

# 5

## Savings and Investments

### 5.1 Introduction

You have learnt in the previous lesson that all money income available in a month is not to be spent away immediately on the monthly requirements of the family. A part should be kept for future use. Since the money is for special use in future, you may also think where you would keep it. What can be done with it till the time it is actually used. In this lesson I, we shall try to answer these and other related questions.

### 5.2 Objectives

After studying this lesson, you will be able to:

- explain the concept of saving and suggest guidelines for saving;
- identify the needs for saving money;
- explain the role of financial institutions;
- explain the concept of investment;
- identify the factors that influence the selection of an investment scheme;
- list and describe the characteristics of some investing schemes.

### 5.3 What are Savings

As you have learnt earlier, saving for any month is the difference between the income and expenditure of that month.

$$\text{Income} - \text{Expenditure} = \text{Saving}$$

Very often this difference rarely exists. The soaring prices and the increasing needs and desires of the family members make it difficult for the homemaker to save. But it is the duty of every household, to plan out their expenditures and thus put aside some money from the present income for future use. This money accumulated over the months accounts for the family's savings.

Money from the present income that is collected or put aside for emergency or future use is known as savings.

#### 5.4 Guidelines for Saving

To accumulate savings, you need to plan carefully

- Your saving plan should be realistic — if you are earning Rs 5000, can you save Rs 2000? No. Your family's expenses cannot be met with just Rs. 3000. The amount you need can be saved gradually over a number of months.
- Your saving plan should be regular. If you want a large saving to accumulate, you will need to save every month for a couple of years.
- You must be clear about the purpose for saving — if you know your goal for which you are saving, it becomes easier for you to save.

#### 5.5 Need for Saving Money

Irrespective of the income group you belong to, you must save. There are several reasons for you to save. Some of them are foreseeable while others are not. Some of the reasons for saving are:

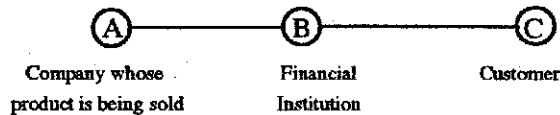
- **For a secure future :** After retirement the source of income is pension which is much less than one's regular monthly salary. The expenditure remains more or less the same. Savings can help bridge the gap. One feels comfortable if one has some income from savings. This comfortable feeling will be felt even more by people in non-pensionable jobs, where the income becomes nil.
- **For meeting emergencies :** Someone in your family may suddenly become seriously ill or may meet with an accident. In either case, the person may require immediate medical attention at home or in hospital. You need to save for such unforeseen situations.
- **Fulfilment of family's goals :** Savings are also required for fulfilling a family's long term goals, e.g. some of the goals of your family may be to buy curtains, to provide fancy clothes for the family, to buy a house, a car or a tractor . The former two goals can be achieved fast, as not much expenditure would be required for them. To buy a house, car or tractor, you would need a large sum of money. You will have to gradually save for a number of years, to be able to buy any of these.
- **To raise the family's standard of living :** All of us always want to have more and better things for our house. Most of the articles which raise our standard of living, like washing machine, television are expensive. Buying these articles from our monthly income may be difficult. You can start saving for them and buy them only when you have saved enough. If you wish to have these gadgets fast, you can purchase them on instalment basis. You may ultimately pay more this way, but you also enjoy more of its benefits.
- **For starting a small business or for self employment :** You or any of your family members may want to start a small business. You need some capital or a lumpsum money to start with. Your accumulated savings will provide you the money needed.

**INTEXT QUESTIONS 5.1**

1. Write down two reasons for which each of the following families will save.
  - (a) Mr. Lal, a middle-income man is working in a private firm. He has two college-going daughters. Mrs. Lal is a heart patient.
  - (b) Mr. and Mrs. Gupta are in their early forties. They have a school-going son, who wants to become a doctor. This middle-income family lives in a rented house. They wish to have a high standard of living.
  - (c) Mr and Mrs Arora are a middle-aged couple having no children. Mr. Arora, a chartered account works in a private firm. They live in a rented house.

**5.6 Role of Financial Institutions**

You want to buy a car. But you have not saved for it. If you begin saving now, it will take you years to have enough saving to buy the car. You need not be disheartened! To help you and other people in a similar situation, there are financial institutions in our country. These institutions provide loans, so that one may be able to buy what one desires. The financial institutions work as intermediaries between you (the customer) and the company whose product is being sold.

