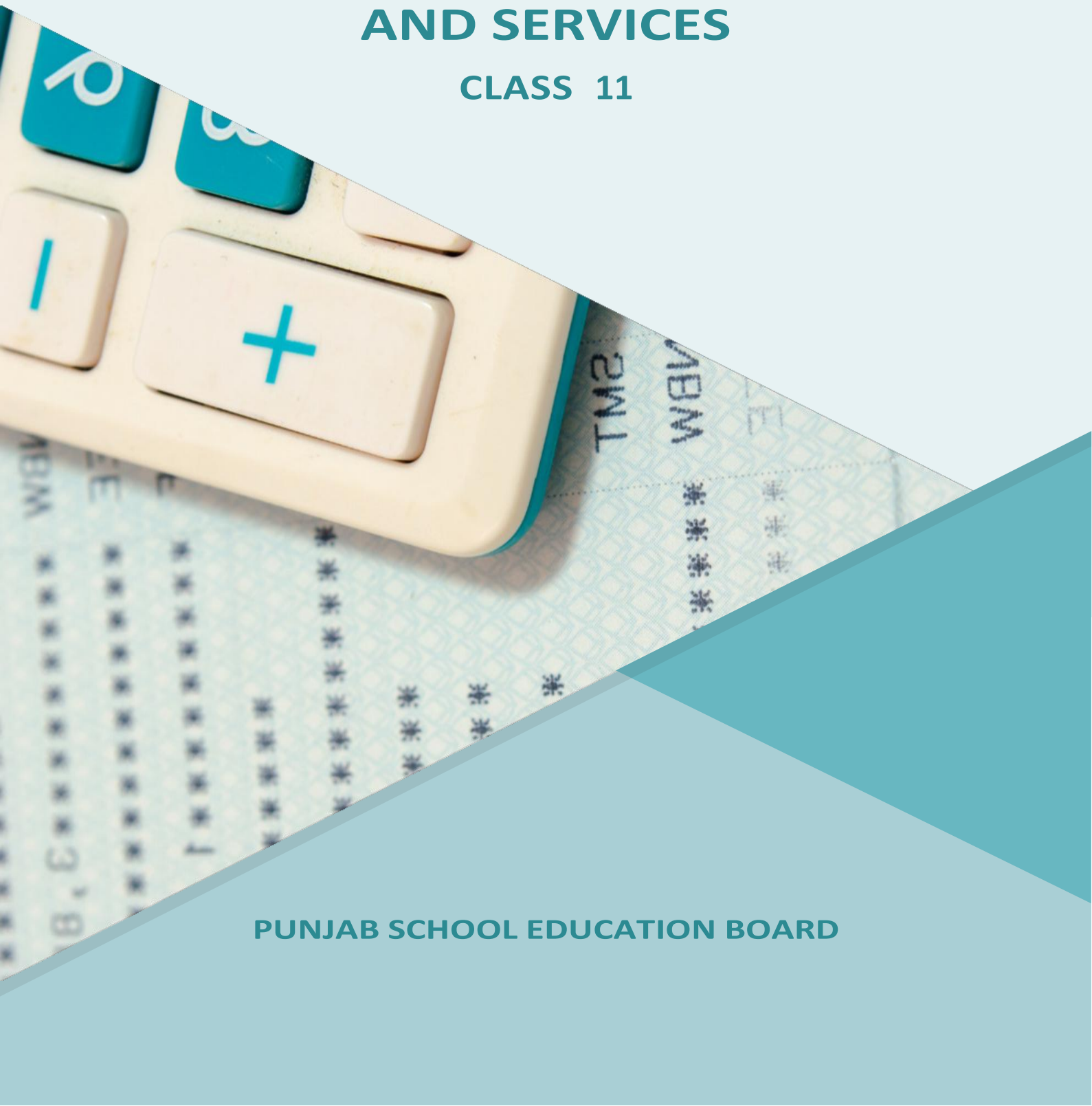


BANKING, FINANCIAL SERVICES & INSURANCE

FINANCIAL PRODUCTS AND SERVICES

CLASS 11



PUNJAB SCHOOL EDUCATION BOARD

Subject 2: Financial Products and Services

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Instructional Note

The activities included in this chapter are designed to enhance understanding. Teachers are encouraged to select and implement activities based on their time and resource availability. However, it is essential that they engage in at least a few of these activities to ensure a comprehensive learning experience for the students. Additionally, certain keywords and supplementary information are provided to offer better clarity on the concepts discussed. These are intended as additional resources for students to explore further at their own pace. Teachers may choose to emphasize these elements as needed, but they are not essential for mastering the core content of the chapter.

UNIT 01

Fundamentals of Banking System



Topics

- Concept of Banking and Functions of Bank
 - Importance of Money
 - Introduction to Banks
 - Functions of Banks
- Types of Bank accounts
 - Savings Accounts
 - Benefits of a Savings Account
 - Features of a Savings Account
 - Current Accounts
 - Benefits of a Current Account
 - Features of a Current Account
 - How to Choose Between a Savings and a Current Account
 - Fixed Deposit Accounts
 - How do Fixed Deposit Accounts Work?
 - Benefits of Fixed Deposit Accounts
 - Recurring Deposit Accounts
 - How do Recurring Deposit Accounts Work?
 - Benefits of Recurring Deposit Accounts
 - Forex Services (NRI, NRO, Remittances)
 - Currency Exchange
 - Remittance Services
 - NRE (Non-Resident External) Account
 - NRO (Non-Resident Ordinary) Account
 - Why do we have NRE & NRO Accounts?



Learning Objectives

- Understand the basic concept of banking.
- Describe the primary functions of banks.
- Demonstrate knowledge of and discuss the different types of Bank Accounts- Savings Accounts, Current Accounts, Fixed Deposits, Recurring Deposit Accounts, NRE Accounts, NRO Accounts.
- Recognize specialized bank accounts, such as, NRO (Non-Resident Ordinary) accounts, and remittance services, and understand their role in international banking.



Materials Required

- Sample Debit cards
- Sample Credit cards
- Sample/Cancelled Cheque Books or cheques
- Sample Passbooks
- Mobile with a good internet connection and banking apps
- Sample currency notes of different countries



Introducing Amar and Simran!



Activity 1: Before We Begin!

What is the purpose of money in our daily lives? Write down two reasons.

1.0 Concept of Banking and Functions of Bank:

1.1 What is Money?

Money plays an important role in our everyday lives, serving as a medium of exchange for goods and services. In the past, people relied on bartering, trading one item for another directly. However, this method had limitations, as finding someone who wanted what you had could be challenging.



Money is a widely accepted way to trade goods and services. Whether it is coins or paper, money makes buying and selling easier by giving us a common value to work with. But it's not just for transactions; it is also for saving and helping others. When we keep money in a

bank, it can grow over time. Plus, we can use money to support people who need it, showing kindness and community spirit.

Definition: Money refers to any widely accepted medium of exchange and store of value, facilitating transactions and economic activities.



Activity 2: Bank Account Overview

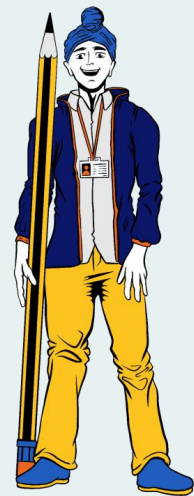
Question 1: How many of you have a bank account?

Take a moment to think about it. Raise your hand if you do.

Question 2: List down the names of the banks where you have accounts. In parallel, note down the services offered by each bank.

_____	_____
_____	_____
_____	_____
_____	_____

It seems like many of you have experience with bank accounts, which is fantastic! Now, let us learn about what banks actually do with our money.



1.2 Introduction

Think of a world without banks. No safe place to keep your money, no way to easily pay for things, and no one to give (lend) you money when you need it. Banks keep our money, and help us manage it wisely. Let us learn about banking and its important functions.

Definition

So, what exactly is a bank? A bank is a financial institution that accepts deposits from the public and gives loans. It keeps your money safe and also helps you grow it over time.






Lending

Giving someone money that they will pay back later.

1.3 Functions of Bank

Banks perform many key roles that are useful for the smooth functioning of our society.

Safekeeping of Money	Payment Services	Lending Money
<p>Banks provide a safe place for people to store their money. Instead of keeping large sums of cash at home where it could be lost or stolen, people can deposit their money in a bank account.</p> <p>Example: A student receives money on their birthday and decides to deposit it into their bank account to keep it safe.</p> 	<p>Banks offer various payment services such as giving debit and credit cards, online transactions, and giving cheque books. These services make it easy for people to buy things without using cash.</p> <p>Example: A family uses the ATM to withdraw cash. They teach their child how to use the ATM, including inserting the card, entering the PIN, selecting the amount.</p> 	<p>Banks lend money to individuals and businesses in the form of loans. This enables people to buy homes, start businesses, or pursue higher education, even if they don't have enough money saved up.</p> <p>Example: A family wants to buy a new car but doesn't have enough money saved up. They visit the bank to apply for a car loan.</p> 



Activity 3: Understanding why people take loans

Question 1: How many of you have heard of someone who has taken a loan?

Take a moment to think about it. Raise your hand if you do.

Question 2: Can anyone share why they needed a loan?

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<hr/>	<hr/>
<hr/>	<hr/>

Let's discuss different situations in which people might need to take loans.

Financial Advice by Experts

Banks have financial experts who can give advice and guidance on managing money, investing, and planning for the future. This helps people make decisions about their finances.

Example: Amar's family wants to save for his college education, so they meet with a bank's financial advisor. The advisor listens to their goals, suggests opening an education savings account, and helps them create a financial plan.



Knowledge Check

Let us recap the knowledge we have gained so far.

1. True/False: Lending money is not a function of banks.....
2. True/False: Financial experts at banks help people make informed decisions about their finances.....

Answers: 1. False 2. True



Activity 4: Bank Transactions

Objective: To understand basic bank transactions through interactive role-play.

Instructions:

- Divide students into small groups.
- Give each group a bank transaction case.
- Allow groups time to plan and act out their case.

Examples:

- Depositing Money: A student wants to save their birthday money in their bank account.
- Withdrawing Money: A student needs cash to buy a gift for a friend.
- Applying for a Loan: A family wants to borrow money to buy a new computer.

Summary of Key Takeaways:

- Understand the process and requirements for adding money to a bank account.
- Learn how to correctly and safely withdraw cash from a bank account.
- Learn the steps and important points to consider when applying for a bank loan.

2.0 Types of Bank Accounts

Now that we have an understanding of the function of Banks, let us learn the various kinds of Bank Accounts in India. Here are some of the most common types of Bank Accounts:

Savings Account	Recurring Deposit Account	NRE Account
Current Account	Senior Citizen Savings Scheme	NRO Account
Fixed Deposit Account	Public Provident Fund	Joint Account

2.1 Savings Account

A savings account helps you to deposit and store money while earning a rate of interest on the deposited amount.

Why are Savings Accounts so common and important?



Rate of Interest

The rate of interest is how much extra money you get or pay when you borrow or save. For example, if you borrow ₹100 at a 5% interest rate, you pay back ₹105 in total.

Here are some reasons:

- **Interest Earnings:** By depositing your money in a savings account, you can earn interest on your balance.
- **Safety and Security:** A savings account provides a secure place to store your money.
- **Access to Funds:** With a savings account, your money remains easily accessible whenever you need it. You can withdraw money from an ATM using your debit card easily.

Example

Simran receives ₹100 per month as pocket money from her mother. She realised she was saving ₹50 each month but was confused about where to save it for future purchases. One day, she talked to her teacher, Gurdeep, about her problem.



Simran: Ma'am, I save 50 Rupees from my pocket money every month, but I don't know where to keep it safe. I want to use it for something important later.

Gurdeep: Simran, have you heard about savings accounts?

Simran: No, ma'am. What's that?

Gurdeep: A savings account is like a special box at the bank where you can keep your money safe. Plus, the bank pays you a little extra money called interest. This way, your savings grow over time.

Simran: That sounds great! How do I open a savings account?

Gurdeep: You can visit a bank, like Punjab National Bank, with your parents. They will help you open an account and explain how to deposit and withdraw money.

Excited by the idea, Simran opened a savings account at Punjab National Bank. Now, whenever she has extra money, she deposits it in her account.

Simran: I love how my money grows with interest! Now I can save for books, a bicycle, or even my college education.



What are the features of a Savings Account?

Here are some key points:

WITHDRAWAL LIMITS

ATM withdrawal limits typically range from INR 20,000 to INR 1,50,000 per day.



Source: <https://www.businessinsider.in/rbi-raises-atm-withdrawal-limit-to-rs-10000-per-day/articleshow/56598698.cms>

INTEREST RATE

Interest rates on savings bank accounts at Unity Small Finance Bank.

Amount	Rate(%)
Upto 1 Lakh	6.00%
> 1 lakh - 5 lakh	7.00%
> 5 lakh - 50 lakh	
> 50 lakh - 10 cr.	
> 10 cr.	

Source: <https://www.livemint.com/money/personal-finance/how-can-you-cultivate-a-strong-financial-safety-net-for-your-siblings-mutual-funds-sip-insurance-11713338033268.html>

PASSBOOK

Source: <https://twitter.com/sachinmahla12/status/1078479043312472064/photo/1>

DEBIT CARD

Source: <https://bfsi.cletoonline.com/banks-issued-63-percent-higher-debit-cards-in-2019-than-in-2015/>

**Discuss**

1. Do saving accounts allow unlimited withdrawals each month? What is the withdrawal limit for a savings account?

2. Who cannot open a savings account?

**Knowledge Check**

Let us recap the knowledge we have gained so far.

1. What do savings accounts help individuals earn on their deposited money?

Coupons	Balance	Interest	Taxes
---------	---------	----------	-------

2. What type of card do savings accounts usually come with for ATM withdrawals and online transactions?

Gift Card	Debit Card	Membership Card	None of the above
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3. TRUE/FALSE: Savings accounts come with a passbook or bank statements to track transactions.....

Answers: 1. Interest 2. Debit Card 3. True

2.2 Current Account

Current accounts are a type of bank account that is used for day-to-day business transactions. They are often used by business owners and companies to manage their finances. Also, current accounts provide a higher number of transaction limits on monthly cash deposit/withdrawal compared to savings accounts.



Withdrawal

Taking money out of a bank account.

Let us learn about why Current Accounts can be helpful.

1. **Convenience:** Current accounts provide a convenient way to manage day-to-day financial transactions. They offer features such as cheque-writing, debit cards, online banking, and mobile banking apps, making it easy to access and manage funds.
2. **Liquidity:** Current accounts allow for quick and easy access to funds, providing liquidity for everyday expenses and unforeseen emergencies.
3. **Payment Facilities:** With a current account, you can arrange automatic payments for things like home rent, electricity bill, and loan payment. This makes it easier to manage your money and ensures you pay on time.
4. **Access to Other Services:** Holding a current account with a bank may give you access to many other products and services, such as loans, and investment accounts.



What are the features of a Current Account?

Here are some key points:

- There are no interest earnings.
- You can have unlimited Transactions.
- Need to maintain minimum balance.
- Cheque books can be used.
- Can be accessed through various channels- ATM, online, etc.

Now, let's go back to the example of Simran's savings account.

Example

After opening a savings account, Simran used to deposit all her extra money in it. Impressed by how Simran was handling her money, her mother asked her one day if a savings account was suitable for an Achaar business she had started. Simran replied saying that savings accounts are for an individual's savings and not a business. To ask for help, Simran went back to her teacher.



Simran: Ma'am remember you helped me open a Savings account? So my mother has an Aachar business and she also wanted an account to manage her money. Could you help?

Gurdeep: Of course! Savings accounts are not suitable for businesses. In this case, a Current Account would help.

Simran: What is a Current Account?

Gurdeep: Listen carefully, a current account is like a magic wallet where you can keep your money safe and easily access it whenever you need it. Unlike a savings account, where you earn extra money, a current account is perfect for everyday transactions especially for businesses. Your mother can use her current account to deposit and withdraw money as often as she wants, without any restrictions.

Simran: Thank you so much ma'am. This should work for my mother.



Knowledge Check

Let us recap the knowledge we have gained so far.

1. TRUE/FALSE: Unlike savings accounts, current accounts typically do not offer any interest on the deposited amount.....
2. TRUE/FALSE: Cheque book facility is not available for current accounts.....
3. TRUE/FALSE: Current accounts provide account holders with the flexibility of unlimited transactions.....

Answers: 1. True 2. False 3. True

How to choose between a Savings & a Current Account?

Differences between a Savings and Current Account		
	Savings Account	Current Account
Purpose	Used for saving money and earning interest.	Used for regular transactions and easy access to money.
Interest Earning	Earns interest on the deposited amount.	Does not earn interest on the deposited amount.
Withdrawal Limits	Has limitations on the number of withdrawals per month to encourage saving.	Typically allows unlimited withdrawals and transactions.

**Activity 5: Financial Choices**

Objective: To apply the understanding of savings and current accounts to real-life situations and consider the specific needs of an individual or business owner in India.

Example 1: Jasmeet runs a clothing shop in Ludhiana and wants to organize her business finances better with a bank account. She is confused if a savings account or a current account would be best for her business.

**Here's what Jasmeet is thinking about:**

- She has regular bills and payments to suppliers for her shop.
- Customers pay in cash or through other payment methods when they buy from her shop.
- She wants to know if she can earn extra money through interest on her account balance.
- Jasmeet is worried about any monthly charges or fees that might come with the account.

Now, let's discuss:

- Which account do you think Jasmeet should choose and why?
- How will the number of transactions in Jasmeet's business affect her choice?
- If Jasmeet wants to earn interest, will that affect her decision?

Example 2: Yuvraj, a college student in Chandigarh, is thinking about getting a bank account to manage his monthly salary and money he receives as gifts from his family. He plans to use the account for daily expenses and save some money for the future.



Here's what Yuvraj is considering:

- He receives a monthly income for college expenses.
- He gets surprise money gifts from his family.
- Yuvraj needs the account to manage his daily expenses like food and travel.
- He wants to save some of his income for future needs like study materials.
- Yuvraj is thinking if he can earn interest on the money he saves.

Now, let's discuss:

- Should Yuvraj choose a savings account or a current account, and why?
- How might the fixed monthly income affect Yuvraj's choice?



Knowledge Check

Identify whether the following example are better suited for a savings account or a current account:

1. Rohan receives a fixed amount of money from his parents every month for his personal expenses. He wants to save a portion of it for buying a new bicycle.
2. Anjali runs a small bakery and frequently receives payments from customers. She needs an account where she can deposit and withdraw money frequently for business expenses.
3. Vivek's parents deposit a sum amount in his bank account at the beginning of each semester to cover his college fees and expenses throughout the term.

Answers: 1. Savings Account 2. Current Account 3. Savings Account

2.3 Fixed Deposit Account

A Fixed Deposit (FD) is a type of investment in which an individual deposits a sum of money with a bank for a **specified period of time**. It is a popular investment option in India known for its safety and providing stable returns, which means regular earnings.

How do Fixed Deposit Accounts Work?

Here are some points:

- **Opening an Account:** To open an FD account, you need to deposit an amount of money, usually specified by the bank.
- **Choosing the Term:** You then choose the term or duration for which you want to keep the money deposited. This can range from a few months to several years.
- **Interest Rate:** The bank offers you a fixed interest rate on this amount, which is usually higher than what is offered for savings accounts.



Fixed Interest Rate

The interest rate offered on a fixed deposit is set when the deposit is made and does not change during the term of the deposit.

Benefits of Fixed Deposit Accounts:

- FDs typically offer **higher interest rates** compared to savings accounts, leading to better returns on your investment.
- FDs are considered **safe investments** as they are not subject to market fluctuations.
- With options for interest to be paid out periodically, FDs can provide **a regular source of income**.
- The returns on FDs are fixed and assured, making them **a reliable investment** choice.

Let's go back to Simran's example.

Example



Simran turned 17 years old in December. To celebrate her birthday, her father gave her a sum of ₹5,000. Simran was very excited about this gift but was also confused about what to do with it. She didn't want to buy something expensive but wanted to keep the money carefully. She thought of putting the money in her savings account but the returns were not good enough.

She went to the branch of Punjab National Bank where she had an account and had the following conversation with an employee.

Simran: I have ₹5,000 with me. I want to invest this money somewhere. Could you help me?

Manjot: Hello Simran, so we offer accounts called fixed deposits. So, in this account, you can deposit your money for a pre-decided period, known as the "term," and earn money on top of your original deposit.

Simran: This sounds like a good idea. What kind of interest rate do you offer?

Manjot: 3.25% Simran.

Simran: Okay, I would like to start an account.

Example

Amar's mother wanted to give him a special gift that would help him in the future but would not cost too much. So, she decided to put ₹25,000 in a special account called a Fixed Deposit Account for Amar.

When Amar turned 5, he already had ₹35,000 in his Fixed Deposit account! This money helped him start his schooling, and his parents did not have to worry about Amar's fees for quite a while.



Key Points:

- Amar's mother deposited a large sum of money all at once into the account.
- She wanted to make sure the money would grow steadily.
- Amar did not need the money right away.
- Amar's mother chose this because it is a safe and sure way to save money for the future.



Knowledge Check

Let us recap the knowledge we have gained so far.

1. Fixed Deposit accounts offer a...interest rate compared to regular savings accounts.
2. True/False: In a Fixed Deposit (FD), the interest rate is variable and can change over time.....
3. True/False: Opening a Fixed Deposit account requires a minimum deposit specified by the bank.....

Answers: 1. higher 2. False 3. True

2.4 Recurring Deposit Accounts

A Recurring Deposit (RD) is a unique term-deposit offered by Indian banks. It is an investment tool that allows people to make regular deposits and earn decent returns on their investment. Due to the regular deposits and the rate of interest, it makes investments easy for individuals.



Recurring Deposit

A type of term-deposit where regular, fixed amounts are deposited at regular intervals.

How Recurring Deposit Accounts Work?

Here are some points:

Decide on the Deposit Amount: You first decide on a fixed amount of money that you want to deposit into the bank regularly.

Regular Deposits: This fixed amount will be taken from your account regularly, which can be monthly or quarterly. Each deposit is made on a pre-decided date agreed upon at the time of starting the RD.

Interest Rate: The bank offers fixed interest rates for the RD account, which remain constant throughout the deposit period. These rates are usually lower than what is offered for fixed deposits but higher than savings accounts rates.



Benefits of Recurring Deposit Accounts:

- RDs encourage **regular saving habits**, as a fixed amount is deposited periodically.
- RDs are considered **a safe investment option** with assured returns.
- The returns on RDs are fixed and assured, providing **stability in earnings**.
- RDs generally **offer higher interest rates** compared to savings accounts, making them a more attractive option for regular savings.

Let's take the case of Simran again.

Example

As Simran turned 17, she decided to give Maths tuition to children from 6th-8th class in her locality in the village. With these tuitions, she was able to earn ₹6,000 per month. She was again concerned about how she could effectively invest some of this money earned. So, she went to the bank again.



Simran: Hi Manjot! I need some help with my accounts.

Manjot: Welcome back Simran! How can I help you?

Simran: So, I have recently started giving tuitions. Now that I have some income every month, I want to invest this money somewhere. Please guide me.

Manjot: Sure, Simran! You can try starting a Recurring Deposit Account. In a recurring deposit account, you commit to depositing a fixed amount of your earnings each month for a pre-decided period, known as the "term." Your savings would grow steadily over time, earning you extra interest on your monthly deposits.

Simran: This sounds exciting! So, I can invest ₹3000 per month for a period of a year and get an interest of 2.75% on this amount?

Manjot: Yes, Simran!



Example

Amar visited the bank to find a way to save money little by little each month. Here's what he learned:

Amar: I want to save some money every month so I can surprise my family with something special later on. What options do I have?

Bank Employee: A Recurring Deposit would be perfect for you! You can put in as little as ₹500 or more every month, for as short as 6 months or as long as 10 years. You can even change the amount you deposit each month if you want. The best part is that when you take the money out later, you will get back even more because of the extra interest added to it!



Key Points:

- Desire to save on a regular basis.
- Starting with a small amount of money.
- Planning to use the saved money for something special in the future.



Knowledge Check

Tick the correct answer:

1. What is a Recurring Deposit (RD)?
 - a. A credit card feature
 - b. A type of insurance policy
 - c. An investment tool offered by Indian banks

2. How does a Recurring Deposit work?

- a. By making regular deposits at a fixed interest rate
- b. By investing in stocks and bonds
- c. By depositing a lump sum amount at once

Answers: 1. c, 2. a



Activity 6: Bank Transactions

Make a chart with the different features of Fixed Deposit Account and another chart with the features of a Recurring deposit account.

(An example of a chart or infographic is given here. You can make any kind of chart or infographic, but make sure it is simple and clear with all the key points noted down)

Fixed Deposit Account(FD)	
Features	Description
Interest Rate	Fixed interest rate for the entire tenure
Investment Amount	Lump-sum investment

2.5 Forex Services (NRI, NRO, Remittances)

Banks in India provide a range of foreign exchange services to facilitate international trade, travel, and financial transactions. Here are some common foreign exchange services offered by banks in India:

Currency Exchange:

As we know different countries have their own currency in which money is circulated. For example, in India we have the Rupee but in the USA money is circulated in dollars. So, banks in India allow individuals and businesses to exchange Indian Rupees for foreign currencies. This service is particularly useful for travellers, importers, and exporters.



Definition:

Currency exchange refers to the process of converting one currency into another at an agreed-upon exchange rate.

Example



Simran's sister, Asha, has to go to Canada to continue her higher studies. Before going abroad she needs to carry a certain amount of cash for her daily transactions. To ensure that she has cash, her father takes her to a local currency exchange shop to get a currency exchange. Because of this



service, Asha can now go to Canada with Canadian Dollars.

Example

Idyant, an Indian student, is excited about studying at a university in Germany. But before he can go, he needs to exchange his Indian Rupees for the local currency in Germany, called Deutsche mark. This way, he can pay for things like food and books while he is there.



Currency exchange helps him make this switch from Indian Rupees to Deutsche mark, so he is all set for his studies abroad.



Remittance services:

Remittance services allow you to send money to your loved ones living in another part of the world. These services, provided by Indian banks, make it convenient for you to support your family financially, even when they are living outside India.



Definition:

Remittance services help with the transfer of funds abroad. They can be used for sending money to family members or making international payments.

Example

After Asha moved to Canada for her education. She started working part-time in a coffee shop in Canada. She wanted to send a part of the money back home to her parents. She used the Remittance Services provided by the bank to send this money back home.





Discuss the potential challenges that individuals like Asha might face when remittance services are unavailable during critical situations or emergencies.

NRE (Non-Resident External) Account

The Non-Resident External (NRE) Account in India is a type of bank account made for **Non-Resident Indians (NRIs)** to manage their **foreign income** in Indian currency.

Non-Resident Indians (NRIs) can open NRE accounts to send their foreign earnings, including income from jobs abroad, investments, or any other source, in India. The funds in an NRE account can be converted to any foreign currency and sent abroad without any problems. This type of account is used for saving and investing, as well as for managing finances while living abroad.

Example

Meet Rajesh!

Profession: Software Engineer

Location: United States

Goal: Support his family in India

Solution: NRE Account

- Rajesh opens an NRE (Non-Resident External) account with an Indian bank.
- He sends US dollars from his American bank account to his NRE account.
- The funds convert to Indian rupees and are easily accessible.
- Rajesh can withdraw cash from ATMs or use online banking.
- His family can also deposit money into the NRE account.
- Funds are freely transferable, meaning Rajesh can transfer money back to the US anytime without restrictions.



Benefits:

Efficient cross-border management. Rajesh can support his family while working abroad.



Knowledge Check

Let us recap the knowledge we have gained so far.

1. True/False: The NRE Account in India is made for Resident Indians to manage their domestic income in Indian currency
2. True/False: Non-Resident Indians (NRIs) can open NRE accounts to deposit their foreign earnings, such as income from jobs abroad or investments, in India
3. True/False: Funds held in an NRE account can only be converted to Indian currency and cannot be transferred to any foreign currency

Answers: 1. False, 2. True, 3. False



Discuss

Can you think of any more examples like the case of Rajesh in which NRE accounts can be useful?

NRO (Non-Resident Ordinary) Account

A Non-Resident Ordinary (NRO) Account is a way for many **Non-Resident Indians (NRIs)** to manage their **deposits or income earned in India** such as pension, rent, etc. This account allows you to receive funds in either Indian or foreign currency. NRO accounts can be used for various purposes, including receiving income from Indian sources, making local payments, and managing finances related to Indian investments or valuables.

Example

Aman, a non-resident Indian (NRI) living in the United Kingdom, has savings in Indian rupees that he wants to manage efficiently. To do so, he chooses to open an NRO (Non-Resident Ordinary) account with an Indian bank.



Example

Satinder lived in Australia, but he had a house in India, in Bangalore, that he rented out. His parents lived in Kolkata, India, and could not look after the house for him. So, Satinder needed a way to handle the money he made from renting out his house.



Key points:

- Satinder needed an NRO account to manage the income he earned from his Indian house.
- He also needed to pay for things like repairs or his parents' medical bills in India. Satinder wanted his parents to be able to use the account if they needed money for emergencies.
- With the NRO account, Satinder could easily handle all his income and expenses in India from Australia.

**Knowledge Check**

Let us recap the knowledge we have gained so far.

1. True/False: An NRO account is primarily used by residents of India.....
2. True/False: NRO accounts can only receive funds in Indian currency.....
3. True/False: With an NRO account, Satinder can easily handle all his income and expenses in India from Australia.....

Answers: 1. False, 2. False, 3. True

Why do we have NRE & NRO Accounts?

As per the **Foreign Exchange Management Act (FEMA)** guidelines, **an NRI cannot have a savings account in his or her name in India**. You must convert all your savings (money earned abroad) to a Non-Resident External Account (NRE) or Non-Resident Ordinary (NRO) account. Therefore, continuing to use the savings account in the home country can attract penalties. Opening an NRE or NRO account is, hence, a practical option for Non-Resident Indians.

It can help NRIs in two ways:

1. They can send their foreign earnings to India at any point.
2. They can also keep their income from India (via any belongings) in the home country itself.

**Penalties**

Fines or punishments imposed for breaking rules or laws.



Knowledge Check

Riya resides in Dubai and is originally from Amritsar. She owns a boutique that makes women's apparel in Amritsar, which she manages from Dubai. She needs a bank account that will allow her to manage the funds of the business and manage her employees in Amritsar.

1. Which type of Bank account does she need and why?

2. What are the advantages of that bank account?



Activity 7: Review and Discuss

Instructions:

- You may form small groups and give each group a specific banking concept or service, such as savings accounts, NRE accounts, or remittance services.
- In groups, students summarise the main points of their given topic, focusing on definition, function, example and significance.
- Groups share their summaries with the class, using pictures or flowcharts or other visual tools to help explain their ideas.

Let's Recap

1. Banking involves understanding and managing various **financial services and products**.
2. It includes different types of bank accounts such as **Savings, Current, and Fixed Deposits**, each with unique features and benefits.
3. Specialised accounts like **NRE (Non-Resident External) and NRO (Non-Resident Ordinary)** accounts cater to the financial needs of Non-Resident Indians (NRIs).
4. **Foreign exchange services** provided by Indian banks, including currency exchange and remittance services, facilitate **international trade, travel, and financial transactions**.
5. Practical application through activities and discussions helps in effectively utilizing banking knowledge for **better financial management**.



EXERCISE

Objective Type Questions

One line answer:

1. What is money?
2. Define the concept of banking.
3. What is the meaning of a Savings account?
4. Define a Current account.
5. What is a Fixed Deposit account?
6. What is a Recurring Deposit account?
7. Write any two advantages of a Fixed Deposit account.
8. Define a bank.
9. Which type of bank account typically offers a higher rate of interest: a Savings account or a Fixed Deposit account?
10. Which type of account is commonly opened by traders or businessmen?

Short Answer Type Questions

11. Explain the functions of a bank.
12. Write the differences between a Savings account and a Current account.
13. Explain why Current accounts can be helpful.
14. Explain the features of a Savings account.
15. How do NRE and NRO accounts help NRIs?

Long Answer Type Questions

16. Explain the common foreign exchange services offered by Indian banks.
17. Explain the different types of bank accounts in detail.

**Topics**

- Lending Products: Loans and Mortgages
 - Lending Products
 - Loans
 - Types of Loans
 - Processing a Loan
 - Why Are Loans Used?
 - Factors Lenders Consider
 - The Guide to Education Loans
 - Documentation Required for a Loan
 - EMI
 - Key Features of EMI
 - Mortgages
 - Types of Mortgages
 - Types of Mortgage Lenders
 - Mortgage Payments
 - Mortgage Payment Calculation
- Overdraft Facilities, Credit Cards
 - What is an Overdraft
 - Types of Overdraft
 - Features of Overdraft
 - Overdraft Protection
 - Credit Cards
 - Features of Credit Cards
 - Components of a Credit Card
 - Using the Credit Card
- Investment Products: Mutual Funds (Meaning and Schemes)
 - What is an Investment?

- What is a Mutual Fund?
 - Types of Mutual Funds
 - Mutual Funds Based on Maturity Period
 - Mutual Funds Based on Principal Investment
 - Mutual Funds Based on Risk
 - Mutual Funds Based on Investment Goals
 - How to Invest in Mutual Funds
- Meaning of Bonds and Stocks
 - What is a Bond?
 - Stocks
 - How stocks work



Learning Objectives

- Understand the purpose and types of loans, including education loans, and key terms associated with borrowing.
- Define mortgages, explore different types, and comprehend mortgage payments and lender responsibilities.
- Define overdraft facilities, identify types and features, and understand the concept of overdraft protection.
- Explain the components and usage of credit cards, including responsible financial practices.
- Define mutual funds and their types, explore investing principles, and differentiate between bonds and stocks in investment portfolios.



Materials Required

- Sample Loan and Mortgage Documents
- Sample Credit and Debit Cards
- Mutual Fund Brochures and Prospectuses
- Stock and Bond Certificates or Mock Certificates



Activity 1: Before We Begin!

1. List down all the banking products and services you are familiar with, and write a brief description or example of each:

1.0 Lending Products: Loans and Mortgages

1.1 Lending Products

As financial institutions, we recognize that individuals, businesses, and organisations may sometimes face financial gaps that hinder their ability to complete projects or make necessary purchases. In these situations, they turn to lenders for assistance.

A **lender** is a person or entity (a public or private organisation, or a financial institution like a bank or a non-banking financial company (NBFC)), that provides funds to another, expecting repayment with interest.



Lending

The act of giving money to someone with the expectation that it will be repaid, usually with interest.

Preferred Lenders: Banks and NBFCs are favoured for their reliability and adherence to regulations, ensuring transparency and security in lending. Banks are committed to providing lending solutions that meet the clients' needs while managing risk effectively.

'Risk' refers to the possibility that a borrower may not repay the loan as agreed due to various reasons. Banks manage risks to protect their financial health. This involves assessing the borrower's repayment ability by reviewing credit history and setting appropriate loan terms before approving the loan.



Credit History

A record of a borrower's past loans and payments, used by lenders to assess their trustworthiness for future loans.

Example

Sunny wants to expand his sweet shop in Kapurthala by opening a second store in Bathinda for wider reach. To do this, he needs additional funds.

Can you come up with some options that can help Sunny to fund his project?



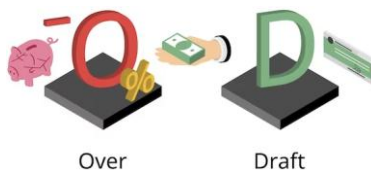
Let's look at some options that Sunny considered to fund his project -



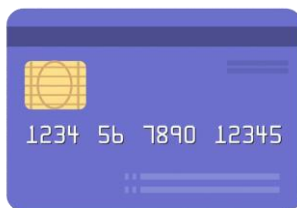
Loan: Sunny approaches a local bank with his expansion plans. The banker reviews his business plan, financial statements, and credit history. After a thorough assessment, the banker approves a business loan of ₹ 5,00,000 at an interest rate of 12% per annum for a term of 5 years. Sunny uses this loan to secure a new location, purchase equipment, and hire staff for the new shop.



Mortgage: Deciding to purchase the new property instead of renting, Sunny applies for a mortgage. The banker offers him a mortgage of ₹ 20,00,000 at an interest rate of 8% per annum for a term of 15 years. Sunny makes monthly payments towards the mortgage, which includes both principal and interest, securing a long-term asset for his business.



Overdraft Facility (OD): To manage working capital, i.e., the funds used to cover short-term expenses and operational needs, Sunny applies for an overdraft facility. The banker approves an overdraft limit of ₹3,00,000, providing him the flexibility to cover short-term expenses like purchasing raw materials, paying salaries, or handling unexpected costs.



Credit Card: Sunny also obtains a business credit card with a limit of ₹ 1,00,000 to manage day-to-day expenses. He uses the card to buy ingredients, packaging materials, and other supplies, and pays the credit card bill monthly, ensuring smooth cash flow management.

1.2 Loans

A loan is a financial arrangement where a **borrower** receives funds from a **lender** and commits to repaying the principal amount along with any additional charges, such as interest, over a specified period. Borrowers can be individuals, businesses, or organisations, while lenders typically include banks, government entities, and other financial institutions. Loans come in various forms, including secured, unsecured, business, and personal loans, each with specific terms and conditions.

Loans have four main components:

1. **Principal:** The amount of money borrowed.
2. **Term:** The duration over which the loan must be repaid
3. **Interest Rate:** The cost of borrowing, calculated as a percentage of the principal.
4. **Payments:** Regular instalments made to repay the loan, including both principal and interest.

An **amortisation table** helps calculate these payments. An amortisation schedule is a table that shows how each loan payment is split between paying off the loan amount (principal) and paying interest over the life of the loan. Lenders may also charge fees and require collateral. **Collateral** is an asset that a borrower pledges to a lender as security for a loan, which the lender can seize if the borrower fails to repay the loan (like property).

Example

Ranbir, the owner of a textile company, decides to take a loan to grow his business. He secures a loan of ₹5,00,000 at a 10% annual interest rate for a 5-year term. Here's a breakdown of his loan:

1. Principal: ₹5,00,000, the amount Ranbir borrowed.
2. Term: 5 years, the period Ranbir has to repay the loan.
3. Interest Rate: 10% per annum, meaning every year Ranbir pays 10% of ₹5,00,000, which is ₹50,000 as the **cost of borrowing** money.

So, over 5 years, the total interest would be $₹50,000 \times 5 = ₹2,50,000$. Therefore, Ranbir borrows ₹5,00,000 but repays a total of ₹7,50,000 (₹5,00,000 principal + ₹2,50,000 interest).

4. Payments: Monthly instalments calculated using an amortisation table, covering both principal and interest.



To secure this loan, Ranbir gives the bank a promise that if he can't repay the loan, they can take his workshop as **collateral**. Collateral is an asset that the borrower offers to the lender as security for the loan. If Ranbir fails to make his loan payments, the bank has the right to seize the workshop to recover the loan amount.

In addition to the interest, the bank charges a small extra fee for setting up the loan and managing it. Other costs like late payment charges, prepayment penalties, insurance, and legal fees are also part of the loan agreement.

1.2.1 Types of Loans

Loans come in different forms to suit diverse financial goals and situations. Here's a quick look at some common types:

- **Business Loan:** A business loan helps people who want to start a new business or make their existing business bigger.

- **Agricultural Loan:** Agricultural loans are for farmers. They help them buy things for their farms, like seeds, tools, or machinery.
- **Home Loan:** A home loan helps people buy a house or renovate one they already have. It's a way to own a home without paying all the money at once.
- **Education Loan:** An education loan helps students pay for their studies, like college fees or school expenses. It helps them focus on learning without worrying about money.
- **Gold Loan:** A gold loan is a secured loan. When someone gives their gold as security (collateral) to get money from a bank. If they can't pay back, the bank keeps the gold.

Understanding these loans helps in making informed decisions when considering borrowing options. There are many other kinds of loans, including travel loans, wedding loans, car loans, medical emergency loans, loans against property, and many more.

By offering a diverse range of loan products, financial institutions ensure that clients have access to the necessary financial support to achieve their goals.

1.2.2 Processing a Loan

Getting a loan is a step-by-step process, turning dreams into reality:

1. **Starting Point:** The applicant.
2. **Bank's Decision:** The bank reviews the application to assess the feasibility of lending.
 - a. If No: Clear reasons are provided for the decline, offering constructive feedback for the applicant to explore other options.
 - b. If Yes: Mutual agreement on repayment terms is reached, and the funds are disbursed accordingly.
3. **Repayment:** The borrower initiates repayment in accordance with the agreed-upon schedule and terms.

Example

Preet, a young entrepreneur from Punjab, dreamed of opening a boutique to sell Punjabi dresses. She needed financial support, so she approached a bank with a solid business plan. The bank carefully verified her application and documents. Impressed with her idea and thorough preparation, they approved her loan request. With the funds, Preet opened her boutique, which quickly became a favourite spot for people to buy traditional clothes. Her success showed everyone that with a good plan and a little help, big dreams can come true.



1.2.3 Why Are Loans Used?

Loans serve as vital financial tools for individuals and businesses to address various needs and opportunities. Here's why loans are commonly used:

Financing Purchases: Loans enable individuals and businesses to afford significant purchases, such as homes, vehicles, or educational expenses, which they are unable to afford up front.

Business Expansion: Companies use loans to grow their operations, buy machinery, recruit staff, and stock up on goods, helping them to grow and make profits.

Emergency Expenses: Loans provide financial relief for unexpected costs like medical emergencies or urgent home repairs, ensuring stability during unforeseen circumstances.

Investment: Borrowers may use loans to invest in stocks, bonds, real estate, or to fund entrepreneurial ventures, aiming to generate returns and build wealth over time.

Credit Building: Responsible borrowing and timely repayment of loans help individuals build and improve their credit scores. This, in turn, enhances their eligibility for future loans, credit cards, and favourable interest rates.

1.2.4 Factors Lenders Consider

When evaluating loan applications, lenders focus on several key factors to assess the borrower's ability to repay:

- **Income:** The applicant's income from employment provides a measure of their capacity to pay back the loan.
- **Job Stability:** If the applicant has a job for a long time, it shows they have a steady income, enhancing confidence in their repayment ability.
- **Credit Score:** Reflects the applicant's past credit repayment history; a higher score indicates lower risk for lenders.
- **Other Loans:** The number and amount of current loans impact the applicant's ability to take on additional debt.
- **Debt-to-Income Ratio:** Compares the applicant's monthly debt payments to their income; a lower ratio suggests the applicants are in a better position to handle a new loan.



Lenders prioritise these factors to ensure responsible lending and minimise the risk of non-repayment. It's crucial for borrowers to manage finances wisely for a secure financial future.

Let us understand these factors in more detail by looking at some scenarios where loan applications were rejected:

Example

Rajdeep Singh had a dream to grow his furniture business. He needed some extra money to buy new tools and hire more workers. So, he decided to **apply for a loan** at the bank. But the bank couldn't give him the loan because Rajdeep's income wasn't regular, and he didn't have a stable job. This was a setback for Rajdeep, but he didn't lose heart. He began exploring other options to raise funds, like inviting people to invest in his business. Through this experience, Rajdeep understood that to be eligible for a loan, it's important to have a steady income and a solid work record. Now, he is focused on building a more reliable business so he can apply for the loan again with confidence.

**Example**

Amit, a hardworking young man, saved up for his dream car. He was excited and applied for a car loan. But the bank said no because Amit had too much debt compared to his income, known as a poor debt-to-income ratio. Amit was surprised but took a good look at his money matters. He saw he owed more money each month than he earned.



1. **Debt-to-Income Ratio:** This ratio compares how much Amit owes each month (debt) to how much he earns (income). A high ratio means that a large portion of his income goes toward paying debts, leaving little room for other expenses or savings.
2. **Amit's Situation:**
 - Monthly Income: Let's say Amit earns ₹50,000 each month.
 - Monthly Debts: He has to pay ₹30,000 towards loans, credit card bills, etc.
3. **Debt-to-Income Ratio Calculation:**
 - $\text{Ratio} = (\text{Monthly Debts} / \text{Monthly Income}) \times 100$
 - $\text{Ratio} = (\text{₹}30,000 / \text{₹}50,000) \times 100 = 60\%$
4. **What This Means:** A 60% debt-to-income ratio means Amit is using 60% of his monthly income just to pay off his debts.
5. **Amit's Realisation:**
 - Income: ₹50,000 per month
 - Debts: ₹30,000 per month
 - Leftover Income: ₹20,000 for all other expenses (rent, groceries, savings, etc.)

Amit felt sad about this but knew he had to fix it. He made a plan to pay off his debts, spend less on things he didn't need, and try to earn more. Amit didn't lose hope. He understood it would take time to get his finances right. But he was ready to work hard to one day make his dream of owning that perfect car come true.

1.2.5 The Guide to Education Loans

Education loans provide crucial financial support to students for covering school and living expenses, facilitating their pursuit of higher education after high school. Here are key points about education loans:

Eligibility: Available to Indian residents who are enrolled in recognized colleges or universities.

Loan Amount: Up to 50 lakh rupees for studies in India; up to 1 crore rupees for studies abroad.

Interest Rate: This is the extra money that borrowers pay back, Typically ranges from 8% to 16%, adding to the repayment amount.

Repayment: Begins after the student or borrower completes their studies or gets a job.

Collateral: Sometimes the borrower needs to promise something valuable for larger loans, which acts as security against the borrowed amount.

Required Documents: Include admission letter, fee structure, and proof of income for the loan guarantor.

Tax Benefits: Eligible for tax savings on the interest paid under applicable regulations.

Coverage: Funds can be used for tuition fees, books, uniforms, and other educational expenses.

Application Process: Applicants can visit the bank branch or apply online for convenience.

Government Support: Some schemes help students from families with less money by not charging interest for a while (for a specified period).

Education loans empower students to focus on their academic pursuits without financial stress. However, it's essential for borrowers to carefully review and understand the loan terms to make informed decisions.

After exploring the various purposes for which loans can be taken, it is equally important to understand the different structures loans can have. Let us delve into the nature of loans, distinguishing between secured and unsecured to gain a complete picture of the financial tools available.



Repayment

The act of returning borrowed money, typically in scheduled instalments that include both principal and interest amounts.



Loan Guarantor

Someone who agrees to be legally responsible for repaying a loan if the primary borrower cannot make the payments.

Secured Loan	Unsecured Loan
<ul style="list-style-type: none"> • A loan that needs something valuable, like a house or car, to guarantee it. • Safer for Banks: Because they can take the valuable item if the loan isn't paid back. • Examples: Home loans are backed by the house, and car loans by the car. 	<ul style="list-style-type: none"> • A loan given based on trust and your financial history, without needing a valuable item as a guarantee. • Riskier for Banks: Higher interest rates because there's no guarantee. • Examples: Personal loans and student loans depend on your credit history.



Knowledge Check

Let us recap the knowledge we have gained so far.

1. What is a collateral in a loan agreement?
2. Which of the following is a secured loan:
 - a. Personal loan
 - b. Credit card
 - c. Car loan
 - d. Education loan
3. State TRUE or FALSE: An unsecured loan requires collateral.

Answers:

1. Collateral is an asset pledged as security for repayment of a loan.
2. c. Car loan 3. False



Knowledge Check

Below you will see the various steps a borrower undergoes when taking out a loan. However, the steps have been jumbled up. In this activity, you will arrange the steps in the proper order.

- A. Applying for a loan
- B. Spending the principal amount for the required use
- C. Noticing a need for financing
- D. Bank approves and processes the loan application
- E. Repayment process begins
- F. Researching about loans
- G. Preparing the documents required to apply for a loan
- H. Bank assesses the documents submitted with the loan application
- I. The loan has been repaid in full

Answer:

The correct order will be: C, F, G, A, H, D, B, E, I

1.2.6 Documentations Required

The documents needed for a loan application varies based on the lender and the type of loan. But for the majority of loans, the following standard documents are usually needed:



Identity Proof

- Aadhaar Card
- Passport
- Voter ID Card
- PAN Card
- Driving Licence



Address Proof

- Aadhaar Card
- Passport
- Voter ID Card
- Utility bills (electricity, water, gas)
Not older than 3 months
- Rent Agreement



Income Proof

- Salary slips for the last 3 months (for salaried individuals)
- Bank statements for the last 6 months
- Income Tax Returns (ITR) for the last 2-3 years (for self-employed individuals)
- Audited financial statements (for businesses)



Employment/Business Proof

- Offer letter, appointment letter, or employment certificate (for salaried individuals)
- Business continuity proof (for self-employed individuals)
- Business registration documents (for businesses)



Property Documents (for secured loans)

- Sale deed
- Title deed
- Encumbrance certificate



Guarantor Documents (if applicable)

- Identity proof
- Address proof
- Income proof



Loan Application Form

- Filled and signed by the applicant(s)



Photographs

- Passport-sized photographs of the applicant(s)

However, we must remember that the documents required may differ from lender to lender. There are some documents, like the property documents, which are required to apply for secured loans and may not be necessary when applying for an unsecured loan. The type and loan amount may also be a deciding factor when it comes to the required documents. This is, therefore, just a general list of documentation. For an exact list of documents, advise a borrower to reach out to their lender.



Knowledge Check

1. What document is required as income proof for salaried individuals applying for a loan?
2. Which document is needed as income proof for self-employed individuals applying for a loan?

Answers: 1. Salary slips for the last 3 months 2. Income Tax Returns (ITR) for the last 2-3 years

1.2.7 EMI

EMI stands for **Equated Monthly Instalment**, where borrowers repay a fixed amount to the lender each month on a specified date. This amount comprises both the principal and interest components of the loan over its duration.

Key Features of EMI:

Predictable Budgeting: The fixed EMI amount allows borrowers to plan and budget their monthly expenses effectively throughout the loan term.

Principal and Interest Components: Each EMI consists of two parts—principal repayment and interest payment. Initially, a larger proportion of the EMI goes towards paying interest, while more goes towards repaying the principal in the later stages of the loan.

Detailed Repayment Schedule: Borrowers receive a repayment schedule detailing the allocation of each EMI towards principal and interest. This helps in tracking the progress of

loan repayment.

Impact of Early Payments: Making early repayments can reduce the outstanding principal amount, potentially reducing the total number of EMIs or shortening the loan tenure, depending on the loan terms.

Understanding these features empowers borrowers to manage their finances effectively and make informed decisions throughout the loan repayment journey.

1.3 Mortgages

A mortgage is a specialised loan used to purchase real estate or refinance existing properties.

Key Points to Understand When Obtaining a Mortgage:

- **Securing Funds:** The borrower secures funds from a lender, such as a bank or mortgage company, to acquire or refinance a property.
- **Repayment Terms:** The borrowed amount, plus interest, is repaid by the borrower over a predetermined period, typically spanning 15 to 30 years.
- **Collateral:** The property being purchased serves as collateral for the loan. This means the lender has a claim on the property until the loan is fully repaid.
- **Foreclosure:** If the borrower fails to make the required payments (defaults), the lender can initiate foreclosure. This process allows the lender to take possession of the property and sell it to recover the outstanding loan balance.



