

The financial markets: direct and indirect transfers



In economics, a financial market refers to a media that allows people to buy, sell, create and exchange financial securities such as share and bonds, commodities such as basic agricultural goods and precious metals, and other fungible items of value at low transaction costs and at prices that reflect the efficient-market.

Both general markets where many commodities are traded and specialized markets where only one commodity is traded exist in financial market.

Markets work by placing many interested buyers and sellers in one media, thus making it easier for them to find each other. The financial markets can be divided into different types such as capital markets commodity markets, money markets, insurance market and foreign exchange market.

A saver refers to the one who deposit their money in bank, invest in company share and pays premium to an insurance company with objective to earn interest, dividend and profit. They aim also to accumulate their fund for future investment and expenses. However, a borrower just the reverse to saver. A borrower borrowed the money from saver by financial market to fulfill their need and need to effort the interest charge or give the dividend to saver.

In a well-functioning economy, capital will flow efficiency from saver to borrower. The transfer of fund can make by three different ways such as direct transfer, indirect transfer through investment bankers and indirect transfer through financial intermediary.

2. 0 Body

2. 1 Direct transfer

The first way is through direct transfer. It refers to a transfer of assets from one type of tax-deferred retirement plan or account to borrower. Direct transfers are not considered to be distributions and not taxable as income or subject to any penalties for early distribution. Most transfers take several days to complete, although this process is now generally faster in the electronic than in the past. Direct rollovers from qualified plans are a form of direct transfer. It occurs when firms direct sell their stock or bond to saver without going through any financial institution

The advantages of direct transfer are direct transfers convenience and simple to trade between borrower and saver. The reason is when both borrower and saver agree with the term and condition, the transaction will be in process. Besides, it will be save time and cost. The reason is the transaction can complete online, just taking few days to complete and there is no high commission to pay for intermediate.

Even though it is a lot of advantages using this method, there also bring some disadvantages to both parties. The savers will face lack of professional consultation from expertise. This will lead to the saver making wrong investment, facing loss the money and cheat by the business. Beside, the business will also facing less efficiency when direct transfer the securities. The reason is there is no expertise to help them promote the securities and it may not planning well when issuance of securities.

2. 2 Indirect transfer through investment bankers

The second way is indirect transfer through investment bankers. Investment bank refers to a financial institution that helps individuals and corporations to raising their capital by underwriting. They also act as the client's agent when issuance of securities such as stock and bond. An investment bank may also help organization involved in mergers and acquisitions and provides ancillary services. In investment banking there are two main which are trading securities for cash or other securities and promotion of the securities.

In this way, the investment banker assumes the risk of selling a new security issue at a satisfactory price. This is called underwriting. An underwrite serve as a middleman and facilitates the issuance of securities. The company's securities and saver's money will pass through the investment banking house. The investment banker will buy the entire issue of securities from the company that needs of financial capital. Then investment bank will turn sells these same securities to savers at a higher price. However, the investment bank taking the risk when they buy and hold the company's a security for certain time and it may not resell to savers for as much as they paid after a period of time. The reason is new securities are involved and company receives the proceed of the sale, this is called a primary market transaction. Besides, the investment banker also advises firms on the details of selling securities.

The advantages for this method are the business will get professional suggestion from expertise about the details of selling securities. The business can raise the capital more efficient, the reason is the investment

banker will buy over the securities and hold to sell for savers. This will help to business dispense with the pending time to wait saver transfer the money.

The disadvantages for this method are the business may face depress in price of securities. The reason is when the business need capital emergency, the investment banker will depress the price of securities in order to make more money. The savers may also face receive inaccuracy information from investment banker. The reason is the investment banker wants to resell the hold securities, they may give inaccuracy information to the saver.

2. 3 Indirect transfer through financial intermediary

The third way is indirect transfer through financial intermediary. Financial intermediary consists of “ channeling funds between surplus and deficit agents”. A financial intermediary is a financial institution that connects surplus and deficit agents. The classic example of a financial intermediary is a bank that transforms bank deposits into bank loans. Insurance companies, credit unions, pension fund and mutual funds also include as financial intermediary. Insurance defined as the equitable transfer of the risk of a loss, from one entity to another, in exchange for payment. Credit union is a cooperative financial institution that is owned and controlled by its members and operated for the purpose of promoting thrift, providing credit at reasonable rates, and providing other financial services to its members. Pension fund is any plan, fund, or scheme which provides retirement income. Mutual fund is a professionally-managed type of collective investment scheme that pools money from many investors to buy securities

Through the process of financial intermediation, certain assets or liabilities are transformed into different assets or liabilities. As such, financial intermediaries channel funds from savers to those borrowers. As example, saver will save the surplus money in bank and get the deposit certificate, the bank will use the money to borrow to borrower by term of mortgage.

Financial intermediaries provide important advantages to savers. Lending through an intermediary is usually less risky than lending directly. The major reason for reduced risk is that a financial intermediary can diversify.

Financial intermediary will give many loans to different borrower. When mistake happen, the financial intermediary can cover by others loan interest.

But if savers borrow direct to business, the risk will face by individual.

Another reason is financial intermediary specialize in lending and better predict which of the people able to repay compare to individual savers.

Second advantage financial intermediaries give savers is liquidity. Liquidity is the ability to convert assets into form money quickly. A house is an illiquid asset; selling one can take a great deal of time. If an individual saver has lent money directly to another person, the loan can also be an illiquid asset.

Third advantage financial intermediaries give savers is cost advantage.

Using financial intermediaries can reduce the costs of borrowing. The reason is there are a lot of borrowings complete in financial intermediaries, it can lead to economic of scale and save cost for savers.

3. 0 Conclusion