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## Financial Institutions

**What are financial institutions** Any institution through which savers can directly provide to borrowers / 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**  $\text{Nominal Interest Rate} = \text{Real Interest Rate} + \text{Inflation Rate}$

**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**  $\text{National Savings} = \text{Public Savings} + \text{Private Savings}$

**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.

$$\text{Public Savings} = T - G$$

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

**Balanced Budget**  $T = G$

**Budget Surplus**  $T > G$

**Budget Deficit**  $T < G$

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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.

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

Where  $Y$  is the national income and  $C$  is the consumption.