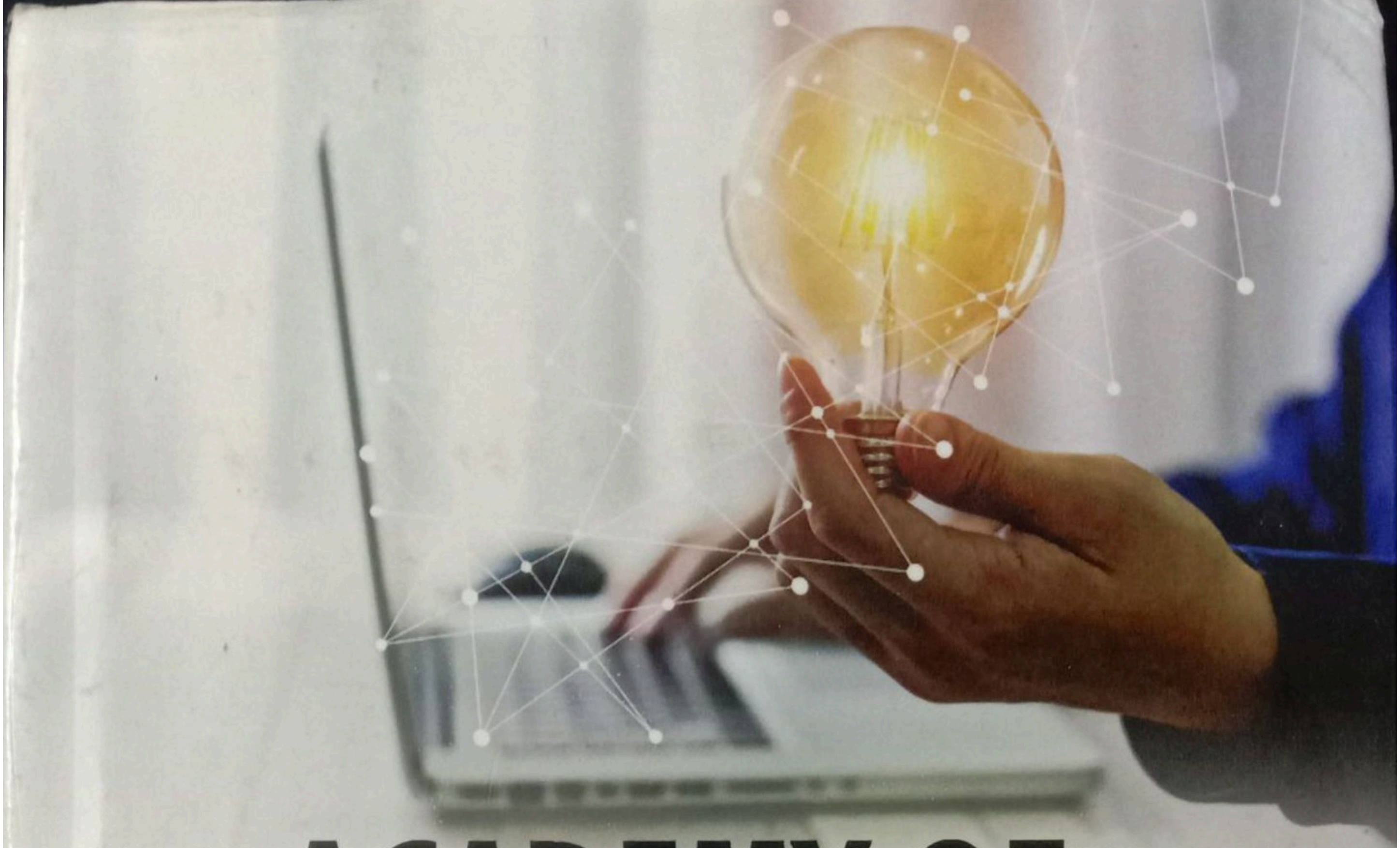

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Dr. VINITHA A.S.

ANU A.N.

VIDYA K.

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Message from the Principal

"Knowledge is always the light of happiness"

Dr. Jayan Erancheri Ilam

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Foreword

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Education aims to empower the mankind through knowledge acquisition and sharing. Due to rapid technological advancement the world is getting changed within no time. The fruits and benefits of these changes make life more easy, happy and comfortable. The Covid pandemic situation paved easy for the widespread use of technology among the people of different walks of life across the world. Innovations are taking place in production, financing, marketing, human resources, operations, logistics, warehousing, tourism etc. The knowledge, hypotheses and theories have to be shared and made available to the stakeholders of the society through different platforms. Research enriches the teaching and learning process while contributing to the body of knowledge. Organising seminars, conferences, workshops, panel discussions etc. are some of the initiatives in this direction. Publishing research articles through journals and magazines you have online and offline create platforms for the stakeholders of education like students, teachers, researchers and other academicians to understand, discuss, share, internalize and implement innovations taking place in the field of education.

