❖ Get an Overview of Primary and Secondary Markets

➢ Primary Market and Secondary Market

Companies raise short term funds through the money market. But when the requirements are for long term, this is where the capital market comes in picture. The capital market comprises of primary and secondary market.

Now let's understand in depth about the primary and secondary market and what the difference between primary and secondary market is.

➢ Primary Market and Secondary Market

Primary market is a place where securities are issued by the company for the first time to general public for raising funds in order to fulfill the long term capital requirement. Issues are made in various forms like public issues, offer for sale, rights issue, bonus issue, issue of IDR, etc.

While secondary market is a place where existing securities like shares, debentures, bonds, options, commercial papers, treasury bills, etc. are traded amongst investors. It is like an auction market where the trading of securities is done through exchange or a dealer (OTC).

➢ Features of Primary market

- Primary market is a market for creation of long term capital.
- Fresh issue of securities takes place in primary market.

➢ Features of secondary market

- Secondary market facilitates the liquidity and marketability of existing securities.
- Secondary market ensures a true and fair dealing for protection of the investor's interest.

➢ Difference between primary market and secondary market

The difference between the primary and secondary market mainly relates to the nature of financing and the organizations involved. The basic differences between the two types of market are as follows:

- The securities that are formerly issued in a market are referred to as primary market, whereas, when the company gets listed on a recognized stock exchange for trading, then the stocks are traded in secondary market.
- Primary market is also known as a new issue market and the secondary market is known as after issue market. Depending upon the demand and supply of the securities traded the prices in the secondary market vary. While in primary market the prices are fixed.
- The primary market provides financing to the new and the old companies for their expansion and diversification while the secondary market does not provide financing to companies as they are not involved in any transactions.
- In primary market the investors can purchase the shares directly from the company, whereas in secondary market, the investors buy and sell the securities (shares and bonds) among themselves.
- In case of primary market, investment bankers do the selling. Conversely in secondary market, the broker acts as an intermediary while the trading is done.
- In primary market, the company will gain from the sale of security. While in secondary market, investor will gain from the securities.
- The securities in the primary market can only be sold once, while in secondary market it can be done an infinite number of times.
- The amount that is received from the securities becomes the capital for company whereas; in case of secondary market same is the income of investors.
- Hence, from the above pointers we conclude that the two financial markets (primary market and secondary market) play a major role in the mobilization of money in the country’s economy. The primary market encourages a direct interaction with the company and the investor. While, secondary market is where brokers help out the investors to buy and sell the stocks among other investors.

The process to buy Equity in secondary market is very easy. The following procedure is followed while buying or selling shares in the secondary market:

- Open demat account with a depository participant (DP).
- Open a trading account with a broker.
- Link your bank account with demat and trading account.
- The broker buys or sells the shares by executing orders on the electronic terminal provided by the stock exchange.
- A contract note is issued by the broker detailing the value of shares purchased plus his brokerage cost.
- The broker collects shares via settlement process (T+1) and makes payment on the behalf of investor.
- Order gets executed on the final settlement date (T+2).

I hope the above details clarified your doubts and made you understand the concepts of primary market and secondary market. Now as you know about the primary and secondary market you will also be interested to know that there is also a third market and forth market, but these are rarely been heard. In the third and the fourth market transactions happen between the dealers and the brokers and the large institution of high volume using Over the Counter (OTC) network.

The third party caters the transactions between dealer or broker and the large institution, but the fourth market caters only the transactions between large institutions. The transactions happening in these markets are always of high volume.

Primary Market and Secondary Market – How do they work?

Stock markets are an important component of the financial system. It is a powerful tool that works like an auction for the exchange of capital/credit and has two autonomous and indivisible segments: Primary Market and Secondary Market.

In financial words, Stock Markets can also be defined as a procedure that permits people to trade in stocks and bonds, commodities, etc. which facilitates:

- Issue of new shares (IPO)
- Raising of capital (IPO, Bonds)
- Transfer of risk (Derivative market)
- Transfer of liquidity (Money markets)
- International trade (Currency markets)

In this article, we are going to discuss the primary and secondary market in order to under how stock market exactly works. Let's get started.

