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FINANCIAL MARKET

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Abstract- **A financial market is a market in which people and entities can trade financial securities, commodities, and other fungible items of value at low transaction costs and at prices that reflect supply and demand. Securities include stocks and bonds, and commodities include precious metals or agricultural goods. In economics, typically, the term *market* means the aggregate of possible buyers and sellers of a certain good or service and the transactions between them.**

I. INTRODUCTION

A financial market is a market in which people and entities can trade financial securities, commodities, and other fungible items of value at low transaction costs and at prices that reflect supply and demand. Securities include stocks and bonds, and commodities include precious metals or agricultural goods.In economics, typically, the term market means the aggregate of possible buyers and sellers of a certain good or service and the transactions between them. The term "market" is sometimes used for what are more strictly exchanges, organizations that facilitate the trade in financial securities, e.g., a stock exchange or commodity exchange. This may be a physical location (like the NYSE, BSE, NSE) or an electronic system (like NASDAQ). Much trading of stocks takes place on an exchange; still, corporate actions (merger, spinoff) are outside an exchange, while any two companies or people, for whatever reason, may agree to sell stock from the one to the other without using an exchange.Trading of currencies and bonds is largely on a bilateral basis, although some bonds trade on a stock exchange, and people are building electronic systems for these as well, similar to stock exchanges.

II. TYPES OF FINANCIAL MARKET

Within the financial sector, the term "financial markets" is often used to refer just to the markets that are used to raise finance: for long term finance, the *Capital markets*; for short term finance, the *Money markets*. Another common use of the term is as a catchall for all the markets in the financial sector, as per examples in the breakdown below.

- **Capital markets** which consist of:
  - Stock markets, which provide financing through the issuance of shares or
  - common stock, and enable the subsequent trading thereof.
  - Bond markets, which provide financing through the issuance of bonds, and enable the subsequent trading thereof.
- **Commodity markets**, which facilitate the trading of commodities.
- **Money markets**, which provide short term debt financing and investment.
- **Derivatives markets**, which provide instruments for the management of financial risk.
- **Futures markets**, which provide standardized forward contracts for trading products at some future date; see also forward market.
- **Insurance markets**, which facilitate the redistribution of various risks.
- **Foreign exchange markets**, which facilitate the trading of foreign exchange.

The capital markets may also be divided into primary markets and secondary markets. Newly formed (issued) securities are bought or sold in primary markets, such as during initial public offerings. Secondary markets allow investors to buy and sell existing securities. The transactions in primary markets exist between issuers and investors, while secondary market transactions exist among investors.Liquidity is a crucial aspect of securities that are traded in secondary markets. Liquidity refers to the ease with which a security can be sold without a loss of value. Securities with an active secondary market mean that there are many buyers and sellers at a given point in time. Investors benefit from liquid securities because they can sell their assets whenever they want; an illiquid security may force the seller to get rid of their asset at a large discount.

III. RAISING CAPITAL

Financial markets attract funds from investors and channel them to corporations—they thus allow corporations to finance their operations and achieve growth. Money markets allow firms to borrow funds on a short term basis, while capital markets allow corporations to gain long-term funding to support expansion (known as maturity transformation).Without financial markets, borrowers would have difficulty finding lenders themselves. Intermediaries such as banks, Investment Banks, and Boutique Investment Banks can help in this process. Banks take deposits from those who have money to save. They can then lend money from this pool of deposited money to those who seek to borrow. Banks popularly lend money in the form of loans and mortgages. More complex transactions than a simple bank deposit require markets where lenders and their agents can meet borrowers and their agents, and where existing borrowing or lending commitments can be sold on to other parties. A good example of a financial market is a stock exchange. A company can raise money by selling shares to investors and its existing shares can be bought or sold.

The following table illustrates where financial markets fit in the relationship between lenders and borrowers:

Financial Markets	Borrowers
Interbank Stock Exchange Money Market Bond Market Foreign Exchange	Individuals Companies Central Government Municipalities Public Corporations

FIG 1. Relationship b/w lenders and borrowers

IV. LENDERS

Who have enough money to lend or to give someone money from own pocket at the condition of getting back the principal amount or with some interest or charge, is the Lender.

