Personal Finance and Tax Planning

Unit- I

UNIT-I: Introduction to Personal Finance: Definition, Importance & Need of Personal Finance, Key areas of Personal Financial Management, Personal Financial Management Processes. Introduction to Personal Finance

Introduction to Personal Finance

Personal finance is the process of managing your money to achieve financial stability and future goals. It includes:

- **Earning** – income from jobs, side hustles, or allowances.
- **Spending** – expenses like food, transportation, tuition, and entertainment.
- **Saving** – setting aside money for emergencies or future needs.
- **Investing** – using money to grow wealth over time.
- **Protecting** – managing risks with insurance and financial planning.

Why is Personal Finance Important?

- Builds **money management habits** early.
- Helps avoid **debt traps** (like credit card overspending).
- Encourages **saving for emergencies** or big goals (travel, gadgets, future studies).
- Teaches **decision-making skills** (needs vs. wants).
- Lays the foundation for **financial independence** after graduation.

Key Principles of Personal Finance

- **Budgeting:** Track income and expenses to live within your means.
- **Saving First:** Follow the "Pay Yourself First" rule—save before spending.
- **Avoiding Debt:** Use credit wisely; borrow only what you can repay.
- **Emergency Fund:** Keep at least 3–6 months of expenses saved.
- **Investing Early:** The earlier you start, the more your money grows (thanks to compound interest).
- **Setting Goals:** Short-term (buying a laptop), medium-term (study abroad), long-term (retirement).

Case Study: The Story of Riya and Arun

Background: Riya and Arun are both 20-year-old college students. They receive the same monthly allowance of **₹5,000** from their parents.

Riya's Approach (No Financial Planning):

- Eats out almost every day.
- Buys clothes and gadgets on impulse.
- Uses credit card for online shopping (doesn't track expenses).
- At the end of the month, she often borrows from friends or parents.
- By the end of the year, she has **no savings** and **₹10,000 debt** on her credit card.

Arun's Approach (Practices Personal Finance):

- Creates a **monthly budget**:
    - ₹2,500 for food & transport
    - ₹1,500 for personal expenses
    - ₹1,000 savings
- Looks for **student discounts** and avoids unnecessary purchases.
- Builds an **emergency fund** of ₹12,000 by the end of the year.
- Uses a digital app to track expenses.

Result after 1 Year:

- **Riya:** Struggles with debt, stress, and depends on parents.
- **Arun:** Has savings, no debt, and peace of mind. He even invests ₹5,000 of his savings in a mutual fund.

Conclusion:

1. **Personal finance is not about how much money you get—it's about how you manage it.**
2. **Budgeting, saving, and avoiding unnecessary debt make a big difference.**
3. **Small financial habits built in student life lay the foundation for financial independence later**.

Need and Importance of Personal Finance:

Need for Personal Finance

- **Rising Costs of Living & Education:** Students face increasing expenses (tuition, rent, food, gadgets). Managing money is essential to avoid financial stress.
- **Limited Income Sources:** Most students rely on allowances, part-time jobs, or scholarships. Smart money management helps stretch a limited income.
- **Early Exposure to Credit & Debt:** Credit cards, student loans, and online shopping make it easy to overspend. Learning personal finance helps avoid debt traps.
- **Financial Independence:** Students need to learn how to rely less on parents and manage their own finances.

- **Preparation for the Future:** Decisions made during student life (saving, borrowing, spending habits) impact future financial health.
- **Limited Income Sources** – Most people depend on a fixed salary or a single source of income. Personal finance helps stretch and allocate resources wisely.
- **Debt Management** – With easy access to loans and credit cards, poor planning can lead to debt traps. Personal finance teaches responsible borrowing.
- **Future Goals** – Buying a house, children's education, travel, or retirement require systematic planning.

Importance of Personal Finance

- **Encourages Responsible Spending:** Helps differentiate between *needs* and *wants*.
- **Promotes Saving Culture:** Builds the habit of saving regularly—even small amounts.
- **Reduces Stress:** Financially disciplined students feel less anxious about money.
- **Supports Goal Achievement:** Enables planning for short-term goals (gadgets, trips), medium-term (further studies), and long-term (career, retirement).
- **Builds Creditworthiness:** Good financial behavior (timely loan/credit payments) improves credit score for future needs like car loans, mortgages, or business funding.
- **Foundation for Wealth Creation:** Early investing and money management lead to financial security later in life.
- **Promotes Financial Independence** – Reduces dependency on others (family, friends, or loans).
- **Ensures Retirement Planning** – Early planning helps maintain a comfortable lifestyle after retirement.
- **Provides Financial Security** – Emergency funds and insurance protect against sudden shocks.

Key Areas of Personal Financial Management:

1. Income Management

- Understanding all sources of income (salary, allowance, business, side hustle).
- Planning how to allocate it effectively.

2. Budgeting

- Creating a plan for spending and saving.
- Tracking expenses to ensure you live within your means.
- Differentiating between **needs vs. wants**.

3. Saving

- Setting aside money regularly for short-term needs and emergencies.
- Building an **emergency fund** (3–6 months of expenses).

4. Investing

- Growing wealth through investments (stocks, mutual funds, bonds, real estate).
- Understanding **risk and return**.
- Starting early to benefit from **compound interest**.

5. Debt & Credit Management

- Using loans and credit cards wisely.
- Avoiding unnecessary debt.
- Maintaining a **good credit score** for future financial needs.

6. Insurance & Risk Management

- Protecting against financial losses due to accidents, illness, or disasters.
- Health, life, and property insurance are key safeguards.

7. Retirement & Long-Term Planning

- Planning for financial security after active working years.
- Contributing to retirement accounts or pension plans.

8. Tax Planning

- Understanding and managing taxes efficiently.
- Using legal ways (deductions, exemptions) to reduce tax burden.

9. Estate Planning

- Preparing wills, trusts, and succession planning.
- Ensuring smooth transfer of wealth to heirs.

Case Study 1: Retirement Planning

Situation: Ananya is 22 years old, has just completed her MBA, and got her first job with a monthly salary of ₹40,000.

Decision Point:

- Option A: Spend most of her salary and save only ₹500/month.
- Option B: Start a **Systematic Investment Plan (SIP)** of ₹2,000/month in a mutual fund that gives ~12% return.

Outcome after 38 years (at age 60):

- **Option A (₹500/month)** → Around **₹19 lakh**
- **Option B (₹2,000/month)** → Around **₹77 lakh**

Lesson: By starting small and early, Ananya secures her retirement and avoids depending only on family or government pensions.

Case Study 2: Estate Planning

Situation: Rahul, a 25-year-old software engineer, has A bank balance of ₹3 lakh, A bike worth ₹80,000, A term insurance policy worth ₹20 lakh and He has aging parents who depend on him.

Decision Point:

- Rahul writes a **simple will** stating that his parents will inherit all his assets.
- He also nominates them as beneficiaries in his bank account and insurance policy.

Outcome:

- If something happens to Rahul, his parents can **directly access his savings and insurance** without legal struggles.
- Without estate planning, they might face long legal battles to claim the money.

Lesson: Estate planning is not only for the rich or elderly — it ensures your loved ones are financially secure and reduces disputes.

Case Study: Tax Planning for a Young Professional

Situation: Arjun, a 24-year-old software engineer, earns **₹5,00,000 per year** (₹41,600/month). He wants to reduce his tax liability.

Without Tax Planning:

- His taxable income = ₹5,00,000
- According to tax slabs, he ends up paying around **₹12,500 in income tax**.

With Tax Planning (Legal & Smart Choices):

Arjun decides to use deductions under the Income Tax Act (India):

1. **Section 80C**: Invests ₹1,00,000 in ELSS Mutual Funds + PF.
2. **Section 80D**: Buys health insurance premium for parents = ₹20,000.
3. **Education Loan Interest**: Pays ₹30,000 interest on his student loan.

Now, his **taxable income** = ₹5,00,000 – (₹1,00,000 + ₹20,000 + ₹30,000) = **₹3,50,000**

Tax Result:

- Instead of paying ₹12,500, his tax reduces to about **₹2,500 only.**
- **Savings = ₹10,000**

Lesson : Tax planning is not about avoiding tax—it's about using **legal deductions and exemptions** wisely.

Personal financial management process

Personal Financial Management Process

1. Assessing Financial Situation

- Review income, expenses, savings, debts, and assets.
- Example: A student checks allowance + part-time income vs. hostel, food, and travel costs.

2. Setting Financial Goals

- Define short-term, medium-term, and long-term goals.
- Example: Save ₹5,000 for a new phone (short-term), ₹50,000 for study abroad (medium-term), plan retirement savings (long-term).

3. Creating a Financial Plan (Budgeting & Strategy)

- Develop a plan to achieve goals.
- Example: Allocate 50% for needs, 30% for wants, 20% for savings/investments.

4. Implementing the Plan

- Put the plan into action.
- Example: Start saving ₹1,000/month in a savings account or SIP, cut down on unnecessary spending.

5. Monitoring and Tracking

- Regularly check if spending and saving match the plan.
- Example: Use an app or Excel to track daily expenses and compare with the budget.

6. Reviewing and Adjusting

- Modify the plan as income, expenses, or goals change.
- Example: If a student gets a part-time job, increase savings and reduce reliance on parents.

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Unit -II Investment Decisions

UNIT-II: Introduction to Investment Decisions: Investment, Speculation and Gambling, Features of Investment, Investment Process, the Investment Environment, Securities Market of India, Securities Trading and Settlement, Types of Orders, Margin Trading.

