FICCI

Federation of Indian Chambers
of Commerce and Industry

Prakash's First Saving



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FOREWORD



The financial markets in India have seen tremendous growth over these past few years, setting many global benchmarks along the way. However, there is still a lot more to be done, and retail participation is going to have a very important role to play in its development in the years to come.

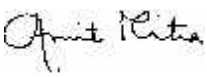
Even as the markets acknowledge the importance of the retail investor, from the viewpoint of the investor, these past few years have seen the introduction of a multitude of products and services to cater to his financial needs. Thus, while on the one hand, he has a range of financial instruments available to him, this also greatly increases the complexity of financial alternatives available to him and hinders his ability to take informed decisions. In such a scenario, the need for financial literacy and education has assumed further significance, especially as recent data indicates that less than 3% of Household savings is currently invested in financial products.

While regulatory and quasi-regulatory bodies have to a large extent been the drivers behind investor education and protection initiatives in India, there is a concurrent need for an institutional setup to look into the education of would be investors and apprise them of the benefits of investing at a young age. There is a need to create awareness about the usefulness of saving, advantages of investing and the way and means of various investment options available.

With this booklet on 'Prakash's First Saving', we hope to acquaint school children and anyone else who might be just starting off with investments about the fundamentals of investment, as well as their rights and duties and the basics of a financial vocabulary. I hope our humble effort will

make its token contribution in how financial education initiatives have been traditionally targeted.

It goes without saying that this work would not have been possible but for the support extended by the Ministry of Corporate Affairs. At this juncture, FICCI would also like to congratulate the Ministry on its various investor awareness programmes and initiatives and for providing the necessary momentum towards the movement for a more educated and informed investor.



Dr Amit Mitra
Secretary-General
FICCI

सलमान खुर्शीद, सांसद
Salman Khurshid, MP



सत्यमेव जयते

राज्य मंत्री (स्वतंत्र प्रभार)
कारपोरेट कार्य एवं अल्पसंख्यक कार्य
भारत सरकार
Minister of State (Independent Charge) for
Corporate Affairs & Minority Affairs
Government of India

MESSAGE

The economic reforms process initiated during the 1980s by the then Finance Minister and now the Hon'ble Prime Minister, Dr. Manmohan Singh has resulted in a rapid expansion of the Indian corporate sector. The present decade has seen emergence of Indian multinational companies making their presence felt in the global economic space. During this period we also saw expansion of capital market which offered investment opportunities to a large section of Indian population.

While some of the Indian companies are now enjoying market capitalizations amongst the top companies of the world; we still have a significantly large section of our society which has remained disconnected from this corporate economic boom. Thus we have a peculiar situation where a significant amount of household savings available with the common people remains uninvested and on the other hand we have corporate sector looking forward to more and more investments by the Indian public. This gap needs to be filled-up through investor education and awareness.

I am happy that the Federation of Indian Chambers of Commerce and Industry (FICCI) has started this programme of reaching out to the investors through their investor awareness programmes. This booklet on basic financial planning explaining the nuances of savings and investments is aimed at catching the young minds at an early stage. I congratulate FICCI on bringing out this publication and I am sure that a large number of people will benefit from this publication.

(SALMAN KHURSHID)

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Secretary

सत्यमेव जयते

भारत सरकार
कारपोरेट कार्य मंत्रालय
नई दिल्ली
Government of India
Ministry of Corporate Affairs
New Delhi



June 24, 2010

MESSAGE

Buoyant and participative financial and capital markets are not only one of the most important requirements for growth of corporate economy, but are also an important instrument of financial inclusion. The buoyancy in these markets is as much dependent on the performance of the corporate sector as is on the participation of informed investors in the market operations. In order to increase the participation of common people in the corporate economy, a far greater penetration of the financial market is required to be achieved. With the twin objectives of bringing more people into the corporate economy by way of investment of their surplus incomes and to make them informed investors, the Ministry of Corporate Affairs has undertaken various initiatives under the aegis of Investor Education and Protection Fund.

2. In its endeavour to convert the investor education and awareness programme of the Ministry into a mass movement, we have decided to upscale this initiative in a big way and celebrate the 'India Investor Week' in July, 2010 with the motto 'Informed Investor – An Asset to the Corporate India', as a part of the year long programme.

3. The Ministry appreciates the efforts of FICCI in the field of financial awareness and education by bringing out this booklet on the 1st day of the celebration of India Investor Week. With this easy to follow and simple book on financial planning, I hope young people will have an early understanding of the basics of finance, as well as access to information on how they can go about practicing financial planning in their lives. I sincerely hope that all our readers will start practicing Prakash's lessons in their lives also.

4. I wish FICCI success in all its future endeavours.

(R. BANDYOPADHYAY)

PREFACE



Financial Literacy is the foundation for a strong financial system and a robust and well-capitalised economy. As the Indian economy grows rapidly in the next few decades, its requirement for a larger quantum of risk capital and debt funding will grow along with the need to manage complex global and local risks. These requirements can be met by the financial markets, which can be an effective tool for distribution of wealth by shifting savings from low-yielding bank deposits to higher earning instruments like Bond and Equity. As financial markets are poised for accelerated growth, an important challenge for all market participants is to equip the investors with an understanding and appreciation of various financial products, services, trends, developments, and initiatives. Thus the imperative for investors' education.

However, financial literacy will have its strongest impact if the process is started early on. Like health education, financial education should be made a part of the curriculum for school children. Enlightening the younger generation about the importance of savings and educating them about various elementary savings products today will ensure a well-informed and adequately skilled investor base tomorrow and pave the way for evolution of the next-generation financial market players.

As the country's latest exchange, MCX Stock Exchange believes in the power of financial literacy to promote inclusive growth. Since inception, the Exchange has relied on Information, Innovation, Education and Research to systematically develop our markets. A few of its forays into financial literacy include a weekly television show to spread financial literacy in villages and towns through Doordarshan that has extensive reach and access across the country; MoUs and collaborations with a

wide range of academic, research, and trade institutions to promote knowledge and knowhow on various aspects of the financial markets across a diverse range of constituencies, stakeholders, etc.

This 'Financial Literacy' booklet is an outcome of the efforts of the Federation of Indian Chambers of Commerce & Industry (Ficci) which is India's leading Chamber of Commerce, to provide complete and comprehensive information written in a style that is easy to read and understand and that will be highly relevant and useful to the potential investors.

It is a great privilege for the MCX Stock Exchange to partner in this productive endeavour. I compliment FICCI for this exemplary effort and I am sure India's investors will greatly benefit from this booklet, enabling them to take informed decisions on investments, leading to deeper financial inclusion.



Ashok Jha,
Chairman,
MCX Stock Exchange



Prakash's first saving

Prakash is actually a lot savvier about savings and investments than he thinks. His understanding of savings actually began at a very young age, when he asked his parents for some pocket money in class V upon seeing his friends get some from their parents. His parents agreed to give Rs. 100 a month which he grumbled was a lot less than what his friends were getting, and there was no way he would be able to buy that shiny new bicycle he had been eyeing for the longest time.

But he really did want that shiny new bicycle!

So, while his friends were busy spending their money on ice-creams, chocolates and toffees 2-3 times every month, Prakash instead made sure he had an ice-cream only once a month and ensured that his expenses did not exceed Rs. 20 a month. The remainder of his money would then go into his piggybank that he hid under his bed.

