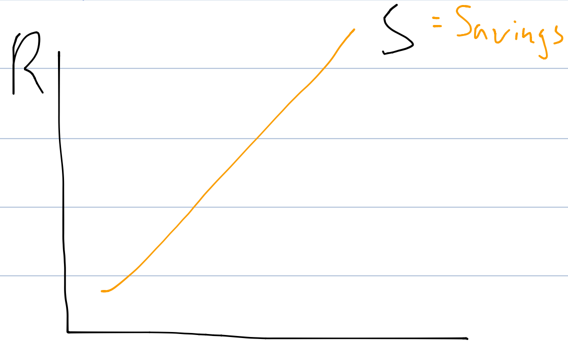
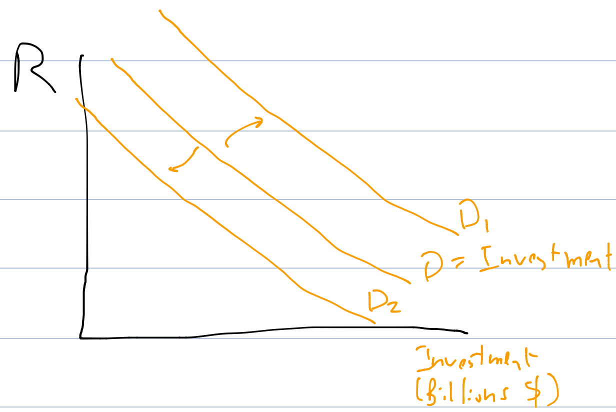
Supply



4 factors

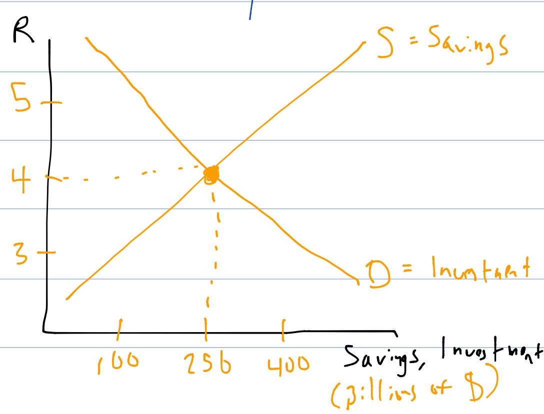
Demand = Investment



3 factors

1. R (-)
2. Capital Productivity (+)
3. Investor Confidence (+

Loanable Funds Equilibrium

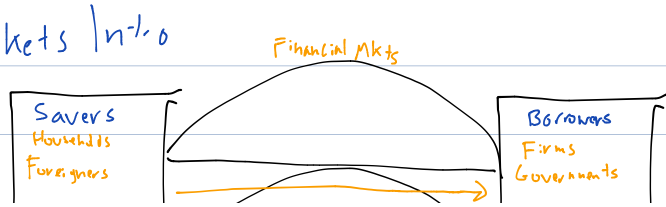


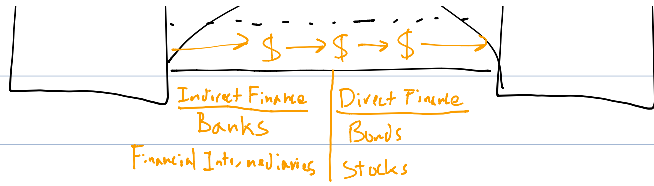
Savings = Investment

S = I

Test 1

Financial Markets Intro





Bonds

What are they?

IOUs or loan contracts

Three key Details

1. Borrower
2. Date of maturity
3. Value at maturity = Face Value = P_m
   par value

Two Bond Price Principles

1. Dollar price determines R

*R is actually:

- rate of return on initial payout
- growth rate of initial payout

$$R = \frac{(P_m - P_0)}{P_0} = \frac{10{,}000 - 8{,}500}{8{,}500}$$

$= 0.1765$

$= 17.65\%$

Ex: Face value = $1000

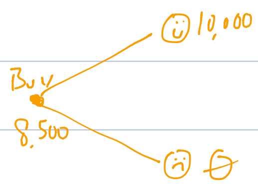
Maturity = 1 year away

$ Price	R
$10000	0%
9,000	11.1%
8,000	25%

2. Dollar Price (P_0) and R move opposite each other

Default Risk

Key Question: Will borrower default?



↑ default risk → ↓ dollar price, ↑ interest rate

Ratings Agencies

- Moody's
- Standard & Poor's

Rating indicates default risk

→ Determines R

→ Crucial for firm