**5.7 Application for a Loan**

When you apply for a loan to buy something, a certain amount of its cost has to be paid by you to the company as direct cash down payment. The rest of the cost may be taken by you as a loan from the financial institution. An interest is charged on the loan. In other words, when you repay the loan, you would be required to pay the amount taken as loan together with an interest. To make the repayment of the loan easy, it is divided into instalments. So, you will be required to pay back only an affordable amount periodically till the instalments are completed. In fact, your repaying capacity is studied before a loan is provided. This is a very convenient method of buying an expensive item. You may note here that when the cash down payment and the instalments are added, you will realise that you would be paying more than the actual market price of the article. But the advantages here are:

- You have been able to buy the article without having saved for it.
- You enjoy the use of the article while you pay for it.

**Suggested Activity**

Find out the names of the financial institutions in your town, which could assist you in :

- (i) buying the following:
  - Car .....
  - House .....
  - Tractor .....
- (ii) Setting up a medium-scale cottage industry .....

## 5.8 Investments

You have learnt that your savings are not for present use. They are collected to be used at a future date.

If you keep your savings at home

- these do not grow
- there is a chance of it getting stolen
- there is a temptation to use the same for some present desire.

In order to avoid the above, put your savings in a bank or any other institution for investment. Here your savings are not only kept safe but these also grow.

When savings are made to grow, it is called investment.

For example you have saved Rs 10,000. If you keep this money at home, it will remain the same even after many years. But if you keep this money in a bank, it will earn interest and grow. The longer you keep it, the more it will grow.

There are a number of other ways in which you can invest your money. You will read more about them later in this lesson. But first you must understand how to choose an investment scheme.

## 5.9 Factors Influencing Selection of an Investment Scheme

Banks and saving institutions offer various investment schemes, suitable to various categories of people. Before you invest your money in any scheme, you must study the following points carefully.

- **Your capacity to save** : If you are a small saver, you should invest in a scheme which does not require a large amount as the minimum specification to invest.
- **Safety of the investment** : To save, you have to often sacrifice some present requirement. You would therefore, definitely want your saving to be safe. Your investment documents should be kept very safely. Moreover, there are certain schemes which are not likely to pay you a good return owing to the fluctuating market prices. You must try to avoid such schemes.
- **Higher rate of interest** : The longer you keep your money in an institution, the higher is the rate of interest it offers you. Also different institutions offer different rates of interest for the same period. Institutions which require your money urgently, may offer you a very high rate of interest. You have to be cautious to see that the institution is a reliable one.
- **Easy liquidity** : There may be times when you suddenly need your money. Easy liquidity enables you to get your invested saving back, when in need. There are some schemes where you cannot withdraw your money before a stated period. Investing all your saving in such schemes will make it difficult for you to get your money when you need it.
- **Other benefits** : Besides a high rate of interest, there are some other benefits like dividends and income-tax relief which are offered by a few schemes.
- **The purchasing power** : At the end of the investment period, the grown value of the saving should be equal to or more than the inflation during that period.

- **Convenient place of investment :** Most investments require paperwork. If the institute in which you invest is at a convenient place, visits can be made without the loss of much time.

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### INTEXT QUESTIONS 5.2

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1. Indicate whether the following statements are true or false by writing 'T' or 'F' against each statement:
    - (a) All investment schemes offer the same rate of interest.
    - (b) The returns from some investment schemes are affected by the fluctuating market prices.
    - (c) Investment schemes are suitable only for people who can save a large amount.
    - (d) You should opt for a scheme which offers the highest rate of interest.
    - (e) After the money has grown, its new value should be more than the inflation during that period.
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### 5.10 Institutions of Investment

You may invest your savings in any of the following institutions

- (i) A bank
- (ii) A post-office
- (iii) Provident Fund
- (iv) Life Insurance Company
- (v) Unit Trust of India
- (vi) Stock Exchange
- (vii) Private Company
- (viii) Property or jewellery

#### 1. Putting the money in a bank

Money not required immediately can be kept in a bank. The advantages of keeping money in a bank are :

- Your money is safe.
- Your money grows — you get interest on your deposits.
- You can withdraw money from the bank whenever you need it.
- You can take a loan against your money kept in the bank.

#### How to Open a Saving Accounts in a Bank?

Your request for opening a saving account will have to be made on the prescribed form of the bank. Besides giving the relevant particulars, you will need to furnish the specimen of your signature and copies of two passport size photographs. You will need to be introduced to the bank by a respectable party, i.e. a customer, an employee of the bank or some other well known person. This way, the bank satisfies itself about your integrity, honesty and financial standing. After this, the bank will accept your initial deposit and give you the

following books:

- Pass book — it serves as a copy of your account in the books of the bank.
- Cheque book — it is to be used for withdrawing money from the bank.

The account may be opened by a single person or two or more persons jointly. Either of the persons can operate the account. A nominee's name has to be mentioned. Nominee is a person who would get the money in case the account holder dies. You can start a savings account with Rs. 100.