And guess what! His sacrifices did pay off eventually when he finally finished with his Class X. Not only did he get his shiny bicycle, but he also managed a new dress for his sister and a nice photo frame for his parents. How did saving just Rs. 80 a month get him so many things? Let us see.

Sr. No.	Class	Savings per month (Rs.)	No. of Months	Total for the year (Rs.)
1	V	80	12	960
2	VI	80	12	960
3	VII	80	12	960
4	VIII	80	12	960
5	IX	80	12	960
6	X	80	12	960
			Total	**5760**

Thus, saving just Rs. 80 a month over 6 years gave him an accumulated savings of over Rs. 5760, and he still managed to have one ice-cream a month as well! Imagine, what if he had put the same amount in a bank account every month and earned an interest on it?



Starting your own piggybank: Once you determine how long you have to save for a goal, divide the time you have by the amount you think you can save or invest. If, for example, you want to save Rs. 500 by next year, you'll need to put aside Rs. 41.67 (Rs. 500 divided by 12) a month, or Rs. 9.61 (Rs. 500 divided by 52) a week.

What Is Savings and Why Do We Need To Save –

Mehengayi Ka Zamaana Aa Gaya

Savings vs. Investments: Many of us use the words 'saving' and 'investment' interchangeably, and they are essentially two sides of the same coin. However, when we talk about saving, we are more concerned with storing money safely - such as in a bank - for short-term needs such as upcoming expenses or emergencies. Typically, with this kind of 'saving', you earn a low, fixed rate of return, with very limited risk of loss and you can withdraw or have access to your money, easily.

Investing, on the other hand, involves taking a little more risk with a portion of your savings. This could include investments in a mixture of stocks, bonds or mutual funds with varying levels of risk and return with the hope of realising higher long-term returns as compared with your savings bank account. We shall shortly learn about all these investment options, but first, why do we need to save?

We need to save to:-

- Earn return on idle resources
- Generate a specified sum of money for a specific goal in life
- Make provisions for an uncertain future

One of the important reasons why one needs to save wisely is to meet the cost of Inflation. **Inflation is the rate at which the cost of living increases**. The cost of living is simply what it costs to buy the goods and services you need to live. Inflation causes money to lose value because it will not buy the same amount of a good or a service in the future as it

does now or did in the past. For example, if there was a 6 per cent inflation rate for the next 20 years, anything that costs Rs. 100 today would cost Rs. 321 in 20 years. Remember how your grandmother reminiscences about the good old days when rice was only 3 rupees a kg!

Thus, it is important to consider inflation as a factor in any long-term savings strategy. Remember to look at an investment's 'real' rate of return, which is the return after inflation. The aim of investments should be to provide a return above the inflation rate to ensure that the investment does not decrease in value over time. **For example, if the annual inflation rate is 6 per cent, then the investment will need to earn more than 6 per cent to ensure it increases in value**. If the after-tax return on your investment is less than the inflation rate, then your assets have actually decreased in value; that is, they won't buy as much today as they did last year. **Prakash's piggybank** did not compensate him for the cost of inflation.



SIMPLE INTEREST vs. COMPOUND INTEREST – Things Get A Bit Technical

Simple interest can be defined as the interest calculated on the principal amount, i.e. the original investment amount that you started off with. Thus the amount of interest earned remains fixed across time periods.

In the case of compound interest, however, interest is calculated and earned not only on the principal amount, but also on the interest earned so far as well. For example, for a deposit of Rs. 1,000 with a compound interest rate of 5% p.a., the balance at the end of the first year is Rs. 1,050, out of which Rs. 50 is the interest earned. In the case of compound interest, the Rs. 50 interest will also be included to calculate interest in the second year. So the total balance at the end of the second year will be, Rs. 1,000 (1 + 0.05) + Rs. 50 (1 + 0.05) = Rs. 1,102.5, or simply Rs. 1,000 $(1+ 0.05)^2$ = Rs. 1,102.50.

In contrast, if we have simple interest, then the balance at the end of the second year will be only Rs. 1,100, since we simply earn another Rs. 50 in the second year. In other words, if the interest is specified as simple interest as opposed to compound interest, then we earn

interest only on the principal. As you can see, we definitely prefer compound interest as far as savings deposits are concerned.

In terms of formula,

Simple Interest = p * i * n, where: p = principal (original amount invested); i = interest rate for one period; n = number of periods

Compound interest is: P = C(1+ r/n)*n*t ; Where: P = future value C = initial deposit r = interest rate (expressed as a fraction: e.g. 0.06 for 6%) n = no. of times per year interest is compounded t = number of years invested



How do a few Rupees grow over time...?

We will now try and understand how putting his money in a bank account could have earned Prakash additional money. The amount you'll need to put aside each week or month will be less if your money earns you some return as compared to a piggybank which merely stores your money. Let us now practice what we have learnt about compounding so far.

For example, the table below shows you that if you put Rs. 10 a month in a bank account earning 3 percent interest, in a year you'll have Rs. 122. If you put aside Rs. 40 a month, you'll have Rs. 488 (Rs. 122 times 4). If you can earn a higher interest rate -- say, 7 percent -- after one year you'll have Rs. 500.

Year	RATE OF INTEREST						
	@ 3%	@ 5%	@ 7%	@ 8%	@ 10 %	@ 12%	@ 13 %
1	(121.97)	(123.30)	(124.65)	(125.33)	(126.70)	(128.09)	(128.79)
2	(247.65)	(252.91)	(258.31)	(261.06)	(266.67)	(272.43)	(275.37)
3	(377.15)	(389.15)	(401.63)	(408.06)	(421.30)	(435.08)	(442.17)
4	(510.59)	(532.36)	(555.31)	(567.26)	(592.12)	(618.35)	(632.00)
5	(648.08)	(682.89)	(720.11)	(739.67)	(780.82)	(824.86)	(848.03)
6	(789.76)	(841.13)	(896.81)	(926.39)	(989.29)	(1,057.57)	(1,093.88)
7	(935.75)	(1,007.47)	(1,086.29)	(1,128.61)	(1,219.58)	(1,319.79)	(1,373.67)
8	(1,086.18)	(1,182.31)	(1,289.47)	(1,347.61)	(1,473.99)	(1,615.27)	(1,692.08)
9	(1,163.10)	(1,366.10)	(1,507.33)	(1,584.79)	(1,755.04)	(1,948.22)	(2,054.43)
10	(1,400.91)	(1,559.29)	(1,740.94)	(1,841.66)	(2,065.52)	(2,323.39)	(2,466.81)



The table also shows the growth of monthly Rs. 10 deposits invested at various interest rates over a period of time and can be used to find out how long it will take to reach your financial goals. Put aside Rs. 10 a month for five years at 10 percent, for example, and you'll have Rs. 781 -- the figure at the intersection of the year five and 10 percent interest columns. If you can invest Rs. 50 each month, you will have five times Rs. 781, or Rs. 3,905.

But what does this mean for Prakash?

It means that the sooner Prakash or for that matter you start investing, the greater you stand to gain. Let us see how the power of compounding works through an example.

Prakash has two friends at school, Asif and Romita. Romita starts saving Rs. 750 per year at the age of 15 years and continues to contribute to her little investment kitty till the time she turns 30. Her friend Asif on the other hand starts investing Rs 5,000 per year only when he is 30 and continues to invest till the age of 60.