The journal entitled **"Academy of Commerce Review"** is a noble attempt in this direction by the V.T. Bhattathiripad College, Sreekrishnapuram under the initiative of the P.G. Department of Commerce and Management Studies. It contains reviews and research papers related to different areas of Commerce and Management. The original articles and review papers contained therein are sure to take the readers forward in their quest for excellence in the field of academic research. I wish the College in general and the Department of Commerce and Management in particular and all success in this endeavour and hope they will continue the journey further on the path to create a benchmark for the coming generations as it will be highly useful to create, develop and sharpen the research mindset of the readers.

Sd

Prof. B. Johnson

Preface

Research is the important part for the academic development of faculty members and students of the college. We are publishing this journal from June 2015. Our research journal has separate expert committee and advisory committee which look after the plagiarism of papers. The selected papers are published in the research journal. We also promote other institutions' faculty to publish the papers in our research journal "Academy of Commerce Review". Our teachers are encouraging the students to take up research projects and involve students too.

The objective of the journal is to provide a platform to faculty, research scholars and practitioners of management discipline to highlight new knowledge, innovation, and technology usage in the commerce and management field. These papers are not meant to be the final word but rather a step towards classification and to stimulate the debate and helps you to do your further researches and thinking on the subject.

We would like to convey our appreciation to all the contributors including the authors of the chapters in this book. We would like to express special thanks to our HOD, Ms. Bindu T. for her continuous support and great effort to bringing the book into fruition. We also express our sincere gratitude to Dr. E.Jayan–our Principal, Dr. Saritha Namboodiri—IQAC Coordinator, all colleagues and staff of our college.

Dr. Vinitha A.S.

Ms. Vidya K.

Ms. Anu A.N.

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A Study on the Role of Financial Intermediaries in the Capital Market

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ABSTRACT

Intermediaries are the middlemen between any two parties that are partaking in a transaction. These middlemen act as the bridge between them and help in exchanging necessary information towards fulfilling the objective of a common goal. In a stock market, or business, or any traditional marketplace, these intermediaries act as the connecting links between the producers and consumers. They facilitate intermediate action or transactions between those parties.

To understand their functions in the marketplace and the role they play in providing a common platform to the players, one has to understand the types of Intermediaries. Depending on the type of intermediary, their functions are also predefined. You should also note that there can be intermediaries at various levels of a supply or distribution chain. Hence, these levels could be a parameter to decide the roles of an intermediary.

So select the topic to study the role of intermediaries in capital market and this study is purely based on secondary data.

Keywords: *intermediaries, capital market.*

Introduction

An intermediary in a stock market is a person or an organization which helps people to invest their money in various company stocks. A person involved in such intermediary activities is usually called a fund manager.

Trading has become easy as pie with the advent of technology. But from the time you place a trade to the securities getting credited to your Demat account, several entities are responsible for the seamless flow of your transaction. These entities are the financial intermediaries of the stock market. Let us learn about a few in this article.

The SEBI Act, 1992, broadly mentions stockbrokers, authorised persons (sub-brokers), share transfer agents, bankers to an issue, trustees of trust deeds, issue registrars, merchant bankers, underwriters, portfolio managers, investment advisers, depositories, custodians of securities, foreign institutional investors, credit rating agencies as 'Intermediaries of SEBI'.

Intermediaries occupy an indispensable and pivotal space in today's capital market. While some trade dealings may involve only a single intermediary entity, more complex transactions comprise networks and chains of intermediaries at different levels. These market dynamics are further complicated by proprietary dealings by such intermediaries, where the thin line of distinction between investors and intermediaries as separate market players gets diluted. In the face of such market complexities, market intermediaries often tend to put themselves in conflict of interests situations. Given the sensitive market scenario, it is imperative to keep a vigil on the growth of intermediaries, especially the new categories of intermediaries who may or may not be covered by the existing regulatory framework, particularly in the context of the new, innovative, and hybrid products that are frequently launched.

