

M. Com. Sem. I

Subject - Business Finance

Topic - Role of Financial System
in Economic Development

An efficient and developed financial system is essential for the rapid economy growth of any country or any economy. The role of financial system in economic development is very significant. A well developed financial system can help effectively in the process of economic development through three ways -

First, through technical progress which can be achieved with the help of human and physical capital. Any increase in human and physical capital is provided by an increase in saving and investment.

Second, the economic development ^{much} depends on the rate of capital formation. But the capital formation depends on whether finance is made available in ~~the~~ time, ~~and~~ in adequate quantity and on favourable terms.

Third, financial system enlarges the markets and enhances the efficiency of the medium of exchange and thereby help in economic development.

The role of financial system may be explain under following points —

1. Financial system helps in development by creating more efficient payments, transfer and remittance mechanism through financial institutions.
2. Financial system facilitates allocation of resource.
3. It performs various functions such as — a) mobilisation of savings, b) diversification and reducing risk, c) transferring of financial claims, d) providing better portfolio management, e) facilitation of exchange of goods and services.
4. Financial system provides a precondition to economic growth.
5. It provides sound corporate governance practices.
6. A sound financial system helps the central bank to conduct monetary policy.
7. It helps the management of companies.

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