↳ Financial System:

→ Consists of institutions which help to match one person's savings with another person's investment.

→ key ingredients of long-run economic growth: savings & investment

→ Moves the economy's scarce resources from savers to borrowers.

savers
- spend less than what they earn
- ~~invest~~ supply their money to financial institutions expecting to get back the money at per rate of interest from them.

borrowers.
- spend more than they earn
- borrow money from financial institutions expecting that they should repay their loans.

→ Consists of various financial institutions to co-ordinate savers & borrowers.

financial institutions
- **Financial markets** → Financial institutions in which a person who wants to save can directly save by supplying ~~money~~ funds to those who want to borrow.
  - Bond market
  - Stock (Share) Market
- **Financial intermediaries** ← banks, mutual funds.

→ mutual funds → diversification → distributing wealth among many assets.

Perpetuity → A bond that never expires (In some British firms)
- ↳ never repays the principal
- ↳ A bond with no maturity date
- ↳ interest paid forever to the firm.

→ Long-term bonds are riskier as holders of long-term bonds need to wait longer for getting their principal amount back. So, long-term bonds pay ↑er rates of interests than short-term bonds.

→ Credit risk of bonds → The probability that the borrower of the bond fails to pay some of the interest/principal.

→ Failure to pay → default..

Bond owner

↓

pays some of this interest as income tax. (if bond is NOT issued by state/local Govts. → NOT MUNICIPAL BOND)

$\boxed{\text{Bond}}$

Bond borrower

↓

pays interest to bond owner (till maturity date)

• Stock Market (Shares)

↳ ownership in a firm ⇒ claim to a portion of the firm's profits.

↳ A way to raise funds → ~~xxx~~ sell stock in the company.

↳ Eg: 1000 shares in a firm ⇒ Each share can claim = $\frac{1}{1000}$ of the firm's profit.

↳ firm's stock → ↑ demand ⇒ ↑ profit of firm ⇒ price of each stock ↑ses. Firm → ↓ profit ⇒ price of each stock ↓ses.

Bond vs Shares (stock)

Bonds	Shares (Stock)
• Bond lender sells a bond.	• A firm owner sells stock to raise funds.
• Less risky as borrower pays bond owner interest regularly.	• Share holders get dividends of profit, depending on profit.
• Bond lenders get a fixed interest from borrowers.	• Share holders get dividends of profit which is not fixed.
• Maturity date	• No maturity date
• Tax deductable	• Shares are given on dividends of already tax deducted ~~interest~~ profit.