CHAPTER-III

Conceptual Framework

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CONCEPTUAL FRAMEWORK

3.1 Introduction:

The savings and investment pattern plays vital role for the development of any country. India is not an exception to that. It means that the savings and investment of people of India are playing important role for India's development. India is one among the world's most efficient financial markets in terms of regulation, system and technology. It has one of the highest savings rate in the world,

The economic development of any country depends upon development of industrial sector, service sector and agricultural sector, and optimum utilization of all the factors of production i.e. land, labor, capital and organization. Amongst all these factors of production the most important is capital. Capital is the scarcest resource available to most of the countries of the world. India is also not an exception to this. Hence there is need to effectively utilize capital.

3.2 Saving:

Saving is income which is not spent or deferred consumption. Saving means that amount which a man saves out of his income after he has incurred his consumption expenditure. Saving also means the income which is not consumed. It means the excess of income over consumption expenditure.

Example: If a farmer earning Rs.50,000 p.a. out of it he spends Rs.40, 000p.a for food, clothing, accommodation, house hold needs etc., his saving amounts to Rs.10,000 p.a. Suppose he spends Rs.5,000 on irrigation or purchase of agriculture equipments or in repairing the farm house. We should not then think that his saving is Rs.5,000p.a. The saving will still Rs.10,000 p.a. Rs.5,000, spent on irrigation, purchase of agriculture equipments or in repairing the farm house etc. is called investment and cannot be included in consumption expenditure. To find out saving, we should deduct from income only domestic or consumption expenditure and not investment expenditure.

Thus saving is a part of income that is not consumed, it could be money put in a bank or in form of cash available with an individual

3.3 Investment:

Investment means an employment of fund with the aim of earning income. Investment is done with positive expectation of return in future. The investor can earn expected return in the form of interest, dividend, premium, capital appreciation etc. by making investment into various investment avenues.

In other words an investment is a sacrifice of current money or other resources for future benefits. There are so many avenues of investment are available today. You can deposit money in a bank account or purchase a long term government bond or investment in the equity shares of a company or contribute to provident fund account or buy a stock option or acquire a plot of land or investment in some other form. Investment is generally long term activity for future gain.

3.4 Classification of investments:

The investments are broadly classified into two main types Financial and economic investments.

1. Financial investments: The investor invests their savings into different avenues in anticipation of earning future income in the form of interest, dividend or benefits. Ex-investment in equity shares, debentures, bonds, post office, insurance etc. These are also called financial assets.

2. **Economic investments:** The investor invest their savings into different avenues in anticipation of appreciation capital stock, example-investment in land, building, plant, machinery, equipments etc.

3.5 Investment v/s Speculation:

Speculation is short term activity in anticipation of earning huge returns. It is difficult make the distinction between investment and speculation, the following main points helps us to make the difference between investment and speculation.

1. **Time horizon:** An investment is generally done for long period of time say more than one year. But speculation is generally done for short period of time say a few days too few months.

2. **Risk:** In investment the risk is limited or moderate because the investment is done for long period. But in speculation the risk is high.

3. **Return:** In investment the investor receives the moderate return but in speculation the speculator receives high return.

4. **Basis for decision:** The decision of investment in various avenues depends on safety liquidity, return, etc. But a speculator relies more on technical charts, market psychology etc.

5. **Use of funds:** The investment is done by the investor by his own funds. But in case of speculation, a speculator uses own fund as well as borrowed fund.

3.6 Investment v/s gambling:

Gambling refers to high risk with unexpected gain for high excitement. It is unsystematic, unplanned and unscientific use of fund. It involves unnecessary high risk for increasing the return. Ex- horse race, lotteries, cards playing.etc. But investment involves safety, liquidity, systematic and planned use of saving.

3.7 Characteristics of investment:

The following are the main features or characteristics of investment-

1. **Return:** The important characteristic of an investment is to get moderate or more return on all investment. The return either in the form of interest or dividend or capital appreciation or in any other form. The return on investment depends upon the nature, maturity period, and market conditions etc.

2. **Risk:** The important feature of an investment is risk. It means that every investment there is a risk. Risk is inherent in investment. The risk in the form of no interest, no dividend, or delay in payment of interest or dividend. Therefore the investor should take care while making investment .High risk-high return and low risk-low return.

3. **Safety:** Safety is another important feature of an investment. The investor has to analyze the economic condition and industry condition before selecting an investment avenue. The safety of investment is possible through diversifying investment.

