

## Relevance and effectiveness of financial markets on quality of economic growth and mature in Iran

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**ABSTRACT:** One of the most important and determinant factors in economic growth and glory is capital account and investment inside of economy and in its pursuant, there is the financial markets and its importance impress in economy efficiency and effectiveness. In sight of economists, capital account and investment are acting the main role inside economy, so attention and investigating to this importance could be very big step on growth and glory of economy. The financial market's affects are appreciated in a time that, the capitals need to be managed and conducted, and in its pursuant they need to have economic efficiency. In permanent economic growth and economic development, we are dealing with several principles in the areas of financial markets that playing an important role in economic development by financial markets and being financial markets served up in industry, are known as the most important principles. By these describes, the financial market as itself is detected as the most influential factor in economy's mature. The purpose of this essay is that, after providing useful information in plain language to the readers about financial markets, assess the relevance and impact of financial markets on how to grow and mature in economy

**KEYWORDS:** Economy, Capital account, Investment, Financial markets, Growth

### 1 INTRODUCTION

A market is a place which brings together the consumers and supplier of merchandises and facilitates their interaction with each other. Financial markets are places in which individuals and legal persons, by paying a very small cost, can transact securities, exchangeable commodities, and in short any products for which the prices are determined by the 'supply and demand.' Here, by securities, stokes, bonds, and valuable metals, or agricultural products is meant.

Extending the definition of market, it can be inferred that markets are places where people needing capital are easily introduced to the people willing to invest it. It goes without saying that in financial markets the lender of the capital receives a receipt, called a security guarantee, from the receiver of the money to guarantee refund which is also salable. In addition to the money he/she pays, the provider of the loan expects a reward in return of his/her investment which is called interest.

In Iran, financial markets are divided into two branches, namely the capital market and the currency market. The currency market itself is also divided into two branches of primary and secondary markets. The primary market is where the capital is made and the shares are distributed and transacted for the first time. However, the secondary market is where the securities which have already been transacted in the first market are circulated.

Currency markets are made up of currency organizations which in the developing countries are mainly represented by banks. Banks and other currency organizations are the main operators of the financial system and it can be said that money depositors lend their money to the public and private institutes through such organizations; this type of investment is referred to as indirect investment. With a brief look, it can be easily discerned that our country is one of the countries belonging to this model of economy and the financial system of Iran is a bank-based one. In Iran, a number of studies have attempted to uncover the relationship between development of currency markets with the economic growth.<sup>[4][5]</sup> These studies have not been able to confirm the existence of a clear relationship between the progress of currency markets and economic growth. Also, unfortunately, the research into the negative effects of financial indexes on economy, which its main causes are lack of supervision and specialty, has been ineloquent.

## 2 THE EFFECT OF FINANCIAL SECTOR ON ECONOMIC GROWTH AND THE RELATIONSHIP BETWEEN THEM

### 2.1 THE COMPARISON OF THE GROWTH RATE OF IRANIAN FINANCIAL SECTORS WITH THAT OF OTHER PARTS OF THE WORLD

In the economical literature, the physical hoarding of currency is known as one of the important factors to reach production, growth, and development.

*Table 1 – the comparison of economic growth of Iran with other parts of the world*

Year/Regions	1960	1970	1980	1990	2000
Iran	3.8	3.3	2.4	2.4	3
Turkey	2.3	2.1	2	2.5	2.8
Africa	2.3	2.5	2.3	1.5	1.5
Latin Americas	2.4	2.9	3	3.4	3.5
South Asia	1.6	1.7	2.4	2.7	2.9
East Asia	1.8	2.9	4.1	5.7	5.8
Industrial Countries	3.9	4.6	5.1	5.9	6

As can be seen from the statistics released by the International Monetary Fund (**Table 1**), up to 2000, we had not had a satisfactory financial and/or economic growth. According to the most recent statistics from the same organizations we still do not have an acceptable financial growth rate which, of course, is mainly due to the sanctions put against our country and some other problems.<sup>[1][5]</sup>

### 2.2 THE COMPARISON OF THE DEVELOPMENT OF FINANCIAL MARKETS OF IRAN WITH OTHER MENA (MIDDLE EAST AND NORTH AFRICA) COUNTRIES