Indian financial system and its components

A **financial system** is a set of institutions, markets, instruments, rules, and procedures that facilitate the **flow of funds** between savers (investors) and borrowers (users of funds) in an economy.

The financial system helps people and organizations **save**, **invest**, **borrow**, and **manage risk**. It acts like a bridge between those who have surplus money and those who need money for productive purposes.

Key Functions of a Financial System:

1. **Mobilization of savings**
2. **Allocation of capital to productive investments**
3. **Facilitation of credit and liquidity**
4. **Risk management through insurance and derivatives**
5. **Price discovery of financial assets**
6. **Promoting economic growth and stability**

The **Indian Financial System** is a complex network of institutions, markets, instruments, and services that facilitate the flow of funds within the economy. It plays a vital role in economic development by mobilizing savings and allocating them efficiently to productive investments.

Components of the Indian Financial System

The Indian Financial System can be broadly divided into the following components:

1. Financial Institutions

These are entities that provide financial services like savings, investment, loans, and insurance.

a. Banking Institutions

- **Commercial Banks** :

  These are profit-making institutions that accept deposits and provide loans and other financial services.

  Examples:

  - **State Bank of India (SBI)** – Public sector
  - **Punjab National Bank (PNB)** – Public sector
  - **ICICI Bank** – Private sector
  - **HDFC Bank** – Private sector
  - **Axis Bank**

- **Bank of Baroda**

- **Cooperative Banks:**

  These are member-owned financial institutions that work on a cooperative model, especially in rural and semi-urban areas.

  Examples:

  - **The Saraswat Cooperative Bank**
  - **The Shamrao Vithal Cooperative Bank**
  - **The Punjab State Cooperative Bank**
  - **The Maharashtra State Cooperative Ban**
  - **Abhyudaya Cooperative Bank**

- **Regional Rural Banks (RRBs):**

  These are government-sponsored banks set up to serve rural areas and promote financial inclusion.

  Examples:

  - **Prathama UP Gramin Bank** (sponsored by PNB)
  - **Andhra Pragathi Grameena Bank** (sponsored by Canara Bank)
  - **Kerala Gramin Bank** (sponsored by Canara Bank)
  - **Karnataka Gramin Bank** (sponsored by Canara Bank)

- **Small Finance Banks:**

  These are niche banks aimed at providing financial services to underserved and unbanked sections, like small farmers and MSMEs.

  Examples:

  - **AU Small Finance Bank**
  - **Equitas Small Finance Bank**
  - **Ujjivan Small Finance Bank**
  - **Suryoday Small Finance Bank**
  - **Jana Small Finance Bank**
  - **Payments Banks**

- **Payments Banks**

  These banks offer basic banking services like deposits, remittances, and payments (but cannot offer loans or credit cards).

  Examples:

  - **Airtel Payments Bank**
  - **India Post Payments Bank**
  - **Paytm Payments Bank**
  - **Fino Payments Bank**
  - **Jio Payments Bank**

b. Non-Banking Financial Companies (NBFCs)

- Provide similar services as banks but do not hold a banking license.
- Examples: Bajaj Finance, LIC Housing Finance

c. Development Financial Institutions (DFIs)

- Long-term project financing
- Examples: NABARD, SIDBI, EXIM Bank

2. Financial Markets

Platforms where financial instruments are traded.

a. Money Market (short-term funds, <1 year)

- Instruments: Treasury bills, Commercial papers, Certificates of deposit
- Regulated by RBI

b. Capital Market (long-term funds)

- **Primary Market**: IPOs (Initial Public Offerings)
- **Secondary Market**: Stock trading (e.g., NSE, BSE)
- Regulated by SEBI

c. Foreign Exchange Market (Forex Market)

- For currency trading

d. Derivatives Market

- Futures, options, swaps for risk management

3. Financial Instruments

These are products that are traded in financial markets.

- **Equity Shares**
- **Debentures/Bonds**
- **Treasury Bills**
- **Mutual Funds**
- **Derivatives (Futures & Options)**
- **Insurance Products**

4. Financial Services

Supportive services that facilitate financial transactions.

- **Investment Services**
- **Insurance Services**
- **Asset Management**

- **Credit Rating Services** (e.g., CRISIL, ICRA)
- **Stock Broking**

5. Regulatory Bodies

Ensure transparency, stability, and investor protection.

Regulator	**Role**
Reserve Bank of India (RBI)	Regulates banking and money markets
Securities and Exchange Board of India (SEBI)	Regulates capital markets
Insurance Regulatory and Development Authority (IRDAI)	Regulates insurance sector
Pension Fund Regulatory and Development Authority (PFRDA)	Regulates pension sector

Investment Decisions:

Introduction to investment Decisions:

"Investment Decisions", including **investment, speculation, and gambling**

Investment, Speculation, and Gambling

Investment

- **Definition**: Investment is the commitment of funds to an asset or project with the expectation of generating a return in the future. Or **Investment** refers to the **allocation of money or resources** into an asset, project, or venture with the **expectation of generating income or profit** in the future. Or Investment is the process of committing money or capital to an endeavor (such as stocks, bonds, real estate, or a business) with the expectation of obtaining an additional income or profit over time.
- **Objective**: To earn a **stable** and **secure** return over a **long period**, with relatively **low risk**.
- **Examples**: Buying shares, bonds, mutual funds, real estate.

  Example of Investment – Case Study: Investing in Equity Shares

  Investor Profile

    - **Name**: Rohan Sharma
    - **Age**: 30
    - **Profession**: Software Engineer
    - **Investment Objective**: Long-term wealth creation for retirement
    - **Risk Appetite**: Moderate

  Investment Decision

Rohan decides to invest ₹1,00,000 in **Infosys Ltd. shares** in January 2019, **Stock price in Jan 2019**: ₹650 per share, **Number of shares bought**: ₹1,00,000 ÷ ₹650 ≈ **154 shares**

Dividends Received (2019–2023)

Infosys paid average dividends of ₹15 per share per year.

Total Dividends (5 years) = 154 × ₹15 × 5 = ₹11,550

Capital Appreciation

By January 2024, Infosys share price rose to **₹1,550**.

Value of investment in 2024 = 154 × ₹1,550 = **₹2,38,700**

Returns Summary

Component	**Amount (₹)**
Initial Investment	1,00,000
Dividend Income	11,550
Final Value (2024)	2,38,700
Total Gain	2,38,700 + 11,550 − 1,00,000 = **₹1,50,250**
Return on Investment	150.25% in 5 years

Analysis

- Rohan's decision to invest in a fundamentally strong company paid off over the long term.
- The investment provided both **capital gains** and **dividend income**.
- This is a classic example of a **long-term equity investment** with a **moderate risk** and **high return** profile.

Example of Investment – Case Study: Investing in Fixed Deposits (FD)

Investor Profile

- **Name**: Priya Mehta
- **Age**: 40
- **Profession**: School Teacher
- **Investment Objective**: Capital safety and stable income
- **Risk Appetite**: Low

Investment Decision

Priya decides to invest ₹2,00,000 in a **5-year Fixed Deposit (FD)** at her bank in January 2020. **FD Interest Rate (2020)**: 6.5% per annum (compounded quarterly),**Tenure**: 5 years, **Compounding Frequency**: Quarterly, **Interest Type**: Cumulative (interest paid at maturity)

Maturity Calculation

We use the compound interest formula and we get ₹2,75,275

Returns Summary

Component	Amount (₹)
Initial Investment	2,00,000
Interest Earned	75,275
Maturity Amount (2025)	**2,75,275**

Analysis

- Priya earned **₹75,275** safely over 5 years without any market risk.
- FDs are **ideal for conservative investors** who prioritize capital safety.
- Though the return is lower compared to equity investments, the **risk is minimal**.
- The interest earned is **taxable**, which slightly reduces the net return.

Speculation

- **Definition**: Speculation involves taking **calculated risks** to achieve **quick gains** from short-term fluctuations in market prices.
- **Objective**: **Higher return** with **higher risk**, usually over the **short term**.
- **Examples**: Trading in volatile stocks, options, or commodities.

Example of Speculation – Case Study: Intraday Trading in Stock Market

Speculator Profile

- **Name**: Arjun Patel
- **Age**: 28
- **Profession**: Freelance Graphic Designer
- **Experience**: 1 year in stock market
- **Risk Appetite**: High
- **Objective**: Short-term profit using price fluctuations

Speculative Action

Arjun speculates that **Tata Motors** stock, currently priced at ₹680, will rise today due to positive auto sales data.

- **Date**: March 15, 2024
- **Strategy**: Intraday buying and selling (buy in the morning, sell before market closes)
- **Capital Used**: ₹50,000
- **Broker provides 5x margin**, so Arjun can trade for ₹2,50,000
- **Buys**: 368 shares at ₹680 per share (₹2,50,000 / ₹680)

Outcome

- By 2 PM, the stock price rises to ₹690
- Arjun sells all 368 shares at ₹690

Profit Calculation

Item	**Value (₹)**
Buy Price	₹680 × 368 = ₹2,50,240
Sell Price	₹690 × 368 = ₹2,53,920
Gross Profit	₹3,680
Less: Brokerage & Taxes	₹500 (approx.)
Net Profit	₹3,180
Return on Own Capital	₹3,180 / ₹50,000 = **6.36% in 1 day**

What if the stock had dropped to ₹670 instead?

- **Loss** = ₹10 × 368 = ₹3,680
- Net loss after charges: ~₹4,000
- **Entire capital at risk** due to leverage (margin trading)

Analysis

- Arjun's action is **speculation**, not investment.
- Decision based on **short-term news**, not long-term fundamentals.
- Uses **margin trading** to amplify profits — and losses.
- **High reward, high risk**.

