Bus 101

ASSIGN BUSTER

Business 101 Summarize how the Federal Reserve regulate the money supply. The Federal Reserve System tries to control or regulate the size of themoney supply by " conducting open market operations in which the Federal Reserve lends or purchases specific types of securities with authorized participants, known as primary dealers such as the United States Treasury. All open market operations in the United States are conducted by the Open Market Desk at the Federal Reserve Bank of New York, with an aim to making the federal funds rate as close to the target rate as possible." When a central bank is " easing", it triggers an increase in money supply by purchasing government securities on the open market thus increasing available funds for private banks to loan through fractional reserve banking (the issue of new money through loans) and thus grows the money supply. When the central bank is " tightening", it slows the process of private bank issue by selling securities on the open market and pulling money (that could be loaned) out of the private banking sector. It reduces or increases the supply of short term government debt, and inversely increases or reduces the supply of lending funds and thereby the ability of private banks to issue new money through debt.

The operative notion of easy money is that the central bank creates new bank reserves (in the US known as " federal funds"), which let the banks lend out more money. These loans get spent, and the proceeds get deposited at other banks. Whatever is not required to be held as reserves is then lent out again, and through the magic of the " money multiplier", loans and bank deposits go up by many times the initial injection of reserves. (Wilkepedia. org.)

2. Describe the advantages and disadvantages of the different methods of

short term financing.

Cash: Advantages: Flexibility, liquidity,. Disadvantages: low return, slack might lead to agency costs.

Inventory-Advantages: fewer " outs", might be able to take advantage of volume discounts, more economical production runs . Disadvantages: Must be financed, spoilage, it can hide problems

Accounts Receivable. Advantages: credit sales may increase sales . Disadvantages: May not be paid, must be financed

Current Liabilities Advantages: Speed, Flexibility, often lower rate . Disadvantage: Volatile, downside if you can not refinance

Accounts Payable: This is the most important source of short-term financing for many firms. Beware that increased use of Accounts payables (such as by not paying off when you should) can be expensive as most firms offer favorable terms for prompt payment and delaying payments can also upset your suppliers.

Short-term loans:

Bank Loans , Commercial paper , Commercial paper vs Bank Loans

Money Markets Securities

T-Bills , Federal Agency Discount Notes , Bankers' Acceptances , Negotiable CDs

Commercial Paper-IOUs. Advantages: Flexibility, liquidity, Disadvantages: low return, slack ... firms bank and trade credit are the only sources of short-term debt financing. (www. financeprofessor. com)

3. Appraise the four general techniques of risk management.

1. Risk avoidance

Includes not performing an activity that could carry risk. Avoidance may

seem the answer to all risks, but avoiding risks also means losing out on the potential gain that accepting (retaining) the risk may have allowed. Not entering a business to avoid the risk of loss also avoids the possibility of earning profits.

2. Risk reduction

Involves methods that reduce the severity of the loss. Examples include sprinlers designed to put out a fire to reduce the risk of loss by fire. This method may cause a greater loss by water damage and therefore may not be suitable.

3. Risk retention

Involves accepting the loss when it occurs. True self-insurance falls in this category. Risk retention is a viable strategy for small risks where the cost of insuring against the risk would be greater over time than the total losses sustained.. War is an example since most property and risks are not insured against war, so the loss attributed by war is retained by the insured. Also any amounts of potential loss (risk) over the amount insured is retained risk.

4. Risk transfer/Shifting Risk

Means causing another party to accept the risk, typically by contract or by hedging. Insurance is one type of risk transfer that uses contracts. Other times it may involve contract language that transfers a risk to another party without the payment of an insurance premium. Liability among construction or other contractors is very often transferred this way.

4. Risk Assumption

Technique of risk management (better known as retention or Self-Insurance) under which an individual or business firm assumes expected losses that are not catastrophic, but protects against catastrophic losses through the

purchase of insurance. Also refers to (1) instances where insured place themselves in situations that they realize pose a danger, and (2) the acceptance of risks by an insurance company. (Business Dictionary)

Sources:

1. Business Dictionary. Dictionary of Business Terms. Copyright 2000 by Barron's Educational Series, Inc..

2. Wilkepedia. Org.

3. www. finaceprofessor. com