If we assume a 15% rate of return per annum on their investments, who will have more wealth when they retire at age of 60? The answer will surprise you.

Romita. Her Rs. 750 annual savings between age 15 and 30 will amount to Rs27.7 Lakhs by age 60, whereas, Asif's Rs5,000 annual savings between age 30 and 60 will aggregate to only Rs25 Lakhs.

The BIG ADVANTAGE for Romita is that in order to build her wealth, she required a lower amount of annual investment and less number of years for making investments. Sacrificing a little today could lead to bountiful returns tomorrow.

Now that Prakash has understood the importance of starting early and the magical power that compounding has of multiplying his money, he had another question for us, which might seem a little silly to you at first, but I bet you have never really given it much thought as well **– "Now that I have the bicycle I wanted, what do I need to save for?".**

What does Prakash need to save for? – Prioritising your needs



One of the most important things you can do for your financial wellbeing is to get in the habit of saving. As an investor, one needs to prioritise ones investment needs, i.e. plan your 'Hierarchy of Savings', or in simpler words, list out your monetary and saving requirements, a few of which are given below.

- **Immediate near-term and Basic contingency needs** - This should be the money that you need to meet your day-to-day expenses such as buying groceries, or the movie that you like to watch once a month, as well the money that might be required to handle personal emergencies, such as sudden medical expenses. Such money should be available instantly at short notice partly as physical cash and partly as funds that can be immediately withdrawn from a bank.



A simple rule of thumb states that at any point of time you should have sufficient savings to meet immediate three month expenses. Any excess saving over and above that should ideally be invested for your short-term and long-term goals.

- **Savings for Foreseeable Short - Term Goals -** This is money that is needed for expenses that are planned to be made within the next two to three years. This might include the television set you plan to buy, or a holiday you want to save for. Almost all of this money should be in minimal risk deposit-type savings avenues.
- **Savings for long-term foreseeable goals -** This is money that you save in anticipation of planned expenses that are more than three to five years away. This could include amongst others, planning for a car, house, further education, marriage, retirement, etc. You could take some risk with these investments to achieve greater returns.

These are only broad saving goals, which can easily be modified or altered depending on one's circumstances and individual requirements. Prakash might be young right now, but it will be extremely useful for him



to understand the kind of savings requirements he might have when he grow up.

Now that Prakash has a broad understanding of his savings goals, let us see how he can go about achieving these goals, and if there are more efficient and effective ways for his savings to grow over time as compared to a simple savings bank account.

Prakash's Investment options

Let us see what options he would need to keep in mind going ahead. Investment options can be categorised based on the nature of assets i.e. on the basis of what is being invested in or on the basis of time period for the investment –

Based on nature of assets one could invest in:

- **Physical assets** like real estate, gold/jewellery, commodities etc.
- **Financial assets** such as fixed deposits with banks, small saving instruments with post offices, insurance/provident/pension fund etc. or securities market related instruments like shares, bonds, debentures etc.

We are only focusing on financial assets in this book.

Based on the time period one could invest in:

Short-term financial options –

- **Savings Bank Account** is often the first banking product people use, which offers low interest (4 per cent-5 per cent p.a.), but offers easy access to your funds.
- **Fixed Deposits with Banks** also referred to as term deposits, wherein the money is locked in with the bank for a certain period of time. The minimum investment period for bank FDs is 30 days. Fixed Deposits with banks are for investors with low risk appetite. Bank deposits are generally considered to be safer as compared to company deposits, which do offer high returns but are riskier as well.



All bank deposits are covered under the insurance scheme offered by Deposit Insurance and Credit Guarantee Corporation of India (DICGC) up to a maximum amount of Rupees one lakh. If you have deposits with more than one bank, deposit insurance coverage limit is applied separately to the deposits in each bank.



- **Recurring Deposits**: Under a Recurring Bank Deposit Saving Scheme, investor puts a fixed amount in a bank every month for a given rate of return. At the end of the pre-determined tenure, you get your principal sum as well as the interest earned during that period.

  Recurring Deposit encourages disciplined and regular savings at high rates of interest applicable to Term Deposits.

- **Money Market or Liquid Funds** are a specialised form of mutual funds that invest in extremely short-term fixed income instruments. These funds are ideal for corporates, institutional investors and business houses that invest large sums for very short periods. **Their aim is to provide immediate access to funds rather than to maximise returns**. Money market funds usually yield better returns than savings accounts, but lower than bank fixed deposits.



Many banks offer the facility of **No Frills or Zero balance Savings Accounts,** which can be maintained without any minimum or average balance requirement, while offering you all basic banking facilities.

A few Long-term financial options –

- **Post Office Savings Schemes (POSS):**

  Post Office Monthly Income Scheme is a low risk saving instrument, available at your local post office. They typically yield a higher return than bank FDs, and their monthly income plans are particularly suited



you if for retired individuals. Besides the low (Government) risk, the fact that there is no tax deducted at source (TDS) is one of its key attractive features.

The Post Office offers various schemes that include National Savings Certificates (NSC), National Savings Scheme (NSS), Kisan Vikas Patra, etc.

- **Public Provident Fund (PPF):**

  A PPF is a long-term savings instrument that pays 8% p.a. interest compounded annually and has a maturity of 15 years. A PPF account can be opened through any public sector bank, and major advantages include tax benefits and a very low government risk attached to it.

  However, you can withdraw your investment made in the first year only in the seventh year (although there are some loan options that begin earlier). Nevertheless this is one of the most preferred fixed income investment options for investors.

- **Bonds:**

  A bond is generally a promise to repay the principal along with a fixed rate of interest on a specified date, called the Maturity Date. Government bonds are generally considered to be a safer bet as compared to corporate bonds, as there is a lower risk of default. We shall understand bonds in greater detail later in this booklet.

- **Stocks:**

  Stocks or equity give you part ownership in a company and a share of its profits and losses. An easy way to remember the difference between stocks and bonds is: **"With stocks**, **you own. With bonds, you loan."**

  There are two ways in which you can invest in equities-

  1. Through the primary market (by applying for shares that are offered to the public)

2. Through the secondary market (by buying shares that are listed on the stock exchanges)



Historically speaking, equity shares have offered one of the highest returns to investors in the long run. However, as an investment option, investing in equity shares is also perceived to carry a high level of risk, and it is advisable that novice investors approach the equity markets via mutual funds initially. We shall study stocks in greater detail later in the book

- **Mutual Funds:**

  Mutual Finds essentially pool in money from various investors, and are a substitute for those who are unable to invest directly in equities or debt because of resource, time or knowledge constraints. We shall learn more about mutual funds later in this book.

> **Warren Buffett (on investing in stocks) – "I never attempt to make money on the stock market. I buy on the assumption that they could close the market the next day and not reopen it for five years."**



RISK-RETURN TRADE OFF and THE IMPORTANCE OF DIVERSIFICATION

The Risk-Return trade off is a very basic investment principle. There are two very important theorems that guide this principle.

First, all investments carry some degree of risk – there is uncertainty regarding how much you stand to gain or lose when you buy stocks, mutual funds or any other investments. Second, the greater the potential for higher returns from a particular investment, the greater the risk attached to it.