Understanding these fundamentals is crucial for borrowers navigating the mortgage process responsibly.

1.3.1 Types of Mortgages

There are six common types of mortgages in India:

Simple Mortgage: In a simple mortgage, the borrower (**mortgagor**) promises to pay back the borrowed amount. Although the property remains with the borrower, if they don't pay back the money, the lender (**mortgagee**) can sell the property. **Example:** A homeowner mortgages their house to a bank to secure a home loan.

English Mortgage: The borrower agrees to pay back the borrowed sum by a specific date and transfers the property to the lender. Once the debt is cleared, the lender will return the property to the borrower. **Example:** Mrs. Kaur sells her house to Mr. Singh, but Mr. Singh agrees to re-transfer it when Mrs. Kaur repays the loan.

Usufructuary Mortgage: The borrower hands over the property to the lender, who can use it to earn income (like rent) until the loan is repaid, while the borrower retains ownership.

Example: A farmer mortgages their land to a bank, allowing the bank to collect rent from the land while the farmer still remains the owner of the land.

Mortgage by Deposit of Title Deeds: Also known as an equitable mortgage, here the borrower gives the lender the property's title deeds to create a security interest in the property. **Example:** Mr. Singh borrows money from a bank and provides the property title deeds as collateral without transferring ownership.

Mortgage by Conditional Sale: This arrangement involves the borrower selling the property to the lender with the condition that the sale will be reversed once the loan is repaid. **Example:** Mr. Hemant lends money to Mr. Idyant, who mortgages his property. Upon repayment, the property reverts to Mr. Idyant's ownership.

Anomalous Mortgage: Any mortgage that doesn't fit into the standard categories is considered anomalous. It may have unique terms that are specifically agreed upon by the borrower and lender. **Example:** A loan against property (LAP) structured to accommodate irregular income streams or unique property characteristics.



Knowledge Check

TRUE or FALSE:

1. A usufructuary mortgage allows the lender to enjoy the benefits of the property.
2. An anomalous mortgage is a standard mortgage agreement with no special conditions.

Answers:

1. True
2. False

1.3.2 Types of Mortgage Lenders

In India, there are various types of mortgage lenders who provide mortgages for different purposes. Some of the common types include:

Banks: State Bank of India (SBI), HDFC Bank, ICICI Bank
Housing Finance Companies (HFCs): HDFC Ltd, LIC Housing Finance, DHFL
Non-Banking Financial Companies (NBFCs): Bajaj Finance, Tata Capital, L&T Finance
Cooperative Banks: Punjab State Cooperative Bank, Saraswat Cooperative Bank, The Cosmos Cooperative Bank
Regional Rural Banks (RRBs): Punjab Gramin Bank, Malwa Gramin Bank, Sutlej Gramin Bank
Public Sector Undertakings (PSUs): National Housing Bank (NHB), Housing and Urban Development Corporation (HUDCO)

1.3.3 Mortgage Payments

Mortgage payments in India are usually calculated using the EMI method. The formula for calculating a mortgage EMI is

$$\text{Equated Monthly Instalment, EMI} = \left[\frac{P \times R \times (1+R)^N}{(1+R)^N - 1} \right]$$

Where,

- P is the principal amount
- R is the monthly interest rate (annual interest rate divided by 12)
- N is the loan tenure in months

Along with this, the following factors also affect mortgage payments:

1. **Loan Amount:** A higher loan amount will result in a higher EMI, making the mortgage payment high.
2. **Interest Rate:** A higher interest rate will result in a higher EMI, making the mortgage payment high.
3. **Loan Tenure:** In India mortgage tenures range from 5 to 30 years. Longer tenures result in lower EMIs but higher total interest paid over the loan term.
4. **Prepayment:** Making prepayments reduces the outstanding loan amount, which can reduce future EMIs or shorten the loan tenure.
5. **Down Payment:** A higher down payment reduces the loan amount and, consequently, the EMIs.

Mortgage Payment Calculation

Example

Calculate the monthly payment for a home mortgage with these characteristics.

Amount borrowed = ₹10,00,000

Number of years to make the mortgage payments = 15

Market interest rate = 9%

Mortgage Calculator

SHARE

What Is The Amount Of Loan You Want To Borrow?

₹ 1000000

Rate Of Interest (P.A)

9 %

Duration Of The Loan

15 Years

Principal Interest

Monthly EMI Is	₹10,143
Total Amount Payable Is	₹18,25,680
Interest Component	₹8,25,680

Source: <https://cleartax.in/s/mortgage-calculator>

Good to Know!

Loan Details:

- **Principal Amount (P):** ₹10,00,000
- **Annual Interest Rate:** 9%
- **Loan Tenure:** 15 years

Steps to Calculate EMI:

Convert Annual Interest Rate to Monthly Interest Rate:

- Monthly Interest Rate (R) = Annual Interest Rate / 12
- R = 9% / 12
- R = 0.75% per month or 0.0075 (in decimal form)

Convert Loan Tenure to Months:

- Loan Tenure in months (N) = 15 years × 12 months/year
- N = 180 months

Apply the EMI Formula:

- $$EMI = \frac{[P \times R \times (1+R)^N]}{[(1+R)^N - 1]}$$
- $$EMI = \frac{10,00,000 \times 0.0075 \times (1 + 0.0075)^{180}}{(1 + 0.0075)^{180} - 1}$$

Calculate $(1 + R)^N$:

1.0075¹⁸⁰ = 3.83804326748

$$= (1 + 0.0075)^{180} = 3.838$$

The steps for calculating $(1 + 0.0075)^{180}$ in calculator is given below:

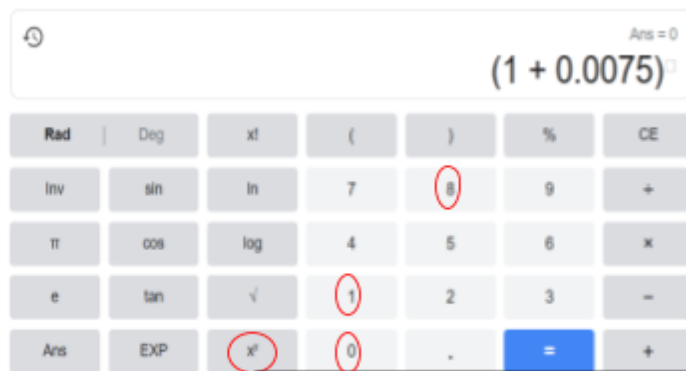


1. Open the bracket



3. Close the bracket

2. Enter 1 + 0.0075



4. Press x^y and enter 180



Thus,

$$EMI = \frac{10,00,000 \times 0.0075 \times 3.838}{3.838 - 1}$$

$$EMI = \frac{28785}{2.838} = 10142.70$$

EMI for a ₹10,00,000 loan at 9% annual interest rate for 15 years is approximately ₹10143.

For more detailed problems and explanations on repayment calculations and EMI, refer to the unit 'Understanding Basic Banking Calculations,' Section IV, Loan Repayment Calculations or EMI.



Discuss

What key factors should individuals consider before taking out a loan or applying for a mortgage, from a banker's viewpoint?

2.0 Overdraft Facilities, Credit Cards

2.1 What is an Overdraft?

A common credit facility provided by banks is the **overdraft (OD)** facility. This short-term loan allows clients to withdraw money from their savings or current account even if the account balance is **zero**. Borrowers typically use the OD facility to manage their business operating expenses. The withdrawn amount, known as "**overdrawn**," must be repaid within the specified period set by the bank.

Lenders may impose interest rates on the overdrawn amount, which borrowers must repay according to the bank's terms and conditions. Notably, interest is charged only on the utilised overdraft amount, not on the total overdraft limit. The interest rate for OD facilities is fixed, not variable.

The Key Differences Between a Loan and an Overdraft

1. Loans are borrowed funds, while overdrafts are withdrawals exceeding your account balance.
2. Loans are suited for long-term needs (5 - 20+ years), whereas overdrafts are for short-term fund requirements.
3. Loan interest is calculated monthly, while overdraft interest is calculated daily on the amount you overdraw.
4. Loans are repaid through EMIs, while overdrafts are repaid by depositing funds into your account.



2.1.1 Types of Overdraft

In India, there are primarily two types of Overdraft facilities, namely Secured and Unsecured.

Example

Amarjeet Singh's Overdraft Against Property: Amarjeet Singh, a grocery store owner, faces a cash flow problem due to the pandemic. He needs funds to pay suppliers and employees.

- He thinks, "Why not use my shop's value to get some quick cash?"
- Amarjeet talks to his bank and asks for an overdraft using his shop as a guarantee.
- The bank checks his shop's worth and says, "Alright, you can get up to ₹25 lakhs!"
- Whenever he needs, Amarjeet takes some cash from the bank, only paying interest on what he uses.
- Sales improve, and Amarjeet starts repaying the bank.
- His smart use of the overdraft keeps his store open and his dreams alive!

Secured Overdraft	Unsecured Overdraft
<ul style="list-style-type: none"> Secured overdraft facilities are supported by valuable assets, securities, or real estate. Because the lender has the option to seize the collateral in the event of default, there is less risk for them. 	<ul style="list-style-type: none"> An unsecured overdraft facility is dependent on the borrower's creditworthiness and does not require collateral. Greater risk for the lender because there isn't any collateral to help them get their money back if they default.

Example

Gurpreet Kaur's Overdraft Against Fixed Deposit: Gurpreet Kaur, a retired government employee, needs funds for her husband's medical expenses. She has a fixed deposit (FD) of ₹10 lakhs.



- Instead of closing her fixed deposit, she opts for an overdraft.
- Her bank says she can borrow up to ₹9 lakhs, which is 90% of her FD.
- She uses the money for the treatment, with the plan to pay it back when she can.
- Once things get better, she will repay the overdraft while her FD keeps growing.

Example**Manpreet Singh's Overdraft Against Insurance**

Policy: Manpreet Singh has been paying life insurance premiums for 15 years. His policy offers a maturity benefit of ₹20 lakhs. Manpreet is facing a financial emergency due to his parents' medical expenses.

- Manpreet learns he can get an overdraft facility from his bank up to his insurance policy's surrender value (₹10 lakh).
- He applies and submits necessary documents.
- The bank approves an overdraft limit of ₹5 lakh (50% of the surrender value).
- Manpreet uses the overdraft for his parents' medical expenses.
- He pays interest only on the amount he uses.
- He plans to repay once his financial situation improves or he receives funds from other investments.
- The overdraft provides financial flexibility during a tough time without affecting long-term goals.

Note: Although Gurpreet and Manpreet's overdrafts are backed by their Fixed Deposit and Insurance Policy respectively, these are **unsecured overdrafts**. The FD and insurance policy are not used as collateral, but rather **determine the overdraft limit**. This means that the overdraft facility does not convert the FD or insurance policy into secured assets, and the funds remain accessible to Gurpreet and Manpreet, allowing for financial flexibility.

Example



Harpreet Singh's Overdraft Secured by Property:

Harpreet Singh, a small business owner, needs a large sum of money to expand his shop. Instead of taking a regular loan, he chooses a secured overdraft from his bank.

- He uses his commercial property, worth ₹50 lakhs, as security for the overdraft.
- The bank allows him to borrow up to ₹30 lakhs, which is 60% of his property's value.
- Since the overdraft is secured by his property, the interest rate is lower than what he would pay on an unsecured loan.
- Harpreet withdraws money from the overdraft as needed for his business, paying interest only on the amount he uses.
- If Harpreet doesn't repay the overdraft, the bank can take and sell his property to recover the money.

Banks offer tailored overdraft facilities to meet various customer needs, ensuring flexibility and financial support in times of need while managing their risk through secured and unsecured options.



Knowledge Check

1. What is an overdraft facility?
2. What is the main difference between a secured and unsecured overdraft facility?
 - a. The interest rate
 - b. The repayment term
 - c. The presence of collateral
3. An overdraft against which of the following requires the borrower to pledge collateral?
 - a. Fixed deposit
 - b. Insurance policy
 - c. Property

Answers:

1. A common form of credit facility offered by banks.

2. c. The presence of collateral
3. c. Property

2.1.2 Features of Overdraft

The features of an overdraft underscore how an overdraft facility supports financial management, transparency, and responsible borrowing practices in banking.

Approved Credit Limit: Banks set a maximum borrowing limit based on creditworthiness and collateral, ensuring responsible lending.

Interest Rate: Interest is charged on the used amount, calculated daily and billed monthly at a fixed rate for clarity in repayment. The overdraft fees and interest rates vary by bank and account type.

No Prepayment Charges: Borrowers can repay anytime without extra costs, promoting financial flexibility.

Minimum Monthly Payments: While no minimum monthly payment is set, staying within the credit limit is crucial to maintain a good credit score.

Joint Borrowers: Shared responsibility ensures all parties commit to timely repayment, fostering accountability.

Overdraft Usage Monitoring: Banks regularly monitor overdraft usage to ensure that customers do not exceed their approved limits.

Alerts and Notifications: Many banks offer alerts to notify customers of low account balances or when they are approaching their overdraft limit. These alerts help customers manage their finances more effectively.

2.1.3 Overdraft Protection

Banks offer overdraft protection to help clients avoid overdrawing their accounts and paying penalties. This service covers transactions when there isn't enough money in the account, allowing the transaction to proceed. Benefits include avoiding rejected transactions and related costs, and ensuring necessary transactions are handled. However, using overdraft protection may involve fees or interest. Sufficient funds in linked accounts or credit lines are needed to cover overdrafts.

Example

Automatic Transfer: Scenario: Harjit Singh, a small business owner, links his savings account to his current account for automatic transfer overdraft protection.



Situation: Harjit's current account doesn't have enough funds to pay suppliers due to a client's delayed payment.

Outcome: The bank automatically transfers funds from Harjit's savings account, covering the transaction and avoiding overdraft fees.

Example

Overdraft Transfer: Manpreet Singh, a working professional, links his checking account to his credit card for overdraft transfer protection.

Situation: Manpreet's checking account is low due to a salary delay and can't cover his rent payment.

Outcome: The bank automatically transfers funds from Manpreet's credit card, ensuring the rent payment goes through, avoiding overdraft fees.



Knowledge Check

1. How does an overdraft facility work?

2. What is overdraft protection?

- Protection against fraudulent transactions
- Protection against account closure
- Protection against overdrawing the account

Answers:

- When an account holder has an overdraft facility, they can take money from their account up to a predetermined authorised limit, even if their account balance is zero or negative. The overdraft is normally repayable on demand, and fixed interest is assessed to the account holder on the amount overdrawn.
- c. Protection against overdrawing the account

2.2 Credit Cards

A **credit card** is a financial tool issued by banks or financial institutions, allowing users to borrow money for transactions. The borrowed amount, known as '**credit**', comes with a predefined credit limit. Users must repay this borrowed amount within a specified period. Each month, the



cardholder receives a statement detailing all transactions. They have the choice to either pay the full amount to avoid interest charges or pay a minimum amount, carrying forward the balance with accrued interest. Default or late payments may incur penalties or additional interest charges by the credit card issuer.

2.2.1 Features of Credit Cards

- **Convenience:** Credit cards enable users to make purchases conveniently without the need for cash.
- **Credit Limit:** Each card has a predefined maximum amount that users can borrow, known as the credit limit.
- **Rewards and Benefits:** Users can earn rewards such as points, cashback, discounts, and other perks based on their spending patterns.
- **EMI Facility:** Allows users to convert large purchases into manageable monthly instalments, providing financial flexibility.
- **Safety:** Credit cards offer security features like fraud protection and secure transaction processes to safeguard users' financial transactions.

2.2.2 Components of a Credit Card

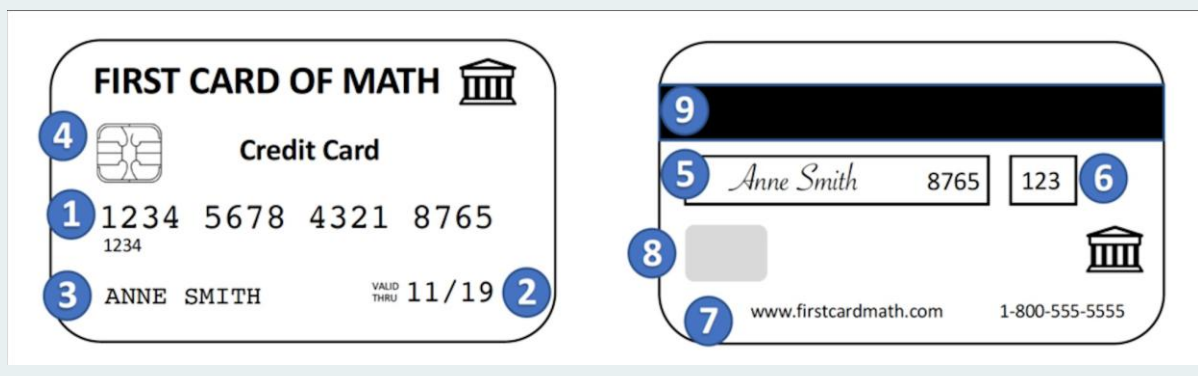
Essential components that can help in navigating credit card transactions are typically found on both the front and back of the card.

- **Card Number:** A unique 16-digit number.
- **Cardholder Name:** The name of the person authorised to use the card.
- **Expiry Date:** The date until which the card is valid.
- **CVV:** A security code used for online transactions.
- **Chip and Magnetic Stripe:** Used for processing transactions.
- **Hologram:** Used to prevent counterfeiting. It's a three-dimensional image that changes appearance from different angles, making it hard to copy.



Activity 2: Recognize the components

Identify every component that you can recognise.



- | | |
|----------|----------|
| 1. _____ | 6. _____ |
| 2. _____ | 7. _____ |
| 3. _____ | 8. _____ |
| 4. _____ | 9. _____ |
| 5. _____ | |

2.2.3 Using the Credit Card

Example

One day, Raj decides to use his credit card to buy a new laptop and pay his monthly electricity bill. Here's how he uses the card:

Raj visits an electronics store and selects a laptop worth ₹40,000. At the checkout, he **swipes his credit card**, and the transaction is approved. Later, he pays his electricity bill of ₹2,000 through the **bank's mobile app**, earning 5% **cashback**. At the end of the month, Raj receives his **credit card statement**.



- It shows all his transactions, the total amount spent (₹42,000), the minimum payment due (₹2,100), and the due date.
- Raj decides to pay the full balance of ₹42,000 to avoid interest charges. He logs into his online banking account and makes the payment before the due date.
- Since Raj paid the full balance, he doesn't incur any interest charges.
- If he had only made the minimum payment of ₹2,100, the remaining balance of ₹39,900 would attract interest at the specified rate.

For his purchases, Raj earns reward points and cashback. He plans to redeem the points for gift vouchers and enjoys the cashback on his electricity bill.



Discuss

How did Raj benefit from using the credit card? What were the costs Raj had to be mindful of?

3.0 Investment Products: Mutual Funds (Meaning and Schemes)

3.1 What is an Investment?

An investment is an asset purchased with the expectation of appreciating in value or generating income over time. Instead of using funds for immediate consumption, investors allocate capital into opportunities that offer potential growth or returns in the future.

For instance, purchasing stocks, bonds, or mutual funds reflects an investor's expectation of value appreciation or income generation. This increase in value is referred to as **appreciation**.

Key Points to Understand:

Profit and Value Increase: Investors seek to generate returns over time, **aiming for profitability** through the appreciation of their investments.

Resource Commitment: Investing involves using resources like **money, time, or effort** with the expectation of getting more back later.

Risk: All investments carry the risk of potential financial loss. **Diversification**—spreading investments across different types helps mitigate risk, though it may also impact potential returns.

Investment Vehicle

An **investment vehicle** is a financial instrument used by investors to generate profits. These vehicles come in various forms, each with its own risk and return characteristics. Common investment vehicles include stocks (shares in a company), bonds (loans to a company or government), and mutual funds (pools of money from many investors used to buy a variety of stocks and bonds). Investment vehicles provide a way for individuals or organisations to invest their money and potentially grow their wealth. They offer different options to suit various risk tolerances and financial goals.

Example

Gurpreet's Plans for Retirement: Let's look at Gurpreet's scenario to understand investment products better. Gurpreet owns a profitable clothing store in Chandigarh and wants to invest some of her profits to grow her wealth and secure her future.

Mutual Funds: Gurpreet decides to invest in mutual funds, which pool money from many investors to buy a variety of stocks, bonds, or other securities. She picks a mutual fund focused on the National Stock Exchange of India (NSE) because she believes in India's economic growth. Gurpreet invests ₹1,00,000 in this mutual fund, hoping for appreciation in value as the Indian economy grows. The mutual fund is managed by a professional fund manager.



Bonds: Gurpreet also considers bonds, which are loans to governments or corporations that pay fixed interest. She invests ₹50,000 in a government bond with a 7% annual interest rate for 5 years. Gurpreet receives regular interest payments and gets her ₹50,000 back at the end of the term. Though bonds offer stable returns, they don't provide the same potential for appreciation in value as stocks or mutual funds.

Stocks: Additionally, Gurpreet buys stocks in a well-established textile company listed on the NSE. She purchases 100 shares at ₹500 each, totaling ₹50,000. Gurpreet hopes the company's stock price will appreciate, allowing her to sell the shares at a profit in the future.

By diversifying her investments across mutual funds, bonds, and stocks, Gurpreet aims to grow her wealth and ensure financial security for her retirement.

3.2 What is a Mutual Fund?

A mutual fund is an **investment vehicle** where money from many investors is pooled together and invested in a variety of assets like stocks, bonds, and other securities. When you invest in a mutual fund, you are essentially buying a small share of a large, diversified portfolio (a collection of different investments). This diversification spreads your investment across different types of assets, reducing the risk compared to investing in a single stock or bond.

Risk vs. Return: Mutual funds offer a range of options with varying levels of risk and return. Generally, investments that have the potential for higher returns also come with higher risks. For instance, low-risk mutual funds might invest in safer assets like government bonds, while higher-risk funds might invest in stocks with greater growth potential. Investors can choose mutual funds based on their risk tolerance and return expectations.

How Mutual Funds Work

Mutual funds are managed by **professional fund managers** who make decisions about where to invest the pooled money. These managers aim to achieve specific financial objectives, such as capital growth or income generation. The expertise of these managers allows individual investors to benefit from professional management, making mutual funds a convenient and potentially profitable investment vehicle.

Regulated by the Securities and Exchange Board of India (SEBI), mutual funds operate under strict guidelines to protect investor interests and ensure transparency in operations. They provide a relatively lower-risk entry point for new investors looking to participate in financial markets.

Importance and Benefits of Investing in Mutual Funds

- 1. Professional Management:** Mutual funds are managed by experienced fund managers who make informed investment decisions based on thorough research and market analysis.

2. **Diversification:** By pooling money from many investors, mutual funds spread investments across various securities, reducing the risk associated with individual stocks or bonds.
3. **Accessibility:** Mutual funds offer easy access to diversified investment portfolios, allowing investors to participate in the financial markets with even modest amounts of money.
4. **Liquidity:** Investors in mutual funds can easily buy or sell their units, providing liquidity and flexibility to access funds as needed, unlike other investments that may be less liquid.
5. **Convenience:** Investing in mutual funds is straightforward and offers a range of options tailored to different financial goals and risk appetites, making it convenient for investors to achieve their investment objectives.
6. **Regulation:** Mutual funds are regulated by SEBI (The Securities and Exchange Board of India), ensuring strict guidelines and protecting investor interests.

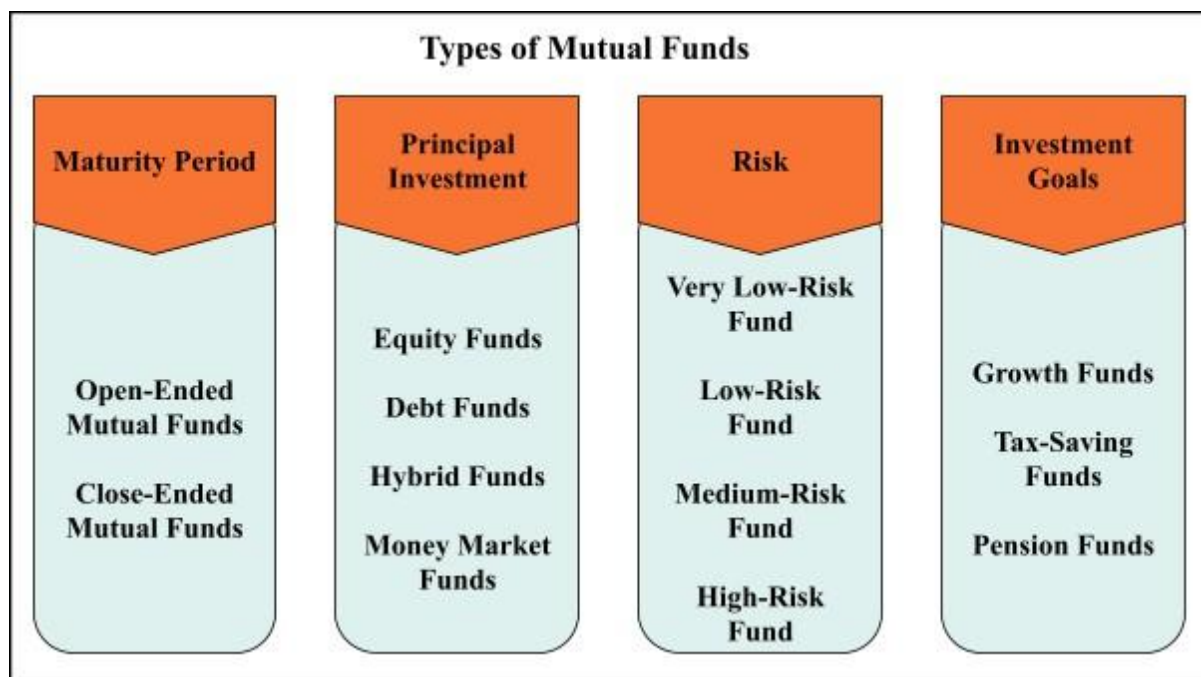


Discuss

Why do you think mutual funds are a popular choice for many investors?

3.2.1 Types of Mutual Funds

Now that we understand what mutual funds are and the benefits they offer, let's explore the different types of mutual funds available. This will help you understand how mutual funds can be tailored to meet various investment goals, risk levels, and time horizons.



Mutual Funds Based on Maturity Period:

Open-Ended Mutual Funds - Open-ended mutual funds allow investors to buy or sell units at any time, providing flexibility and liquidity. These funds do not have a fixed maturity date, enabling investors to stay invested according to their financial needs and market conditions.

Example: Investor Harpreet invests in an open-ended mutual fund for flexibility and potential growth. He appreciates the ease of buying and selling units as per his financial needs.

Close-Ended Mutual Funds- Close-ended mutual funds have fixed maturity dates and are traded on stock exchanges. Investors commit their funds for a specific period and cannot redeem their investment before the maturity date.

Example: Rajbir diversifies his portfolio with a close-ended mutual fund for potential higher returns. He understands that the fixed maturity date provides a structured investment approach.

Mutual Funds Based on Principal Investment:

Equity Funds- Equity funds primarily invest in stocks, offering the potential for high returns over a long term. These funds are suitable for investors seeking capital appreciation.

Example: Simran chooses an equity fund for long-term growth potential. She understands the risks involved but believes in the growth prospects of the companies in the fund's portfolio.

Debt Funds - Debt funds invest primarily in fixed-income securities like bonds, providing stable income and lower risk compared to equity funds. These funds are suitable for investors seeking regular income with capital preservation.

Example: Aman opts for a debt fund for stable income and lower risk. He prefers the predictable returns offered by bonds and values the safety of his investment principal.

Hybrid Funds - Hybrid funds invest in a mix of stocks and bonds, offering balanced growth and income. These funds are suitable for investors seeking diversification and moderate risk.

Example: Ritu selects a hybrid fund for balanced growth and income. She appreciates the combination of growth potential from stocks and stability from bonds in the fund's portfolio.

Money Market Funds - Money market funds invest in short-term, low-risk securities like Treasury bills and commercial paper. These funds provide liquidity and safety, making them suitable for investors with short-term cash needs.

Example: Anil invests in a money market fund for liquidity and safety. He values the stability of his investment and the ability to access funds quickly when needed.

Mutual Funds Based on Risk:

Very Low-Risk Fund - Very low-risk funds focus on preserving capital with minimal risk. These funds invest in low-risk securities like government bonds and offer stable returns with minimal volatility.

Example: Meena chooses a very low-risk fund for short-term savings. She prioritises the safety of her investment principal and values the stability of returns offered by government bonds.

Low-Risk Fund - Low-risk funds aim for steady income with low volatility. These funds invest in a mix of fixed-income securities like bonds issued by governments or corporations and offer stable returns with moderate risk.

Example: Rohan invests in a low-risk fund for retirement savings. He appreciates the consistent returns offered by the fund and the lower volatility compared to equity funds.

Medium-Risk Fund - Medium-risk funds seek moderate growth with balanced risk. These funds invest in a diversified portfolio of stocks and bonds, offering potential for growth with controlled volatility.

Example: Karan selects a medium-risk fund for long-term financial goals. He understands the trade-off between risk and return and believes in the balanced approach offered by the fund.

High-Risk Fund - High-risk funds pursue aggressive growth with higher volatility. These funds invest in high-risk assets like small-cap stocks and offer the potential for high returns over the long term.

Example: Neha invests in a high-risk fund for potential high returns over time. She is willing to accept higher volatility in exchange for the possibility of significant capital appreciation.

Mutual Funds Based on Investment Goals:

Growth Funds - Growth funds aim for capital appreciation over the long term by investing

in high-growth companies. These funds are suitable for investors seeking long-term wealth accumulation.

Example: Priya chooses a growth fund for wealth accumulation. She believes in the growth potential of the companies in the fund's portfolio and aims to achieve her long-term financial goals.

Tax-Saving Funds - Tax-saving funds offer tax benefits under specific investment schemes like Equity Linked Savings Schemes (ELSS). These funds invest primarily in equities and have a lock-in period of three years.

Example: Arjun invests in a tax-saving fund for tax planning purposes. He appreciates the tax benefits offered by ELSS and aims to save taxes while achieving his investment goals.

Pension Funds - Pension funds are designed to provide income during retirement and invest in a mix of equities and debt instruments. These funds offer long-term wealth accumulation and retirement security.

Example: Shreya contributes to a pension fund for retirement security. She values the disciplined approach to retirement planning offered by the fund and aims to build a substantial retirement corpus.



Knowledge Check

1. **TRUE or FALSE:** Investors who have invested in an open-ended mutual fund cannot subscribe or redeem units at any time.
2. **Close-ended mutual funds have:**
 - a. A specified tenure
 - b. Premature redemption options
 - c. No stock exchange listing
3. **TRUE or FALSE:** Debt funds primarily invest in fixed-income securities such as bonds.
4. **Which type of fund invests in a mix of stocks and bonds?**
 - a. Debt fund
 - b. Equity fund
 - c. Hybrid fund
5. **Which type of fund is suitable for investors planning for retirement?**
 - a. Tax-saving fund
 - b. Pension fund
 - c. Growth fund

Answers: 1. False, 2. a. A specified tenure, 3. True, 4. c. Hybrid funds, 5. b. Pension fund



Activity 3: Mutual Fund Poster Creation

Objective: To create a poster showcasing different types of mutual funds with descriptions and examples.

Materials Needed: Access to computers or devices with internet connection, research materials (websites, articles, etc.), poster board, markers, glue or tape.

Instructions:

- Divide students into groups.
- Instruct students to create a poster that displays each type of mutual fund along with its description and example.
- Encourage students to be creative with their posters by using colours, illustrations, and other visual elements to make them visually appealing.
- Once the posters are complete, have each group present their poster to the class.
- Organise a gallery walk for students to observe and discuss each poster.
- Encourage students to walk around and observe each poster, noting the different types of mutual funds and their respective examples.

3.2.2 How to Invest in Mutual Funds

Mutual funds are a great option for investors who want to increase their wealth but lack the capital or the time to do extensive market research. Expert fund managers invest the money received in mutual funds in accordance with the program's declared goal. A tiny fee is collected from the investment by the fund house in exchange.

Interested in investing in mutual funds? Here's a practical guide:

1. **Understand Mutual Funds:** Mutual funds pool money from investors to invest in various assets like stocks and bonds. Fund managers make investment decisions based on the fund's objectives.
2. **Type of Mutual Funds:** Choose from different types such as Open-Ended, Close-Ended, Equity Funds, Debt Funds, Hybrid Funds, etc.
3. **Choose a Mutual Fund:** Consider your investment objectives, risk tolerance, and time horizon. Examine the track record, fund management experience, and expense ratio of several funds. Choose a fund that aligns with your financial goals and risk tolerance.
4. **Open an Account:** Create an account through a registered intermediary such as a financial advisor or mutual fund distributor, or directly with a fund house like HDFC Mutual Fund, ICICI Prudential Mutual Fund, or Nippon India Mutual Fund. Accounts can also be opened through banks that offer mutual fund services, such as State Bank of India (SBI). Complete necessary documentation including KYC (Know Your



Customer) forms.

5. **Investment Options:** Invest a lump sum amount or set up a Systematic Investment Plan (SIP). It is a method of investing in mutual funds where you regularly invest a fixed amount of money, usually on a monthly or quarterly basis. This approach helps in building wealth over time through consistent investments.
6. **Make the Investment:** Transfer funds to the mutual fund account for lump sum investments. Set up automatic transfers for SIP investments.
7. **Monitor and Review:** Keep track of your investment's performance and review your portfolio regularly. Make adjustments as needed to stay aligned with your goals.
8. **Redeem or Switch Funds:** Partially or fully redeem investments if needed. Switch between funds within the same fund house to adapt to changing goals.
9. **Tax and Fees:** Understand the tax implications of redemption. Short-term capital gains tax applies if redeemed before one year, while long-term capital gains tax applies if redeemed after one year. For a comprehensive understanding, it is advisable to consult an intermediary, conduct personal research on tax regulations, and seek detailed guidance from a tax professional or financial planner.
10. **Stay Informed:** Stay updated on market and economic trends that may impact your investments. Consider seeking guidance from financial advisors for personalised advice.

Following these steps will empower you to invest in mutual funds confidently and effectively, helping you achieve your financial goals over time.

4.0 Meaning of Bonds and Stocks

4.1 What is a Bond?

A bond is a fixed-income security in which the investor lends money to the borrower – usually a government agency or a company – in return for periodic interest payments over a specified period of time.

Imagine you lend ₹1,00,000 to the Indian government. In return, they promise to pay you a 7% interest every year and return the full ₹1,00,000 after 10 years.

Example

Let's imagine a bond as a special kind of “promise note” that a company or a government gives to a bank that wants to lend out some money. Here's how it works:

The Promise: A company or government needs money to do big things like building roads or schools. So, they ask banks if they can borrow their money. In return, they give these banks a “promise note” called a **bond**.



The Deal: The bond says, “We promise to pay you back your money after a certain number

of years, and we'll also give you a little extra money every year for lending it to us." This extra money is like a thank you gift, and it's called **interest**.

The Wait: The bank lends the money (**the bondholder**), keeps the bond and waits. Every year, they get the extra money (interest) as promised. It's like getting a reward every year until the bond reaches its end date called the maturity date.

The Payback: When the time is up (**the maturity date**), the company or government says, "Thank you for lending us your money!" and gives back all the money that was originally lent. The bondholder has made some extra money from the interest, and the company or government was able to do its big projects.

So, a bond is like a long-term loan where the bank lending the money gets a little reward every year, and then gets all their money back at the end. It's a way for banks to help out and make some extra money at the same time!

Example

Imagine Bank ABC has ₹10,00,000 that it wants to save and grow over time. The bank decides to lend this money to the government by buying a bond. Here's what happens:

1. **Issuance:** The government issues a bond with a **face value** of ₹10,00,000. This is the amount Bank ABC will get back when the bond matures. The bond also has a **coupon rate** of 5%, which is like the interest rate the government agrees to pay Bank ABC for borrowing its money.
2. **Purchase:** Bank ABC buys this bond, either directly from the government or from someone else who already owns it.
3. **Interest Payments:** Every six months, the government pays the Bank ABC interest based on the coupon rate. So, the bank gets ₹25,000 every six months (because 5% of ₹10,00,000 is ₹50,000 per year, and half of that is ₹25,000).
4. **Maturity:** The bond has a maturity date, which is when the bond "grows up." Let's say it's in 10 years. At that time, the government will return the ₹10,00,000 face value to the Bank.
5. **Redemption:** On the maturity date, the bank gets back its ₹10,00,000. If the bond was callable (redeemable early), the government could have chosen to pay back the money earlier, but in this case, they waited until the 10-year period was over.

So, in essence, a bond is like a formal agreement where Bank ABC lends money to the government, gets regular interest payments as a reward, and then gets its original amount back after a certain period.



Knowledge Check

1. **What is the coupon rate of a bond?**
 - a. The annual interest rate paid by the issuer
 - b. The current market price of the bond
 - c. The face value of the bond
2. **What is the face value of a bond?**
 - a. The value of the bond when it is issued
 - b. The value of the bond at maturity
 - c. The value of the bond in the secondary market
3. **What does the tenure of a bond refer to?**
 - a. The date the bond was issued
 - b. The date the bond matures
 - c. The date the bond pays its first interest payment

Answers: 1. a. The annual interest rate paid by the issuer, 2. a. The value of the bond when it is issued, 3. b. The date the bond matures



Activity 4: Savings Adventure

Objective: To understand bonds through a quick role-play.

Materials Needed: Play money, Bond certificates (paper slips)

Setup:

- You may divide the class into two groups: one group will be the “Government” and the other group will be “Investors.”
- Give the “Government” group bond certificates that they can sell. Each certificate should have a face value of ₹100, a coupon rate of 5%, and a maturity of 4 rounds (representing 4 years).
- Give each “Investor” play money worth ₹100 to buy bonds.

Instructions:

- Round 1 - Issuance & Purchase: Investors decide whether to buy a bond from the Government. If they buy it, they give the Government their ₹100 in exchange for a bond certificate.
- Round 2 - First Interest Payment: The Government pays each Investor ₹5 as interest (5% of ₹100).
- Round 3 - Second Interest Payment: Repeat the interest payment from Round 2.
- Round 4 - Maturity & Redemption: The Government returns the face value (₹100) to each Investor, along with the final interest payment.

Discussion:

- How did it feel to be an Investor receiving money back?
- What did the Government do with the money during the 4 rounds?

4.2 Stocks

Stocks, also known as equities, represent ownership in a company. When a company needs money to operate or grow, it sells stocks to investors. Each unit of stock is called a **share**, giving the **shareholder** a right to a portion of the company's profits and assets.

Key Terms:

- **Stock:** A type of security that signifies ownership in a corporation.

Example: XYZ Tech Ltd. issues stock to raise capital. Owning 100 shares of XYZ Tech Ltd. means having a partial ownership share in the company.

- **Shares:** Units of stock that give the right to share in the company's profits.

Example: If XYZ Tech Ltd. has issued 1 lakh shares and an investor owns 100 of them, the investor holds 0.1% of the company's total shares.

Note: A stock signifies ownership in a company, and shares are individual units of that stock. The term "stock" refers to the overall ownership, while "shares" refer to the specific portions of that ownership.

- **Stock Exchange:** A marketplace where stocks are bought and sold (e.g., NSE, BSE in India).

Example: XYZ Tech Ltd.'s stock is bought and sold on the Bombay Stock Exchange (BSE).

- **IPO (Initial Public Offering):** The first sale of stock by a company to the public.

Example: XYZ Tech Ltd. conducted an IPO last year, allowing investors to purchase stock for the first time.

- **Market Capitalization:** The total value of a company's outstanding shares (share price multiplied by number of shares).

Example: With 10 million shares outstanding and a share price of ₹50, XYZ Tech Ltd.'s market capitalization is ₹50 crore.

- **Dividends:** Portions of a company's profit paid to shareholders.

Example: XYZ Tech Ltd. pays a ₹5 dividend per share. For an investor owning 100 shares, the dividend received would be ₹500.

- **Share Price:** The price at which a single share trades on the stock exchange.

Example: The current share price of XYZ Tech Ltd.'s stock is ₹50 on the BSE.

- **Trading:** The act of buying and selling stocks.

Example: Purchasing 50 shares of XYZ Tech Ltd. at ₹50 each and later selling them at ₹60 each illustrates trading activities.

- **Return:** Profit from stock investment, including capital appreciation and dividends.

Example: Buying XYZ Tech Ltd.'s stock at ₹40 per share and selling it at ₹50 per share, with a ₹5 dividend per share, results in a total return of ₹15 per share.

- **Risks:** Potential loss if the company underperforms or the market declines.

Example: If XYZ Tech Ltd. faces financial difficulties and the stock price drops to ₹30, a loss may be incurred on the investment.

4.2.1 How Stocks Work

- **Research:** Investigate companies and market trends to make informed decisions.
- **IPO Subscription:** Buy shares in a company's IPO by filling out an application and paying the required fee.
- **Allotment:** Shares are distributed to IPO applicants based on demand and availability.
- **Trading:** Buy and sell shares on the stock exchange through brokers or online platforms.
- **Monitoring:** Regularly check on your investments, staying updated on relevant news and trends.

Example

Gurpreet, a young investor, decides to invest in a company going public through an IPO. Here's what she does:

- **Research:** Gurpreet examines the company's financials and future prospects.
- **IPO Subscription:** She subscribes to the IPO by completing the necessary forms and payments.
- **Allotment:** If shares are allotted, she becomes a shareholder.
- **Trading:** Once listed, she can trade the shares on the stock exchange.
- **Monitoring:** Gurpreet keeps track of his investment and market conditions.

Gurpreet understands the risks and benefits of stock investing and plans to diversify her portfolio to manage risks effectively.



Knowledge Check

Let us first recap the knowledge we have gained so far.

1. **Choose the correct answer: What are stocks?**
 - a. Fixed-income securities
 - b. Ownership shares in a company
 - c. Bonds issued by the government
2. **TRUE or FALSE: Investing in stocks guarantees a fixed return.**
3. **What is the full form of IPO?**

Answers:

1. b. Ownership shares in a company
2. False
3. Initial Public Offering

**Activity 5: Role Play**

Instructions: Divide the class into ‘Companies’ and ‘Investors.’ Let the ‘Companies’ explain why their business is good, and the ‘Investors’ decide which company to invest in with play money.

Discussion: Talk about what makes a company worth investing in and the risks involved.

Let's Recap

1. **Loans:** Borrowing money for specific purposes like education, home purchase, or personal needs, repaid over time with interest.
2. **Mortgages:** Loans specifically for purchasing real estate, secured by the property itself, with repayment typically spanning years.
3. **Overdraft Facilities:** Short-term credit allowing account holders to withdraw more money than available funds, useful for managing cash flow and unexpected expenses.
4. **Credit Cards:** Revolving credit lines that enable purchases up to a set credit limit, with the flexibility to repay in full or over time, accompanied by interest and potential fees.
5. **Mutual Funds:** Pooled funds from investors used to invest in diversified portfolios of stocks, bonds, or other assets, managed by professionals to achieve specific financial goals.
6. **Bonds:** Debt instruments where investors lend money to governments or corporations in exchange for periodic interest payments and repayment of principal at maturity.
7. **Stocks:** Ownership shares in a company, providing potential for capital appreciation and dividends based on company performance.

EXERCISE

Objective Type Questions**State True or False:**

1. An amortization table helps calculate loan payments.
2. Personal loans are secured loans.
3. An unsecured loan requires some kind of collateral.
4. The full form of EMI is "Equated Monthly Installment".
5. There are three types of overdraft facilities.
6. A credit card has an 11-digit number.
7. The Stock Exchange is a marketplace where stocks are bought and sold.

Short Answer Type Questions

8. Explain the various types of loans.
9. What is the difference between a secured loan and an unsecured loan?
10. Write the names of documents required for a loan.
11. Explain the benefits of investing in mutual funds.
12. How many types of mortgage are there? Explain each type of mortgage.

Long Answer Type Questions

13. What is a credit card? Explain its features and components.
14. What are the types of mutual funds? Explain.

ANSWER KEY

Objective Type Questions**State True or False:**

- | | |
|----------|----------|
| 1. True | 4. True |
| 2. False | 5. False |
| 3. False | 6. False |
| | 7. True |

UNIT 03

Using Payment Instruments



Topics

- Applying for a Cheque Book
 - What are Cheques?
 - How to Obtain a Cheque Book?
 - Channels to Request a Cheque Book
- Using Cheques: Writing, Depositing, and Clearing
 - Writing a Cheque
 - Steps on How to Write a Cheque
 - Key Elements Printed on a Cheque
 - Understanding Cheque Transactions
 - Difference Between 'Crossed' and 'Bearer' Cheques
 - Depositing a Cheque
 - Steps Involved in Depositing a Cheque
 - Cheque Clearing Process
 - Steps Involved in Clearing a Cheque
 - Bounced Cheque
 - Consequences of Issuing a Bounced Cheque
 - Understanding Stop Payment Requests for Cheques in India
 - How to Request a Stop Payment
 - Placing a Stop Payment Request
 - What Happens After the Request?
- Applying for Electronic Fund Transfers (EFT)
 - Understanding UPI
 - What is UPI
 - Key Features of UPI
 - Understanding EFT
 - Processing of EFT Transactions

- Security Measures in EFT
 - Types of EFT Systems
 - Application Process
 - Preferred EFT Methods
- Differences Between UPI and EFT
- Using EFT like RTGS and NEFT for Transfers and Payments
 - Introduction to RTGS
 - Explanation
 - Features and Benefits of RTGS
 - How Real-Time Gross Settlement Transactions Work
 - Different Modes for Initiating RTGS Transactions in India
 - Information Required to Begin an RTGS Transaction
 - How to Make an RTGS Transfer
 - Online RTGS Transfer Process
 - Offline RTGS Transfer Process
 - Introduction to NEFT
 - Features and Benefits of NEFT
 - How NEFT Transactions Work
 - Different Modes for Initiating NEFT Transactions in India
 - Information Required to Begin an NEFT Transaction
 - How to Make an NEFT Transfer
 - Online NEFT Transfer Process
 - Offline NEFT Transfer Process
 - Transaction Limit to Transfer Money through NEFT
 - Comparison between NEFT and RTGS
 - Understanding Demand Drafts
 - What is a Demand Draft
 - How Demand Drafts Work
 - What is a Pay Order
 - Online Banking
 - Debit and Credit Cards



Learning Objectives

- Learn how to apply for a cheque book with a bank
- Demonstrate the ability to accurately write and deposit a cheque
- Understand the process of applying for electronic fund transfer (EFT) services
- Demonstrate proficiency in initiating EFT transactions securely.
- Differentiate between cheques and electronic fund transfers (EFT).
- Identify the advantages and limitations of each payment method



Materials Required

- Sample Debit Cards
- Sample Cancelled Cheque Books or Cheques
- Pamphlet on Online Banking (from a local bank)
- Pamphlet on Safety while using Online Banking or Digital Payment Services (from a local bank)
- Computer/Mobile Phone with good internet connection and banking applications, and a Projector



Activity 1: Before We Begin!

1. Imagine you have just opened your first bank account. What is the first banking service you would like to use, and why?

1.0 Applying for a Cheque Book

1.1 What are Cheques?

A **cheque** is a written order that instructs a bank to pay a specific amount of money from one person's account to another person or organisation or to withdraw cash from their own account (also known as a Self cheque). Cheques provide a secure and convenient method of transferring funds without the need for physical currency. When customers use cheques, they can make payments for various transactions, such as paying bills, making purchases, and transferring money between accounts. A collection of cheques bound together in a booklet form is known as a **cheque book**, which enables account holders to make payments easily and efficiently from their bank accounts.



1.2 How to Obtain a Cheque Book

To assist customers in obtaining a cheque book, it is important to guide them through the process, step-by-step. There are multiple channels available for requesting a cheque book, offering flexibility and convenience.

1.2.1 Channels to Request a Cheque Book:

- **In-Person Request at a Bank Branch:**
 1. Visit the bank branch: Customers can visit their local bank branch.
 2. Fill out a request form: They need to complete a cheque book request form by providing their account number, contact details, and the number of cheque leaves needed.
- **Online Banking Platform:**
 1. Log in to online banking: Customers log in to their bank's online banking platform.
 2. Navigate to the services section: They find the option to request a cheque book.

3. Submit request electronically: They fill in the necessary details and submit the request online.
- **SMS or Phone Call:**
 1. Contact customer service: Some banks offer the option to request a cheque book via SMS or a phone call to their customer service helpline.
 2. Follow instructions: Customers follow the bank's instructions to initiate the request process through their preferred channel.

Example: Online Request

Imagine you have recently opened a savings account with Punjab National Bank. To facilitate your transactions, you decide to request a cheque book through the bank's online banking platform. After logging in to your account, you navigate to the "Services" section and locate the option to request a cheque book. You fill out the required details, such as the number of cheque leaves needed, and submit your request.

The first screenshot shows the 'Home' screen of the Punjab National Bank mobile app. The 'Services' icon is highlighted with a red box. The second screenshot shows the 'Services' menu with the 'Cheques' option highlighted with a red box. The third screenshot shows the 'Cheque Book' request form with the 'Number of cheque leaves' field set to '100' and the 'Request for Cheque Book' button highlighted with a red box.

Example: In-Person Request



Imagine you have opened a new savings account with Punjab National Bank. To facilitate your transactions, you visit the nearest branch and approach the customer service desk to request a cheque book.

Customer Interaction:

Gurpreet: Sat Sri Akaal! I recently opened a savings account with Punjab National Bank.

Jaspreet: Sat Sri Akaal, Gurpreet! How can I assist you today?

Gurpreet: I would like to apply for a cheque book to make transactions easier. Can you help me with that, Jaspreet?

Jaspreet: Of course, Gurpreet! We can certainly arrange that for you. Could you please fill out this cheque book request form?

Gurpreet: Changa, no problem.

Jaspreet: Once you have filled out the form, please provide me with your account details, and we will process your request right away.

Gurpreet: Here you go. I have filled out the form and here are my account details.

Jaspreet: Thank you, Gurpreet. Your cheque book request has been successfully submitted. You can expect to receive your cheque book within the next 4 working days, delivered to your registered address by registered post.

Gurpreet: That's great. Thank you for your assistance, Jaspreet!



Activity 2: Requesting a Cheque Book via Phone Call

Objective: To simulate a phone call to the bank's customer service helpline to verbally request a cheque book, demonstrating effective communication skills and understanding of the process.

Instructions:

1. Divide the class into pairs, with one student playing the role of the customer and the other playing the role of the bank representative.
2. Provide each pair with the following scenario and guidelines for the role play:
 - **Scenario:** You are a customer who recently opened a savings account with Punjab National Bank and now wishes to request a cheque book via a phone call to the bank's customer service helpline.
 - **Guidelines for the Customer:** Introduce yourself politely and provide your account details if prompted. Clearly state your request for a cheque book. Provide any additional information required by the bank representative. Thank the representative for their assistance before ending the call.
 - **Guidelines for the Bank Representative:** Greet the customer warmly and ask for their account details to verify their identity. Listen attentively to the

customer's request and confirm the details. Inform the customer about the processing time for the cheque book request and any other relevant information. Thank the customer for choosing the bank's services before ending the call.