4. **Liquidity:** Liquidity means conversion of any asset into cash. The investor always prefers liquidity through marketable securities. When there is more liquidity there is low return.

3.8 Various Avenues of investment:

There are number of investment avenues. They are classified into Marketable and Non-marketable and liquid assets. The classification is also made like Financial Assets, Marketable Assets and Physical Assets. Therefore the investor has to select proper investment avenue. Broadly investment avenues are classified as follows.-

1. Corporate Securities:

A. Equity Shares

B .Preference Shares

C. Debentures / Bonds

2. Bank Deposits

3. Non-Banking Company Deposits

4. Post Office Deposits

5. Insurance Schemes

6. Provident Fund Schemes.

7. National Saving Certificate.

8. Government and Semi –government Securities.

9. Mutual Fund Schemes.

10. Real Assets

11. Gilt Edged Securities.

1. Corporate Securities:

Corporate securities are issued by joint stock companies in the private sector. It includes

A. Equity Shares:

Equity shares capital represents ownership capital. The equity share holders are called the real owners of the organization. They bear risk and enjoy the ownership rights. The equity shares as a most important fixed income investment avenue . The liability of equity shareholders is limited to the extent of shares held by them. The investors can invest in shares through primary market and secondary market. When the company performs better and the future is bright, the price of the company's shares goes up in the market. AS a result the investor can invest in shares for getting dividends and capital gains.

Benjamin Graham has described the nature of equity shares, referred to as common stocks in the U.S., very aptly: "Common stocks have one important characteristic and one important speculative characteristic. Their investment value and market price tend to increase irregularly but persistently over the decades, as their net worth builds up through the re-investment of undistributed earnings. However ,most of the time common stocks are subject to irrational and excessive price fluctuations in both directions ,as the consequence of the ingrained tendency of most people to speculate or gamble , i.e. ,to give way to hope ,fear ,and greed."

Share is a share in a share capital of the company. It means they are the real owners of the organization. They have to voting right.

Features of equity shares:

1. More risk and more return.

2. Investment for medium and long term.

3. Claims on income.

4. Claims on assets and properties.

5. Right to control and manage.

6. Pre-emptive rights-rights issue.

7. Limited liability.

B. Preference Shares:

Preference shares are another important avenue of investment, which carries the some of the features of equity shares and some of the features of debentures. Therefore these are called as hybrid type of securities. They have consistency in getting return on investment.

As compared to equity shares preference shares have less risky. And return is also low. These shareholders do not have voting rights. They get fixed rate of dividend after paying interest and tax. These shares are high liquidity and low risk. The preference shares carry fixed rate of dividend, there dividend is generally cumulative, and these are redeemable.

Features of preference shares:

1. Less risky than equity shares.

2. Lower return than the equity shares.

3. Convertibility of preference shares into equity shares.

4. Commutation of dividend.

5. Participation in surplus dividend and assets of the company.

6. No voting power

C. Debentures or Bonds:

Debentures or bonds are the long term debt instruments. The issuer of a debenture or bond promises to pay certain fixed rate of interest. These generally comprise of periodic interest payments over the life of the instrument and principal payment at the time of redemption. The

Government securities, RBI saving bonds, Private sector debentures, PSU bonds etc.

Debentures are classified into bearer debentures, registered debentures, convertible debentures, non-convertible debentures etc. RBI Tax Free Bonds are issued to the investors which carry tax benefits to the investors.

Features of debentures and bonds:

1. The risk is low.

2. The return is also low.

3. It generally creates some charge on property of the company.

4. A debenture holder has no voting rights.

5. Right to sue the company for any unpaid dues.

6. Right to sale of security in case of default.

2. Bank Deposits:

Bank deposits perhaps the very simplest avenue of investment. By opening a bank account and depositing money in it can make a bank deposit. There are various kinds of bank deposit accounts like savings bank deposits, fixed deposits, reinvestment deposits, and recurring deposits etc. the investor can receive the interest on these deposits. These deposits are very safe, the interest rate depends upon the period of investment, high liquidity, and loans can be available against these deposits, no ceiling on interest rate on saving bank deposits also.

Features of bank deposits:

1. Bank deposits are very safe.

2. The interest rate on fixed deposits varies with term of deposit.

3. Bank deposits enjoy exceptionally high liquidity.

4. Loans can be raised on bank deposits.

5. There are various types of bank deposits like- monthly interest, quarterly interest, reinvestment deposits, recurring deposits etc.

