DEVELOPMENT OF CAPITAL MARKET AND ITS IMPLICATIONS UPON THE ECONOMIC DEVELOPMENT

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Abstract
This work is conceived as a comparative study regarding the occurrence, development and implication of the capital market in the economic development of states located in the area of emergent countries and of those under development. This study peruses in parallel the evolution of the emerging countries which absorb capital and those granting funds within the environment of the security markets. The study's purpose is to prove the capacity of a well developed capital market to generate economic growth and, moreover, durable economic development. The data grounding this study, used as well in previous personal research, support the hypothesis according to which the capital market can and must represent a viable alternative for the funds' capitalization before the market of short term titles.

Keywords: *capital markets, economic growth, financial systems, banking system.*

Introduction

Our work mainly endorses a comparative study upon the emergent and under development countries which have developed a financial system based on the capital market and of the countries where the financial system has been controlled by banks' development. The study plays a significant role in researching the consequences related to the place and role of the capital markets within the ensemble of the financial mechanisms. In terms of the place occupied by the capital market within the ensemble of financial mechanisms, we mention that there cannot be drawn a firm border of its range. Thus, the differences between the financial market, capital market and monetary market are entailed by each country's legal regulations with respect to the financial instruments used, which require distinct features and distinct operators for each individual market.

It is well known that, according to the Anglo-Saxon economic doctrine, the capital market is identical with the securities market and differs from the financial market and monetary market. Thus, the capital market and the monetary market are comprised by the financial market. In such context, the capital market is deemed as being the financial system where international organizations, trading companies and the government may invest substantial amounts of money or may borrow/lend capital; also, natural persons are entitled to make profitable investments on medium and long term.

On the other hand, the monetary market finances the capital needs on short term or keeps the financial surpluses on periods with due dates shorter than one year.

In line with the continental European experts, both the financial market and the monetary market are elements of the capital market. This fact is due to the theory, according to which the capital is divided in physical assets (lucrative technical capital), financial assets (valuable papers which certify the ownership right upon the technical capital) and monetary assets (financial capital). Therefore, the capital market comprises the following elements: the financial market where the issuance, placement and negotiation of securities, is carried out and the financial market, having the role to attract and keep available funds in the company, on medium and short term. The

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operators, specific for this market, different from those acting on the financial market are the central bank, commercial banks and other financial-banking type institutions. Also, the capital market includes the mortgage market, which operates with financial resources necessary, specially, to the housing construction.

According to the regulations in force in Romania (the law no. 52/1994 and no. 297/2004 regarding the capital market, securities and stock exchanges), the capital market is an element of the financial market. Taking into account the Romanian legislation for this field and its specific operators, the structure of the capital market is as a network of relations, mechanisms and efficient allotment levers of the available financial resources, accessible to the economic agents and the state.

Literature review

These aspects are researched, relating firstly to the Romanian literature and to the foreign one, which equally comprise the capital market within the financial market and, on the other hand, they see it as a global market arising from the financial and baking markets, such: Anghelache Gabriela, „Bursa si piata extrabursiera", 2000 or Basno, Cezar August, Nicolae Dobrache, Floricel Constantin – „Moneda, credit, banci", 1997. The best management of the "capital market" term is meat at Stoica Victor, Galiceanu Mihaela, Ionescu Eduard, - „Piete de capital si burse de valori", 2001. By means of this approach, its authors get the closest to the foreign literature represented Laporta, Rafael; Lopez-de-Silanes, Florencio; Shleifer, Andrei; and Vishny, Robert W. "Law and Finance," Journal of Political Economy, December 1998, Levine, Ross. "Law, Finance, and Economic Growth", Journal of Financial Intermediation, January 1999 as well as Demirgüç-Kunt, Asli and Maksimovic, Vojislav. "Law, Finance, and Firm Growth," Journal of Finance, December 1998.

The clarification of this aspect has deep connotations, meaning that we perceive the economic development of a state related to a global financial-banking market in a way and in a different way if we compare the same development with a sector of the financial market.

1. The connection existing between the capital market and the economic growth

There is an inseparable liaison between the economic development of each human society and the way that society's institutions function. Specialists associate economic development with the industrialization level of a country and with the development and modernization degree of that country's agriculture. Also, economic development is often mistaken for economic growth, although these two terms have a relation similar with the one between entirety – part, such development automatically implying the growth of all economic markers. However, not any economic growth implies development.