Gambling

- **Definition**: Gambling is a game of **chance** where outcomes are largely **unpredictable** and not based on analysis.
- **Objective**: Chance-based gain with **very high risk**.
- **Examples**: Lottery, casino games, betting.

  Example of Gambling – Case Study: Sports Betting

  Gambler Profile

    - **Name**: Raj Malhotra
    - **Age**: 20
    - **Profession**: College Student

- **Experience**: None in investing or trading
- **Objective**: Quick money based on luck or instinct
- **Risk Appetite**: Very High

Gambling Scenario

Raj bets ₹5,000 on an IPL cricket match using an online betting app.

Bet Type: Predicting which team will win (Mumbai Indians vs Chennai Super Kings)

Wagered Amount: ₹5,000

Odds Offered: 2:1 (If his team wins, he gets ₹10,000 total; if he loses, he gets nothing)

Outcome Scenarios

If Mumbai Indians win:

Winnings: ₹10,000 (includes initial ₹5,000)

Net Profit: ₹5,000

ROI: 100% (but purely based on outcome, not analysis)

If Chennai Super Kings win:

Loss: ₹5,000 (entire amount lost)

No refund, no collateral, no asset ownership

Analysis

- Raj's decision is based entirely on **guesswork or emotional support** for a team.
- There is **no analysis**, no asset, no real economic activity.
- This is a **high-risk, zero-sum activity** — one wins, others lose.
- **Returns are based purely on chance**, not skill, strategy, or market knowledge.

Differences between Investment, Speculation and Gambling:

Aspect	Investment	Speculation	Gambling
Definition	Commitment of funds for future return	Taking calculated risk for short-term gains	Wagering money on uncertain outcomes
Risk	Low to Moderate	High	Very High
Return	Steady, long-term	Uncertain, short-term	Unpredictable
Time Horizon	Long-term	Short-term	Instantaneous or very short
Basis	Fundamental analysis	Market trends and timing	Luck/Chance

Features of Investment:

- **Risk and Return Trade-off**: Every investment has a certain level of risk and corresponding return.
- **Safety of Principal**: Investors seek to preserve the original amount invested.
- **Liquidity**: Ease with which an investment can be converted to cash.
- **Marketability**: Availability of a market to buy or sell investments.
- **Income and Capital Appreciation**: Investments may provide regular income (dividends, interest) or increase in value.
- **Tax Benefits**: Certain investments offer tax deductions under various sections of the Income Tax Act.

Investment Avenues:

"Investment avenues" refer to the various options or vehicles available for individuals or institutions to invest their money and potentially earn returns. These avenues vary in terms of risk, return, liquidity, and time horizon.

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1. Traditional Investment Avenues

1. **Savings Account**
    - Low return, very safe, high liquidity
    - Suitable for emergency funds
2. **Fixed Deposits (FDs)** / **Recurring Deposits (RDs)**
    - Fixed interest, low risk
    - Ideal for conservative investors
3. **Public Provident Fund (PPF)**
    - Long-term, tax-free returns, government-backed
    - Lock-in period of 15 years
4. **National Savings Certificate (NSC)**
    - Safe, fixed income, tax benefits under Section 80C

2. Market-Linked Investment Avenues

1. **Stocks/Equities**
    - High risk, high return
    - Requires market knowledge and long-term horizon

2. **Mutual Funds**
    - Professionally managed, diversified
    - Types: equity, debt, hybrid, index funds
3. **Exchange Traded Funds (ETFs)**
    - Trade like stocks, low cost, tracks indices or sectors
4. **Bonds / Debentures**
    - Fixed income instruments, varying credit risk

3. Real Assets

1. **Real Estate**
    - Tangible asset, rental income + capital appreciation
    - Low liquidity, high entry cost
2. **Gold / Precious Metals**
    - Hedge against inflation, safe-haven asset
    - Can be physical or digital (e.g., Sovereign Gold Bonds)

4. Alternative Investment Avenues

1. **Cryptocurrencies**
    - High risk and volatility, decentralized
    - Requires deep understanding and risk tolerance
2. **Peer-to-Peer (P2P) Lending**
    - Higher returns with credit risk
    - Regulatory oversight in some regions
3. **REITs (Real Estate Investment Trusts)**
    - Invest in property portfolios, regular income
    - Traded on stock exchanges
4. **Venture Capital / Angel Investing**
    - Investing in startups, high return potential, very risky
    - Requires large capital and due diligence

5. Retirement & Tax-Saving Instruments

1. **Employee Provident Fund (EPF)**
    - Mandatory for salaried employees, employer contribution
    - Long-term savings for retirement

2. **National Pension System (NPS)**
    - Government-backed retirement plan, partial tax benefits
3. **Tax-Saving Mutual Funds (ELSS)**
    - Equity-oriented, lock-in of 3 years, tax deduction under 80C

Investment Process:

The **investment process** is a structured approach to planning, executing, and monitoring investments to meet financial goals. It typically involves **five key steps**:

1. **Investment Policy:**
   The investor before proceeding into investment formulates the policy for sysyematic functioning. It includes
   - Investible funds
   - Objectives
   - Knowledge

   Investible Funds: The Investment procedure depends upon the availability of funds. Funds may be savings or borrowings. If funds are borrowed, the investor has to take extra care in the selection of investment alternatives. The return should be more than the interest.

   Objectives: The objectives are based on the rate of return, the Regularity of Income, and Risk perception. The risk taker's objective is to earn a high rate of return.

   Knowledge: The Knowledge about investment alternatives and markets plays a key role in policy formulation. The investor should be aware of the stock market structure, functions, and brokers. It enables him to trade intelligently.

   An **Investment Policy Statement** or **IPS** is a **strategic roadmap** that outlines how an individual or organization plans to invest their money to achieve specific financial goals. It serves as a written guide to ensure consistency, discipline, and alignment with the investor’s objectives and risk tolerance.

Investment Policy Statement Example – For a Student Investor

Investor Profile

- **Name:** Riya Sharma
- **Age:** 22
- **Occupation:** Student (Final Year)
- **Investment Start Date:** August 1, 2025
- **Time Horizon:** 10+ years
- **Monthly Investment:** ₹2,000 (from part-time job and savings)

Investment Objectives

- **Goal 1:** Build long-term wealth

- **Goal 2:** Save for future business/startup or higher education
- **Goal 3:** Learn investing with low initial risk

Risk Tolerance

- Moderate: Riya is willing to take some risk for higher returns, but prefers diversified investments to avoid big losses.

Asset Allocation Strategy

Asset Class	Target Allocation	Reason
Equity Mutual Funds	60%	High growth potential
Debt Mutual Funds	30%	Stability and lower volatility
Cash / Savings	10%	For emergencies or quick access

Investment Selection

- **Equity Mutual Funds:**
  - Nifty 50 Index Fund
  - Small-cap Mutual Fund for growth
- **Debt Mutual Funds:**
  - Short-term bond fund
- **Platform Used:** Zerodha or Groww (mutual fund apps)

Rebalancing & Review

- Review investments every 6 months
- Rebalance if one asset class grows beyond 10% of its target

Liquidity Needs

- Keep ₹5,000 in a bank account as an emergency fund
- Avoid locking money for more than 3 years

Performance Benchmark

- Equity: Compare returns to Nifty 50 (India's stock index)
- Debt: Compare to CRISIL Short-Term Bond Index

Monitoring Plan

- Use mutual fund app to track monthly
- Read financial news or blogs weekly

- Annual review with a senior or mentor

Summary

Riya will invest ₹2,000 monthly:

- ₹1,200 in equity funds
- ₹600 in debt funds
- ₹200 kept as cash buffer

She is investing for long-term growth while learning how the market works, with a focus on consistency, low cost, and manageable risk.

Security Analysis:

After formulation of investment policy, the securities have to be bought. Security analysis can be done through

- Market Analysis
- Industry Analysis
- Company Analysis

Market Analysis: The Stock market reflects the economic position of a country. Gross Domestic Product and Inflation affect the stock prices. The recession results bear market. In the short run, stock price fluctuates, and in the long run, they move either upward or downward.

Industry Analysis: Industries contribute more output to the major segment of the economy, vary in their growth rates, and overall contribution to economic activity. Some industries grow faster than GDP and are expected to continue.

Company Analysis: The purpose of company analysis is to help investors make better decisions. They should give information about profitability, the company's earnings, efficiency, capital structure and management have to be screened.

Valuation:

The Valuation helps the investors to determine the risk and return expected from an investment in common stock. **Valuation** is a critical step in the investment process. It helps investors determine the **fair value** of an asset (like a stock, bond, or property) and decide whether it is **overvalued**, **undervalued**, or **fairly priced**. The goal is to **buy undervalued assets** (cheap compared to their real worth) and **sell or avoid overvalued ones**.

Common Valuation Methods

Method	**Description**
1. Discounted Cash Flow (DCF)	Estimates the present value of future cash flows (e.g., dividends or earnings). Most fundamental method.
2. Price-to-Earnings (P/E) Ratio	Compares stock price to earnings. Helps compare companies in the same industry.

Method	Description
3. Price-to-Book (P/B) Ratio	Compares stock price to book value (assets – liabilities). Useful for asset-heavy companies.
4. Dividend Discount Model (DDM)	Values a stock based on the present value of expected dividends. Best for dividend-paying firms.

For Bonds:

- **Present Value of Future Cash Flows:** Use the bond's coupon payments and face value discounted at the market interest rate.
- **Yield to Maturity (YTM):** The rate of return if the bond is held until maturity.

