

The Stock Market and The Economy

Econ 202 Lecture 10

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- 1 Stocks and Bonds
- 2 The Stock Market Indices: an illustration
- 3 The Impact of the Stock market on the Economy
- 4 Monetary Policy Actions in Times of Crises

Where does the money for investment come from?

Investment projects are usually very large, often requiring external financing:

- ① *Internal financing* means payment out of retained earnings
- ② *External financing* means raising additional funds outside the company
 - Bank loans
 - Issuing bonds
 - Issuing stock

The bond markets

What is a bond?

Definition: A bond

A bond is a debt security that promises to make payments periodically for a specified period of time.

The bond market is where bonds are traded. Why is the bond market important?

- it enables corporations or governments to borrow to finance their activities
- it is where interest rates are determined

Definition: A security

A security is a claim on the issuer's future income

Definition: An asset

Any financial claim or piece of property that is subject to ownership

The stock markets

What is a stock?

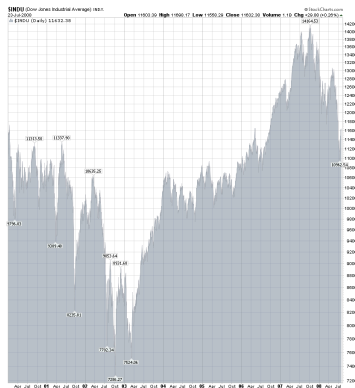
Definition: A stock

A share of ownership in a corporation. It is a security that is a claim on the earnings and assets of the corporation.

The stock market is where stocks are traded:

- Do you think you can make money on it?
- How do you think it affects your wealth, your spending attitudes, your savings?

How is the stock market moving during the last 8 years?



Can it have any impact?

The Stock Market Indices: an illustration



DJ 5000 Composite



US Banks



DJIA



US Commodity Companies

The Stock Market Indices: an illustration (2)



DJ Hardware Firms



DJ Mobile Phone Industry



DJ Software Firms



DJ Oil Industry

The Stock Market Indices: an illustration (3)



DJ Real Estate Firms



DJ Leisure Industry

The Stock Market Indices: an illustration (4)

Index PX

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Prague

RTS Index History chart (Java-version)

Period: from 3 February 1995 to 4 February 2009

Values: ☒ US dollars ☐ Rubles

☒ Closing

First value: 100.0

Min value: 38.53

Last value: 512.34

Max value: 2487.92

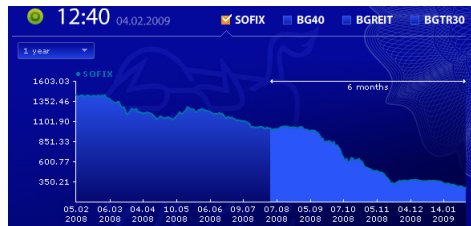


Moscow

The Stock Market Indices: an illustration (5)



Almaty



Sofia

The impact of stock market movements

The Boom of the 1990s

- 1 Between December 31, 1994, and March 31, 2000, the S&P 500 rose 226 percent, an annual growth rate of 25 percent
- 2 This was the largest stock market boom in U.S. history
- 3 The runup in stock prices added about \$14 trillion to household wealth (about \$2.5 trillion per year)

The stock market, consumption, and investment decisions

- ① One of the factors that affect consumption is wealth, and one of the main components of household wealth is the value of the stocks they hold. Empirical research shows that for every \$1.00 change in stock value, planned spending changes by \$0.03 to \$0.04.
- ② If a firm's stock price rises, it becomes easier to raise new capital

Stock Market Crashes and Policy Responses