3. Allow each pair a few minutes to prepare their roles and dialogues.
4. Conduct the role plays, encouraging students to speak clearly and confidently.
5. Provide feedback and discuss any areas for improvement in communication or understanding of the process after each role-play.



Why do we need cheque books? (Points for consideration - Convenience, Record Keeping, Security, Flexibility, Accessibility, Legal Validity).

2.0 Using Cheques: Writing, Depositing, and Clearing

Now that you have your cheque book, let's learn how to use it effectively for making payments and deposits:

2.1 Writing a Cheque

A cheque typically contains fields for the date, payee's name, amount in figures and words, and your signature.

(Image reference: <https://www.bankbazaar.com/ifsc/know-your-cheque.html>)

The image shows a sample cheque form from bankbazaar.com. It includes fields for the payee's name, date, amount in words and figures, account number, and a signature line. Labels with arrows point to these fields: 'Write The Name Of The Payee' points to the 'PAY' field; 'Write The Amount In Words' points to the 'रुपये RUPEES' field; 'Account Number' points to the 'Acc No.' field; 'Write The Date' points to the date box; 'Write The Amount' points to the 'अदा करें ₹' field; and 'Signature' points to the 'Please sign above' line.

2.1.1 5 steps on how to write a Cheque

1. **Date:** Properly date the cheque to avoid misuse. An undated cheque can be filled in by anyone, leading to potential misuse. Ensure the date is accurate to prevent dishonour due to incorrect or outdated information.
2. **Payee:** On the "pay" line of the cheque, clearly write the name of the individual or organisation who will receive the funds.
3. **Cross the cheque:** To ensure that the funds are only withdrawn by the intended recipient, draw two parallel lines in the top left corner of the cheque and write "Account Payee".
4. **Account Information:** Ensure that your cheque includes your account number and the bank's address. Nowadays, it is mandatory for each cheque leaf to bear your name, especially in the case of a joint account.
5. **Signature:** Carefully sign the cheque, ensuring that your signature matches the one provided to the bank during the account opening process.



Dishonor

Dishonour occurs when a bank refuses to honour a cheque due to issues like insufficient funds or incorrect details.

2.1.2 Key Elements Printed on a Cheque

1. **Cheque Number:** Each cheque in a cheque book has a unique identification number printed on it. This number helps in tracking and recording cheque transactions.
2. **Bank's Logo:** The logo of the bank where the account is held is usually printed on the cheque for branding and identification purposes.
3. **MICR Line:** The Magnetic Ink Character Recognition (MICR) line contains important information encoded in magnetic ink, including the cheque number, bank code, and account number. This information is used for the automated processing of cheques.
4. **RBI A/C No. (Reserve Bank of India Account Number):** This refers to the account number held by the RBI, the central banking institution of India. It may appear on certain types of cheques issued by the RBI or other government agencies for specific purposes, such as tax refunds or government payments.
5. **Transaction Code:** This is a unique identifier assigned to a specific transaction. It may appear on the cheque for internal tracking or reference purposes, providing additional information about the nature or purpose of the payment. Transaction codes help banks and account holders identify and reconcile individual transactions more efficiently.

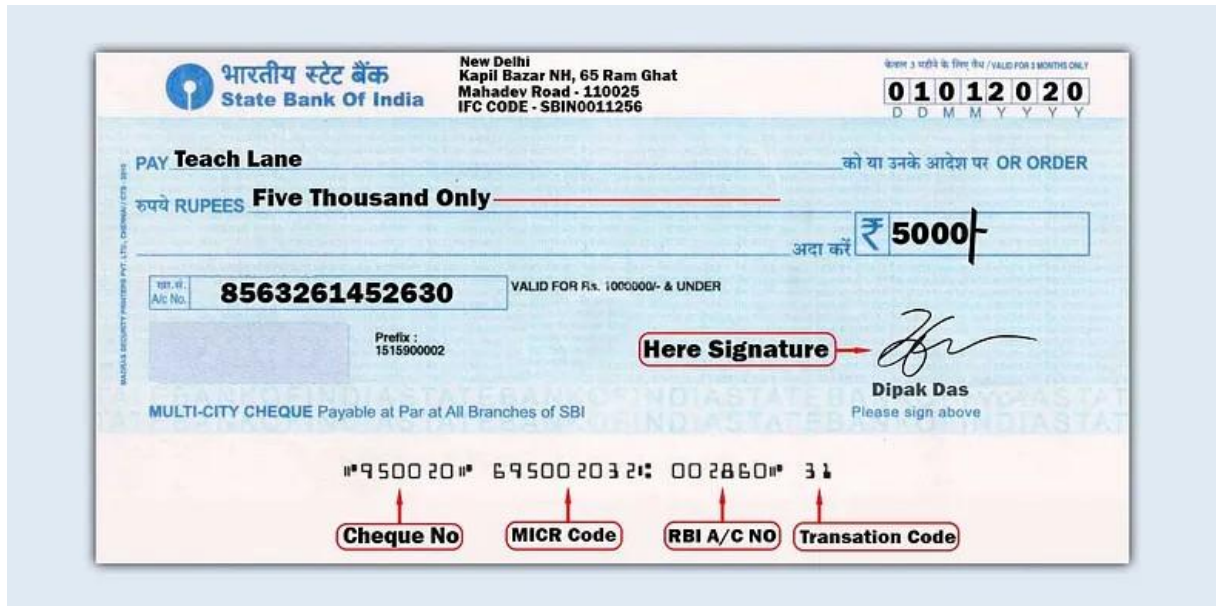


Image Source: <https://techykhushi.medium.com/10-essential-elements-characteristics-of-cheque-25936b7f948a>



Why do you think it is important for individuals to understand how to write a cheque properly?

2.1.3 Understanding Cheque Transactions

Parties Involved:

Drawer	Drawee	Payee
The person who owns the bank account and writes/signs the cheque.	The bank that holds the account of the drawer and is directed to pay the specified amount mentioned on the cheque.	The person to whom the payment will be made.

2.1.4 Difference Between 'Crossed' and 'Bearer' Cheques

Crossed Cheque ('A/C Payee')	Bearer Cheque
It has two parallel lines drawn across its face.	Does not have parallel lines drawn across its face.
Intended for deposit into a bank account.	Can be cashed by anyone presenting it to the bank.
Payment is made only to the person named on the cheque or their bank account.	Payment can be received in cash.
Use when you want the payment to be securely deposited into your bank account.	Use when you want to receive cash directly without depositing into a bank account.
Recommended for transactions involving larger amounts or payments to specific individuals.	Suitable for smaller transactions or when immediate cash is needed.

HDFC BANK → These two black marked lines makes your cheque "CROSSED CHEQUE"

दिनांक Date: 10/10/2019 Valid for 3 months Only

Pay Basavaraj Tonagatti Or Bearer

Rupees रुपये Fifty Thousand Only या धारक को

₹ 50,000/- अदा करें

A/c No. XXXXXXXXXXXXXX SB AC For XXXXXXXXXXXXXXXXXXXXXXXXXXXX

Payable at par through clearing/transfer at all branches of HDFC BANK LTD

Authorised Signatory
Please sign above / कृपया यहाँ हस्ताक्षर करें

Note: The following process applies only if the cheque is crossed (A/C payee). If it is a bearer cheque (not A/C payee), then it does not need to be deposited. It can be just encashed.

2.2 Depositing a Cheque

Depositing a cheque is a straightforward process that allows you to add funds to your bank account. Whether you receive a cheque from a friend, client, or employer, depositing it ensures that the funds are safely credited to your account for future use. *However, if the cheque is a bearer cheque, it can be encashed instead of being deposited.*

2.2.1 Steps involved in depositing a cheque

1. **Endorsement:** Before depositing the cheque, endorse it on the back by signing your name on the designated endorsement line. This confirms that you authorise the bank to credit the funds to your account.

2. **Visit the Bank:** Take the endorsed cheque to your bank branch or a nearby ATM equipped with deposit functionality. Alternatively, you may use your bank's mobile app for digital cheque deposits.

The image shows a Union Bank of India deposit slip form. It includes fields for the bank name, branch, date, and transaction type (Current, Saving, Cumulative, or Cash Credit A/C No.). There are sections for the depositor's name and address, and a table for recording cash notes and coins. The form also has a section for the teller's signature and a 'Total' field.

3. **Deposit Slip:** If depositing at a bank branch, fill out a deposit slip. Include information such as your account number, the amount being deposited, and the cheque number. Double-check the accuracy of the information before submitting the deposit slip along with the endorsed cheque.
4. **Deposit the Cheque:** Hand the endorsed cheque and deposit slip to the bank teller or insert the cheque into the designated slot if using an ATM. For mobile banking, follow the app's prompts to capture images of the front and back of the cheque and submit the deposit electronically.
5. **Confirmation:** After depositing the cheque, you will receive a receipt or confirmation of the transaction. Keep this receipt for your records as proof of the deposit.



The image shows an SBI deposit slip form. It includes fields for the branch, date, and transaction type (Deposit or Pay in Slip). There are sections for the depositor's name and address, and a table for recording cash notes and coins. The form also has a section for the teller's signature and a 'Total' field.

2.3 Cheque Clearing Process

Once you have written and deposited a cheque, the next step is the clearing process, which involves verifying and transferring funds between banks to fulfil the cheque's payment.

2.3.1 Steps involved in clearing a cheque

1. **Presenting the Cheque:** After you deposit a cheque into your bank account, your bank presents it to the clearing-house for processing. The clearinghouse acts as an intermediary between banks, facilitating the exchange of cheques and settlement of funds.
2. **Verification:** The clearing-house verifies the details of the cheque, including the account numbers, signatures, and amount. This verification ensures that the cheque is

- genuine and that there are sufficient funds in the issuer's account to cover the payment.
3. **Clearing Process:** Once the cheque is verified, the clearing-house initiates the clearing process, which involves transferring funds from the issuer's bank to the recipient's bank. This transfer typically takes a few days to complete, depending on the banks involved and the type of cheque.
 4. **Settlement:** After the funds are transferred between banks, they are settled, and the recipient's account is credited with the cheque amount. The clearing-house reconciles the transactions and ensures that the funds are properly allocated to the respective accounts.
 5. **Notification:** Once the cheque has been cleared and the funds are available in your account, you will receive notification from your bank confirming the transaction. You can then access the funds and use them for your financial needs.
 6. **Handling Invalid or Insufficient Funds:** If the cheque is invalid or there are insufficient funds in the issuer's account, the paying bank returns the cheque to the depositing bank with a reason for non-payment. The depositing bank then informs the account holder about the dishonoured cheque, and the funds are not credited to the recipient's account.

Example

- **Writing:** Suppose you need to pay your school fees. You write a cheque payable to your school, mentioning the amount and date.
- **Clearing:** The school deposits the cheque into its bank account. The bank verifies the details and processes the cheque for clearance.
- **Depositing:** The school receives the funds in its account after the cheque is successfully cleared, allowing you to fulfil your school fees payment.



2.4 Bounced Cheque

A bounced cheque occurs when the bank cannot process and honour the payment due to reasons such as insufficient funds, errors in the cheque details, post-dated cheques, or closed accounts. This results in the cheque being returned unpaid to the recipient's bank, causing inconvenience and potential financial penalties for both the issuer and the recipient.

2.4.1 Consequences of Issuing a Bounced Cheque

Issuing a bounced cheque is a serious matter and can result in criminal prosecution under Indian law. The severity of the consequences depends on the reason for the bounce and the applicable legal provisions.

1. **Legal Implications:** If a cheque bounces due to insufficient funds in the payer's account, it is considered a criminal offence under the Negotiable Instruments Act of 1881 in India. The payer (drawer) may face prosecution for issuing a cheque against

an account with insufficient funds. Legal penalties may include fines and imprisonment for up to two years.

2. **Legal Recourse and Resolution:** The payee (recipient) of the bounced cheque has the option to pursue legal action against the payer or allow the payer to reissue a cheque within a specified period. Legal recourse may involve filing a complaint with the appropriate authorities and pursuing legal proceedings.
3. **Bank Penalties:** In addition to legal consequences, banks typically impose penalties for bounced cheques. The penalty charges vary among banks and may depend on factors such as the amount of the cheque and the frequency of bounced cheques.

2.5 Understanding Stop Payment Requests for Cheques in India

A stop payment request is submitted to your bank when you want to cancel a cheque you have issued but that has not yet been cashed or deposited. This can be a crucial tool if you have made a mistake, need to cancel a payment, or have other reasons for stopping the cheque.

2.5.1. How to request a stop payment

Requesting a stop payment usually involves a fee, which varies from bank to bank in India. For example, banks like State Bank of India (SBI), HDFC, ICICI, and others might charge different amounts for this service.

2.5.2 To place a stop payment request, you can:

- Visit your bank branch in person.
- Call your bank's customer service number and speak directly with a representative.
- Use your bank's online banking platform or mobile app, if the service is available there.

You will need to provide specific details about the cheque, including the cheque number, the date on the cheque, the amount, and the payee's name.

2.5.3 What happens after the request?

The bank will mark the cheque so that it cannot be cashed or deposited once your request is processed. If the cheque is already presented for payment, the stop payment request cannot be completed, and you may need to contact the cheque recipient to resolve the matter.



Knowledge Check

1. What is a bounced cheque?
2. What is the main reason for dating a cheque accurately?
 - a. To make the cheque look official
 - b. To avoid dishonour due to incorrect or outdated information
 - c. To meet legal requirements

3. What is the primary purpose of the MICR line on a cheque?

- a. To enhance the cheque's appearance
- b. To include the account holder's name
- c. To encode essential cheque and bank information for automated processing

Answers:

1. a. A bounced cheque, also known as a dishonoured or returned cheque, occurs when a bank refuses to process and honour the payment specified on the cheque.
2. b. To avoid dishonour due to incorrect or outdated information
3. c. To encode essential cheque and bank information for automated processing

3.0 Applying for Electronic Fund Transfers (EFT)**3.1 Understanding UPI**

In the realm of digital payments, understanding the differences between various modes of transactions is crucial. Two commonly used terms are UPI (Unified Payments Interface) and EFT (Electronic Fund Transfer). Both facilitate electronic payments, but they operate differently and serve different needs.

3.1.1 What is UPI?

UPI is a system that lets you manage multiple bank accounts through a single mobile app from any participating bank. It combines various banking features, making it easy to transfer money and pay merchants. You can send money anytime, 24/7, throughout the year.

Some apps that are popularly used to carry out UPI payments are - PhonePe, Paytm, Google Pay, as well as BHIM UPI. While the app interface differs, the process to authenticate a payment through these apps is the same, i.e., scanning a QR code or entering a UPI ID, specifying the amount and entering your UPI PIN to complete the transaction.

3.1.2 Key Features

- Instant money transfers between banks using mobile devices.
- Uses a Virtual Payment Address (VPA) - a unique identifier that does not require bank account details.
- Operates 24/7, so you can send and receive money anytime.
- Supports checking account balances, QR code payments, and more.

Example: Paying for Street Food

Imagine you are visiting Amritsar, and you decide to treat yourself to some delicious street food, say, a plate of Amritsari Kulcha. Instead of searching for change or cash, you can simply ask the vendor if they accept UPI payments. Most vendors display a QR code that you can scan using any UPI-enabled app like BHIM, Paytm, or Google Pay, or PhonePe on

your smartphone. You enter the amount, authenticate the transaction with your PIN, and balle balle! The payment is completed in seconds. The vendor receives an instant notification of the payment, and you enjoy your meal without any cash exchange.

3.2 Understanding EFT

In today's digital era, electronic fund transfers (EFT) have transformed financial transactions by offering convenience, speed, and security. EFT allows individuals to transfer money electronically by debiting one account and crediting the other, eliminating the need for physical cash or cheques. Whether you're paying bills, transferring funds to family members, or making online purchases, EFT provides a convenient and efficient way to manage your finances.

Example:

Sonia, a college student in Punjab, needs to send money to her parents who live in a different city. Instead of using traditional methods like cash or cheques, Sonia chooses electronic fund transfers (EFT) for a quick and secure transaction. She logs into her bank's online banking platform and initiates a transfer from her savings account to her parents' account. Within minutes, the funds are electronically transferred, giving her parents instant access to the money. This seamless process highlights the efficiency and convenience of EFT for managing financial transactions.



What are the main advantages of using electronic fund transfers (EFT) over traditional payment methods like cash or cheque?

3.2.1 Processing of EFT Transactions

EFT transactions undergo several stages of processing within the banking system.



Authorization: When you initiate a transfer, your bank checks if you have enough money and confirms your identity.



Clearing: The details of the transaction are sent securely to the recipient's bank, making sure they get the correct information.



Settlement: After the transaction is authorised and cleared, the money is moved from your bank to the recipient's bank. This can happen immediately or within a set time, depending on the type of transaction.

The involvement of the **National Clearing Cell (NCC)** in the EFT process includes the following steps:

1. **Initiation:** You place a fund transfer request with your bank.
2. **Consolidation:** The sending bank consolidates all such fund transfer requests and sends them to the service branch.
3. **Transmission to NCC:** The service branch transmits data to the EFT system, specifically the National Clearing Cell (NCC), which is an automated clearing house.
4. **Inter-NCC Transmission:** The NCC transmits the EFT data to another NCC on the receiver end.
5. **Processing by Receiving NCC:** The receiving NCC processes the data and forwards it to the beneficiary bank.
6. **Crediting the Beneficiary:** The beneficiary bank branch credits the beneficiary's account on the same business day of receiving the transfer request.

This detailed process ensures secure and efficient handling of electronic fund transfers within the banking system.

Example:

Idyant, a student in Ludhiana, who wants to transfer money from his savings account to his sister's account for her birthday gift. Instead of visiting the bank, he can easily do it through his smartphone using EFT.

- **Authorization:** Idyant's bank checks if he has enough funds and verifies his identity.
- **Clearing:** Details of the transaction are securely transmitted to his sister's bank.
- **Settlement:** Funds are transferred from Idyant's bank to his sister's bank, completing the transaction. This process may take a few minutes, hours or days. Nowadays, EFTs get processed in seconds!

3.2.2 Security Measures in EFT

EFT systems employ robust security measures to protect the confidentiality, integrity, and authenticity of transactions.

1. **Encryption:** Transaction data is encrypted using secure protocols during transmission over the internet, preventing unauthorised access or tampering.



Encrypted

Data that has been converted into a code to prevent unauthorised access.

2. **Authentication:** Users must authenticate their identity using secure login credentials, such as passwords, PINs, or biometric verification methods.
3. **Fraud Detection:** Banks use advanced algorithms to monitor transaction patterns and detect suspicious or unauthorised activity. For example, if a transaction differs significantly from your usual spending behaviour, the bank may flag it for further review.

3.2.3 Types of EFT Systems

EFT transactions can be processed through various electronic payment systems, each catering to specific transaction types and use cases:

Type of Electronic Funds Transfer	Description	Key Features
IMPS (Immediate Payment Service)	Allows immediate transfer to the beneficiary's account, even on bank holidays or weekends.	Available 24/7 through ATMs, mobile phones, or net-banking.
RTGS (Real Time Gross Settlement)	Used for high-value transactions, with a minimum transfer amount of ₹ 2 Lac. Funds are typically transferred within 30 minutes.	Available during specific hours, both sender and receiver's branches must support RTGS.
NEFT (National Electronic Fund Transfer)	Commonly used for transfers, banks may charge a fee ranging from ₹ 2.50 to ₹ 25 per transaction, depending on the amount transferred.	Available during bank working hours; no upper limit on transfer amount.
UPI (Unified Payments Interface)	Facilitates transactions up to ₹ 1 lakh using UPI-enabled apps on smartphones. No need to provide bank details for each transaction.	Real-time transfers, no fees for person-to-person transfers, quick and simple process.
Direct Deposit	Used for various purposes, including settling invoices and paying employees.	Typically takes 2-3 business days; commonly used for payroll and personal transfers.
Credit and Debit Card Transactions	Used for purchases in stores, online, or by phone.	Immediate transaction verification; funds may take a few days to clear.
ATM Transactions	Withdrawals involve electronic communication between ATM and bank.	Provides cash through electronic funds transfer, ensuring funds are available.
Online Payment Systems	Secure online systems for purchases and invoice settlement.	Facilitates quick and secure digital payments; examples include Square Online Payments.

Wire Transfers	Transfers funds electronically between banks or wire facilities.	Quick transfer of funds globally; typically used for large sums.
Automated Clearing House (ACH) Direct Payments	Electronic transfers between financial institutions via ACH network.	Includes various transaction types; widely used for electronic payments and direct deposits.

We will learn in detail about NEFT and RTGS in the following sections.

3.2.4 Application Process

This section will guide you through the process of applying for EFT services.

Visit Your Bank Branch: Speak to a customer service representative at your bank branch to start the process. They will guide you through the application and help with any necessary information. For example, if you are a student like Sonia, you might need to provide your student ID and proof of enrollment.

Online Banking Platforms: Many banks offer online banking platforms where you can apply for EFT services from home. Just log in to your online banking account and go to the EFT or fund transfers section. For example, if you are comfortable with technology, you'll appreciate the convenience of managing your finances anytime, anywhere with online banking.

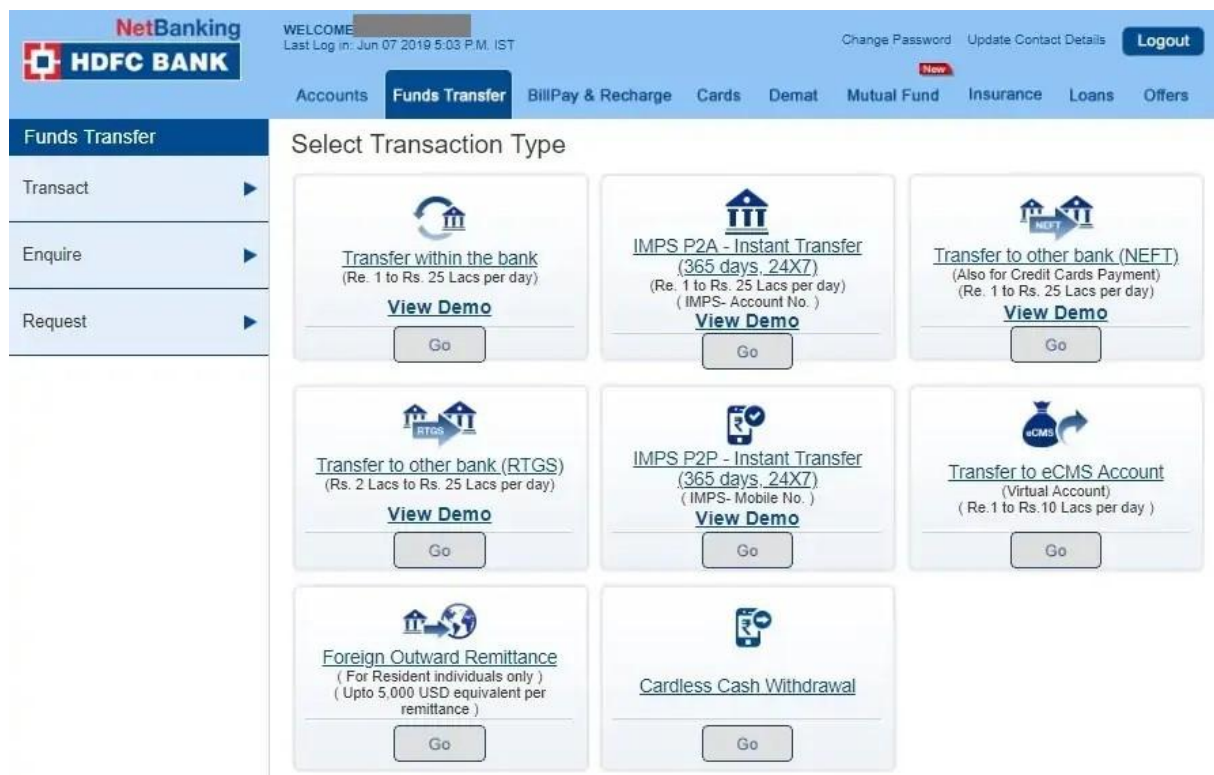


Image Source: <https://www.paisabazaar.com/banking/hdfc-net-banking/>

When applying for EFT services, you may need to provide the following information:

- Your account details, including account number and type.
- Your preferred EFT methods, such as online transfers, mobile banking, or automatic bill payments.
- Security measures, such as authentication methods or password settings, to ensure the safety of your transactions.

3.2.5 Preferred EFT Methods

Various EFT methods include online transfers, mobile banking, automatic bill payments, wire transfers, and mobile wallets.

Online Transfers: Online banking platforms make it easy to transfer funds electronically. With a few clicks on your computer or taps on your mobile device, you can move money between accounts or send it to others. For example, Rohan, a busy professional, prefers online transfers to manage his finances easily.

Mobile Banking: Mobile banking apps let you handle EFT transactions directly from your smartphone or tablet. You can transfer money, pay bills, or check account balances with ease. For example, Maya, a retiree, uses her mobile banking app to pay utility bills effortlessly.

Automatic Bill Payments: Set up recurring payments for utility bills, rent, loan instalments, and other expenses to ensure they are paid on time. This saves you time and gives you peace of mind, knowing your financial obligations are handled automatically.

Wire Transfers: For large or international transactions, wire transfers are a secure and reliable EFT method. Whether you're sending money to family overseas, paying business suppliers, or buying property abroad, wire transfers offer a fast and efficient way to move funds across borders. Although they may come with higher fees compared to other EFT methods, they ensure quick processing and reliable fund delivery.

Mobile Wallets: With the rise of digital wallets, mobile payment apps like Google Pay, Apple Pay, and Paytm have become popular for EFT transactions. These apps securely store your payment card information on your smartphone, allowing you to make contactless payments at participating merchants. Whether you're shopping in-store or online, mobile wallets provide a convenient and secure way to pay without using physical cards or cash.

Example:

Imagine you are a student working on a group project with your classmates. To contribute your share of funds for project expenses, you need to transfer money to your friend's account. Instead of visiting the bank or writing a cheque, you decide to apply for EFT services to make the transaction hassle-free.



Gurpreet: Sat Sri Akaal! I am here to inquire about applying for electronic fund transfer services.

Bank Teller (Jaspreet): Sat Sri Akaal, Gurpreet! Sure, I can assist you with that. Have you used our online banking services before?

Gurpreet: No, I haven't but I have heard about the convenience of electronic transfers.

Jaspreet: Oh, it's quite convenient indeed. Let me guide you through the process. Do you have your account details?

Gurpreet: Yes, I have my account number and other necessary details.

Jaspreet: Great! We will need to fill out an application form for electronic fund transfers. Here's the form. Please fill in your account details.

Gurpreet: Alright, I will fill it out.

Jaspreet: Once you have filled out the form, please submit it along with a copy of your identification for verification purposes.

Gurpreet: Here's the completed form and my ID. Is there anything else I need to do?

Jaspreet: That's all. Thank you, Gurpreet. Your application for EFT services has been submitted. You will receive a confirmation once it's processed, and then you can start enjoying the convenience of electronic fund transfers.

Gurpreet: Thank you so much for your help, Jaspreet! I appreciate it.

Jaspreet: You are welcome, Gurpreet! If you have any further questions, feel free to ask.



Knowledge Check

1. What are the benefits of Electronic Fund Transfer?
2. Sarah needs to pay her monthly rent to her landlord. She wants to ensure that the payment is made on time and securely. Which EFT method should Sarah use?
 - a. Online bank transfer
 - b. Mobile banking app
 - c. Automatic bill payment

3. Match the following EFT methods with their descriptions:

1. Online transfers	a) Sets up recurring payments for bills, ensuring timely payments without manual intervention.
2. Mobile banking	b) Offers a fast and efficient way to transfer funds across borders, albeit with additional fees.
3. Wire transfers	c) Allows you to initiate fund transfers between accounts or to other recipients with just a few clicks or taps.
4. Automatic bill payments	d) Provides a user-friendly interface on smartphones or tablets for performing EFT transactions.

Answers:

- The benefits of electronic fund transfers are numerous, offering convenience, speed, cost-effectiveness, and accessibility. Whether a busy professional, student, or retiree, EFT simplifies financial transactions and enhances overall banking experience.
- c) Automatic bill payment 3. 1-c, 2-d, 3- b, 4-a

3.3 Differences Between UPI and EFT

Speed: UPI transactions are processed instantly, making them faster compared to some EFT transactions that can take up to a few days.

Ease of Use: UPI transactions can be completed using just a UPI ID, without needing the recipient's bank account details. In contrast, EFT transactions require detailed information about the recipient's bank account.

Transaction Costs: UPI transactions are typically free or carry a minimal charge, whereas EFT transactions may involve higher fees, especially for immediate or international transfers.

Transaction Limits: UPI has a lower transaction limit per day compared to EFT, making EFT more suitable for larger transfers.

4.0 Using EFT like RTGS and NEFT for Transfers and Payments**Discuss**

How many of you have heard about or used the terms RTGS or NEFT before?

Have you ever seen notices like these before?

<u>NOTICE</u>	
<i>Students can also transfer the fee through ONLINE/NEFT/ RTGS</i>	
Name of the Bank	HDFC BANK LTD
Branch	CHANDIGARH
College Name	PUNJAB EDUCATION
Account Number	6876543211234
Account Type	SAVING
IFSC CODE	HDFC0000001
For DEMAND DRAFT: - in favour of:- "PUNJAB EDUCATION" payable at Chandigarh	

4.1 Introduction to RTGS

In today's fast-paced world, transferring money quickly and securely is essential. RTGS, or Real-Time Gross Settlement, meets this need by enabling instant and direct transfers of funds between bank accounts. It's especially useful for transferring large amounts, typically ₹2 Lakhs or more, in real-time. Let's explore how RTGS works!

4.1.1 Explanation

RTGS allows for instant settlement of high-value transactions, ensuring that the funds are transferred in real-time and settled on a gross basis, meaning each transaction is processed individually. RTGS stands for Real-Time Gross Settlement.

R - Real-Time: The '*Real-Time*' aspect refers to the immediate processing and settlement of transactions without any delay.

T - Transfer: The '*Transfer*' aspect signifies the movement of funds from one bank account to another, facilitated by the RTGS system.

G - Gross: The '*Gross*' refers to the individual processing of each transaction without any consolidation or netting. Each transaction is settled independently.

S - Settlement: The '*Settlement*' aspect refers to the final and irrevocable transfer of funds between the sender's and recipient's accounts, ensuring that the transaction is complete and cannot be reversed.

4.1.2 Features and Benefits of RTGS

Safety and Security

RTGS offers a highly secure method of transferring funds, significantly reducing the risk of loss, theft, or fraudulent activity compared to physical instruments like cheques or demand drafts.

No Maximum Limit	RTGS transactions typically do not have a maximum limit, making it suitable for transferring both small and large sums of money within the RTGS framework.
Real-Time Transfer	RTGS provides real-time fund transfers, ensuring that the recipient's account is credited immediately upon initiation of the transaction, enhancing its efficiency.
Seven Days a Week	RTGS operates on all days, including weekends and holidays, providing uninterrupted access for users to transfer funds when needed, enhancing convenience and accessibility.
No Physical Instruments	RTGS eliminates the need for physical instruments like cheques or demand drafts, streamlining the process and reducing associated risks.
Convenience of Internet Banking	RTGS transactions can be initiated conveniently from the user's home or workplace through internet banking, offering flexibility and ease of use.

4.1.3 How Real-Time Gross Settlement Transactions Work

The RTGS process begins when a sender instructs their bank to transfer a specific amount of money to a recipient's account at another bank. This instruction can be given through various channels, including *online banking, mobile banking, or by visiting a bank branch*.

The sender's bank verifies the availability of sufficient funds and authorises the transaction, following which it is transmitted to the RTGS system. The central bank processes the transaction, debits the sender's bank's settlement account, and credits the recipient's bank's settlement account with the transaction amount. The recipient's bank receives a notification of the incoming funds, credits the recipient's account, and sends an instant confirmation to the sender, completing the transaction.

4.1.4 Different Modes for Initiating RTGS Transactions in India

RTGS transactions can be initiated through internet banking, mobile banking apps, or by visiting a bank branch. Internet banking allows customers to initiate RTGS transfers online, while mobile banking apps enable customers to perform RTGS transactions using their smartphones or tablets. These apps are user-friendly and convenient for on-the-go banking. Alternatively, customers can visit their bank's physical branch and request an RTGS transfer in person, where bank staff will assist in processing the transaction.

4.1.5 Information Required to Begin an RTGS Transaction

To initiate an RTGS transaction, the following information is necessary:

- The name of the beneficiary bank and branch.

- Recipient's full name.
- IFSC code of the receiving bank.Amount to be transferred.
- Any relevant remarks or notes.
- Sender's account particulars.
- Beneficiary's account number.

4.1.6 How to Make an RTGS Transfer

Online RTGS Transfer Process:

- Log in to the your internet banking account
- On the main page, click on 'Fund transfer'
- From the drop down menu that appears, select 'RTGS'
- Note that you need to 'Add beneficiary' to the list of beneficiaries in your account if you haven't done so already
- To add a new beneficiary, you need to click on 'Add beneficiary' option on the page
- Enter the beneficiary's required information such as his/her name, bank account number, IFSC code, etc.
- Click on 'Confirm' or 'Add'.
- To authenticate this step, you will be asked to enter the OTP sent to your registered mobile number
- After doing so, your action would be processed. It will take around 24 hours to add a beneficiary
- Once the beneficiary is added to your account, you need to select the beneficiary details (to whom you need to send the money) from your list of beneficiaries and enter the amount that needs to be transferred.
- Click on 'Confirm' and the amount will be transferred from your bank account to the beneficiary's account.



IFSC code

A unique alphanumeric code used to identify bank branches.



Beneficiary

An individual designated to receive funds or benefits from a financial transaction.



Offline RTGS Transfer Process

1. **Visit your bank branch:** Head to your nearest bank branch and request an RTGS form from a bank representative.
2. **Fill in transaction details:** Carefully fill in the transaction details, including the beneficiary's information and the amount to be transferred.
3. **Attach a cheque leaf:** Attach a cheque leaf from your account with the beneficiary's details.
4. **Submit the form:** Submit the completed RTGS form to the bank representative for verification and processing.

HDFC BANK We understand your world		Application Form For Funds Transfer Through Real Time Gross Settlement (RTGS) / National Electronic Funds Transfer (NEFT)	
Branch Code / Name		Maximum Limit for NEFT Transaction	
Date		HDFC Bank Customer	No Limit
Time		Non HDFC Bank Customer & Indo-Nepal NEFT Remittance	Up to INR 50,000/-
You are requested to remit the proceeds as per details below through RTGS <input type="checkbox"/> / NEFT <input type="checkbox"/> . (Tick ✓ the appropriate Box). Attaching Cheque No. _____ for Rs. _____. (For RTGS draw cheque favouring "HDFC Bank Ltd – RTGS" and for NEFT draw cheque favouring "HDFC Bank Ltd – NEFT")			
Beneficiary Details			
Beneficiary Name			
Beneficiary Account Number			
Beneficiary Account Number			
Beneficiary Address			
Beneficiary Bank Name & Branch			
Beneficiary Bank IFSC Code	Account Type : Resident <input type="checkbox"/> / Non Resident <input type="checkbox"/>		
Amount (in figures) to be credited			
Amount (in words) to be credited			
My / Our Details (Remitter)			
Remitter (Applicant) Name			
Remitter Account Number			
Cash Deposited (Non HDFC Bank Customer)			
Mobile / Phone Number of Remitter (Mandatory)	E-Mail Id:		
Address of the Remitter (Mandatory for Non – HDFC Bank Customer)			
Remarks			



Activity 3: Mastering Online Banking and RTGS Transfers

- Practice Logging In:** Access your bank's online banking platform and navigate through the process of adding a beneficiary and initiating an RTGS transfer.
- Create a Checklist/Flowchart:** Develop a detailed checklist or flowchart outlining the key steps and considerations for initiating a successful RTGS transfer, ensuring compliance with banking protocols and security measures.

4.2 Introduction to NEFT

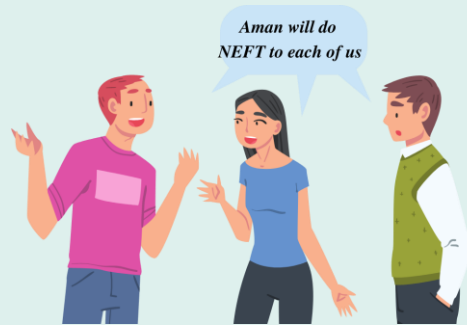
In the realm of electronic funds transfer (EFT), NEFT (National Electronic Funds Transfer) is another important method for transferring money between bank accounts. Unlike RTGS, NEFT operates on a deferred net settlement basis, meaning transactions are processed and settled in batches at scheduled intervals rather than instantaneously. This allows for more flexibility in timing and batching of transactions.

NEFT is commonly used for various types of transactions, including salary payments, bill payments, online purchases, and more. It is widely used due to its low cost, broad availability, and convenience. Let's explore NEFT in more detail!

Let us imagine that you have a friend named Aman who needs to transfer money to three different people: Gurpreet, Harman, and Manpreet. Aman decides to use NEFT for these transfers. Instead of sending each transfer separately, NEFT allows Aman to group all three transactions together and send them in one batch.

Now, let's say Aman initiates the transfers in the morning. Instead of the money being instantly transferred to Gurpreet, Harman, and Manpreet, the transactions are queued up and processed together at a later time, typically in batches every hour or so.

This batching system offers more flexibility because Aman doesn't have to worry about timing each transfer individually. He can initiate the transfers whenever it's convenient for him, knowing that they will be processed along with other transactions in the next batch.



NEFT stands for National Electronic Funds Transfer.

N - National: NEFT is a nationwide electronic funds transfer system that enables individuals and businesses to transfer funds across the country seamlessly.

E - Electronic: The 'Electronic' aspect signifies that NEFT transactions are conducted electronically, eliminating the need for physical instruments like cheques or demand drafts.

F - Funds: NEFT facilitates the transfer of funds between bank accounts, enabling individuals and businesses to make payments and transfers conveniently.

T - Transfer: NEFT allows for the transfer of funds from one bank account to another, providing a secure and efficient method of moving money.

4.2.1 Features and Benefits of NEFT

1. **Convenience:** NEFT offers convenience to users by providing a secure and efficient method of transferring funds electronically, eliminating the need for physical visits to banks or the use of paper-based instruments.
2. **Cost-Effective:** NEFT transactions are generally cost-effective, with many banks offering low or zero fees for transferring funds using the NEFT system, making it an affordable option for individuals and businesses.
3. **Widespread Availability:** NEFT is widely available across banks and financial institutions in India, allowing users to initiate transactions from various channels, including internet banking, mobile banking, ATMs, and bank branches.
4. **Scheduled Settlement:** NEFT transactions are settled in batches at scheduled intervals throughout the day, providing users with flexibility in timing their payments and transfers according to their convenience.
5. **Secure Transactions:** NEFT transactions are highly secure, with robust encryption and authentication mechanisms in place to safeguard sensitive information and prevent unauthorised access.

4.2.2 How NEFT Transactions Work

NEFT transactions involve the following steps:

- The sender initiates an NEFT transaction through their bank, providing details such as the beneficiary's account number, IFSC code, and the amount to be transferred.
- The sender's bank forwards the transaction request to the NEFT system, which processes and schedules the transaction for settlement in the next available batch.
- The NEFT system processes the transaction and forwards it to the recipient's bank for credit to the beneficiary's account.
- Upon receiving the funds, the recipient's bank credits the amount to the beneficiary's account and notifies the recipient of the successful transaction.

4.2.3 Different Modes for Initiating NEFT Transactions in India

NEFT transactions can be initiated through various channels, including:

1. **Internet Banking:** Users can initiate NEFT transactions through their bank's internet banking portal by logging in and providing the required details for the transaction.
2. **Mobile Banking:** Many banks offer mobile banking apps that allow users to initiate NEFT transactions conveniently from their smartphones or tablets.
3. **ATMs:** Some ATMs are equipped with NEFT functionality, allowing users to initiate transactions by selecting the NEFT option from the menu and providing the necessary details.
4. **Bank Branches:** Users can visit their bank branch and request assistance from bank staff to initiate NEFT transactions in person.

4.2.4 Information Required to Begin an NEFT Transaction

To initiate an NEFT transaction, users need to provide the following information:

- Beneficiary's account number and name
- IFSC code of the recipient's bank branch
- Amount to be transferred
- Sender's account particulars
- Any relevant remarks or notes for the transaction

4.2.5 How to Make an NEFT Transfer

Online NEFT Transfer Process:

- Log in to your internet banking account.
- On the main page, click on 'Fund transfer'.
- From the drop-down menu that appears, select 'NEFT'.
- Note that you need to 'Add beneficiary' to the list of beneficiaries in your account if you haven't done so already.

- To add a new beneficiary, you need to click on the 'Add beneficiary' option on the page.
- Enter the beneficiary's required information such as his/her name, bank account number, IFSC, etc.
- Click on 'Confirm' or 'Add'.
- To authenticate this step, you will be asked to enter the OTP sent to your registered mobile number.
- After doing so, your action would be processed. It will take around 24 hours to add a beneficiary.
- Once the beneficiary is added to your account, you need to select the beneficiary details (to whom you need to send the money) from your list of beneficiaries.
- Enter the amount that needs to be transferred and confirm your transaction.
- Click on 'Confirm' and the amount will be transferred from your bank account to the beneficiary's account.

Offline NEFT Transfer Process

- Visit your bank branch and request an NEFT transfer form from a bank representative.
- Fill out the NEFT transfer form with the required details, including the beneficiary's information and the amount to be transferred.
- Submit the completed form to the bank representative for verification and processing.

4.2.6 Transaction Limit to Transfer Money through NEFT

NEFT transactions offer the flexibility of transferring any amount, there is no minimum or maximum limit to transfer money. An individual can transfer as low as ₹1 through NEFT. There is also no limit on the maximum amount that can be transferred through NEFT.

However, it is important to note that while RBI may not have any limitations on NEFT amount transfers, specific banks may enforce their own restrictions.



Activity 4: Mastering NEFT Transfers

Initiate an NEFT Transfer using the Internet or Mobile Banking. Log into your bank's online or mobile banking. Add a beneficiary and initiate an NEFT transfer. Note the required information and security steps.

4.3 Comparison between NEFT and RTGS

Here's a comparison table highlighting the similarities and differences between NEFT and RTGS:

Feature	NEFT	RTGS
Minimum Transfer	₹1	₹2 Lakhs

Limit		
Maximum Transfer Limit	No limit by RBI but individual banks may impose their own maximum limits.	No maximum limit.
Settlement Timing	Settlement occurs in hourly batches.	Settlement occurs instantly and individually.
Transaction Speed	Takes a few hours to settle.	Settles transactions instantly.
Availability	Operates on all days except bank holidays.	Operates on all days except bank holidays.
Cost	Transaction fees may apply based on the bank's policy.	Generally, higher transaction fees compared to NEFT.
Usage	Suitable for small to large transactions.	Suitable for large transactions.



Activity 5: Choosing Between NEFT and RTGS

Harpreet is required to pay his annual school fees, amounting to ₹2,20,000. His school offers two payment options: NEFT and RTGS. Considering this situation, what factors should Harpreet take into account when deciding between NEFT and RTGS for fee payment?



4.4 Understanding Demand Drafts: A Secure Payment Instrument

In the world of banking transactions, a demand draft (DD) stands out as a reliable and secure payment instrument issued by banks. Let's dive into what demand drafts are when they are used, and how they differ from other payment methods, especially cheques.

4.4.1 What is a Demand Draft?

- A demand draft is a pre-paid instrument, similar to a cheque, issued by a bank on behalf of a customer.
- Unlike cheque, where the payment is drawn from the issuer's account, demand drafts are paid for upfront by the purchaser.
- The bank guarantees the payment to the recipient (payee) upon presentation, as the funds are already secured.
- Demand drafts are typically used in scenarios where assurance of funds is crucial. They are used for transactions involving large amounts of money or between parties who don't know each other and may not trust each other.
- Demand drafts provide assurance of funds upfront, making them ideal for transactions where certainty is essential. Cheques, while commonly used, may pose a risk of being

bounced if the issuer's account does not have sufficient funds at the time of presentation.

YES BANK
CASH MANAGEMENT SERVICES
VALID FOR THREE MONTHS FROM DATE OF ISSUE
NOT OVER ₹ 100.00
20/11/2014
D D M M Y Y Y Y
A/C. PAYEE / Non-Negotiable
Pay **ANURAG GUPTA******* or Order
Rupees ONE HUNDRED ONLY ** को या उनके आदेश पर
रुपये अदा करें ₹ *****100.00
DEMAND DRAFT
YES BANK
YES BANK LIMITED
DEHRADUN
DRAWEE BANK AND BRANCH
YES BANK LIMITED
MUMBAI
ISSUING BANK AND BRANCH
For YES BANK Ltd
K. SOMASUNDARAM KAPIL JUNEJA
AUTHORISED SIGNATORY (IES)
16910 000532000 999998 16

4.4.2 How Demand Drafts Work

Scenario: Rajveer is purchasing a piece of land from a seller who lives in a different city. The seller is unfamiliar to Rajveer, and wants to ensure that the transaction is secure and the funds are guaranteed.

Solution: Rajveer decides to obtain a demand draft from his bank for the amount. He provides the demand draft to the seller, who can deposit it into their bank account. Once the demand draft is presented, the funds are immediately available to the seller, providing assurance of payment.



What is the difference between DD and cheque?

4.4.3 What is a Pay Order

A Pay Order (PO) is a financial instrument, also known as a Banker's Cheque, issued by the bank on the customer's behalf, allowing them to pay a specified amount to a third party, whether an organisation or an individual. To obtain a Pay Order, you must provide the required amount to the banking executive, either in cash or via cheque. Once the bank issues the Pay Order, the specified amount will be transferred to the beneficiary's account upon deposit.

Some key features of a Pay Order:

- Only a bank can issue a Pay Order, which is why it is also referred to as a Banker's Cheque.
- Once issued, a Pay Order cannot be cancelled.
- Processing a Pay Order may take up to 24 hours.
- Customers must provide the payment amount in cash or another accepted mode when requesting a Pay Order.
- A Pay Order is a non-negotiable instrument, which means that it cannot be transferred to someone else. Only the person or organisation named on the PO can receive the payment, making it a secure payment method.
- A Pay Order is valid for three months from the date of issuance.
- It is payable only at the issuing bank's branch within the same city.

Note: A Pay Order can be cleared at any branch of the issuing bank within the same city and a Demand Draft can be cleared at any branch of the issuing bank, regardless of the city.

4.5 Online banking

Online banking lets customers manage their accounts over the internet, so they don't need to visit a physical branch. With online banking, you can check account balances, transfer funds, and pay bills using a computer or smartphone. This service makes banking more convenient, reduces branch traffic, and provides a secure way to handle your banking activities.

4.6 Debit and Credit Cards

Debit cards are linked directly to a customer's bank account, allowing for electronic transactions that withdraw funds directly from the account. They are used for everyday activities like shopping, paying bills, and withdrawing cash from ATMs. The amount spent is immediately deducted from the account balance, providing a secure and convenient way to access money without carrying cash.

Credit cards allow customers to borrow money from the issuing bank up to a set credit limit. Unlike debit cards, which use funds from a bank account, credit cards provide a line of credit for purchases or cash advances. The borrowed amount must be repaid, often with interest if not paid off within a certain time. Credit cards offer flexibility for managing larger expenses and provide benefits such as rewards and protection against fraud.



Let's Recap

1. **Cheques** are written orders to a bank to transfer a specific sum of money from one person's account to another.
2. **EFT** enables the electronic transmission of funds without the usage of cheques.
3. **NEFT** and **RTGS** are electronic payment systems that allow consumers and businesses to move funds between their bank accounts.
4. **Debit cards** let the cardholder make purchases or take out funds that are already present in their bank accounts electronically.
5. **Online banking** is a way to manage your bank account using the internet. Instead of going to a bank branch, you can use a computer or a smartphone to access your account, check your balance, transfer money, and pay bills.

EXERCISE

Objective Type Questions

Fill in the blanks:

1. A cheque is a _____ order that instructs a bank to pay a specific amount of money from one person's account to another person's account.
2. EFT stands for _____.
3. DD stands for _____.
4. In RTGS, an amount of _____ is transferred within _____ minutes.
5. NEFT stands for _____.
6. A crossed cheque has _____ parallel lines drawn across its face.
8. What is the difference between a crossed cheque and a bearer cheque?
9. What is the meaning of RTGS? Explain its features.
10. What is the difference between UPI and EFT?
11. Write the features and benefits of NEFT.

Long Answer Type Questions

12. What is EFT? Explain the types of EFT systems.
13. How is an RTGS transfer made or processed?

Short Answer Type Questions

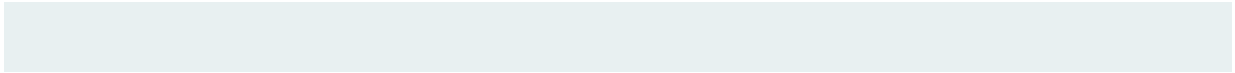
7. What are channels to request a cheque book? Explain.

ANSWER KEY

Objective Type Questions

Fill in the blanks:

1. Written
2. Electronic Fund Transfer
3. Demand Draft
4. ₹2 lakh, 30 minutes
5. National Electronic Fund Transfer
6. Two





Topics

- Review of Basic Arithmetic Operations
 - Review Table: Key Arithmetic Operations and Their Importance in Business
 - Managing Personal Finances in Banking
 - Effective Budgeting in Banking
 - Calculating Loan Repayments with Multiplication & Division
 - Handling Bank Transactions with Precision
 - Calculating Interest and Fees in Accounts
- Understanding Fractions, Decimals, and Percentages for Business Applications
 - Review Table: Understanding the Types, Examples, and Conversion of Fractions, Decimals, and Percentages
 - Application of Fractions in Business and Banking Context
 - Application of Decimals in Business and Banking Context
 - Application of Percentages in Business and Banking Context
- Ratios and Proportions in Business Applications
 - Ratios and Proportions
 - How to Check the Financial Health of a Bank Using Ratios
 - Banking Ratios
 - Profitability Ratios
 - Growth Rates
 - Earnings Growth Rate



Learning Objectives

- Solve banking and financial problems using addition, subtraction, multiplication, and division.
- Develop and monitor efficient budgets for banking operations.
- Accurately manage and record bank transactions, including loans, interest, and fees.
- Understand the fundamentals of fractions, proportions, and decimals and how they can be converted to each other.
- Application of fractions, decimals, and percentages in business and banking scenarios.
- Understand how ratios and proportions are used to analyse and compare financial data in banking.
- Learn essential banking ratios, such as the Loan-to-Deposit Ratio, CASA Ratio, and Net Interest Margin.