Construction of Portfolio:

A portfolio is a combination of Securities. It is constructed in such a manner to meet the investors' goals and objectives. Investors try to attain maximum returns with minimum risk. Towards this end, he diversifies his portfolio and allocates funds among the securities.

Diversification: The main objective of diversification is the reduction of risk in the loss of capital and income. A diversified portfolio is comparatively less risky than a single portfolio.

Debt and equity diversification: Debt instruments provide an assured return. Both debt and equity instruments are combined to complement each other.

Industry diversification: Industry growth and government policies differ from each other. Banking industry provide regular returns. It Yields high return. Thus, industry diversification is needed and it reduces risk.

Company diversification: Securities from different companies are purchased to reduce risk. Technicl analyst suggest the investor to buy securities based on the price movements. Fundamental analysist suggest financially sound and investore friendly companies.

Selection: Funds are allocated for the selected securities. Selection of Securities and allocation of funds and seals the construction of portfolio.

Evaluation of Portfolio:

Portfolio has to be managed efficiently. The efficient management calls for evaluation of portfolio. It consists of apparaisal and revision

Appraisal: The risk and return performance of the securities vary from time to time. The variability in returns of the securities is measured and compared. The developments in the economy industry and relevant industry or companies from which the stocks are bought have to be appraised this appraisal warns the loss and steps can be taken to avoid the losses.

Revision:

The revision depends on the results of the appraisal. The low yielding securities with highy risk are placed with high yielding securities with low risk factor. The investor has to revise the components of the portfolio periodically for a good rate of return.

Investment environment:

The **investment environment** refers to the overall economic, financial, political, and social conditions that affect investors' ability to achieve desired returns on their investments. It includes a wide range of factors that influence how attractive or risky different types of investments may be at a given time.

Key Components

1. **Economic Factors**
    - **Interest rates:** Set by central banks; higher rates often reduce investment in stocks and bonds.
    - **Inflation:** Affects purchasing power and real returns; moderate inflation is usually ideal.
    - **Economic growth (GDP):** A growing economy supports business earnings and investment returns.
    - **Unemployment levels:** Indicate economic health and consumer spending power.
2. **Financial Market Conditions**
    - **Stock market trends:** Bullish or bearish trends can impact investor sentiment and risk appetite.
    - **Bond yields and credit spreads:** Reflect credit risk and interest rate expectations.
    - **Liquidity:** Availability of buyers/sellers and ease of entering/exiting positions.
3. **Political and Regulatory Climate**
    - **Stability and governance:** Political unrest or uncertainty can deter investment.
    - **Tax policy:** Changes in capital gains taxes or corporate taxes affect returns.
    - **Regulations:** Especially in sectors like finance, energy, or tech.
4. **Global Influences**
    - **Geopolitical tensions:** Wars, sanctions, or trade conflicts affect markets.
    - **Currency fluctuations:** Important for international investors.
    - **Global economic conditions:** Interdependence of markets (e.g., U.S. slowdown affecting emerging markets).
5. **Technological and Social Trends**
    - **Innovation and disruption:** Impact sectors differently (e.g., AI, green energy).
    - **Demographic shifts:** Aging populations, urbanization, etc., can shape investment opportunities.
6. **Investor Sentiment and Behaviour**
    - **Risk tolerance:** Varies depending on economic conditions and market volatility.

- **Herd behaviour:** Can create bubbles or crashes.

Need for study:

Understanding the investment environment helps:

- **Identify opportunities and risks.**
- **Allocate assets effectively.**
- **Time investments more strategically.**
- **Adjust portfolios to current and anticipated conditions.**

Structure of Securities Markets in India:

India's securities markets are a vital part of its financial system, facilitating the mobilization of capital and investment. Here's an overview of the **Securities Markets of India**, including its structure, regulatory framework, and major components:

1. **Structure of Securities Markets in India**

India's securities markets are broadly divided into two segments:

A. **Primary Market (New Issue Market)**
Where companies issue new securities to raise money from investors.

- **Public Issue: Securities are offered to the public (e.g., IPOs).**
- **Private Placement: Offered to select investors.**
- **IPO (Initial Public Offering): First-time issue of shares.**
- **FPO (Follow-on Public Offering): Additional issue of shares.**
- **Rights Issue: Existing shareholders get the right to buy more shares.**
- **Preferential Allotment: Shares issued to selected investors (e.g., mutual funds).**

B. Secondary Market

- Previously issued securities are traded among investors.
- Facilitates liquidity and price discovery.
- **Major Stock Exchanges**:
  - **BSE (Bombay Stock Exchange)** – Oldest in Asia.
  - **NSE (National Stock Exchange)** – Largest by volume in India.
  - **Others**: Calcutta Stock Exchange, Metropolitan Stock Exchange of India (MSEI).

2. **Key Regulators and Institutions**

SEBI (Securities and Exchange Board of India)

- Apex regulatory authority established in 1992.
- Powers:
  - Regulates stock exchanges and intermediaries.

- Protects investor interests.
- Promotes fair and transparent markets.
- Registers and oversees mutual funds, brokers, FIIs, etc.

RBI (Reserve Bank of India)

- Regulates the government securities market and money market.
- Manages forex reserves and currency markets.

Ministry of Finance

- Policy-making body for capital markets.
- Oversees SEBI and exchanges indirectly.

3. Types of Securities Traded

- **Equity Shares** (ownership in a company)
- **Preference Shares**
- **Debentures and Bonds** (debt instruments)
- **Government Securities (G-Secs)**
- **Mutual Fund Units**
- **Derivatives** (Futures and Options on stocks, indices, etc.)
- **Exchange-Traded Funds (ETFs)**

4. Market Participants

- **Retail Investors: Individual investors who buy and sell securities (shares, bonds, mutual funds, etc.) for their personal account, not on behalf of any institution.**
- **Institutional Investors** (Mutual Funds, Insurance Companies, Pension Funds): These are large organizations that invest on behalf of others (such as policyholders or pensioners).
    - **Mutual Funds:** Pool money from retail and institutional investors to invest in various financial instruments.
    - Managed by **Asset Management Companies (AMCs)**.
    - Examples:
        - **SBI Mutual Fund**
        - **HDFC Mutual Fund**
        - **ICICI Prudential Mutual Fund**

    - **Insurance Companies:** Collect premiums and invest a portion in capital markets for returns and financial stability.

- Examples:
    - **Life Insurance Corporation of India (LIC)**
    - **HDFC Life Insurance**
    - **ICICI Lombard**
- **Pension Funds:** Manage retirement savings and invest in stocks, bonds, and other instruments to grow the corpus.
- Examples:
    - **Employees' Provident Fund Organisation (EPFO)**
    - **National Pension Scheme (NPS) – managed by PFRDA**

- **Foreign Institutional Investors (FIIs) / Foreign Portfolio Investors (FPIs):** Foreign entities (like hedge funds, investment banks, pension funds) that invest in India's capital markets.
    - Examples:
        - **BlackRock**
        - **Goldman Sachs**
        - **Vanguard Group**
- **Stock Brokers and Sub-brokers:**Intermediaries who help investors buy and sell securities through stock exchanges. They are licensed and regulated by SEBI.
    - Examples:
        - **Zerodha**
        - **Angel One**
        - **ICICI Direct**
        - **Groww**
        - **Motilal Oswal**
- **Merchant Bankers:** Financial intermediaries who manage **issue of securities** (IPOs, FPOs), mergers & acquisitions, corporate restructuring, and capital raising.
    - Examples:
        - **JM Financial**
        - **ICICI Securities**
        - **Kotak Mahindra Capital**
        - **Axis Capital**
- **Credit Rating Agencies:** Evaluate the **creditworthiness** of companies and their financial instruments (like bonds, debentures). Help investors assess the risk of default.
    - Examples:
        - **CRISIL (Credit Rating Information Services of India Ltd.)**
        - **ICRA**
        - **CARE RatingsClearing Corporations**

5. Key Market Infrastructure Institutions

- **Stock Exchanges** – BSE, NSE

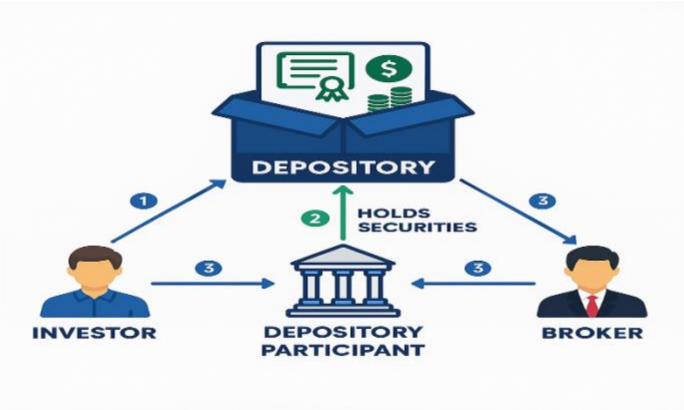
    - **BSE (Bombay Stock Exchange)**
        - **Founded**: 1875 (Oldest in Asia)
        - **Location**: Mumbai
        - **Major Index**: SENSEX
        - **Status**: Active and Recognized
    - **NSE (National Stock Exchange)**
        - **Founded**: 1992
        - **Location**: Mumbai