#### (ii) By putting the money in a post-office

Saving in a post-office has the following advantages:

- they are conveniently located
- you can start a savings account with a very small amount, i.e. Rs 20.
- you do not have to pay income-tax on the interest earned in many of its schemes, e.g. National Saving Certificates (NSC), Indira Vikas Patra, etc.
- You can also get rebate in income-tax by investing in many of its schemes.

The method of opening an account is the same as that in a bank.

#### (iii) Investing in Provident Fund

To protect the salaried people in old age, the Government has introduced a retirement benefit scheme called the Provident Fund Scheme. The main purpose of the scheme is to provide for compulsory saving, out of the current income of the employee. The employer gives the employee the saved amount together with the interest at the time of retirement.

While the money accumulates in the fund, the Government uses it for the developmental projects in the country. So by investing in Provident Fund, you serve two purposes.

- you provide for yourself in old age
- you help in the development of the country.

The main features of Provident Fund are :

- Every month, a certain percentage of the basic salary is compulsorily deducted from the employee's salary. This deduction is his contribution towards the fund.
- An interest is worked on the contribution.
- The money deposited and the interest on it are both exempted from income-tax.
- You can take a loan against the money deposited.

There are two types of Provident Fund Schemes:

- General Provident Fund (G.P.F.) — This is suitable for all salaried people. The employee, if he wishes, can increase his contribution towards the fund. At the time of retirement, the employee gets his contribution together with the interest, in a lumpsum.

If the employee needs money before he retires, say for the marriage of children or for the construction of a house, he can take a loan from his Provident Fund.

- Public Provident Fund (P.P.F.) — Any self employed person can open this account with the State Bank of India or the post-office. The money may be deposited either regularly in instalments or in lumpsum. After five years, the investor can take back a certain percentage of his or her money. The rate of interest is 12% per annum. The

investor also enjoys income-tax relief. Loan can be taken against the money invested in the fund.

#### (iv) Taking an Insurance Policy

Insurance is a means of providing against loss caused by natural or man-made factors. When one takes an insurance policy, one has to enter into a contract with the Insurance Company. Under the contract, the insured has to pay a sum of money known as premium periodically to the Insurance Company. In return the insurance company makes good the loss suffered by the insured person or agrees to make a compensation.

Insurance is of two types :

- **General Insurance**—This covers risks such as theft, fire, flood, drought or any other contingency. The contract is generally made for a year. The insured has to pay the premiums periodically. The amount of the premiums to be paid will depend on the amount for which the contract is drawn up. In case of a loss suffered by the insured, he or she can recover from the insurance company, the actual amount of the loss or the amount of policy, whichever is less. The advantages of this policy are:
  - it is an easy and forced form of saving
  - it provides security against loss or risk.
- **Life Insurance** — It is a contract under which the insured pays premium periodically. How much the premium will be, will depend upon the total amount of the policy and the number of years for which the policy is drawn up. At the end of the period, the money along with the interest, is returned to the insured. In case the insured dies, the full amount for which the policy is taken, is payable to the person whose name has been nominated by the insured. This person is called the beneficiary. The advantages are:
  - it is a safe investment
  - it provides financial protection in the event of death or disability
  - it is an easy and forced form of saving
  - it provides income-tax relief on the paid-up premiums
  - loans can be taken against money deposited for the policy of insurance company.

#### Suggested activity:

Find out the names of some policies offered by the Life Insurance Corporation of India and understand how they can help you.

#### (v) Buying Units

You can buy units in your name or in joint names from the Unit Trust of India. Each unit has a face value of Rs. 10. A minimum of 100 units has to be bought. Every year, in June, the Unit Trust of India declares dividends out of its projects. The advantages of investing in units are:

- you get regular interest
- you get income-tax relief on the amount invested
- the dividend you get is completely exempted from income-tax
- whenever you are in need of money, you can encash the units by selling them back to the UTI at the repurchase price fixed by it from time to time.
- you can transfer the units to another person
- it is a safe investment.

#### (vi) Buying shares

When private companies want to develop, they float shares to the public. When you buy a share, you become a part owner of the company. You will now share both the profit and loss of the company. When buying shares, you must buy from

companies which you expect will do well.

The main advantage of this type of investment is that it may quickly give you a very high profit. But this is not always so. Do you watch the news on TV? The Sensex news will tell you, that the Sensex may either fall or rise. When the Sensex remains at a low level, you may lose on your shares.

**(vii) Buying debentures**

Debentures are also known as bonds. When you purchase a debenture from a company, it means that you have loaned the money to the company. In return, the company, promises to pay back the investor not only the amount invested but also a fixed rate of interest on it at regular intervals.

When compared to investing in shares, this is a safer method of investment. You get your interest, irrespective of the company's profit or loss.

**(viii) Buying property or jewellery**

If you have a large saving you can buy any one of these and keep it with you. You can sell it at a later date when its price goes up.