Materials Required

- Charts and graphs to illustrate the application of ratios.
- Financial Calculators: Tools for calculating ratios and interest.



Activity 1: Before We Begin!

1. Have you ever thought about how businesses use mathematics in their daily operations? From calculating profits and losses to setting prices and making financial decisions, mathematics plays a crucial role in the business world. Can you think of other ways businesses might use maths?

1.0 Review of Basic Arithmetic Operations

In this chapter, we will learn the key maths concepts used in banking and finance. We will cover how to calculate interest rates, loan payments, and investment returns. Understanding these calculations is important for managing personal finances and banking tasks.

We will also discuss basic arithmetic, fractions, decimals, percentages, and ratios, all of which are important in everyday banking. Mastering these maths skills will help you make informed financial decisions, manage accounts accurately, and optimise investment strategies.



Precision

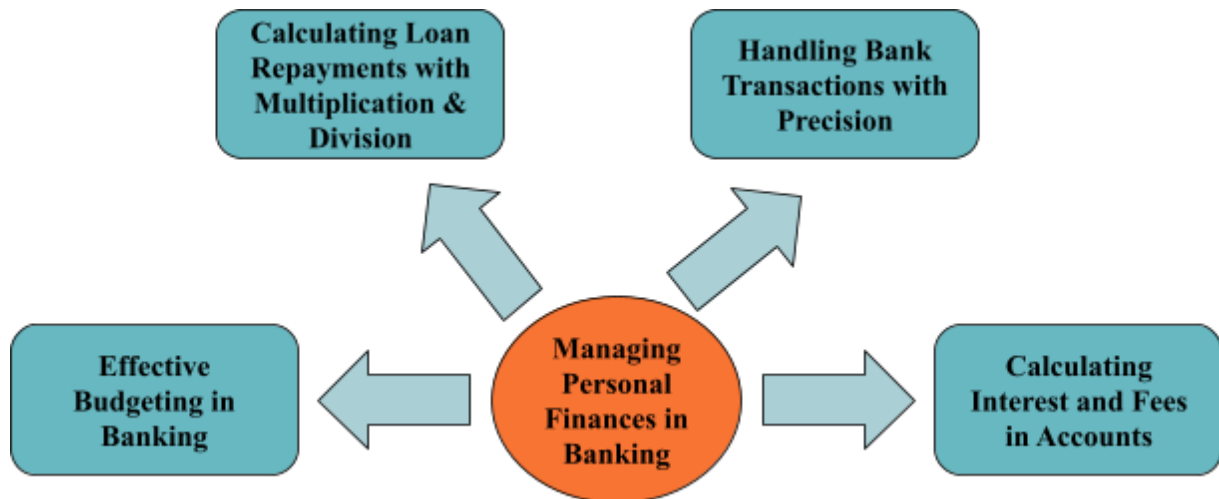
Precision means being exact, accurate and free from errors.

1.1 Review Table: Key Arithmetic Operations and Their Importance in Banking

Operation	Concept	Example	Importance of Precision
Adding Decimals	Align decimal points and add corresponding digits.	$\begin{array}{r} 245.50 \\ + 312.75 \\ \hline = 558.25 \end{array}$	Small errors can lead to inaccuracies in account balances and financial records.
Multiplying Decimals	Multiply the numbers as if they were whole numbers, then place the decimal point in the answer.	$45.5 \times 3.2 = 145.60$	Accurate multiplication is crucial for precise interest calculations and financial estimates.
Subtracting Fractions	Find a common denominator and subtract numerators.	$\frac{5}{8} - \frac{1}{4} = \frac{3}{8}$	Incorrect subtraction can affect calculations for loan repayments and interest distribution.

Multiplying Fractions	Multiply the numerators together and the denominators together.	$\frac{2}{5} \times \frac{3}{4}$ $= \frac{6}{20} = \frac{3}{10}$	Precise multiplication is essential for calculating financial ratios and resource allocations.
Dividing Fractions	Invert (flip) the second fraction and multiply .	$\frac{3}{4} \div \frac{1}{2}$ $\frac{3}{4} \times \frac{2}{1}$ $= \frac{6}{4} = \frac{3}{2}$	Errors in division can lead to incorrect loan terms or investment calculations, impacting financial decisions.

1.2 Managing Personal Finances in Banking



1.2.1 Effective Budgeting in Banking

Budgeting in banking means managing financial resources efficiently. It involves setting aside funds for things like loans, interest payments, and daily operations. Strategic decisions help make the best use of funds, offering competitive loans while staying profitable. Mastering budgeting leads to better financial health and customer satisfaction. Let's dive into practical budgeting challenges in banking!



Loan Disbursement

The process of transferring the approved loan amount from the lender to the borrower's bank account.

Problem 1(a): Budget Allocation for Loan Disbursement

A bank has a total budget of ₹1 crore for the financial year. They plan to allocate ₹70 lakhs for new loans and ₹10 lakhs for operational expenses. What is the remaining budget after these allocations?

Solution:

Total budget = ₹1 crore

Loan allocation = ₹70 lakhs

Operational expenses = ₹10 lakhs

Remaining budget = Total budget - Loan allocation - Operational expenses

= ₹1 crore - ₹70 lakhs - ₹10 lakhs

= ₹100 lakhs - ₹80 lakhs

= ₹20 lakhs

The remaining budget is **₹20 lakhs**.

Problem 1(b): Budget Allocation for Loan Disbursement (Over Budget Scenario)

A bank has a total budget of ₹1.2 crore for the financial year. They plan to allocate funds as follows: ₹60 lakhs for new loans to small businesses, ₹40 lakhs for personal loans, ₹15 lakhs for operational expenses, ₹10 lakhs for marketing and promotions. How much budget remains after these allocations?

Solution:

Total budget = ₹1.2 crore

Small business loan allocation = ₹60 lakhs

Personal loan allocation = ₹40 lakhs

Operational expenses = ₹15 lakhs

Marketing and promotions = ₹10 lakhs

Remaining budget = Total budget - (Small business loan allocation + Personal loan allocation + Operational expenses + Marketing and promotions)

= ₹1.2 crore - (₹60 lakhs + ₹40 lakhs + ₹15 lakhs + ₹10 lakhs)

= ₹120 lakhs - ₹125 lakhs

= -₹5 lakhs

The bank will be over budget by **₹5 lakhs**.

Accurate calculations help ensure that budgets are properly allocated, preventing overspending and financial strain. By identifying that they are over budget, the bank can make necessary adjustments, such as reallocating funds or reducing expenses, to stay within their financial limits.

Problem 2: Budget Allocation for New Branches

A bank has a budget of ₹5 crore for opening new branches. They have already spent ₹2 crore on two branches and need to allocate the remaining budget equally for two more branches. How much budget is allocated for each of the remaining branches?

Solution:

Total budget for new branches = ₹5 crore

Spent on two branches = ₹2 crore

Remaining budget = Total budget - Amount spent

$$= ₹5 \text{ crore} - ₹2 \text{ crore} = ₹3 \text{ crore}$$

Budget for each remaining branch = Remaining budget / Number of branches

$$= ₹3 \text{ crore} / 2$$

$$= ₹1.5 \text{ crore}$$

₹1.5 crore is allocated for each of the remaining branches.

Accurate budgeting ensures that each branch receives the necessary funds for setup and operations. By calculating the budget allocation, the bank can ensure that it efficiently uses its resources, avoids overspending, and maintains financial balance.



Knowledge Check

1. A bank has a total annual budget of ₹3 crore. They plan to allocate ₹1.2 crore for new loan approvals, ₹50 lakhs for marketing and promotions, and ₹30 lakhs for employee training. What is the remaining budget after these allocations?
2. A bank has allocated a budget of ₹3 crore for installing new ATMs across the city. They have already spent ₹1.5 crore on installing 30 ATMs. How much budget is left for installing the remaining ATMs, and what is the average cost per ATM if the remaining budget is to be divided equally among 20 new ATMs?

Answers:

1. The remaining budget is ₹1 crore.
2. The remaining budget of ₹1.5 crore will be used to install 20 new ATMs, with an average cost of ₹7.5 lakh per ATM, which is higher than the first phase where each ATM cost ₹5 lakh.



1.2.2 Calculating Loan Repayments with Multiplication & Division

To calculate the total amount repaid over the life of a loan, you need to multiply the repayment amount with the total number of payments. Total Number of Payments is the total number of instalments made over the loan term (e.g., number of months, weeks, or years).

$$\text{Total Amount Repaid} = \text{Repayment Amount} \times \text{Total Number of Payments}$$

Here's how you can approach it:

A person takes out a loan with monthly repayments of ₹2,500 for 4 years. Calculate the total repayment amount over the life of the loan.

Solution:

Number of Months in 4 years = 4 years \times 12 months = 48 months

Total Repayment = Monthly Repayment Amount \times Number of Months

Total Repayment = ₹2,500 \times 48 = ₹1,20,000

So, the total repayment amount for the monthly repayments is **₹1,20,000**.

Problem 2: Weekly Repayments

If a person takes out a loan with weekly repayments of ₹1,200 for 3 years, how much would be the total repayment amount?

Solution:

Number of Weeks in 3 years = 3 years \times 52 weeks = 156 weeks

Total Repayment = Weekly Repayment Amount \times Number of Weeks

Total Repayment = ₹1,200 \times 156 = ₹1,87,200

So, the total repayment amount for the weekly repayments is **₹1,87,200**.

1.2.3 Handling Bank Transactions with Precision

Handling bank transactions with precision is vital for maintaining accuracy in a bank's financial operations. Whether it's processing deposits, withdrawals, transfers, or other financial transactions, attention to detail ensures that customers' accounts are accurate, balances are maintained correctly, and the bank's financial records are reliable. This section highlights the importance of precise calculations in daily banking to ensure trust and efficiency.

Problem 1: Accurate Deposit and Withdrawal Management

You started the month with ₹500 in your savings account. The following table lists all the transactions you made during the month using cheques. What is your account balance at the end of the month after all these transactions?

Date	Transaction Type	Cheque Number	Amount (₹)
04/09	Withdrawal	384102	120
12/09	Deposit	275146	200
22/09	Payment to LIC	384103	240
29/09	Deposit	801351	150

Solution:

According to the question,

Starting with a balance of ₹500 in your savings account:

- On 4th September, ₹120 was withdrawn using cheque number 384102.
- On 12th September, ₹200 was deposited using cheque number 275146.
- On 22nd September, ₹240 was paid to LIC using cheque number 384103.
- On 29th September, ₹150 was deposited using cheque number 801351.

The final balance in your account is calculated as follows:

Final Balance = Initial Balance + Total Deposits - Total Withdrawals

= ₹500 + ₹200 + ₹150 - ₹120 - ₹240

= ₹850 - ₹360

= ₹490

After all transactions, the final balance is **₹490**.

Problem 2: Handling Multiple Account Transactions

A customer operates three accounts with the bank:

Account	Balance
A	₹1,00,000
B	₹2,50,000
C	₹3,00,000

The customer transfers ₹30,000 from Account A to Account B, ₹50,000 from Account B to Account C, and ₹20,000 from Account C to Account A. Calculate the final balances in all three accounts.

Solution:

According to the question,

Account A	Account B	Account C
Initial: ₹1,00,000	Initial: ₹2,50,000	Initial: ₹3,00,000
After transfer to B: ₹1,00,000 - ₹30,000 = ₹70,000	After receiving from A: ₹2,50,000 + ₹30,000 = ₹2,80,000	After receiving from B: ₹3,00,000 + ₹50,000 = ₹3,50,000
After receiving from C: ₹70,000 + ₹20,000 = ₹90,000	After transfer to C: ₹2,80,000 - ₹50,000 = ₹2,30,000	After transfer to A: ₹3,50,000 - ₹20,000 = ₹3,30,000
Final Balance: ₹90,000	Final Balance: ₹2,30,000	Final Balance: ₹3,30,000



Knowledge Check

1. Amar has ₹5,50,000 in his bank account. After withdrawing ₹75,000, how much money remains in his account?
2. Amar starts with ₹20,000 in his savings account. He makes the following transactions: a withdrawal of ₹2,000, a deposit of ₹1,500, and another withdrawal of ₹500. What is Amar's current balance?



Answers:

1. The remaining amount is ₹4,75,000.
2. Amar's current balance is ₹19,000.

1.2.4 Calculating Interest and Fees in Accounts

Calculating interest and fees is a key part of banking. It involves determining how much interest to charge on loans or pay on savings, and figuring out various fees associated with banking services like ATM fees, account maintenance fees, credit card fees, etc. Let's explore how interest and fees are calculated in real banking scenarios!

Problem 1: Simple Interest Calculation on a Savings Account*

Simran deposits ₹1,00,000 into a savings account with an annual interest rate of 5%. What is the interest amount that Simran will earn after one year?

Solution:

Here,

Principal = ₹1,00,000

Rate = 5% per year

Time = 1 year

$$\text{Simple Interest, S.I.} = \frac{\text{Principal} \times \text{Rate} \times \text{Time}}{100}$$

$$S.I. = \frac{1,00,000 \times 5 \times 1}{100}$$

$$S.I. = 5,000$$

So, Simran will earn **₹5,000** in interest after one year.

**Interest**

The amount to be paid on the borrowed money or the amount received on the money lent.

Simple interest is calculated on the principal, or original, amount of a loan.

Note: Interest is presented as a rate, such as 5%, which is mathematically expressed as 5/100. This is why the Simple Interest (SI) formula uses division by 100, as it converts the percentage rate into a decimal for accurate calculation of interest.

**We will discuss S.I. in more detail in Section 2.2.*

Scenario: Incorrect Interest Calculation

Simran has a savings account with a principal amount of ₹1,00,000 at an annual interest rate of 5% for one year. Due to an error, the bank credited ₹3,000 instead of the correct amount of ₹5,000.

Consequences:

- Customer Dissatisfaction: Simran noticed the error and contacted the bank but also lost trust in the bank.
- Operational Impact: The bank had to spend time and



resources to fix the mistake, including recalculating and compensating Simran.

- Reputation Damage: Such errors can harm the bank's reputation as customers' negative feedback impacts their credibility.
- Financial Penalty: As a result of the delayed credit, the bank may be required to pay additional interest to Simran. In this case, the bank could owe ₹2,000 as compensation for the delay, increasing the financial cost of the error.

Problem 2: Service Fee Calculation

Fee income is the revenue that banks earn from fees on services and products like loans, credit cards, account maintenance, overdrafts, and ATM usage. These fees must be accurately calculated to avoid overcharging or undercharging customers.

If a person pays an ATM fee of ₹18 each month for 6 years, what will be revenue to the bank from the fee charged over 6 years?

Solution:

Monthly ATM Fee: ₹18

Number of months in 6 years: 6 years \times (12 months/year) = 72 months

The total revenue from ATM fees would be:

Total Revenue = Monthly Fee \times Number of Months = ₹18 \times 72 = ₹1,296

So, the total revenue of the bank from the fee charged over 6 years would be **₹1,296**



Knowledge Check

1. A bank charges an account service fee of ₹16 per month and a transaction fee of ₹0.90 per transaction. If a customer makes 15 transactions in a month, what will be the total fees paid by the customer for that month?
2. HDFC Bank charges an account service fee of ₹10 per month, a transaction fee of ₹0.50 per transaction, and an overdrawn account fee of ₹6. Calculate the total fees incurred by a customer in a month during which they made 5 transactions and incurred 2 overdrawn account fees.

Answers:

1. The total fees paid by the customer for that month would be ₹29.50.
2. The total fees paid by the customer in one month are ₹24.50.

Note: Banks usually charge these fees to meet the operational costs in providing the services to customers, like operating and maintaining the ATMs.





Activity 2: Banking Role-Play

Objective: To understand and apply key banking concepts.

Instructions:

1. You may divide students into groups.
2. Each group will have members take on different roles: Bank Manager, Customer Service Representative, Financial Advisor, and Account Holder.
3. Scenario Setup:
 - **Scenario 1: Budget Management**
The Bank Manager needs to allocate the annual budget for various bank operations, including loan disbursements, branch openings, and marketing. The group must discuss and decide on the best way to allocate the budget efficiently, ensuring they cover all necessary areas without overspending.
 - **Scenario 2: Handling Transactions**
The Customer Service Representative will handle a series of customer transactions, such as deposits, withdrawals, and transfers. They need to ensure that each transaction is processed accurately and efficiently. The group should discuss how to handle discrepancies and ensure all transactions are recorded precisely.
4. Each group presents their scenario and the strategies they discussed. Focus on how they addressed precision, budgeting, and customer service in their roles.



2.0 Understanding Fractions, Decimals, and Percentages for Business Applications

Now that you have learned about basic arithmetic operations such as addition, subtraction, multiplication, and division, this section will guide you in understanding the fundamental concepts of fractions, decimals, and percentages. The table below provides definitions, types, and examples of each concept, offering a foundation to analyse profitability and interest rates and interpret and present financial data accurately. This knowledge will help you make informed decisions in real-life scenarios.

2.1 Review Table: Understanding the Types, Examples, and Conversion of Fractions, Decimals, and Percentages

Concept	Definition	Types	Example	Conversion
Fraction	A number that represents a part of a whole.	Proper Fraction: The numerator is smaller than the denominator.	$\frac{3}{4}, \frac{2}{5}, \frac{1}{3}$	To Decimal: Divide the numerator by the denominator To Percentage: Convert to decimal and then multiply by 100.
		Improper Fraction: The numerator is greater than or equal to the denominator.	$\frac{3}{2}, \frac{7}{4}, \frac{9}{6}$	
		Mixed Fraction: A combination of a whole number and a proper fraction.	$2\frac{1}{3}, 4\frac{2}{3}, 8\frac{1}{2}$	
Decimal	A precise way to express fractions of a whole number or amounts less than one.	Terminating Decimal: A decimal that ends after a finite number of digits.	0.5, 0.75, 0.125, 2.4	To Fraction: Write the decimal as a fraction with a denominator of 1. Multiply both the numerator and denominator by a power of 10. Simplify the fraction by dividing both the numerator and the denominator by their greatest common divisor. To Percentage: Multiply the
		Repeating Decimals: A decimal where a group of digits repeats infinitely.	0.3333, 1.666, 0.5555	

				decimal by 100 and add the per cent symbol (%).
Percentage	A number is expressed as a fraction of 100.		25%, 30%, 90%, 45%	To Decimal: Divide the percentage by 100. To Fraction: Write the percentage as a fraction with a denominator of 100. Simplify the fraction by dividing both the numerator and denominator by their greatest common divisor.

2.2 Application of Fractions in Business and Banking Context

Fractions are widely used in business and banking operations.

1. They help calculate ratios, such as profit margins.
2. They are used to allocate resources and predict future financial performance.
3. Fractions assist in computing interest rates and loan repayments.
4. They break down complex data into manageable parts, facilitating better decision-making.

Here are some of the key applications of fractions:

I. Stock Market Investment - Fractions are commonly used to represent the ownership of a person or entity in the company through shares. When investors purchase shares, they are given a fraction of the shares, which indicates their proportionate ownership in the company. This fractional representation helps to clarify each person's or entity's stake and influence within the company.



Stock Market

The stock market is where shares of companies and other financial instruments are bought and sold.

Example

An investor buys 20 shares out of a total of 100 shares from ABC Company. The fraction of shares owned by the investor is $\frac{20}{100}$. This fraction represents the investor's ownership stake in the company, showing that they own **20%** of the total shares.

II. Calculating Interest Rate - Banks use fractions to determine the interest rates for loans and fixed deposits. While interest rates are often expressed as percentages, fractions are essential for accurately determining interest charges over various time periods. By using fractions, banks can precisely calculate interest amounts, ensuring fair and accurate financial transactions for both borrowers and depositors.

Example

A bank is offering a fixed deposit with an annual interest rate of 6%. For a customer planning to invest money for 6 months, the bank calculates the interest rate for that period $\frac{6\%}{2}$ which equals **3%**. This is because 6 months is half of a year, so the interest for 6 months is half of the annual rate.

A. Calculating Simple Interest: Simple interest is a basic method of calculating interest that is applied only to the principal amount of a loan or investment. It is calculated as a percentage of the principal amount over a certain period. The formula for calculating simple interest is:

$$\text{Simple Interest, } S.I = \frac{P \times R \times T}{100}$$

Where:

- P is the principal amount (initial investment or loan amount).
- R is the annual interest rate (expressed as a fraction).
- T is the time period (in years).

Example

If you invest ₹10,000 in a savings account with a simple interest rate of 6% per year for 3 years, the interest earned would be:

$$P = ₹10,000$$

$$R = 6\%$$

$$T = 3 \text{ years}$$

$$\text{Simple Interest (SI)} = \frac{P \times R \times T}{100}$$

$$\begin{aligned}
 &= \frac{10000 \times 6 \times 3}{100} \\
 &= \frac{180000}{100} \\
 &= 1,800
 \end{aligned}$$

Thus, the interest earned will be **₹1,800**

B. Calculating compound interest: Compound interest is a method of calculating interest where interest is earned on both the initial principal amount and the accumulated interest of previous periods.

$$\text{Compound amount, } A = P \times \left(1 + \frac{r}{n}\right)^{nt}$$

Where:

- A is the amount of money accumulated after t years, including interest.
- P is the principal amount (initial investment or loan amount).
- r is the annual interest rate (expressed as a decimal).
- n is the number of times interest is compounded per year.
- t is the time the money is invested or borrowed for (in years).

Example

If you invest ₹10,000 in a savings account with an annual compound interest rate of 6% for 3 years, the value of your investment would be

$$A = P \times \left(1 + \frac{r}{n}\right)^{nt}$$

$$P = ₹10,000$$

$$r = 6\% = \frac{6}{100} = \frac{3}{50}$$

$$n = 1 \text{ (Compounded annually)}$$

$$t = 3$$

So, according to the formula:

$$A = 10,000 \times \left(1 + \frac{\frac{3}{50}}{1}\right)^{1 \times 3}$$

$$A = 10,000 \times \left(1 + \frac{3}{50}\right)^3$$

$$A = 10,000 \times \left(\frac{53}{50}\right)^3$$

$$A = 10,000 \times \left(\frac{148877}{125000}\right)$$

$$A = 10,000 \times 1.191016$$

$$A = 11,910.16$$

Thus, the value of your investment is **₹11,910.16**

III. Fractional Reserve Ratio: The Reserve Bank of India requires all banks to maintain a fractional reserve system. This means that banks must keep a fraction of their deposits as reserves and can lend out the remaining amount to customers. This system is designed to ensure liquidity and stability in the banking sector.



Liquidity

Liquidity refers to a bank's ability to easily convert assets into cash to meet immediate financial needs.

Example

If the cash reserve ratio set by the RBI is 4%, this means that the bank must keep 4% or $\frac{4}{100}$ of its total deposits in reserve. For instance, if a bank has total deposits of ₹1,00,000, it must keep $\frac{4}{100} \times 1,00,000 = \text{₹4,000}$ in reserve. The remaining ₹96,000 can then be used for lending and other investments.

IV. Loan Repayment Calculations or EMI: Fractions are used to calculate the EMI (Equated Monthly Instalment) for personal loans, home loans, and other types of loans offered by banks and financial institutions.

$$\text{Equated Monthly Instalment, EMI} = \left[\frac{[P \times R \times (1+R)^N]}{[(1+R)^N - 1]} \right]$$

Where:

- P = Principal or loan amount
- R = Monthly interest rate (annual interest rate divided by 12)
- N = Loan tenure in months

Example

Simran decided to buy a new phone for ₹10,000 on a 1-year loan at an annual interest rate of 10%. Let's calculate how much EMI she would pay monthly.

From the given information,

Loan Amount (Principal) = ₹10,000

Annual Interest Rate = 10%

Loan Tenure = 1 year



Where,

$$P = ₹10,000$$

R = Monthly interest rate

$$R = \frac{\text{Annual Interest}}{12}$$

$$R = \frac{10\%}{12} = \frac{\frac{10}{100}}{12}$$

$$R = \frac{0.1}{12} = 0.00833$$

By using the EMI formula -

$$\left[\frac{[P \times R \times (1+R)^N]}{[(1+R)^N - 1]} \right]$$

$$EMI = \left[\frac{[10000 \times 0.00833 \times (1+0.00833)^{12}]}{[(1+0.00833)^{12} - 1]} \right]$$

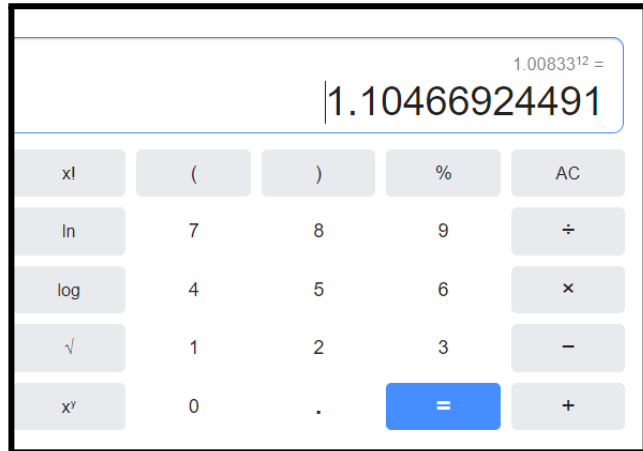
$$= (1 + 0.00833)^{12} = (1.00833)^{12}$$

$$\text{Numerator} = 10,000 \times 0.00833 \times 1.10467 = 92.019011$$

$$\text{Denominator} = 1.10467 - 1 = 0.10467$$

$$EMI = \frac{92.02}{0.10467} = 879.14 (\text{Approx})$$

Thus, Simran has to pay **₹879.14** as EMI every month.



V. Profit and Loss Analysis: Businesses use fractions to analyze the profit/loss margins, which is important in interpreting the financial outcomes. **Profit margin** is a financial ratio that measures the percentage of income remaining after a company deducts all its expenses from its sales revenue.

$$\text{Net Profit Margin} = \left(\frac{\text{Net Profit}}{\text{Revenue}} \right) \times 100.$$

Where:

- **Net Profit** = Total Revenue - Total Expenses (including cost of goods sold, operating expenses, interest, taxes, etc.)
- **Revenue** = Total sales or income generated by the company.

Loss Margin indicates the percentage of revenue that does not cover the total expenses, resulting in a financial loss.

$$\text{Net Loss Margin} = \left(\frac{\text{Net loss}}{\text{Revenue}} \right) \times 100.$$

Where:

- **Net Loss** = Total Expenses - Total Revenue (when expenses exceed revenue).
- **Revenue** = Total sales or income generated by the company.

Example

- If a company earned a profit of ₹15,000 on revenue of ₹1,00,000, the net profit margin is $\left(\frac{15,000}{1,00,000}\right) \times 100 = 15\%$.
- If a company incurred a loss of ₹5,000 on revenue of ₹50,000, the loss ratio is $\left(\frac{5,000}{50,000}\right) \times 100 = 10\%$.



Knowledge Check

1. Company X bought 30 shares from Company Y out of a total of 100 shares. The fraction of shares owned by Company X is _____.
2. The bank offered Rajesh a home loan at an annual interest rate of 6% for 6 months. The bank interest rate for 6 months will be _____.
3. If RBI sets a cash reserve ratio of 5%, the bank must keep _____ fraction of their total deposit in their bank.
4. Reena has a car loan of ₹60 lakhs at an 8% rate of interest for 10 years; the EMI that she will pay monthly is _____.



Answers:

- 1) $\frac{30}{100}$ or $\frac{3}{10}$ 2) 3% 3) $\frac{5}{100}$, $\frac{1}{20}$ 4) ₹72,900.

2.3 Application of Decimals in Business and Banking

Decimals are crucial in the business and banking sectors, as they ensure precision and accuracy in various financial calculations. Their applications include pricing, accounting, interest calculation, preparing accurate financial statements, exchange rate estimation, etc. Decimals help in maintaining the integrity of financial data and decision-making processes. Here are some of the applications of decimals in the business and banking sector.

Currency Exchange: In the global economy, decimals are essential for handling exchange rates. They provide the precision needed for accurate currency conversions and international transactions, ensuring that financial exchanges are conducted with exactness and reliability.

Example

If the exchange rate from USD (US Dollar) to INR (Indian Rupee) is 82.355, then converting \$1,000 to INR would be $1,000 \times 82.355 = \mathbf{82,355 \text{ INR}}$.

Decimals are crucial here, as they ensure accurate currency conversion and prevent errors in financial transactions.

Interest calculations: Banks use decimals to calculate interest rates, ensuring accuracy in financial products such as savings accounts, loans, and investments.

i) Using decimals for calculating Simple Interest:

$$\text{Simple Interest } S.I = P \times R \times T$$

Where,

- P is the principal amount (initial investment or loan amount).
- R is the annual interest rate (expressed as a decimal).
- T is the time period (in years).

Example

If you invest ₹40,000 in a savings account with a simple interest rate of 5% per year for 3 years, the interest earned would be:

$$P = ₹40,000$$

$$R = 5\% = \frac{5}{100} = 0.05$$

$$T = 3 \text{ years}$$

$$\text{So, } S.I = P \times R \times T$$

$$S.I = 40,000 \times 0.05 \times 3 = 6,000$$

Thus, the interest earned would be **₹6,000**.

ii) Using decimals for calculating Compound Interest (C.I):

$$\text{Compound Interest } C.I. = P \left(1 + \frac{r}{n} \right)^{nt} - P$$

Where,

- P is the principal amount (initial investment).
- r is the annual interest rate (expressed as a decimal).
- n is the number of times that interest is compounded per year.
- t is the time in years.

Example

If you invest ₹40,000 in a savings account with an annual compound interest rate of 5% for 3 years, how much compound interest will you earn?

$$A = P \times \left(1 + \frac{r}{n}\right)^{nt}$$

$$P = ₹40,000$$

$$r = 5\% = \frac{5}{100} = 0.05$$

$$n = 1 \text{ (Compounded Annually)}$$

$$t = 3$$

So, according to the formula:

$$C.I = 40,000 \times \left(1 + \frac{0.05}{1}\right)^3 - 40,000$$

$$C.I = 40,000 \times (1.05)^3 - 40,000$$

$$C.I = 40,000 \times (1.157625) - 40,000$$

$$C.I = 46,305 - 40,000 = 6,305$$

The total amount after three years is **₹6,305**.

Bank fees and charges: Banks use decimals to accurately calculate various fees, such as transaction charges and service fees. This precision ensures transparency and fairness in financial transactions, allowing customers to clearly understand the costs associated with their banking activities.

Example

A bank charges a fee of 0.7% for international transactions. If the transaction amount is ₹2,00,000, to calculate the fee:

- The percentage will be converted to a decimal $0.7\% = 0.007$.
- The fees for the transfer will be $2,00,000 \times 0.007 = \text{₹1,400}$.

Accounting and Bookkeeping Calculation: Decimals are crucial in accounting and bookkeeping as they provide the precision needed to accurately track income, expenses, assets, and liabilities. Using decimals ensures that every cent is accounted for correctly, maintaining the integrity and accuracy of financial statements.

Example

Riya Ltd needs to prepare an account of total assets with the information given below:

- Cash: ₹2,50,000.75
- Account receivable: ₹1,50,000.50
- Inventory: ₹3,75,000.25.

Total assets will be calculated as = ₹2,50,000.75 + ₹1,50,000.50 + ₹3,75,000.25
= ₹7,75,001.50.

Therefore, the total assets for Riya Ltd will be **₹7,75,001.50**.

Stock Price and Changes: Decimals are essential for accurately representing stock prices and tracking their fluctuations. They allow for precise pricing and detailed monitoring of stock market movements, ensuring that investors can make informed decisions based on exact price information.

Example

If you bought 100 shares of Tia Company at ₹3500.75 per share and later decided to sell them at ₹4576.50 per share, the profit you would make is:

- **Calculating the total selling price**

Total Selling Price = Selling Price per Share × Number of Shares

Total Selling Price = ₹4576.50 × 100 = ₹4,57,650

- **Calculating the total purchasing price**

Total Purchasing Price = Purchase Price Per Share × Number of Shares

Total Purchasing Price = ₹3500.75 × 100 = ₹3,50,075

Profit = Total Selling Price – Total Purchase Price

Profit = 4,57,650 – 3,50,075 = 1,07,575

Thus, the profit from the transaction is **₹1,07,575**.

**Knowledge Check**

1. Isha is planning a trip to the United States and needs to exchange ₹50,000 for USD. With an exchange rate of 1 USD = ₹83.75, how much USD will she receive for ₹50,000?
2. Priya invested ₹1,50,000 in a fixed deposit with an annual interest rate of 6.2%, compounded annually. Calculate the total amount she will have in the account after 3 years.

3. The bank charges a transaction fee of 0.5% for all international transactions. If Rekha wants to send ₹2,00,000 abroad to her friends, what will be the transaction fee charged by the bank?
4. Hiya Pvt. Ltd is preparing its financial statements for the year. The company has the following assets. Calculate the total assets of Hiya Pvt. Ltd with accurate decimal places:
 - Cash: ₹3,75,000.4587
 - Accounts Receivable: ₹2,50,000.30
 - Inventories: ₹4,50,000.80
5. Fida invested in 200 shares of XYZ Corporation at a price of ₹2,350.44 per share. After 4 months, she sold the shares at ₹2,780.90 per share. Calculate the profit she made from selling all the shares.



Answers:

1. \$597.01, 2. ₹1,79,665.54, 3. ₹1000 4. ₹10,75,001.5587, 5. ₹86,092

2.4 Application of Percentages in Business and Banking

Percentages play a crucial role in both the business and banking sectors. They are used to:

- **Calculate Profit and Loss:** Companies use percentages to determine profit or loss margins on goods sold, helping them assess performance and make strategic decisions.
- **Perform Data Analysis:** Percentages help in analysing market trends, customer behaviour, and sales performance, allowing businesses to make informed decisions.
- **Manage Finances:** Businesses use percentages to manage budgets, forecast financial performance, and allocate resources effectively.
- **Negotiate Contracts:** When negotiating deals, companies can discuss profit-sharing percentages or distribution rates to secure favourable terms.

Here are some examples of how percentages are applied in business and banking functions:

Interest Rates: Percentages are essential for calculating interest rates on loans, fixed deposits, and savings accounts. These rates, expressed as percentages, determine the cost of borrowing and the return on investments.

Example

If Diya takes out a loan of ₹5,00,000 with an annual interest rate of 8%, the interest amount that needs to be paid in a year can be calculated using the simple interest formula:

$$\text{Interest Amount} = P \times \frac{R}{100} \times T$$

$$= ₹5,00,000 \times \frac{8}{100} \times 1$$

$$= ₹40,000$$

Thus, the interest amount is **₹40,000**

Investment returns: The Return on Investment (ROI) is a key metric used by businesses to evaluate the profitability of an investment. ROI is calculated by dividing the net profit or loss from the investment by the initial cost of the investment. This percentage reflects the efficiency and profitability of the investment, helping businesses make informed decisions.

$$ROI = \left(\frac{\text{Net Profit}}{\text{Initial Investment}} \right) \times 100$$

Example

If Priya had invested ₹50,000 in a mutual fund, and after a year, the value of the investment grew up to ₹60,000

$$ROI = \left(\frac{\text{Net Profit}}{\text{Initial Investment Cost}} \right) \times 100$$

$$ROI = \left(\frac{\text{Final Value} - \text{Initial Investment}}{\text{Initial Investment Cost}} \right) \times 100$$

$$ROI = \frac{60,000 - 50,000}{50,000} \times 100 = 20\%$$

This indicates a **20%** return on the initial investment, showing the investment's effectiveness in generating profit.

Pricing Strategies: Businesses use percentages to calculate and apply discounts to attract customers, or to set markups to ensure a desired profit margin. **Markups** refer to the amount added to the cost price of a product to determine its selling price.

Example

A product is priced at ₹45,000 with a discount rate of 20%. To find the final price:

$$\text{Discount} = \text{Original Price} \times \text{Discount Rate}$$

$$\text{Discount} = ₹45,000 \times \frac{20}{100} = ₹9,000$$

Thus, the final price will be ₹45,000 - ₹9,000 = **₹36,000**.

Analysing Market Share: Percentages are crucial for companies to understand their position in the industry relative to competitors. Market share is expressed as a percentage and indicates how much of the total market sales a company controls.

Example

If a company has sales of ₹25,000 in a market where the total sales amount to ₹4,00,000, the company's market share is:

$$\begin{aligned}\text{Market Share} &= \left(\frac{\text{Company's Sales}}{\text{Total Market Sales}} \right) \times 100 \\ &= \frac{25,000}{4,00,000} \times 100 = 6.25\%\end{aligned}$$

Thus, the market share of the company is **6.25%**

Cost Control: Businesses use percentages to analyze and manage expenses effectively. By expressing costs as a percentage of revenue or total expenses, companies can set spending limits, monitor procurement efficiency, and manage inventory effectively.

Example

If a company had total expenses of ₹50,00,000 in a year and spent ₹7,50,000 on marketing, the percentage of expenses allocated to marketing is calculated as:

$$\begin{aligned}\text{Percentage of Marketing Expenses} &= \frac{\text{Marketing Expenses}}{\text{Total Expenses}} \times 100 \\ &= \frac{7,50,000}{50,00,000} \times 100 = 15\%\end{aligned}$$

Thus, the marketing expenses constitute **15%** of the total expenses.

**Knowledge Check**

1. A bank is taking out a loan of ₹5,00,000 with an annual interest rate of 4%. What will be the total interest amount for the year?
2. A company invested ₹1,00,000 in a product, and by the end of the year, the sales revenue from the product reached ₹1,20,000. Calculate the return on investment (ROI) for this product.
3. Shriya Electronics is offering a 15% discount on all products at the end-of-the-season sale. Rehana bought a TV originally priced at ₹80,000. What will be the final price of the TV after applying the discount?
4. A company has total expenses of ₹10,00,000, with ₹20,000 spent on marketing. What percentage of the total expenses was allocated to marketing?



Answers - 1. ₹20,000 2. 20% 3. ₹68,000 4. 2%

3.0 Ratios and Proportions in Business Applications

Ratios and proportions are fundamental mathematical concepts that play a crucial role in business management and decision-making. They are used to relate and compare different quantities, helping businesses analyse performance, manage resources, and make informed decisions.

3.1 Ratios and Proportions

Ratios are a way to compare two or more quantities that have the same unit. They are often expressed as fractions or using a colon (:) or the word "to". A ratio of **a:b** can be represented as **a/b**.

Example: If the ratio of a bank's assets to liabilities is 3:1, it means that for every ₹3 in assets, the bank has ₹1 in liabilities. Mathematically, this can be represented as:

$$\text{Ratio} = \frac{\text{Assets}}{\text{Liabilities}}$$

Proportions involve two ratios that are set equal to each other. If two ratios are proportional, their cross-products are equal. This concept can be represented using the symbols "::" or "=". For instance, if the ratio of assets to liabilities is 3:1 and another ratio is 6:2, these ratios are proportional because:

$$\frac{3}{1} = \frac{6}{2}$$

This indicates that the relationship between assets and liabilities is consistent across different scenarios.

In summary, ratios help in comparing quantities, while proportions establish the equality between two ratios.

3.2 How to Check the Financial Health of a Bank Using Ratios

Example

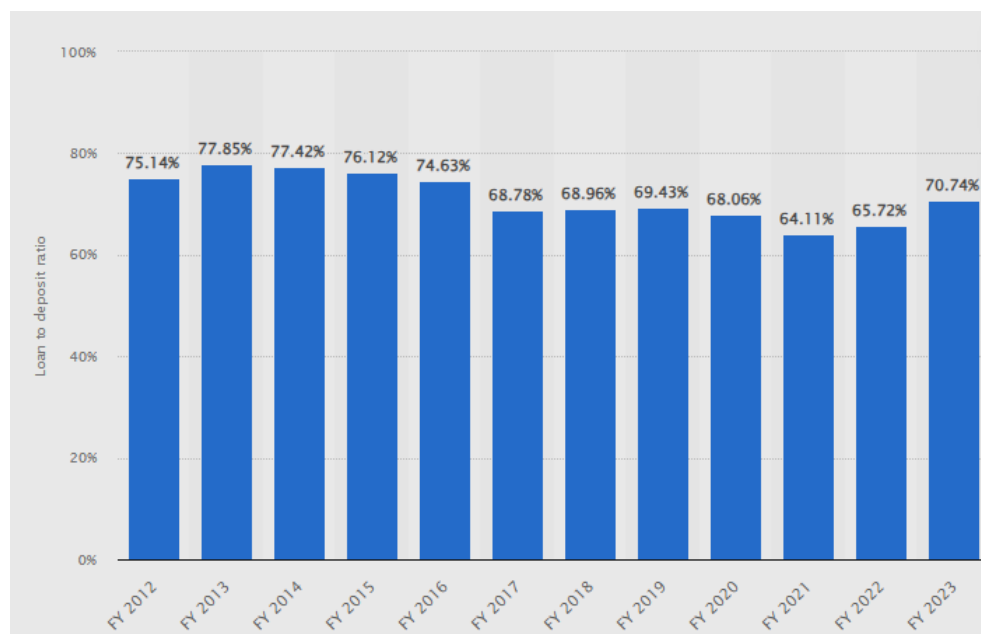
The **credit-to-deposit ratio** in India for the financial year 2023 was over 70% (Statista, 2023), reflecting an increase from the previous year. This ratio is a crucial indicator of a bank's financial health and liquidity. It measures the proportion of a bank's deposits that are being used for lending.

A high credit-to-deposit ratio suggests that a significant portion of the bank's available funds is being utilised for loans, which could potentially lead to liquidity issues if not managed properly. On the other hand, a low ratio may indicate that the bank is not efficiently using its funds to generate income through loans, which could impact its profitability and growth.



Assets & Liabilities

Assets are resources your business owns. Liabilities are what your business owes to external parties.



(Source: Statista. (2023, December 12). *Loan to deposit ratio of public sector banks in India FY 2012-2023*.
<https://www.statista.com/statistics/794872/india-loan-to-deposit-ratio-of-public-sector-banks/>)

3.3 Banking Ratios



The **Current Account Savings Account or CASA Ratio** is a key metric used to assess a bank's deposit structure. It represents the proportion of deposits held in current and savings accounts compared to the total deposits of the bank.

$$\text{CASA Ratio} = \frac{\text{Current Account Deposits} + \text{Savings Account Deposits}}{\text{Total Deposits}}$$

Example

Suppose a bank's total deposits amount to ₹2,00,000 crores. Out of this, ₹50,000 crores are held in current accounts, and ₹1,00,000 crores are held in savings accounts.

Using the CASA ratio formula:

$$\begin{aligned} \text{CASA Ratio} &= \frac{\text{Current Account Deposits} + \text{Savings Account Deposits}}{\text{Total Deposits}} = \frac{₹50,000 + ₹1,00,000}{₹2,00,000} \\ \text{CASA Ratio} &= \frac{₹1,50,000}{₹2,00,000} = 0.75 \end{aligned}$$

A CASA Ratio of **0.75**, or 75%, indicates that **75%** of the bank's total deposits are held in current and savings accounts. This suggests a cost-effective deposit base for the bank, as savings accounts have a lower interest cost, and current accounts bear no interest at all.

Note: **Current Accounts** and **Savings Accounts** generally offer lower interest rates compared to fixed deposits. As a result, funds in these accounts are less expensive for the

bank to maintain. A higher CASA ratio indicates that a larger portion of the bank's deposit base is made up of these low-cost accounts, which is beneficial for the bank's profitability.



Discuss

Research online and discuss in class the advantages and disadvantages of both high and low CASA ratios for banks. How do these ratios impact a bank's profitability and overall financial health?



Low Cost

Low Cost refers to the lower interest rates that banks typically offer on deposits in current and savings accounts compared to other types of deposits, such as fixed deposits.



The **Net Interest Margin (NIM) Ratio** is a key profitability ratio used to measure the difference between the interest income generated by banks from their loans and investments, and the interest they pay out on deposits and other borrowings.

$$\text{Net Interest Margin(NIM) Ratio} = \frac{\text{Interest Earned} - \text{Interest Paid}}{\text{Earning Assets}} \times 100$$

Example

Assume Bank ABC has a loan interest income of ₹10,00,000, a deposit interest expense of ₹20,00,000, and average earning assets of ₹1,00,00,000.

- Loan Interest Income of ₹10,00,000: This is the amount the bank has earned by lending money to its customers.
- Deposit Interest Expense of ₹20,00,000: This is the amount the bank pays to its customers for keeping their money in savings accounts, fixed deposits, or other deposit accounts.
- Average Earning Assets of ₹1,00,00,000: This refers to the average value of assets (like loans, investments, etc.) that generate income for the bank.

According to the formula,

$$\text{Net Interest Margin(NIM) Ratio} = \frac{\text{Interest Earned} - \text{Interest Paid}}{\text{Earning Assets}} \times 100$$

Here, Interest Earned: ₹10,00,000 (Loan Interest Income)

And, Interest Paid: ₹20,00,000 (Deposit Interest Expense)

So, Interest Earned - Interest Paid = ₹10,00,000 - ₹20,00,000 = -₹10,00,000

$$\text{Net Interest Margin (NIM) Ratio} = \frac{-₹10,00,000}{₹1,00,00,000} \times 100$$

ABC's Net Interest Margin (NIM) is **-10%** in this scenario.

This negative NIM indicates that the bank is losing money because it is paying more in deposit interest expenses than it is earning from its interest income on loans.



The **Loan-to-Deposit Ratio (LDR)** is used to assess a bank's liquidity by comparing a bank's total loans to its total deposits for the same period. To calculate the loan-to-deposit ratio, divide a bank's total amount of loans by the total amount of deposits for the same period.

$$\text{Loan - to - Deposit Ratio (LDR)} = \frac{\text{Total Loans}}{\text{Total Deposits}}$$

Example

If a bank has ₹500 crore in deposits and ₹400 crore in loans, the bank's LDR ratio would be calculated by dividing the total loans by its total deposits.

$$\text{Loan - to - Deposit Ratio (LDR)} = \frac{₹400 \text{ crores}}{₹500 \text{ crores}} = 0.80$$

So, the LDR Ratio is **80%**



Knowledge Check

Research Question:

1. Which banks in India had the lowest Loan-to-Deposit Ratios in 2023.
2. How do changes in the Loan-to-Deposit Ratio affect a bank's ability to lend?

3.3.1 Profitability Ratios

Profitability ratios are key financial metrics used to assess a company's ability to generate profit in relation to its sales, assets, and equity.

Return on Assets (ROA)	Return on Equity (ROE)
ROA measures how efficiently a bank uses its assets to generate profit. It is calculated by dividing the net income by the total assets.	ROE evaluates the profitability relative to shareholders' equity, showing how effectively a company is using the shareholders' funds to generate profit. It is calculated by dividing net income by shareholders' equity.

$$\text{ROA Formula: } ROA = \frac{\text{Net Income}}{\text{Total Assets}}$$

$$\text{ROE Formula: } ROE = \frac{\text{Net Income}}{\text{Shareholder's Equity}}$$

Example



Amar: Hi Simran, I was looking at some financial statements, and I'm confused about assets and equity. Can you explain the difference?

Simran: Sure, Amar! Think of assets as everything a company owns, like cash, buildings, or equipment.

Amar: Okay, so what about equity?

Simran: Equity is the value left after subtracting all the company's debts from its total assets. It represents the owner's share in the company. If a company had no debt, the

assets and equity would be the same.

Amar: Ah, I get it now. Assets are what we have, and equity is what's left for the owners after paying off all the debts.



What does return on equity tell you?

BANKS	ROA		ROE	
	Last 1-Yr	10-Yr Avg	Last 1-Yr	10-Yr Avg
➤ HDFCB	1.78%	1.69%	15.27%	16.62%
ICICI	1.32%	1.21%	10.98%	9.85%
Kotak	1.65%	1.25%	12.13%	9.52%
Axis	0.66%	0.99%	6.48%	10.49%
IndusInd	0.78%	1.44%	6.54%	13.68%
➤ Bandhan (7Yr)	1.92%	2.41%	12.67%	13.96%
IDBI	0.46%	-1.14%	3.69%	-12.16%
Yes	-1.27%	0.29%	-10.43%	5.35%
➤ AU Small (5Yr)	2.27%	3.00%	18.66%	20.06%
Federal	0.85%	0.95%	10.63%	10.57%
City Union	0.96%	1.40%	8.99%	16.13%
RBL	0.50%	0.77%	4.01%	7.55%

More Greens
(the lot looks better)

(Source: <https://getmoneyrich.com/compare-indian-banks/>)

NOTE: This is only a reference image. The values of ROA (Return on Assets) and ROE (Return on Equity) are subject to change depending on how well a business is performing and market conditions. These percentages can fluctuate with changes in business performance and external factors.

- A business with a high ROE is profitable and generates earnings with equity.

- A higher ROE indicates better asset and resource management.
- Investors widely use the ROE to assess a company's growth prospects.

3.3.2 Growth Rates

Growth rates measure how a company's sales, earnings, or other financial metrics increase over time, reflecting its overall growth trajectory.

Asset Growth Rate
<p>This measures the rate at which a bank's assets have increased or decreased over a period of time.</p> $\text{Asset Growth Rate} = \frac{\text{Current Year Assets} - \text{Previous Year Assets}}{\text{Previous Year Assets}} \times 100$
Loan Growth Rate
<p>This measures the change in the total amount of loans a bank issues to customers.</p> $\text{Loan Growth Rate} = \frac{\text{Current Year Loans} - \text{Previous Year Loans}}{\text{Previous Year Loans}} \times 100$

3.3.3 Earnings Growth Rate

The earnings growth rate measures the percentage increase in a bank's earnings over a specific period.

$\text{Earnings Growth Rate} = \frac{\text{Current Period Earnings} - \text{Previous Period Earnings}}{\text{Previous Period Earnings}} \times 100$

Why is Earnings Growth Rate Important?

The Earnings Growth Rate is crucial for investors as it provides insights into a company's financial health and growth potential. It helps investors:

- Evaluate and compare the growth rates of different companies to identify which ones are performing better.
- Measure a company's current earnings growth against its historical performance to understand its trajectory.
- Compare a company's earnings growth with the average growth rate of its industry or sector to gauge its relative performance.

Mastering financial ratios and growth metrics is key to evaluating a bank's performance. These tools help investors and managers make informed decisions and improve financial strategies.