Therefore, low levels of risk are associated with low potential returns, and similarly high levels of uncertainty is associated with high potential returns. Taking on some risk is unavoidable if you want to achieve some return on your investment. The goal is to find the right balance between appropriate levels of profit and uncertainty. Some investments are certainly more "risky" than others, but no investment is risk free. **Trying to avoid risk by not investing at all can be the riskiest move of all. (Remember inflation!)**

DIVERSIFICATION - Do Not Put All Your Eggs in One Basket

Diversification across investments is one way to reduce the risk of your portfolio. By choosing two or more assets whose returns are not correlated (this is important) like say an investment in a company that makes health foods and another company which makes automobiles, you can reduce your overall risk while not necessarily affecting your returns. In summary, there are two things that are important to keep in mind while planning your investments -

1. Every asset has a risk attached to it – the higher the risk; the higher should be its expected returns, and vice versa.
2. Don't put all your eggs in one basket.

This does not always have to involve complex calculations; you just need to be aware that if you diversify your portfolio, your overall portfolio risk will be lower.

Prakash has also heard so much about capital markets and bonds and equity and primary and secondary markets on the news and in the papers that he is very curious about them and wants to know more about how he could use them to get better returns on his investments.



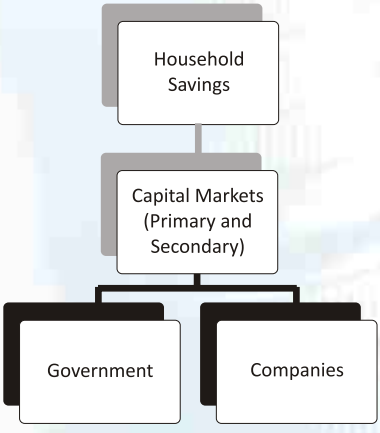
CAPITAL MARKETS

A straightforward definition of capital markets would be a market for securities, where companies and governments can raise long-term funds. Both the stock and bond markets are parts of the capital markets.

However, while the basic function of capital markets is to mobilise and channelise funds from those with excess funds to those who are in need of capital, the markets are an important source of investment for the economy. It plays a critical role in mobilising savings for investment in productive assets, with a view to funding the long term growth of the economy.

The chief role of the capital market is to channelise investments from investors who have surplus funds to the ones who are in need. It offers both long-term funds as well as funds for very short durations such as overnight funds. Short- or medium-term instruments are dealt in the money market whereas the financial instruments that have long maturity periods are dealt in the capital market.

In terms of instruments, there are number of capital market instruments used for market trade including stocks, bonds, debentures, T-bills, foreign exchange and others. However, for the purpose of understanding key financial instruments in the market, we shall concentrate on shares (equity) and bonds in this book





Shares

There are essentially two types of shares – equity shares and preference shares. However, for the purpose of this book, whenever we talk about 'shares' we shall be referring to equity shares only.



PREFERENCE SHARES

As the name suggests, these shares are given preference with regards to payment of dividend and repayment of capital, as compared to equity or ordinary shares. These shares are best suited for investors who want the security of a fixed rate of dividend and refund of capital in case of bankruptcy of the company. However, their drawback is that they enjoy limited voting rights and cannot be traded on exchanges.

However, after a fixed period, a preference shareholder can sell his/her preference shares back to the company.

When you invest in stocks also known as shares or equity of a company, it gives you part ownership of the company i.e. you are effectively one of the owners of the company. More the number of shares held by you in the company, greater your voting rights in the company as well as your share in both the company's profits as well as losses.

The value of a stock is determined by potential buyers of the stock, i.e. a simple case of demand and supply. A share or stock in any corporation is only worth what others are willing to pay for it. As the company grows, the value of the profits and the brand name they create increases the value of the stock and people are willing to pay more for it. The opposite is true for a company that performs badly. In good times, the company may also choose to distribute some of its profits to the shareholders as a return on their investment, known as **dividends**.

A stock is generally a very volatile instrument. However some stocks tend to be more stable than others. For e.g. blue chip stocks of large

companies generally tend to have less volatility compared to smaller companies whose stock prices can go up and down quite rapidly.





ALL ABOUT BULLS AND BEARS

You might have often heard people talk about bull and bear markets. Bulls and bears refer to opposite trends in the stock market. To understand this further, try and picture the personality of each animal.

Bears are cautious animals who don't like to move too fast. Bulls are bold animals who might charge right ahead. An investor is said to be "bearish" if he or she believes the stock market will go down. A "bearish" investor will buy stock cautiously. A "bullish" investor believes the market will go up. He or she will charge ahead and put more money into the market. An investor can be bearish or bullish about a particular kind of stock. Likewise, the term "bear market" describes a time when stock prices have been falling on the whole. A "bull market" is a period when stock prices are generally rising. So, bulls good, bears bad...

Certainly no one can argue that both animals are intimidating. Maybe they're meant to serve as a warning to investors: Unless you know what you are getting into, you could hurt yourself.

Do you think India is in a bull market or a bear market right now?



Bonds:

No, we are not talking about James Bond here! The financial bonds that we are talking about here may not be as exciting but they are definitely very useful instruments.

The easiest way to understand how bonds work is through the concept of a loan. When you invest/buy a bond, you are essentially lending your money to that particular company or government. In return you get a receipt from that institution which is basically an IOU (I Owe You) for that amount, with a promise to pay you regular interest on that amount.

Bonds may be used by companies, municipalities, states and U.S. and foreign governments to finance a variety of projects and activities. Two features of a bond - credit quality i.e. the ability of the company to repay the 'loan' and duration or tenure of the bond are the principal determinants of a bond's interest rate.

Once a bond 'matures' on its due date, the principal amount (i.e. the original amount invested,) is returned to the investor. Different bonds are issued for different maturity dates. Some bonds can be of durations up to 30 years as well.

A few types of bonds are given below:

Zero Coupon Bond: This is a special type of Bond where no periodic interest is paid. What would you gain from such a bond? Well these bonds are issued at a discount and redeemed at face value on maturity. The buyer of these bonds receives only one payment, at the maturity of the bond. So, effectively what you earn is the difference between what you bought it for and what it is redeemed at.

Convertible Bond: This is a bond that gives the investor an option to convert their bond into equity at a fixed conversion rate on maturity.

Treasury Bills: These are short-term (up to one year) bonds issued by government as a means of financing their cash requirements. Governments need money too, you see! They are widely considered to be one of the safest risk-free investments.

In addition, there are other types of bonds including junk bonds, callable bonds, etc.



A simple rule of thumb, when deciding how much of your funds need to be allocated to equity vis-a-vis debt, is the age rule. As a general principle you should invest 100 less your age in equity and the remainder in debt. Thus, if you are 25 years of age, you would put 75% of your money in equity and 25% in debt.

However, this is not a hard and fast rule and you should consider your specific requirements as well while allocating funds.





BONDS vs. STOCKS

When purchasing bonds you are investing in a company, but without claiming ownership. The reason why bonds are often called fixed-income securities is because they provide a dependable, steady source of income in the form of fixed and periodic interest on your principal amount. However, while your returns are predictable, unlike stocks, you will not have any stake in the success of the company or the amount of its profits.

Investing in bonds isn't completely risk-free either. If the company fails, you may only receive partial payment or no payment at all. **However, in case of bankruptcy, bondholders have first right to the proceeds from the sale of the companies assets over equity share holders.**

Stocks, unlike bonds, are more volatile in their returns. As discussed earlier, their value is based directly on the performance of the company, since they represent a part ownership of the company. Because of this, investing in stocks is much riskier than investing in bonds. Returns in the case of stocks could be in the form of stock-price appreciation or dividends that the company may pay at times out of a portion of earnings.