        - **Major Index**: NIFTY 50
        - **Status**: Active and Recognized
    - **MSEI (Metropolitan Stock Exchange of India Ltd.)**
        - **Founded**: 2008
        - **Location**: Mumbai
        - **Status**: Recognized by SEBI, but very low trading volumes
- **Clearing Corporations:** Ensure smooth **clearing and settlement** of trades executed on stock exchanges. They guarantee that buyers get securities and sellers get paid.Examples:
    - **NSCCL** (National Securities Clearing Corporation Ltd.) – linked with NSE.
    - **ICCL** (Indian Clearing Corporation Ltd.) – linked with BSE.
    - **MCXCCL** (MCX Clearing Corporation Ltd.) – for commodity market.
- **Depositories :** A **Depository** in the securities market is like a **bank for securities** (such as shares, debentures, bonds, mutual fund units). It **holds securities in electronic (demat) form**, facilitates transfer of ownership, and helps in safe and quick transactions.
    - **NSDL (National Securities Depository Limited)**
        - **Established**: 1996
        - **Promoted by**: NSE
        - **Headquarters**: Mumbai
    - **CDSL (Central Depository Services Limited)**
        - **Established**: 1999
        - **Promoted by**: BSE
        - **Headquarters**: Mumbai

Functions of Depositories

Function	**Explanation**
Dematerialization	Converting physical share certificates into electronic form
Rematerialization	Converting electronic shares back into physical certificates (rare now)
Transfer of Securities	Enables easy transfer of shares between buyer and seller (through a broker)
Updating Ownership	Records ownership when shares are bought/sold
Corporate Benefits	Passes dividends, bonuses, rights, etc. to shareholders
Safe Custody	Stores investor securities securely in digital form

- **Depository Participants:**DPs act as **intermediaries** between the investor and the depository.
    - Examples: **Zerodha**, **Groww**, **ICICI Direct**, **HDFC Securities**, etc.



Depository System diagram shown above:

1. **Investor** – A person who wants to buy/sell shares.
2. **Depository Participant (DP)** – Acts as a middleman between the investor and the depository.
3. **Depository** – A central organization (like NSDL or CDSL) that holds the investor's securities in **electronic (demat) form**.
4. **Broker** – A registered agent who executes buy/sell orders on behalf of the investor on the stock exchange.

Step 1: Investor Gives Instructions

- The **investor** opens a **Demat Account** with a **Depository Participant (DP)**.
- When the investor wants to buy or sell securities, they place an order through a **broker**.

Step 2: Depository Holds Securities

- Once the order is executed:
    - If **buying**, the **depository (NSDL/CDSL)** credits the purchased securities to the **investor's demat account**.
    - If **selling**, it debits the securities from the demat account and transfers them to the buyer.
- The actual holding and transfer of securities happen electronically within the **depository system**.

3: Flow of Information and Confirmation

- The **DP**, **broker**, and **depository** communicate with each other to:
    - Confirm the trade
    - Ensure settlement
    - Update the investor's holdings

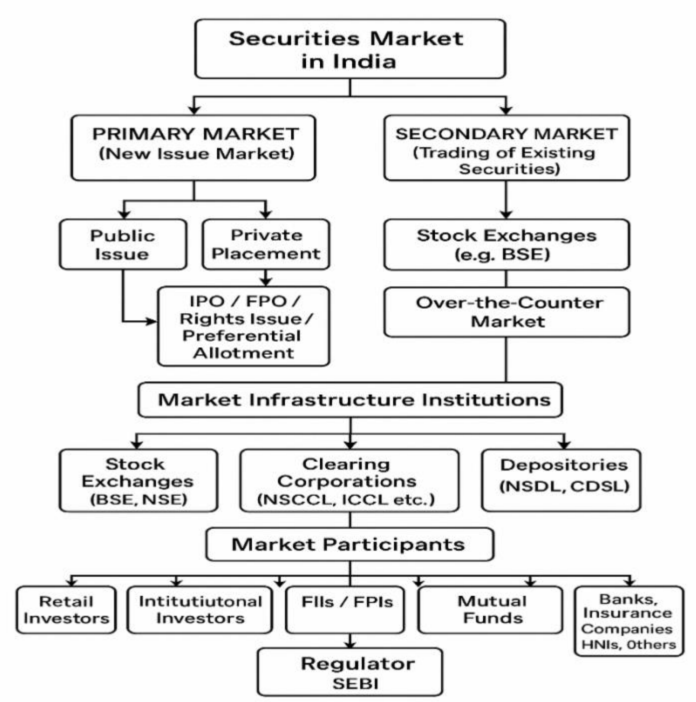
6. Trading Mechanism

- **Fully electronic and screen-based trading (T+1 settlement cycle).**

- **Online platforms allow investors to trade via demat accounts.**

7. Reforms and Developments

- Dematerialization of securities (demat accounts).
- Implementation of T+1 settlement.
- Introduction of REITs and INVITs.
- Algorithmic trading and rise of fintech.
- Tightened rules for insider trading and corporate governance.



Securities Trading and Settlement:

Securities Trading and Settlement involves the processes of buying and selling financial instruments like stocks, bonds, and derivatives, and then transferring the ownership and payment between the involved parties. Here's a breakdown of the two core concepts:

Securities Trading: Securities trading is the act of buying and selling financial instruments through exchanges (like the NYSE, Nasdaq) or over-the-counter (OTC) markets.

Types of Securities Traded:

- **Equities:** Common and preferred stocks
- **Debt Instruments:** Bonds, debentures
- **Derivatives:** Options, futures
- **Mutual Funds, ETFs, etc.**

Key Market Participants:

- **Investors/Traders**
- **Brokers/Dealers**
- **Exchanges**
- **Market Makers**

Trade Lifecycle:

1. **Order Initiation and Execution:** Investor places order; broker executes.
2. **Trade Capture:** Trade details recorded.
3. **Trade Confirmation/Matching:** Both sides agree on trade terms.

Settlement: Settlement is the process of transferring securities from the seller to the buyer and funds from the buyer to the seller. It finalizes the trade.

T+2 Settlement Cycle:

In most markets, settlement occurs two business days after the trade date (T+2).

Key Steps in Settlement:

1. **Clearing:** Matching trade details and calculating obligations.
2. **Netting:** Offsetting buy and sell positions to reduce volume.
3. **Settlement:** Transfer of securities and funds.

Entities Involved:

- **Clearing House:** Intermediary that guarantees trade performance.
- **Central Counterparty (CCP):** Takes on counterparty risk.
- **Depositories (like NSDL, CDSL):** Hold securities in dematerialized form.

Risks in Trading and Settlement:

- **Counterparty Risk:** One party defaults before settlement.
- **Settlement Risk:** Issues in delivering securities or payments.
- **Operational Risk:** Errors, system failures, etc.

Modern Trends:

- **Blockchain/Distributed Ledger Tech (DLT):** Increasingly used to streamline clearing/settlement.
- **Real-time Gross Settlement (RTGS):** Immediate settlement without netting.
- **Shortened Settlement Cycles (T+1, T+0):** To reduce risk and free up capital.

Types of orders:

In securities trading, **types of orders** define how you want to buy or sell a security. Here are the most common types:

1. Market Order

- **Definition:** Buy or sell immediately at the best available price.
- **Use case:** When execution speed is more important than price.
- **Pros:** Guaranteed execution
- **Cons:** No control over execution price

2. Limit Order

- **Definition:** Buy or sell at a specific price or better.
- **Buy Limit:** Executes at the limit price **or lower**
- **Sell Limit:** Executes at the limit price **or higher**
- **Pros:** Price control
- **Cons:** Execution not guaranteed

3. Stop Order (Stop-Loss)

- **Definition:** Becomes a market order once a trigger price (stop price) is hit.
- **Use case:** Limit losses or protect profits.
- **Pros:** Helps manage risk
- **Cons:** May execute at a worse price than expected

4. Stop-Limit Order

- **Definition:** Becomes a **limit order** when the stop price is reached.
- **Pros:** Combines stop-loss with price control
- **Cons:** No guarantee of execution

5. Trailing Stop Order

- **Definition:** Stop price trails the market price by a fixed percentage or amount.
- **Pros:** Locks in gains while allowing upward movement
- **Cons:** Can trigger prematurely in volatile markets

6. Good Till Cancelled (GTC)

- **Definition:** Order stays active until executed or manually canceled (often up to 90 days).
- **Pros:** Useful for long-term positions
- **Cons:** May be forgotten or left unmonitored

7. Day Order

- **Definition:** Expires at the end of the trading day if not executed.
- **Pros:** Avoids lingering orders
- **Cons:** Requires re-entry each day if not filled

8. Fill or Kill (FOK)

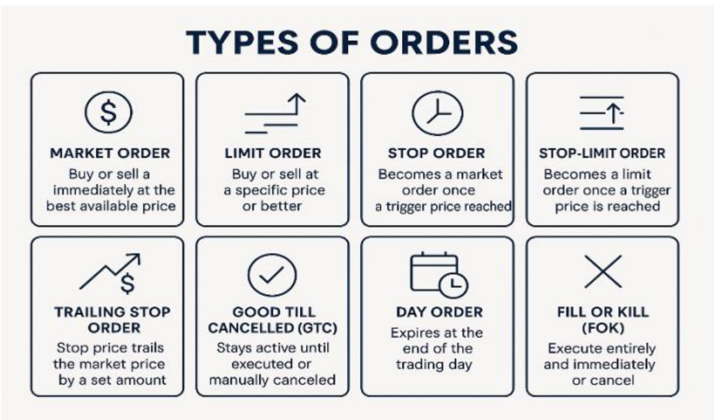
- **Definition:** Execute **entire order immediately** or cancel it entirely.
- **Pros:** All-or-nothing execution
- **Cons:** Risk of no fill at all

9. Immediate or Cancel (IOC)

- **Definition:** Execute any available portion immediately, cancel the rest.
- **Pros:** Partial execution allowed
- **Cons:** May result in partial fills

10. All or None (AON)

- **Definition:** Only execute if the **entire quantity** can be filled.
- **Pros:** Avoids partial fills
- **Cons:** May take longer to execute



Margin Trading:

Margin trading is when you borrow money from a broker to buy more assets (stocks, crypto, etc.) than you could with just your own funds.