Let's Recap

1. Understanding arithmetic operations like **addition, subtraction, multiplication, and division**, and the importance of **being precise** with calculations, is essential for managing personal finances in banking.
2. Managing personal finances in banking includes **calculating interest and fees in the account, handling bank transactions with precision, calculating loan repayment**, and **effective budgeting in banking**.
3. **Fractions** are used as numbers that represent a **part of the whole**. They are used in stock market investments, calculating ratios, profit margins, interest rates, fractional reserve ratios, and loan repayment calculations.
4. **Decimals** are used to express a **fraction of a whole number in value less than one**. They are used in exchanging currency, interest calculation, calculating bank fees, and accounting and bookkeeping for both business and banking perspectives.
5. **Percentages** are used to **express a fraction of 100**. They are used to express interest rates, return on investment, pricing strategies, and analyse market shares and cost control during inventory management, which will increase profitability.
6. **Ratios and Proportions** are used in business to check the financial health of a bank, by using various indicators like **credit-to-deposit ratios, CASA ratio**, and **Net Interest Margin (NIM) Ratio**.
7. **Profitability Ratios** are used to measure a company's profit by using **return on assets and return on equity**.
8. **Growth Rates** are used to analyse the company's sales, earnings, and other financial metrics over time by using **asset growth rate** and **loan growth rate**.



EXERCISE

Objective Type Questions**MCO:**

1. Mastering these maths skills will help you to:
 - a. Make informed financial decisions
 - b. Manage accounts accurately
 - c. Optimise investment strategies
 - d. All the above

State- True/False:

2. Budgeting in banking means managing financial resources efficiently.
3. The Loan - to - Deposit Ratio (LDR) is used to assess a bank's liquidity by comparing a bank's total loans to its total deposits for the same period.

Fill in the blanks:

4. In the global economy, _____ are essential for handling exchange rates.
5. _____ refers to the amount added to the cost price of a product to determine its selling price.
6. The _____ market is where shares of companies and other financial instruments are bought and sold.

liquidity by comparing a bank's total loans to its total deposits for the same period.

7. _____ ratios are key financial metrics used to assess a company's ability to generate profit in relation to its sales, assets, and equity.

Short Answer Type Questions

8. Describe the application of percentages in business and banking.
9. What is the difference between Return on Assets (ROA) and Return on Equity (ROE)?

Long Answer Type Questions

10. Explain the application of fractions in business and banking.
11. Explain the application of decimals in business and banking.

ANSWER KEY

Objective Type Questions**MCO:**

1. d. All the above

State- True/False:

2. True
3. True

Fill in the blanks:

4. Decimal
5. Markup
6. Stock
7. Profitability

NUMERICAL EXERCISE

Objective Type Questions**MCQ:**

1. A bank has a total budget of ₹1 crore for the financial year. They plan to allocate ₹60 lakhs for new loans and ₹10 lakhs for operational expenses. What is the remaining budget after these allocations?
 - a. ₹10 lakhs
 - b. ₹20 lakhs
 - c. ₹30 lakhs
 - d. None of these
2. Amarjit starts with ₹40,000 in her savings account. She makes the following transactions: a withdrawal of ₹3,000, a deposit of ₹2,000, and another withdrawal of ₹500. What is Amarjit's current balance?
 - a. ₹20,000
 - b. ₹38,500
 - c. ₹39,000
 - d. None of these
3. A bank charges a fee of 0.6% for international transactions. If the transaction amount is ₹2,00,000, calculate the amount of the fee.
 - a. ₹1,200
 - b. ₹1,400
 - c. ₹1,800
 - d. None of these
4. If a company has sales of ₹25,000 in a market where total sales amount to ₹4,00,000, the company's market share is:
 - a. 7.25%
 - b. 6.25%
 - c. 8.25%
 - d. None of these

Fill in the blanks:

5. Company X bought 40 shares from Company Y out of a total of 100 shares. The fraction of shares owned by Company X is _____.
6. If RBI sets a cash reserve ratio of

5%, the bank must keep _____ fraction of their total deposit in their reserve.

One line answer:

7. Sahib Ltd needs to calculate its total assets based on the following information: Cash: ₹2,50,000.50
Account receivable: ₹1,50,000.50
Inventory: ₹3,75,000.25. What is the total value of the company's assets?
8. Tejinder plans to travel to the United States and needs to exchange ₹80,000 for USD. If the exchange rate is ₹83.75 per USD, how many dollars will he receive?

Short Answer Type Questions

9. A bank has allocated a budget of ₹5 crore for installing new ATMs across the city. They have already spent ₹1.5 crore on installing 30 ATMs. How much of the budget is left for installing the remaining ATMs, and what is the average cost per ATM if the remaining budget is to be divided equally among 20 new ATMs?
10. A bank charges an account service fee of ₹16 per month and a transaction fee of ₹0.90 per transaction. If a customer makes 15 transactions in a month, what will be the total fees paid by the customer for that month?
11. If Maninderpal invests ₹50,000 in a savings account with a simple interest rate of 5% per year for 3 years, calculate the amount of interest.
12. Harsimrat buys 200 shares of XYZ Corporation at a price of ₹2,340.44 per share. After 4 months, she sold the shares at ₹2,780.90 per share. Calculate the total profit from selling all the shares.
13. A product is priced at ₹48,000 with a discount rate of 20%. Find out the final price.

Long Answer Type Questions

14. Raman has availed a loan of ₹10 lakhs to build a house at a 7.2% rate of interest for 10 years. Calculate the monthly EMI for the loan.
15. Mr. Ranbir Singh invested ₹80,000 in a savings account with an annual compound interest rate of 5% for 3 years. Calculate how much compound interest he will earn?
16. a. A bank takes a loan of ₹6,00,000 with an annual interest rate of 4%. What will be the total interest amount for the year?
b. A company invested ₹1,00,000 in a product, and by the end of the year, the sales revenue from the product reached ₹1,30,000. Calculate the return on investment (ROI) for this product.
17. A bank's total deposits amount to ₹3,00,000 crores. Out of this, ₹50,000 crores are held in current accounts, and ₹1,00,000 crores are held in savings accounts. Calculate the CASA ratio.

NUMERICALS ANSWER KEY

Objective Type Questions

MCQ:

1. c. ₹30 lakhs
2. b. ₹38,500.
3. a. ₹1,200
4. b. 6.25%

Fill in the blanks:

5. 40/100 or 4/10
6. 5/100, 1/20

One line answer:

7. The total value of the company assets is ₹7,75,001.25.
8. Tejinder will receive 955.22 USD.

Short Answer Type Questions

9. The remaining budget for the ATMs is ₹3.5 crore, and the average cost per ATM is ₹17.5 lakhs.
10. The total fees : ₹29.50.
11. ₹7,500
12. ₹88,092
13. ₹38,400

Long Answer Type Questions

14. ₹11,714
15. ₹12,610
16. a. ₹24,000; b. 30%
17. 0.50

**Topics**

- Basics of Insurance: Meaning of Insurance, Insurer and Insured
 - What is Insurance?
 - Insurance Premium
 - Key Components of Insurance
 - Factors Affecting Life and Health Insurance Premiums
 - Significance of Insurance
- Types of Insurance Products
 - Life Insurance
 - Understanding Life Insurance: Purpose and Benefits
 - Types of Life Insurance Policies
 - Benefits and Limitations of Life Insurance
 - Health Insurance
 - Coverage Details
 - Preventive Care Benefits
 - Exclusions and Limitations
 - Benefits of Health Insurance
 - Property Insurance
 - Benefits of Property Insurance
 - Types of Property Insurance
 - Liability Insurance
 - Benefits of Liability Insurance
 - Types of Business Insurance Coverage



Learning Objectives

- Understand the fundamental concept of insurance and its importance in managing risks.
- Differentiate between various types of insurance products such as life insurance, health insurance, property insurance, and liability insurance.



Materials Required

- Samples of insurance policies or policy documents.
- News Paper Cutouts: Collect real-life stories or news articles related to insurance claims.
- Sample of Health, Life, Property, and Liability insurance pamphlets or brochures



Activity 1: Before We Begin!

1. What are some risks or uncertainties in life that people might want to protect themselves against?

1.0 Basics of Insurance: Meaning of Insurance, Insurer and Insured

1.1 What is Insurance?

Insurance is a contractual agreement between an **individual (policyholder)** and an **insurance company (insurer)**, wherein the insurer agrees to provide **financial compensation** to the policyholder or their beneficiaries in the event of specified losses or damages, in exchange for **premium payments**.



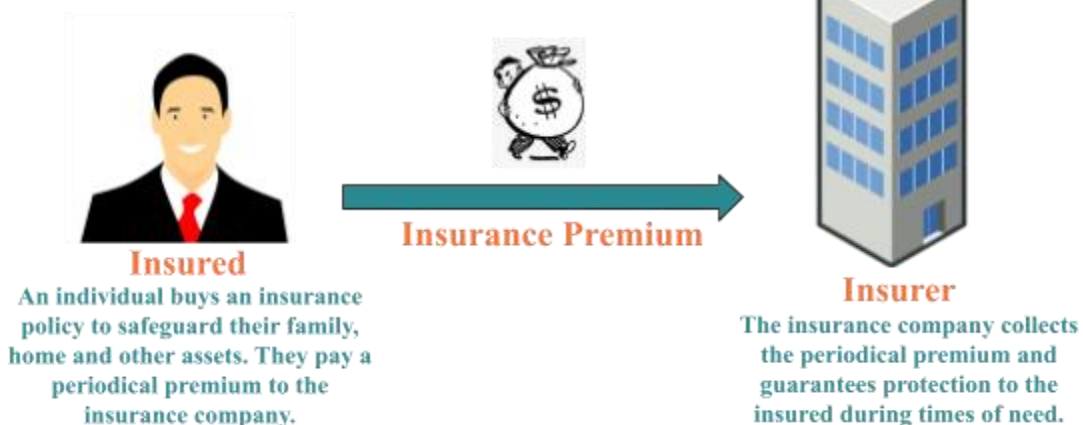
1.2 Insurance Premium

An insurance premium is a fixed amount that you pay to an insurance company at regular intervals. This payment ensures the maintenance of your insurance policy and gives you access to the various benefits. and coverage outlined in your policy.



Beneficiaries

Those who receive benefits from a financial arrangement or will.



1.3 Key Components of Insurance

Policyholder: The individual or entity that purchases an insurance policy and pays premiums to the insurance company.

Example

Sukhdev just bought his first house. He is excited but also aware of the risks, so he decides to get homeowners insurance. Sukhdev now becomes the policyholder, ensuring his new home and personal belongings are protected from any unexpected incidents.



Insurance Company: The entity that provides insurance coverage and assumes the financial risk associated with potential losses.

Example

You must have come across boards like these on the road. Do you recognise what is common in all these boards? All of them talk about various types of insurance. These are the various insurance companies that provide us insurance.

Source: <https://360hoardings.com/west-india/maharashtra/mumbai/Mahim-L.J-Road-DN-Mumbai-Pioneer-105>



Source: <https://www.media4growth.com/campaigns/acko-launches-new-campaign-to-save-consumers-time-and-money-5271>



Premium: The amount paid by the policyholder to the insurance company in exchange for coverage.

Example

Every month, Parvinder keeps Rs. 100 for her health insurance premium. Knowing she's covered for medical expenses and prescriptions if anything unexpected happens. This amount that she sets aside every month is called the premium.



Coverage: The specific risks and events for which the insurance policy provides protection. This can include property damage, liability claims, medical expenses, or loss of income, depending on the type of insurance.

Example

Let's say Sartaj got his vehicle insurance policy. It is like his safety blanket on the road. It covers everything from minor dents to major accidents, ensuring he is protected against damage to his vehicle and any harm caused to others. This is referred to as coverage.



Claim: A formal request made by the policyholder to the insurance company for compensation due to a covered loss or event.

Example

Imagine Kiran Ji dealing with a burst pipe in her home. She has got homeowners insurance. So, she files a claim with her insurance company to get the repairs covered. It is like having a helping hand when things go wrong.



Activity 2: Insurance Role-Playing Game

Objective: To help students understand the roles of policyholders, insurers, and insurance agents in the insurance process.

Instructions:

- Divide the class into small groups.
- Assign each student a role: policyholder, insurer, or insurance agent.

- Present an example to each group, such as filing a claim or purchasing insurance.
- In their groups, students act, taking on their assigned roles.
- Reflect on the experience as a class, discussing the importance of each role and the challenges faced.

Write your reflection on the role-playing activity below:



Knowledge Check




Let us recap the knowledge we have gained so far.

1. True/False: Policyholders buy insurance and pay premiums_____
2. True/False: Insurers provide coverage and handle financial risk_____
3. True/False: Insured is a person or legal entity whose financial losses are covered by the insurance policy_____

Answers: 1. True 2. True 3. True

1.4 Factors Affecting Life and Health Insurance Premiums

Several factors influence insurance premiums, including:

 <p><u>Age and health:</u> Younger and healthier individuals typically pay lower premiums.</p>	 <p><u>Lifestyle choices:</u> Smoking, hazardous occupations, and risky hobbies may lead to higher premiums.</p>	 <p><u>Coverage amount and term:</u> Higher coverage amounts and longer terms often result in higher premiums.</p>
--	--	--







Discuss

Can you name some examples of dangerous occupations that might result in higher life insurance premiums?

Notes: _____



1.5 Significance of Insurance

 <p>Provides financial security and peace of mind to individuals and businesses.</p>	 <p>Helps in reducing financial losses arising from unexpected events such as accidents, illnesses, etc.</p>
 <p>Promotes economic stability by redistributing risks among a large group of people.</p>	 <p>Facilitates long-term savings and investment through various insurance products.</p>

Example



Garima: Hey, meet Livpreet, a talented graphic designer who recently started freelancing. Tell us, Livpreet, what's been your biggest challenge so far?

Livpreet: Hi! Well, I had a bit of a problem when I was diagnosed with a serious illness. It was scary.

Garima: That sounds tough. How did you handle it?

Livpreet: Thankfully, I had good health insurance. It covered my medical bills and even helped with extra expenses during my recovery.

Garima:: Wow, that's a relief. Insurance really came through for you.



Livpreet: Absolutely! It made a huge difference, allowing me to focus on getting better without worrying about finances.

Garima: Thanks for sharing, Livpreet. It's a great reminder of how important insurance can be.

Livpreet: Definitely! It's worth investing in for peace of mind during unexpected times.



Knowledge Check

Let us recap the knowledge we have gained so far.

1. What is the primary purpose of insurance?
 - a. To maximise profits for insurance companies
 - b. To transfer risks and provide financial compensation for losses
 - c. To eliminate the need for financial planning
 - d. To increase the financial burden on individuals and businesses

Answer: b

2.0 Types of Insurance Products

Insurance products refer to financial instruments or contracts offered by insurance companies to individuals or entities, providing protection against specific risks in exchange for premium payments. These products are designed to reduce financial losses or uncertainties arising from unforeseen events. Insurance products typically involve a contract between the insured (the policyholder) and the insurer (the insurance company), outlining the terms, conditions, and coverage details. There are various types of insurance products. Let us look closely at all of them.



Life Insurance: Provides **financial protection** to the insured's beneficiaries in case of the insured's death.

Example: In life insurance, if someone passes away, their family receives financial support from the insurance company. This money can be used for important expenses such as education, living costs, and other needs, ensuring the family's financial stability during a difficult time.



Health Insurance: Covers **medical expenses** and provides financial protection against illnesses and injuries.

Example: With health insurance, when someone falls ill and requires medical attention, the insurance company covers the medical expenses. This relieves the individual and their family from financial worries, allowing them to focus on recovery without financial strain.



Property Insurance: Protects against **damage or loss of property** due to events like fire, theft, or natural disasters.

Example: In property insurance, if a house suffers damage from events like fire or flood, the insurance company bears the cost of repairs or rebuilding. This prevents the property owner from bearing the financial burden of unexpected damages, ensuring their peace of mind.

Note: For natural disaster prone areas the insurance company may not cover damages against natural disaster. Or may charge a high premium to cover losses from natural disasters.



Liability Insurance: Covers **legal liabilities** arising from bodily injury or property damage caused to third parties.

Example: Liability insurance covers situations where someone accidentally causes damage to another person's property. In such cases, the insurance company pays for the repairs, relieving the individual from personal financial responsibility and maintaining good relationships with neighbours or others affected.



Knowledge Check

Choose the correct option:

1. Which type of insurance provides financial protection to the insured's beneficiaries in case of the insured's death?

- A. Health Insurance
- B. Life Insurance
- C. Property Insurance
- D. Liability Insurance

Answers: 1. B

2.1 Life Insurance



Life insurance is a type of insurance product designed to provide financial protection to beneficiaries in the event of the insured person's death. It offers a lump-sum payment, known as the death benefit, to the designated beneficiaries upon the death of the insured. Life insurance helps ensure that loved ones or dependents are



financially supported and can maintain their standard of living after the insured's passing. The image shows a very famous life insurance company 'LIC'.



Activity 3: Recognise Insurance Company



Question 1: Take a moment to think. Have you seen posters, hoardings, and TV advertisements showing this image, or similar ones? Raise your hand if you have one.

Question 2: Can you name another insurance company? Take a moment to think, then raise your hand to respond. _____

Source: <https://www.zeebiz.com/companies/news-max-financial-services-q4-net-profit-slips-64-to-rs-52-crore-234792>

2.1.1 Understanding Life Insurance: Purpose and Benefits




Life insurance serves as a financial safety net, providing peace of mind and security to individuals and their loved ones. Its primary purpose is to offer financial protection to beneficiaries in the event of the insured's death.

Benefits include:

Providing financial support to surviving family members	Covering funeral expenses	Paying off debts and mortgages	Ensuring continuity of lifestyle for dependents
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2.1.2 Types of Life Insurance Policies

Life insurance policies come in various forms, each catering to different needs and financial goals. The three primary types of life insurance policies commonly offered in India are:

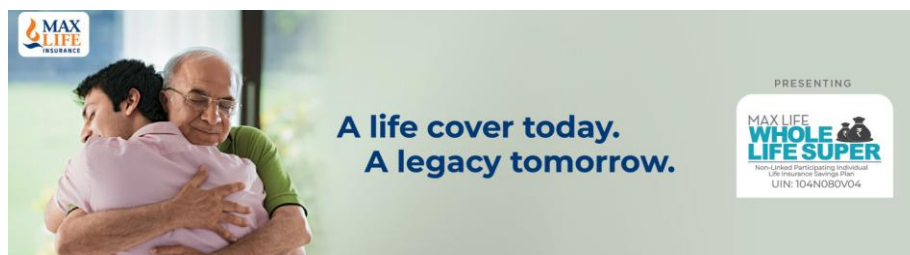
<u>Term Life Insurance:</u>	
	<p>Description: Term life insurance provides coverage for a specified period, known as the policy term. If the insured individual passes away during the term, the policy pays out a death benefit to the beneficiaries. However, if the insured survives the term, there is typically no payout.</p>
<p>Examples: LIC's Tech Term Plan, ICICI Prudential's iProtect Smart, HDFC Life's Click2Protect Life.</p>	<div>   </div>

Whole Life Insurance



Description: Whole life insurance offers coverage for the **entire lifetime** of the insured, as long as premiums are paid. In addition to providing a death benefit to beneficiaries, whole-life policies also collect cash value over time, which policyholders can access through withdrawals or loans.

Examples: LIC's Whole Life Policy, SBI Life's Smart Bachat, Max Life's Whole Life Super.



Endowment Policies



Description: Endowment policies combine life insurance coverage with a savings or investment component. These policies offer a death benefit to beneficiaries in case of the insured's death during the policy term. Additionally, if the insured survives the policy term, the policyholder receives the maturity benefit, which includes the sum assured plus bonuses.

Examples: LIC's New Endowment Plan, HDFC Life's Sampoorn Samridhi Plus, Kotak Life's Endowment Plan.



Knowledge Check

Choose the correct option:

1. Which type of life insurance policy provides coverage for a specified period and pays out a death benefit to beneficiaries if the insured passes away during the term.
 - a. Whole Life Insurance
 - b. Endowment Policies
 - c. Term Life Insurance
 - d. Universal Life Insurance

Answers: c

2.1.3 Benefits and Limitations of Life Insurance

Life insurance offers essential financial protection, it also has its benefits and limitations.

Benefits

- Provides financial security to loved ones
- Offers tax benefits on premiums and death benefits
- Helps cover end-of-life expenses

Limitations

- Premiums can be costly, especially for older individuals or those with health issues
- Exclusions and limitations may apply, such as suicide clauses or pre-existing conditions

Example

Harpreet, a young professional at a big company, got really sick and needed a lot of medical care. But the sudden illness and all the medical bills made it hard for him financially.

Luckily, Harpreet had bought a good health insurance plan. It covered most of his medical costs, like hospital stays, surgeries, and treatments. This insurance was a huge help for Harpreet because it meant he did not have to worry about money while he focused on getting better.



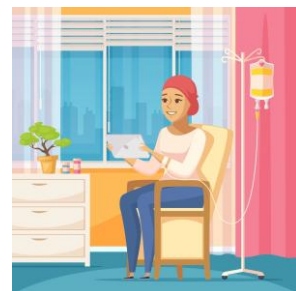
Having health insurance didn't just give Harpreet access to good healthcare. It also gave him peace of mind during a tough time. With the support of his insurance, Harpreet was able to beat his illness and get back to his normal life feeling

confident and strong.

Example

Ritu, a middle-aged individual, decided to purchase a critical illness insurance policy to protect herself against potential health issues. Unfortunately, Ritu was diagnosed with a severe medical condition shortly after purchasing the policy.

When Ritu attempted to file a claim for her medical expenses, she was informed by the insurance company that **the policy had a waiting period clause**, which required her to wait for a specified period before coverage for pre-existing conditions would begin.





Due to the waiting period clause, Ritu was unable to receive coverage for her medical expenses immediately after her diagnosis. This delay in coverage resulted in significant financial strain for Ritu and her family, emphasising the importance of understanding waiting periods and their implications when purchasing insurance policies.

Example

Aman, a young professional, purchased a life insurance policy to secure his family's financial future. Unfortunately, Aman met with an accident while participating in a sports event, resulting in his unexpected death



Upon filing a claim with the insurance company, Aman's family was shocked to discover that **the policy had an exclusion clause for death resulting from hazardous activities** such as extreme sports. Despite paying premiums, the insurance company refused the claim, citing the policy's exclusion clause.



As a result, Aman's family was left without the financial support they had expected from the life insurance policy. This case highlights the importance of carefully reviewing policy terms and exclusions to understand the limitations of coverage provided by life insurance policies.



Knowledge Check

Choose the correct option:

- 1) What is one of the limitations of life insurance policies?
 - a. Life insurance policies are not accessible to middle-aged individuals
 - b. Life insurance policies only provide coverage for medical expenses
 - c. Life insurance policies may have waiting period clauses and exclusions
- 2) Which of the following is a benefit of life insurance?
 - a. Provides financial security to loved ones
 - b. Guarantees investment in high-risk stocks
 - c. Offers discounts on everyday purchases

Answers: 1. c, 2. a



Activity 4: Insurance Agent and Client Interaction

Objective: To help students understand the process of choosing a life insurance policy based on individual needs and goals through role-play interaction.

Instructions:

- Pair up students, assigning one as the insurance agent and the other as the client seeking life insurance.
- Provide an example where the client needs to select the most suitable life insurance policy considering factors like age, income, and family situation.
- Encourage role-play dialogue, with the client sharing their financial details and the insurance agent asking relevant questions to assess needs.
- Based on the information, the insurance agent recommends the best policy, considering coverage, term, and affordability.

2.2 Health Insurance



Health insurance is a form of insurance coverage designed to reduce the financial burden associated with medical expenses resulting from illnesses and injuries. This insurance product provides reimbursement for incurred medical and surgical costs or directly pays the healthcare provider on behalf of the insured individual.

2.2.1 Coverage Details

Health insurance plans typically cover a wide range of medical expenses, including hospitalisation, doctor visits, prescription medications, diagnostic tests, and preventive care services. This comprehensive coverage ensures that individuals have access to necessary healthcare services without worrying about the medical expenses. However, most plans include a co-pay feature, meaning the policyholder pays a fixed percentage of the claim amount, and the insurance company covers the rest. This copay can vary but usually ranges from 10% to 30%. For example, with a 10% co-pay on an Rs. 80,000 claim, the policyholder pays Rs. 8,000 and the insurance company pays Rs. 72,000.

2.2.2 Preventive Care Benefits

Preventive healthcare means taking steps to stay healthy and avoid getting sick. This includes things like eating healthy food, exercising regularly, getting vaccines, and going for regular check-ups with the doctor. The goal is to prevent diseases before they happen, so you can stay healthy and strong.

Health insurance plans often include coverage for preventive care services, such as annual check-ups, vaccinations, and screenings. These services are crucial for maintaining overall

health and detecting potential health issues early. By covering preventive care, health insurance encourages individuals to prioritise their health and well-being.

2.2.3 Exclusions and Limitations

While health insurance plans offer comprehensive coverage, they may have exclusions or limitations on certain services or treatments. For example, cosmetic procedures, elective surgeries, or pre-existing illness may not be covered. Additionally, there is often a maximum insured amount, such as 5 lakhs per year, which is the most the insurance company will pay annually. This limit can be a problem if medical costs exceed this amount, as the insured person will have to pay the extra expenses. It's important for individuals to review their insurance policy carefully to understand what is and what is not covered. This will be discussed in detail in the *Grade 12 chapter Principles & Practice of Insurance*.

Scenario:

Meet Maya, a college student who recently enrolled in a health insurance plan provided by her university. Maya wants to understand how her health insurance works, so she schedules a meeting with the insurance advisor on campus.



Maya: Hi, I am Maya, and I am a bit confused about how my health insurance works. Can you help me understand?

Insurance Advisor: Of course, Maya! Let's start by talking about your health insurance coverage. Your plan is designed to help you pay for medical expenses, such as doctor visits, prescription

medications, and hospital stays.

Maya: That sounds great, but how do I know what's covered and what's not?



Insurance Advisor: Good question! Your insurance policy will have a list of covered services, known as benefits. These typically include things like preventive care, diagnostic tests, and treatments for illnesses and injuries.

Maya: Okay, so if I need to see a doctor, do I have to pay for everything out of pocket?

Insurance Advisor: Not necessarily. Your health insurance includes upto 10 doctor visits in a year, you don't have to pay any money for the 10 visits and if you go for more doctor visits then you will have to pay for the rest of the visits.

Maya: Thanks for explaining, that makes a lot more sense now!

Insurance Advisor: You're welcome, Maya. Remember, if you ever have questions about your health insurance or need help understanding your coverage, don't hesitate to reach out. Understanding your insurance plan is the first step to making informed healthcare decisions.

2.2.4 Benefits of Health Insurance

Financial Protection against Rising Medical Costs: Health insurance helps protect you from expensive medical bills. If you get sick or hurt, the insurance pays for your treatment so you don't have to worry about money.

Critical Illness Coverage: Imagine if you had a serious illness like cancer. Health insurance can give you extra money to help pay for the treatment. It's like having a safety net when things get tough.

Convenient Cashless Claims: When you go to the hospital, you don't need to pay right away. Health insurance lets you get treatment without worrying about money upfront. The insurance company takes care of the bill.

Introducing Indian Health Insurance Companies

New India Assurance Company Limited: As one of the largest insurance companies in India, New India Assurance offers a wide range of health insurance products adjusted to meet diverse healthcare needs.



दि न्यू इन्डिया एश्योरन्स
कंपनी लिमिटेड
The New India Assurance
Company Limited

Star Health and Allied Insurance Company Limited: Specialising in health insurance, Star Health is the first dedicated health insurance company in India.



HDFC ERGO General Insurance Company Limited: HDFC ERGO provides a range of health insurance products designed to fit various healthcare needs.





Knowledge Check

Identify TRUE or FALSE in the following sentences:

1. Health insurance is designed to increase the financial burden associated with medical expenses_____
2. Health insurance companies can cancel coverage for individuals without any reason or notice_____
3. Health insurance plans offer coverage for preventive care services such as vaccinations and screenings_____

Answers: 1.False 2. False 3. True



Activity 5: Health Insurance Research

Objective: Explore Indian health insurance options.

Instructions:

1. Divide students into groups and assign each group a different health insurance company in India.
2. Groups research their assigned company, focusing on plan types, coverage, benefits, and premiums.
3. Each group presents their research to the class, followed by a brief Q&A.
4. Discuss similarities, differences, and strengths among the plans.

2.3 Property Insurance



Property insurance provides financial protection against damage or loss of property resulting from various risks such as fire, theft, natural disasters, or intentional damage. It offers coverage for residential, commercial, and industrial properties, keeping your investment safe. In case of any claims the insured person receives the benefit.

2.3.1 Benefits of Property Insurance

Financial Protection: Property insurance helps cover repair or replacement costs, easing the financial burden on owners.

Peace of Mind: Knowing that their property is insured against unforeseen events gives property owners peace of mind.

Rebuilding and Repair: If damage occurs, insurance helps pay for rebuilding or repairs, restoring the property.

Liability Protection: Property insurance also protects against legal responsibilities for injuries or damages on the property.

2.3.2 Types of Property Insurance

1. **Homeowners Insurance:** Covers home structure, belongings, liability, and living expenses if the home is unlivable.
2. **Renters Insurance:** Covers belongings, liability, and living expenses for renters, but not structure.
3. **Commercial Property Insurance:** Protects business assets like buildings, equipment, and inventory from various risks.
4. **Industrial Property Insurance:** Covers manufacturing plants, warehouses, etc., including structure, machinery, and inventory.

Example

Rohan's house catches fire due to an electrical fault. The fire causes extensive damage to the structure, including the roof, walls, and interior. However, Rohan had purchased homeowners insurance, which covers fire damage. The insurance company assesses the damage and covers the costs of repairing the house, allowing Rohan to rebuild his home without bearing the financial burden.



Example

Arjun's restaurant suffers fire damage in the kitchen, destroying cooking equipment, food inventory, and part of the dining area. His commercial property insurance policy helps pay for fixing the damage and making up for lost income while the property is closed for repairs.



Example

Rahul's apartment is broken into while he is away on vacation, resulting in the theft of his laptop, television, and other personal belongings. Fortunately, Rahul has renters insurance, which covers the stolen items and provides reimbursement for



the losses.

Indian Property Insurance Companies

HDFC Ergo General Insurance Company Limited:

One of India's leading insurers, HDFC Ergo offers a wide range of property insurance solutions adjusted to meet the diverse needs of homeowners and businesses.



ICICI Lombard General Insurance Company Limited: Known for its innovative products and customer-centric approach, ICICI Lombard provides comprehensive property insurance coverage, including protection against dangers like fire, theft, and natural disasters.



Bajaj Allianz General Insurance Company Limited:

With a strong presence in the insurance market, Bajaj Allianz offers reliable property insurance plans designed to safeguard homes, businesses, and valuables against various risks and uncertainties.



Knowledge Check

Identify TRUE or FALSE in the following sentences:

1. Property insurance covers residential, commercial, and industrial properties, keeping your investment safe _____
2. Property insurance helps cover repair or replacement costs, easing the financial burden on owners _____

Answers: 1. True 2. True

2.4 Liability Insurance



Liability insurance, often referred to as third-party insurance, is a fundamental component of the broader general insurance framework aimed at reducing financial risks for policyholders. It safeguards the insured party from potential liabilities arising from lawsuits and related claims. In essence, it provides a safety net for the insured in the event of legal action brought against them for covered claims outlined in the insurance policy.



For businesses, liability insurance is super important. It protects assets, reputation, and future success. Without it, businesses and people could face big money problems from accidents, injuries, or property damage claims. With liability insurance, they feel safe because they know they

are financially protected if anything unexpected happens.

Example

Imagine a driver gets into a car accident, causing damage to another vehicle and injuring its passengers. The injured parties file a lawsuit seeking compensation. Luckily, the driver has vehicle insurance with third-party liability coverage. This insurance covers the costs of repairs, medical expenses, legal fees, and settlements. Without this coverage, the driver would face significant expenses.



2.4.1 Benefits of Liability Insurance

Coverage for Legal Expenses: Insurance pays for legal defence costs, like lawyer fees and court expenses, saving money during lawsuits.

Protection Against Claims: Liability insurance protects policyholders against claims brought by third parties for bodily injury, property damage, or other losses caused by the policyholder's actions, products, or services.

Risk Management: Liability insurance is vital for managing risks. It shifts the burden of potential liabilities to the insurance company, helping you handle unexpected accidents without financial stress.

2.4.2 Types of Business Insurance Coverage

1. **General Liability Insurance:** Important for businesses, it protects from financial losses due to lawsuits for injury or damage caused by the business's activities. It covers claims from customers or others harmed by the business.
2. **Professional Liability Insurance (Errors and Omissions Insurance):** Also called errors and omissions (E&O) insurance, it helps professionals like lawyers or doctors if they're accused of mistakes or negligence in their work. It covers legal costs and damages from lawsuits.
3. **Product Liability Insurance:** Crucial for manufacturers and sellers, it protects from claims for harm caused by defective products. It covers legal costs and damages from lawsuits filed by people hurt by the product.

Example

A client sues an accountant for providing inaccurate financial advice that results in financial losses. The accountant's professional liability insurance, also known as errors and omissions (E&O)



insurance, covers the costs of defending against the lawsuit and any damages awarded to the client.

Example

A driver causes a car accident that results in property damage and injuries to other motorists. The driver's vehicle liability insurance covers the costs of repairing the damaged vehicles, medical expenses for the injured parties, and any legal claims filed against the driver.



Knowledge Check

Choose the correct option:

1. What does liability insurance cover?
 - a. Legal expenses for the insured party
 - b. Medical expenses for the insured party

Answers: a.



Activity 6: Insurance Terminology

Objective: To strengthen understanding of insurance words.

Instructions:

1. The teacher asks a student for the meaning of an insurance term.
2. The student provides the meaning and an example.
3. Classmates can add examples or ask questions.
4. Summarise key points and encourage discussion.

Example Terms:

Deductible: _____

Premium: _____

Coverage: _____

Claim: _____

Let's Recap

1. **Insurance is a contract** where an individual pays premiums to an insurer for financial protection against losses or damages.
2. Insurance provides **financial security, reduces the impact of unexpected events, and promotes economic stability**.
3. Types of insurance include **life, health, property, and liability insurance**, each offering different coverage options.
4. **Property insurance** protects against damage or loss from risks like fire, theft, or natural disasters, while **liability insurance** covers legal expenses and third-party claims.

EXERCISE

Objective Type Questions**MCQ:**

1. Premium is paid by the:
 - a. Insurer
 - b. Insured
 - c. Agent
 - d. Development Officer
2. Claim is provided by the:
 - a. Insured
 - b. Insurer
 - c. Development Officer
 - d. Agent
3. Life insurance is related to:
 - a. Health
 - b. Property
 - c. Liability
 - d. Life
4. Property Insurance is related to:
 - a. Health
 - b. Property
 - c. Life
 - d. Liability
5. Health insurance co-pay usually ranges from:
 - a. 10% to 30%
 - b. 15% to 25%
 - c. 10% to 50%
 - d. 20% to 45%
6. "Sar Utha Ke Jiyo" is the slogan of the company:
 - a. HDFC Life
 - b. SBI Life
 - c. LIC of India
 - d. Birla Sun Life Insurance
7. Industrial Property Insurance covers the risks of:
 - a. Manufacturing Plants
 - b. Warehouses
 - c. Machinery
 - d. All of the above
8. Critical Illness coverage benefits are given under:
 - a. Life Insurance
 - b. Property Insurance
 - c. Health Insurance
 - d. Liability Insurance
9. Which of the following are benefits of Property Insurance?
 - a. Peace of Mind
 - b. Financial Protection
 - c. Rebuilding and Repair
 - d. All of the above
10. What does Product Liability Insurance cover?
 - a. Medical expenses for the insured
 - b. Claims for harm caused by defective products
 - c. Covers professionals like C.A., lawyers, doctors
 - d. None of the above

Short Answer Type Questions

11. What do you mean by Life Insurance?
12. Explain the meaning of Health Insurance.
13. Define Health Insurance and name any two health insurance companies.
14. Explain the types of Property Insurance.
15. Explain the types of Liability Insurance.
16. What are the benefits and limitations of Life Insurance?

Long Answer Type Questions

17. Explain the different types of Life Insurance Policies.
18. Define Liability Insurance with a suitable example. Explain the benefits of Liability Insurance.

ANSWER KEY

Objective Type Questions

MCQ:

- | | |
|--|--|
| <ol style="list-style-type: none">1. b. Insured2. b. Insurer3. d. Life4. b. Property5. a. 10% to 30% | <ol style="list-style-type: none">6. a. HDFC Life7. b. All of the above8. c. Health Insurance9. d. All of the above10. b. Claims for harm caused by defective products |
|--|--|

UNIT 06 Financial Inclusion

Topics

- What is Financial Inclusion?
 - The Importance of Financial Inclusion in Society
 - Barriers to Financial Inclusion
 - Women and Financial Inclusion
 - Challenges Faced by Women
 - The Role of Microfinance
 - Self-Help Groups (SHGs)
 - The Role of Technology
 - Easy Access-Relaxed KYC norms
- Need for Responsible Financial Practices
 - Importance of Responsible Financial Practices
- What are Savings and Why Should Savings be Encouraged?
 - How Banks Encourage Savings
- What are Investments and Why Should They Be Encouraged?
 - Importance of Investing Money
 - Importance of Investment for Banks
 - Different Types of Investments
 - Risk vs. Return Chart
- What is Financial Planning?
 - Components of Financial Planning
- Relevant Government Schemes and Initiatives for Financial Inclusion
 - Financial Inclusion Schemes in India
 - Pradhan Mantri Jan Dhan Yojana (PMJDY)
 - Stand Up India Scheme
 - Atal Pension Yojana (APY)
 - Pradhan Mantri Suraksha Bima Yojana (PMSBY)

- Sukanya Samriddhi Yojana
- Pradhan Mantri Mudra Yojana (PMMY)



Learning Objectives

- Define financial inclusion and recognise its importance in improving access to financial services for underserved populations.
- Learn the significance of adopting responsible financial practices.
- Understand why savings and investments are essential for financial growth and how banks facilitate these activities.
- Identify the key components of financial planning.
- Explore government initiatives designed to promote financial inclusion and support individuals in managing their finances effectively.



Materials Required

- HDFC Bank Savings Calculator
- National Pension System (NPS) Calculator
- Sample investment statements from different types of investments, such as fixed deposits, mutual funds, or stocks
- Brochures or printed information about relevant financial inclusion schemes



Activity 1: Before We Begin!

1. Imagine a world without banks or other financial institutions. How would this impact individuals and communities?

1.0 What is Financial Inclusion?

Financial Inclusion is the process of ensuring that all individuals have access to essential banking and financial services without any form of discrimination. The goal is to ensure that all people, especially those who are economically underprivileged, have access to essential financial services. It also involves providing information and raising awareness to help individuals make informed decisions about these financial services.



1.1 The Importance of Financial Inclusion in Society

Financial inclusion is a critical factor in driving economic growth, reducing poverty, and promoting social equity. It refers to the process of ensuring that all individuals have access to a range of financial services, including savings accounts, loans, insurance, and payment systems.

Economic Growth: Financial inclusion empowers individuals to start and grow businesses, creating jobs and driving economic growth. Access to credit enables individuals to invest in education, healthcare, and other productive assets. By providing financial services to marginalised groups, financial inclusion can help lift people out of poverty.

Social Development: Financial inclusion empowers individuals to make informed financial decisions, build assets, and improve their quality of life. By providing access to financial services to all, financial inclusion can help reduce income and wealth inequality.

Financial Stability: Access to savings accounts encourages individuals to save for future needs. Financial products like insurance can help protect individuals from financial risks. Access to credit can help individuals build a credit history, which is essential for accessing larger loans in the future.

Example

Pratap, a farmer from a rural village, dreamt of expanding his small agricultural business. However, he faced a significant challenge: **limited access to formal banking services**. His savings were kept at home, hindering his ability to secure loans for essential investments like high-quality seeds and modern equipment.



A local bank recognized the urgent need for financial inclusion in the village and introduced banking services. They established a convenient **banking booth** where residents like Pratap could easily **open savings accounts and access credit**.



Empowered by this newfound access to financial services, Pratap was able to **save regularly and secure a loan** to upgrade his farming practices. He invested in high-quality seeds, modern equipment, and even attended training sessions on advanced agricultural techniques.



Pratap's success story inspired other villagers to start using banking services. As more people gained access to financial services, the **local economy flourished**.

**Discuss**

Reflect on Pratap's story. Can you think of similar instances in your community where financial inclusion has positively impacted individuals and communities?

1.2 Barriers to Financial Inclusion

Here are some of the key barriers to financial inclusion and potential solutions:

Lack of Financial Literacy

Solution: Financial education programs, workshops, and campaigns to increase awareness.

Geographical Barriers

Solution: Expanding the branch network of banks and financial institutions, promoting digital financial services, and leveraging technology to reach remote areas.

Discriminatory Practices

Solution: Implementing policies to promote gender equality and inclusivity in financial services, raising awareness about discriminatory practices, and encouraging women's empowerment.

Lack of Trust in Financial Institutions

Solution: Building trust through ethical practices, transparency, and effective customer service.

High Transaction Costs

Solution: Promoting digital financial services, which often have lower transaction costs, and advocating for regulatory measures to reduce fees.

Complex Procedures and Documentation

Solution: Simplifying KYC norms and other bureaucratic processes to make it easier for individuals to access financial services.

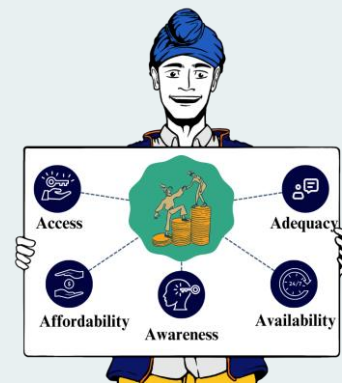


Activity 2: Research and Create an Infographic on the 5 A's of Financial Inclusion

Objective: Identify and illustrate the 5 A's of financial inclusion with examples.

Instructions:

1. **Research:** Find out what the 5 A's of financial inclusion are and gather examples for each.
2. **Create:** Design a chart or infographic showing each "A" and its example.
3. **Present:** Share your infographic with the class and explain your examples.



1.3 Women and Financial Inclusion

Women's financial inclusion is a critical aspect of broader economic and social development. Despite significant progress in recent years, women continue to face unique challenges in accessing financial services. Let us explore the barriers hindering women's financial inclusion, the role of microfinance and self-help groups in empowering women, and the potential of technology to bridge the gender gap.






1.3.1 Challenges Faced by Women

Women often face significant barriers that limit their access to financial services:

1. **Discriminatory Practices:** Gender bias and discriminatory practices can prevent women from opening bank accounts, obtaining loans, or accessing other financial services.
2. **Lack of Financial Literacy:** Limited financial education and awareness can hinder women's ability to make informed financial decisions.
3. **Limited Economic Opportunities:** Societal norms, cultural practices, and lack of property rights can restrict women's economic activities.
4. **Collateral Constraints:** Women often lack collateral to secure loans, making it difficult to access credit.
5. **Household Responsibilities:** Domestic responsibilities can limit women's time and energy to engage in economic activities.

1.3.2 The Role of Microfinance

Microfinance institutions have emerged as a powerful tool for empowering women by providing them with access to small loans and savings services. Real-world examples of microfinance institutions empowering women:

	SKS Microfinance: This microfinance institution provides small loans to rural women, enabling them to start businesses, invest in education, and improve their livelihoods.
	Bandhan Bank: Originally a microfinance institution, Bandhan Bank has evolved into a full-fledged bank that continues to serve low-income individuals and small businesses , particularly women.
	Ujjivan Small Finance Bank: This bank offers a range of financial services, including microloans, to women entrepreneurs, enabling them to start and grow their businesses.

By providing access to credit, savings, and financial education, microfinance institutions empower women to break free from poverty, improve their financial literacy, and contribute to the economic growth of their communities.

1.3.3 Self-Help Groups (SHGs)

Self-Help Groups (SHGs) are informal groups of people, primarily women, who come together to save money, provide loans to each other, and support each other's economic activities. These groups have been crucial in empowering women and promoting financial inclusion, particularly in rural areas.

Example

Kudumbashree is a women empowerment program in Kerala. It has successfully utilised the SHG model to uplift rural women.



Kudumbashree SHGs provide a platform for women to save money, access credit, and learn new skills. These groups have empowered women to become entrepreneurs, improve their livelihoods, and contribute to the economic development of their communities.



Activity 3: Simulating a Study Group

Objective: To understand the benefits of collaborative learning and mutual support.

Instructions:

1. Divide your class into groups of 5-7 students.
2. Each group member should set specific study goals for a particular subject or topic.
3. Schedule regular study sessions to:
 - a. Discuss concepts and clarify doubts.
 - b. Solve practice problems together.
 - c. Share study tips and strategies.
 - d. Motivate each other to stay focused.
4. Provide support and encouragement to group members during exams and assignments.
5. Maintain a record of study sessions, progress, and achievements.

Discussion Points:

How did the experience of forming a study group help you in your studies?

What are the benefits of collaborative learning?

How can study groups improve academic performance and reduce stress?

1.3.4 The Role of Technology

Technology has revolutionised the way financial services are delivered, making it easier for individuals to access and utilise them.

- **Mobile Banking:** Apps like PhonePe, Google Pay, and Paytm allow individuals to access their bank accounts, transfer funds, and make payments from their smartphones, even in remote areas.
- **Financial Literacy Apps:** Apps like Finshots provide financial education and tools, empowering individuals to make informed financial decisions.
- **Online Lending Platforms:** Platforms like Lendingkart offer loans to entrepreneurs, especially those who may not have access to traditional banking services.

By leveraging technology, individuals can overcome geographical barriers, gain financial literacy, and access a wider range of financial services. This can lead to increased economic empowerment and improved livelihoods.



Knowledge Check

Answer the following questions:

1. What is Financial Inclusion? Why is it important for everyone, including economically weaker sections of society, to have access to financial services?

1.4 Easy Access-Relaxed KYC norms

One of the key factors driving financial inclusion is simplifying the process of accessing financial services. Relaxed **Know Your Customer (KYC)** norms have played a significant role in this regard. By streamlining the documentation and verification processes, financial institutions can onboard a larger number of customers, especially those from low-income and marginalised groups.



Discuss

What are the potential benefits and risks of relaxed KYC norms?

2.0 Need for Responsible Financial Practices

Having understood what financial inclusion is and how it aims to provide equitable access to financial services, it's important to delve into how individuals can use these services responsibly.

Example

Harpreet was a small business owner running a successful grocery shop in his town. With rising competition, he decided to expand his shop and took out a large loan without carefully evaluating his ability to repay it. He failed to create a budget to plan for covering loan payments and other expenses. Over time, he began using credit cards to pay off monthly bills, which led to additional high-interest debt.



Unfortunately, Harpreet's business did not grow as expected, and he struggled to manage both the loan and his credit card debt. As his debt increased, so did his financial stress. Harpreet found himself trapped in a **cycle of bad debt**, borrowing more to cover his past dues, which eventually led to the closure of his business.



Harpreet's situation could have been avoided if he had created a financial plan and borrowed within his means.

Responsible financial practices revolve around living within your means, which entails **spending less than you earn**, **saving for future needs and emergencies**, and **paying your bills on time**. While financial responsibility may not always be exciting, it leads to long-term benefits such as financial security and independence.

Example



Simran is a young professional working at a local bank. After receiving her first salary, she decided to create a monthly budget to manage her finances effectively. She tracked her expenses, including rent, groceries, utilities, and transportation, ensuring that her total expenses were less than her income.

By following this budgeting strategy, Simran was able to save a portion of her salary each month. After a year of diligent saving, she had accumulated enough funds to invest in a fixed deposit, which provided her with a secure return.

Through **budgeting and expense tracking**, Simran not only lived within her means but also set herself up for future financial stability.

2.1 Importance of Responsible Financial Practices

Responsible financial practices are essential for creating a stable and secure financial future. These practices offer multiple benefits, including:

Goal Achievement	Wealth Building	Reduced Stress
Enables saving and planning for future needs, such as education, purchasing a home, or starting a business.	Encourages smart investment strategies that help grow wealth over time.	Minimises financial stress and uncertainty by ensuring effective money management.



Activity 4: Planning a Financial Literacy Workshop

Objective: Plan a workshop to help villagers with low levels of literacy understand the importance of responsible financial practices.

Instructions:

1. Form groups of 3-4 students.
2. Imagine you are a banker organising a financial literacy workshop for villagers with low levels of literacy near your house. Choose **one** of the following topics for your workshop:
 - Avoiding Debt
 - Building an Emergency Fund
 - Investing Wisely
 - Managing Financial Health
3. Outline the key points you will cover in the workshop. Include practical advice and real-life examples to make the session engaging for the villagers.
4. Present your workshop plan to the class in 5 minutes, highlighting how you would teach villagers to make smart financial decisions.



3.0 What are Savings and Why Should Savings be Encouraged?

Saving is the practice of setting aside a portion of income for future use. It's a fundamental financial habit that can significantly impact your financial well-being.

Financial Stability: A savings buffer helps individuals avoid high-interest debt during emergencies, protecting their creditworthiness and enabling them to meet financial obligations on time.

Increased Capital and Economic Growth: Savings deposits are crucial for banks to provide loans and investments, which fuel business expansion, job creation, and overall economic growth.

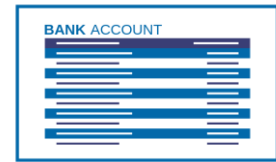
Long-Term Financial Goals: Savings can help individuals achieve long-term financial goals like buying a home, planning for retirement, or funding education.

Risk Mitigation and Creditworthiness: Regular saving can improve creditworthiness, leading to better loan terms and access to larger credit limits.

3.1 How Banks Encourage Savings

Different Types of Savings Products

Banks offer a range of products like savings accounts, fixed deposits, and recurring deposits to match various financial goals. These options are designed to accommodate individuals with varying income levels and saving capacities.



Offering Competitive Interest Rates

To incentivise saving, banks offer attractive interest rates on savings accounts and deposits. Higher returns on savings can motivate customers to prioritise saving over spending.



Personalised Financial Planning

Many banks provide personalised financial advice to assist customers in creating effective savings plans tailored to their income, goals, and risk tolerance.



Using Technology to Promote Savings

Banks leverage technology to enhance customer engagement with savings. Mobile apps, calculators, and online tools allow customers to easily track their savings and financial progress.



For example, **Google Pay** and **Paytm Money** are popular mobile apps in India that offer financial planning and investment management features. The **Vyapar App** is a free cloud-based accounting software that helps small businesses manage invoicing, expenses, inventory, and GST compliance efficiently. For loan rate comparison, platforms like **BankBazaar** and **Paisabazaar** allow users to compare various loan options, enabling them to choose the best rates.

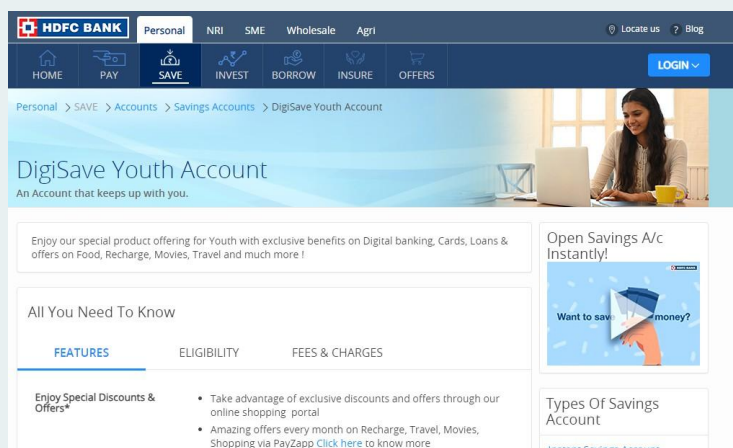


Activity 5: Research Bank Initiatives for Supporting Savings Among Youngsters

Objective: Help students explore how different banks are encouraging savings among the younger generation.

