your questions answered

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UNDERSTANDING THE U.S. FINANCIAL MARKET - ONE OF THE LARGEST FINANCIAL MARKETS OF THE WORLD IS ALSO ONE OF THE MOST COMPLEX TO UNDERSTAND

1. Can you explain as to who are the main players of the U.S. financial market?

The U.S. financial market comprises of several players such as:

(i) corporations and governments issuing securities
(ii) persons and corporations buying and selling a security
(iii) the broker-dealers and exchanges which facilitate such trading of securities
(iv) banks which safe keep assets, and
(v) regulators who monitor the markets' activities.

The U.S. system is more complex as there are multiple players in each of the above categories.

2. Who are the players in each of the above categories in the U.S.?

(i) As we are aware, securities are issued by a company or the government to raise capital either as debt or equity. Debt and equity may be issued in various forms such as bonds, notes, debentures for debt and common or preferred shares for equity. Issues may be sold privately to investors, or sold to the public via the various markets described below.

(ii) An investor is a person or corporate entity that makes an investment by buying and selling securities.

There are two sub-categories of these investors:

a) Individual person making investment in the securities for himself.
b) Institutions which make investments on behalf of a third party who is their client, such as investment and hedge fund managers.

(iii) A broker-dealer is a natural person, company or other organization that engages in the business of trading securities for its own account or on behalf of its customers.

All broker-dealers must be registered with the **Financial Industry Regulatory Authority, Inc.** (FINRA) or a national securities exchange or both, depending on the securities they are dealing with.

> U.S. equities, corporate and municipal bonds can be issued in certificated form, though this practice has been largely replaced due to the costs and inefficiencies of keeping them. Rather, holdings are kept as "immobilized" or "street name", with the beneficial owners keeping them in accounts at broker-dealers and banks, just as they do for currencies.

Commodity brokers include futures commission merchants, commodity trading advisors and commodity pool operators. They must register with the National Futures Association (NFA).

A stock exchange is a physical or digital place to which brokers and dealers send, buy and sell orders in stocks/shares, bonds, and other securities.
In the USA, there are several exchanges and within the same exchange there are several markets depending on the type of securities or commodities to be traded.

The following are the U.S. Exchanges for equities, options, futures and derivatives:

a. For Equities - There are multiple exchanges in the U.S. such as the New York Stock Exchange (NYSE), National Association of Securities Dealers Automated Quotations (NASDAQ) and BATS Global Markets.
b. Options on equities - Similar to equities, but including the Chicago Board Options Exchange and the International Securities Exchange.
c. Futures and derivatives - The Chicago Mercantile Exchange, including its acquisitions of similar exchanges, is the sole venue for many derivative contracts that must be cleared at the same exchange.
d. Energy related derivatives - The Intercontinental Exchange dominates energy related derivative trading, again with its own clearing arrangements. This exchange is owned by NYSE.

It must also be noted that the U.S. government debt securities do not trade on exchanges. They are bought by primary dealers and resold to other broker-dealers and institutional investors.

(iv) The next players in the security market are the banks and such other institutions that are the custodians of the securities for safe keeping.

There are four main players:

(a) Custodian banks - They offer active safekeeping and administration of clients' securities portfolios.
(b) Prime brokers - They are broker-dealers who offer custody and other services to hedge funds.
(c) Transfer agents - They provide a variety of services to issuing companies, including maintaining a registry of all shareholders, paying dividends and conducting proxy campaigns.
(d) Central securities depositories and clearing organisations.

