CAPITAL MARKET

What is capital market?

A capital market is a place that allows the trading of funding instruments such as shares, debentures, debt instruments, bonds, ETFs, etc. It is a source for raising funds for individuals, firms, and governments.

The securities exchanged here would typically be a long-term investment with over a year lock-in period. On the other hand, short-term investments are usually found in the money market**.**

What are types of capital market?

1. primary market

The primary market is for trading freshly issued securities, i.e., first-time trading. It enables an initial public offering. It is also known as the new issues market.

Here, companies raise funds with the help of preferential allotment, rights issue, electronic IPOs, or the pre-selected issue of securities or private placement. Usually, like an investment bank, the intermediary attaches an initial price to the shares. Once the sale materializes, firms take their shares to the stock exchange to facilitate trading between different investors.

2. secondary market

The trading of old securities occurs in the secondary market, which occurs after transacting in the primary market. Both stock markets and over-the-counter trades come under the secondary market. We also call this market the stock market or aftermarket.

Examples of secondary markets are the London Stock Exchange, the New York Stock Exchange, NASDAQ, etc.

What are features of a Capital Market?

The following are the features of capital markets:

Safety: Government regulates the capital markets. They operate under a defined set of rules. Therefore, investors consider it a safe place for trading.

Channelizes savings: Capital markets act as a link between savers and investors. They mobilise the savings from savers to industry players and promote economic growth.

Long term investment: Capital markets provide a platform for long term investments. Any investors looking for investing in long term investments can do so through capital markets.

Wealth Creation: The capital market provides an opportunity to investors with surplus funds to invest in capital market instruments like shares and bonds and create wealth for themselves through the power of compounding.

Helps intermediaries: The capital market mobilises savings from savers to borrowers with the help of intermediaries like stock exchanges, brokers, banks, etc. By doing so, the capital market is helping intermediaries conduct business and earn income.

Are Capital Markets the Same as Financial Markets?

Capital markets are not the same as financial markets.

Financial markets involve buying and selling assets, such as stocks, bonds, and currency. Capital markets are part of the financial market. They allow companies to raise capital from investors by issuing shares.

The two most important capital markets are:

Primary markets: These allow companies to issue new shares and debt for the first time. They also allow investors to trade existing shares and debt. For example, when a company wants to raise money by issuing new shares, it will launch an Initial Public Offering (IPO).

Secondary markets: These allow investors to trade existing shares and debt. For example, when a company wants to sell its shares on the stock market or investors want to sell bonds, they will go through one of the many secondary markets.

What is the work of financial intermediaries?

Financial intermediaries are the organisations that assist in the transfer of money. They serve as a link between the surplus and deficit parties.

For example:

Brokers: A broker assists in buying and selling shares for a commission.

Stock Exchanges: For example, National Stock Exchange (NSE), Bombay Stock Exchange (BSE), etc

Regulator: Securities Exchange Board of India (SEBI) governs the capital markets in India.

How does capital market works?

A capital market assists an economy by providing a platform to gain funds for business operations, development activities, or wealth enhancement. The functioning of a capital market follows the theory of the circular flow of money.

For example, a firm needs money for business operations and usually borrows it from households or individuals. In the capital market, the money from individual investors or households is invested in a firm's shares or bonds. In return, investors gain profits as well as goods and services.

The market comprises suppliers and buyers of finance, along with trading instruments and mechanisms. There are also regulatory bodies. Stock exchanges, equity markets, debt markets, options markets, etc., are some capital market examples.

Which Markets Do Firms Use to Raise Capital?

The main markets firms use to raise capital are the equity, debt, and money markets.

When a firm wants to raise funds by issuing new shares or bonds, it can do so directly on the stock market or via a financial intermediary such as an investment bank (e.g., Rothschild). In some cases, companies also issue securities in private placements where only institutional investors buy these issues.

The main reason for issuing shares is to raise capital. Companies usually issue new shares when they need to finance an expansion or diversification of their operations. They can also use share issues to reward employees, takeovers, and corporate restructurings.

Are capital markets efficient?

Most markets are not perfectly efficient. The capital market is no exception, but to some extent, the prices of securities reflect that they have incorporated the current information in the market.

Who Controls the Capital Market in India?

The three regulatory bodies that control the Indian capital market are the Reserve Bank of India (RBI), the Securities & Exchange Board of India (SEBI), and the Ministry of Finance (MoF).

What is the role of SEBI in capital markets?

The Indian Capital Markets are effectively monitored and governed by the Securities Exchange Board of India (SEBI). The government has established the SEBI as a regulating organisation to stop the malpractices such as false issues, supply delays, and violations of stock market rules and regulations.

The SEBI’s responsibilities and goals are:

1. Control the activities of transfer agents, stockbrokers, commercial bankers, etc.

2. Monitor how securities markets and stock exchanges operate.

3. Promote the establishment of Self-regulatory Organisations.

4. Create guidelines to prevent misconduct

5. SEBI has outlawed internal trading, which gives certain traders an advantage over others.

what is the advantage of capital market?

Money moves between people who need capital and who have the capital.

There is more efficiency in the transactions.

Securities like shares help in earning dividend income.

With the passage of time, the growth in value of investments is high.

The interest rates provided by securities like Bonds are higher than interest rates given by banks.

Can avail tax benefits by investing in stock markets.

Scope for a wide range of investments.

Securities of capital markets can be used as collateral for getting loans from banks.

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240938751/07/2021