Instructions:

1. Each student will choose 2-3 banks to research (e.g., PNB, HDFC, AU Small Finance Bank).



2. Visit the official websites of the selected banks and find out:
 - a. What savings products are offered specifically for young people?
 - b. What special schemes, incentives, or rewards are available for young customers?
3. Write down key points from each bank's initiatives and how they support young people's savings.
4. In the next class, each student will share a summary of one bank's initiatives with the group.

4.0 What are Investments and Why Should They Be Encouraged?

Investment refers to allocating money or resources to assets, projects, or financial products (such as new business ventures, or stocks and bonds) with the expectation of generating income or capital appreciation over time or for the goal of meeting identified expenses – such as children's higher education or daughter's wedding.

Unlike savings, which are meant to keep your money safe, investments help you grow your wealth and often come with a higher risk or risk-reward ratio.

- **Risk-to-Reward Ratio:** This term means comparing how much money you might gain to how much you might lose. For example, if an investment has a risk-to-reward ratio of 1:2, it means that the potential profit is twice the size of the potential loss.

Saving vs. Investing: If you invest ₹1,000 in a Fixed Deposit (FD) with a bank at an interest rate of 6% for one year, your return at the end of the year will be ₹1,060, with minimal risk involved. On the other hand, if you invest ₹1,000 in a Systematic Investment Plan (SIP) in mutual funds, the returns may be higher, during a certain period, say around 10%, giving you ₹1,100 at the end of the year. However, SIPs are market-linked and come with higher risks, meaning the value of your investment could fluctuate depending on market conditions in different periods.

Thus, while **Fixed Deposits provide security with moderate returns, investments like SIPs offer higher potential growth but involve more risk as well.** Banks and Financial Providers act as intermediaries, connecting savers with investment opportunities and providing advisory services to help clients maximise returns while minimising risk. Encouraging investments benefits both individuals and the broader economy.



Discuss

Do you think people should save and invest money? What are the possible benefits and risks of investing, and how does it differ from saving?

4.1 Importance of Investing Money

Investing money is important for individuals because it helps build a stable and growing financial future. Here are some key reasons why investing matters:

- Investments help individuals **grow their wealth over time**. The longer the investment period, the more significant the benefits from compounding interest i.e., earning interest on interest.

- Investments provide returns that **outpace inflation**, preserving and potentially increasing the purchasing power of one's money. *(Inflation is the rate at which prices rise, usually expressed as a percentage. For instance, if a bottle of cola in India costs ₹40 and increases to ₹42 over a year, the inflation rate would be 5%.)*

Over time, inflation reduces the value of money. For example, if the annual inflation rate is 5%, ₹1,000 today will only be worth approximately ₹783 in 5 years in terms of purchasing power (assuming a constant inflation rate). This means that your money will buy fewer goods and services in the future. Therefore, investing in assets that provide returns higher than the inflation rate is crucial to maintaining or increasing the value of your savings.

- Smart investing can provide **financial security and independence**, allowing individuals to be less reliant on traditional income sources.
- Investing in various assets (gold, stocks, bonds, NSCs, insurance, mutual funds) helps **spread out risk**, which can lead to more stable returns over time.

Example (Return on Investment)

Shreyas invested ₹10,000 @ 5% pa at the age of 25, while Riya started investing the same ₹10,000 also @ 5% pa at the age of 35.



When they were 50, Shreyas had ₹33,863, while Riya had ₹20,789. Even though both friends invested the same amount at the same interest rate, Shreyas had more money because he started investing earlier. This demonstrates the power of compounding interest and how investing over longer periods can lead to greater returns.



Activity 6: Inflation Shopping Challenge

Objective: To demonstrate the impact of inflation on purchasing power.

Instructions:

1. Set up a mock "store" with items labelled with prices, such as snacks, stationery, and small treats.
2. Give each student a fixed amount of "money" (e.g., ₹1000 in fake currency) to spend at the store.

3. Start with a round of shopping where students buy items at today's prices.
4. For the second round, increase prices by 10% to simulate inflation and ask students to shop again with the same amount.
5. Discuss the difference in what they could buy before and after inflation, highlighting that investing can help keep up with rising prices over time.

4.1.1 Importance of Investment for Banks

For banks, promoting investment products is vital for their growth and sustainability:

- Investments provide banks with **additional revenue** through commissions, advisory fees, and management fees.
- Investment services allow banks to **cross-sell other financial products**, such as insurance or personal loans, enhancing overall customer engagement and profitability.
Note: Banks should ensure that they recommend products that truly meet the needs and financial goals of their clients, rather than pushing unnecessary products for profit. Ethical cross-selling builds trust and long-term relationships.
- Offering a range of investment products helps in **retaining clients** by addressing their long-term financial needs and goals.
- Providing investment advice and managing portfolios fosters **deeper relationships with clients**, increasing trust and loyalty.

Example

Rajesh Mehta, a high-net-worth individual, approached XYZ Bank seeking investment advice. The bank's financial advisor, Priya Sharma, crafted a tailored investment plan for Rajesh, including a mix of equity funds, government bonds, and a structured investment plan (SIP).

This strategy aligned with Rajesh's goals of wealth growth and retirement planning. As a result, XYZ Bank not only increased its assets under management but also earned significant advisory fees and management charges.

Rajesh, pleased with the results and personalised service, continued to invest with the bank and referred other high-net-worth clients.



4.2 Different Types of Investments

Investments come in various forms, each with unique characteristics, benefits, and risks. Below are some popular investment options in India:



Fixed Deposits

Offers fixed returns on a lump-sum deposit with flexible maturity periods and the option for early withdrawal with a penalty.



Bonds

Debt securities where you lend money to the government or companies, earning fixed interest over time.



Stocks

Represent ownership in a company, allowing you to earn returns through dividends and capital appreciation.



Mutual Funds

Pool money from multiple investors to invest in diversified portfolios of stocks, bonds, or other assets.

These investment options have already been covered in Unit 1 and Unit 2, so let's quickly revisit the key points.

Fixed Deposit (FD): Offered by almost all scheduled banks and some non-banking financial companies (NBFCs), FDs provide a secure way to grow your funds by offering a fixed interest rate on a lump-sum deposit. With flexible maturity periods, FDs allow investors to earn higher interest than regular savings accounts. Upon completion of the chosen tenure, the lump-sum deposit and the interest accrued are paid out. In case of emergencies, investors can withdraw their money before maturity, though a small penalty may apply, which varies from bank to bank.

Bonds: Bonds are a type of fixed-income security where investors lend money to the bond issuer, usually the government or a corporation. In return, the issuer agrees to pay regular interest (called a **coupon**) at a fixed rate until the bond matures. Once it matures, the investor gets back the original amount they invested. Bonds are considered a safer investment option because the risk of the issuer not repaying is low.

In India, most bonds offer a fixed interest rate, but other types like floating-rate bonds (where interest changes) and zero-coupon bonds (which don't pay interest but are sold at a discount) are also available.

Stocks: When you buy a company's stock (also known as equities) you become a part-owner of that company. However, investing in the stock market requires careful analysis to select the right stocks and determine the best time to buy and sell. The stock market is highly volatile, and returns are influenced by market fluctuations and the investor's risk tolerance. Due to its

volatility and the potential for significant financial losses, the stock market should not always be considered a reliable or guaranteed option for investment.

To invest in stocks, individuals must have a Demat account (a digital account to hold and trade shares), which can be opened online or through a broker. Trading takes place on stock exchanges, where investors can buy and sell shares based on their financial strategies.

Mutual Fund: Mutual Funds allow investors to pool their money together, which is then managed by professional fund managers to invest in a mix of stocks, bonds, or other securities. Mutual Funds are ideal for investors who may not have the financial expertise or time to track markets but still want to benefit from potential growth. They offer a range of options such as equity funds (focused on stocks), debt funds (focused on bonds), and balanced funds (a mix of both), catering to different risk preferences.

For those who prefer smaller, regular investments, a Systematic Investment Plan (SIP) is a popular choice, allowing contributions as low as ₹500. Additionally, tax-saving mutual funds like the Equity Linked Savings Scheme (ELSS) help investors maximise returns while enjoying tax benefits.



Activity 7: Stock Market Scenarios: Understanding Gains and Losses

Objective: To demonstrate how external events impact stock prices and help students analyse stock market risks and rewards.

Instructions:

1. Have students calculate the new stock price based on each scenario card and discuss the factors influencing the price change.
2. After calculations, each student or pair will research and list: Potential Rewards of Investing in Stocks and Risks of Investing in Stocks.
3. Conclude by discussing each group's thoughts on whether they would consider investing in stocks, considering the risks and rewards they have identified.

Starting Stock Price	Starting Stock Price
₹100	₹100
Change in Stock Price	Change in Stock Price
+₹60	-₹30
Reason	Reason
The company's app becomes the most popular of the year, boosting sales and attention.	A major store chain that sells the company's gadgets goes out of business, closing 10,000 stores.



Public Provident Funds (PPF)

A long-term government-backed savings scheme offering tax benefits and attractive interest rates.



Exchange Traded Funds (ETFs)

Funds that track indices or commodities, traded on stock exchanges like individual stocks.



National Pension Scheme (NPS)

A government-backed retirement savings plan with tax benefits and flexible investment options.



Real Estate Investment Trusts (REITs)

Real estate investments offering diversification, professional management, and liquidity.

Public Provident Fund (PPF): The Public Provident Fund (PPF) is a government-backed fixed-income savings scheme in India, that offers a secure investment option. To invest in PPF, you can open an account at any bank or post office, typically starting with a minimum deposit as low as ₹100 (this may vary by bank). You can contribute between ₹500 and ₹1.5 lakh annually, and the investment is locked in for 15 years. A key benefit of PPF is that contributions are eligible for tax deductions under Section 80C of the Income Tax Act, with a maximum deduction of ₹1.5 lakh per year.

PPF accounts offer facilities such as withdrawals and extensions of maturity periods. Additionally, you can also take a loan against your PPF balance.



Post Office Savings Account is a deposit scheme under the Government of India, available at all post offices. It gives returns on your investment at a fixed interest rate.

- Minimum deposit required is ₹500
- Anyone above the age of 10 years can open the account.

Example



Simran: Hey Amar, I heard that investing in the Public Provident Fund (PPF) can help save on taxes. How does that work?

Amar: That's right! When you invest in a PPF, the amount you contribute can be subtracted from your total taxable income.



Simran: So, if I invest ₹1.5 lakh in a PPF account, does that mean I can reduce my taxable income by the same amount?

Amar: Exactly! If your total income is ₹6 lakh, your taxable income would drop to ₹4.5 lakh after your PPF investment.

Simran: Wow, that could save me a lot on taxes! I guess it's a smart way to save for the future while getting some tax benefits too.

Exchange-Traded Funds (ETFs): Exchange-Traded Funds (ETFs) are passively managed funds that pool money from investors to invest in a range of securities (financial assets) based on a specific index (a benchmark used to measure performance). Unlike mutual funds, ETFs are traded on stock exchanges like regular stocks.

The risk of ETFs depends on the underlying index—for instance, tracking a mid-cap index (an index that includes medium-sized companies) carries moderate risk. ETFs typically have lower management fees (the costs charged for managing the fund) than mutual funds and are highly liquid, allowing investors to buy and sell them during trading hours.

Registered with the Securities and Exchange Board of India (SEBI), ETFs are a good option for those with limited stock market expertise.

National Pension Scheme (NPS): The National Pension Scheme (NPS) is a government-sponsored retirement savings plan managed by the Pension Fund Regulatory and Development Authority of India (PFRDA). NPS pools contributions from investors and invests in assets like stocks, government bonds, and corporate bonds.

It helps build a retirement fund, allowing partial withdrawals at retirement, with the remaining amount paid as a regular pension. Open to Indian citizens aged 18 to 60, the account matures at 60 but can be extended to 70 years.

NPS contributions also offer tax deductions, and partial withdrawals (up to 25%) are allowed after three years of having the account.

REITs (Real Estate Investment Trusts): REITs are companies that own and operate income-producing real estate properties, offering investors a way to participate in the real estate market without directly owning physical property.

REITs allow you to invest in a diversified portfolio of real estate properties. They are managed by professionals who handle property management and leasing. Additionally, REITs are traded on stock exchanges, making them more liquid than directly owning real estate. Many REITs pay regular dividends to their investors, and in some cases, they offer tax advantages. Overall, REITs provide exposure to the real estate market without the need for direct ownership or management.



Activity 8: Analysing Investment Options

Objective: Understand different investment options.

Instructions:

1. Divide the class into small groups of 4-5 students.
2. Each group will take on the role of a bank's investment advisory team. Assign each group one of the investment options to analyse (FDs, Mutual Funds, Stocks, etc.).
3. Each group should research their assigned investment option and discuss the following points.
 - a. What are the main characteristics of this investment option?
 - b. Who would benefit most from this option (e.g., risk-averse clients, retirees)?
 - c. What are the pros and cons of this investment option?
 - d. When would you recommend this option to a client, and why?
4. After the discussion, each group will present their findings to the class (5-10 minutes per group).

Risk vs. Return Chart:

Investment Option	Risk	Returns
Fixed Deposit (FD)	Low	Low
Bonds	Low-Medium	Medium
Stocks	High	High/Medium/Low/Losses
Mutual Funds	Medium-High	Medium/High/Losses
Public Provident Fund (PPF)	Low	Medium
Exchange-Traded Funds (ETFs)	Medium-High	Medium/High/Losses
National Pension Scheme (NPS)	Low	Medium
Real Estate Investment Trusts (REITs)	Medium-High	Medium/High/Losses

Note: The risk and returns of each investment can vary based on market conditions and individual circumstances. This chart provides a general representation.



Knowledge Check

Answer the following questions:

1. What is one of the benefits of investing in Mutual Funds?

2. What are REITs, and how can investors benefit from them?

3. What does the National Pension Scheme (NPS) primarily aim to provide?

5.0 What is Financial Planning?

Financial planning is a strategic process that helps you manage your money to achieve your life goals. It involves assessing your **current financial situation**, **setting clear objectives**, and **creating a roadmap to reach them**.



5.1 Components of Financial Planning

Here are a few essential components that should be part of every comprehensive financial plan:

Cash Flow Management: Understanding cash flow is crucial for tracking income and expenses. This helps create a sustainable budget, allowing for better planning of future expenses and investments.

Investment Planning: An effective financial plan includes a strategy for growing wealth through investments. Assessing risk tolerance and diversifying across various options ensures financial stability and helps achieve goals.

Risk Management and Insurance: Protecting financial well-being involves securing appropriate insurance coverage for health, life, and property. Insurance mitigates potential risks that could disrupt financial plans.



Tax Planning: Effective tax planning reduces liabilities through deductions and smart investments. By utilising tax-advantaged accounts (like Public Provident Fund, and National Pension System), you can maximise savings and ensure more funds contribute to your financial goals.

Retirement Planning: Preparing for retirement involves saving and investing to ensure sufficient funds for a comfortable lifestyle. Establishing a retirement account and regularly contributing helps secure your financial future.

Estate Planning: Estate planning ensures your assets are distributed according to your wishes after your passing. This process involves creating wills and trusts to manage your legacy and minimise tax implications.

Real-World Example: Amar's Financial Journey

Example

Amar recently graduated and has just landed his first job. Dressed in formal attire for the first time, he feels a mix of excitement and nervousness as he receives his first pay cheque. His mother reminds him to save for the future, his younger brother asks for a new game, and his friends are eager to celebrate with a party. Amar is now faced with the dilemma of how to manage his income.



If you were Amar, how would you prioritise in this situation?

A financial plan can help him:

- **Prioritise:** Determine which financial goals are most important.
- **Budget:** Create a budget to allocate his income effectively.
- **Save:** Establish an emergency fund and save for future goals.
- **Invest:** Explore investment options to grow his wealth.
- **Protect:** Secure his future with insurance coverage.

By following a structured financial plan, Amar can make informed decisions, achieve his goals, and build a secure financial future. Financial planning is not merely about managing money; it's about **creating a lifestyle that reflects personal values and aspirations**.



Knowledge Check

Answer the following questions:

1. Why is cash flow management important in financial planning?



Activity 9: Personal Financial Planning Exercise

Objective: To help students understand and apply the concepts of financial planning by creating their financial plan.

Instructions:

1. Divide students into small groups or have them work individually.
2. Ask them to imagine they have just started their first job (similar to Amar)
3. Provide them with a scenario where they have a monthly income, a list of expenses (rent, groceries, transportation, savings, etc.), and a set of goals (such as saving for an emergency fund, paying EMI for a smartphone, buying a vehicle, etc.).
4. Students will:
 - a. Calculate their current cash flow.
 - b. Create a simple budget based on their income and expenses.
 - c. Set financial goals (short-term and long-term).
 - d. Plan how they will allocate their money towards savings, investments, and expenses.
5. Have each student or group present their financial plan to the class and explain how they have prioritised their spending and savings.

6.0 Relevant Government Schemes and Initiatives for Financial Inclusion

Financial inclusion is a key priority for the Government of India, aimed at extending financial services to the vast unserved and underserved population to unlock the country's growth potential. In 2014, the government launched the **National Mission for Financial Inclusion (NMFI)**, known as the **Pradhan Mantri Jan Dhan Yojana (PMJDY)**, to provide universal banking access to every unbanked household. Operating under the principles of "**banking the unbanked, securing the unsecured, funding the unfunded, and serving unserved and underserved areas,**" the mission shifted in 2018 to focus on ensuring every unbanked adult has access to financial services.



The motto "**from Jan Dhan to Jan Suraksha**" reflects a holistic approach to enhancing social security and financial stability for all.

Globally, about **1.4 billion people** in developing

economies lack access to formal credit and savings (*Overview*, n.d.)¹. In India, the government promotes financial inclusion through **regulatory frameworks**, **financial literacy programs**, and **investments in digital infrastructure**. These efforts help reduce barriers and encourage financial institutions to serve marginalised populations, expanding access to the formal financial system.

Key government strategies include:

- Establishing rules and guidelines for financial institutions to ensure inclusivity.
- Enhancing financial literacy among individuals.
- Expanding internet connectivity and mobile networks, especially in remote areas.

6.1 Financial Inclusion Schemes in India²



Pradhan Mantri Jan Dhan Yojana (PMJDY)

Launched in 2014, PMJDY is a national mission aimed at providing affordable banking services to every household, especially those without prior access to formal financial systems. Under this scheme, individuals can open zero-balance savings accounts and receive benefits like debit cards with insurance, access to credit, and other financial services. The program has been crucial in expanding financial inclusion, particularly in rural areas.



Key Features:

- **No minimum balance** is required.
- **RuPay debit cards** with accident insurance coverage up to ₹2 lakh.

¹ *Overview*. (n.d.). World Bank. <https://www.worldbank.org/en/topic/financialinclusion/overview>

² *Government of India*. (n.d.). <https://financialservices.gov.in/beta/en/project/new-initiatives-03>

- Use of "**Bank Mitras**" to provide banking services in areas without branches. A Bank Mitra is an agent who provides banking services in areas without bank branches or ATMs, helping unbanked communities access essential financial services.
- **Access to schemes** like Pradhan Mantri Suraksha Bima Yojana (accident insurance), Pradhan Mantri Jeevan Jyoti Bima Yojana (life insurance), and Atal Pension Yojana (pension scheme).



Stand Up India Scheme

Launched on April 5, 2016, the Stand Up India Scheme promotes entrepreneurship among women and Scheduled Castes/Scheduled Tribes (SC/ST) by facilitating access to credit for new business ventures. This initiative provides loans for greenfield projects (new businesses launched from scratch) in various sectors, including manufacturing, services, and trading. By empowering underrepresented groups, the scheme aims to address income inequality and stimulate economic growth, ensuring that these entrepreneurs receive the necessary support to thrive.



Key Features:

- Provides financing between **₹10 lakh and ₹1 crore**.
- Specifically designed for **women and SC/ST entrepreneurs**.
- Supports businesses across **manufacturing, services, and trading sectors**.
- **Collateral-Free Loans**; Backed by the Credit Guarantee Fund for Stand Up India (CGFSI).
- **Offers hand-holding assistance**, including guidance and advice for entrepreneurs.



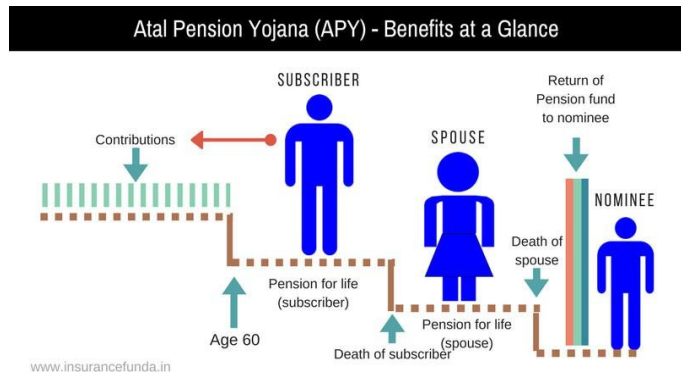
Atal Pension Yojana (APY)

The Atal Pension Yojana (APY), launched on May 9, 2015, is designed to offer financial security to individuals in the unorganised sector during retirement. The scheme allows subscribers to receive a fixed monthly pension upon reaching the age of 60, with government co-contribution for eligible participants, making it an affordable option for those without access to formal pension systems. In case of the subscriber's premature death, the spouse has the option to continue contributing to the account until the original subscriber has reached 60, thus maintaining the pension benefits.




Key Features:

- Available to individuals **aged 18 to 40** with a savings bank or post office savings account.
- Subscribers can select a monthly pension between **₹1,000 and ₹5,000**, depending on their contributions. (Image Source:




<https://www.insurancefunda.in/atal-pension-vojana-details/>

- Co-contribution from the government** enhances the affordability of the scheme.
- The **spouse can continue contributions** if the subscriber passes away early, ensuring continued pension benefits.
- Upon the **death of both the subscriber and spouse**, the accumulated pension wealth is transferred to the **designated nominee**.




Pradhan Mantri Suraksha Bima Yojana (PMJDY)

Provides affordable accidental insurance coverage to all eligible individuals.



Sukanya Samriddhi Yojana

A savings scheme to promote the financial security of the girl child.



Pradhan Mantri Mudra Yojana (PMMY)

Offers loans to micro and small enterprises for business growth.

Pradhan Mantri Suraksha Bima Yojana (PMSBY)

The Pradhan Mantri Suraksha Bima Yojana (PMSBY) aims to provide affordable accidental insurance to individuals, particularly benefiting those from low-income backgrounds. For a **nominal annual premium of ₹12**, it offers coverage of **₹2 lakh for accidental death or full disability** and **₹1 lakh for partial disability**. This initiative aims to enhance

financial security for those who may not have access to traditional insurance options.



Key Features:

- Open to individuals **aged 18 to 70 years** with a bank account.
- Requires **consent for auto-debit**, with enrollment open until May 31 for coverage from **June 1 to May 31** of the following year.
- **Aadhaar** is used as the primary KYC for bank accounts.
- Offered by **Public Sector General Insurance Companies** and other willing **General Insurance Companies**, in collaboration with banks.
- Death due to suicide, alcohol or drug abuse, and other **self-inflicted harm** are **not covered**.

Sukanya Samriddhi Yojana

The Sukanya Samriddhi Yojana is a government-backed savings initiative designed to secure the future of the girl child in India. Launched as part of the "**Beti Bachao, Beti Padhao**" campaign, this scheme offers one of the highest interest rates among small savings schemes, encouraging long-term savings for the education and marriage of girls. The account can be opened by parents or guardians for a girl child under the age of 10 and comes with significant tax benefits under Section 80C of the Income Tax Act.³

**Key Features:**

- The account can be opened for **a girl child** who has **not attained the age of 10 years**. Only **one account** can be opened in the name of **each girl child**, and **a maximum of two accounts can be opened in a family** (with exceptions for multiple births).
- The **minimum initial deposit** required is **₹250**, while the **maximum deposit** allowed in a financial year is **₹1.5 lakh**.
- The account **matures after 21 years** from the **date of opening**. However, it can be prematurely closed in case of the girl child's marriage after the age of 18.
- Partial withdrawals of up to **50% of the balance are permitted after the account holder reaches 18 years** of age or passes the tenth standard, whichever comes first, for educational purposes.
- **Until the girl child turns 18**, the account is operated by the **guardian**. **Afterward, the account holder can operate it herself**.

Pradhan Mantri Mudra Yojana (PMMY)

Launched on April 8, 2015, the Pradhan Mantri Mudra Yojana (PMMY) aims to provide financial support to aspiring entrepreneurs and small businesses in India. The scheme offers

³ Sukanya Samriddhi Account Scheme. (n.d.). NSI India. Retrieved October 6, 2024, from [https://www.nsiindia.gov.in/\(S\(0vhf452vpqod4r453ur3ct45\)\)/InternalPage.aspx?Id_Pk=89](https://www.nsiindia.gov.in/(S(0vhf452vpqod4r453ur3ct45))/InternalPage.aspx?Id_Pk=89)

collateral-free loans to promote self-employment and entrepreneurship among young and skilled individuals. It is **categorised into three sub-schemes** based on the loan amount required, enabling both new and existing businesses to secure funds for growth.



Key Features:

- Sub-Schemes:
 - **Shishu**: Loans up to ₹50,000.
 - **Kishore**: Loans from ₹50,001 to ₹5 lakhs.
 - **Tarun**: Loans from ₹5,00,001 lakhs to ₹10 lakhs.
- Accessible funding **without the need for any collateral**.
- **Supports young and skilled individuals** in starting their ventures.
- **Provides financial assistance** for the growth of small businesses.

These government-led financial inclusion schemes are driving a more equitable and inclusive economy, ensuring that every citizen has access to essential financial services, and fostering growth and development across all sections of society.



Knowledge Check

Choose the correct option:

1. Under the Pradhan Mantri Mudra Yojana, which sub-scheme offers loans up to ₹50,000?
 - a. Tarun b. Kishore c. Shishu
2. What is the primary focus of the Stand-Up India Scheme?
 - a. Encouraging entrepreneurship among SC/ST and women
 - b. Providing housing for the urban population
 - c. Promoting girl child education

Answers:

- c. Shishu
- a. Encouraging entrepreneurship among SC/ST and women



Activity 10: Success Stories Poster Presentation

Objective: To research and showcase real-life success stories of beneficiaries of government schemes and understand their impact.

Instructions:

1. Divide the class into small groups of 4-5 students.
2. Each group will choose one government scheme and research a success story of a real beneficiary who has used the scheme to improve their life or business.
3. On a chart paper, create a poster that includes:
 - a. Scheme Name
 - b. Beneficiary's Story (Who they are, how they used the scheme, what changes it brought to their life)
 - c. Key Achievements (Personal or business growth, financial stability, empowerment, etc.)
4. Each group will present their success story to the class, explaining how the scheme made a positive difference in the individual's life in 3-5 minutes.

**Let's Recap**

1. **Financial inclusion** ensures access to essential financial services for all individuals, especially the economically underprivileged, without discrimination.
2. **Responsible financial practices** emphasise **budgeting, saving, investing, and avoiding debt traps** to achieve long-term financial stability.
3. **Savings** are encouraged for **financial security, managing unforeseen expenses, and achieving long-term goals**. Banks promote savings through various products like savings accounts and fixed deposits.
4. **Investments** are important for achieving financial milestones. Different types of investments include **stocks, bonds, and mutual funds**, each with unique benefits and risks.
5. Financial Planning involves managing financial resources. Key components include **cash flow management, investment planning, risk management, tax planning, retirement planning and estate planning**.
6. Government initiatives like **Pradhan Mantri Jan Dhan Yojana (PMJDY)** aim to provide banking access and enhance financial inclusion, especially for underprivileged sections of society.



EXERCISE

Objective Type Questions**MCQ:**

- What are the common challenges faced in achieving Financial Inclusion?
 - Lack of Documentation
 - Minimum Eligibility Criteria
 - Lack of Awareness
 - All of the above
- What are the different types of saving products?
 - Saving Accounts
 - Fixed Deposits
 - Recurring Deposits
 - All of the above
- Financial services includes:
 - Savings Accounts
 - Loans
 - Insurance
 - All of the above
- Planning how to allocate income to cover all expenses and achieve financial goals is called:
 - Budgeting
 - Saving
 - Investing
 - None of these
- Pradhan Mantri Jan Dhan Yojana (PMJDY) was launched in:
 - 2010
 - 2011
 - 2012
 - 2014
- “Beti Bachao, Beti Padhao” Campaign relates to:
 - Pradhan Mantri Suraksha Bima Yojana
 - Sukanya Samriddhi Yojana
 - Pradhan Mantri Mudra Yojana
 - Pradhan Mantri Jan Dhan Yojana
- Technology used to promote savings includes:
 - Mobile apps
 - Online tools
 - Google Pay

d. All of the above

State True or False:

- Financial Inclusion is the process of ensuring that all banking and financial services are available to everyone without any form of discrimination.

One line Answers:

- Write down the full form of P.P.F.
- Write down any one strategy for implementing responsible financial practices.

Short Answer Type Questions

- What is financial planning?
- What are the objectives of financial planning?
- What are the key areas of financial inclusion?
- What are the key aspects of responsible financial practices?
- What are the different types of investments?
- Write down different strategies for implementing responsible financial practices.
- How are banks adapting to help the younger generation?

Long Answer Type Questions

- What is financial inclusion? Write down its features.
- What are responsible financial practices? Write down their importance.
- What are savings? Why should savings be encouraged?
- What are investments? Write down their importance.
- What is financial planning? Write down the objectives of financial planning.
- Write down the components of financial planning.
- Explain different types of government schemes and initiatives for financial inclusion.

ANSWER KEY

Objective Type Questions

MCQ:

1. d. All of the above
2. d. All of the above
3. d. All of the above
4. a. Budgeting
5. d. 2014
6. b. Sukanya Samriddhi Yojana
7. d. All of the above

State True or False:

8. True

One line Answers:

9. Public Provident fund
10. Promoting financial literacy among individuals / Create a budget / build an emergency fund / use credit wisely / plan for the future / provide financial education / promote responsible lending.

UNIT 07

Debt Collection Techniques and Processes



Topics

- Understanding Debt Collection
- Debt Collection Process
 - Regulatory Framework Governing the Debt Collection Process
 - Types of Debt Collection Methods
 - Stages of Debt Collection
 - Pre-collection Stage
 - Collection Stage
 - Legal Stage
 - Post-Judgemental Stage
- Techniques For Effective Debt Collection
 - Communication Skills for Effective Debt Collection
 - Persuasion Techniques to Encourage Debt Repayments
- Handling Objections And Excuses
 - Common Objections and Excuses from Debtors
 - Dealing With Debtors Properly



Learning Objectives

- Understand the basic concept of debt collection
- Understand the steps in the debt collection process - pre-collection, collection, legal, and post-judgemental stages
- Learn the techniques involved in effective debt collection through communication skills and persuasion techniques
- Understand the ways to handle objections and excuses from debtors and learn ways to deal with them



Materials Required

- Chart paper to create a flowchart/diagram to demonstrate understanding of the various points in the debt collection process.



Activity 1: Before We Begin!

Imagine your friend borrowed ₹10,000 to buy a phone and promised to repay it in two months. It's now been five months, and they haven't returned the money. You have tried asking them nicely, but they keep giving excuses. What would you do?



1.0 Understanding Debt Collection

Debt collection is the process used by banks and financial institutions to recover money from individuals who have not repaid their loans. This process involves following legal procedures to ensure the recovery is done in compliance with the law. Debt collection also requires handling the situation professionally and ensuring that the rights of both the lender and the borrower are respected. When someone owes money and has not repaid it, the creditor may work with a debt collector to recover the amount. The person or organisation responsible for collecting the money is called a **debt collector**.

In the past, debt collection by banks and lending companies was a slow and difficult process, relying on collection agencies to send frequent reminders to borrowers. This often led to disputes, as borrowers faced constant pressure to repay the debt, and resolving these issues took considerable time.

Banks, as lending institutions, rely on debt collection to operate efficiently. If people do not repay their loans, it becomes difficult for the bank to manage credit risk. Therefore, it is important to recover unpaid debts while adhering to the legal and regulatory requirements in the country.



Debt

The amount of money you borrow from a bank, institution, or person with an agreement to repay it in the future.

Example

Simran took a loan of ₹35,000 to buy a laptop and agreed to repay ₹3,000 monthly for one year.

She made the payments on time for the first six months but missed her payments for the



next three months. The bank sent her reminders about the missed payments, but she didn't respond. To resolve the issue, the bank contacted a debt collection agency.

The agency explained to Simran that failing to pay is impacting her credit score and future loan eligibility. Understanding the situation, Simran repaid the overdue amount, and the bank was able to recover the missed payments with the help of the debt collector.

2.0 Debt Collection Process

2.1 Regulatory Framework in the Debt Collection Process

Debt collection is a detailed process that involves important legal and ethical guidelines. In India, various regulations and authorities ensure that the debt collection process is fair and efficient. These laws protect the rights of both creditors and debtors, ensuring that the collection process is conducted properly while safeguarding everyone's interests.

1. **The Reserve Bank of India** plays an important role in setting the guidelines for debt collection for banks and other financial companies. The guidelines issued by RBI ensure that borrowers are protected from unfair treatment and seek remedies if their rights are violated. These guidelines also ensure that all banks and financial institutions follow the same standard procedures, promoting transparency and fairness in the debt collection process.
2. **The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act of 2002** allows banks and financial institutions to auction commercial or residential properties, except agricultural land, to recover loans when borrowers fail to repay without going to court. This Act helps banks reduce their Non-Performing Assets (NPAs) by providing mechanisms for loan recovery and asset reconstruction.
3. **The Recovery of Debts Due to Banks and Financial Institutions (RDDBFI) Act, 1993**, is a law that establishes tribunals Debt Recovery Tribunals (DRTs) to recover debts owed to banks and financial institutions.



Non-Performing Asset

A classification of loans where the borrower has failed to make interest or principal payments for a specified period, typically 90 days or more.

2.2 Types of Debt Collection Methods

Debt collection in India can be carried out in various methods, such as:

- **In-House Debt Collection:** In this approach, lenders, such as banks or non-banking financial companies (NBFCs), attempt to recover unpaid debts using their resources

instead of hiring third-party agencies. They contact borrowers directly through messages or notifications, avoiding third-party fees while maintaining full control over the recovery process.

Example

Ramesh took a loan of ₹35,000 from RXY Bank but was unable to repay it due to a family medical emergency.

The bank's team contacted him through phone calls and text messages, reminding him about the unpaid loan and offering a repayment plan with smaller instalments to accommodate his financial situation.

Since the bank handled the communication directly, it didn't need to pay any extra fees to an external agency. This method helped the bank stay in control and maintain a positive relationship with Ramesh.



- **Third-Party Debt Collection Agency:** Financial institutions and lenders often engage third-party debt collection agencies to recover long overdue unpaid debts. These agencies work on behalf of lenders and are paid a commission for their services. They frequently use advanced tools, such as skip tracing and automated calling systems, to remind debtors to make payments.

Example

Rohan took a loan of ₹50,000 from the bank to buy a bike. Initially, he made payments for the first three months, but later, he defaulted. The bank attempted to contact him, but he did not respond. To recover the loan, the bank enlisted the help of YBS, a third-party debt collection agency specialising in recovering unpaid loans.

The agency sent automated calls and messages to remind Rohan of his debt and the consequences of non-payment. As a result, Rohan resumed payments from the next month. The bank paid ₹10,000 to YBS for their services in recovering the loan.



- **Legal Debt Collection:** In this method, financial institutions like banks, as well as non-financial lenders, take legal action by suing the borrower to obtain a court order for debt collection. This process is usually considered a last resort and is typically used when the borrower has significant assets but has failed to repay the loan. Legal

debt collection can be an effective way to recover money, though it may take time and involve additional costs.

Example



Heena owns multiple factories in Punjab and took a loan of ₹3 Crores from XYZ Bank to establish a new cloth manufacturing unit, with a commitment to repay the full amount within two years.

However, due to lower-than-expected sales, she was unable to repay the loan by the due date. XYZ Bank reached out to her via calls and messages, reminding her of the outstanding debt and granting her an additional month to settle the amount. Despite this extension, Heena still could not make the payment.

As a last resort, the bank filed a lawsuit against her, seeking a court order to seize one of her factories. Although the court gave her a month to repay after issuing the notice, she still failed to do so. Consequently, the bank seized one of her factories in Punjab to recover the outstanding debt.

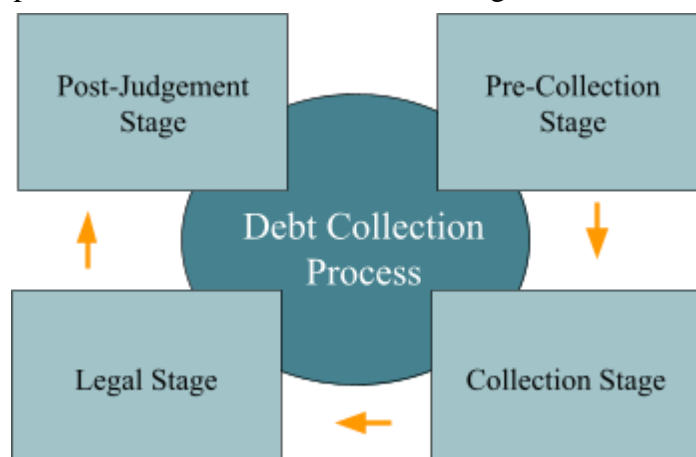


Discuss

Can you think of strategies individuals and companies can implement to avoid falling into debt?

2.3 Stages of Debt Collection

The debt collection process can be classified into four stages.



2.3.1 Pre-Collection Stage

The pre-collection stage is vital for creditors in managing outstanding debt, which refers to the money owed by individuals or businesses that has not yet been repaid. During this phase, the creditor gathers essential information about the borrower's financial status and formulates a collection strategy by the guidelines established by the Reserve Bank of India (RBI). Effective communication between the creditor and the borrower is crucial in the debt recovery process, as it fosters understanding and encourages timely repayment.

- 1. Understand the borrower's financial situation:** To effectively understand a borrower's financial situation before taking any action, creditors should follow these steps:
 - **Reviewing borrower's credit report:** The credit report provides valuable insights into the borrower's financial history, including previous debts, payment patterns, and overall creditworthiness.
 - **Assess the income and expense:** Creditors need to evaluate the borrower's monthly income and expenses. This assessment allows creditors to determine how much the borrower can realistically afford to pay toward their debt, helping to create a more manageable repayment plan.
 - **Evaluate the assets:** Understanding the assets owned by the borrower, such as property and vehicles, is essential. This information gives creditors a clearer picture of the borrower's financial status and can be instrumental in negotiating repayment terms or considering potential collateral for the loan.
- 2. Developing a collection strategy that complies with RBI guidelines:** To develop a collection strategy that complies with the Reserve Bank of India (RBI) guidelines, creditors must ensure that their practices are fair and ethical throughout the debt collection process.
 - Communication with borrowers should be conducted respectfully and professionally, avoiding any form of harassment or intimidation.
 - Creditors can reach out to borrowers using various methods, including phone calls, letters, and emails. Offering different channels for communication helps ensure that borrowers can respond in a manner that suits their situation.
 - During conversations, creditors should engage borrowers in discussions about repayment options.
 - Consistent follow-up communications reinforce the importance of repayment and show borrowers that their financial responsibilities are being monitored.

The pre-collection approach not only helps in recovering the loan amount but also fosters a positive relationship between the borrower and the creditor.

2.3.2 Collection Stage

Once the pre-collection stage is complete and a collection strategy has been developed, the next step is understanding how the collection stage works.

1. **Initial contact with the borrowers:** The collection process begins when the creditor reaches out to the borrower to request payment for the outstanding debt. This initial contact must be respectful and empathetic, taking into account the borrower's financial situation.
2. **Verification of debt using RBI guidelines:** Before requesting repayment, the creditor must confirm that the debt indeed belongs to the borrower and that the amount is accurate. This involves reviewing transaction records and cross-checking the borrower's information against credit records to prevent any misunderstandings.
3. **Follow up on the communication with fair practice:** The creditor should maintain respectful and patient communication throughout the repayment process. All follow-up communications must comply with fair practice codes, reinforcing the importance of repayment without resorting to harassment.
4. **Reporting to the credit bureaus in compliance with the RBI guidelines:** If the borrower continues to fail to repay the debt despite multiple attempts to collect, the creditor may report the outstanding debt to credit bureaus. This action can negatively impact the borrower's credit score, affecting their ability to secure loans or credits in the future. The creditor must inform the borrower before making such a report.
5. **Online Dispute Resolution (ODR) option:** In cases of disputes between the creditor and borrower, Online Dispute Resolution (ODR) provides a faster and more efficient method for resolving issues without lengthy legal proceedings. Both parties can visit the ODR service website, create an account, and file a case, after which a mediator is assigned to help resolve the dispute.

2.3.3 Legal Stage

If a borrower fails to repay their debt after multiple reminders from the creditor, the creditor may proceed with legal action. Taking legal action is a lengthy process and usually involves these steps:

1. **Filing a case under the RDBFI:** Creditors initiate legal proceedings when all other debt collection efforts have failed. Before filing the case, they must gather comprehensive information about the borrower, including loan agreements, location, payment records, and documentation of communication efforts. The creditor files the legal case in the respective tribunal where the borrower resides. Once the case is filed, the Debt Recovery Tribunal (DRT) will issue a notice to the borrower, allowing them an opportunity to respond to the creditor's claims.
2. **Receiving a recovery certificate from the DRT:** If the DRT rules in favour of the creditor, it will issue a recovery certificate. This certificate empowers the creditor to employ various methods, including attaching and selling the borrower's assets, to recover the outstanding debt.
3. **Attachment and sale of asset:** The creditor may utilise the recovery certificate to seize and sell the borrower's assets, including properties, vehicles, or funds from bank

accounts, to recover the owed amount. The proceeds from the sale will be applied towards settling the debt, and any excess funds will be returned to the borrower.

Note: Legal actions are generally considered a last resort for debt collection due to their complexity and the significant costs involved, including attorney fees, court fees, and other related expenses. Moreover, legal proceedings can damage the relationship between the borrower and the creditor. Therefore, it is crucial to seek legal advice before proceeding to court.

2.3.4 Post- Judgement Stage

Once the creditor receives the recovery certificate from the Debt Recovery Tribunal (DRT), they enter the post-judgement stage, where they proceed to implement the tribunal's decision for debt recovery. The following steps are involved in this stage:

1. **Debt collection method:** The creditor can utilise the recovery certificate to recover the outstanding debt from the borrower. This process may include various approaches, such as seizing and selling the borrower's assets, garnishing their wages, or freezing their bank accounts.



Wage Garnishment

A legal process where a portion of individuals' earnings is withheld for the payment of debt.

2. **Negotiation with the creditor:** There may be instances where the creditor and borrower can negotiate a mutually acceptable settlement.

- The creditor might extend the repayment schedule or lower monthly payments based on the borrower's financial situation.
- The creditor could accept a reduced lump-sum payment to settle the debt, allowing the borrower to avoid further collection actions.



Lump-sum payment

A single, one-time payment made in full, rather than in instalments.

3. **Repossession or Foreclosure:** If the debt is secured by collateral, such as a vehicle or property, the creditor has the right to repossess the asset (e.g., taking back a car) or foreclose (taking legal ownership of property for home loans).
4. **Bankruptcy:** In certain situations, the borrower may file for bankruptcy to restructure their debt. This process may involve selling assets to repay the creditor, leading to the discharge of some loans. The borrower can also request a repayment plan that allows them to pay off debts over a specified period (e.g., 3 to 5 years), with creditors receiving payments accordingly.



Discuss

Simran borrowed ₹5,00,000 from XYZ Bank with a repayment term of six years. She managed to pay the monthly EMI on time for the first year. However, after one year, she had a medical emergency and was unable to pay her loan repayments for over three months.

From the given scenario, **discuss** and explore what happens at each stage of the debt collection process when the borrower fails to meet their repayment obligations.



Knowledge Check

Answer the following questions:

1. Arrange them correctly: Post-Judgement Stage, Pre-collection stage, Legal stage, Collection stage.
2. The legal authority that handles cases related to debt recovery for banks and other financial institutions is known as _____.
3. In which of the debt collection stages is there a chance that the bank will involve a debt collection agency? _____
4. True or False: In the collection stage, the bank can seize the assets of the borrower without a court order. _____
5. True or False: Rekha has a credit card debt of ₹20,000 with ABC Bank. The first thing the bank will do is immediately contact the DRT. _____

Answers:

1. Pre-collection stage, Collection stage, Legal stage, Post-Judgement Stage, 2. Debt Recovery Tribunal (DRT), 3. Collection stage, 4. False, 5. False

3.0 Techniques for Effective Debt Collection

As previously discussed, debt collection plays a critical role in the financial management of institutions, businesses, and individuals. Effectively managing debt collection can be challenging without well-defined strategies in place. Therefore, it is essential to implement effective debt collection practices that not only facilitate the recovery of outstanding debts but also preserve a positive relationship with customers, ensuring long-term commitments.

In this section, we will explore various communication strategies and persuasion techniques that can enhance the effectiveness of debt collection efforts.

3.1 Communication Strategies for Effective Debt Collection

Effective debt collection relies heavily on strategic communication methods that foster understanding and cooperation between creditors and debtors. Here are some key strategies to consider:

1. Understand the Debtor's Perspective

It's essential to consider the debtor's personal or financial situation when communicating. Many debtors may face hardships such as job loss, medical emergencies, or business failures. Demonstrating empathy and acknowledging their concerns fosters a more positive relationship between the creditor and the debtor.

Example

XYZ Bank noticed that Ravi, a small business owner, had missed his loan payments for the last two months. Instead of immediately pursuing legal action, the bank representative approached Ravi to understand the issue. Ravi explained that one of his clients had delayed a payment, causing his payment delay. In response, the bank granted him a 15-day grace period to settle the overdue amount.

2. Clear and Concise Communication

To effectively communicate with a debtor, the message from the creditor must be simple and straightforward. Avoiding complex technical terms ensures that the information is easily understood by the debtor. Clear communication should mention the amount owed, the due date, and the consequences of non-payment.

Example

ABX Bank needed to contact Sneha, who had missed her credit card bill payments for the past three months. Rather than sending a complicated message, the bank used simple language to convey the necessary information:

"Dear Sneha, your payment of ₹10,000 is overdue. Please pay by 12/10/2024 to avoid additional charges. If you have any queries, kindly contact us at 0000000000."

This clear and concise message reduces the chances of confusion and ensures that the debtor understands the situation.

3. Active Communication

Effective debt collection requires two-way communication between the debtor and the creditor. Active listening plays a key role, as it helps the creditor understand the debtor's challenges and work out a repayment plan that benefits both parties.

Example

ABC Bank had given Remya a car loan, but after three months, she was unable to make payments. A bank representative called her to discuss the situation and learned that she had recently lost her job. Understanding her difficulties, the bank did not insist on immediate full repayment but instead allowed her to make smaller payments. A week later, Remya found a new job and managed to pay the full amount. This approach helped the bank recover the loan without damaging its relationship with Remya.

Active communication and flexibility can lead to a positive outcome for both the creditor and the debtor.

4. Offering a Flexible Payment Option

Many debtors intend to repay their loans but may struggle with the current repayment terms due to financial difficulties. Offering alternative payment plans, such as instalment options or temporary suspensions, can help debtors manage their repayments better and increase the chances of recovering the loan.

Example

PBC Bank had provided a loan to a textile industry owner in Punjab. Due to market fluctuations in the textile industry, the owner was unable to make full payments. Instead of demanding large overdue amounts, the bank offered more flexible terms, allowing the owner to extend the repayment period. Alternatively, the owner could start by paying 50% of the monthly instalment for six months and resume full payments once business conditions improve.

This flexibility helped the business manage its cash flow and increased the likelihood of recovering the loan without straining the debtor's financial situation.

5. Documentation and Record Keeping

Properly documenting all agreements and payments is essential for ensuring accountability and transparency. In case of any disputes, these records serve as crucial evidence for legal proceedings.

Example

Geetha received a notice from the bank stating that she had not paid her EMI for a car loan over the past few years. She claimed that all her payments had been made on time and that the bank was mistaken. However, the bank had maintained a detailed record of customer transactions, which indicated that Geetha had indeed missed payments.

This documentation helped the bank resolve the dispute professionally.

Note: We will learn this topic in detail in Unit 8, Documentation and Compliance in Debt Collection

6. Professionalism and Respect

Maintaining a respectful and professional tone during communication with debtors is crucial. Using harsh language can worsen the situation and make debt recovery more difficult.

Example

A student borrowed ₹50,000 from ABC Bank to finance his college education. When the bank representative contacted him regarding the unpaid loan, the student reacted defensively, sharing his frustration over unexpected tuition hikes and the impact on his finances, which delayed his repayment. Instead of escalating the situation, the bank representative responded calmly and offered a grace period of 30 days for repayment.

This respectful approach helped maintain a positive image for the bank and ultimately led to the successful recovery of the loan amount.

7. Timely Follow-up

Consistent follow-up is essential for effective debt recovery. Creditors should send a reminder payment notification a few days before the payment due date, followed by a phone call if the payment is missed. It is also important to avoid excessive or inappropriate communication when engaging with the debtor.

Example

SBS Bank employs a well-timed strategy for their borrowers. They send a reminder message well in advance about the upcoming due date, and if the debtor misses the payment, they follow up with a phone call four days after the due date to understand the reason for the missed payment.



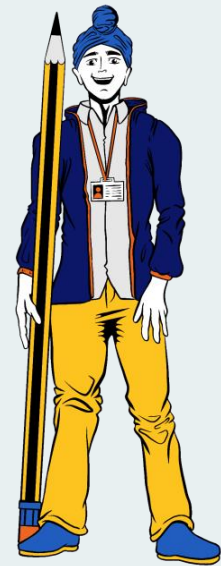
Knowledge Check

Answer the following questions:

Tick the correct answer:

1. The correct time to contact a debtor for debt collection is:
 - a. Early morning

- b. During regular business hours
 - c. Late night
 - d. Weekends only
2. Which form of communication is effective for keeping formal records of discussion?
 - a. Phone call
 - b. Verbal agreements
 - c. Text message
 - d. A formal letter or email
3. True or False: Debt collectors can talk aggressively to ensure that debtors repay on time and quickly. _____
4. True or False: As a debt collector, you always need to give a realistic timeline to the debtor rather than asking for immediate repayment. _____
5. True or False: If nothing works, a debt collector can misrepresent the amount owed to pressure the debtor to repay the amount. _____



Answers: 1. b. During regular business hours, 2. d. A formal letter or email, 3. False, 4. True, 5. False



Discuss

Imagine you are working as a debt collector for XYZ Bank in Punjab. You called Amar, a customer who has missed his last three monthly payments for a car loan. He is very upset and shares that he recently lost his job and cannot pay the monthly instalment.