There are three central securities depositories and they are -

(i) The main securities depository is the Depository Trust Company, a subsidiary of the Depository Trust & Clearing Corporation (DTCC)
(ii) The Federal Reserve for all U.S. government bonds and notes
(iii) The Chicago Mercantile Exchange (CME) for futures and other derivative contracts

There are four clearing organizations in the U.S. and they are -

(i) National Securities Clearing Corporation, a subsidiary of DTCC, for market-traded stocks and corporate bonds
(ii) Fixed Income Clearing Corporation, also a subsidiary of DTCC, for government bonds and mortgage-backed securities
(iii) Options Clearing Corporation (OCC) for all equities related options
(iv) Intercontinental Exchange (ICE) for energy related derivative contracts

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Options, futures and other derivatives are traded based on contracts, rather than certificates. OCC, CME and ICE act as clearing agents and repositories, keeping track of book entry positions among the various clearing brokers.

U.S. government bonds and notes are un-certificated (dematerialized), which means that certificates are never issued. Instead, the clearing brokers keep book entry positions at the Federal Reserve on behalf of their various clients.

The Financial Stability Oversight Council has designated each of these institutions, with the exception of the Federal Reserve, as a systemically important financial market utility.

(v) The last and most important players are the regulators.

The securities markets are overseen by -

(i) the Security and Exchange Commission (SEC),
(ii) by individual state securities commissions established under blue sky laws, and
(iii) the self-regulatory organizations, which are overseen by the SEC.

Nationally, there are two commissions regulating the trading of securities:

(a) The first is the U.S. Securities and Exchange Commission (SEC), which governs equities, equity options, corporate bonds, and municipal bonds.

The SEC is an independent agency of the United States federal government. It also holds primary responsibility for enforcing the federal securities laws, proposing securities rules and regulating the securities industry, the nation's stock and options exchanges, and other activities and organizations, including the electronic securities markets in the United States.
The SEC falls under the responsibility of the U.S. Senate Committee on Banking.

(b) The second is the Commodity Futures Trading Commission (CFTC), which generally governs activities in the derivatives markets.

The CFTC oversees designated contract markets (DCMs) or exchanges, swap execution facilities (SEFs), derivatives clearing organizations, swap data repository, swap dealers, futures commission merchants, commodity pool operators and other intermediaries.

The CFTC falls under the oversight of the U.S. Senate Agriculture Committee.

3. Can you give us a brief history of the New York Stock Exchange (NYSE) and NASDAQ?

The New York Stock Exchange dates back to May 17, 1792. On that day, 24 stockbrokers from New York City signed the Buttonwood Agreement at 68 Wall Street.

The New York Stock Exchange started with five securities, which included three government bonds and two bank stocks.

Along with American stocks, foreign-based corporations can also list their shares on the NYSE if they adhere to certain listing standards.

A series of mergers has given the New York Stock Exchange its massive size and global presence. The company started as NYSE before merging with the Euronext and adding the American Stock Exchange.

NYSE Euronext was purchased in an $11 billion deal by the Intercontinental Exchange (ICE) in 2013. The following year, Euronext demerged from ICE via an initial public offering (IPO), but ICE retained ownership of the NYSE.

NASDAQ officially separated from the NASD and began to operate as a national securities exchange in 2006. In 2007, it combined with the Scandinavian exchange group OMX to become the NASDAQ OMX group, which is the largest exchange company globally, powering 1 in 10 of the world's securities transactions.

Headquartered in New York, NASDAQ OMX operates 25 markets - primarily equities, and also including options, fixed income, derivatives and commodities - as well as one clearing house and five central securities depositories in the U.S. and Europe. Its cutting-edge trading technology is used by 70 exchanges in 50 countries. It is listed on the NASDAQ under the symbol NDAQ and has been part of the S&P 500 since 2008.

Since 2008, a number of mergers and acquisitions have made NASDAQ one of the largest exchange companies in the world.

4. What is the difference between NYSE and NASDAQ?

The first difference is the place or location of doing business.

The NYSE still retains a physical trading floor on Wall Street in New York City. A significant portion of trade flows through its data center in Mahwah, New Jersey.

The NASDAQ, on the other hand, does not have a physical trading floor. At both data centers, trading takes place directly between investors seeking to buy or sell, and market makers through an elaborate system of companies electronically connected to one another.