Because of the variables with a stock and the amount of research that needs to be done to pick a winner, a bond is considered a much safer and more conservative way to go if you are willing to forgo higher returns possible with stocks



When you buy bonds, you need to ask how the bond is rated– i.e. is the company or agency capable of repaying you? Will the interest rate compensate for inflation?

When deciding to buy stocks, many things need to be considered. How robust are the future prospects of the company? How capable Is the management of the company? How easy is it to sell the stock of the company if you suddenly need money?

Primary and Secondary Markets

The capital markets consist of the primary market, where new shares are issued anddistributed to investors, and the secondary market, where existing securities and instruments are traded. Thus, the primary market provides a platform for the sale of new securities while the secondary market deals in securities previously issued.

The Primary markets provide an opportunity to issuers of securities, government as well as corporates to raise resources to meet their requirements of investment and/or meet their obligations. They may issue the securities at face value, or at a discount/premium and these securities may take a variety of forms such as equity, debt etc.

TYPES OF ISSUES

An **initial public offering (IPO)** is the initial sale of shares by a company to the public.Broadly speaking, companies are either private or public. Going public stands for a company is changing from private ownership to public ownership.

A **follow on public offering (FPO)** is when an already listed company makes an additional offer for sale to the public

A Preferential issue/ Private Placement is an issue of shares or of convertible securities by listed companies to a select group of persons which is neither a rights issue nor a public issue. This is a faster way for a company to raise equity capital.

Rights Issue/ Rights Shares: It consists of the issue of new securities to **existing shareholders** at a ratio to those already held, at a price. For e.g. a 2:3 rights issue at Rs. 100, would entitle a shareholder to receive 2 shares for every 3 shares held at a price of Rs. 100 per share. Thus this gives existing shareholders the ability to ensure that their ownership of the company is not diluted.

Bonus Shares: A company may decide to issue shares to its shareholders free of cost based on the number of shares the shareholder owns, as an alternative to paying out dividend.



Secondary market refers to a market where securities are traded after being initially offered to the public in the primary market and/or listed on the Stock Exchange. Majority of the trading is done in the secondary market. Thus, when you buy and sell shares of Reliance or other companies that are already listed, you are doing it on the secondary market. Secondary market comprises of equity markets and the debt markets, where previously issued securities are purchased and sold.

Major stock exchanges such as Bombay Stock Exchange **(BSE)**, MCX Stock Exchange **(MCX-SX)** and National Stock Exchange **(NSE)** are the most tangible examples of secondary markets. For the general investor, the secondary market provides an efficient platform for trading of his securities, and the proceeds do not affect the issuer or the original company.

Secondary markets provide liquidity to the investors who initially buy the securities. Liquidity is important as it increases the ease with which investors can convert shares to cash.



What is the Bombay Stock Exchange (BSE) Sensex?

The **BSE Sensex or Bombay Stock Exchange Sensitive Index** is an indicator of all the major companies of the BSE. It gives you a general idea about whether most of the stocks have gone up or most of the stocks have gone down. The Sensex is a value-weighted index composed of the **30 largest and most actively traded stocks,** representative of various sectors and is regarded as a broad indicator of the domestic stock markets in India. These companies account for approximately fifty per cent of the market capitalization of the BSE. If the Sensex goes up, it means that on the whole, prices of the stocks of most of the major companies on the BSE have gone up, and vice versa.

Just like the Sensex represents the top stocks of the BSE, the Nifty represents the top 50 stocks of the NSE. Besides Sensex and the Nifty there are many other indexes. For example, the "BSE Mid-cap Index" gives you an idea about the performance of mid-cap stocks, and so on.

However, Prakash still finds the equity and bond market a scary and unfamiliar place to be in, and is not sure if he wants to risk his money with something he does not understand completely. But he understands how important it is for his money to grow over time. Let us see how he can take the help of people more knowledgeable about the markets than him to make his money work for him.

Mutual funds

A Mutual Fund pools the savings of a number of investors who share a common financial goal. The money thus collected is then invested in capital market instruments such as shares, debentures and other securities. The income earned through these investments and the capital appreciation realised are shared by its unit holders in proportion to the number of units owned by them.

Thus a Mutual Fund is the most suitable investment for the common man looking to access the capital markets as it offers an opportunity to

invest in a diversified, professionally managed basket of securities at a relatively low cost. The flow chart below describes broadly the working of a mutual fund:





Advantages of Mutual Funds

- **Professional Management** - The primary advantage of funds is the professional management of your money, as they are better equipped both in terms time as well as expertise to manage portfolios. Thus a mutual fund is a relatively inexpensive way for a small investor to get a full-time manager to monitor investments for him.
- **Diversification** - By owning shares in a mutual fund instead of owning individual stocks or bonds, your risk is spread out. Large mutual funds typically own hundreds of different stocks in many different industries.
- **Economies of Scale** - Because a mutual fund buys and sells large amounts of securities at a time, its transaction costs are lower than what it would cost an individual.
- **Liquidity** - Just like an individual stock, a mutual fund allows you to request that your unit holdings in the fund be converted into cash at any time.



Types of Mutual Fund Schemes

A wide variety of Mutual Fund Schemes exist to cater to a variety of needs such as risk tolerance and return expectations etc. Broadly these schemes can be classified as:

In terms of lock-in periods and redemption:

A. Open-ended Funds

These funds are generally open for subscription and redemption i.e. bought and sold, throughout the year. Their prices are linked to the daily net asset value (NAV). From the investors' perspective, they are much more liquid than closed-ended funds.

B. Close-ended Funds

These funds are open initially for entry during the New Fund Offer (NFO) period (similar in concept to IPOs for stocks) and thereafter closed for entry as well as exit. These funds are open for subscription only once and can be redeemed only on the fixed date of redemption, normally after 3 years. However, in some cases, the units of these funds are listed on stock exchanges and are tradable enabling subscribers to the fund to exit from the fund at any time through the secondary market.

In terms of type of investment made, mutual funds may be classified as:

A. Equity Funds/ Growth Funds

Funds that primarily invest in equity shares are called equity funds. They carry the principal objective of capital appreciation of the investment over the medium to long-term. They are best suited for investors who are seeking capital appreciation, and have a high risk tolerance as well. There are different types of equity funds such as Diversified funds, Sector specific funds and Index based funds.

B. Debt/Income Funds

These funds invest predominantly in high-rated fixed-income-bearing instruments like bonds, debentures, government securities, commercial

paper and other money market instruments. They are best suited for the medium to long-term investors who are averse to risk and seek capital preservation.



C. Balanced Funds

These funds invest both in equity shares and fixed-income-bearing instruments (debt) in some proportion i.e. they are a mix of equity and debt funds. They provide a steady return and reduce the volatility of the fund while providing some upside for capital appreciation. They are ideal for medium to long-term investors who are willing to take moderate risks.



Systematic Investment Plans (SIPs) and Rupee Cost Averaging

SIPs for Mutual funds are based on the principle of Rupee cost averaging i.e. systematically investing a fixed rupee amount at regular time intervals, which smoothens out the ups and downs of the market in the long run. This method eliminates the need to time the market (making an entry or an exit) -- an area where most investors are prone to go wrong.