Considering the fact that the income from oil is one of the most important economic characteristics of Mena countries, comparing the economic condition of Iran with other countries in the same category will lead us toward a more accurate understanding of its economy.<sup>[1][5]</sup>

*Table 2 – the comparison of the conditions of financial markets and economic growth of Mena countries*

low	Average	high
Mauritania	Al Jazeera	Bahrain
Libya	Egypt	Jordan
Sudan	Djibouti	Kuwait
Syria	Iran	Lebanon
Yemen	Pakistan	Qatar
		Arabia
		Emirates

2.3 IN ORDER TO SHOW THE DATA TABULATED ABOVE MORE CLEARLY THEY HAVE BEEN PUT INTO DIAGRAMS HERE

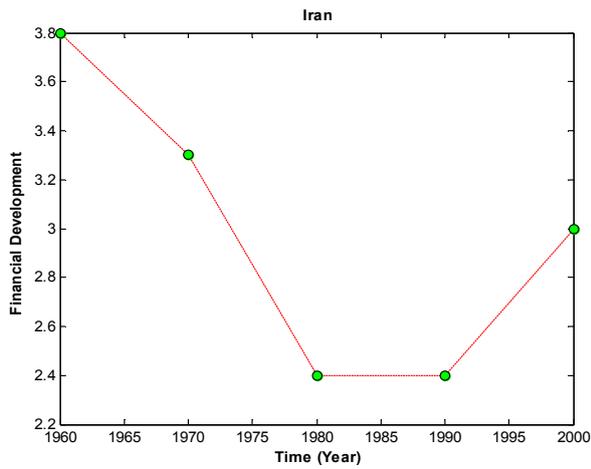


Fig.1 – Financial development of Iran

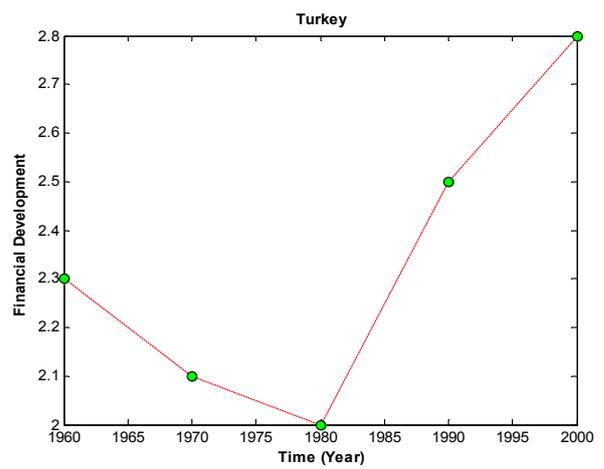


Fig.2 – Financial development of Turkey

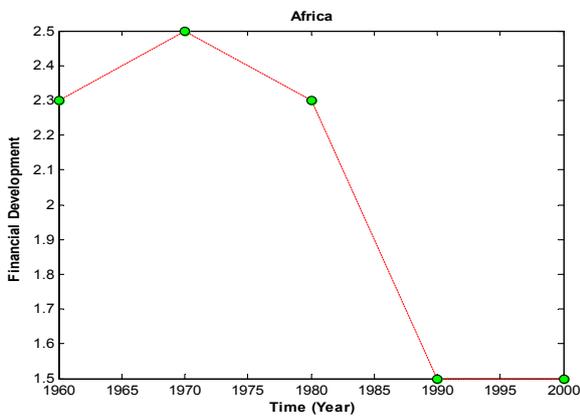


Fig.3 - Financial development of Africa

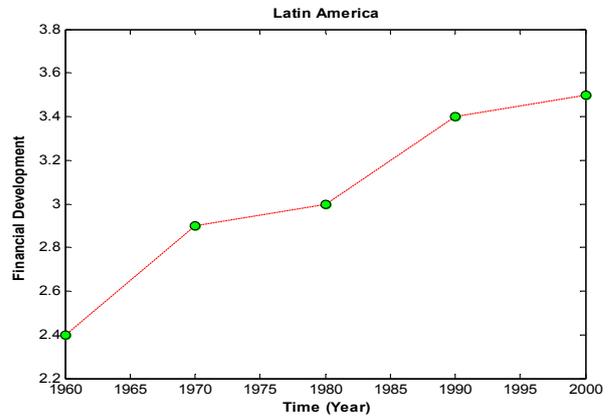


Fig.4 - Financial development of Latin Americas

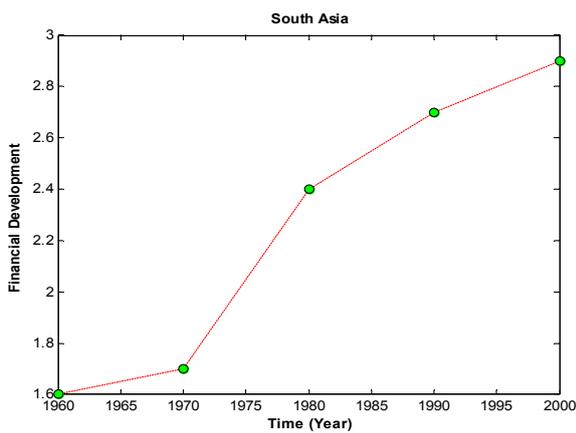


Fig.5 – Financial development of South Asia

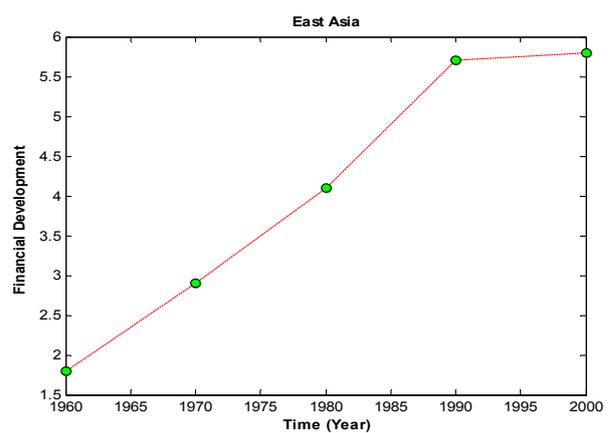