Review of Literature

There are only a few researchers regarding the effect of financial intermediaries on firm performance. Majority of researchers have conducted research on financial intermediaries on economic growth. One of the primary roles of financial intermediaries is to facilitate the provision of liquidity. Financial intermediation involves banks borrowing from a large number of agents through deposit contracts, and providing a large number of consumers and firms with liquidity. In general terms, financial intermediaries reduce the costs of search for borrowers and lenders, and facilitate the ability to trade at low transaction costs (Harris, 2003; Kyle, 1985).

Objectives

1. To identify the different intermediaries in the capital market
2. To analyse the role of intermediaries

Statement of the Problem

While buying and selling stocks seems like a straightforward process, there needs to be governing authority that ensures tight control to keep malpractices and frauds at bay. To protect the interest of investors and to regulate and promote securities markets in India, SEBI designed processes that had multiple checkpoints by creating stock market intermediaries. And they had performed their role efficiently.

Results and Discussion

A financial intermediary is an entity that acts as the middleman between two parties in a financial transaction, such as a commercial bank, investment bank, mutual fund, or pension fund. Financial intermediaries offer a number of benefits to the average consumer, including safety, liquidity, and economies of scale involved in banking and asset management. Although in certain areas, such as investing, advances in technology threaten to eliminate the financial intermediary, disintermediation is much less of a threat in other areas of finance, including banking and insurance.

Financial intermediaries serve as middlemen for financial transactions, generally between banks or funds. These intermediaries help create efficient markets and lower the cost of doing business... Financial intermediaries offer the benefit of pooling risk, reducing cost, and providing economies of scale, among others.

1. *Stockbrokers*

As per SEBI mandate, only stockbrokers can execute a trade on exchanges. So, you'll need to place your orders through a stockbroker. A stockbroker is an intermediary responsible for mediating between the bourse and the trader.

A corporate entity must fulfil the criteria laid down by the exchanges to obtain a license to become a stockbroker. Find more about the stockbroker here. To trade in stocks, you will have to open a trading account with a stockbroker.

2. *Depository and Depository Participants*

Companies allot share certificates to their investors to authenticate their partnership with the company to the extent of shares bought by them. Earlier, the companies issued physical share certificates. But they have now been converted to digital format and are transferred directly to the Demat account. This process is more convenient and transparent. Converting physical share certificates to digital format is called 'Dematerialisation', often abbreviated as DEMAT.

To ensure accessible and secure storage of electronic share certificates, Depository came into existence. They are governed and regulated by SEBI. Depositories store the dematerialised share certificates in a dedicated account called a DEMAT account. It is responsible for holding the records of all the securities in digital form and manages and regulates all the DEMAT accounts.

Like a stockbroker, a Depository Participant (DP) is also an intermediary, mediating between the Depository and investor. A DP is an agency of Depository that lets you set up a DEMAT account.

At present, there are two depositories in India,

1. National Securities Depository Limited(NSDL)
2. Central Depository Service Limited (CDSL)

3. *Banks*

You need to transfer funds to your stockbroker to buy shares. The stockbroker credits funds to you when you sell shares. For the fund transactions between you and your stockbroker, you need a bank account. Hence, banks are one of the critical intermediaries that facilitate fund transfer in capital markets.

4. *Clearing Corporations*

We know that banks establish a clearinghouse to settle mutual claims. Likewise, in capital markets, Clearing Corporations ensure that the trade is closed between two parties. Clearing Corporations prevent defaults by ensuring that buyers have the necessary funds to pay for their trades and sellers have the assets they intend to sell. They are the intermediaries responsible for the credibility of the market ecosystem.

The two primary clearing corporations, the National Security Clearing Corporation Limited (NSCCL), is a subsidiary of the National Stock Exchange, and the Indian

Clearing Corporation Limited (ICCL), a subsidiary of the Bombay Stock Exchange.

5. *Underwriter*

As the name implies, underwriters are entities directly associated with a company or an organization. Their primary function is to manage people and talk to them regarding investment in multiple schemes or so.

In India, for instance, an insurance company can be an underwriter. It charges a certain fee for providing you with insurance services under certain terms and conditions.

6. *Merchant bankers*

These are institutions that extend funds to a company in place of loans and share the ownership of that particular company. So, they gain a right to have a say in the corporate affairs of that organization where they have invested.

Hence, merchant bankers become a link between large organizations and external markets. For instance, in India, State Bank of India, ICICI Bank, Punjab National Bank are some of the merchant bankers.

7. *Portfolio Managers*

It can be a person or a group of people or even an institution that manages money to be traded in the stock market. These intermediaries discuss the entire plan of investment with their team or with the organization and then they trade in stocks or securities in the market.

