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Asset Price Risk, Banks and Markets

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## Highlights

- By introducing asset price risk, this paper shows that Diamond-Dybvig banks are redundant even if financial markets exist.
- Asset price risk makes the incentive-compatibility constraint relaxed such that the deposit contract does not have to mimic the market allocation.
- Banks can choose the portfolio such that no asset liquidation is involved. For a consumer, making deposits provides smoother contingent consumptions than holding the assets directly.

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