Public and Private Capital Markets

With debt and equity the most important instruments traded on them, capital markets are venues – nowadays increasingly frequent electronic platforms -, where savings and investment opportunities are matched between those who have capital (retail and institutional investors) and those who are in demand of capital (corporates, government-related institutions). Thereby, capital markets fulfil an intermediation function by transforming size, maturity as well as risk.

Compared to money markets, where short-term funding is raised (maturity usually less than 1 year), capital markets comprise medium- / long-term funding instruments. Neither is bank lending associated with capital markets transactions.

Whilst there are many sub-segments of capital markets, such as those for currencies, foreign exchange or derivatives, the most relevant ones are those for debt (e.g. bonds) and equity-related securities (e.g. stocks). In the debt capital markets, investors are lending funds to issuers, whilst in the equity capital markets, investors are acquiring ownership stakes in companies. - Naturally, these types of investments differ in their respective risk-reward profiles: Debt capital markets, also referred to as fixed-income markets, are foremost dealing with lending instruments providing regular income streams. From an investor point of view, they are of relatively lower risk and relatively shorter term. Equity instruments, on the other hand, represent a (permanent) portion of ownership in a company: In most cases, investors have the right to ask questions, vote in shareholder meetings and – depending on terms – are entitled to dividend payments.

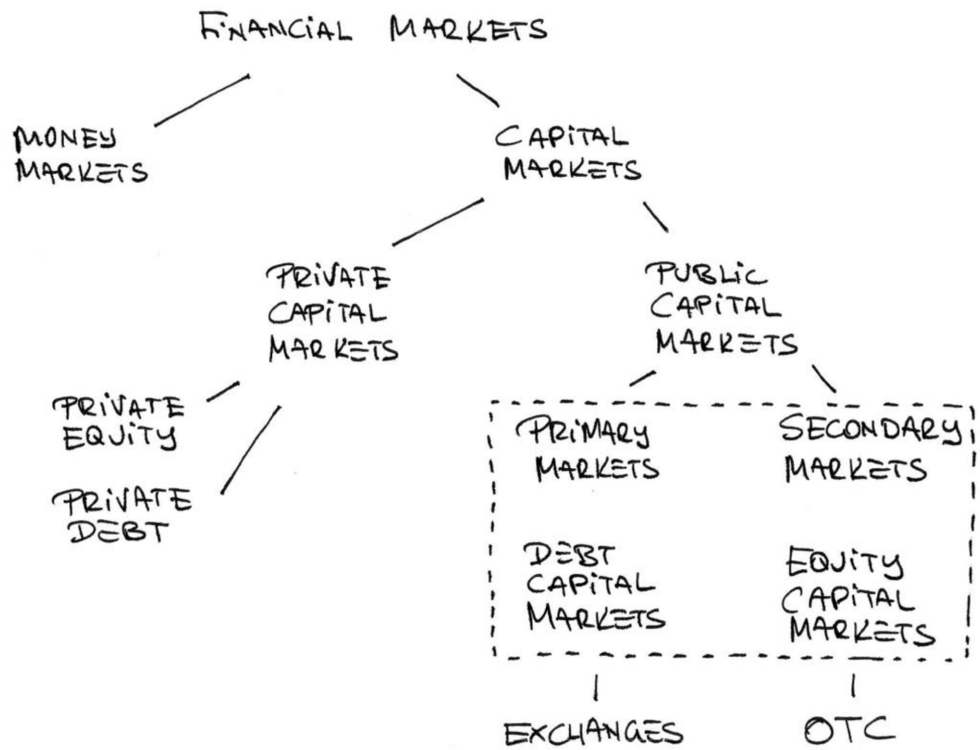
On primary markets, securities are issued and sold for the first time: Hence, investors buy securities directly from the issuer, referred to as primary offerings or initial public offerings (IPOs). In regards to stocks, the issuer may offer primary shares to raise funds (i.e. share capital increase) or secondary shares, if a current shareholder decided to exit (e.g. privatisation, monetization). When a company goes public, it sells its stocks or bonds foremost to large-scale, institutional investors (e.g. mutual funds, pension funds, hedge funds). - A secondary offering describes an equity capital markets transaction regarding a security already trading: Also in this case, the issuer may offer either primary or secondary shares.

On secondary markets, already-issued securities are traded among investors. Latter markets are particularly relevant and important, as they provide liquidity, giving investors the possibility to both, buy and sell securities.

All comments above refer to public capital markets, taking place at and being operated by exchanges: They are dealing with listed (quoted) securities and characterized by being heavily regulated and supervised by a regional securities and exchange commission (SEC).

Private capital markets, on the other hand, are neither much regulated nor provide much (if any) liquidity, with a secondary market practically non-existent: **The so-called private placement market allows companies to raise funds through unquoted securities, which are directly sold to investors. Therefore, this market is regarded as risky, because it** is almost impossible **f**or an investor to exit an investment before it matures. Not least due to lower standards of disclosure in private capital markets, they are only deemed appropriate for institutional investors, family offices or high net-worth individuals, not for retail investors, though.

An over-the-counter (OTC) market is a decentralized market. There, participants trade securities and other instruments directly between each other - without involving a central exchange or broker. Whilst most exchanges do have physical locations (e.g. NYSE – New York, LSE – London), trading on OTC markets is conducted electronically. There, dealers act as market makers by quoting prices at which they are willing to buy and sell, whereby a trade may be executed without others being aware of its respective price. Hence, OTC markets are less transparent than exchanges, they are also subject to fewer regulations.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