Individuals & Doubles

Many individuals are not aware that they are lenders, but almost everybody does lend money in many ways. A person lends money when he or she:

- puts money in a savings account at a bank;
- contributes to a pension plan;
- pays premiums to an insurance company;
- invests in government bonds;

Companies

Companies tend to be borrowers of capital. When companies have surplus cash that is not needed for a short period of time, they may seek to make money from their cash surplus by lending it via short term markets called money markets.

There are a few companies that have very strong cash These companies tend to be lenders rather than borrowers. Such companies may decide to return cash to surplus (e.g. via a share buyback.) Alternatively, they may seek to make more money on their cash by lending it (e.g. investing in bonds and stocks).

Borrowers

- *Individuals* borrow money via bankers' loans for short term needs or longer term mortgages to help finance a house purchase.
- *Companies* borrow money to aid short term or long term cash flows. They also borrow to fund modernization or future business expansion.
- *Governments* often find their spending requirements exceed their tax revenues. To make up this difference, they need to borrow. Governments also borrow on behalf of nationalized industries, municipalities, local authorities and other public sector bodies. In the UK, the total borrowing requirement is often referred to as the Public sector net cash requirement (PSNCR).

Governments borrow by issuing bonds. In the UK, the government also borrows from individuals by offering bank accounts and Premium Bonds. Government debt seems to be permanent. Indeed the debt seemingly expands rather than being paid off. One strategy used by governments to reduce the *value* of the debt is to influence *inflation*.*Municipalities and local authorities* may borrow in their own name as well as receiving funding from national governments. In the UK, this would cover an authority like Hampshire County Council. *Public Corporations* typically include nationalized industries. These may include the postal services, railway companies and utility companies. Many borrowers have difficulty raising money locally. They need to borrow internationally with the aid of Foreign exchange markets. Borrowers having similar needs can form into a group of borrowers. They can also take an organizational form like Mutual Funds. They can provide mortgage on weight basis. The main advantage is that this lowers the cost of their borrowings.

V. ANALYSIS OF FINANCIAL MARKET

Much effort has gone into the study of financial markets and how prices vary with time. Charles Dow, one of the founders of Dow Jones & Company and The Wall Street Journal, enunciated a set of ideas on the subject which are now called Dow Theory. This is the basis of the so-called technical analysis method of attempting to predict future changes. One of the tenets of "technical analysis" is that market trends give an indication of the future, at least in the short term. The claims of the technical analysts are disputed by many academics, who claim that the evidence points rather to the random walk hypothesis, which states that the next change is not correlated to the last change. The role of human psychology in price variations also plays a significant factor. Large amounts of volatility often indicate the presence of strong emotional factors playing into the price. Fear can cause excessive drops in price and greed can create bubbles. In recent years the rise of algorithmic and high-frequency program trading has seen the adoption of momentum, ultra-short term moving average and other similar strategies which are based on technical as opposed to fundamental or theoretical concepts of market Behaviour.The scale of changes in price over some unit of time is called the volatility. It was discovered by Benoît Mandelbrot that changes in prices do not follow a Gaussian distribution, but are rather modeled better by Lévy stable distributions. The scale of change, or volatility, depends on the length of the time unit to a power a bit more than 1/2. Large changes up or down are more likely than what one would calculate using a Gaussian distribution with an estimated standard deviation.

VI. FINANCIAL MARKET SLANG

Poison pill, when a company issues more shares to prevent being bought out by another company, thereby increasing the number of outstanding shares to be bought by the hostile company making the bid to establish majority. **Quant**, a quantitative analyst with a PhD[and above) level of training in mathematics and statistical methods. **Rocket scientist**, a financial consultant at the zenith of mathematical and computer programming skill. They are able to invent derivatives of high complexity and construct sophisticated pricing models. They generally handle the most advanced computing techniques adopted by the financial markets since the early 1980s. Typically, they are physicists and engineers by training; rocket scientists do not necessarily build rockets for a living. **White Knight**, a friendly party in a takeover bid. Used to describe a party that buys the shares of one organization to help prevent against a hostile takeover of that organization by another party.round-tripping**s murfing**, a deliberate structuring of payments or transactions to conceal it from regulators or otherparties, a type of money laundering that is often illegal. **Spread**, the difference between the highest bid and the lowest offer.