Under this system, one need not worry about when and how much to invest. A fixed sum of money can be invested regularly (at the very minimum once a month) and over time it averages out the costs. Thus, if one were to buy units of a mutual fund -- by following rupee cost averaging, the fixed amount of money will fetch more units when the cost of the units are down, and vice versa.

Rupee cost averaging, however, cannot guarantee a positive return in a declining market and you must consider your ability to continue investing on a regular basis under all market conditions. **Let us look at the table below as an example of the benefits of SIPs.**

Time (months)	Fixed amount invested (Rs)	Price per unit(NAV) (Rs)	Mutual Fund units purchased
1	1000	20	50
2	1000	22	45
3	1000	19	52
4	1000	18	55
5	1000	17	58
6	1000	21	47
7	1000	23	43
8	1000	22	45
9	1000	21	47
10	1000	24	41
TOTAL	**10000**	**20.70**	**483**

A look at the table shows how investing regularly can fetch you more units of a mutual fund through rupee cost averaging. In the above example, if you had invested in lump sum at Rs. 22 per unit, you would have ended up buying 454 units.

Instead, if one were to invest Rs 1,000 every month for 10 months, the total number of units purchased adds up to 483, since these were bought at different price levels and the average cost of each unit comes down to Rs 20.7.

And 480 units would definitely fetch a higher return than 454 at the end of ten months.

Now, while Prakash is all excited about all this talk of investments and money, it is important for him to understand one other aspect of financial planning that has an equally important role to play in his life, and is essential to ensure the future financial stability of his family.



Life Insurance

While Prakash might think he is too young to consider Life Insurance at his age, it is very important that he understands the importance and utility of life insurance for his later years in life. Insurance is always bought and never sold, and the earlier you start your own life insurance policy, the lesser the premium amount that you would have to pay to the insurance company.

Insurance is protection against financial loss arising on the happening of an eventuality. In life insurance parlance, the event happens to be the death of an individual.

To begin with, there are two basic types of plans; endowment plans and term plans. All other plans are actually variations of these two. In an **endowment plan,** the premium paid, apart from the death cover also includes a savings element that is invested in different investment instruments to generate returns in the long-term.



A term plan, however is a pure risk cover plan. A term policy insures the life only for a certain number of years, known as the term.. There is no savings element and as a result the insured does not receive anything should he survive the entire term. However, since term life policies often expire without the insurer needing to pay a death benefit, the cost of term life insurance is much lower.

Many financial experts consider life insurance to be the cornerstone of sound financial planning. It can be an important tool to replace income for dependents. This is the primary and most important reason for taking life insurance. Life insurance aims to help those that survive you retain their financial independence by compensating them for income lost through your death

Insurance policies can also be used to create an inheritance for your heirs/charitable contributions. Even if you have no other assets to pass to your heirs or a charity of your choice, you can create an inheritance by buying a life insurance policy and naming them as beneficiaries.



DON'T BUY LIFE INSURANCE SOLELY AS AN INVESTMENT

Life insurance premiums, depending upon the policy selected, include the costs of -

1) Death-benefit coverage

2) Built-in investment returns (average 8.0% to 9.5% post-tax)

3) Significant overheads, including commissions.

This implies that if you buy insurance solely as an investment, you are incurring costs that you would not incur in alternate investment options.

Since Prakash does not have anyone depending on him right now, a life insurance product might not be suitable for him at this age. However, he should definitely keep the lessons that he has learnt about insurance in mind once he has his own family to look after.

GETTING STARTED.....



A. How to Open a Savings Bank A/C

A Saving Bank account is meant to promote the habit of saving among people. It also facilitates safekeeping of money. Hence a savings account is a safe, convenient and affordable way to save your money

Savings Bank Account can be opened in the name of an individual or in joint names of the depositors. Savings Bank Accounts can also be opened and operated by the minors provided they are more than ten years old.

Things to Consider While Opening a Savings Account

It is advisable to seek the following information from bank before opening the account:

- Minimum balance requirements.
- Penalties if any in case the balance falls below the minimum amount
- Penalty in case of bounced cheques.
- Details of charges, if any for issue of cheque books and limits fixed on number of withdrawals, cash drawings, etc.

Document Required For Opening a Savings Account

- Two passport size photographs
- Proof of residence i.e. Passport/driving licence/Gas / Telephone / Electricity Bill/ Ration card/voters identity card
- An introduction of the person from an existing account holder.
- PAN number / Declaration in form no.60 or 61 as per the Income Tax Act 1961.

Once you have your savings account in place, you can approach the same bank for fixed deposits and recurring deposits as well.



B. How to invest in Mutual Funds

How do you evaluate a mutual fund - Things to know

1. **List out your investment objectives** in order to identify which type of a mutual fund suits you best. Do you think a growth fund or a debt fund or a balanced fund is best for you?
2. **Begin your search.** Most financial websites and magazines rate mutual funds according to returns performance, risk and other parameters.
3. **Get to know the basic makeup of your mutual fund,** since mutual funds typically contain a variety of securities, including stocks, bonds and certificates of deposit. Some funds may even have a specific sectoral focus or concentration.
4. **Examine performance -** in particular, a fund's long-term performance, at least over a period of 3-5 years. Also, look at a fund's volatility. A stable fund will have consistent returns from year to year, while a fund with greater risk may go through greater ups and downs.

Investors in Mutual Funds need to comply with 'Know Your Customer' (KYC) norms

KYC is an acronym for Know your Customer, a term commonly used for Client Identification Process. SEBI has prescribed certain requirements to enable Financial Institutions to know their clients. This would be in the form of verification of identity and address, providing information of financial status, occupation and such other demographic information. It is important that you are KYC compliant while investing with any SEBI registered Mutual Fund.

Documents and information to be provided by investors:

Investors in mutual fund schemes have to provide:

- Proof of Identity - PAN Card
- Proof of Address
- Photograph

Investors can contact the agents and distributors of mutual funds who are spread all over the country for necessary information and application forms. These days you can also buy mutual funds via your online trading account



C. How to invest in Stocks

The buying and selling of selling securities is done through a platform called the 'Stock Exchange', where willing parties transact through an intermediary called a broker. Transactions may also occur through a sub-broker, i.e., an agent of a broker. As per the Securities and Exchange Board of India (SEBI) rules, only registered brokers and sub-brokers can buy, sell or deal in securities. It is, hence, essential for an investor to open an account with a broker before he starts buying or selling securities.

Choosing a broker – There are more than 8,000 SEBI registered brokers and sub-brokers, (details of SEBI registered brokers is available on the SEBI website)

All brokers provide a similar service, i.e., buying and selling securities. Given this large number, it would be very difficult for you to find the right broker. You must, hence, look for the following factors before selecting a broker:

- Reputation
- Flexibility
- Broking rates
- Different modes of transactions
- Service Quality

Direct Access Trading Accounts - However, there is also a way for investors to directly access the market as well through online trading and direct access accounts, popularly known as Demat A/Cs which eliminates the need for intermediaries. A lot of banks now offer the



option of online trading portals where you can trade from the convenience of your home.

The following documents are required to open a demat account:

- Proof of residence (NSDL and CDSL provide a list of acceptable documents as Proof of residence, which include electricity bill, phone bill, ration card, driving licence etc.)
- Proof of identity (PAN card is mandatory)
- Bank account details (A cancelled cheque for capturing MICR)
- Nominee details

Need for a banking account – Transactions involving shares require movement of money in and out of your account. Hence, bank accounts are mandatory along with broking and demat accounts. You may use your savings account for purchase and sale of shares by notifying the bank account details in your demat and broking account. Bank account details must get properly captured in a demat account as benefits like dividend and interest are directly credited in the bank account.