3. Non-Banking Company Deposits:

The main function is to mobilize savings. The investors have to be cautious while investing money with non-banking companies. While investing in these companies the investors can go through the credit rating. The Private companies and NBFCs are providing various attractive schemes for mobilizing saving.

The NBFCs consist of leasing companies, hire purchase companies, investment and chit fund companies.

4. Post Office Deposits:

The post offices in India are playing vital role in mobilizing funds through various saving schemes. The post offices are assisting the government in the development of our economy. The various schemes start from Rs.10 to Unlimited. The post offices in India provide various schemes like- post office savings deposits similar to savings bank deposits. The post office time deposits, monthly income scheme of the post office. Kisan Vikas Patra, National Savings Certificate, etc.

Features of post office deposits:

1. More safety.

2. The interest is tax exempt.

3. Helps to small investors whose income are low.

4. Post office Recurring Deposits are very popular.

5. Savings account, Time deposits, Monthly interest deposits, Recurring Deposits.

6. Post office also issues Kisan Vikas Patra (KVP), National Savings Certificate (NSC), Indira Vikas Patra (IVP) etc.

5. Life Insurance Schemes:

The basic need of people met by life insurance policies are protection and savings. The various life insurance policies that provide protection benefits are designed to protect the policy holders or his dependents from financial consequence of unwanted events such as death or disability. Policies that are designed as savings contracts allow the policy holder to build up funds to meet specific investment objectives such as income in retirement or repayment of loan. The common types of insurance policies are- Endowment Assurance, Money Back Plan, Whole Life Assurance, Unit Linked Plan, Term Assurance, Immediate Annuity, Deferred Annuity, etc.

Features of life insurance:

1 The importance of life insurance policies are protection and savings.

2. It covers the risk of life of the earning member in the family.

3. Most of the life insurance policies designed to build up funds to meet specific objectives like-retirement, repayment of loan, etc.

4. Many policies provide a mixture of savings and protection benefits.

5. The common types of insurance policies are- Endowment Assurance, Money Back Plan, Whole Life Assurance, Unit Linked Plan, Term Assurance, Immediate Annuity, Deferred Annuity, etc.

6. Tax benefits.

6. Provident Fund Schemes:

The employee provident fund scheme is the major vehicle of savings for salaried employees. The each employee has separate provident fund account, in which both employer and employee are required to contribute a certain sum of amount on a monthly basis, however the employee can choose to contribute additional amount, The balance in the provident fund account is fully exempt from wealth tax, sometimes employee is eligible to take a loan against the provident fund balance pertaining to his contributions only. It is not subject to attachment under any order or decree of a court.

Public Provident Fund Scheme is the most attractive investment avenues available in India, individuals and HUFs can participate in the scheme, the period of PPF account is 15 years. The minimum deposit of Rs.100 p.a. maximum amount is Rs.70000 p.a. The balance in a PPF account is fully tax exempt from wealth tax, It is not subject to attachment under any order or decree of a court, eligible to take a loan against the provident fund.

Features of provident fund:

1. Each employee has a separate provident fund account.

2. The contribution made by the employer is fully tax exempt.

3. Every year the central government fixes the interest rate.

4. The balance in the provident fund is fully exempt from wealth tax.

5. The employee is eligible to take a loan against the provident fund balance pertaining to his contribution only.

7. National Saving Certificate:

National Saving Certificate are issued in post offices, they are following features- These are issued in denominations of Rs. 100, Rs.500, Rs.1000, Rs.5000 and Rs.10000, These are issued for 6 years period, no tax deduction at source, it can be pledged as collateral for raising loans.

Features of National Saving Certificate:

1. It comes in denomination of Rs.100, Rs.500, Rs.1000, Rs.5000 and Rs.10000.

2. It has a term of 6 years.

3. The investment in NSC is avail exemption under section 80c.

4. No tax deduction at source.

5. It can be pledged as collateral for raising loans.

8. Government and Semi –government Securities:

The debt securities issued by central government, state government and quasi-government agencies are referred to as government securities. The securities have maturities ranging from three years to twenty years. Interest between 7% to 10%, these securities carry some tax advantages, they have traditionally not appealing to individual investors because of low interest and long maturity.