Also, these types of Intermediaries invest in bonds, derivatives, mutual funds, etc to make more money out of their investments.

8. *Debenture Trustees*

These personnel are registered with the Securities and Exchange Board of India (or SEBI) and function based on the rules cited in SEBI Guidelines, 1993. These personnel are monitored by SEBI on their functions of creating security, complaints redressal, interest payments and debenture redemption.

They act as the connecting links between debenture holders and the organization or company whose debentures have been purchased by those holders.

9. *Sub Broker*

A sub-broker is not directly linked to the stock exchanges but is a proxy member who has the necessary knowledge to act on behalf of the trading member. He can assist trading members and also investors in matters of securities dealing.

10. *Stockbroker*

Such brokers are part of the stock market as they assist in trading of securities. Although they charge a specific fee for facilitating such trading, their work is more effective than others. One of the most viable reasons behind such efficiency is their knowledge of the stock market.

A trader lacks such knowledge and is likely to end up buying or selling securities at a higher price than it should be. In such conditions, an intermediator can help in linking the stock exchanges and traders rightfully.

The SEBI crafted a comprehensive regulatory framework encompassing all intermediary categories—the Intermediary Regulations. However, most of the provisions are yet to be notified, except those dealing with enforcement orders and procedures.

Today, intermediaries continue to be governed by the specific regulations governing each category of intermediaries, which *inter alia* include:

- The SEBI (Stock Brokers and Sub- brokers) Regulations, 1992;

- The SEBI (Depositories and Participants) Regulations, 1996;
- The SEBI (Bankers to an Issue) Regulations, 1994; the SEBI (Merchant Bankers) Regulations, 1992;
- The SEBI (Portfolio Managers) Regulations, 1993;
- The SEBI (Registrar to an Issue and Share Transfer Agents) Regulations, 1993;
- The SEBI (Underwriters) Regulations, 1993.

Based on the functions and areas the intermediaries perform their tasks, they are divided into specific categories, that are listed below :

Agents and Brokers

These are personnel who are directly associated with the organization or stock exchanges. They function to link the buyer and sellers. Agents and brokers also handle the necessary paperwork.

Distributors

They are appointed by the manufacturing company directly and act as a link between the wholesalers and the company itself. For instance, businessmen purchase from the company and distribute it to the wholesalers for further selling.

Retailers

These are the connecting links between the consumers and wholesalers. Their job is to purchase goods from wholesalers and sell it to the end-customers.

Resellers and Wholesalers

Wholesalers purchase from distributors and sell it to multiple retailers. They buy goods in bulk and sell them after that to other businesses or retailers.

Functions of Financial Intermediaries

A financial intermediary achieves the following functions:

- As said before, the principal function of these intermediaries is to transform savings into investments.
- Intermediaries like commercial banks, deliver storage facilities for cash and other liquid assets, like precious metals.
- Providing short and long term loans is a primary function of financial intermediaries. These intermediaries receive deposits from customers having surplus cash and then lend them to entities in need of funds. Intermediaries give the loan at interest, part of which is given to the depositors, while the balance is reserved as profits.
- Another key function is to support customers in increasing their money through investment. Intermediaries like mutual funds and investment banks use their expertise to offer investment products to support their consumers, maximize returns, and diminish risks.

Some of the significant roles of intermediaries include:

- Link households to the financial market
- They safeguard customers' hard-earned money
- Financial advisory services, provide financial information, and engage in credit rating
- Reducing the cost of business by offering economies of scale to business owners
- It helps corporations optimize the capital structure
- by obtaining an appropriate mix of equity and debt
- Stimulate economic development

Advantages of Financial Intermediaries

- They help lower the risk of a customer with surplus cash by dispersing the risk via lending to several people. Also, they methodically screen the borrower, thus, reducing the default risk.

- They help in managing time and cost. Since they deal with a large number of clients, they relish economies of scale.
- Since they deal with many services, it helps them serve their customers by providing customized services. For example, banks can tailor loans for small and long term borrowers or their specific needs. Similarly, insurance companies modify plans for all age groups.
- They gather and process information, thus reducing the problem of asymmetric information.

Conclusion

In the capital market, transactions go through three phases—trading, clearing and settlement. SEBI has designed processes to ensure that at every stage there is minimal chance of fraud or a scam by including the above mentioned intermediaries to increase transparency and reduce risk. The role of intermediaries in the capital market is defined to make investors feel secure and boost securities market in India.

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