Starting investments – Once you are through with this paper work, you are ready to start investing. Just give a call to your relationship manager assigned to you for buying and selling of shares on the market from 8: 55 a.m. to 3:30 p.m. on all working days. You can similarly trade in bonds, or other instruments.

Eight Ground Rules for Investing

The basic principles of investing are simple. Anyone can become a good investor just by following a few simple and easily understood rules, which also help avoid big mistakes. Here are just a few rules for investment success.

I. **Invest Regularly:** Investing a little bit of money each month is the surest way to reduce the risk of investing, and I'm sure you would



have understood by now that the greatest risk is not investing at all. Remember the story of the tortoise and the hare! Slow and steady wins the race.

II. **Start investing early.** Compounding is your best friend. The longer you have your money working for you, the more you will gain.

III. **Investing is a long-term proposition**. Research your investments, remember your goals, re-examine your risk, and limit how much you listen to day-to-day market commentary.

IV. **Pay attention to what is going on with your investments.** No investment is safe forever. Make sure you have a re-look at your investments at regular time intervals.

V. **Diversify.** Your asset mix should be spread across various asset classes with a mix of shares, bonds, short-term investments, real estate, and perhaps even other things.

VI. **Be realistic about your tolerance for risk.** Ask yourself, "How well will I sleep if my investments drop in value by 10%? By 20%? By 50%?" Invest as per your risk appetite. Understand the risk involved in going ahead with the decision and see if it matches your risk appetite. Only if you are comfortable with the risk involved, should you go ahead with the investment.

VII. **Employ Disciplined Principles.** Invest regularly and intentionally. Force yourself to put your money to work, but don't just throw your money at any investment. Choose your investments wisely.

VIII. **Get Help If You Need It.** The do-it-yourself approach may not be suitable for everyone. If you try it and it's not working, or you're afraid to try it at all, or you don't have the time or desire, then you should seek professional assistance. If you want others to handle your financial affairs for you, remain involved to some degree, to make sure your money is being spent wisely.



A broad checklist to be maintained before making any Investment

Here is a checklist before making an investment

- Obtain written documents explaining the investment.
- Read and understand such documents.
- Verify the legitimacy of the investment, i.e. Do your own research
- Find out the costs and benefits associated with the investment.
- Assess the risk-return profile of the investment.
- Know the liquidity and safety aspects of the investment.
- Ascertain if it is appropriate for your specific goals.
- Compare these details with other investment opportunities available.
- Examine if it fits in with other investments you are considering or you have already made.
- Deal only through an authorised intermediary.
- Seek all clarifications about the intermediary and the investment.

Explore the options available to you if something were to go wrong, and then, if satisfied, make the investment.

“

- **A 'get rich quick' scheme could just as easily mean a 'get poor quicker' scheme.**
- **If it sounds too good to be true it probably is.**

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Lesson to be remembered – The benefit from compounding arises primarily from the fact that income keeps multiplying over the principal amount to generate higher absolute returns each year. The longer you leave your investment to grow the better it is. To summarise, the power of compounding is the single most important reason for you to start investing right now. **Remember, every day that your money is invested, is a day that your money is working for you.**



Who polices our Financial Markets?

I. SECURITIES AND EXCHANGE BOARD OF INDIA (SEBI)

The Securities and Exchange Board of India (SEBI) is the regulatory authority in India for the capital markets, with statutory powers for (a) protecting the interests of investors in securities (b) promoting the development of the securities market and (c) regulating the securities market. Its powers broadly include:

1. Regulating the business in stock exchanges and any other securities markets
2. Registering and regulating the working of stock brokers, sub–brokers etc.
3. Promoting and regulating self-regulatory organisations
4. Prohibiting fraudulent and unfair trade practices
5. Calling for information from, undertaking inspection, conducting inquiries and audits of the stock exchanges, intermediaries, self – regulatory organisations, mutual funds and other persons associated with the securities market.

II. RESERVE BANK OF INDIA (RBI)

The Reserve Bank of India was established on April 1, 1935 in accordance with the provisions of the Reserve Bank of India Act, 1934. In simple words, the Reserve Bank could be thought of as a policeman of the Indian economy in charge of its monetary and financial security. The



Reserve Bank is the umbrella network for numerous activities, all related to the nation's financial sector, encompassing and extending beyond the functions of a typical central bank.

Its primary functions include:

- Monetary Authority
- Issuer of Currency
- Banker and Debt Manager to Government
- Banker to Banks
- Regulator of the Banking System
- Manager of Foreign Exchange
- Regulator and Supervisor of the Payment and Settlement Systems
- Developmental Role

In the absence of any central banking institution in India until 1935, The Imperial Bank of India actually performed a number of functions which are normally carried out by a central bank in addition to all the normal functions which a commercial bank was expected to perform. The Imperial Bank of India would later be re-christened as the State Bank of India in 1955

You can learn about these functions in detail at:
http://rbidocs.rbi.org.in/rdocs/Publications/PDFs/RBI290410BC.pdf

Banking Ombudsman

The RBI defines the Banking Ombudsman Scheme as an expeditious and inexpensive forum to bank customers for resolution of complaints relating to certain services rendered by banks. In short, if the RBI is the policeman for the banking sector, the ombudsman could be thought of as your local area beat constable. The location of your nearest ombudsman is viewable at http://www.rbi.org.in/Scripts/bs_viewcontent.aspx?Id=164.

Some of the grounds for complaints that the Banking Ombudsman can receive and consider relating to the following deficiency in banking services (including internet banking). A full list of the grounds for complaints is http://www.rbi.org.in/Scripts/FAQView.aspx?Id=24

III. INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY (IRDA)



Like what the Reserve Bank is to the banking sector, Insurance Regulatory & Development Authority (IRDA) is to the insurance sector. The IRDA is regulatory and development authority under Government of India in order to protect the interests of the policyholders and to regulate, promote and ensure orderly growth of the insurance industry. This organisation came into being in 1999 after the bill of IRDA was passed in the Indian parliament.

A few of the chief functions of IRDA include:

- It issues to the applicant in insurance arena a certificate of registration, renew, modify, withdraw, suspend or cancel such registration
- It protects the interests of the policy holders in any insurance company in the matters related to the assignment of policy, insurable interest, resolution of insurance claim, and other terms and proposals in the contract.
- It also specifies code of conduct and practical instructions for mediator as well as the insurance company.
- IRDA is also entitled to ask for information, undertake inspection and investigate the audit of the insurers, mediators, insurance intermediaries and other organisations related to the insurance sector.
- It is also empowered to be involved in the settlement of disagreements between insurers and intermediaries or insurance intermediaries.

You can find out more about the Duties, Powers and Functions of IRDA at: http://www.irdaindia.org/



Insurance Ombudsman

Similar to the Banking Ombudsman in purpose, the IRDA has set up the Insurance Ombudsman for the quick disposal of the grievances of the insured customers. A complete list of insurance ombudsman and their areas of jurisdiction is available on the IRDA website. Insurance Ombudsman has two types of functions to perform (1) conciliation, (2) Award making. The insurance Ombudsman is empowered to receive and consider complaints in respect of personal lines of insurance from any person who has any grievance against an insurer. You can look up the IRDA website for further details.