The economic growth, in a wide sense, comprises the multitude of quantitative, qualitative and structural transformations occurred within a state's economic life. Such transformations are followed throughout a long period of time as they follow the ascendant evolution of the agreed economic markers. The compatibility between the results of the economic growth and the social and ecologic ones becomes the essential criterion of economic development. Thus, we may consider that economic development implies the existence of deep mutations within manufacture technologies, within the organizational mechanisms and structure of the economy's functioning, within the human way of thinking and behavior. Moreover [1], a durable economic development is the form or type of development which blends in a harmonious and balanced way the fulfillment of economic growth, the environment protection, social justice and democracy. Therefore, we may, by means of this definition, to deem that there is a series of elements or vectors of the economic growth, such as:

- Re-sizing economic growth taking into account the preservation of natural resources;
- A better satisfaction of needs of work, food, energy, water, housing and medical care for all the inhabitants of a country;
- Preservation and increase of a basis of material and human resources that any state has;
- Technological reorganization and control over its risks;
- Integration of decisions regarding economy and environment within a sole process;

It is understood that these elements and vectors of economic development are generally considered given the existence of major differences according to each country's particularities and features. That's why our specialists' opinions are different regarding the Romanian economic development. On one hand, it is considered that the economic re-launching may be ensured by: macro-stabilization strengthened by reorganizations on microeconomic level; stringent need of investments for the reorganization of existing economic units and stopping of financial indiscipline and granting of non-performing loans. On the other hand, notorious economists deem that the Romanian economic development should "borrow" successful methods from other states' experience, emphasizing the development of infrastructure, tourism and encouragement of investments in small companies with risk capital. What matters in the purpose of the present paper is the existing liaison between the capital market, as financial institution which may ensure the investments' increase and how such market helps a country's economic development.

The capital market, by means of its organization and functioning, has a significant role in the economic development progress. The level of such markets has become a standard of the development level of the emergent countries and under transition towards the market economy. International organizations, such as the World Bank and the International Monetary Fund, by their characteristic action means, promote a series of guidelines on behalf of the establishment of functional market economies, including by the support they provide for the capital markets' establishment. It is known that the capital market may ensure financial resource allotment forms on the level of economic agents and, in parallel, to stimulate their economies and, thus, a series of long term measures can be identified regarding the financial services' development and modernization [2].

1. to ensure the financing preponderance by means of the capital market related to financing by banks;
2. to develop institutional investors, including privately managed pension funds;
3. to create all the circumstances necessary for the development of stock markets and shareholding capitalism, to stimulate the development of the entire range of instruments and services;
4. to develop norms and corporate governing practices, according to the European and global trends;
5. to establish a sole authority for the regulation and supervision of all classes of financial-banking, investment and insurance services;

The historic evolution of developed countries point out a revolution in the capital markets field. According to Alvin Tofler in his famous work – "The Third Wave" – computer science changes dramatically the entire economy and, thus, it can be deemed if the capital market is experiencing a revolutionary process on various layers.

Firstly, the financial globalization manifested by the accumulation of huge funds available to private banks, budgetary deficits and due payments registered mainly in emergent countries transform international capital flows into a major phenomenon of the global economy. Given the desire of the capital markets to attract as many funds as possible, we are witnessing a vast opening of the national financial markets towards private funds.

Secondly, the financial revolution is manifested by deep changes in the structure of the financial instruments, weight and size of the institutional investors, transaction systems and competition manifestation. The patrimony financial instrument are becoming more divers in order to allow the financing of companies based on share issuance. Also, it is increasing the significance of high outturn bonds, deemed in the United States of America as ordinary or second-hand bonds. These bonds are called junk bonds and together with loans and municipal bonds they may wide significantly the opportunities to invest on the capital market. Regarding institutional investors, we can notice the increased degree of the investing easiness for the public at large by means of the pension and insurance funds where everyone can contribute with significant amounts. Together with the increased use of computer science for transactions, operations are carried out faster, it increases the safety of clearings and, not lastly, the transaction costs are significantly reduced. In other words, the transacting activity is becoming more efficient in parallel with the decrease of the capital costs. The de-regulation of the economy and the free competition have triggered the abandonment of the exchanges' control, restrictive measures regarding interests' rates, levy of bonds held by foreigners or fix fee system. All these measures have been taken in order to ease the capitals' circulation on global level.