The second difference is that for NYSE, the market opens and closes at a fixed time. It is by the auction method that NYSE stock prices are set. Before the market's 9:30 a.m. official opening time, market participants can enter, buy and sell orders starting at 6:30 a.m. These orders are matched with the highest bidding price paired with the lowest asking price. Orders for the closing auction are accepted until 3:50 p.m., and orders can be cancelled up until 3:58 p.m

The NASDAQ is a dealer market. Market participants do not buy and sell to one another directly. Transactions go through a dealer which, in the case of the NASDAQ, is a market maker.
The third difference is that at the NYSE, the job of maintaining markets falls upon Designated Market Makers (DMMs), formerly known as specialists.

At the NASDAQ, market makers maintain inventories of stock to buy and sell from their own accounts in transactions with individual customers and other dealers.

The forth difference is, it is more expensive to be listed on NYSE than on NASDAQ.

5. What is the over-the-counter market (OTC) in the U.S.?

Over-the-counter (OTC) market refers to the process of how securities are traded via a broker-dealer network as opposed to a centralized exchange. Over-the-counter trading can involve equities, debt instruments and derivatives, which are financial contracts that derive their value from an underlying asset such as a commodity.

In some cases, securities might not meet the requirements to have a listing on a standard market exchange such as the New York Stock Exchange (NYSE). Instead, these securities can be traded over-the-counter.

However, over-the-counter trading can include equities that are listed on exchanges and stocks that are not listed. Stocks that are not listed on an exchange, and trade via OTC, are typically called over-the-counter equity securities or OTC equities.

6. Can you explain who is a broker-dealer?

A broker-dealer is a person or firm in the business of buying and selling securities for its own account or on behalf of its customers.

The term broker-dealer is used in U.S. securities regulation parlance to describe stock brokerages because most of them act as both agents and principals.

A brokerage acts as a broker (or agent) when it executes orders on behalf of its clients, whereas it acts as a dealer (or principal) when it trades for its own account.

Broker-dealers fulfil several important functions in the financial industry.

These include -

a. providing investment advice to customers
b. supplying liquidity through market making activities
c. facilitating trading activities
d. publishing investment research and
e. raising capital for companies.

Broker-dealers range in size from small independent boutiques to large subsidiaries of giant commercial and investment banks.

There are two types of broker-dealers:

1. a warehouse or a firm that sells its own products to customers; and
2. an independent broker-dealer or a firm that sells products from outside sources.

There are over 3,700 broker-dealers to choose from, according to the Financial Industry Regulatory Authority (FINRA).

7. How one can become a broker-dealer in the U.S.?

The Financial Industry Regulatory Authority (FINRA) is the main regulatory authority for broker-dealers. To register, securities professionals must pass qualifying exams administered by FINRA to demonstrate their competence in the particular securities activity in which they plan to work. An individual must pass the exams prior to engaging in those areas of practice.

There are more than 25 examinations for each type of practice that professionals working in the financial industry must take.

Some of the important examinations are:

(I) Securities Industry Essentials (SIE) - general examination as a foundation course.
(ii) Series 3 - National Commodities Futures Exam
(iii) Series 6 - Investment Company and Variable Contracts Products Representative Exam
(iv) Series 7 - General Securities Representative Exam

8. What are the major indices of the NY stock market?

(i) **Dow Jones Industrial Average (DJIA)**
The Dow Jones Industrial Average is an index of 30 "blue chip" stocks of U.S. industrial companies.

(ii) **NYSE Composite Index**
The NYSE Composite Index tracks the price movements of all common stocks listed on the New York Stock Exchange.

(iii) **S&P 500 Composite Stock Price Index**
The Standard & Poor's 500 Composite Stock Price Index is a capitalization-weighted index of 500 stocks intended to be a representative sample of leading companies in leading industries within the U.S. economy.