The disadvantage here is that when you wish to sell off your property, it may take long to get a suitable buyer. When you sell off your jewellery, a certain amount of loss may be faced in the weight of the jewellery.

Depending upon various characteristics like safety, liquidity, return on-money invested, exemption from tax and availability of loan facility, most of the investment schemes can be plotted in a simple chart.

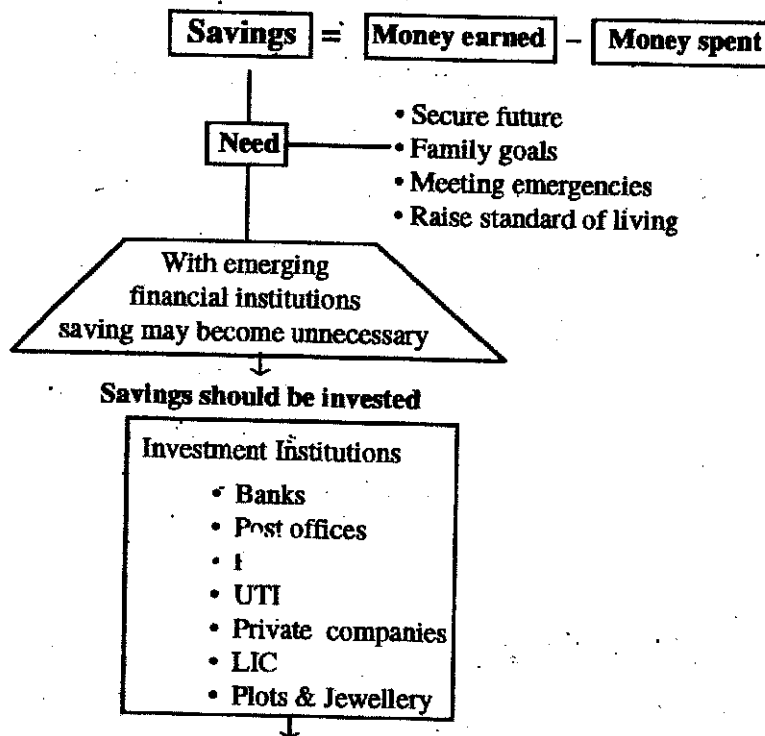
Institution	Safety	Liquidity	Good return	Tax exemption	Loan facility
Bank	√	√	√	—	√
Post-Office	√	—	√	√	—
National Saving Certificate	√	—	√	√	—
General Provident Fund	√	—	√	√	√
Public Provident Fund	√	—	√	√	√
General Insurance	√	—	√	—	—
Life Insurance	√	—	√	√	√
Units	√	√	√	√	—
Share	—	—	√	—	—
Debentures	√	—	√	—	—
Gold / Property	—	√	√	—	—

**Activity :** Find out the above mentioned characteristics of some other investment schemes in your area and add them to the chart given here.

**INTEXT QUESTIONS 5.3**

State whether the following statements are True or False. Write 'T' for True and 'F' for False.

- You enjoy income-tax relief when you invest in debentures.
- Money invested in a Life Insurance Policy can be got back only after the death of the insured.
- You are sure of getting good returns when you buy shares.
- You can sell back the units to the Unit Trust of India.
- Returns from investment in shares are regular.
- General Provident Fund is for salaried people.
- Investing in debentures is safer than investing in shares.
- If you are a policy holder, you can take a loan from the Life Insurance Corporation of India.
- If there is no bank where you live, you can invest in a post office.
- A loan can be taken against your deposit in a bank.

**5.11 What You Have Learnt****Guidelines for selection of Institution of Investment**

- Security
- Risk / Safety
- Tax rebate
- Fluidity
- Growth rate
- Capacity to save

### 5.12 Terminal Exercises

1. Name the investment scheme suitable for you :
  - (a) You want quick multiplication of your money .....
  - (b) You are self-employed and wish to have income-tax relief on your income.....
  - (c) In your village, the nearest bank is 5 km away .....
  - (d) You want your family to be comfortable even after your death .....
  - e) You are in service and wish to enjoy income-tax rebate .....
2. What is investment?
3. What are the ways in which a small saver can invest?
4. What are the factors you would consider before selecting a scheme of investment?
5. If you are the only earning member at home, which scheme would you invest in?

### 5.13 Answers to Intext Questions

- |            |          |       |       |
|------------|----------|-------|-------|
| <b>5.2</b> | 1. (a) F | (b) T | (c) F |
|            | (d) F    | (e) T |       |
|            | 2. (a) F | (b) T | (c) F |
|            | (d) T    | (e) T |       |
| <b>5.3</b> | (a) F    | (b) F | (c) F |
|            | (d) T    | (e) F | (f) T |
|            | (g) T    | (h) T | (i) T |
|            | (j) T    |       |       |
|            |          |       |       |