What would you say to Amar, and how would you handle this situation?

3.2 Persuasion Techniques for Effective Debt Collection

Understanding and applying persuasion techniques is essential in debt collection, as they significantly influence the debtor's behaviour. By utilising strategies such as reciprocity, social proof, scarcity, consistency, and framing, debt collectors can effectively facilitate debt recovery.

1. Reciprocity

The principle of reciprocity states that individuals are more likely to respond positively when they feel they benefit from someone else's actions. When debt collectors offer small incentives or concessions, it encourages debtors to reciprocate positively, increasing the likelihood of repayment.

Example

Remya, a small business owner, took a loan of ₹1,00,000 from the bank to start her new venture. However, due to low sales in her shop for over three months, she struggled to make her monthly repayments. After missing several payments, the bank representative reached out to her. Instead of insisting on immediate repayment, the bank empathised with her situation by reducing the interest rate from 10% to 8% and extending the repayment period from 6 months to 13 months. This considerate approach motivated Remya to repay the loan.

2. Social Proof

Social proof is a principle where individuals look to the actions and experiences of others to guide their behaviour in uncertain situations. Debt collectors can use this principle by sharing stories of clients who have successfully resolved their debts, which can positively influence others and encourage them to take the necessary steps.

Example

Sneha, a teacher, took out a loan of ₹25,000 but encountered financial difficulties in repaying it. When a representative from XYZ Bank contacted her, they shared the story of Amit, another teacher, who had successfully repaid his loan by negotiating a lower interest rate and extending the loan term. By relating a story similar to Sneha's situation, the bank representative inspired her to take action toward repaying her loan.

3. Scarcity

The scarcity principle states that people place a higher value on items perceived as scarce. Debt collectors can use this principle to encourage debtors to prioritise repayment by creating a sense of urgency in the situation. This can include warnings about potential legal actions, negative impacts on credit scores, and increases in interest rates. Such urgency can motivate debtors to act quickly.

Example

Sita had a credit debt of ₹35,000 that she struggled to repay and was unaware of the consequences of non-payment. A debt collector from ABC Bank contacted her and explained that her unpaid debt would negatively impact her credit score, limiting her ability to secure loans in the future as well as the penalty interest rate she is incurring due to her non-payment. Upon realising the long-term implications of not repaying the loan, Sita decided to prioritise repayment. Her understanding of the importance of maintaining a good credit score motivated her to act swiftly.

4. Consistency

The principle of consistency mentions that individuals are motivated to behave according to their prior commitments and beliefs. In the debt collection process, this principle can effectively motivate debtors to adhere to repayment plans. For instance, debt collectors can encourage debtors to start with small repayments, which fosters a sense of accountability and increases the likelihood of continued payments.

Example

Arun, a small business owner, borrowed ₹40,000 from ABC Bank for shop renovations. Due to a financial crisis, he was unable to make payments for three months. When a debt collector from ABC Bank contacted him, they suggested an initial payment of ₹5,000. The bank emphasised the importance of maintaining his commitment to repay the debt, reassuring him that he could gradually increase his payments as his financial situation improved.

5. Framing

Framing refers to the way information is presented to influence perceptions. In the context of debt collection, how repayment options and their consequences are framed can significantly impact a debtor's motivation and willingness to repay. By presenting repayment as a positive and achievable goal rather than an overwhelming burden, debt collectors can inspire debtors to take action.

Example

Hiba took an education loan of ₹1,00,000 from XYZ Bank but missed four monthly instalments, leaving her with an outstanding balance of ₹70,000. When a debt collector from the bank called her, they highlighted the progress she had made with her previous payment of ₹30,000, rather than focusing solely on the remaining ₹70,000. The collector also mentioned that making regular payments could improve her credit score and increase her chances of securing future loans.



Knowledge Check

Answer the following questions:

In the scenarios below, choose the approach or response you believe is the most effective way to deal with the scenario as a debt collector.

1. Amritha took a housing loan and has missed the last five repayments. You found out she recently lost her job. How will you approach this situation?

- a. Request an immediate payment.
 - b. Empathise with their situation and offer flexible payment options accordingly.
 - c. Ignore their situation and proceed with the legal procedure.
2. A debtor shouted on the call because he was scared about his financial situation. He was confused about what to do in the future. As a debt collector, how should you respond?
 - a. You need to repay the loan as soon as possible.
 - b. This is your problem; you need to manage it better.
 - c. I understand your situation; I am here to help you. Let us find a solution to resolve this together.
3. Riya was unable to pay a small amount she had borrowed by the due date. How should your response be?
 - a. Offer a partial payment plan, increase her loan term, and suggest a lower monthly instalment.
 - b. Tell her that if she doesn't pay the full amount by the given date, there will be a legal charge against her.
 - c. Remind her about the repayment plan and continue with the normal process.



Answer:

- 1) b) Empathise with their situation and offer flexible payment options accordingly;
- 2) c) I understand your situation; I am here to help you. Let us find a solution to resolve this together.
- 3) a) Offer a partial payment plan, increase her loan term, and suggest a lower monthly instalment.



Activity 2: Role Play as Debt Collector and Debtor

Objective: To understand effective ways of communicating in a debt collection situation.

Instructions:

- Split the class into pairs and sit facing each other.
- One student will be a debt collector, and the other will be a debtor.
- The debt collector can start the conversation by asking the debtor to repay the outstanding debt.
- The debtor can explain the reason for not being able to make the full payment.



- The debt collector should listen carefully to the debtor's situation and work together to find a solution that both parties can agree upon.
- After a few minutes, the students can switch roles so that both students can practise as debt collectors and debtors.

4.0 Handling Objections And Excuses

During debt collection, debtors often raise objections and excuses that can hinder the recovery process. To effectively handle these situations, debt collectors should be prepared with strategies to address objections calmly and clearly. Here are some key strategies:

4.1 Common Objections and Excuses from Debtors

In this section, we will learn about some common objections and excuses from debtors and how you, as a debt collector, can respond effectively to these objections.

1. Objection/ Excuse: I don't owe this debt.

This type of objection often arises when the debtor questions the legitimacy of the debt. In such situations, you need to remain calm and explain the debt's validity. To clarify, you can provide a list of documents, such as invoices, contracts, or transaction records, to support your claim. This will help address the misunderstanding and build trust.

- **You can respond by saying:** *"I understand your concern, but according to our documents, you signed our loan agreement on 04/10/2024, which outlines the terms of this debt. I can share a copy of this agreement with you for reference. If you have any doubts, I am happy to clarify them."*

2. Objection/ Excuse: I cannot afford to pay the amount right now.

A debtor may be facing financial difficulties, such as a high cost of living, medical expenses, education costs, job loss, or other family obligations. During this time, it is important for you to empathise with their situation and offer a flexible solution, such as a smaller and more manageable instalment. This demonstrates your support during difficult times and helps find a solution that works for both parties.

- **You can respond by saying:** *"I completely understand your situation, and we don't want to put extra pressure on you. We are planning to offer a repayment plan that fits your budget; we can extend the repayment period so you can start paying smaller amounts, and later, if your situation improves, we can revert to the normal repayment plan."*

3. Objection/ Excuse: I have already paid the debt.

Debtors may claim that they have already made payments. In such a situation, politely ask them for proof of payment, such as receipts or bank statement details, and cross-check with your records. If you find any discrepancies, discuss the issue with the debtor and work towards a resolution.

- **You can respond by saying:** *"Thank you for letting us know you paid the debt. However, according to our records, the debt amount is still pending. Since you have already made the payment, could you please share the receipts or any proof of payment you have so that I can look into it and ensure everything is accurate?"*

4. Objection/ Excuse: I don't trust this collection agency.

One common issue debt collectors face is dealing with the debtor's trust issues. Many debtors feel nervous or anxious about the process. One effective way to handle such a situation is to build transparency, clarify your role, and reassure the debtor that their rights are safeguarded.

- **You can respond by saying:** *"I understand your concern about dealing with collection agencies. I can assure you that our goal is not to cause any trouble but to resolve the matter fairly and respectfully. We guarantee that all your rights are respected. If you have any questions or doubts, I will explain everything about our agency in detail."*

4.2 Dealing with Debtors Properly

It can be challenging to deal with debtors during the debt collection process. Some individuals may be uncooperative, avoid communication, or even become angry for some reason. This can be a difficult task for the debt collector. However, the debt collector needs to remain calm and professional while using the effective strategies mentioned below to handle the situation.

- Always establish **clear communication** with the debtor. Ensure that you have a solid understanding of the situation and possess accurate information about the debtor. Then, determine how you want to communicate with the debtor—through phone calls, messages, emails, or face-to-face communication.
- Always **listen** to what the debtor has to say. Instead of pressuring them, allow them to express their feelings, try to understand their perspective, and create an environment where you can collaboratively find a solution.
- After discussing the situation with the debtor, if they are facing difficulties, **offer them financial payment options** to ease their burden.
- Many debtors are unaware of the **consequences** of not paying the debt. Thus, a debt collector needs to emphasise how non-payment can affect their credit score or lead to legal action.
- Maintain **records** of all documents as proof of your attempts to resolve the debt. This can serve as essential evidence if the debt collector plans to take legal action. Ensure that all details are noted, such as dates, what was discussed, and any agreements made.

- Negotiation is crucial when dealing with debtors. The debt collector needs to be ready to **offer compromises**, such as reducing the interest rate, extending the loan, or accepting partial payments.
- Sometimes, even after all efforts, the debtor may remain uncooperative. In such cases, consider taking **legal action**, but this should be a **last resort** after exploring other methods.

Note: We will learn more about this topic in Unit 8, Documentation and Compliance in Debt Collection.



Knowledge Check

State True or False:

1. As a debt collector, it is acceptable to ignore a debtor's objection if you feel that they don't seem valid to you. _____
2. A debt collector cannot visit the debtor's home at any time of the day to collect the payment. _____
3. Recording a call without the debtor's permission is acceptable as long as it is for the debt collection process. _____
4. It is always better to argue with the debtor who is making excuses rather than providing them with alternative solutions. _____
5. If a debtor is confused about their debt amount, then the debt collector must clarify all the questions that they have. _____



Answers

6. False 2. True 3. False 4. False 5. True



Activity 3: Role Play on Common Objections and Excuses from Debtors

Objective: Understand how to professionally manage various objections and excuses from debtors.

Instructions:

- Divide the class into pairs.
- One student will play the role of a debtor, and the other will play the role of a collector.
- A box will contain a list of cards, each with an excuse/reason written on it, such as:
 - I don't have money right now.

- I'm facing a big financial issue and cannot pay the full amount.
 - I lost my job, and I'm unable to pay the money.
 - I have already paid you the money.
 - The amount is wrong, so I'm not paying the amount.
 - How can I know that you are a genuine debt collector?
- The debtor will pick a card and read it aloud.
 - The debt collector will respond professionally to resolve the issue.
 - Each group will have 5 minutes to complete their role-play, after which the next pair will repeat the same steps.



Let's Recap

1. **Debt collection** is the process that banks and other financial institutions use to **recover money** from individuals or organisations that have not paid their loans.
2. The person or organisation responsible for collecting the debt is known as a **debt collector**.
3. The debt collection process is governed by **The Reserve Bank of India, The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act of 2002, The Recovery of Debts Due to Banks and Financial Institutions (DRT) Act, 1993**. These regulatory bodies are the backbone of debt collection and protect the interests of both the debt collector and the debtor.
4. The debt collection process uses methods such as **in-house debt collection, third-party debt collection agencies, and legal debt collection**.
5. The debt collection process can be broadly classified into four stages: **pre-collection, collection stage, legal stage, and post-judgement stage**.
6. Debt collection techniques can be done through **effective communication and persuasion techniques**, enhancing the chance of recovering the debt collection.
7. During the debt collection process, it is common for the debtor to present **objections and excuses**. Therefore, the debt collector must handle the situation in a **professional manner** that works to provide a solution.



EXERCISE

Objective Type Questions

Fill in the blanks:

1. The money borrowed from others with a promise to repay in the future is called_____.
2. NPA stands for _____.
3. DRT Stands for_____.
4. There are _____stages in the debt collection process.
5. The full form of ODR is _____.
6. The full form of NBFC is _____.
7. RBI stands for _____.

Short Answer Type Questions

8. Explain the meaning of debt and debt collection.

9. What are Non-Performing Assets?
10. Define Legal Debt collection method.
11. Explain the term Bankruptcy.
12. Describe the pre-collection stage in the debt collection process.
13. Explain the legal stage in the debt collection process.

Long Answer Type Questions

14. Which communication strategies are effective for debt collection?
15. What are the different persuasion techniques used for effective debt collection?
16. Explain the different stages of the debt collection process.

ANSWER KEY

Objective Type Questions

Fill in the blanks:

1. Debt
2. Non-Performing Assets
3. Debt Recovery Tribunal

4. 4
5. Online Dispute Resolution
6. Non-Banking Financial Companies
7. Reserve Bank of India

UNIT 08

Documentation and Compliance in Debt Collection

Topics

- Documentation and Record-Keeping in Debt Collection
 - What is Documentation and Record-Keeping?
 - Why is Documentation Important in Debt Collection?
 - Types of Documentation in Debt Collection
 - Debt Collection Process Flowchart
- Dealing with Difficult Situations and Conflict Resolution
 - Handling Difficult Situations
 - Dealing with Aggressive Debtors
 - Navigating Legal Issues Related to Debt Collection
 - Conflict Resolution
 - Key Skills Involved in Conflict Resolution
 - Resolving Disputes with Debtors
- Ethics and Compliance in Debt Collection
 - Key Ethical Principles in Debt Collection
 - Compliance with Relevant Laws and Regulations
 - Importance of Compliance
 - RBI Guidelines for Debt Collection: An Overview
 - Impact of Compliance on Borrower Relations
 - Consequences of Non-Compliance in Debt Collections
 - Best Practices for Compliance

Learning Objectives

- Define the role of documentation and record-keeping in the debt collection process.

- Understand the essential steps in handling difficult situations and conflict resolution in debt collection.
- Apply conflict resolution techniques to manage difficult debtor situations.
- Explore the ethical principles that govern debt recovery practices.
- Identify best practices for ensuring compliance with relevant laws, including the RBI guidelines.



Materials Required

- Sample Debt Collection Records (Communication Logs/Payment Receipts/Debtor Agreements)
- Debt Collection Policy Templates (Templates outlining ethical debt collection practices and compliance standards)
- Sample of a Debt Recovery Notice to Borrowers



Activity 1: Before We Begin!

Imagine you are a debt collector working for a bank. You have been handling the case of a customer who owes ₹50,000. You have followed all the debt collection steps, but now the customer is disputing the amount owed. They claim they only owe ₹40,000 and have already paid ₹10,000.

Your task is to gather the documents and evidence needed to resolve the issue. Which documents would you look for to prove the correct amount owed? Why are they important?

1.0 Documentation and Record-Keeping in Debt Collection

1.1 What is Documentation and Record-Keeping?

Documentation and record-keeping involve creating, organising, storing, and managing important information. In debt collection, this includes keeping track of all the paperwork and digital records of interactions between the lender (like a bank) and the borrower (the person who owes the debt).



Discuss

Reflect on your experiences: Have you ever kept records of an important project or event? How did it help you stay organised?

Proper documentation, like transaction logs and communication records, is essential for managing daily operations smoothly. Accurate and up-to-date records ensure that organisations comply with the law and protect themselves if any disputes arise.

1.2 Why is Documentation Important in Debt Collection?

When a debtor refuses to pay, they might deny owing the debt by claiming they never received the service or bill, or they might argue that the debt is too old to be collected. These tactics can sometimes succeed if businesses fail to keep accurate records, highlighting the importance of carefully documenting each transaction.

Documentation helps **track** the amounts repaid and still owed, ensuring a clear record of debt repayment progress.

Proper records serve as **legal proof** in case of disputes with the debtor, protecting the lender in legal situations by providing clear evidence of all communications and transactions.

Accurate documentation **prevents misunderstandings and errors** in the collection process, facilitating smooth communication and reducing conflicts.

By documenting all debt collection communications, lenders ensure compliance with **legal regulations**, helping avoid penalties or legal complications.

Example (Lack of Documentation Leads to Financial Loss)

A small microfinance company issued a ₹50,000 loan to a local shop owner. The borrower made several partial payments but eventually stopped. Although the company had phone conversations and in-person meetings with the borrower, they failed to properly document these interactions or maintain detailed payment receipts.

Later, the borrower claimed to have paid ₹30,000, but due to inadequate documentation, the company couldn't confirm the exact amount still owed. As a result, the borrower refused to pay the remaining ₹20,000, and the company couldn't pursue legal action because they lacked proper records, leading to a financial loss.

Reflection Question: *How could the microfinance company have avoided this situation? What steps should they have taken?*

Example (Effective Documentation Resolves Disputes)

Satleen, a debt collector, is managing a case with a debtor named Gurpreet. Throughout their interactions, Satleen diligently records every call, noting Gurpreet's concerns, his promises regarding payment, and any issues he raises.

One day, Gurpreet disputes that he ever agreed to a payment plan. However, Satleen can quickly find the recording of the call where Gurpreet had confirmed his agreement. She

shares this with her manager, Rajesh, which helps clarify the situation and resolve the misunderstanding efficiently.

1.3 Types of Documentation in Debt Collection

Type of Documentation	Description
Letters to Debtors	Written communications detailing the debt, including payment reminders and settlement proposals.
Communication Logs	Records of all interactions with debtors—phone calls, emails, letters, and in-person meetings—documenting dates, times, summaries, and any commitments made.
Payment Receipts	Official documents confirming payments made by the debtor, specifying the amount and date of each transaction.
Legal Documents	Formal papers such as court orders and judgments are necessary for any legal actions related to the debt.
Debtor Information	Comprehensive profiles for each debtor, including personal details (name, address, contact information), account numbers, outstanding balances, and payment history.
Agreements and Settlements	Written agreements for negotiated payment plans or settlements, specifying terms, deadlines, and potential consequences for non-compliance.
Dispute Resolutions	Documentation of the investigation process for disputed debts, including evidence gathered and final outcomes.

An example of a formal notice for a debtor who has failed to make a payment

<p style="text-align: center;">Legal Notice</p> <p>Ref. No. _____ Dated: _____</p> <p>REGD.A.D.</p> <p>LEGAL NOTICE</p> <p>To,</p> <p><u>Satpal Singh</u></p> <p>Dear Sir,</p> <p>Pursuant to the instructions from and on behalf of my client <u>HDFC Bank Ltd.</u>, through its <u>Debt Collector</u>, I do hereby serve you with the following Legal Notice: -</p>
--

1. That my client is a Bank firm/individual under the name and style of M/s HDFC Bank Ltd.
2. That my client provided you with a loan amounting to ₹50,000/- via cheque no. 879463, dated 01/04/2022.
3. That despite acknowledging your liability for repayment of the principal sum of ₹50,000/-, you have deliberately failed to make the due payment to my client. This non-payment appears to be intentional and made in bad faith, rendering you liable for the full repayment. You are, therefore, liable to repay not only the principal balance of ₹50,000/- but also interest at a rate of 8% per annum from the due date until the full realisation of the amount. The total outstanding sum as of today stands at ₹58,320/-.
4. That you are liable to pay the total amount of ₹58,320/- to my above-named client and my above-named client is entitled to recover the same from you.
5. That my client requested you several times through telephonic messages and by sending a personal messenger to your office for the release of the said outstanding payment. However, you have consistently delayed payment by citing various excuses and have not remitted even a single paisa of the outstanding amount.

I, therefore, through this Notice finally call upon you to pay my client ₹58,320/- , along with future interest @ 8% p.a. from the date of notice till the actual realisation of the said amount. Additionally, a notice fee of ₹100/- is to be paid, all of which can be settled via cash, demand draft, or cheque— whichever mode suits you better. This payment must be made within 30 days of receipt of this Notice.

Failure to comply within the stipulated period will leave my client with no option but to initiate civil and criminal proceedings against you in the appropriate court of law. In such an event, you will bear full responsibility for the consequences.

Please note that a copy of this Notice is being retained in my office for future reference and further action.

(Basant Gupta)
ADVOCATE



Activity 2: Exploring Documentation in Debt Collection

Objective: Understand the significance of documentation in debt collection through research and real-life examples.

Instructions:

1. Choose one type of documentation from the list (e.g., Letters to Debtors, Payment Receipts).
2. Investigate its importance in debt collection, focusing on its role and best practices.
3. Provide a relevant example of how this type of documentation was effectively used in a real-life debt collection scenario.
4. Prepare a brief 3-5 minute presentation summarising your research and example to share with the class.



Knowledge Check

Answer the following questions:

1. Why is accurate record-keeping important in the debt collection process?

2. What key information should debtor profiles include?

1.4 Debt Collection Process Flowchart

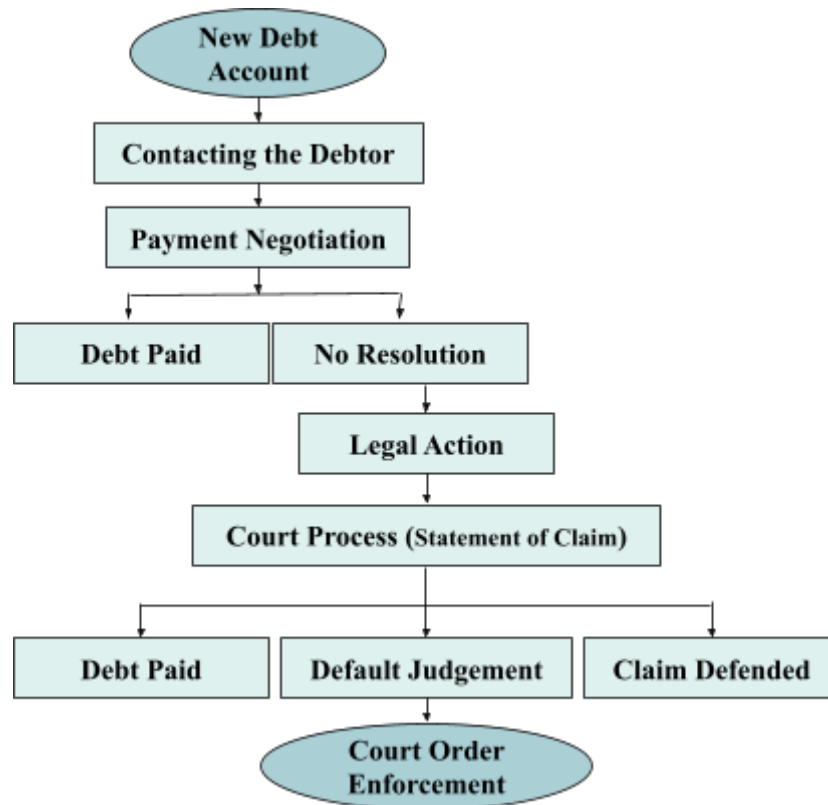
When a person or business owes money (a debt), the lender starts by registering **a new debt account**. Once the debt is confirmed, the lender **contacts the debtor** (the person who owes the money) through letters, phone calls, emails, and SMS messages. These messages remind the debtor to pay what they owe.

If the debtor responds, the lender may enter into **payment negotiations**, where they agree on how and when the debt will be paid. The debtor might offer to pay in instalments or settle the debt in another way.

If the debt is paid, the process stops here. However, if there is no resolution, meaning the debtor doesn't pay or respond, the lender may need to take **legal action** to recover the money.

In the legal process, the lender files a **Statement of Claim** in court, which is an official request to recover the debt. Once this is done, the debtor can either pay the debt or ignore the claim. If

the debtor pays after receiving the claim, the case is closed. But if they don't respond, the court can issue **a default judgement**, which allows the lender to collect the money legally. Sometimes, the debtor might choose to **defend the claim**, meaning they argue against the debt in court. If the court sides with the lender, **the court enforces the decision**, and the debtor has to follow the court's orders.



Discuss

Should debt collection agencies be allowed to take legal action without first attempting to resolve the debt through negotiation?

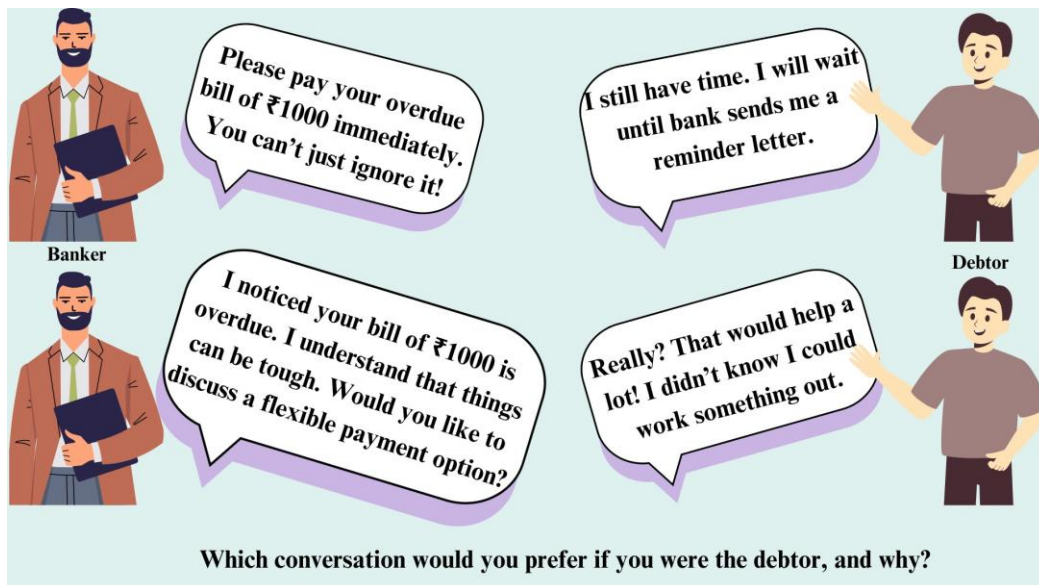
2.0 Dealing with Difficult Situations and Conflict Resolution

2.1 Handling Difficult Situations

Navigating challenging situations in debt collection is key to maintaining professionalism and achieving positive outcomes. As a debt collector, your goal is to resolve issues calmly and avoid escalation.

In Chapter 7, we discussed communication strategies crucial for effective debt collection. A significant part of the debt collection process depends on clear and efficient communication

between all involved parties at various stages of collection. Proper communication ensures that both the debtor and the creditor understand the terms, amounts owed, and possible solutions for



repayment. Now, let's explore strategies for managing difficult scenarios effectively.

Active Listening

Active listening is key in difficult customer interactions. Focus on the customer's concerns, let them speak without interruption, and paraphrase their main points to show understanding. This helps validate their feelings and encourages solutions that work for both parties.

Remain Calm and Professional

In difficult situations, it's crucial to stay calm and composed. Even if the customer becomes angry or abusive, avoid reacting emotionally. Maintain professionalism, understanding that their frustration is with the situation, not directed personally at you.

Empathise and Validate

Empathy helps diffuse tense situations. Acknowledge their challenges with statements like, "I understand this is difficult for you." This validation can foster rapport and lead to more productive conversations.

Offer Flexible Payment Options

For customers facing financial difficulties, offering smaller instalments or temporarily pausing payments can encourage repayment while maintaining a positive relationship.

Educate and Communicate Clearly

Clear communication is essential. Explain the debt process, outstanding balances, potential consequences of non-payment, and available solutions. Transparency helps avoid misunderstandings and allows customers to make informed decisions.

Follow Up and Follow Through

Stick to promises and communicate delays clearly. Regular follow-ups show dedication to resolving concerns.

Know When to Seek Assistance

If the situation escalates beyond your control, get help from a supervisor to defuse or resolve the issue.

Handling difficult customers in collections requires empathy, professionalism, and effective problem-solving. By listening actively, showing empathy, and offering flexible solutions, you can turn challenging interactions into opportunities to build trust and strengthen customer relationships.

2.1.1 Dealing with Aggressive Debtors

Dealing with aggressive debtors can be emotionally challenging, but using the right strategies helps collectors maintain professionalism. This section outlines effective techniques to manage such interactions while upholding ethical debt collection practices. Each encounter is a chance to demonstrate your skills and commitment to a calm resolution.



1. **Maintain Composure:** When a debtor raises their voice or uses aggressive language, your initial reaction should be calmness. It's natural to feel a surge of emotions, but it's essential to remain composed. For instance, if a debtor yells, "**I refuse to pay this!**" respond professionally, such as saying: "**I understand you are upset, and I am here to help resolve this.**"
2. **Establish Boundaries:** If a debtor becomes verbally abusive, it's important to set boundaries. Assert your position firmly but respectfully, stating that while you are willing to assist, abusive behaviour will not be tolerated. You might say, "**I want to assist you, but I need us to have a respectful conversation. Let's try to find a solution together.**"
3. **Acknowledge Their Emotions:** Show empathy by validating their feelings. For example, if a debtor expresses frustration, say, "**I can see that this situation is frustrating for you, and I want to understand your concerns better.**" This approach helps in diffusing tension and building rapport.
4. **Direct the Conversation Towards Solutions:** Focus on resolving the issue by asking questions. For example, "**What can we do to make this payment manageable for you?**" This shift encourages collaboration and reduces the focus on their aggression.
5. **Involve a Supervisor When Necessary:** If the situation escalates despite your efforts, do not hesitate to involve a supervisor. You could say, "**Let me get my supervisor to help us find a better solution,**" which shows that you are taking their concerns seriously while seeking additional support.

By employing these strategies and examples, you can create a safer and more productive environment when dealing with aggressive debtors. Remember, the goal is to transform confrontation into constructive dialogue.



Activity 3: Strategies for Managing Difficult Scenarios

Objective: To visually represent effective strategies for managing difficult debt collection scenarios.

Instructions:

1. Choose key strategies such as active listening, staying calm, showing empathy, offering flexible payments, and clear communication.
2. Create a poster that includes a title, key strategies with brief descriptions, and engaging visuals or hypothetical scenarios.
3. Share your poster with the class, explaining your strategies.
4. Hang the posters around the classroom to share insights.



2.1.2 Navigating Legal Issues Related to Debt Collection¹

When collecting debts, banks must operate within specific laws to ensure they are both legally compliant and ethically sound. Below are key Indian laws related to debt collection and their practical implications for banks:



1. Securitisation and Reconstruction of Financial

Assets and Enforcement of Security Interest (SARFAESI) Act, 2002: As we learned in the last Unit, the **SARFAESI Act** empowers banks to recover loans quickly by taking control of and selling the borrower's assets without going through lengthy court processes.

What the Law Allows: **Banks can take possession of the borrower's collateral** (such as property) if they fail to repay, but must first give them notice. This act allows the bank to sell the collateral through an auction.

Procedure: A demand notice is sent, giving the borrower a period (usually 60 days) to repay. If the borrower fails to repay, the bank can seize and sell the asset to recover the money.

¹ Credgenics. (2024, February 21). Why should you know debt recovery laws in India? | Credgenics Blog. Blog. <https://blog.credgenics.com/understanding-debt-recovery-laws/>

Debtor Rights: Borrowers have the right to redress grievances and can file an application to the Debts Recovery Tribunal (DRT) within 45 days if they feel their rights have been violated.

This act is a powerful tool for banks, but it must be used responsibly to avoid unfair practices.

2. Recovery of Debts Due to Banks and Financial Institutions (RDDBFI) Act, 1993:

This law created **Debt Recovery Tribunals (DRTs)** to help banks recover money quickly. **DRTs handle cases related to large amounts of unpaid loans, allowing banks to settle disputes without going through traditional courts.**

What the Law Allows: Banks can file cases in DRTs to recover unpaid loans, significantly reducing the time and procedural complexities involved in regular court systems.

This act provides banks with a more efficient system for resolving debt-related disputes.

3. Insolvency and Bankruptcy Code (IBC), 2016: The IBC provides a structured time-bound process for banks to deal with borrowers who are unable to repay their debts. *Insolvency means a situation where a borrower is unable to meet their financial obligations to creditors, essentially being unable to pay back what is owed.* The IBC is primarily used in cases involving corporate debtors (businesses) and aims to manage the borrower's assets to repay the bank.

What the Law Allows: **The bank can start insolvency proceedings against a borrower who cannot repay a significant debt.** An insolvency professional is appointed to manage the process and ensure creditors (banks) get their money.

This code helps banks recover debts in an organised and legally sound way.

4. Negotiable Instruments Act, 1881: The Negotiable Instruments Act governs the use of negotiable instruments like cheques, promissory notes, and bills of exchange. **When a borrower issues a cheque to repay a loan, and it bounces due to insufficient funds, this act provides a legal framework for recovery.**

What the Law Allows: If a cheque is dishonoured (bounces), the bank can issue a legal notice to the borrower, demanding payment. The borrower is usually given 15 days post the notice to settle the amount. If the borrower fails to pay, the bank can file a legal case under the act, specifically invoking **Section 138**, which addresses penalties for dishonoured cheques due to insufficient funds.

This law provides banks with a clear and efficient mechanism to handle cases of dishonoured cheques, ensuring timely recovery of debts.



Knowledge Check

Answer the following:

Write the full form of the following laws related to debt collection:

1. SARFAESI Act _____
2. RDDBFI Act _____
3. IBC _____
4. DRT _____



Activity 4: Drafting a Legal Notice

Objective: To improve students' skills in drafting legal notices and deepen their understanding of debt collection laws.

Instructions: Fill in the blanks in the legal notice template below with the appropriate details. Use the prompts provided to guide your responses.

REGD.AD/SPEED POST/COURIER

DATED: _____

To,

[Name _____]

[Designation _____]

[Address _____]

[Pin code _____]

LEGAL NOTICE

Sir/Madam,

Under instruction from and on behalf of my client [_____]

S/o [_____] R/o [_____] (hereinafter referred to as “my client”). I do hereby serve you with the following legal notice:

1. That you issued my client a Cheque No [_____] dated ____ for the sum of ₹ [_____] /- (In words: [_____]) against the goods purchased by you vide Bill No [_____] dated ____.
2. That the said cheque was presented by my client at [_____] **CLIENT BANK NAME**, [_____] **CITY** for credit in his account in the month of [_____] , but it bounced due to insufficient funds. My client hereinafter

contacted you and was assured of cash in lieu of the bounced cheque; therefore, my client did not take legal action earlier.

3. That my client thereafter again requested many times for the payment of the said cheque amount by [_____] **method of communication: telephone, email, personal visit, etc.**], but in vain.
4. That in [_____] **MONTH/YEAR**], my client again tried depositing the cheque with [_____] **CLIENT BANK NAME**], [_____] **CITY**] but it was again returned as unpaid with remarks – Funds Insufficient, vide [_____] **DRAWER BANK NAME**] memo dated ____.
5. That it appears that in order to cheat and defraud my client and without any intention on your part to pay my client, you had deliberately and intentionally issued the aforesaid cheque, knowing that it was bound to be dishonoured on account of 'Insufficient funds' in your bank account.
6. That your said act and conduct render you liable to be dealt with under the provisions of Section 138 of the Negotiable Instruments Act, besides rendering you liable to be punished for the offence under Sections 406/420 of IPC.

By means of this legal notice, I hereby call upon you to pay the cheque amount of ₹[_____]/- (Rupees [_____] to my client within 15 days from the date of receipt of this notice failing which I have clear instructions from my client to take appropriate legal action against you in the competent court of law at your risks, costs, and consequences. You are also liable to pay Rs. [_____] **Notice Fee**]/- as the fee for this notice.

Also note, that I have retained a copy of this notice in my office for further reference.

(_____) **Advocate Name**)

Advocate

[_____] **City**

[_____] **Date**

Discuss: How does the legal framework (like Section 138 of the Negotiable Instruments Act) support the client's claim?

2.2 Conflict Resolution

Conflict resolution involves methods and processes to facilitate the peaceful ending of conflict and retribution. Effective conflict resolution can lead to better relationships with clients, increased recovery rates, and improved overall customer satisfaction.



2.2.1 Key Skills Involved in Conflict Resolution

Communication Skills

- Active Listening: Understanding the debtor's concerns and frustrations.
- Clear Articulation: Conveying information clearly to avoid misunderstandings. Instead of saying, “**Your account is in arrears,**” you might say, “**You have an outstanding balance on your account.**”

Empathy

- Understanding Perspectives: Putting yourself in the debtor’s shoes to understand their situation.
- Building Rapport: Establishing a connection to ease tensions. For instance, if a debtor is upset about their financial situation, saying, “**I understand this must be hard for you,**” can help build rapport and trust.

Problem-Solving and Negotiation

- Identifying Solutions: Analysing the situation and offering flexible options, like **manageable payment plans.**
- Finding Common Ground: Working towards a win-win solution through compromise and negotiation, such as **agreeing on a middle payment amount.**

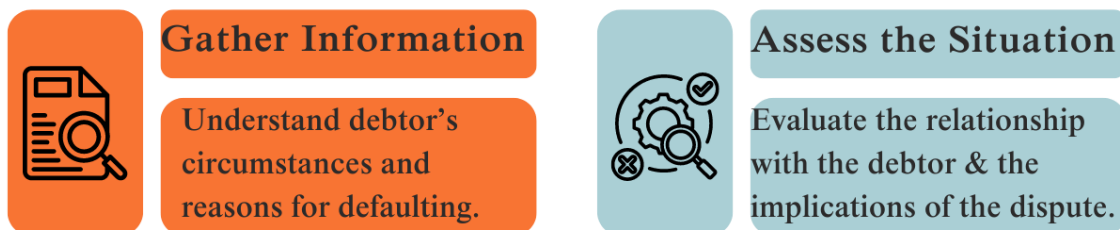
Patience and Emotional Control

- Staying Calm: Managing emotions during heated discussions.
- Taking Time: **Allowing time for the debtor to express their concerns** without rushing.

2.2.2 Resolving Disputes with Debtors

Resolving disputes with debtors effectively is crucial for maintaining positive relationships while ensuring that debts are collected. Below are strategies that debt collectors can employ to resolve disputes successfully.

Initial Steps



Strategies for Resolution



Recall how third-party agencies can be hired for debt collection (Unit 7). As discussed in Section 2.2, Unit 7, different debt collection methods can be employed before escalating to legal recourse.

Follow-Up



Example (Handling Customer Payment Disputes)

A customer, Harpal Singh, calls and says he has questions about the amount he needs to pay.

Listen actively and empathetically: “Hi Harpal ji, I see you have some concerns about the amount you need to pay. Thank you for calling to clear this up! Can you tell me more about the payments you have made and when?”

Remain calm and professional: “I’m sorry for any confusion this has caused you. We are here to help you sort this out quickly.”

Clarify the facts and the policies: “From our records, the original amount was ₹50,000, and the last payment we received was ₹15,000 on January 15th. So right now, it looks like your balance is ₹35,000, plus interest and fees. We usually update our records within a day

of receiving a payment and send a confirmation email. Do you have any proof of your payment, like a receipt or bank statement?”

Negotiate a mutually acceptable solution: “Thanks for sharing that! I see that you paid ₹25,000 on February 10th, but it seems there was a technical issue, and we didn’t process it. I’m sorry about that. I’ll get it fixed right away! So now your balance is ₹10,000, plus interest and fees. I can offer you a 10% discount if you settle the remaining amount today, or we can set up a payment plan that works for you. What would you prefer?”

Example (Supporting Customers During Financial Hardships)

A customer, Bableen Kaur, calls to discuss her inability to make payments due to a recent job loss.

Listen actively and empathetically: “Hi Bableen ji, I understand you are facing some tough times right now. Thank you for reaching out. Can you share a bit about what’s going on?”

Acknowledge the situation: “I’m really sorry to hear that you are dealing with this. Losing a job can be really challenging, and I completely understand how it can affect your ability to make payments.”

Explore alternative arrangements: “Let’s see how we can work together. We can discuss a temporary payment plan that suits your current situation. Would it help if we reduced your monthly payments for a while or extended your payment timeline?”

Foster goodwill: “I appreciate your honesty, and we want to support you during this time. Finding a solution that works for you is our priority. What other options would you feel comfortable with?”



Discuss the approach you would take to resolve a conflict with a debtor, such as a disagreement over the amount owed or missed payments. What strategies from this section would you incorporate, and why do you think they would be effective?

3.0 Ethics and Compliance in Debt Collection

When it comes to debt collection, ethical practices should always be the foundation of your approach. Debt collection is a sensitive process, and it's important to remember that behind every unpaid bill or overdue account, there is a person who may be experiencing financial difficulties or other challenges. By maintaining empathy and professionalism, debt collectors can uphold ethical standards while also increasing the chances of successful collections.

3.1 Key Ethical Principles in Debt Collection

1. **Fair Communication:** Debt collectors must ensure their communication with debtors is clear, honest, and respectful. They must avoid aggressive language and maintain professionalism throughout the collection process.

Example: A debt collector should clearly explain the debt details (amount, due date, and payment options) without resorting to threats or coercion. For instance, saying "**You must pay by tomorrow, or we will take legal action**" may create undue stress, whereas, "**We encourage you to make a payment arrangement within the next 10 days to avoid further complications**" is both respectful and effective.

2. **Confidentiality and Privacy:** Maintaining the privacy of debtors is paramount. Debt collectors should not disclose the debtor's financial situation to third parties, such as family members or colleagues. The information should be kept confidential between the collector and the debtor.

Example: If a debtor's spouse answers the phone, the collector must not disclose any details about the debt. Instead, they should leave a message asking the debtor to return the call without revealing personal or financial information.

3. **Non-Harassment:** Debt collectors must avoid repeated or excessive communication that could be deemed harassing. There are laws in place that regulate the number of times a collector can contact a debtor in a day or week. Aggressive tactics, such as visiting a debtor's home or workplace without prior arrangement, should be avoided.

Example: A debt collector calls a debtor once a day but respects a gap of at least 24 hours between each attempt, ensuring not to call outside of regular business hours.

4. **Respect for Debtor's Circumstances:** Debt collectors should understand that some debtors are unable to pay due to genuine financial hardships. While it is important to

collect the owed money, offering flexible payment options or negotiating a settlement is an ethical way to resolve the situation without undue pressure.

Example: A debtor explains they are going through a medical crisis and cannot make the full payment. The collector offers a plan allowing smaller monthly payments to avoid further legal action.



Discuss

Imagine this scenario: A debtor claims they have been receiving phone calls from a debt collector at all hours of the day, despite having requested that the calls be limited to specific times. The debtor is feeling harassed and frustrated, but the debt collector still needs to recover the outstanding debt.

What steps should the debt collector take to balance their responsibility of recovering the debt with the debtor's request for limited contact?

3.2 Compliance with Relevant Laws and Regulations

Compliance in debt collection refers to adhering to legal standards and ethical guidelines established by regulatory authorities. This ensures that debt collection practices are conducted fairly, transparently, and responsibly. In India, debt collection is governed by various laws that empower banks and financial institutions to recover dues while ensuring that the process remains fair and compliant with established regulations.

3.2.1 Importance of Compliance

Legal Protection	Reputation Management	Consumer Protection
Helps organisations avoid legal repercussions and penalties associated with violating debt collection laws.	Maintains the integrity and reputation of lending institutions, fostering trust with borrowers.	Ensures that borrowers are treated fairly, enhancing their experience and safeguarding their rights.

3.2.2 RBI Guidelines for Debt Collection: An Overview

The Reserve Bank of India (RBI), as the central banking authority, is responsible for regulating and supervising debt collection practices. RBI has developed

comprehensive guidelines that banks and financial institutions must follow to protect borrowers' interests and maintain ethical practices in debt collection.



भारतीय रिज़र्व बैंक
RESERVE BANK OF INDIA

Objective

The primary goal of RBI's debt collection guidelines is to establish fair and transparent procedures, ensuring the protection of borrowers' rights. These guidelines aim to prevent harassment and unethical practices during debt recovery while maintaining the dignity of borrowers. RBI's framework outlines the dos and don'ts, enabling banks to engage ethically with borrowers.

Key Features of RBI Guidelines

1. **Fair Practices Code (FPC):** Banks and financial institutions must adopt a transparent, non-coercive Fair Practices Code that outlines debt collection policies. This code acts as a guideline for ethical behaviour, allowing borrowers to understand their rights and responsibilities.
2. **Communication and Contact:** RBI emphasises that communication with borrowers must be respectful, avoiding any form of abuse, harassment, or coercion. Contact should be made at reasonable times and places, without causing inconvenience or embarrassment.
3. **Privacy and Confidentiality:** Banks must ensure the privacy of borrower information, sharing debt-related details only with authorised individuals directly involved in the recovery process, and not with third parties without the borrower's consent.
4. **Dispute Resolution:** Banks are required to have mechanisms in place for resolving disputes that arise during debt collection. Borrowers must have access to a grievance redressal system to address complaints in a fair, transparent, and timely manner.
5. **Prohibition of Coercive Methods:** Physical force, coercion, and intimidation are strictly prohibited during debt recovery. Debt collectors cannot threaten to seize assets or visit a borrower's workplace without explicit consent.
6. **Documentation and Transparency:** Banks must maintain accurate and up-to-date records of debt collection activities. Borrowers must be provided with documents clearly outlining the amount owed, the rights and obligations of both parties, and any updates in the recovery process.

Significance of RBI Guidelines

Borrower Protection: The guidelines protect borrowers from unethical practices, ensuring fair treatment during debt recovery and providing recourse for violations of their rights.

Standardisation and Transparency: The guidelines promote uniform practices across banks and financial institutions, ensuring consistency and transparency in debt collection.

Reputation and Trust: Adherence to RBI guidelines enhances the reputation of financial institutions, building trust with borrowers and fostering long-term relationships.

Systemic Stability: By regulating debt collection practices, RBI contributes to the overall stability of the financial system, ensuring fair practices and preventing undue harassment.



Knowledge Check

True/False Questions:

1. Debt collectors can visit a borrower's workplace without prior consent.
2. The RBI guidelines protect both borrowers and lenders by ensuring fair practices.

Scenario-Based Questions:

3. A borrower receives a call from a debt collector who demands payment for a debt that the borrower believes has been fully paid. The collector becomes aggressive, insisting on immediate payment and threatening legal action. According to RBI guidelines, what should the borrower do in this situation?
 - a. Pay the amount immediately to avoid legal trouble
 - b. Request written documentation of the debt and remain calm while disputing the claim
 - c. Ignore the call and hope the collector stops contacting them

Answers:

1. False 2. True 3. b.



Activity 5: Understanding RBI's Guidelines for Debt Collection

Objective: To help students understand the Reserve Bank of India's (RBI) role in regulating and supervising debt collection practices in India.

Instructions:

1. Students will form groups of 5-6 to research the role of the RBI in debt collection.
2. Each group will create a PowerPoint presentation (8-9 slides) that includes:
 - a. An overview of the RBI's functions related to debt collection
 - b. Key guidelines issued by the RBI
 - c. The impact of these guidelines on borrowers and lenders
 - d. Examples of ethical practices encouraged by the RBI



3. Groups will present their findings to the class, allowing for a brief Q&A session after each presentation.
4. After all presentations, engage the class in a discussion about how the RBI's role affects their perceptions of debt collection practices.

3.2.3 Impact of Compliance on Borrower Relations

Compliance is crucial for **building positive relationships with borrowers**. When debt collectors handle interactions fairly and ethically, it builds trust and encourages cooperation. On the other hand, failing to comply with regulations can result in **deteriorated relationships, increased complaints, and potential legal issues**. Adhering to compliance standards enables collectors to reach more amicable solutions with borrowers.

3.2.4 Consequences of Non-Compliance in Debt Collections



**Fines and
Sanctions**



**Reputation
Damage**



**Losing
Clients**



**Criminal
Charges**

Non-compliance within the debt collection sector can lead to severe consequences. Lenders and collection agencies may **incur legal penalties, such as fines and sanctions**. Additionally, non-compliance can **damage reputations and lead to a loss of clients**. In some instances, it may also lead to **criminal charges**, carrying significant consequences for those involved in the debt collection process.



Discuss

How can reputational damage from unethical debt collection practices affect a bank's long-term relationship with its customers? Consider the role of social media and online reviews in shaping public perception, and discuss how negative publicity could influence a bank's ability to attract and retain clients.

3.2.5 Best Practices for Compliance

Training Programs: Debt collection agents must undergo regular training to stay updated on national and local debt collection laws, ethical standards, and customer interaction skills.

Training should emphasise ethical behaviour, legal compliance, and conflict resolution techniques.

Example: Banks can conduct bi-annual workshops to ensure agents are well-equipped to communicate effectively, handle disputes, and adhere to legal requirements in debt recovery.

Monitoring Systems: Implementing monitoring systems is crucial for overseeing the behaviour of debt collectors. This includes recording phone calls, reviewing communications, and conducting periodic checks to ensure compliance with ethical and legal standards.

Example: Regularly reviewing call logs or recordings can help banks ensure their debt collectors are not using harassment tactics and are following fair communication guidelines.

Internal Audits: Frequent internal audits of debt collection processes help identify gaps in compliance and allow for corrective action. These audits ensure that practices align with laws, ethical standards, and the bank's compliance policies.

Example: A quarterly audit may uncover areas where agents are failing to comply with guidelines, leading to necessary interventions like additional training or policy changes.

Complaint Redressal Mechanism: Banks must provide a clear and accessible process for borrowers to raise concerns about unethical or illegal practices. This complaint-handling system should be transparent and efficient, ensuring issues are promptly investigated and resolved.

Example: A bank could set up a dedicated customer service team to handle borrower complaints related to debt collection, providing timely resolutions, and maintaining trust with customers.

Protecting Privacy: Debt collectors must prioritise the protection of borrowers' personal and financial information. Any sharing or disclosure of sensitive data without proper authorisation is strictly prohibited. This ensures compliance with privacy regulations and protects borrowers from risks such as identity theft and fraud.

Example: A bank must ensure that only authorised personnel have access to borrower data, and any communication of personal details is handled securely and confidentially.

Consent and Authorisation: Before taking any debt recovery action, collectors must obtain

explicit consent and authorisation from the borrower. This includes actions like negotiating settlements or deducting funds, and all permissions should be well documented.

Example: Collectors should secure proper written consent before initiating any settlement negotiations, ensuring transparency and legal compliance.

Continuous Improvement Through Feedback: Banks should regularly seek feedback from borrowers on their debt collection experiences and use it to improve their practices. This not only promotes accountability but also helps in building better borrower relations.

Example: After resolving a case, banks can ask borrowers for feedback through surveys to refine their collection strategies and improve communication methods.

In conclusion, adhering to RBI guidelines and implementing best practices enables financial institutions to foster trust with borrowers and safeguard their reputations.