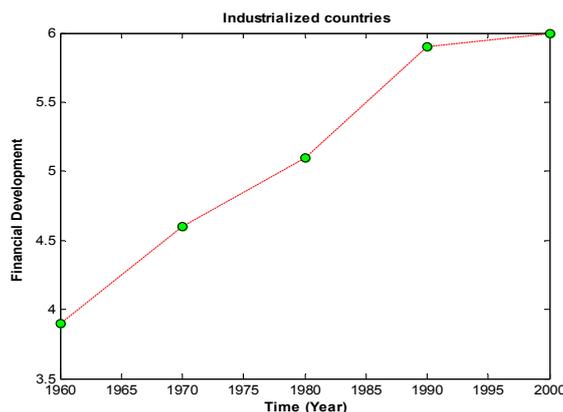


Fig.6 – Financial development of East Asia



**Fig.7 – Financial development of industrial countries**

The results from these tables show that Iran does not have a favorable condition with regard to its financial markets and economic growth and, by looking at the diagrams above (Fig.1 to Fig.7), it can be easily inferred that in order to fulfill the goals brought in the National Perspective document we must have a correct and proper planning. "[8]"

### 3 THE FUNCTIONS OF FINANCIAL MARKETS

The functions of financial markets are as follows:

- The transfer of the extra money from the families interested in investment toward people or organizations who require the money (actually, based on the definition of the market the relationship between these entities is made easier through the market).
- Equipment of saving

Now, this question rises that while our country has the highest amount of deposited money among the Middle Eastern countries, why should its economic growth be among the lowest ranks compared to other countries mentioned above?