Here's the idea in simple terms:

1. **Your own funds (margin)** – You deposit a certain amount of money as collateral.
2. **Borrowed funds** – The broker lends you extra capital based on that collateral.
3. **Leverage** – The ratio of total position size to your own money (e.g., 2× leverage means your total trade size is twice your own funds).
4. **Interest & fees** – You pay interest on the borrowed amount for as long as you hold the position.
5. **Margin call** – If the trade moves against you and your equity falls below the required maintenance margin, the broker can demand more funds or liquidate your position to limit losses.

Why brokers give margin trading

1. **Interest income** – They charge you interest on the money you borrow.
2. **Higher trading volumes** – With leverage, traders open larger positions, which increases the broker's commission or spread earnings.
3. **Customer attraction** – Margin trading can make the platform more appealing to active traders, especially those wanting to maximize returns.
4. **Loan security** – The broker controls the collateral (your margin), so they can liquidate positions if needed to protect themselves from loss.

Who gets margin trading

Brokers usually allow margin trading only for clients who meet certain requirements:

- **Approved brokerage account** – Often requires a separate margin agreement.
- **Minimum deposit** – Many brokers require a starting balance
- **Risk disclosure acknowledgment** – Clients must confirm they understand the risks.
- **Experience check** – Some brokers restrict margin to traders with a certain history or risk profile.

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Unit- III

UNIT-III: Investment Alternatives-I: Investment Avenues: Financial Assets, Capital market instruments- Stocks, Bonds, Commodities and Derivatives, Post office Deposits, Bank Deposits. Money Market Instruments: Need and Importance, Types-Commercial Papers, Treasury bills, Certificate of Deposits, Bills of Exchange, Mortgage loans. Other Investment Avenues: Gold, Real estate, PPF, NPS and SIP. Investment Avenues

Investment Alternatives- I

Investment avenues refer to different channels where investors can put their surplus funds to earn returns. They can be broadly classified into:

A. Financial Assets
B. Money Market Instruments
C. Other Investment Avenues

1. Stocks (Equity Shares): A stock (or share) represents ownership in a company. Shareholders are part-owners and can participate in profits.

- o **Equity Shares (common stock):** Voting rights, dividends (not fixed), and high growth potential.
- o **Preference Shares:** Priority over equity shareholders for dividends and repayment during liquidation; fixed dividend but usually no voting rights.

- **Returns:**
  - o **Dividends:** Part of profit distributed to shareholders.
  - o **Capital Gains:** Increase in share price over time.
- **Risk Level:** High (due to market fluctuations).
- **Liquidity:** Very liquid (traded on stock exchanges like NSE, BSE).

2. Bonds (Debentures: A bond is a fixed-income instrument representing a loan made by an investor to a borrower (corporate or government).

- o **Corporate Bonds:** Issued by companies for raising capital.
- o **Government Bonds (G-Secs):** Issued by central/state governments; considered very safe.
- o **Convertible Debentures:** Can be converted into equity shares after a period.
- o **Non-convertible Debentures (NCDs):** Remain debt instruments till maturity.

- **Returns:** Fixed interest (coupon rate) paid periodically + repayment of principal on maturity.
- **Risk Level:** Lower than stocks but depends on issuer’s creditworthiness.
- **Liquidity:** Tradable in bond markets, but liquidity varies.

3. Commodities: Investment in physical goods like gold, silver, crude oil, natural gas, agricultural products, etc., through commodity exchanges (like MCX, NCDEX in India).

- Physical holding (e.g., gold jewelry, silver coins).
- Commodity futures (contracts to buy/sell at future price).
- ETFs and mutual funds linked to commodities.

- **Returns:** Based on price fluctuations in global & domestic markets.
- **Risk Level:** Moderate to High (affected by geopolitical events, inflation, supply-demand).
- **Liquidity:** High in exchanges, low in physical form.

4. Derivatives: Financial contracts whose value is derived from an underlying asset (stocks, commodities, currencies, indices).

- **Futures:** Contract to buy/sell asset at a future date at a predetermined price.
- **Options:** Right (but not obligation) to buy/sell asset at a fixed price within a period.
- **Swaps:** Agreement to exchange cash flows (like interest rate swaps, currency swaps).
- **Forwards:** Customized contracts between two parties to buy/sell at future date (not traded on exchange).

- **Purpose:**
  - **Hedging:** Protect against price fluctuations.
  - **Speculation:** Profit from market movements.
- **Returns:** Can be very high (but also lead to huge losses).
- **Risk Level:** Very High (leveraged & volatile).
- **Liquidity:** High in exchanges, low in OTC contracts.

5. Post Office Deposits: Government-backed small saving schemes through post offices, designed for safe investments.

- Post Office Savings Account
- Recurring Deposit (RD)
- Time Deposit (TD)
- Monthly Income Scheme (MIS)
- National Savings Certificate (NSC)
- Kisan Vikas Patra (KVP)

- **Returns:** Fixed interest rates, revised quarterly by Government of India.
- **Risk Level:** Very Low (sovereign guarantee).
- **Liquidity:** Limited (lock-in periods, penalties on premature withdrawal).

6. Bank Deposits: Deposits with banks, offering fixed returns with safety.

- **Savings Account:** Low interest, high liquidity.

- **Fixed Deposit (FD):** Higher interest, fixed term.
- **Recurring Deposit (RD):** Monthly investment, fixed returns.

- **Returns:** Predetermined interest rate.
- **Risk Level:** Low (insured up to ₹5 lakh in India by DICGC).
- **Liquidity:** High in savings accounts, but FDs and RDs have penalties for early withdrawal.

Comparison of Capital Market Instruments

Instrument	Risk Level	Return Potential	Liquidity	Investment Horizon	Tax Benefits
Stocks (Equity)	High (market volatility)	High (dividends + capital gains)	Very High (traded daily on NSE/BSE)	Short to Long term	LTCG & STCG taxation; No Sec 80C benefit
Bonds (Debentures)	Moderate (depends on issuer)	Moderate (fixed interest, lower than stocks)	Moderate (tradable but less liquid than stocks)	Medium to Long term (1–10+ years)	Interest taxable; Some Govt bonds eligible for tax exemption
Commodities (Gold, Oil, Agri etc.)	Moderate to High (global price fluctuations)	Moderate to High (inflation hedge, volatile)	High on exchanges, Low in physical form	Short to Medium term	No direct 80C benefits; Gold ETFs taxed like mutual funds
Derivatives (Futures, Options)	Very High (leverage & speculation risk)	Very High (potential high gains/losses)	Very High (exchange-traded, highly liquid)	Very Short term (days to months)	Taxed as business income/short-term capital gains
Post Office Deposits (NSC, KVP, MIS etc.)	Very Low (Govt. backed)	Low to Moderate (fixed interest)	Low to Moderate (premature withdrawal restrictions)	Medium to Long term (5–15 years)	Many schemes qualify for 80C (e.g., NSC, PPF)
Bank Deposits (FD, RD, Savings)	Very Low (insured up to ₹5 lakh by DICGC)	Low to Moderate (fixed interest rates)	High for Savings, Low for FDs/RDs	Short to Medium term	No major benefits; 80C only for 5-year Tax Saver FD

B. Money Market Instruments (Details)

1. Commercial Paper (CP): An unsecured, short-term promissory note issued by **corporates, financial institutions, or primary dealers** to raise working capital.

- **Maturity:** 7 days to 1 year (commonly 90–180 days).

- **Issuer:** Large companies with good credit ratings.
- **Investor:** Banks, mutual funds, corporations, individuals.
- **Return:** Issued at a discount, redeemed at face value (the difference is the return).
- **Risk:** Moderate (depends on issuer's credit rating).
- **Liquidity:** High (traded in secondary market).

2. Treasury Bills (T-Bills): Short-term debt instruments issued by the **Government of India** to meet short-term funding needs.

- **Maturity:** 91 days, 182 days, and 364 days.
- **Issuer:** Reserve Bank of India (on behalf of the Government).
- **Investor:** Banks, financial institutions, corporations, individuals.
- **Return:** Issued at discount, redeemed at par (zero-coupon).
- **Risk:** Risk-free (sovereign guarantee).
- **Liquidity:** Very high, actively traded.

3. Certificate of Deposits (CDs): Negotiable term deposits issued by **scheduled commercial banks** and **financial institutions**.

- **Maturity:** 7 days to 1 year (for banks), up to 3 years (for financial institutions).
- **Investor:** Corporates, individuals, mutual funds.
- **Return:** Fixed interest rate, higher than savings accounts.
- **Risk:** Low (backed by banks/financial institutions).
- **Liquidity:** Tradable in secondary market (but less liquid than T-Bills).

4. Bills of Exchange (Trade Bills): A written order binding one party (the debtor) to pay a fixed sum to another party (the creditor) either on demand or at a future date.

- **Usage:** Commonly used in **trade and commerce** to finance receivables/payables.
- **Maturity:** Usually 90 days.
- **Investor:** Banks (by discounting bills), traders.
- **Return:** The holder earns discounting charges (interest).
- **Risk:** Depends on the creditworthiness of the drawer.
- **Liquidity:** Moderate (can be discounted with banks/NBFCs).