We hope this book has helped you understand the basics of finance the way it has Prakash. Financial planning is not something that concerns only your parents or grandparents, and we hope this little guide has shown you the importance of managing your finances early on into your life. We expect that you use this book as a stepping stone for a greater understanding of financial terms and concepts and towards managing your personal finances.

To start off, maybe you could try and see if your parents are aware of the need for financial planning in their lives.

A FEW A, B, C, Ds of FINANCE – A Glossary of Financial Terms

Let us spare some time to understand some of the instruments and everyday terminologies of financial markets:-

Annual General Meeting: This is a yearly meeting of shareholders at which the company management reports and discusses the company's annual results with shareholders.

Annual Report: It is an annual financial statement of a company's state of affairs at the end of the financial year, showing its assets, liabilities, revenues, expenses and earnings. It contains all relevant information of interest to shareholders. The important contents include the profit and loss statement, Balance Sheet and Cash Flow statement.

Annuity: An Annuity is an investment or insurance policy that pays a fixed sum of money each year periodic payment to the policyholder for a specified period of time.

Assets: Assets are anything of value that is own by an individual or a company

Bad debt: Bad debts are arrears or liabilities that a company deems uncollectible and hence writes it off.

Balance Sheet: It is a representation of the financial position of an enterprise as on date, with information about its assets, liabilities, and net worth at a specific time

Bankruptcy: A term that describes the legal procedure for companies unable to meet their financial commitments and effectively have no money to pay off their debts.

Blue chip Company: A share of a company that is financially very sound, with an established brand name and widely known for the quality and wide acceptance of its products or services, and for its ability to make money and pay dividends.

Broker: An intermediary who charges commission in return for buying and selling securities, commodities or other property on behalf of the public.

Credit Rating: The exercise of assessing and grading the credit record, integrity and capability of a potential borrower to meet their financial commitments.

Capital gain/loss: The excess earned from the sale of a capital asset over and above its cost price is known as capital gain. (A capital gain that persists for one year or less is called a short-term capital gain. Likewise, one that persists for more than one year is called a long-term capital gain). Similarly a loss on the sale of a capital asset is known as a capital loss.

Contract Note: Contract Note is a confirmation of trades done on a particular day on behalf of the client by a trading member. It imposes a legally enforceable relationship between the client and the trading member with respect to purchase/sale and settlement of trades.

Default risk: The risk that a company will default, or fail to meet its financial obligations, i.e., fails to pay the interest or principal on its bonds

Depreciation: The decrease in value of an asset due to wear and tear, obsolescence, decline in price, e.g., a new car purchased at Rs. 500000 might be worth only Rs. 50, 000 in five years

Disposable income: The amount of personal income an individual has after taxes and government fees, which can be spent on necessities, or non-essentials, or be saved.

Depository: It works similar to a financial sector bank, except that in a depository the deposits are financial instruments (eg. shares, debentures, bonds, government securities, units etc.) in electronic form.

Dematerialization: Dematerialization is the process by which physical certificates of an investor are converted to an equivalent number of securities in electronic form and credited to the investor's account with his Depository Participant (DP).

Face Value of a share/debenture: Also known as Par value or simply par, Face value is the nominal or stated amount (in Rs.) assigned to a security by the issuer. For shares, it is the original cost of the stock shown on the certificate; for bonds, it is the amount paid to the holder at maturity. For an equity share, the face value is usually a very small amount (Rs. 5, Rs. 10) and does not have much bearing on the price of the share. However, the price at which the security trades greatly depends on the fluctuations in the interest rates in the economy.

Financial intermediaries: Institutions that provide the market function of matching borrowers and lenders or buyers with sellers.

Fund manager: The person whose responsibility it is to oversee the allocation of the pool of money invested in a particular mutual fund. The fund manager is charged with investing the money to attain the returns and level of risk of the mutual fund investors.

Hedging: The action of combining two or more transactions or two or more investment positions so as to achieve a reduce risks. The objective, generally, is to protect a profit or minimize volatility that may result on a transaction

Informational efficiency: It refers to the speed and accuracy with which new information is reflected in prices,

Insider: A term used for one who has access to information concerning a company that is not available in public domain and enables him or her to make substantial profits in share transactions. It is illegal for holders of this information to make trades based on it, however received.

Insolvent: An insolvent firm is one that is unable to pay debts i.e. its liabilities exceed its assets.

Junk Bonds: The debt securities of companies bearing a considerable degree of risk that is reflected in their mediocre or poor credit ratings. They are alternatively referred to as 'Low-grade' or 'High-risk' bonds, and often pays a higher rate of interest to compensate for their low ratings.

Lock in period: A lock in period refers to a period of time for which a person cannot sell his shares/securities.

Liabilities: These include all the claims and obligations of a person or company to pay money to another party.

Market Manipulation: Any false or misleading activity or operation that aims at raising or depressing the price to induce purchase or sale by others.

Market Capitalization: The value of equity shares outstanding at prevailing market prices.
Market capitalization = Number of shares x Market price of each share.

Market price: The last reported price at which the stock or bond sold, or the current quote.

Net Asset Value (NAV): In simple terms, the NAV of a mutual is the summation of the market value of all investments made by a mutual fund with its investment corpus divided by the number of units outstanding.

Paper gain (loss): Unrealized capital gain (loss) on securities held in a portfolio based on a comparison of current market price to original cost.

Prospectus: It is very important that an investor before applying for any issue has an idea future potential of a company. A Prospectus is a formal written document that describes the plan for a proposed business enterprise, or the facts concerning an existing one, that an investor needs to make an informed decision. In the case of mutual funds, they describe fund objectives, risks, and other essential information.

Premium and Discount in a Security Market: Securities are generally issued in denominations of 5, 10 or 100. This is known as the Face Value or Par Value of the security as discussed earlier. When a security is sold above its face value, it is said to be issued at a Premium and if it is sold at less than its face value, then it is said to be issued at a Discount.

Portfolio: A Portfolio is a combination of different investment assets mixed and matched for the purpose of achieving an investor's goal(s).

This includes financial assets such as shares, debentures, bonds, mutual fund units to items such as gold, art and even real estate etc.

Real assets: Identifiable assets, such as land and buildings, equipment, patents, and trademarks, as distinguished from a financial investment.

Real rate of return: The percentage of return on an investment over one year after adjustments for inflation

Redemption: Repayment of a debt security or preferred stock issue, at or before maturity, at par or at a premium price.

Retained earnings: Accounting earnings that are retained by the firm for reinvestment in its operations; earnings that are not paid out as dividends.

Riskless or risk-free asset: An asset whose future return is known today with certainty; normally the interest rate on a government bond is taken as the risk-free asset.

Secured debt: Debt that has first claim on specified assets in the event of default.

Speculation: An approach to investing that relies more on chance and involves purchasing risky investments that present the possibility of large profits, but also pose a higher-than-average possibility of loss.

Takeover: General term referring to transfer of control of a firm from one group of shareholders to another group of shareholders. Change in the controlling interest of a corporation, either through a friendly acquisition or a hostile bid.

Voting right: This refers to the Common stockholders' right to vote their stock in affairs of a company. Preferred stock usually has the right to vote when preferred dividends are in default for a specified period. The right to vote may be delegated by the stockholder to another person.

Yield: The percentage rate of return paid on a stock in the form of dividends, or the effective rate of interest paid on a bond or note.

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