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Financial Markets in India - I

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1. Introduction

Let us start this topic with the meaning of Financial System

The financial system provides a mechanism where any firm or lender may conveniently make funds available to net borrowers who intend to spend more than their current income. A financial system may be defined as, "a set of institutions, instruments and markets which foster savings and channel them to their most efficient use".

The financial system of any country consists of financial markets, financial institutions, financial instruments and financial services. Financial institutions are the firms, which provide financial services to lenders and borrowers. The next important role is being played by financial markets. It is the place where net lenders can lend their funds directly to net borrowers. A financial market is one in which financial assets one created or transferred. Financial markets may be defined as, "A market which is an aggregate of possible buyers a sellers of financial securities, commodities and other fungible items as well as the transaction between them."

It simplicities the flow of investment from savings. Financial market bridges the gap between one set of financial intermediaries with another set of players. They are the centres which provide the facility for buying and selling of financial instruments.

There are different set of parties included in the transactions of financial markets for example Individuals, financial institutions, government, central bank and other intermediaries. Currently the financial sector of India has reached the Rs 34, 28,475 million mark.

2. The role and functions of financial market

Let’s discuss the role and functions of financial market.

Financial market gives strength to the economy by providing finance available at the right place. So these points will give us a brief idea about role of financial markets.

1. Borrowers and lenders
2. Enables price determination
3. Offers liquidity to financial assets
4. Condenses the cost of transaction
5. Mobilizes the savings

In detail explanation of the above points is mentioned below:

1. Borrowers and Lenders: Financial markets allow the parties to transfer the funds from one agent to another for either investment purpose or consumption purposes. It helps the borrowers and lenders to come together at same platform.

2. Enables price determination: The demand and supply of any goods or services determines the prices of the financial assets. Financial market provides tools by which prices for both newly set up financial assets and existing stock of financial assets can be set.

3. Offers liquidity to financial assets: Financial Markets provides the holders of financial assets with a chance to resell or liquidate the assets at any available time.

4. Condenses the cost of transactions: As different instruments are issued and used in the market at regular intervals so the

transactions costs tend to increase but with the help of regulatory bodies of the market.

5. Mobilization of savings: Obtaining funds from the savers or surplus units such as household individuals, business firms, public sector units, central government, state governments, etc. is an important role played by financial markets. In the absence of financial system, the savings would never be mobilised and channelized to productive investments from the unproductive ones.

3. The types of financial markets vs. capital market vs. stock market

Now let us understand the types of financial markets vs. capital market vs. stock market

A financial market majorly consists of two segments those are Capital Market and Money Market. The capital market handles the medium and long term credit while money market handles short term credit.

Money market is the market for short term fund and handles short-term financial assets (less than a year) whereas capital markets take care of those financial assets which have maturity period of more than an year and deals with long term funds

The capital market is further classified as Primary markets and secondary markets. Primary market handles new issue of securities whereas secondary markets deals with those of securities that are presently available in the stock market.

Capital Market

Capital markets provide access to long term financial assets using debt capital and equity capital such as stocks, bonds, options and futures.

The market is divided into two segments known as primary markets and secondary markets as mentioned above and Capital markets contain organized platforms for exchanges and over the counter markets.

The primary market is where securities are issued for the first time which is also known as IPO, and secondary market is where securities that have been already issued are traded among investors. It is apt to note that the capital markets consists the stock market as well as the bond market.

The capital markets are regulated Securities and Exchange Board of India, to ensure that securities traded have good credit ratings so that no fraud may occur with the investors.

Stock market

Capital market itself has one more component which is stock market, consisting of the primary and secondary markets.

The stock market is the platform for the shares which are issued and traded among investors, providing an opportunity for investors to obtain fractional ownership of the firm, as well as decision making power in relation to the percentage of ordinary shares that they hold in the company and for corporations to obtain capital for their expansion purposes and an opportunity for.

Stocks that are sold in the stock market are listed on the stock exchanges in relation to the country in which the stock are sold. The stock sold are also categorized into indexes that track the movement of a number of these similar stocks, such as the BSE30 index that tracks the movement of 30 top financial companies in India where BSE stands for Bombay Stock Exchange.

Capital market vs. Stock market

The stock market is a part of the capital market, and both these markets serve a common purpose of providing a mechanism under which capital can be raised by a firm for their business operations.

A capital market is a mixture of the stock market and the bond market which issues debt securities such as bonds and debentures, in the addition with stocks. On the other hand the Stock market is the only platform for trading shares and is also known as the equity market.

The securities traded on a capital market such as bonds have different financial characteristics than stock in that at the time of maturity the coupon payments as well as the face value needs to be paid back. As for stock, since it is an equity investment, once issued, the firm will hold onto the capital, and income for investors will be dividends and capital increments arising from the increase in the value of the stock during the holding period, which can be ultimately sold for a higher price.

Thus one can say that stock market is a part of capital market holding only the equities of different types while capital market is a part of financial market dealing with stock market and bond market which issues long term securities and finally wholesome considering all the markets together where any sort of borrowing or lending of any financial assets is done is known as financial markets.

Symbolically one can say,

Financial Market > Capital Market > Stock Market

4. The players of financial market

Now let’s understand the players of financial market

There are various kinds of participants in financial market. They may be issuers, investors or other intermediaries. The financial market basically has two sectors which are known as Organised and Unorganized sectors. Organised sector is the one which is controlled by RBI, SEBI and other regulatory bodies while unorganised has been dealt by money lenders, landlords, traders and many more. Accordingly the participants are divided and explained below are of the organised sector. The principle participants are:

1. Banks
2. Government
3. Retail Investors
4. Brokers
5. Institutional Investors
6. Mutual Funds
7. Insurance Corporation
8. Finance companies

They are explained below in detail:

1. Banks: they are largest provider of funds to business houses and corporates and are one of the major participants.
2. Government: they are the authorised dealers basically looking after the demand and supply operations of the market and sometimes work to fill up the gap in between them.
3. Retail Investors: these are those investors who invest individually for their personal account and not on behalf of any other company or organisation.

4. Brokers: A broker is a commissioned agent of a buyer (or seller) who facilitates trade by locating a seller (or buyer) to complete the desired transaction.

5. Institutional Investors: An institutional investor is an entity, company, mutual fund, insurance corporations, brokerage, or other such group that has a large amount of money or assets to invest. These firms typically represent investors who might be retail or other firms.

6. Mutual Funds: they basically acquire funds from the general public and invest their money in money market, shares or bonds and charge a small fee for managing the fund.

7. Insurance Corporations: these corporations issue a contract with individuals or firms with a promise to refund the money to them in future in case of any contingency and for the time period invest that money in debts, equities, properties, securities etc.

8. Finance Companies: they basically engage in short and medium term financing for the business by getting funds by issuing debentures and borrowing from general public.

5. Summary

Financial market being a part of any financial system helps participants to deal in financial instruments by providing a facility of adjusting finance. There are basically two types of financial markets namely capital market (dealing with long term securities) and money market. It provides variety of services which can affect the growth of the economy. The different players of financial sector are individuals, corporates, government, banks etc. which plays important role in the market.