

Capital Markets & Investments

Session 9: Fixed Income (6) – Not-so-Fixed Income

Spring 2026
Professor Simon Oh

Midterm Exam Logistics

- March 8th Sunday 12am – March 13th Friday 11:59pm
- 1.5 hours (once you start, need to finish within this time)
- Practice midterms uploaded in Files/Practice Midterms
- Materials up to Fixed Income 6
- AI and Proctoring Policy
 - You are not allowed to use AI tools during the exam.
 - Monitored using Proctorio – one monitor, laptop (no iPad)
 - Class materials (e.g. lectures, assignments) are permitted

Interest Rate Risk and Duration Galore

- **Interest rate risk matters for understanding:**
 - Banks
 - Pension Funds
 - Insurance Companies
 - Student Loans
 - ...
 - **Housing Contracts**

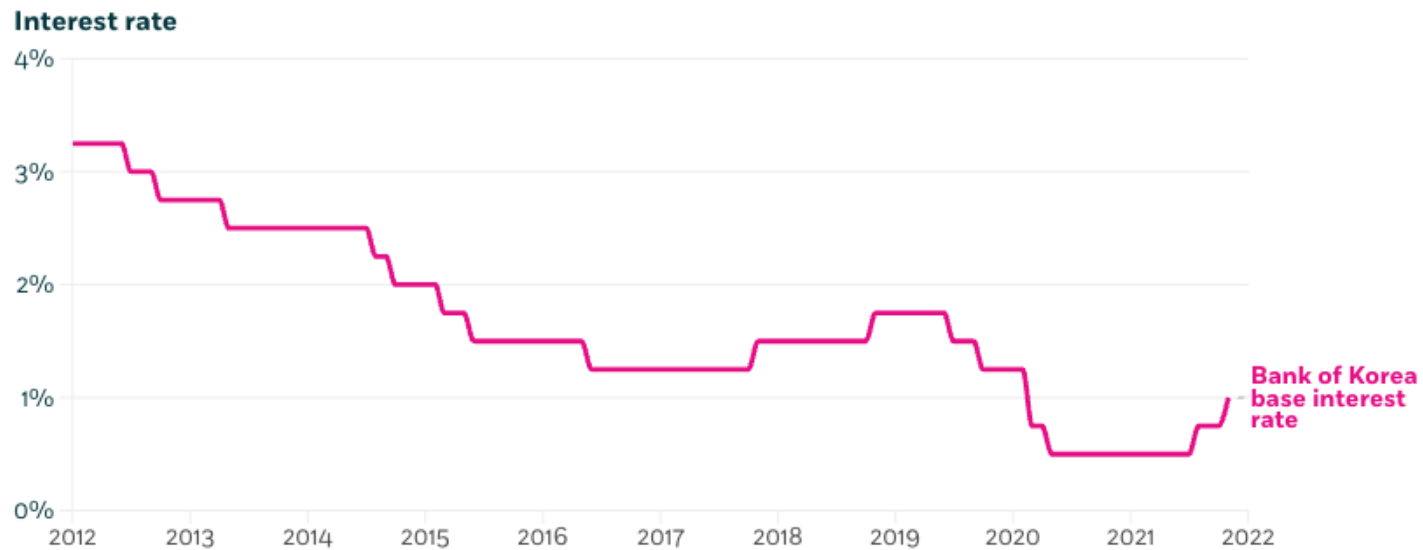
Chonseil System

- Korea's unique deposit-based rental system
 - In 2020, 70% of Seoul leases were Jeonse
- How it works:
 - Tenant pays 50-80% of property value upfront
 - No monthly rent, deposit returned in full after 2 years
 - Landlords invest the deposit
 - Deposit = interest-free loan
 - When lease ends, deposit is returned

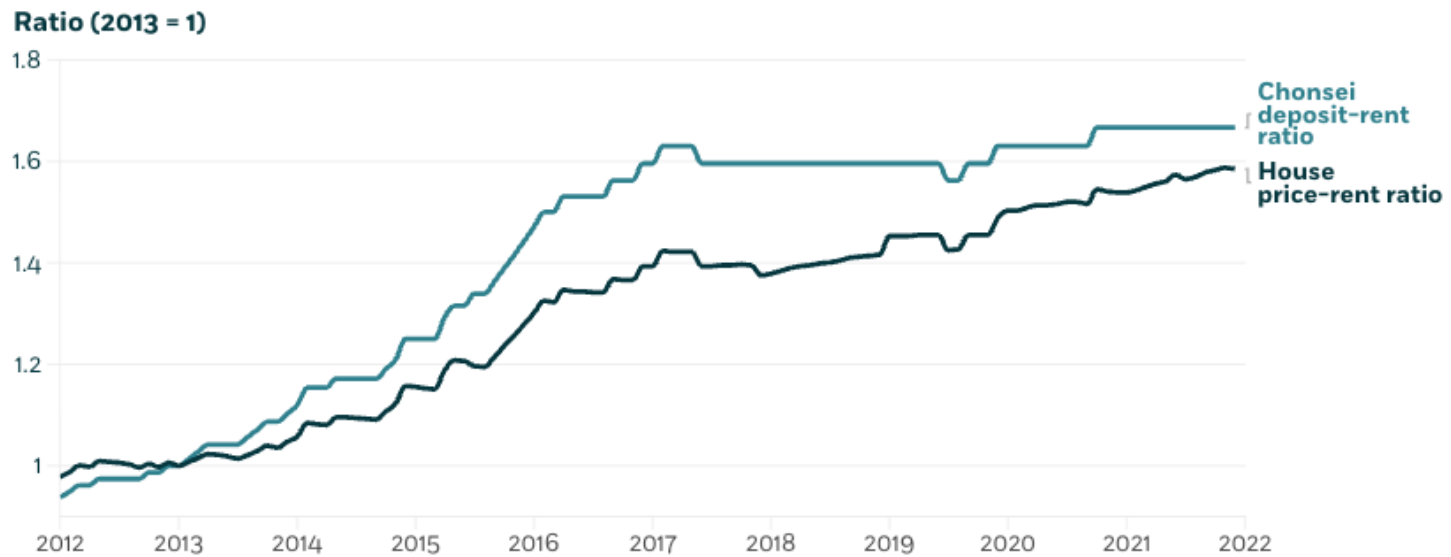
Gap Investments

- Landlords purchased many properties using “gap investments,” funding each purchase with deposits from tenants
 - $\text{Gap} = \text{House Price} - \text{Chonseil Amount}$
 - Essentially a leveraged bet on house prices
- What happens when the tenants want their money back?
 - Find a new tenant, collect their deposits, and use that cash to repay the departing tenant
 - Important: new deposit should be at least as large as the old deposit!

Chonsei and Interest Rates



Chonseil and Interest Rates



Human Cost: Chonsei Fraud

- When interest rates rise and house prices fell, the “villa kings” began going bankrupt or dying.
 - July 2021: landlord with 240 housing units turned up dead
 - October 2022: landlord with 1,139 housing units suddenly died
 - And many more
- Believed to be co-conspirators in a criminal enterprise
 - Koreans in their 20s and 30s died by suicide as they had taken out bank loans to cover their deposits

Takeaways

- Initially a system designed for high rates (landlord parks the deposit in a bank and earns cash)
 - When rates fell, tenants borrow to fund deposits and landlords invest in high-yield assets (real estate), which made them vulnerable when rates came back up
- Dangers of unregulated private financing (vs. banks)
- Using new deposits to repay old ones = Ponzi Structure