

Chapter 8 – Savings, Investment and the Financial Sector

Motivation – $Y/L = Af(K/L, H/L, N/L)$

- Increases in K/L result in increased _____ and increased _____.
- _____ in the economy is what results in greater capital.
- Businesses get their money for investment spending from _____.
- Financial Sector plays an important role in _____ savings to Investments spending.

Financial Institutions

- The **financial system**: the group of institutions that helps match the _____ of one person with the _____ of another.
- **Two types of financial institutions**
- **1. Financial markets**: institutions through which savers can _____ provide funds to borrowers. Examples:
 - The Bond Market.
A **bond** is a certificate of _____.
 - The Stock Market.
A **stock** is a claim to _____ in a firm.

Bonds



Bonds normally consist of:

1. Face Value - Value that lender receives at maturity
2. Coupon rate - fixed or variable rate paid to lender:

Rate is determined by:

1. _____ - _____ of a company going bankrupt. Higher risk, _____ return.
2. _____ of Bond: _____ term bonds usually pay _____ rates due to _____ chance of default.
3. _____ - People have to pay taxes on most interest income. However bonds issued by _____ are tax exempt and thus are likely to pay _____ rates.

Advantages

Disadvantages

Rank the following bonds from lowest to highest return.

Joey Startup, The State of New York, McDonalds,..

Stocks



Savers make money on stocks with

1. Dividends

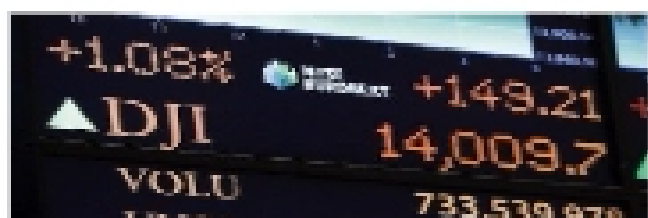
2. Capital Gains

Price of stock determined by:

Efficient Market hypotheses predicts that the value of the stock should always be a true reflection of the value of the _____.

This is true during _____ but not during _____.

Performance of stocks measured



Advantages

Disadvantages