Financial market development

Finance, Market

In many of the developing countries it has been hitherto believed that the financial market reform has to be gyrating around the commercial banking system. It is true that the commercial banking sector's contribution to growth in economy in these developing countries such as Chile and Mexico has over time grown inextricably connected to the development and growth of the other related capital market areas such as equity, government debts and the corporate securities.

Therefore, reform in the capital market has hitherto emphasized the use of strategies with the potential of not only strengthening but also deepening the capital markets i. e. both the debt and equity markets. This paper seeks to highlight the general issues in the development in the capital markets such as GDP, interest rate spreads not only in the global context but also in the developing countries thereby showing how the global trends have affected developing countries and these countries' policy response so as attract, emulate and manage reform and development in domestic capital markets. The paper finally highlights the comparative trends in domestic capital market with specific focus to country experience: Chile and Mexico in regards to their participation in international capital market.

Development of a country is measured by the GDP. However there are other factors which the UN has identified as measure for development such as life expectancy, rate of literacy etc. The UN has on the other developed a compound indicator called HDI which is a combination of the above named measures and is used to measure level of development. The global economy generally impacts on the economy, especially on the capital market of the developing countries. This means that governments cannot borrow because

the states that lend are also engrossed in economic woes of recession. Further, if the lending states manage to lend, the interest rates are higher than recommended thus pushing thus tradi0ng a big blow to the development of the developing countries (Bożyk, 2006).

In countering the global; economic trend especially that of recession, the developing countries have resolved to internal borrowing through the use of corporate securities and bonds in the state owned corporations so as to raise themoneyrequired to run these governments and initiate industrialization and other forms of development. Secondly, the governments in the developing countries have resolved to IPOs thus relinquishing their right in state owned organizations to the public to raise the much required funds. The practice in developing countries implies that financial integration facilitates growth of capital markets but it may negatively affect the volatility of share prices and efficiency of stock market especially when the capital market reforms are not suitable (Sheffrin, 2003).

The main questions that remain are how the developing countries can develop without depending on the already developed countries for assistance, can GDP alone be used to measure development in the developing countries? How can the developing countries manage to insulate their economies from being affected and greatly influenced by the global economic trends such as recession through their capital markets without necessarily adversely affecting the volatility of the stock market and share prices?

Actually, the countries that qualify to categorize as developing can invest heavily in the capital market thereby using the funds raised from these

investments in industrialization and other forms of sustaining developments. For instance, the countries such as Chile and Mexico have invested in the capital market top help catapult the development needed . but it has proven such a step if not carefully managed may lead to the total crashing of the capital; markets. The two countries are simply a tale of capital market crises.

The 1994Mexicanpeso crisis demonstrates a typical capital market crisis which sent shock waves through the global economy. In the 1980s, Chile suffered a similar crisis as Mexico because of the 1970s structural reforms characterized by a radical opportunity in the economy; rampant privatization, and deregu- lation effort in a bid to realize a modern financial sector. In a bid to save themselves from the capital market crises, the countries' use of predetermined exchange rates aimed to get rid of inflation collaborated with the resultant huge capital inflows intermediated by a fragile banking system to bring forth an exchange- rate overvaluation, a susceptible financial sector and the eventual crumpling of the currency