

Financial Instruments in the Capital Market

Financial instruments in the capital market are the various types of assets or securities that are traded to raise funds for businesses, governments, and other entities. These instruments are primarily used for long-term financing, and they come with varying levels of risk, returns, and time horizons. Here's a detailed explanation of the key financial instruments in the capital market:

1. Equity Instruments (Stocks):

- **Common Stocks:** Represent ownership in a company, offering dividends and voting rights. Higher risk with potential for high returns.
- **Preferred Stocks:** Offer fixed dividends and higher claim on assets than common stocks, but usually no voting rights. Lower risk than common stocks.

2. Debt Instruments (Bonds):

- **Government Bonds:** Safe investments with fixed returns, issued by the government.
- **Corporate Bonds:** Issued by companies, offering higher returns than government bonds but with more risk.
- **Convertible Bonds:** Bonds that can be converted into stocks, offering a mix of fixed interest and potential stock gains.

3. Derivatives:

- **Options:** Contracts giving the right (but not the obligation) to buy or sell an asset at a set price. High risk with potential for significant returns.
- **Futures:** Contracts to buy or sell assets at a future date. High risk as they must be executed.
- **Swaps:** Agreements to exchange cash flows or financial instruments, typically involving interest rates. High risk.

4. Mutual Funds and ETFs:

- **Mutual Funds:** Pooled investments managed by professionals, offering diversification. Risk varies by type (e.g., equity, bond).
- **ETFs:** Traded like stocks, tracking an index or asset. Offer diversification with lower fees and flexibility. Risk varies by underlying assets.

These instruments provide different options for raising funds and investing, each with its own risk and return profile.



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Type	Instrument	Description	Risk Level	Returns
Equity Instruments	Common Stocks	Ownership in a company, with dividends and voting rights.	High	Potential for high returns
	Preferred Stocks	Fixed dividends and higher claim on assets, no voting rights.	Moderate	Fixed income, lower risk
Debt Instruments	Government Bonds	Issued by the government, low risk.	Low	Fixed, lower returns
	Corporate Bonds	Issued by companies, higher risk and returns.	Moderate to High	Higher returns
	Convertible Bonds	Can be converted into stocks, combining fixed interest with stock potential.	Moderate	Fixed income with upside
Derivatives	Options	Contracts to buy/sell assets at a set price.	High	Potentially high returns
	Futures	Contracts to buy/sell assets at a future date.	High	Depends on market movement
	Swaps	Exchange of cash flows or financial instruments.	High	Varies based on agreement
Mutual Funds & ETFs	Mutual Funds	Pooled investments managed by professionals, diversified.	Varies	Varies by fund type
	ETFs	Traded like stocks, tracking indices or assets.	Varies	Diversified, lower fees