

Banking services/Financial institutions

Banks provide a number of important [financial services](#) to businesses:

1. Loans provide businesses with expansion capital. A secured loan is one that is guaranteed by some form of asset such as buildings and property. An unsecured loan is not backed in the same way. A bank will lend a business a given sum for a specified period of time e.g. £6,000 for 2 years. The business will then repay the capital sum in instalments with interest added e.g. £360 per month. The rate of interest on unsecured loans is higher than for secured loans.
2. Business account services enable a business to transact its day-to-day affairs, for example paying wages into employee's accounts, paying bills, and taking up periods of credit when applicable. Businesses are able to use bank services such as standing orders and direct debits to pay water, electricity, business rates and other regular bills.
3. Overdraft facilities enable a business to have a short period of credit to smooth out cash flow difficulties. The business arranges an overdraft limit with its bank and is permitted to borrow up to the arranged overdraft ceiling. Interest is only charged on the amount overdrawn each day. So, for example, if the bank was only overdrawn by £100 for 1 day of the year it would pay 1/365 of annual interest rate for £100.
4. Cheques, credit cards and bank drafts enable a business to smoothly manage its day-to-day payments and transactions. Bank statements enable the business to keep a regular check on its accounting position.
5. The bank will also provide systematic and ongoing advice, particularly to small businesses and start ups. For example, the bank will provide detailed advice on how to construct and organise a business plan.
6. Banks also provide long-term finance in the form of mortgages for the purchase of land and property.
7. Merchant banks and issuing houses also support companies in the management of share issues, for example, by arranging for financial institutions to underwrite a new share issue.

Financial Institutions

Financial institutions, such as the Bank of England, Stock Exchange, High Street Banks, Pension Funds, Insurance Companies and others, enable business to take place smoothly. Financial intermediaries, such as banks, channel funds from savers to borrowers.

The variety of financial institutions reveals the complex requirements of both borrowers and lenders. Banks, building societies, investment trusts and pension funds are just a few of the organisations whose job it is to channel funds to those that require them.

These institutions operate in the short-term (money) market and the long-term (capital) market.

In the money market, the main activity centres around funds, which are lent for periods from as short as overnight up to about one year. The capital market focuses on money borrowed and lent for periods of five years or more. There is a grey area, of one to five years that is not incorporated into the two definitions and, hardly surprisingly, this is called the medium-term market.

The main functions of financial institutions are:

1. To help businesses manage risks e.g. by providing insurance in the case of insurance companies.

2. To provide corporate finance as is the case with banks, or investment trusts, which enable lots of investors to own shares in a range of companies.

Buying stocks and shares

The Stock Exchange makes it possible for large companies to raise finance. Members of the public can buy shares through Stock Exchange dealers in a number of ways:

1. You can deal directly with a market maker (who belong to firms that buy and sell shares first hand). This is commonly done by large buying institutions e.g. pension funds and investment trusts.
2. You can deal with a local broker/dealer who will then buy on your behalf (e.g. through your local bank).
3. You can buy from a share shop, which deals directly in stocks and shares. Some major department stores have departments specialising in stocks and shares.

Shareholders are part owners of a company. Many large financial institutions like pension funds are major shareholders in leading companies.