5. Mortgage Loans (as Investment Avenue): A loan secured by **real estate property** (residential or commercial).

- **Issuer:** Banks, housing finance companies, NBFCs.
- **Investor:** Lenders consider this as an investment since they earn interest.

- **Maturity:** Long-term (5–30 years).
- **Return:** Interest on loan repayments.
- **Risk:** Low to moderate (secured by property, but default risk exists).
- **Liquidity:** Low (funds are locked till repayment or property foreclosure).

Quick Comparison Table: Money Market Instruments

Instrument	Issuer	Maturity	Risk Level	Return Type	Liquidity
Commercial Paper	Corporates/Financial Institutions	7 days – 1 year	Moderate	Discount-based	High
Treasury Bills	Government of India	91–364 days	Very Low (Risk-free)	Discount-based	Very High
Certificates of Deposit	Banks/Financial Institutions	7 days – 3 years	Low	Fixed interest	Moderate
Bills of Exchange	Traders/Businesses	~90 days	Moderate	Discount charges	Moderate
Mortgage Loans	Banks/NBFCs	5–30 years	Low to Moderate	Interest on loans	Low

C. Other Investment Avenues

1. Gold: A traditional and safe-haven investment option, used as a hedge against inflation and currency fluctuations.

- **Forms of Investment:**
    - Physical (jewelry, coins, bars)
    - Gold Exchange Traded Funds (ETFs)
    - Sovereign Gold Bonds (SGBs) issued by Government of India
- **Return:** Depends on gold price movement; SGBs also provide ~2.5% annual interest.
- **Risk:** Moderate (prices fluctuate globally).
- **Liquidity:** High in physical and ETF form.

2. Real Estate: Investment in residential, commercial, or agricultural property for rental income and capital appreciation.

- **Returns:**
    - Rental income (regular cash flow).
    - Value appreciation over time.

- **Risk:** Moderate to High (depends on market demand, location, and economic conditions).
- **Liquidity:** Low (takes time to sell property).
- **Other Point:** REITs (Real Estate Investment Trusts) provide indirect, liquid real estate investment.

3. Public Provident Fund (PPF): A **government-backed, long-term saving scheme** designed to encourage small savings with tax benefits.

- **Maturity:** 15 years (extendable by 5 years).
- **Returns:** Fixed interest rate (revised quarterly, ~7–8% per annum).
- **Risk:** Very Low (sovereign guarantee).
- **Liquidity:** Partial withdrawal allowed after 6 years.
- **Tax Benefits:**
    - Investment eligible under Sec 80C (up to ₹1.5 lakh).
    - Interest & maturity amount tax-free (EEE – Exempt-Exempt-Exempt).

4. National Pension System (NPS): A **retirement-focused investment scheme** regulated by PFRDA.

- **Structure:**
    - **Tier I Account (Mandatory):** Long-term retirement savings.
    - **Tier II Account (Optional):** Voluntary savings, more flexible.
- **Returns:** Market-linked (invested in equity, corporate bonds, and government securities).
- **Risk:** Low to Moderate (diversified portfolio).
- **Liquidity:** Withdrawals allowed only at retirement (60 years), with partial withdrawal under special conditions.
- **Tax Benefits:**
    - Sec 80C: Up to ₹1.5 lakh.
    - Sec 80CCD(1B): Additional ₹50,000 (exclusive for NPS).

5. Systematic Investment Plan (SIP): A disciplined way of investing in **mutual funds** through small, regular monthly installments.

- **Returns:** Market-linked, depends on the performance of the chosen mutual fund (Equity, Debt, Hybrid).
- **Risk:**
    - High (Equity SIPs).
    - Low to Moderate (Debt SIPs).
- **Liquidity:** High (can redeem mutual fund units anytime, except in ELSS which has 3-year lock-in).

- **Benefits:**
    - Rupee-cost averaging (reduces risk of market timing).
    - Power of compounding (long-term wealth creation).

Comparison Table: Other Investment Avenues

Instrument	Risk Level	Return Potential	Liquidity	Horizon	Tax Benefits
Gold	Moderate	Moderate (inflation hedge)	High (ETFs/SGBs), Medium (physical)	Short to Long term	SGB interest taxable; No Sec 80C benefit
Real Estate	Moderate–High	High (rental + appreciation)	Low	Long term	Tax deduction on home loan interest (Sec 24), principal (Sec 80C)
PPF	Very Low	Moderate (~7–8% fixed)	Low (partial after 6 years)	Long term (15 years)	Full EEE (Sec 80C + tax-free returns)
NPS	Low–Moderate	Moderate to High (market linked)	Low (tied till retirement)	Very Long term	Sec 80C + extra ₹50k under 80CCD(1B)
SIP	Depends on Fund (Low–High)	Moderate to High (market linked)	High (except ELSS lock-in)	Medium–Long term	ELSS SIP eligible under Sec 80C

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Unit-IV

Investment Alternatives II

UNIT-IV: Investment Alternatives-II: Introduction to Mutual funds: Definitions of Mutual funds, Structure of Mutual funds, advantages and disadvantages of Mutual funds, Types of Mutual funds. AMFI. Insurance: IRDA; definition and characteristics of Insurance, Types of Insurance, Life Insurance, General Insurance and Health Insurance.

1. Mutual Funds

Definition of Mutual Funds

A Mutual Fund is a financial vehicle that collects money from several investors and invests the pooled amount into different securities such as stocks, bonds, money market instruments, and other assets. The fund is managed by a professional fund manager on behalf of investors with the objective of earning returns in line with the fund's stated objectives.

The essence of a mutual fund lies in collective investment and professional management. By investing in a mutual fund, even a small investor can participate in a diversified and professionally managed portfolio.

Structure of Mutual Funds in India

The mutual fund industry in India has a three-tier structure, with regulatory oversight:

1. Sponsor – The entity that promotes and sets up the mutual fund. It must be approved by SEBI and should have a sound track record in financial services.
2. Mutual Fund Trust – The mutual fund is set up as a trust under the Indian Trusts Act, 1882. The trust is managed by a Board of Trustees who safeguard the interests of unit holders.
3. Asset Management Company (AMC) – The AMC is appointed by the trustees to manage the fund's investments. It employs professional fund managers, research teams, and analysts to make investment decisions.
4. Custodian – An independent entity that holds the securities of the mutual fund in safe custody.
5. Registrar and Transfer Agents (RTAs) – They maintain investor records, process transactions, and provide customer service.
6. Regulator – SEBI – The Securities and Exchange Board of India (SEBI) regulates the mutual fund industry. It issues guidelines, monitors compliance, and protects investor interests.
7. AMFI – The Association of Mutual Funds in India is the self-regulatory organization that promotes ethical practices and investor education in the mutual fund industry.

Advantages of Mutual Funds

1. Diversification – Mutual funds invest in a wide variety of securities, reducing the risk of loss from any one investment.
2. Professional Management – Fund managers, with expertise in financial markets, make investment decisions on behalf of investors.
3. Liquidity – Open-ended mutual funds allow investors to buy and sell units at any time, ensuring liquidity.
4. Affordability – Investors can start with small amounts (e.g., through SIP – Systematic Investment Plan).
5. Regulated Industry – Mutual funds are regulated by SEBI, ensuring transparency, disclosure, and investor protection.
6. Variety of Schemes – Different funds are available to suit different risk appetites and goals, such as growth, income, or tax-saving.

Disadvantages of Mutual Funds

1. Market Risk – Mutual funds are subject to market volatility; returns are not guaranteed.
2. Costs and Fees – Expense ratios, management fees, and exit loads can reduce investor returns.
3. Lack of Control – Investors cannot choose individual securities; decisions rest with the fund manager.
4. Taxation – Gains are subject to capital gains tax, reducing overall profitability.
5. Over-diversification – Sometimes diversification is so broad that potential high returns may get diluted.

Types of Mutual Funds

Mutual funds can be classified on different bases:

1. **Based on Structure**
    - Open-ended Funds – No fixed maturity, investors can enter or exit any time.
    - Closed-ended Funds – Have a fixed maturity period; units are listed and traded on stock exchanges.
    - Interval Funds – Allow purchase/redemption only during specific intervals.
2. **Based on Investment Objective**
    - Equity Funds – Invest in shares, suitable for long-term capital appreciation.
    - Debt Funds – Invest in bonds and fixed-income instruments, focusing on regular income.

- Hybrid Funds – Invest in a mix of equity and debt to balance risk and return.
- Money Market Funds – Invest in short-term instruments like Treasury Bills, providing high liquidity.
- Index Funds/ETFs – Replicate a stock market index such as Nifty 50.

3. **Other Classifications**
   - Sectoral/Thematic Funds – Invest in specific sectors (IT, Pharma, Banking).
   - ELSS (Equity Linked Savings Scheme) – Provide tax benefits under Section 80C.

Association of Mutual Funds in India (AMFI)

- **AMFI is a self-regulatory body of the mutual fund industry in India, formed in 1995.**
- **Objectives:**
  - Promote investor awareness and education.
  - Ensure ethical standards and professional practices among members.
  - Act as a representative body of all AMCs with SEBI, government, and RBI.
  - Regulate distributors by issuing AMFI Registration Number (ARN).

2. Insurance

Definition of Insurance

Insurance is a contract between an insurer and the insured, where the insurer promises to compensate for financial losses caused by specific risks in return for a premium paid by the insured. It is essentially a risk management tool, where the financial burden of an uncertain event (such as death, accident, or property loss) is transferred to the insurance company.