- Proper identification of the capital and helping the process of price discovery

The price of currency and capital is determined in the market. By determining the price, the financial market helps the financial establishments in making decisions about investment and planning and makes it possible for them to compare the price of the capital with their profit expectation. This way, the establishments can allocate their capital to the investments for which there is higher or equal return rates. Also, by determining the price of the capital in the currency market, the comparison of the choices of long- and short-term investments becomes feasible. However, the process of identifications of the right prices is only possible when there is a state of competition in the market. Only under such circumstances the supply and demand of money will determine the price appropriately. Provided that the prices are determined in this way, they can provide the best guide for the providers of the capital (i.e. the money depositors) and the investors, or the borrowers, of the money. Under such circumstances, the making of decisions will be much easier for the both parties of depositor and investors and the money resources will be allocated in the best way possible. "[6]"

- Increase in cashability and decrease in the amount of risk
- The creation of a situation in which it is possible to control the amount of risk

### 4 THE RELATIONSHIP BETWEEN FINANCIAL MARKET AND ECONOMIC GROWTH

By creating a tunnel between the two groups of money depositors and entrepreneurs, equipment of small and large savings, and through the already mentioned procedures, the financial market can provide an appropriate atmosphere for promising financial activities. In an economy in which the financial market operates satisfactorily, on one hand, the amount of investment increases, and on the other hand, the vigor and quality of investment amplifies. The increase in the availability to financial organizations and establishments decreases the costs of transactions and simplifies the process through which information are obtained. The sum of the effects of all these factors will eventually lead to economic growth. "[4]"[2]"

## 5 THE FUNDAMENTAL OBSTACLES ON THE WAY OF FINANCIAL MARKETS AND ECONOMIC GROWTH IN IRAN

Our dear country, Iran, has the highest amount of capital among the competing financial markets. However, the rate of economic growth is not satisfactory. There are a number of reasons which prevent our country from growing economically. The three most important ones of these obstacles will be discussed here. First, we do not have a proper system for the circulation of capital among the generators of the capital, entrepreneurs, and in short, the sectors that can cause economic growth "[3]"

It goes without saying that one other reason that has been hindering the growth of economy in recent years is unreasonable interferences in the capital markets such as the stock market. The codification of rules and regulations in order to prevent these types of interferences has been given priority by the 'Contrivance and Hope' government and some bills have been passed in this regard by the parliament. Through such efforts, some of the obstacles in this area have been removed "[9]"

Third, in the last several years we have had a rather closed economy and in areas such as importing and exporting our country has not had sufficient international vitality due to political problems such as the sanctions and lack of functional planning. Here, it should be noted that importing and exporting are of the most vital indexes of economic growth. These problems have engendered several obstacles on the way of our economic growth. Under such state of affairs and with a closed economy, the national manufacturers decrease the amount of their production because of the difficulties associated with exporting their products. Similarly, because of the impediments on the way of importing, the provision of necessary raw materials for the production faces problems. In the long run, these problems can take away the possibility of growth from our economy.

Of course, there are several other factor factors which deserve consideration. The author, however, has just mentioned three of the factors because of their utmost importance.

## 6 CONCLUSION

According to what has been said thus far, we have a number of obstacles on the way of our economic growth due to the following reasons:

1. There are shortcomings in both distribution of capitals and identification of the factors which can bring about economic growth.
2. There is lack of proper planning in the areas such as management of the loans distributed by the banks.

The question here is that why in spite of the existence of huge amounts of money deposits in the banks of the country, which are the most important capital markets of Iran, there is not a proper and functional supervision over their functioning (either in the allocation of the capital or in the supervision of the distributed loans)?

3. The economy is closed because of sanctions and political problems (Of course, based on the economic principles, there cannot be a completely closed economy; here by closed economy the existence of numerous obstacles in the area of international transactions is meant).
4. There is a lack of consistent laws that can prevent unreasonable interferences in the financial markets such as the stock market.

## 7 SUGGESTIONS

- A) Considering the negative effects of indexes of financial development on economic growth whose main culprits are lack of specialty and proper supervision of the way loans are distributed by the banks, it is recommended that banks employ specialized workforces and use them in the related areas such as directing the expenditure of loan money in manufacturing.
- B) Since the openness of economy, both in short- and long-term, affects the economic growth positively, the removal of the obstacles of transactions including the importing and exporting and increasing the amount of international economic transactions and alleviating other economic problems can help us reach a higher economic growth rate.
- C) Strong legislation in order to create a healthy financial market to prevent unwarranted and non-normative interference from outside.

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