Capital markets are experiencing a deep modernization process and, also, the banking system. Probably the most developed payment, clearing and saving techniques and instruments will always be held by the banking system and that's why it will be more sensitive in the event of economic and politic changes. Stock exchange analysts and practitioners of the capital market deem that the banking system is ideal for the funds' collection and their transformation into large capital deposits, for the transformation of short term deposits into long term assets with low cash flow or transfer of financial funds from risking activities with low outturn towards more risking activities, but which are profitable. In exchange, it is considered that the capital market is more anchored in the financial-economic and even social reality. This conclusion arises from the fact that the capital market adjusts more rapidly to the market's evolution by revising the assets' value and by means of the complete image discovered with respect to the listed companies. Moreover, it is assumed that in the vent of a banking crash, the economic balance is re-established herder that in the event of a stock exchange crash because banks are more sensitive to political interferences and population psychosis. This can be proved easily in our country and maybe even better in Bulgaria, where a crisis of the banking system, very sensitive to the information which should not have been published, has severe consequences on long term. It could be a matter of perception, as it is known that in a transition economy, the society does not handle risk too well (aversion before risk), putting its hopes in the safety of the banking system, while in a developed economy, a population which is not so afraid of risk, undertakes easily the risk and prefers the stock exchange system.

The crucial issue of the secondary market is its credibility, how investors and the business world, generally, credit the stock movement. We have here the field of the symbolic values which need a real business basis to be viable economically because, otherwise, the businesses' instability generates the speculative trend. On one hand, if the market functions, titles are bought and sold, thus acquiring an economic support; on the other hand, if the titles are transacted, they support and develop the market. But this virtuous circle may transform into a "vicious" one when the market "does not function": titles loss their value; and when the market crushes, valuable papers may become mere papers and the speculative trend may lead to a stock exchange crash. These crashes are significantly felt when a country's economy is fragile.

In this respect, the secondary market must fulfill a series of **requirements** in order to complete it role, such as:

▪ Cash flow, namely lots of available funds, on one hand, and financial assets, on the other hand. The cash flow ensures the permanent functioning of the market and this is a condition for the uninterrupted accomplishment of the general economic circuit;

▪ Efficiency, namely the existence of mechanisms for operative accomplishment regarding transaction costs as low as possible because such costs affect the attractiveness degree of the assets;

▪ Transparency, respectively direct and fast access to information important for the holder of financial assets. Transparency is a condition of efficiency and, thus, it reduces transaction costs;

▪ Free market is tightly connected to transparency. In principle, complete information is sufficient in order for the market regulation mechanisms to be able to act. In practice, it is necessary the creation of a strict frame for the transaction's regulation, for counter-acting the trend for market manipulation and the establishment of a proper frame for the free competition;

▪ Adaptability, which implies the prompt answer of the market to the new economic extra-economic conditions, new opportunities; a financial market is efficient if it is innovative, if it finds new ways to reply to the demand and supply characteristics and of the norms established within the general economic system.

Drawing a conclusion, we can say that the stock exchange is a *sine qua non* condition for the existence of a viable and efficient market economy.

2 Occurrence and development of the capital market on global level

Occurrence of capital markets

The developed capital markets are beneficial for the national economy of the host-states. They increase the economic performances making available for companies new ways to attract capital against low costs. These companies can develop faster because they do not rely on the domestic financing.

One of the advantages of the developed capital markets is the one that, in these countries, companies are less dependent on the banking financing which leads to the decrease of the loan risk. Financial markets allow companies to rely more on securities and less on debts instruments, creating a les risking financial structure in the event of economic crisis.

Not lastly, capital markets increase the efficiency of the corporate investments and management by means of corporate governing. In general, a mixed policy based on banking agency and capital market leads to the increase of the economic degree development.

