**Financial Institutions** 

What are financial institutions Any institution through which savers can directly provide to bor-

rowers / facilitates interactions between saver and borrowers.

**Financial System** Institutions in the economy that help match the saving of one person with the

investment of another.

Financial markets

• Financial Intermediaries / Banks

**Saver** Someone who gives their money to financial institutions for safe keeping. Savers spends less

than what they save.

Nominal Interest Rate Nominal Interest Rate = Real Interest Rate + Inflation Rate

**Financial Intermediation** The process of savers depositing money in banks, which then lend the

money to borrowers.

**Investment** Investment is the purchase of new capital goods.

**National Savings** National Savings = Public Savings + Private Savings

**Public Savings** Savings made by the government and public institutions. This saving is made when

the government's revenue (Tax) exceeds its spending (G). i.e.

Public Savings = T - G

Where T is the tax revenue and G is the government spending.

Balanced Budget T = G

Budget Surplus T > G

 ${\bf Budget\ Deficit} \quad T < G$ 

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**Financing of Budget Deficit** In the situation where the government spending exceeds its revenue, the government can finance the deficit by:

- Borrowing:
  - Domestic:
    - \* From the public
  - External:
    - \* From foreign countries
- Aid and Grants
- Printing Money

**Private Savings** Saving by individuals and firms. This saving is made when the income of individuals and firms exceeds their consumption.

 ${\sf Private \ Savings} = Y - C$ 

Where  $\boldsymbol{Y}$  is the national income and  $\boldsymbol{C}$  is the consumption.