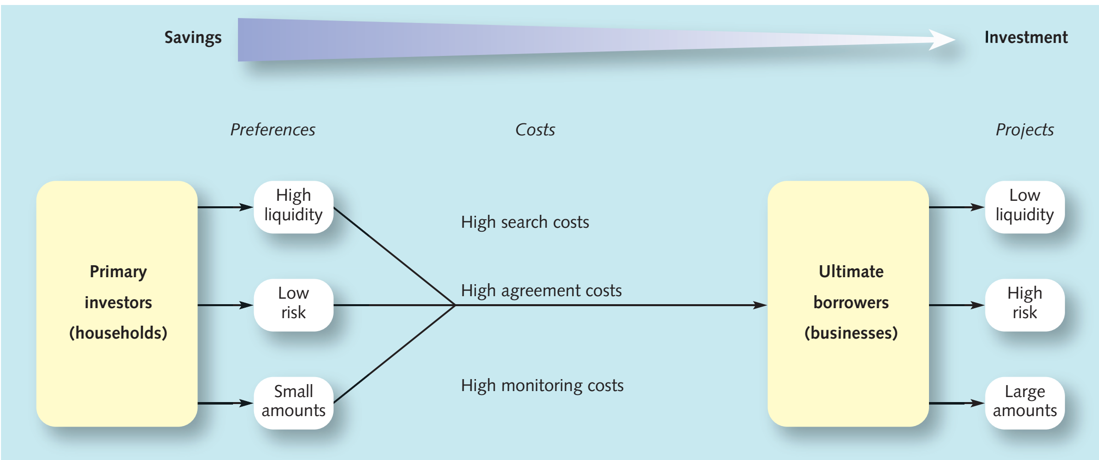
3.2.Conflict of preferences

- **Conflict of preference** ➔ between primary investor wanting low-cost liquidity and certainty and the ultimate borrowers wanting long-term risk-bearing capital.
  - **Search costs** ➔
  - **Agreement costs** ➔
  - **Monitoring costs** ➔

3.3. The introduction of financial intermediaries

- Alleviation of the under-investment problem with the introduction of FI & Fm
- Financial intermediaries aim to facilitate the flow of funds:
  - Primary investors ➟ ➟ ➟ Ultimate borrowers
  - Low-cost.
  - by solving the conflict of preferences
- 2 types of financial intermediations:
  - **Agency / brokerage type** operation ➔ rigs together menders and firms.
  - **Asset transforming type** of intermediation ➔ conflict of preferences solved by the creation of intermediate securities
    - IST have the risk, liquidity, volume characteristics which investors prefer.

Offers securities for sale
↓*[funds]*
Financial Intermediaries
↓*[funds]*
Purchase primary securities issued by Firms



3.4. Brokers

- Go-between = someone who matches up a provider of finance with the user of funds ➔ reducing the search cost for both parties.

7. Primary and secondary markets

- **Primary Market** ➔ financial instruments issued for the first time and sold directly to investors (the primary market) by FI such as: Investment banks ➔ helps to decide the inital price and oversee the sale to the public.
  - **NIM = New Issue Market** ➔ company sells its shares on a regulated exchange for the first time.
  - **IPO = Initial Public Offering**
  - **Flotation** ➔ shares are sold.
- **Secondary trading** ➔ the shareholder, bond holder, etc. to liquidate their shares (exchange them for cash) quickly, taking a profit (or loss), while the company's holdings of assets are not diminished because it is not forced to pay the security owners for their shares or bonds. Secondary markets include the stock markets of the world.
- Publicly traded ➔ shares are sold on the market. ≠ Privately held companies ➔ the IPOs did not take place.

8. Exchange-traded and OTC markets

- **Exchange trading** takes on the myriad regulated share markets and other security exchanges around the world.
- Published prices ➔ Stock exchanges publish accurate share prices for listed companies and make them available for wide dissemination.
- Exchanges have to fulfill statutory requirements ➔ protect and assure investors.
- Regulated exchanges are
  - bonds
  - derivatives
  - commodities
  - currencies
  - other securities
- Exchanges are funded by:
  - Commission on trades
  - Admission fees
  - Annual charges for listings
  - Selling their information to interested parties
- **OTC** = Over-the-Counter Market = Off-exchange market ➔ trade on a private basis, not on the recognized formal exchanges such as the LSE/NYSE.
  - more risky
  - little transparency in traded prices
- Trades formats:
  - shares
    - Come shares called **unlisted stocks** ➔ trades OTC because the company is small and unable to meet stock exchange requirements. ➔ More risky activity: little transparency in traded prices.
  - bonds
  - commodities