

INTRODUCTION OF FINANCIAL ECONOMIC



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Preface

The field of financial economics bridges the disciplines of economics and finance, providing a comprehensive framework for analyzing how individuals, institutions, and governments make decisions under conditions of scarcity, risk, and uncertainty. In a global economy marked by rapid financial innovation, increased market volatility, and complex decision-making, a solid understanding of financial economics is more relevant than ever.

This book, titled "Introduction of Financial Economic", is designed to equip students, professionals, and educators with a deep and applied understanding of key financial principles and tools. Structured across five well-defined modules, it offers a gradual progression from foundational economic concepts to advanced investment decision-making techniques.

- Module 1 introduces the discipline of financial economics, tracing its roots and laying the groundwork for the application of economic principles in financial decision-making.
- Module 2 explores stock market behavior and the time value of money, including essential market theories like the Efficient Market Hypothesis and the Adaptive Market Hypothesis.
- Module 3 covers pricing strategies of securities, encompassing bond valuation, equity pricing, warrants, and modern asset pricing models such as CAPM, BSOPM, and APT.
- Module 4 shifts the focus to investment decisions under risk, providing tools such as expected utility theory, decision trees, sensitivity analysis, and behavioral insights.

- Module 5 addresses decisions under uncertainty, introducing classical decision criteria like Wald's Maximin and Savage's Minimax Regret, along with practical illustrations and regret-payoff matrices.

The content has been developed with an emphasis on clarity, real-world application, and pedagogical structure. Each module includes illustrative examples, tables, diagrams, and case-based scenarios to enhance conceptual understanding and analytical thinking. At the end of each unit, review questions are provided to reinforce learning outcomes and support examination preparation.

This book is especially suited for undergraduate and postgraduate students pursuing studies in economics, finance, business administration, and related fields. It can also serve as a valuable resource for professionals, researchers, and policymakers seeking structured insights into the economic logic behind financial markets and investment behavior.

I extend my sincere gratitude to the mentors, academic peers, and institutions that supported the development of this text. I hope this book not only informs but inspires its readers to think critically and engage confidently with the evolving landscape of finance.

Acknowledgement

We express our heartfelt gratitude to the Almighty for bestowing upon us the strength, wisdom and perseverance to bring this book, *Introduction of Financial Economic*, to fruition. The journey of conceptualizing and completing this academic work has been enriching and rewarding, made possible through the guidance, encouragement and cooperation of several individuals and institutions.

First and foremost, we extend our deepest thanks to our families, whose unwavering support and patience have been the foundation of our professional endeavors. Their understanding during the long hours of research, writing and editing has been a source of constant motivation.

We are especially thankful to the academic institutions and libraries that provided access to valuable literature, data sources and financial databases. Their assistance enabled us to delve into extensive research and present accurate, up-to-date content in this book.

Our sincere appreciation goes to our students and colleagues, whose queries, feedback and discussions inspired us to refine our ideas and enhance the clarity of complex concepts. Their enthusiasm for the subject has been a driving force in our commitment to deliver a comprehensive and engaging textbook.

We gratefully acknowledge the contribution of **Bharat Global Publications**, our esteemed publisher, for believing in the academic merit of this book and facilitating the publication process with professionalism and dedication. The editorial team deserves special mention for their meticulous attention to detail and commitment to quality.

Finally, we extend our thanks to all the scholars and researchers whose works have been referenced in this book. Their contributions

have enriched our understanding of financial economics and provided a strong foundation for the development of this text.

We hope that this book will serve as a valuable resource for students, educators, researchers and practitioners in the field of economics and finance. Any suggestions for improvement are most welcome and will be gratefully acknowledged in future editions.

Dr. Mohsina Hayat
Dr. Rachana Saxena
Dr. Mohd Shueb

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Module Summary

About the Book

Introduction to Financial Economics

The book *Introduction to Financial Economics* offers a comprehensive exploration of the key principles, theories and practices that define the field of financial economics. Designed for students, academicians and aspiring professionals, this book provides both a foundational understanding and analytical tools essential for navigating the complex world of finance and investments.

Module 1: Introduction to Financial Economics

The first module sets the groundwork by defining financial economics and exploring its evolution, scope and relevance in today's globalized economic environment. It introduces core concepts such as the role of financial markets, the behavior of economic agents, allocation of resources and how financial decisions influence the overall economy. This module also differentiates between microeconomic and macroeconomic aspects of finance, providing a balanced theoretical background to support deeper understanding in the subsequent modules.

Module 2: Stock Market Behavior and Time Value of Money

This module delves into the dynamic nature of the stock market. It explains how stock prices are influenced by investor behavior, economic indicators, company performance and macroeconomic trends. A crucial concept discussed is the *Time Value of Money* (TVM), which underpins all financial decision-making. Readers are introduced to present and future value calculations, annuities, perpetuities and the real-world application of discounting and compounding in evaluating investments and cash flows.

Module 3: Pricing Strategies of Securities

In the third module, the focus shifts to how securities—such as stocks, bonds and derivatives—are priced in financial markets. It covers valuation models including Dividend Discount Models (DDM), Price-Earnings (P/E) ratios, Bond Valuation techniques and an introduction to the Capital Asset Pricing Model (CAPM). The module also examines how market efficiency and information asymmetry impact pricing and investor decisions.

Module 4: Investment Decisions under Risk

Risk is an inherent part of all financial decisions and this module equips readers with the tools to evaluate and manage it. It explains the types and sources of financial risk—market risk, credit risk, interest rate risk—and how they are measured. Fundamental concepts such as risk-return tradeoff, portfolio diversification, standard deviation, beta and value-at-risk (VaR) are thoroughly discussed. The module emphasizes how rational investors make choices when outcomes are uncertain but probabilities are known.

Module 5: Investment Decisions under Uncertainty

The final module addresses decision-making scenarios where probabilities are either unknown or difficult to quantify. It introduces behavioral finance concepts, expected utility theory and decision-making models such as the Maximin, Maximax and Minimax regret criteria. The module also discusses how ambiguity, investor psychology and irrational behavior can affect market outcomes and individual investment strategies.

Overall, *Introduction to Financial Economics* is a valuable resource for understanding how financial markets operate, how economic theories are applied to real-world finance and how investment decisions are made under different conditions of risk and uncertainty. With clear explanations, practical examples and a modular structure, this book supports both academic learning and practical application in the field of finance.

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