

Financial Markets And Their Purpose

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Financial markets can be defined as institutions that allow an individual to save their assets by directly supplying financing to a business or person who needs to borrow funds. Mankiw (2015) affirms that stock markets and bond markets are the most significant financial markets in the economy.

Bond Market

Bond markets are an eminent type of financial market through which members are facilitated with the issuance and trading opportunities in the field of bonds as well as debt securities. Phenomenally, bonds are specific certificates that assert the indebtedness and highlight the commitments of the borrower to the owner of the subject bond certificate; therefore, the bond becomes an IOU (Investor-owned utility). (Mankiw, 2015) A bond market primarily consists of government as well as corporate-debt securities and assists in the process of transmission and allocation of assets from issuers or establishments to investors. Such financing facilities, in turn, fulfill the demands of assets for ongoing business operations, business development and expansion, and governmental plans.

Stock Market

The stock market is also known as the equity market; through the stock market, public limited corporations and businesses issue and trade their common and preferred shares. Such issuance and trade take place either through exchanges or counter markets. Shares are the instruments that represent ownership of the owner in a corporation, and therefore, the shareholder establishes a claim to the net profits of a corporation. The stock market plays a most significant role in the development of the free-market economy as it provides companies with admittance to assets through the exchange of partial proprietorship to the shareholder.

Financial Intermediaries And Their Function In The Economy

Financial intermediaries are widely known as the basic financial institutions that implicitly offer financings and business funds to different lenders. Such institutions serve as a third party between the contractual procedures of investors and borrowers; therefore, they are called intermediaries. Mutual funds and banks are the two most crucial institutions in this regard; however, no one can deny the imperativeness of insurance companies and pension funds as well. Financial institutions are vital

to an economy as they connect the different economic agents with excessive funds and look forward to lending to those with a lack of financing and seeking borrowings. Through this systematic process, indirect finances carry out the requirements of borrowers and lenders by offering beneficial saving and investing prospects.

Federal Government Budget Deficit And The National Debt And Effect Of Budget Deficit On The Economy

Budget deficits take place when spending surpluses are the revenues received for a financial year. Such a phenomenon is widely known as deficit spending. On the other hand, the national deficit can be defined as the accumulated deficit for each year. The effect of a budget deficit on a country's economic prosperity is theoretically explicated by employing the impact of the deficit on the circulation of money into a particular economy. Palpably, the more that government's expenses surpass the income, the more money will flow throughout the economy, which in turn paves the way for augmented employment and increased overall productivity. (McCandles, 1991)

Consumers And Risk-Aversion

According to a study, consumers who do not have a tendency to cope with uncertainties are known as risk-averse. Such consumers do not have tolerance for risk because they want to evade the possible perilous outcomes. Take the instance of a situation in which a consumer could spend 10 dollars for a ticket lottery that features a probability of winning 1000 dollars. However, if the consumer is extra cautious and would rather not let go of his 10 dollars, considering the possibility of not winning the lottery. Risk-averse consumers can manage the hazards with the help of specific strategies, which include the purchase of different insurances, as they offer peace of mind to the consumers and assure indemnity in case of any predetermined harm. Another approach that is used in this regard is the scaffolding of greater risk in multiple, relatively smaller, and unconnected risks. The subject technique asserts the need not to put all the eggs in one basket. Another method is diversification, which could be attained through buying stocks and instruments of different corporations instead of investing all the assets in a single entity or project.

A Dollar Received Today Is Worth More Than A Dollar Received Tomorrow

The implication of the articulation that states, "A dollar received today is worth more than a dollar received tomorrow," suggests that interest earned throughout one day is worth more than a dollar

received tomorrow. Consequently, the interest makes one dollar more valuable in the present.

Present Value And The Future Value Of Money And Significance Of These Concepts To Economics

The future value of money is implied to measure the worth of one or more cash flows at the end of a predetermined financial period. On the other hand, the present value of money estimates the underlying worth of one or more than one cash flow that is subject to be received in the future will be worth at present; this measurement is denoted as $t=0$. These concepts carry considerable importance in economics because time is money in literary terms. Affirmatively, the monetary value one has today will not be the same in the near or far future. Determining the time value of money through calculating the future and the present value of money can give a distinct comparison among the values of different investments, which yield returns at different times.

Deposited \$1,000 In An Account Paying 6% Interest Compounded Annually, How Long Would It Take To Double?

In the above-mentioned case, it would take about seventeen years to have doubled the balance. The calculation is given below where P stands for Principal, T= time, A= new balance, and r= determines the interest rate.

Summary Of Important Points

- Financial institutions provide an opportunity to develop a direct supply of funds between lenders and borrowers.
- Bond markets and stock markets are the most prominent and important financial markets.
- **Financial intermediaries** are third parties who establish indirect trading and issuance of funds between lenders and borrowers.
- Banks and mutual funds are important financial intermediaries in an economic system.
- Government debts are also called national debts.
- Several consumers are risk-averse because they do not like the possible perils and risks involved in an action.
- Through the concept of time value of money a dollar today worth more than a dollar yesterday because of investment implications and interests.
- The present value (PV) of a future sum of money is an amount of money in the present that would be required through the prevailing rate of interest to create a provided future amount.

- The future value (FV) of a present sum of money can be defined as the amount in the future that a sum of money at present will produce through prevailing interest rates.

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