Capital markets are not newly formed in certain countries in transition - Warsaw Stock Exchange was opened in 1817 and Prague Stock Exchange in 1871. But, due to socialist systems, all capital markets were closed; throughout the passage from planned economy to market economy, these have been reestablished in 20 of 26 economies in transition. They have been used to list mandatory shares of the companies under mass privatization and less for the initial public shares' sale offers.

The first capital markets in countries under transition appeared in 1999, followed by Bulgaria, Lithuania, FYR Macedonia, Moldova and Romania. The main characteristic of the first group of markets was the transfer between investors, attendees to the mass privatization of state companies, ownership rights. In the beginning, these markets listed a large number of shares, lots of them being fixed. Once these markets became more stable, the number of listed shares decreased and the shareholding structure became more focused. Some economists such as Claessens and Djankov claim that it was the case of the Czech Republic and similar patterns can be found in the main countries which have adopted the mass privatization process. However, the economists Earle and Telegdy have found few evidences of a focus of shareholding on the extra-stock exchange Rasdaq in Romania.

Recent research has shown that the markets of mass privatization have been poorly understood by foreign investors who found out later that published information was not enough or complete and that they did not have the means to fight against illegalities as the legal frame was undeveloped. In some countries, these foreign capital flows seem o have slowed down the focusing process of the ownership rights.

The second type of markets – occurred in Croatia, Estonia, Hungary, Poland and Slovenia – have listed a small number of shares by means of initial sale offers (the shares were moderately transacted).

A third group of capital markets was established in 7 countries under transition - Armenia, Azerbaijan, Kazakhstan, Kurd Republic, Russia, Ukraine, Uzbekistan – and were a mixture of the two types. All these countries initiated mass privatization processes, but the initial share exchange was carried out outside the capital market. Some companies under the mass privatization process were listed publicly, but such listing was not mandatory for all companies. In several countries (Kazakhstan, Kurd Republic), it was pursued the development of the capital market and mass privatization in parallel. During the privatization, the capital markets formed by means of the public sale/purchase offers of the companies whose major shares were sold to strategic investors. The government listed a small number of company shares, thus being created a highly varied shareholding structure.

Finally, 6 economies in transition - Albania, Byelorussia, Bosnia-Herzegovina, Georgia, Tajikistan and Turkmenistan – have not established capital markets.

Evolutions in Europe

In Europe, the evolution of the capital market has become, in a certain way, convergent with the one of the United States of America, by means of the fact that the European economy has been influenced by the implementation of the sole currency – euro, on one hand, and by the expansion of the globalization process, on the other hand. In this environment, the European companies are trying to strengthen their position on the market in order to exploit the European and global financial potential. European companies have depended on the banking system with respect to the foreign financing sources. For instance, at the beginning of the 80's, over 80% of the foreign financing of the continental European countries was carried out by means of the banking system, and the trading effects were almost inexistent. But this situation has changed in 25 years and at present the financing by issuance of shares and bonds exceeds the foreign financing provided to companies by the banking system. Obviously, among securities, the shares issuance is preferred as financing source, made for the capital increase, an increase of almost 30% per year from 1995 to 2000.

Later, after 1998, the value of the bonds issued by companies has become increasing (from 18% in 1998 to 58% in the following year), which highlights a higher absorption capacity of the companies. This is point out by the stock exchange capitalization in the domestic gross product in 1999, year when several countries reached record levels, such as Finland with 272%, England with 206% or Luxembourg with 192%. In 2000, transactions on the European markets recorded a very high quota. These aspects point out the fact that the European capital market has developed very late (compared with the United States of America), being tributary to a "emerging shareholding culture" or that it has been preferred the development by means of the banking system.

After 2000, there have been registered certain trends regarding the development of the European capital markets. Firstly, significant increases of the securities transactions and shares demands, noticeable by means of the fact that the number of direct number of shares increases and, as well, the weight of the shares in the investment funds' structure. Secondly, the capital markets become international together with the preference for European national instruments due to the economic and legal difficulties occurred upon the issuance, transacting and clearing of securities on international level. Other trends consisted of competition sharpening and collaboration between stock exchanges and transacting systems, noticing a higher pressure of the capital markets regarding the strengthening of the compensation and clearing activities and registration of an increased instability of the financial assets' prices.

For the last decades the experience of emergent countries in Latin America and Asia proves that many countries, which have initiated a strong offensive regarding the economic reform and modernization, have been successful in the development of the capital markets and stock exchanges, with favorable effect over markets' capitalization and companies' financing input.