VII. ROLE(FINANCIAL SYSTEM AND ECONOMY)

One of the important sustainability requisite for the accelerated development of an economy is the existence of a dynamic financial market. A financial market helps the economy in the following manner.

- **Saving mobilization**: 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.
- **Investment**: Financial markets play a crucial role in arranging to invest funds thus collected in those units which are in need of the same.
- **National Growth**: An important role played by financial market is that, they contributed to a nations growth by ensuring unfettered flow of surplus funds to deficit units. Flow of funds for productive purposes is also made possible.
- **Entrepreneurship growth**: Financial market contribute to the development of the entrepreneurial claw by making available the necessary financial resources.
- **Industrial development**: The different components of financial markets help an accelerated growth of industrial and economic

development of a country, thus contributing to raising the standard of living and the society of well-being.

- **FUNCTIONS OF FINANCIAL MARKET**

- **Intermediary Functions**: The intermediary functions of a financial markets include the following:
  - **Transfer of Resources**: Financial markets facilitate the transfer of real economic resources from lenders to ultimate borrowers.
  - **Enhancing income**: Financial markets allow lenders to earn interest or dividend on their surplus invisible funds, thus contributing to the enhancement of the individual and the national income.
  - **Productive usage**: Financial markets allow for the productive use of the funds borrowed. The enhancing the income and the gross national production.
  - **Capital Formation**: Financial markets provide a channel through which new savings flow to aid capital formation of a country.
  - **Price determination**: Financial markets allow for the determination of price of the traded financial assets through the interaction of buyers and sellers. They provide a sign for the allocation of funds in the economy based on the demand and to the supply through the mechanism called price discovery process.
  - **Sale Mechanism**: Financial markets provide a mechanism for selling of a financial asset by an investor so as to offer the benefit of marketability and liquidity of such assets.
  - **Information**: The activities of the participants in the financial market result in the generation and the consequent dissemination of information to the various segments of the market. So as to reduce the cost of transaction of financial assets.
- **Financial Functions**
  - Providing the borrower with funds so as to enable them to carry out their investment plans.
  - Providing the lenders with earning assets so as to enable them to earn wealth by deploying the assets in production debentures.
  - Providing liquidity in the market so as to facilitate trading of funds.
  - it provides liquidity to commercial bank
  - it facilitate credit creation
  - it promotes savings
  - it promotes investment
  - it facilitates balance economic growth
  - it improves trading floors

VIII. CONSITUTENTS OF FINANCIAL MARKET

Based on market levels

- **Primary market**: Primary market is a market for new issues or new financial claims. Hence it's also called new issue market. The primary market deals with those securities which are issued to the public for the first time.
- **Secondary market**: It's a market for secondary sale of securities. In other words, securities which have already passed through the new issue market are traded in this market. Generally, such securities are quoted in the stock exchange and it provides a continuous and regular market for buying and selling of securities.

Based on security types

- **Money market**: Money market is a market for dealing with financial assets and securities which have a maturity period of up to one year. In other words, it's a market for purely short term funds.
- **Capital market**: A capital market is a market for financial assets which have a long or indefinite maturity. Generally it deals with long term securities which have a maturity period of above one year. Capital market may be further divided into: (a) industrial securities market (b) Govt. securities market and (c) long term loans market.
  - **Equity markets**: A market where ownership of securities are issued and subscribed is known as equity market. An example of a secondary

equity market for shares is the Bombay stock exchange.

- **Debt market**: The market where funds are borrowed and lent is known as debt market. Arrangements are made in such a way that the borrowers agree to pay the lender the original amount of the loan plus some specified amount of interest.

- **Derivative markets**: A market where financial instruments are derived and traded based on an underlying asset such as commodities or stocks.
- **Financial service market**: A market that comprises participants such as commercial banks that provide various financial services like ATM. Credit cards. Credit rating, stock broking etc. is known as financial service market. Individuals and firms use financial services markets, to purchase services that enhance the working of debt and equity markets.
- **Depository markets**: A depository market consist of depository institutions that accept deposit from individuals and firms and uses these funds to participate in the debt market, by giving loans or purchasing other debt instruments such as treasure bills.
- **Non-Depository market**: Non-depository market carry out various functions in financial markets ranging from financial intermediary to selling, insurance etc. The various constituency in non-depositary markets are mutual funds, insurance companies, pension funds, brokerage firms etc.

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