Features of Government and Semi –government Securities:

1. They are issued by central, state and quasi government agencies.

2. More safety but normal return.

3. These are the promissory note.

4. These are in the bearer form.

5. The interest earned is taxable.

6. The bonds are transferable.

7. The bonds can be offered as security to banks for availing loans.

9. Mutual Fund Schemes:

In India all mutual fund schemes are regulated by Securities Exchange Board of India (SEBI). The Unit Trust of India (UTI) was the first mutual fund company established in the year 1964. Today there are number of mutual fund companies providing various mutual fund schemes like- open ended fund and close ended fund, liquid fund, income fund, equity fund, sartorial fund etc. Today the number of commercial banks and financial institutes are offering mutual fund schemes. The open ended MFs are offered by Birla Tax, Morgan Stanley, SBI Magnum ELSS, UTI MF, Prudential ICICI Premier etc. While Alliance Fund, Prudential ICICI Balanced, Reliance Growth, Kotak Mahindra etc. are the close ended funds. The investor has to plan in accordance with share market.

Features of mutual fund:

1. The diversification of portfolio.

2. Professional management.

3. More liquidity.

4. Attracts small investors.

5. Tax benefits.

6. More transference.

10. Real Assets:

The investor gets high expected returns through investment in real assets like- real estate, Precious Metals, Precious stones etc. The investment in real estate includes- residential house, commercial property, urban and semi urban land, agricultural land. The precious metals include-gold and silver. The precious stones like diamonds etc.

Those having huge amount with them, can invest their money in real estate as long term investment. The investor has to very cautious while investing in real estate; he has to see all the documents and legal procedure etc. The investor has to pay tax, capital gain tax, property tax etc.

Precious Metals investment includes gold and silver .These investments have high liquidity, so investors prefer mostly for future use. The said investment is generally made during the period of wedding and special occasions.

Features of real assets:

1. They are tangible or physical in nature.

2. They include real estate, precious metals, precious stones and art objects and collections.

3. Safe havens.

4. Gold and silver are more liquid but real estate is not more liquid.

5. High spread and commissions.

6. Efficient diversification.

7. Inflation hedge.

11. Gilt Edged Securities:

The guilt edged securities refers to near gold or ultimate liquidity. These include all types of government securities like- stock certificates, promissory notes, bearer bonds.

3.8. Objectives of Investment:

The following factors or attributes are considered before going for an investment-

1. Liquidity:

The investors invest the savings in anticipation of some return on said investment, an investor also keeps in mind that as and when he requires money he can withdraw his investment without loss. The investor before investment can analyze need of fund in future and based on his needs he has to choose the investment avenue.

2. Safety:

Safety is another important factor of an investment. The investor has to analyze the economic condition and industry condition before selecting an investment avenue. The safety of investment is possible through diversifying investment.

3. Time horizon:

Investment is normally made by keeping in mind certain time horizon. If that time horizon changes, the objective also changes. Ex- if an individual is considering the long term profit from investment in shares, a person invests his funds in shares. Such investment may not be profitable in short term, similarly, short term investment may not provide expected yield in the long term.

4. Risk bearing capacity:

An investor, who is capable to tolerate the risk, can have investment in risky avenues like equity shares, mutual funds etc. But an investor would not like to take risk can investment in bank deposits, debentures, government securities etc.

5. Objective:

If the investor wants to have fixed or regular income from their investment, they can go for investment in bonds, debentures, fixed deposits in banks etc. But some investors like to have more income and they bear risk they can go for investment in shares, mutual funds etc.

6. Tax Planning:

Some investors provide the benefit to the investors for making investment in certain avenues. Ex-investment in various insurance schemes, tax free bonds, investment in NSC, etc. may provide benefits to the investor. Similarly the capital gain tax is also an important consideration. If there are no tax incentives for investors, the investment in such investment schemes will be reduced.

7. Age of investor:

The age of an investor is also an important factor of investment. Lower the age more is the propensity to save and vice versa. At the old age, people normally would like to have a safer investment. The young investor, on the other hand can have more risky investment.

3.9 Conclusion:

It can be concluded that saving is the part of the income which is not spent on consumption. In other words savings means income minus consumption expenditure. Savings may be in the form of cash and deposit in bank. Savings are made for future contingencies.

Investment means an employment of fund with the aim of earning income. Investment is done with positive expectation of return in future. The investor can earn expected return in the form of interest, dividend, premium, capital appreciation etc. by making investment into various investment avenues.

There are so many investment avenues available at present in India but here some of the important and commonly available avenues are considered.