(iv) **Wilshire 5000 Total Market Index**
The Wilshire 5000 Total Market Index is intended to measure the performance of the entire U.S. stock market

(v) **Russell 2000® Index**
The Russell 2000® Index is a capitalization-weighted index designed to measure the performance of the 2,000 smallest publicly traded U.S. companies based on market capitalization. The Index is a subset of the larger Russell 3000® Index.

(vi) **NASDAQ-100 Index**
The NASDAQ-100 Index is a "modified capitalization-weighted" index designed to track the performance of the 100 largest and most actively traded non-financial domestic and international securities listed on the NASDAQ Stock Market.

Prashant Ajmera (B Sc. LL.B. (India) ICSA (UK)) is a reputed Indian immigration lawyer, NRI and Canadian citizen with more than twenty-five years of experience in the field of corporate and migration law and international trade. He assists HNIs and UHNIs in making investments outside of India in real estate, stock markets, businesses and a second passport.

In recent times he has spoken at various financial events in India on the subject, "Why and how should Indian HNIs consider investing abroad?"

He is a member of the International Bar Association (IBA) and has addressed the IBA Annual Conference as a speaker on two occasions (Cancun-2001 & Durban-2002). Over the years he has authored a number of articles for various media and publications.

In January 2019, he published a first of its kind book, "Millionaires On The Move", which is available on Amazon.in. This book explains how one can obtain a second passport through business immigration by investing in residency and citizenship programs and Start Up programs of several countries.

His second book, "How to plan for your child's foreign education in 2020ne - Myth v/s Reality", is available on Google play and Amazon.in. It is a handy reference for Indian parents who wish to send their children abroad for higher education.

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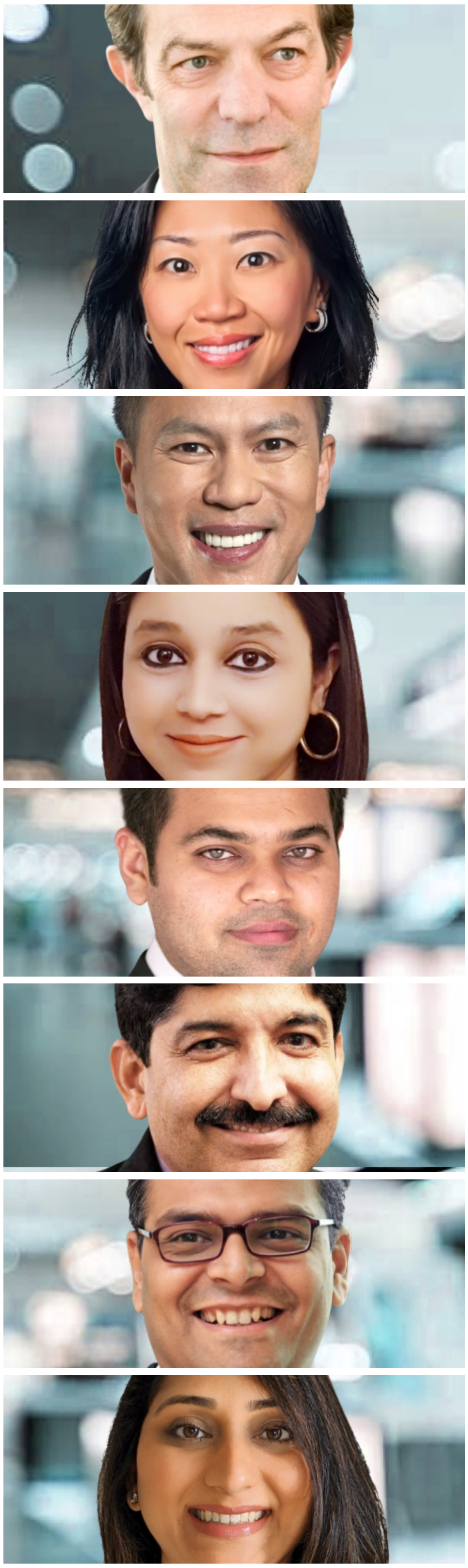

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