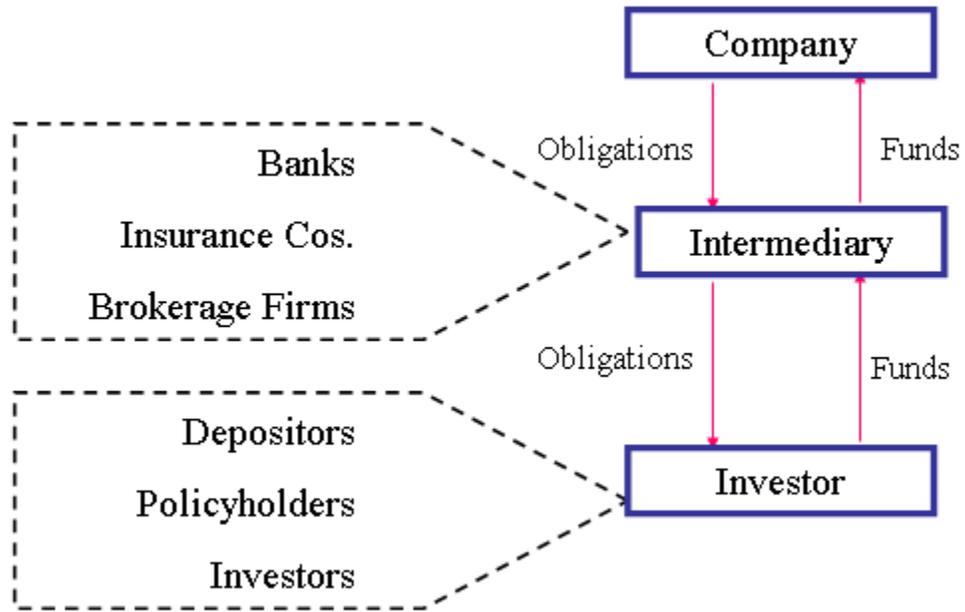


Chapter 1

What is Finance?



Types of Businesses

	Sole Proprietorship	Partnership	Corporation
Is it easy to start?	Yes	Generally	Not Generally
Access to capital?	Limited	Limited	Easy
What is the life of the business?	Limited	Limited	Unlimited
Who owns the business?	The Manager	Partners	Shareholders
Are managers and owners separate?	No	No	Usually
What is the owner's liability?	Unlimited	Unlimited (exceptions)	Limited
Are owners & the business taxed separately?	No	No	Yes

Goal of Corporation

Agency Costs

Definition - Agency costs arise when one party (principal) pays another (agent) to represent them. The conflicts of interest which arise are an agency problem and the subsequent costs to reduce this divergence of agent action from the best interest of the principal.

Stock Markets - Important as a source of cash flows to firm

Types of Markets

Primary - Firm sells stock directly to buyers

Cash from sale goes to firm

Actual sale is not generally directly from the company to the individual, but rather through an underwriter of investment banker who buys shares from the company and sells them to the public on a given day

Secondary - Stockholder sells ownership to another individual

Firm receives no cash

Important since secondary markets allow transfer of ownership, individuals are willing to buy stock

Dealer vs. Auction

Dealer market - NASDAQ

Dealer buys and sells stock, individuals buy stock directly from a dealer

Auction market - no dealer involved - individuals buy and sell from each other - sometimes (NYSE) involve a market maker who is responsible for maintaining an orderly market

Bond Markets

Primary and Secondary

Primary - works through underwriters much the same as stocks, although there are more direct sales to buyers

Secondary - Many bonds are listed on an exchange, however little trading takes place there. On a given day, 2/3 of the bonds on the NYSE do not trade and the average trade is 15 bonds. Most of the secondary market is OTC since most bondholders are institutions such as insurance companies, mutual funds and banks.