It has been said, based on the actions carried out by international companies, that developed capital markets offer an increased degree of financing, reduced capital costs, higher cash flow and good name. When companies in the emergent economies use deposit certificates GDR or SDR or they list their shares on the capital markets in the USA, their financial restrictions loosen up – and this means that new investments are less sensitive to international cash flows. Moreover, domestic companies which enter international markets obtain better financing opportunities and may increase their debts' due dates. Transactions on foreign markets have an increased cash flow than on local markets. For instance, Mexico's shares based on the American deposit certificates ADR are transacted more in New York than on local markets, having multiple benefits for investors.

Due to the fact that the rules of corporate governing are stricter for international listings, companies have addressed to them to signal that they intend to protect the right of minor shareholders. Companies in countries with weak legislation regarding corporate governing are willing to list their titles on other foreign markets as well if they are allowed to. By listing on foreign markets (especially the USA), corporations undertake to act on behalf of the investors and to reduce the costs of loans, to increase the investors' welfare.

Newly established Internet companies from Latin America and Israel establish their legal headquarters in the USA to ease capital access. Simultaneous listing on multiple markets becomes easier and due to the new international accountancy regulations, announced by IOSCO – the International Organization for the Settlement of Capital Markets. These standards endorse multinational companies which list and offer their shares publicly and simultaneously on multiple markets.

These trends are influenced by the IT technologies which allow the players of the capital markets easy access to transacting systems from their terminals.

Transactions are going to be more and more carried out electronically and they are no longer connected to a particular location. The computers of the Nasdaq markets are located in Turnbull, Connecticut, but traders are worldwide.

Electronic communication networks have been established recently. These networks have begun by integrating on the existing markets as "cash flow pools", but, more and more, they are transforming into alternatives of regular transactions. A large number of shares on developed markets are transacted by means of the electronic communication networks – for instance, they transact ¼ of the total transactions in US dollars on Nasdaq.

Alternative transacting systems are established worldwide, usually connected to the exiting ones. For instance, Instinet was established as a brokerage system and now it is connected to a significant number of capital markets. There are speculations that several transacting systems will be established which will allow investors to carry out transactions 24 of 24. The existing markets acknowledge that their transacting services are more and more surpassed. Observers foretell that traditional capital markets (such as NYSE) will cease their existence under their current form in order to reflect better the corporate structural changes, changes of the transacting locations and institutional organization (such as the distinction between specialized and retail brokers).

To cope with these competitive changes and the general desire to increase cash flows by means of developed markets, many capital markets in the developed countries have merged or have tight collaborations. Recent proposals address the merger of the capital markets from Amsterdam, Brussels and Paris, on one hand, and the alliances between Nasdaq and the capital markets from Australia, Canada, Japan and Hong Kong, on the other hand. NYSE has allied with Tokyo Stock Exchange, Australian Stock Exchange, Toronto Stock Exchange, Mexican Bolsa, Sao Pulo Bovespa and Euronext to carry out non-stop transactions. The strengthening of these markets – which comprise more than 60% of the international market's output – leads to the occurrence of a small number of markets of large dimensions.

With few exceptions, the economies under transition have not attended these new trends of market growth. The sole merges which have been taken place were the three "Baltic" markets (Estonia, Latvia and Lithuania), which, on their turn, connected to the capital market on Helsinki (Finland). The other countries are still implementing "made at home" strategies. International trends suggest that many of these "important substitutes" are due to fail. Even according to the most optimistic scenario, most markets of economies in transition will remain small compared to most emergent markets – not including the developed markets. Because of this, the question is if capital markets from economies in transition will be able to reach a sufficiently high level of savings to face the international competition individually or they will have to join international alliances?

To reach the level where the increasing activity on the capital market leads to the decrease of the transacting costs, they must have a capitalization level higher than USD 15 billion. Using the most optimistic scenarios from table 5, we notice that only 4 of the 6 economies in transition will reach this level until 2005 - Czech Republic (with an estimated capitalization level of USD 19 billion in 2005), Hungary (USD 16 billion), Poland (USD 46 billion) and Russia (USD 53 billion). The next markets in terms of size, Romania and Slovakia, will have, each, a stock exchange capitalization lower than USD 5 billion. This suggests that, because of their size, most capital markets from the economies in transition will not be able to face other markets in rendering transaction services. Moreover, these arguments are grounded on the existing economies.