1. Primary Market

The primary market is a market for new issues i.e. Market for fresh capital. It provides a sale for new securities. The primary market provides an opportunity to issuers of securities like government and corporations to raise resources to meet requirements of investment or, discharge some obligation.

The corporate entities mainly issue debt and equity instruments (shares, debentures) while the governments issue debt securities (treasury bills). The issues might be released at face value or, at a discount/ premium which later molds into various forms such as equity, debt, etc. However, these issues can be released in both domestic or, international markets.

The primary market issuance is either done through public issues or, private placement. When an insurance of securities is made to new investors for becoming part of shareholders' family, it is called a public issue. The public issue can be further classified into:

- **Public Issue:**

— **Initial Public Offering (IPO):**

IPO takes place when an unlisted company makes either a fresh issue of securities. This flags off an avenue for listing and trading of the securities issued in the stock exchanges.

— Follow-on Public Offering (FPO):

An FPO takes place when an already listed company makes either a fresh issue of securities to the public or an offer for sale to the public, through an offer document.

- **Private Placement**

When an issuer makes an issue of securities to a specific group of persons where the number of members should not be more than 49, it is called a private placement. However, it is neither a rights issue nor a public issue. Private Placement of shares by a listed issuer can be of two types:

— Preferential Allotment

When a listed issuer issues shares or convertible securities, to a selected group of persons in terms of provisions by a regulatory body, it is called a preferential allotment. The issuer is needed to adhere with diversified provisions which include disclosures, pricing, lock-in, etc.

— Qualified Institutional Placement (QIP)

When a listed issuer issues equity shares or, securities convertible into equity shares to Qualified Institutions Buyers only in terms of provisions of the regulatory body, it is known as Qualified Institutions Placement.

2. Secondary Market

The secondary market allows participants who clasp securities to acclimatize their holdings according to the changes in their evaluation of risks and returns. Once the new securities are issued in the primary market, they are traded in the stock (secondary) market up and onwards from the listing day. The listing of stock enables liquidity and earning of reputation.

The secondary market operates through two channels and they are Over-The-Counter (OTC) Market and the Exchange-Traded market.

OTC markets are informal in nature where the execution of trades has a negotiable option. Most of the government securities are in the OTC Market. In addition, all the spot trades where securities are traded for immediate delivery and payment also take place in the OTC market.
The other option is to trade using the infrastructure provided by the Stock Exchanges where financial instruments are dealt with in money transactions. The four important participants of the securities market are the investors, issuers, intermediaries, and regulators.

1. Investors can be broadly classified into retail investors (HNI, minuscule investors) and institutional investors (banks, insurance, mutual funds, FII, etc).
2. Issuers include governments, corporate, financial institutions, etcetera.
3. Intermediaries include stock exchanges, stockbrokers, depository, custodians, merchant bankers, FII, mutual fund houses, debenture trustees, etc.
4. Regulators include Central Banks.

- **Components of the Secondary Market:**

The securities market is classified into the following markets and further different types of instruments are traded in these markets.

1**. Cash /Equity Markets**:

The equity segment allows dealing in shares, debentures, warrants, mutual funds, ETFs.

2. **Equity Derivatives Market:**

The derivatives segment allows trading in derivative instruments. It is a product whose value is derived from the value of one or more basic variables and is called bases (underlying asset, index). The underlying asset can be equity, forex, commodity or, any other asset. There are two types of derivatives instruments (futures & options).

3**. Debt Market:**

The debt market consists of bond markets that provide financing through the issuance of bonds.

4. Corporate Bond Market:

Bonds issued by firms are Corporate bonds and are issued to meet needs for expansion, modernization, restructuring operations, mergers, and acquisitions.

5. Forex Market:

The foreign exchange market(currency, forex, or FX) is where currency trading takes place. Currently, the Forex market is one of the largest and most liquid financial markets in the world and includes trading between large banks, central banks, currency, speculators, corporations, governments, and other financial institutions.

6. Commodity Derivatives Market:

Commodity markets enable the exchange of raw or, primary products. Raw commodities are traded on standardized commodities exchange in which they are purchased and sold in well – defined contracts. The trading in gold, silver and agricultural goods are also facilitated under this market.