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Lecture 02: Financial institutions.

1_ The meaning of financial institutions:

Financial institutions are organizations that provide financial services to their clients. These include banks, credit unions, insurance companies, brokerage firms, and asset management companies. They play a crucial role in the economy by facilitating monetary transactions, lending, investment, and risk management. Financial institutions act as intermediaries between savers and borrowers, mobilize savings, and channel them into productive investments, thereby fostering economic growth and financial stability.

2_ Types of financial institutions:

There are various types of financial institutions that can meet your specific needs. They can be for-profit or nonprofit, serve different types of customers, provide a specific purpose, or focus on certain services. The main types of financial institutions include:

Commercial bank:

A commercial bank is a financial institution that accepts money from individuals and businesses and provides loans to those in need. They offer services such as loans, savings, certificates of deposits, bank accounts, bank overdrafts, etc., to their customers. These organizations earn money by granting loans to individuals and gaining interest on loans. Business loans, house loans, personal loans, car loans, and education loans are the different types of loans offered by commercial banks.

Investment Banks:

Investment banks work with corporations, governments, and other institutions that need capital and financial advice. They don't deal with customer deposits, but rather assist with financing through securities such as bonds and stocks. They also offer advice on business planning and decisions such as mergers.

Credit Unions:

A credit union is a financial institution similar to a commercial bank. But it is a non-profit institution created, owned, and operated by its members. They provide traditional banking services only to their members, such as account opening, issuing credit cards, loans, etc. Credit unions charge interest and account fees just like a bank, but they reinvest those profits into the products they offer; however, banks provide these profits to their shareholders.

Insurance Companies:

Insurance companies offer various types of insurance policies to offer financial protection. For example, insurance companies often sell products such as life, health, and home insurance. They put the money that comes from insurance premiums into a pool to fund the policy coverage.

Brokerage Firms:

A brokerage firm or company is a middleman who connects the buying and selling parties to facilitate the transaction. They assist in the dealing of securities such as stocks, mutual funds, shares, bonds, options, and other financial instruments. Once the transaction is completed, brokers receive both parties' brokerage (commission).

Savings and Loan Associations:

Savings and loans associations are financial institutions that provide savings and loan services to individuals and businesses. These associations operate as cooperative financial institutions where member's funds are collected and provided as loans to other members. The goal of these associations of to promote savings and provide loans with favorable terms for individuals and community.

3_ The function of financial institutions:

Financial institutions perform several key functions essential to the economy and financial system. Here are the primary functions of financial institutions:

Intermediation:

Financial institutions act as intermediaries between savers and borrowers. They collect funds from individuals and businesses as deposits and then lend them to borrowers who need capital for various purposes, such as starting a business or purchasing a home.

Depository Services:

Financial institutions provide depository services by accepting deposits from individuals and businesses. They offer checking accounts, savings accounts, and other deposit products where customers can securely store their money. These deposits may also earn interest.

Credit Provision:

Financial institutions extend credit to individuals and businesses through loans and credit lines. They evaluate the creditworthiness of borrowers, determine interest rates, and provide financial support for various needs, such as personal loans, mortgages, business loans, and working capital.

Investment Services:

Financial institutions offer investment services to help individuals and businesses manage and grow wealth. They provide access to investment products such as stocks, bonds, mutual funds, and other securities. They also offer advisory services to guide clients in making informed investment decisions.

Risk Management:

Financial institutions assist individuals and businesses in managing financial risks. They provide insurance products, such as life insurance, health insurance, property insurance, and liability insurance, to protect against potential losses and unforeseen events.

Payment and Settlement Services:

Financial institutions facilitate payment transactions between individuals and businesses. They provide payment and settlement services such as processing electronic fund transfers, issuing credit and debit cards, and managing payment systems to enable smooth and secure transactions.

Financial Advisory:

Financial institutions provide financial advisory services to individuals and businesses. They offer guidance on financial planning, retirement planning, tax planning, estate planning, and overall wealth management. They assist clients in making informed financial decisions based on their goals and risk tolerance.

4_ Advantages of Financial Institutions:

1. Procurement of Funds:

Financial institutions are crucial because they make it possible for people to receive money when they need it. For instance, even though banks do various tasks, they primarily collect deposits from those who have money, pool them, and then lend them to individuals who need money. Banks act as middlemen between depositors (who provide the bank with funds) and borrowers (to whom the bank lends money).

2. Offer Safety:

Even though you can keep your money at home or in your wallet, depositing money with a financial institution guarantees its security. You also have an additional layer of protection because government laws provide some protection for your deposits in case of a bank failure.

3. Financial Consultation:

Financial institutions provide people with finances and guide them with the right investment plans and policies. Investment banks inform businesses and individuals about the proper techniques for generating profits. They help their clients raise capital, issue new IPOs, etc . 4.

4. Employment Creation :

Starting or expanding a business requires financial resources, and bank loans are one of the easiest ways to get them. Financial institutions provide credit not only to individuals but businesses also. Startups and small businesses can start their venture by seeking long and medium-term credit from these institutions. This will lead to the opening of new employment opportunities and economic growth. The business owners also have the option to take a loan against their existing property either for a new venture opening or for the expansion and diversification of an existing one.