Upward-Sloping Demand Reactions	23
2.3 Notes on Further Reading	26
3. Boom and Bust Driven by Value-at-Risk	28
3.1 General Equilibrium with Value-at-Risk	29
3.2 Pricing of Risk and Credit Supply	35
3.3 Long-Short Strategy Hedge Fund	41
3.4 Hedge Fund with VaR Constraint	47
3.5 Endogenous Risk	51
3.6 Notes on Further Reading	54
4. Dynamic Hedging	56
4.1 Portfolio Insurance	56
4.2 Delta Hedging	58
4.3 Stock Market Crash of 1987	71
5. Asset-Liability Management	75
5.1 Review of Basic Concepts	77
5.2 Example of a Pension Fund	84
5.3 Example of Ivy College	88
5.4 Prices as Signals for Investment	91
6. Financial System	96
6.1 Accounting Framework	102
6.2 Realized Allocations	104
6.3 Market Value of Debt	109
7. Lending Booms	116
7.1 Credit Risk Model	116
7.2 Value-at-Risk and Lending	118
7.3 Credit Boom	122
7.4 Global Imbalances	125

vii	i Contents	
	7.5 Foreign Holding of US Debt Securities	127
	7.6 Related Literature	131
8.	Case of Northern Rock	132
	8.1 Background	135
	8.2 Securitization Process	137
	8.3 The Run on Northern Rock	140
	8.4 Reassessing the Run on Northern Rock	143
	8.5 Implications for Financial Regulation	149
9.	Securitization and the Financial System	152
	9.1 Accounting Framework Revisited	157
	9.2 Boom Scenario	159
	9.3 Bust Scenario	161
	9.4 Prescriptions	161
	9.5 Size of Banking Sector	167
10). A Fresh Start	171
Re	eferences	176
In	Index	