Wealth
Management

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Financial markets and investment vehicles

How do investment funds give you access to financial markets?

What are financial markets?

Financial markets refer broadly to any marketplace or system that is in place so that financial transactions can happen easily, legally, and with predictability, among buyers and sellers of financial securities.

A **capital market** is a financial market that facilitates the buying and selling of debt and equity securities. The most common capital markets are the stock market, the bond market, and the money market. A stock market is where shares of publicly traded companies (equities) are bought and sold. A bond market is where debt securities (fixed income) are bought and sold. The money market refers to short-term debt securities, with 12 months or less until maturity.

There are three participants in capital markets: financial intermediaries, buyers and sellers.

Financial intermediaries act as the middleperson or the institution facilitating the transactions between buyers and sellers (e.g., commercial banks, investment banks, brokerage firms, mutual funds, pension plans and insurance companies).

Buyers are the investors who have cash and want to invest in securities to potentially generate a return.

Sellers are either other investors, or the issuers of the securities, who want to use the capital markets to generate funds by issuing stocks or bonds. Some examples of issuers are federal, provincial and municipal governments, and corporations.

Financial markets are where buyers and sellers are connected, and stock and bond transactions occur. A **financial exchange** centralizes the communication and transactions for buyers and sellers. A **market index** refers to a group of securities that represent a specific market, sector, class, or investment strategy. Some examples of North American market indices are the S&P 500, TSX, Dow Jones, & Nasdaq. The performance of an investment, investment portfolio or fund, is often measured against an index.

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Investment funds

Investors can purchase securities directly on a financial exchange, or they can use investment funds to participate in the market. An investment fund is sometimes called an investment pool, because deposits from investors are combined, or "pooled" together, into one large fund. Funds hold a mix of securities, and the investor owns units or shares of the fund. Some common types of investment funds are mutual funds, exchange traded funds (ETFs), and segregated funds.

Three types of investment funds

Mutual funds: Operate by pooling funds collected from many investors for the purpose of actively investing in the capital markets. Each fund has a specific mandate to describe what types of securities it will invest in. They offer investors access to professionally managed investment portfolios for a fee.

Exchange Traded Funds (ETFs): Operate similar to a mutual fund in that they invest in several securities, but instead of buying into the fund, you purchase shares of ETFs on a stock exchange. Often ETFs hold securities in direct proportion to an index, rather than being actively directed by a fund manager. Fees tend to be lower than mutual funds as there is less or no management.

Segregated funds: Operate the same way as a mutual fund, but they are sold by insurance companies. They offer additional protections and guarantees. Fees are typically higher because of the additional features.

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