Characteristics of Insurance

1. Risk Transfer – Insurance shifts the burden of risk from the insured to the insurer.
2. Pooling of Risks – Losses of a few are shared by contributions (premiums) from many.
3. Premium – Regular payment made by the insured to the insurer.
4. Utmost Good Faith (Uberrimae Fidei) – Both parties must disclose all material facts truthfully.
5. Insurable Interest – The insured must have a financial/legal interest in the subject matter of insurance.
6. Indemnity Principle – In general insurance, compensation is paid only to cover actual loss, not to make a profit. (Life insurance is an exception.)
7. Legal Contract – It is enforceable in a court of law.

Types of Insurance

1. **Life Insurance**
    - **Provides financial protection to the family in the event of the policyholder's death.**
    - **Types:**
        - Term Life Insurance – Pure protection for a fixed period.
        - Whole Life Policy – Coverage for the entire lifetime.
        - Endowment Policy – Provides lump sum at maturity or death.
        - Unit Linked Insurance Plans (ULIPs) – Combine investment and insurance.
2. **General Insurance**
    - **Covers risks other than life.**
    - **Types:**
        - Motor Insurance – Covers vehicles against accidents, theft, or third-party liability.
        - Fire Insurance – Protects against losses from fire.
        - Marine Insurance – Covers goods in transit over water, air, or land.
        - Property Insurance – Protection against damage to property.
        - Travel Insurance – Covers risks during travel like accidents, loss of baggage, delays.
3. **Health Insurance**
    - **Covers medical expenses of hospitalization, treatment, and critical illness.**
    - **Types:**
        - Individual Health Plan – For a single person.
        - Family Floater – Single policy covering the entire family.
        - Critical Illness Insurance – Lump sum payment on diagnosis of major diseases.

Insurance Regulatory and Development Authority of India (IRDAI)

Introduction

The Insurance Regulatory and Development Authority of India (IRDAI) is the statutory, autonomous body that regulates and promotes the insurance and reinsurance industry in India. It was established under the IRDA Act, 1999, following the recommendations of the

Malhotra Committee, to liberalize and regulate the insurance sector. Headquartered at Hyderabad, IRDAI plays a vital role in ensuring transparency, fair practices, and the protection of policyholders’ interests.

Objectives of IRDAI

1. To protect the interests of policyholders.
2. To regulate, promote, and ensure the orderly growth of the insurance industry.
3. To maintain financial stability of insurers by enforcing solvency requirements.
4. To ensure fair treatment, transparency, and accountability in insurance operations.
5. To promote penetration of insurance in rural and social sectors.

Functions of IRDAI

IRDAI performs both regulatory and developmental functions:

1. **Regulatory Functions**
    - Granting licenses to insurance companies, agents, and brokers.
    - Framing regulations on insurance products, premium rates, commissions, and investments.
    - Monitoring financial soundness of insurers through solvency margins.
    - Protecting policyholders against mis-selling and unfair trade practices.
    - Ensuring compliance with consumer protection and grievance redressal mechanisms.
2. **Developmental Functions**
    - Encouraging growth of insurance in underserved areas such as rural markets.
    - Promoting innovations in insurance products (health, crop, micro-insurance).
    - Creating awareness about insurance through literacy campaigns.
    - Facilitating use of technology for faster claim settlement and transparency.

Powers of IRDAI

- Regulate entry and operations of private insurance players.
- Approve merger, acquisition, or transfer of insurance business.
- Impose penalties for violation of rules and regulations.
- Frame regulations for reinsurance and foreign participation.
- Supervise training and conduct of insurance intermediaries.

Significance of IRDAI

- Strengthened trust between insurers and policyholders.
- Enhanced insurance penetration and density in India.
- Brought consumer-centric reforms like standardized health policies (e.g., Arogya Sanjeevani).
- Encouraged innovation and competition by allowing private and foreign insurers**.**

Conclusion

IRDAI has played a pivotal role in transforming the Indian insurance industry from a state-monopoly market to a competitive, customer-centric sector. By safeguarding policyholder interests, promoting fair competition, and encouraging insurance penetration, IRDAI has contributed significantly to financial inclusion and risk protection in India's economy.

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Unit- V

UNIT-V: Introduction to Taxation: Introduction, types of taxes, direct and indirect taxes, Key terms of IT. Sources of Income: Income from salaries, Income from House Property, Income and Profession and Business, and Income from other sources. Assessment of Individual Tax-Total Income – deductions – Process of E-filing.

1. Introduction to Taxation

Taxation is the process by which a government collects revenue from individuals and organizations to finance its activities. Taxes are a compulsory contribution and not a voluntary payment. They are imposed under the authority of law.

The main purpose of taxation is to raise funds for:

- Public expenditure (infrastructure, education, defense, health, welfare).
- Redistributing wealth and reducing inequality.
- Regulating the consumption and production of certain goods/services.

Thus, taxation plays a vital role in economic development and social welfare.

2. Types of Taxes

Taxes in India are broadly classified into two categories:

(a) Direct Taxes

- Levied directly on the income, wealth, or property of a person.
- Paid directly to the government by the taxpayer.
- Cannot be shifted to others.
- Examples:
    - Income Tax
    - Corporate Tax
    - Wealth Tax (abolished now)

(b) Indirect Taxes

- Levied on the production, sale, or consumption of goods and services.
- Collected by sellers/service providers from consumers, and remitted to the government.
- Can be shifted from one person to another (ultimately borne by the end consumer).
- Examples:
    - Goods and Services Tax (GST)

- Customs Duty (on imports/exports)
- Excise Duty (on manufacture of goods)

3. Direct vs. Indirect Taxes

Basis	Direct Tax	Indirect Tax
Imposed on	Income or wealth	Goods and services
Burden	Cannot be shifted to others	Shifted to end consumer
Equity	More equitable (rich pay more)	Less equitable (same rate for all buyers)
Evasion	Higher chance of evasion	Difficult to evade
Examples	Income Tax, Corporate Tax	GST, Excise, Customs Duty

4. Key Terms of Income Tax (IT)

1. Assessee: Any person liable to pay tax under the Income Tax Act, 1961.
2. Previous Year: The financial year in which income is earned (1st April to 31st March).
3. Assessment Year: The year immediately following the previous year, in which income is assessed and taxed.
4. Gross Total Income (GTI): Aggregate of income from all sources before deductions.
5. Total Income: GTI minus permissible deductions under Chapter VI-A.
6. PAN (Permanent Account Number): A unique 10-digit alphanumeric number issued by the IT department.
7. Deduction: An amount reduced from income under specified sections (80C, 80D, 80G, etc.).
8. Exemption: Income not chargeable to tax at all (e.g., agricultural income, certain allowances).

5. Sources of Income (Five Heads of Income under IT Act)

The Income Tax Act, 1961 classifies taxable income into five heads:

(a) Income from Salaries

- Includes wages, salary, pension, gratuity, allowances, and perquisites received by an employee from the employer.
- Example: Basic pay, HRA, DA, Bonus, Leave Encashment.

(b) Income from House Property

- Income from letting out of owned buildings/lands attached to buildings.

- Even if not actually let out, deemed income may arise from a property (except one self-occupied house, which is exempt).

(c) Profits and Gains of Business or Profession

- Income earned through business (trade, commerce, industry) or profession (lawyers, doctors, CAs, consultants).
- Includes profits from sale of goods, professional fees, and services.

(d) Capital Gains

- Profits arising from transfer of a capital asset (e.g., land, building, shares, gold).
- Two types:
    - Short-Term Capital Gains (STCG)
    - Long-Term Capital Gains (LTCG)

(e) Income from Other Sources

- Residual head covering all incomes not classified under other heads.
- Examples: Dividends, lottery winnings, interest income, gifts, casual income.

6. Assessment of Individual Tax

The process of calculating tax liability of an individual is known as Assessment.

Steps in Computation

1. Compute income under each head (Salary, House Property, Business/Profession, Capital Gains, Other Sources).
2. Add together to arrive at Gross Total Income (GTI).
3. Less: Deductions under Chapter VI-A (Sections 80C to 80U).
    - 80C: Investments in LIC, PF, NSC, ELSS (limit ₹1,50,000).
    - 80D: Health insurance premium.
    - 80G: Donations to approved funds.
    - 80E: Interest on education loan.
4. Total Income = GTI – Deductions.
5. Apply Income Tax Slab Rates (varies for different age groups).
6. Add surcharge/cess if applicable.
7. Deduct rebates (Sec. 87A) for eligible taxpayers.
8. Arrive at Net Tax Payable.

7. E-Filing of Income Tax

E-Filing means filing income tax returns electronically through the official portal of the Income Tax Department: https://www.incometax.gov.in.

Steps in E-Filing

1. Register on the portal using PAN (acts as User ID).
2. Select the applicable ITR Form (ITR-1 for salaried individuals, ITR-3 for business professionals, etc.).
3. Enter personal details, income details, deductions, and tax payments.
4. Upload necessary documents, if required.
5. Validate and submit the return.
6. E-verify through Aadhaar OTP, net banking, or digital signature.

Advantages of E-Filing

- Convenient and quick.
- Reduces paperwork.
- Immediate acknowledgment.
- Faster processing of refunds.
- Ensures accuracy and transparency.

Conclusion

Taxation is the backbone of a country's revenue system. Direct and indirect taxes contribute to government resources and ensure economic stability. Understanding the different heads of income, assessment process, and the facility of e-filing helps individuals comply with tax laws effectively.

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