The globalization of the capital markets increases the value of such scale economies necessary for the transacting systems to operated competitively and to provide the necessary cash flow – the accomplishment of an independent capital market is basically impossible even for those economies in transition which seem to have the appropriate dimension.

The low level of scale economies corroborates with the costs' structure of the capital markets from economies in transition. There are defined explicit and implicit costs of the shares transactions; explicit costs include fees and duties and implicit costs are indirect transacting costs (the main cost is represented by the transacting price). Even if most economies in transition do not have explicit costs which might increase the transacting prices and would reduce cash flows, the total costs of the two markets considered more developed (Budapest and Prague) are twice bigger than the average, thrice bigger than of the most developed markets in Latin America and Eastern Asia.

The conclusion is that even the most developed markets of economies in transition will face competition issues.

Capital migration from emergent and in transition economies towards international markets

Financial markets, in general, and capital markets, in particular, have experienced a spectacular growth in the developed and developing countries for the last two decades. A proper infrastructure (a higher economic growth, macro-economic stability), structural reforms (and, especially, the privatization of state companies), changes of political orientation (regarding the reforms of the domestic financial markets and the liberalization of the capital account) are vectors of the economic growth. The globalization degree, on its turn, has developed for the last two decades: cash flows are freely circulate among countries, financial markets are more integrated, higher trading representation of foreign financial organizations worldwide.

A globalization feature is the migration of the activities specific to the capital markets over border, especially in the emergent economies. Many companies in the emergent economies list their shares both on the domestic and international markets. Also, new IT technologies have sped the markets' globalization trend.

Moreover, these global trends will tone up as the access to information improves, standards – related to the corporate government, listing and accountancy – harmonize, technology develops and the connection between markets improves. These new tendencies raise new questions for countries regarding the development of their own capital market, as a way to ensure an effective use of resources and their distribution in the corporate sector.

There is a relatively small number of fundamental factors which affect both the development of a local market and the attendance on the international markets. As a country's infrastructure improves, the capital market activity increases, but, at the same extent, the activities on the foreign markets increase as well. This suggests the existence of two complementary processes.

There is a limit of domestic development associated with an increase of the activity over border. The migration of most part of market capitalization and of the transactions' volume has adverse consequences over the cash flow of the remaining companies. This large scale migration will render more difficult the support of a mature domestic market and, strictly – it refers to the fix costs for the preservation of the transacting system, clearing and liquidation operations, among others – at a greater extent – it refers to their capacity to generate enough flows for local brokers and sufficient opportunities for domestic investment banks, accountancy companies and other capital market related services.

Conclusions

Regarding Romania, the financial market has been created and comprised two main elements: the monetary market and the capital market. In a developed economy, the organization and functioning characteristic to the capital market has a definitive role in the social-economic progress. This role is underlined by the functions of the capital market in an industrialized economy, such as:

- It ensures the cash flow necessary to carry out transactions, by means of large available funds;
- It ensures efficiency, by carrying out transactions against costs as low as possible;
- It ensures business transparency and accuracy by careful information and transaction surveillance;
- It ensures adaptability, by flexible orientation of investments towards more lucrative economic fields;

From the perspective of these economic advantages, the capital markets have occurred as necessity and not as a form of mandatory completion of the banking system. The economic development and stock exchanges' occurrence are tow economic realities deeply and organically connected. The economic development implies both quantitative changes (manufacture factors, economic markers, etc) and qualitative changes. In such economic environment, people's mentality changes, desires get new manifestation forms, the concern for property and earning desire increase – and they all are ensured by financial stability. That's why an institution such as the market exchange is able to cope with these new economic requirements detailed in the present study.

[1] Dictionar de economie, editia a II-a, Editura Economica, Bucuresti 2001, pg. 159

[2] Prof. dr. Gheorghe Dolgu" Revolutia financiara mondiala implicatii pentru Romania" – Institutul National de Cercetari Economice, grupul de reflectie Evaluarea Starii Economiei Nationale

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