Name:

Reading Guide – Chapter 7 – Financial Markets

Due 10/14

25 points

Some Terms you may want to look up on <http://www.investopedia.com/>

**capital Return Real estate Stocks Bonds mutual fund index**

**fund 401(k) Credit Default Swap S&P 500 Dow Jones**

All financial instruments do the these 4 things: 1) Raising Capital 2) Storing, Protecting, and Making Profitable Use of Excess Capital 3) Insuring Against Risk 4) Speculation – Make sure that you understand each of these.

1. What does it mean to “raise capital”? Why is this important within the economy? (150-151)
2. What is “excess capital”? What is the role of financial instruments in putting excess capital to use?

How does this work? (151-152)

1. What is risk? What role does insurance play in negotiating risk? (152-153)
2. What does it mean to “speculate”? (157)
3. Try to explain how credit default swaps contributed to the financial crisis. This is really difficult but try to make a good faith effort. (157-158)
4. How can the government get involved in the financial markets? (159)
5. How does the “efficient markets theory” play a role in how the financial markets work? (163)
6. How is investing (buying stocks, etc.) like a line at the grocery store? (163-164)
7. What other factors in how people invest challenge the efficient markets theory? In other words, why doesn’t the efficient markets theory explain fully how market work? (165-166)
8. Explain these pieces of investing advice from the author:

Save, Invest, Repeat (168-169)

Take risk, earn reward (169-170)

Diversify (171-172)

Invest for the long run (172-173)