Knowledge Check

State True/False:

1. Non-compliance in debt collection can lead to reputational damage and legal penalties.

Choose the Correct Option:

2. What is a key benefit of compliance for debt collectors?
 - a. Increased complaints from borrowers
 - b. Improved trust and cooperation with borrowers
 - c. Higher legal penalties
3. Which of the following is NOT a best practice for compliance in debt collection?
 - a. Regular training programs for debt collection agents
 - b. Ignoring borrower complaints
 - c. Protecting borrowers' privacy

Answers:

1. True, 2. b, 3. b



Activity 6: Do's and Don'ts for Debt Collectors

Objective: To help students identify ethical practices and avoid unethical behaviour in debt collection.

Instructions:

1. Students will work in pairs to create a list of do's and don'ts for debt collectors.

- Each pair will draw a table with two columns labelled "Do's" and "Don'ts."
- In the "Do's" column, students should write down positive practices that debt collectors should follow. In the "Don'ts" column, they will list practices that should be avoided.
- After completing the table, pairs will share their lists with the class, leading to a group discussion on the importance of ethical behaviour in debt collection.



Let's Recap

- Documentation and record-keeping** are crucial processes that enable organisations to **systematically create, organise, and manage records of interactions** between lenders and borrowers, **ensuring compliance and accountability in debt collection**.
- Strategies like offering flexible payment options and clear communication** can help de-escalate tensions and foster positive relationships, even in challenging interactions.
- Conflict resolution** skills like active listening, empathy, and negotiation are essential for resolving disputes and improving recovery rates.
- Debt collectors** must adhere to **ethical standards** by ensuring fair communication, maintaining debtor confidentiality, avoiding harassment, and respecting debtors' circumstances.
- Compliance with laws and regulations**, such as those set forth by the **RBI**, is vital for maintaining fair practices in debt collection.



EXERCISE

Objective Type Questions

One line Answers:

- What is record-keeping?
- Who are aggressive debtors?
- When did the Negotiable Instrument Act come into effect?
- What is conflict resolution?
- What is the full form of RBI?
- What is fair communication?
- How do lenders handle aggressive debtors?
- What are the consequences of non-compliance with debt collection regulations?
- Explain the key features of the RBI guidelines related to debt collection.

Short Answer Type Questions

- Why is documentation important in the debt collection process?
- Draw a flowchart of the debt

Long Answer Type Questions

- Explain the key Indian laws related to debt collection.
- Explain the ethical principles that should be followed in debt collection.

collection process.

ANSWER KEY

Objective Type Questions

One line Answers:

1. Record-keeping is keeping track of all the paperwork and digital records of interactions between lenders and the borrower.
2. Aggressive debtors are people who borrow money, fail to pay it back on time, and use harsh words against the debt collector.
3. The Negotiable Instrument Act came into effect in 1881.
4. Conflict resolution involves methods and processes to facilitate the peaceful ending of conflict and retribution.
5. The full form of RBI is the Reserve Bank of India.
6. Fair communication occurs when debt collectors communicate honestly, respectfully, and professionally with the debtor and avoid aggressive language during the debt collection process.

UNIT 09

Financial Services Pricing and Commission



Topics

- Introduction to Financial Services
- Principles of Pricing Financial Services
 - Factors Influencing Pricing
 - Objective of Pricing
- Understanding Pricing Strategies
 - Cost-Plus Pricing
 - Advantages and Disadvantages of Cost-Plus Pricing
 - Value-Based Pricing
 - Advantages and Disadvantages of Value-Based Pricing
 - Competitive Pricing
 - Advantages and Disadvantages of Competitive Pricing
- Percentage and Markup Calculations
 - Understanding Markup
 - Markup Fees in International Transactions
 - Calculating Markups and Discounts
 - Discount Formula: Calculation and Examples
- Commission Calculations and Budgeting Basics
 - Understanding Commission
 - Types of Commission
 - Calculating Commission Rates
 - Overview of Budgeting
 - Importance of Budgeting in Financial Services



Learning Objectives

- Understand the definition and basics of financial service.
- Explore the factors and objectives that influence pricing in financial services.

- Learn about different pricing strategies and their advantages and disadvantages.
- Learn the definition and basics of percentages, markup calculations and discounts.
- Understand the concept of commission, its types, and how to calculate commission rates.
- Describe the overview of budgeting, the steps involved in the process, and the importance of budgeting in financial services.



Materials Required

- Financial Service Brochures/Promotional Material(To analyse pricing models, markup fees, or promotional commission offers)
- Currency Conversion Chart
- Sample Commission Agreements
- Interactive Budgeting Tools



Activity 1: Before We Begin!

We all know that banks charge interest rates on loans to generate their income, but have you thought about other ways banks generate income? For example, the fees charged for withdrawing money from ATMs. Can you think of anything else? List it below.



Introduction to Financial Services

In the previous activity, we discussed how banks earn money. One way is through financial services, a crucial part of the financial system.

Financial services refer to the **products and services financial institutions offer that help people and businesses manage their money**. Various **organisations** in the finance industry provide these services. **Banks** handle deposits and loans. **Insurance companies** protect against financial risks through life, health, and other insurance products. **Companies** like Paytm enable

consumers to transfer and receive money digitally. These financial services collect money from many savers and make it available to those who need it, especially businesses looking for funds. **Financial services** are important for the smooth **functioning** of the **financial market**, as they help to manage money effectively.



In this chapter, you will learn about the principles of pricing for financial services by looking into the factors and objectives that influence the pricing of services and products offered by financial institutions. You will also gain information on the pricing strategies, percentage calculations, markup, and discount calculations, as well as understand the commission calculations and budgeting for these financial services.

1.0 Principles of Pricing Financial Service

Pricing is an important part of determining the **success of a business**. Even if a company has a great and innovative product with a strong marketing strategy, the product will fail if the customers are unhappy with the pricing. This is also true in the banking sector.

When a bank provides a financial product, like a demand draft or a letter of credit, it charges a commission or service fee. This fee is the price for using that service. However, understanding the pricing of other banking activities, such as borrowing and lending, is more complicated.

These involve factors like risk, the cost of capital, and market competition, making pricing harder to determine. To handle this complexity, it is important to create an effective pricing strategy. Here are some of the reasons:



Cost of Capital

The expense a company has to pay to get the funds it needs for its business.

- **Banks** offer a range of financial services to their customers, such as **loans, savings accounts, and investment options**. Since these services use **shared resources**, it's important for banks to analyse the **costs of providing** each one. Having accurate pricing information helps the bank set **fair and profitable prices**. **For example**, if a bank charges too little interest on loans, it might struggle to make a profit. But if the interest rate is too high, customers may not be able to afford to borrow. This is why effective pricing is crucial for both the bank's profitability and making services affordable for customers.
- In recent years, the banking industry has faced more competition, especially with the rise of private-sector banks. Many new banks started offering lower prices, forcing others to reduce their prices to stay competitive. This shows that banks need to set their prices not only to **meet customer needs** but also to **stay competitive** in the market.

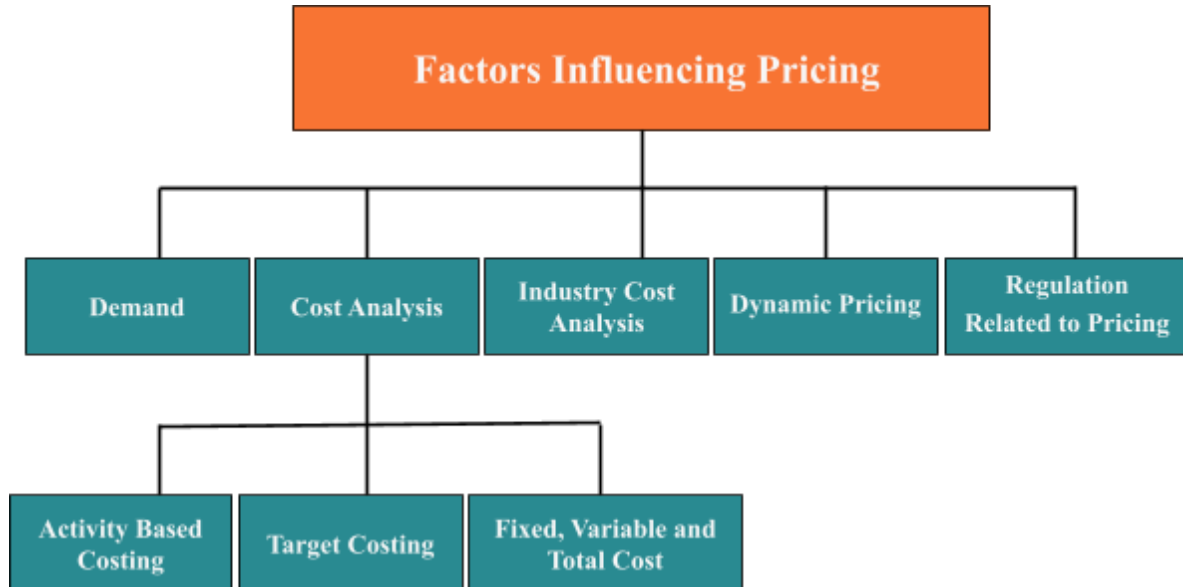
In the banking industry, the main business is borrowing and lending money, and banks create financial products for both. Setting the right prices for these products is essential. **For example**, when a bank offers a new fixed deposit scheme, it needs to decide what interest rate to offer customers for their deposits. This interest rate is the '**price**' of the product. Even though the bank has to pay interest on the deposit, this pricing helps attract customers to invest their money in the bank.

The same idea applies when banks give out loans, like car or home loans. **For example**, when offering a loan without collateral, the bank has to decide the interest rate, which is the 'price' of the loan. These prices play a big role in whether customers choose to invest their money or take a loan.

For banks, besides interest rates, the concept of pricing applies to other fees/charges, such as, monthly **locker maintenance fees, transaction charges, minimum balance requirements, commissions, and service fees**. Some of these fees are charged directly when the customer uses the service, while others are collected indirectly when the service is offered.

1.1 Factors Influencing Pricing

Pricing in the banking sector is influenced by several factors, such as, demand for the product or service, the cost associated with offering the product or service, competitors' pricing and regulations related to the pricing of a product or service.



1. **Demand:** Understanding the link between **price and demand** is important for knowing how changes in price affect the sales of a product or service. Usually, when prices go up, demand goes down because fewer people want to buy. But in some cases, even raising prices can still lead to higher profits. This depends on the **price elasticity** of the product.

Price elasticity of demand measures how much the quantity demanded changes when the price changes. It is calculated by dividing the percentage change in quantity demanded by the percentage change in price. If demand is **elastic**, people are very sensitive to price changes. For example, if the price goes up, they may switch to a cheaper, similar product.

In the **banking sector**, price elasticity plays a significant role. **For example**, if a bank lowers its deposit interest rates, fewer customers may want to deposit their money. **Private, foreign, and cooperative banks** often offer slightly higher deposit rates than public sector banks to attract more customers.

Banks also use different pricing strategies for the same product. **For example**, the fees for a demand draft may vary depending on the amount. Some private banks might offer a free demand draft but charge extra for delivering it.

Example

Simran wants to deposit an amount of ₹5,00,000 in a fixed deposit account. She notices that different banks offer different interest rates for fixed deposits.



a customer.

- At Bank A, the interest rate for fixed deposits had recently been reduced from 7% to 6%. Finding this rate too low, Simran decided to look for other banks with better rates. This shows that customers are sensitive to changes in interest rates.

- Since many customers will move to a bank offering higher interest rates, we can say that the demand for fixed deposits is **elastic**. Even a small change in interest rates can lead to a big change in how much money customers are willing to deposit.

- Simran then went to Bank B, which offered a 7% interest rate. She decided to deposit her money there, causing Bank A to lose

Simran's example shows how price changes in the banking sector can directly affect demand, costs, and profits.

2. **Cost Analysis:** Understanding **costs** is very important for banks because it helps them decide whether to offer a product or service and how to set a fair price. **Cost information** is key to creating a pricing plan, especially when the price in the market is higher than the cost of making the product or service. **For example**, banks charge different fees for issuing credit cards. Some banks have higher initial fees but lower renewal charges, while others have lower initial fees and higher renewal charges. This shows how important cost information is for **understanding pricing** in a **competitive market** and **attracting customers**.

Example

In Punjab, there are two banks: Bank A and Bank B, both offering credit card services with different fee structures.

- Bank A's Fee Structure
 - Admission Fees: ₹2,000
 - Annual Renewal Fee: ₹500
- Bank B's Fee Structure
 - Admission Fees: ₹500
 - Annual Renewal Fee: ₹1,500



- Bank A charges higher admission fees because of its extensive marketing campaigns and premium customer support. This fee structure attracts customers willing to pay a

higher admission fee in exchange for lower renewal fees.

- On the other hand, Bank B has a lower admission fee due to its lower initial marketing costs. They aim to attract more customers by offering a lower admission fee. Research conducted by the bank shows that most customers prefer to keep their credit cards beyond the first year, which helps generate more revenue through renewal fees.

Both banks have conducted cost analysis to understand the expenses related to their credit card services. This research has helped them design pricing strategies that align with their overall business models and meet customer expectations.

Let us look at different kinds of Cost Analysis:

- a. **Activity-Based Costing (ABC):** Activity-based costing (ABC) involves **identifying and listing all activities** required to provide a service and the resources needed for each activity. **For example**, when a bank processes a demand draft, cheque or withdrawal slip, it calculates the **total cost** by **multiplying the time taken for each activity by its cost** to determine ABC. The approach is more **accurate and reliable**.
- b. **Target Costing:** In a competitive banking market, banks cannot charge excessively high fees for services like demand drafts, credit cards, or interest rates, as customers will choose other banks. Therefore, they must set a **target price** that is **neither too low nor too high**. If the cost exceeds the target, the bank will evaluate their staff efficiency, upgrade equipment or remove non-essential tasks to reduce the cost.
- c. **Fixed, Variable and Total Cost:** When making pricing decisions, banks need to calculate various costs involved in delivering services and determine which costs to include. Costs can be broadly classified into two categories: variable costs and fixed costs.
 - **Variable Costs:** These costs change with the level of activity or production. An example in the banking industry is interest expenses, which vary based on the volume of deposits or loans.
 - **Fixed Costs:** These costs remain constant regardless of the bank's activity level. They include expenses like rent, salaries for permanent employees, and utility bills such as electricity and water. Some employee costs may be considered semi-fixed, as banks might hire additional staff to handle short-term demand fluctuations, which can impact overall costs.

After understanding fixed and variable costs, banks will consider these factors when making pricing decisions.

Example**Cost of Processing a Loan Application at Bank A**

Activity-Based Costing (ABC): Bank A identifies key activities to process a loan application.

- Collecting information about the customer:
 - Time: 1 hour
 - Cost: ₹300 per hour
 - Total: $1 \times 300 = ₹300$
- Evaluating the customer's credit history:
 - 2 hours at ₹300 per hour = $₹300 \times 2 = ₹600$
- Processing the loan agreement and finalising the amount:
 - 1 hour at ₹300 per hour
$$= 1 \times 300 = ₹300$$

**Total Cost to Process One Loan Application:**

$$₹300 + ₹600 + ₹300 = ₹1,200$$

Activity-Based Costing helps determine the cost of processing each loan application, allowing for accurate pricing.

Target Costing: After conducting market research, Bank A discovers that a competitor bank offers a loan processing fee of ₹1,000, while Bank A charges ₹1,200.

- To attract more customers and remain competitive, Bank A needs to reduce its fee by ₹200.
- To achieve this, the bank can train its staff to improve efficiency and reduce the time spent on each activity involved in the application process.

Fixed, Variable and Total Cost: Bank A also reviews its cost structure when making pricing decisions.

- Fixed Costs
 - Rent for branch office = ₹50,000 per month
 - Salaries of permanent employees = ₹1,00,000 per month
 - Utility bills (electricity, internet, etc.) = ₹20,000 per month

Total Fixed Cost per Month:

$$₹50,000 + ₹1,00,000 + ₹20,000 = ₹1,70,000$$

Variable Cost per Loan Application:

From Activity-Based Costing: ₹1,200 (Referring to Activity Based Costing)

Total Variable Cost for Processing 100 Loan Applications in a Month:

Total variable costs = $100 \times ₹1,200 = ₹1,20,000$

Total Cost for the Month:

Total cost = Fixed cost + Total variable costs

= ₹1,70,000 + ₹1,20,000 = ₹2,90,000

By understanding the breakdown of fixed and variable costs, Bank A can make informed pricing decisions that ensure all costs are covered while remaining competitive in the market.

3. **Industry Cost Analysis:** Although banking services are quite standard, the profits that banks earn can vary a lot, even after accounting for losses from bad loans. This is because banks have different **cost structures**. Some private and public sector banks are better at managing their costs, but in a competitive market, managing costs alone is not always enough to stay successful.

In the banking sector, **pricing decisions** often depend on **how competitors react**. For **example**, if one bank lowers its interest rate in a competitive market, other banks are likely to do the same to attract more customers. However, this can also lower profits, so banks must consider their competitors' costs before setting prices.

4. **Dynamic Pricing:** This is also called **real-time pricing**, where prices can change based on market conditions. Banks use this strategy by constantly monitoring factors like demand, competition, customer behaviour, and market trends. This flexibility allows them to adjust their prices quickly as needed.
5. **Regulation related to Pricing:** The **government controls** certain aspects of **pricing** for **banking products and services**, such as interest rates. These regulations are in place to protect consumers from exploration and maintain stability in the banking system. These rules help ensure that prices remain fair and reasonable for customers. This is the external factor that forces financial institutions to change their pricing.

1.2 Objectives of Pricing

The following are the objectives that financial services aim to achieve through its pricing:

- **Branding:** The prices a bank sets for its products and services should match its overall brand image. Customers expect fair, consistent, and clear pricing. If prices seem unfair or inconsistent, it can hurt the bank's reputation and the trust customers have in its brand.
- **Profit Maximisation:** Banks aim to make a profit, and setting the right price is key to achieving that. However, increasing prices can sometimes reduce demand or raise costs. So, banks need to carefully analyse factors like demand, costs, and marketing strategies to set a price that helps them maximise profits.
- **Return on Investment (ROI):** ROI measures how profitable an investment is compared to its cost. Banks set prices to reach a target ROI, especially when they've invested heavily in new products or services. When launching new products, banks

must consider how pricing will impact sales, costs, and the overall return on their investment.

- **Market Share:** Banks aim to increase their **market share**, which means attracting more customers. To do this, they often set competitive prices to draw in customers and compete with other banks. They may adjust prices regularly based on market conditions and offer discounts or deals to attract new customers and maintain their position in the market.



Knowledge Check

Answer the following questions

1. **True or False:** If a bank lowers its deposit interest rates, many customers will be ready to deposit their money in the bank.
2. Which of the following is not considered a financial service?
 - a. Investment advisory
 - b. Retail shopping
 - c. Banking
 - d. Insurance

3. Find the total Activity-Based Costing from the information given below.

The key activities to process the loan include

- Collecting information about the customer: 1 hour at ₹500 per hour
- Evaluating the customer's credit history: 3 hours at ₹200 per hour
- The time taken to process the loan agreement and finalise the amount = 1 hour at ₹400 per hour



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-
-
4. The external factor that forces financial institutions to change their pricing is
 - a. Government regulations
 - b. Profit margin
 - c. Operating cost
 5. **True or False:** The Banks need not consider the demand price sensitivity of a customer when looking at the cost of service. _____

Answers:

1. False, 2. b. Retail shopping, 3. ₹1,500, 4. a. Government regulations 5. False



Activity 2: Create a product and price them!

Objective: Understand and explore the factors that influence the pricing of financial services.

Instructions:

- The class may be divided into small groups.
- Each group needs to come up with a name for their bank and decide on one of the financial services they offer from the two options: personal loans and credit cards.
- The group needs to identify their target market and then mention the features provided by these financial services.
- The group can then discuss the factors they will consider when determining the price of their product and the cost analysis.
- Each group will then present their bank's name, chosen financial service and the cost analysis.



2.0 Understanding Pricing Strategies

Have you ever wondered how banks decide the interest rates on loans or the fees for maintaining your savings account? These decisions are not random, but rather the result of well-thought-out pricing strategies designed to meet both the bank's goals and customer expectations.



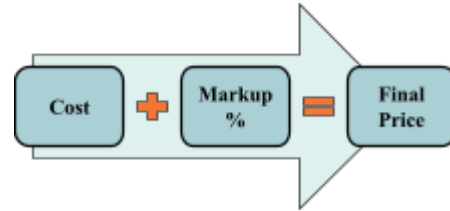
Pricing decisions in banking are complex, especially in competitive markets where banks must often **have to match the prices set by their competitors**. However, when banks do have control over pricing, they focus on three main things:

- **Customer Appeal:** Making sure the product is attractive and affordable for customers.
- **Staying Competitive:** Keeping prices in line with other banks to remain strong in the market.
- **Profitability:** Setting prices that allow the bank to make a profit while covering costs.

It is hard to excel in all these areas at the same time, but banks use different pricing strategies that fit their unique situations. The decisions they make about pricing can have a big impact on their long-term success.

2.1 Cost-Plus Pricing

- **Cost-plus pricing**, also known as **cost-based pricing**, is a straightforward strategy used by banks and businesses to set the price of their products and services.
- This approach involves **calculating the total production costs**—such as materials, labour, and overhead—and then **adding a predetermined markup to ensure profitability**.
- The price of a banking product is established by adding a fixed margin or percentage to the total cost of providing that product.
- The costs can include various expenses, including operational costs, funding, capital, risk, and taxes.



Markup

The amount added to the cost to set a selling price.

Example, If it costs a bank ₹10,000 a year to maintain a business account, they might set the price for the account at ₹11,500. This way, the bank covers its costs and also earns something from the money customers keep in their accounts.

While cost-plus pricing ensures that banks cover their operational expenses and achieve a profit margin, it has some limitations.

Advantages and Disadvantages of Cost-Plus Pricing

Advantages	Disadvantages
Easy to calculate and implement. (Simple formula: Total costs + Markup = Price).	Ignores Demand: It doesn't take customer demand into account, which means prices may be too high for some customers to afford.
Ensures Profit: By covering all costs and adding a profit margin, the business ensures it makes a profit on each product or service.	Ignores Competitors: It doesn't consider what competitors are charging, so prices might be higher or lower than the market standard.
Stable Pricing: It leads to predictable pricing, which can help in avoiding sudden price changes.	No Incentive for Efficiency: Since profits are guaranteed by adding a fixed margin, there's no strong motivation to reduce costs and improve efficiency.

In the next section, we will be learning about **Markup Calculations**, which will help you understand how to apply the markup percentage effectively.



2.2 Value-Based Pricing

Value-based pricing is a customer-focused strategy where banks set prices based on **how much value customers see in a product or service**, instead of just looking at production costs. This approach allows banks to charge higher prices if customers believe the service or product is worth it.

For example, in **Internet Banking**, banks may charge a fee because it saves customers time and offers convenience. People who value their time might be willing to pay for this service because they see it as useful and time-saving.

A bank might also offer a **premium credit card** that comes with special rewards, travel benefits, and insurance. The bank could charge an annual fee of ₹5,000, not based on the cost to provide the card, but because customers see these benefits as valuable. People who are willing to pay this fee recognize the card's value.

Similarly, for services like **wealth management or investment services**, banks may charge higher fees because they offer personalised advice and exclusive benefits. Customers who are looking for financial growth and personalised service are ready to pay more for these added benefits, like access to financial experts and customised investment strategies.

Advantages and Disadvantages of Value-Based Pricing

Advantages	Disadvantages
Allows banks to command higher prices, resulting in larger profit margins compared to cost-plus strategies.	Requires in-depth understanding of customer needs and preferences, which may involve significant research costs.
Tailoring offerings based on customer preferences leads to higher satisfaction and loyalty.	If the perceived value is not accurately assessed, it may lead to overpricing, causing potential customer loss.
Effectively communicating the value proposition helps banks differentiate themselves from competitors.	Pricing must frequently adjust based on changing customer perceptions and market conditions, requiring constant monitoring.
Enables adjustments in response to changing market conditions and customer preferences.	Some customers may feel that the pricing is not justified, especially if they do not perceive the same level of value.



Discuss

Imagine you are choosing between two banks for investment advice. One bank charges higher fees but offers personalised financial planning, while the other charges less but provides basic advice. Which option would you find more valuable, and why?

2.3 Competitive Pricing

Competitive pricing is a strategy where banks set their prices **based on what other banks charge for similar products or services**. This means they look at direct competitors, like other banks, as well as indirect ones, such as credit unions or online lenders. After analysing these prices, banks can decide to match what others are charging, set their prices lower, or position themselves as a premium option with higher prices.



This approach is very common for banks when they **price loans, deposits, or fees for services**. It has worked well over the years because many bank products are quite similar.

Example: In a competitive market, a bank might change its interest rates on loans based on what other banks are offering. For instance, if most banks have personal loans at an interest rate of 10%, a bank might choose to set its rate at 9.5% to attract more customers. By keeping its rates competitive, the bank can gain more market share and bring in new borrowers.

Advantages and Disadvantages of Competitive Pricing

Advantages	Disadvantages
By setting lower prices than competitors, banks can attract more customers looking for good deals. Example: A bank that offers a higher interest rate on savings accounts may attract more customers.	Constantly lowering prices can reduce profit margins, making it harder for banks to cover their costs and maintain profitability.
Competitive pricing can help a bank gain a larger share of the market, especially in a crowded field where many banks offer similar products.	Intense competition can lead to price wars, where banks continuously undercut each other. This can harm the entire industry and result in unsustainable pricing.
This strategy allows banks to quickly adjust their prices in response to market changes, ensuring they stay relevant.	Focusing too much on pricing may lead banks to overlook the value of their services. Customers may perceive lower prices as lower quality.

Offering attractive pricing can lead to customer loyalty, as people appreciate good value and may stick with a bank that offers lower fees or better rates.	Competitive pricing can be a short-term solution. If banks rely on it too heavily, they may struggle to build long-term customer relationships based on trust and value.
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Knowledge Check

Choose the Correct Option:

1. What is Cost-Plus Pricing?
 - a. Pricing based on competitors' prices
 - b. Pricing based on customer perceptions
 - c. Adding a markup to total production costs
2. What is a potential risk of Value-Based Pricing?
 - a. It removes the need for market research.
 - b. Customers may not see the product as valuable enough to pay the higher price.
 - c. It is the only pricing strategy used in banking.

Answers:

1. c 2. b



Activity 3: Create Your Own Pricing Strategy

Objective: To apply the concepts of pricing strategies by designing a pricing plan for a familiar product or service.

Instructions:

1. Choose a product or service, such as mobile phone recharge plan or a basic banking service like a Savings account.
2. Think about how much it costs to provide this service and how much customers would be willing to pay for it.
3. Create a pricing strategy using one of the methods discussed (Cost-Plus, Value-Based, or Competitive Pricing).
4. Write a short explanation of why you chose that strategy and how it would attract customers while ensuring a profit.

3.0 Percentage and Markup Calculations

Understanding percentages and markups is very important in banking because they help decide interest rates, fees, and pricing strategies. In Unit 4, we learned the basics of calculating

percentages. Now, we will look at what markup is and how banks use it. We'll explore how banks set prices for their services and loans using markup percentages.

Recap of Percentage Problem

A bank offers a savings account with an annual interest rate of 5%. If a customer deposits ₹30,000 today but withdraws ₹10,000 after six months, calculate the total interest earned in one year.

Solution:

$$\text{Simple Interest } S.I = P \times \frac{R}{100} \times T$$

where,

- P is the principal amount
- R is the annual interest rate (expressed as a fraction)
- T is the time period (in years)

For the first 6 months:

Interest on ₹30,000 for half a year at 5% per annum:

$$\text{Interest Amount} = 30,000 \times \frac{5}{100} \times \frac{6}{12} = ₹750$$

For the next 6 months (after the ₹10,000 withdrawal):

Interest on ₹20,000 for the remaining half of the year:

$$\text{Interest Amount} = 20,000 \times \frac{5}{100} \times \frac{6}{12} = ₹500$$

So, the total interest earned in one year would be ₹750 + ₹500 = ₹1,250.

3.1 Understanding Markup

Imagine you're waiting in line to buy your favourite cold coffee at a popular café, and you notice that it costs ₹300. It seems a bit high for just a drink, especially since the ingredients don't cost that much. But then you look around and see the cosy seating, beautiful decor, and a friendly barista who helps everyone with a smile. You realise that your ₹300 is not just for the cold coffee—it's also paying for all these things that make your experience enjoyable.



The same idea applies to banking products and services. Sometimes, customers wonder why certain fees or interest rates are higher than expected. Just like the café uses markup to maintain its pleasant atmosphere and service quality, **banks use markup strategies to cover their operational costs while providing value to their clients**. This markup includes things like training their staff, investing in technology, and keeping banking services safe and secure.

In finance, **markup is the difference between the cost of a financial asset (like a loan or stock-how much it costs to provide a service) and its selling price (price that customers pay for it)**. Banks and financial institutions use markups to cover their expenses and make a profit. By understanding this concept, customers can appreciate the overall benefits they receive from their bank and see that it's not just about the price—they're paying for quality service and support too.

3.1.1 Markup Fees in International Transactions

- When making international transactions, such as purchasing from foreign websites or sending money abroad, banks apply a **markup fee**.
- This fee, also called a **foreign exchange markup**, is an extra charge added on top of the actual currency exchange rate.
- It usually ranges from **1% to 3%** of the transaction amount.
- Banks charge markup fees to **cover the costs** of converting currencies and managing the risks involved in foreign exchange.
- These fees also help banks **make a profit** while offering the convenience of converting your money into different currencies.



Calculating Markup Fees in International Transactions

When sending money abroad (outward remittance) from India, it's important to consider **foreign transaction fees**. We read about remittance services in *Unit 1, Section 2.5*, which help transfer funds internationally. Here's an example of how to calculate foreign transaction fees:

Step 1: Identify the Foreign Transaction Fee Percentage Let's say your bank charges a foreign transaction fee of 3%.
Step 2: Convert the Amount to Local Currency: You are sending ₹40,000 to a foreign recipient. The exchange rate is ₹84 per 1 USD. So, $40,000 \div 84 = 476.19$ USD.
Step 3: Calculate the Foreign Transaction Fee: Multiply the converted amount by the transaction fee percentage: 3% of 476.19 USD = 14.29 USD(approx).
Step 4: Total Cost Including the Fee: Add the fee to the original amount: $476.19 \text{ USD} + 14.29 \text{ USD} = 490.48 \text{ USD}$.
Thus, the total cost of sending ₹40,000 abroad, including the 3% foreign transaction fee, would be approximately 490.48 USD . <i>Converting this back to Indian currency at ₹84 per USD, the total cost would be approximately ₹41,200.</i>

Problem: International Wire Transfers and Foreign Transaction Fees

Imagine TechSolutions Pvt Ltd, an Indian software company, needs to pay a \$50,000 licensing fee to a U.S.-based software provider, SoftwareTech Inc. TechSolutions initiates an international wire transfer from its Indian bank.

Solution:

Step 1: Identify the Foreign Transaction Fee Percentage

Foreign Transaction Fee Rate: 2%

Step 2: Conversion to Local Currency

Licensing Fee: \$50,000

Exchange Rate: 1 USD = ₹84

Converted Amount: $50,000 \text{ USD} \times 84 \text{ INR/USD} = 42,00,000 \text{ INR}$

Step 3: Foreign Transaction Fee

Transaction Fee in USD: $2\% \text{ of } 50,000 \text{ USD} = 1,000 \text{ USD}$

Convert the Transaction Fee to INR: $1,000 \text{ USD} \times 84 \text{ INR/USD} = 84,000 \text{ INR}$

Step 4: Total Cost

Total Cost: $42,00,000 \text{ INR} + 84,000 \text{ INR} = 42,84,000 \text{ INR}$

Total Cost for TechSolutions: ₹42,84,000 (including the foreign transaction fee).



Knowledge Check

1. Textile Innovations Ltd. issues an invoice for €20,000 to Global Fashion. The exchange rate is ₹91 per Euro, and the bank charges a foreign transaction fee of 1.5% on the converted amount. What is the total cost for Global Fashion to pay this invoice, including the foreign transaction fee?

Answer:

1. The total cost for Global Fashion is ₹18,47,300, which includes the invoice amount converted to INR and the foreign transaction fee.



3.2 Calculating Markups and Discounts

In business finance, **markup** refers to the additional amount added to the cost of a product or service to establish its selling price. This is typically expressed as a percentage over the cost basis, enabling businesses to cover operational expenses and generate profit.

The markup formula is defined as:

$$\text{Markup Percentage} = \frac{\text{Selling Price} - \text{Cost}}{\text{Cost}} \times 100$$

$$\text{Hence, Selling Price} = \text{Cost} + (\text{Cost} \times \text{Markup Percentage})$$

For example, if a product costs ₹50 to produce and the markup is 40%, the selling price would be calculated as follows:

$$\text{Selling Price} = \text{Cost} + (\text{Cost} \times \text{Markup Percentage}) = ₹50 + (₹50 \times 0.40) = ₹70.$$

Steps to Calculate Markup

Calculating markup involves several key steps to ensure accuracy and effectiveness. Here's a simplified process:

Step 1: Find the Total Cost: First, figure out the total cost of providing a product or service. This includes all direct costs (like fees and salaries) and indirect costs (such as rent, electricity, and technology).

For example, if a bank spends ₹1,000 on processing a loan application (including staff and paperwork), this ₹1,000 becomes the cost of providing that service.

Step 2: Decide on the Profit: Next, the bank needs to decide how much profit it wants to make. Let's say the bank wants to make a 20% profit. This means the bank will add 20% of the cost to its price.

Step 3: Calculate the Markup: Now, to find the final price, the bank adds the 20% profit to the ₹1,000 cost.

Using the previous example:

- Total Cost = ₹1,000
- Desired Profit = 20% of ₹1,000 = ₹200.
- Final Service Fee = Total Cost + Desired Profit = ₹1,000 + ₹200 = ₹1,200

By following these steps, banks can set prices that meet their financial goals while still offering competitive services. It's also important for banks to review their pricing regularly because changes in rules or market demand can impact both costs and prices. This helps banks stay up-to-date and make adjustments when needed, ensuring they continue to meet customer needs and remain profitable.

3.2.1 Discount Formula: Calculation and Examples

A discount is a reduction from the original price (listed price) of a product or service offered to attract customers or introduce new products.

The discount percentage formula is:

$\text{Discount Percentage} = \frac{\text{Discount}}{\text{List Price}} \times 100$
$\text{Discount} = \text{List Price} - \text{Selling Price}$

Banks offer their customers various discounts on short-term money market instruments. Banks provide loans where the interest is deducted upfront from the loan amount. This type of loan is

known as a "**discounted loan**." The deducted interest is called the "**discount**," and the amount the borrower actually receives is referred to as the "**proceeds**." The total amount that needs to be repaid at the end of the loan period is called the "**maturity value**."

The discount (D) is calculated using the formula: $D = M \times r \times t$ where,

- M is the loan amount (maturity value),
- r is the annual interest rate (expressed as a decimal),
- t is the time period of the loan in years.

The proceeds (P), or the amount the borrower receives, is:

$$P = M - D = M - M \times r \times t = M(1 - r.t)$$

Problem: Vivek borrows ₹30,000 for 8 months at a simple interest rate of 12% per year. Calculate the discount and proceeds.

Solution: The discount: $D = M \times r \times t$

Here, $M = ₹30,000$, $r = 12\%$ or 0.12 , $t = \frac{8}{12} = \frac{2}{3}$

Applying the values we have

$$D = ₹30,000 \times 0.12 \times \frac{2}{3}$$

$$D = ₹3,600 \times \frac{2}{3}$$

$$D = ₹2,400$$

Therefore, the bank deducts ₹2,400 as discount from the maturity value of ₹30,000

So, the Proceed $P = M - D = ₹30,000 - ₹2,400 = ₹27,600$.

In this case, Vivek receives ₹27,600, but will need to repay ₹30,000 for 8 months. Hence the discount is ₹2,400, and the proceeds are ₹27,600.

Discounts and Cash-Back in Banking

In what way is it beneficial for banks to offer discounts or cash-back to customers who make payments using their credit or debit cards? Banks offer discounts and cash-back on credit or debit card payments for several reasons that benefit both customers and the bank:

- 1. Encourages more card usage:** When customers get cash-back or discounts, they're more likely to use their cards often, which means more transactions for the bank.
- 2. Builds customer loyalty:** These offers make customers feel rewarded, which encourages them to keep using that bank's card instead of cards from other banks.
- 3. Banks earn from merchant fees:** Every time a card is used, the bank earns a small fee from the merchant. So, the more people use their cards, the more banks earn from these fees.



4. **Interest income from credit cards:** Customers who don't pay their full credit card bill each month end up paying interest. This interest can help banks cover the cost of cash-back rewards.
5. **Attracts new customers:** In a competitive market, cash-back and discounts make a bank stand out, helping it attract new customers who want more benefits from their cards.
6. **Understanding customer preferences:** By studying how customers use cash-back rewards, banks can learn more about spending habits, helping them design better products and marketing.
7. **Promotes partner merchants:** Banks often promote specific categories like groceries or travel by offering cash-back in these areas. This not only helps customers save but also drives business to partner merchants.
8. **Improves customer satisfaction:** Customers feel like they're getting extra value when they receive rewards, making their experience with the bank more positive.

This way, both customers and banks gain from cash-back and discount offers.



Activity 4: Research on Minimising Markup Fees

Objective: Research strategies to minimise markup fees for banking transactions

Instructions:

- The class may be divided into small groups.
- Each group is assigned a specific type of banking transaction, such as international transfer, ATM withdrawal, currency exchange, etc.
- The groups research how banks calculate markup prices for different transactions with the help of online resources, bank websites, books and other resources.
- The groups then need to develop strategies to minimise the markup fees for their assigned transactions.
- Each group can present their findings and strategies to the class and compare them.



4.0 Commission Calculations and Budgeting Basics



Discuss

If you own an insurance company that just launched a new health insurance product. How will you encourage the insurance agents working in your company to sell the products?

4.1 Understanding Commission

Selling products or services can be tough, especially with so much competition. To motivate their sales and marketing employees, companies often give them commissions. **The commission is the fee or percentage of the amount paid or charged by a broker or investment advisor for handling purchases and sales of products for their clients.**



Example: Simran purchased an insurance policy with an annual premium of ₹12,000. She met an insurance agent from XYZ Insurance Company who helped her get the policy.

The insurance company offered the agent a 30% commission on the

first-year premium amount paid by Simran.

So, the agent earned: $\frac{30}{100} \times ₹12,000 = ₹3,600$.

Commissions vary depending on the job. For **example**, someone working at a car dealership earns based on how many cars they sell, while a real estate agent gets a commission based on the house or property they help sell. Companies have different ways of setting and paying commissions, and they can broadly be classified as

- **Flat commission:** The employee earns a fixed amount or percentage for each sale, no matter the price of the product.

Example: An insurance company partnered with an insurance agent, Amar, to sell their health policy. Amar will receive a flat commission of ₹2,000 for every insurance policy he sells without considering the price or premium. So if Amar sells a health policy with an annual premium amount of ₹10,000 to Remya, he would earn ₹2,000. Similarly, if he sells a health policy with an annual premium of ₹50,000, he would still earn ₹2,000.

- **Ramped commission:** The employee gets a commission based on their sales, which means more sales or higher the target or goal more their earning. The commission is not fixed.

Example: Simran works as an insurance agent for ABC Insurance Company. She earns a commission based on the number of policies she sells monthly, and the commission rate increases as she reaches certain sales targets.

The commission tiers say that if 1-5 policies are sold, you get 5% on each policy premium. So, if Simran sold 4 policies in a month, each with a premium amount of ₹10,000, then her commission would be

$$4 \text{ policies} \times 10,000 \text{ premium} \times 5\% = 4 \times 10,000 \times \frac{5}{100} = 40,000 \times 0.05 = ₹2000.$$

These commission amounts will encourage people to put more effort into selling the products and help to create an active and motivated workforce. The commission-based pay also has



Broker

A person or company that helps you to buy and sell things like stocks, bonds or property.



Investment Advisor

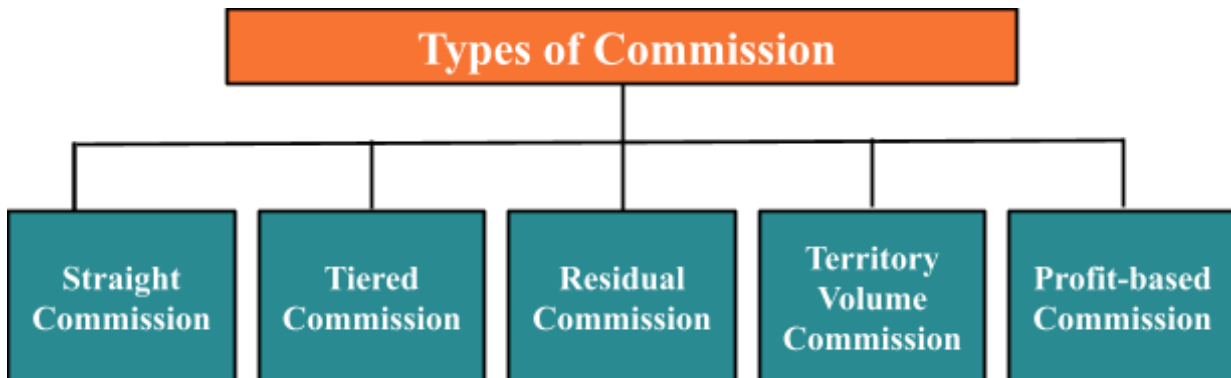
A professional who gives advice on how to invest your money based on your financial goals.

disadvantages, like creating tension within teams, where some would earn more than others, which can lead to demotivation.

Many companies solve this by offering a **blended compensation model**, where employees receive both a base salary and a commission. This keeps employees motivated to work harder while still ensuring a stable income.

4.1.1 Types of Commission

The commission structure can be divided into five types, depending on the business models and their sale objectives.



Let's discuss the two most common types of commission:

Straight Commission:

This is a commission payment method where the person earns **money based on the sale** they make, with **no fixed salary**. This means a person's salary depends on the money they make by selling the products and services. As there is no basic salary, companies often offer a higher commission rate to attract agents to work with them. Companies also benefit from using this commission structure as they have to pay the agents when the sales are made, so they are not spending money on the business without getting revenue.

This type of commission structure is common in industries like real estate, insurance, and car sales.

Example

Ravi is a financial advisor for a finance company that sells insurance policies, investment products, and mutual funds. The company offers a **straight commission plan**, so he gets money based on the policies he sells and does not have any fixed salary.

Ravi earns a commission of 30% on the premium amount of each life insurance policy they sell.

Raj is selling two policies in April:

- Policy A: Premium of ₹50,000
- Policy B: Premium of ₹30,000
- The total premium sold is ₹50,000 + ₹30,000 = ₹80,000

Total Commission = Commission Percentage × Amount Sold

- Thus, the total commission earned is $30\% \times ₹80,000 = \frac{30}{100} \times ₹80,000 = ₹24,000$

In May, Ravi could not sell any policies, so his income for that month was zero. This shows that you earn commission only when you sell policies to people without a fixed salary.

Profit-based commission:

This type of commission is used in sales where the **commission** earned by the salesperson is based on the profit they bring in from their sales, not just the total amount they sell like other types of commission. This encourages salespeople to focus on making profitable deals rather than just boosting sales numbers. Both the company and the salesperson focus on profitability rather than just sales volume, which will contribute to the overall success of the business.

Example

Rekha is a financial advisor who works for XYZ Bank, and she helps clients to get home loans. Anjali wants a home loan of ₹ 50,00,000 and approaches Rekha for financial advice. Rekha suggests Anjali take a loan from XYZ Bank.

The details of the home loan are given below:

Loan amount = ₹50,00,000

Interest Rate = 8% per annum (per year)

Process fees by the bank = 2% of the loan amount

Thus, the bank charges a processing fee of 2% on the loan amount

$$= 2\% \text{ of } ₹50,00,000 = \frac{2}{100} \times ₹50,00,000 = ₹1,00,000$$

The total cost incurred by the bank to process the loan is ₹20,000

This is the **Bank's Profit = Processing Fee - Cost** = ₹1,00,000 - ₹20,000 = ₹80,000

Bank offers a 10% commission to Rekha on the profit made by the bank from the home loan.

Thus, Rekha's **Commission = Bank's Profit × Commission Rate** = ₹80,000 × 10%

$$= ₹80,000 \times \frac{10}{100} = ₹8,000$$

Thus, Rekha received a commission of **₹8,000**.

4.1.2 Calculating Commission Rates

Commission rates are the fees or percentages paid to salespeople based on the sales they make. Professions like insurance brokers, real estate agents, and salespeople often rely on commissions as part or all of their income. That's why knowing how to calculate commission rates is important for them.

- **Identify the desired commission amount:** First, figure out **how much** a salesperson wants to earn from a particular sale or target. Different industries and companies have different goals, so the commission rate may vary based on the targets they need to achieve.

- **Use the formula for commission rate calculation:** After calculating the desired commission amount, you can use the formula to calculate the **commission rate**. This will help determine how much they'll earn based on the sales they make.

$$\text{Commission Rate (\%)} = \left(\frac{\text{Commission Amount}}{\text{Sale or Revenue}} \right) \times 100$$

Example: A salesperson wants to earn a commission amount of ₹1,000, and the total sale generated is ₹40,000. So, the commission rate is:

$$\begin{aligned} \text{Commission Rate (\%)} &= \left(\frac{\text{Commission Amount}}{\text{Sale or Revenue}} \right) \times 100 \\ &= \left(\frac{1,000}{40,000} \right) \times 100 = 0.025 \times 100 = 2.5\% \end{aligned}$$

Similarly, if you know the **commission rate** and **total sale**, you can calculate the commission amount using the following formula.

$$\text{Commission Amount} = \text{Commission Rate} \times \text{Total Sales or Revenue}$$

Applying the same example with a commission rate of 2.5% on a total sales of ₹40,000

$$\begin{aligned} \text{Commission Amount} &= \text{Commission Rate} \times \text{Total Sales or Revenue} \\ &= 2.5\% \times ₹40,000 \\ &= \frac{2.5}{100} \times ₹40,000 = 0.025 \times ₹40,000 = ₹1,000 \end{aligned}$$

Thus, the commission amount is ₹1,000 for a total sale of ₹40,000 with a commission rate of 2.5%.

Example

An insurance agent sells a life insurance policy worth ₹5,00,000, and the agent earns a commission of ₹20,000 for this sale. So, the commission rate is

$$\begin{aligned} \text{Commission Rate (\%)} &= \left(\frac{\text{Commission Amount}}{\text{Sale or Revenue}} \right) \times 100 \\ &= \left(\frac{20,000}{5,00,000} \right) \times 100 = 0.04 \times 100 = 4\% \end{aligned}$$

So, the commission rate for an insurance policy of ₹5,00,000 and a commission amount of ₹20,000 is 4%.



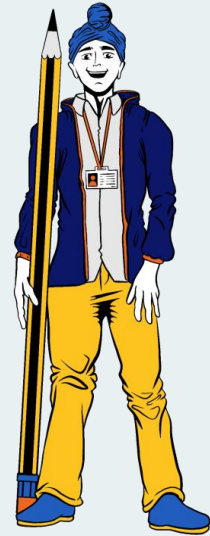
Knowledge Check

Answer the following questions

1. Riya works as a financial advisor, and she earns a commission of 5% on each health insurance policy she sells. If she sells health insurance with a policy coverage amount

of ₹5,00,000. The commission Riya earned from this sale is _____.

2. Thomas sold two policies in January with a premium amount of ₹80,000 and ₹40,000, and he received a commission of 30% of the total premium sold that month. What is the total commission amount he earned that month? _____
3. A financial advisor earns a commission of ₹1,200 for selling a product worth ₹ 8,000. What is the commission rate?
4. Deepa works for a financial company and helped a client invest ₹80,000 as deposit money. She received a commission of 3% on the total amount invested. The commission amount received by Deepa is _____.
5. Gagan works for a financial service company that pays profit-based commissions. He sold 10 health insurance policies and generated a total profit of ₹2,50,000 for the company. With a commission rate of 12%, how much commission did he earn?



Answers:

1. ₹25,000 2. ₹36,000 3. 15% 4. ₹2,400 5. ₹ 30,000

4.2 Overview of Budgeting

Budgeting is the process of planning how to use your money. It helps you decide how much to spend, save, and invest, ensuring you have enough for your needs and goals. **For example**, if you get ₹500 as pocket money, you might budget it by saving ₹200, spending ₹200 on school supplies, and keeping ₹100 for fun activities. This helps you manage your money better and avoid running out unexpectedly. Similarly, companies use a budgeting strategy just like how you manage your pocket money.

Budgeting is the process of planning on how to spend the money. It helps companies determine if they have enough money and prioritise their expenses according to needs and wants.

Most companies use spreadsheets or budgeting apps to organise their money plans. Budgeting is important for managing a business because it helps turn big, long-term ideas into specific, measurable actions. The process involves several steps, from planning the budget to putting it into action. If the budget isn't accurate, it can cause cash flow issues and even put the business at risk.



Steps in Budgeting Process

1. **Review the previous budget:** Before creating a new budget, check last year's budget. Look at what was spent and earned to see if the predictions were right. This helps in learning from past mistakes to make a better budget for the next year.
2. **Calculate current income:** Look at all the ways the business makes money, like sales. Then, figure out how much money will be available to spend in the coming year.
3. **Identify fixed costs:** Fixed costs are the expenses that don't change, like rent, employee salaries, and insurance. These must be paid no matter how well the business is doing, so they should be planned first.
4. **List variable costs:** Variable costs can change depending on the business, such as marketing, buying new supplies, or employee bonuses. These costs are more flexible, so they need careful planning.
5. **Plan for extra expenses:** Sometimes, unexpected costs arise, like buying new equipment. Set aside a certain amount of money for emergencies or one-time expenses.
6. **Analyse cash flow:** Cash flow is the money moving in and out of the business. See if income is steady or changes during the year. For example, some months may have more clients, and others may have fewer. Adjust the budget accordingly to avoid spending more than what's earned.
7. **Make smart business decisions:** After gathering all this information, decide which projects should get funding and which can wait. This step can be tricky, but using data and team discussions makes it easier.
8. **Communicate the budget:** Once the budget is ready, share it with the team. Everyone should know how much they can spend and what to prioritise. Clear communication avoids confusion and helps the team track spending throughout the year.

Example

Let's say your school is planning an annual fair and needs to create a budget. Here's how they would do it:

1. **Review last year's fair budget:** Last year, the school spent ₹50,000 and earned ₹60,000, helping them understand what worked well.
2. **Calculate current income:** This year, they predict earning ₹70,000 from ticket sales and renting stalls.
3. **Identify fixed costs:** Fixed costs include renting tents for ₹10,000 and paying for security guards at ₹5,000. These costs are necessary.
4. **List variable costs:** Variable costs might include spending ₹15,000 on prizes and decorations, which can change based on their plans.
5. **Plan for extra spending:** The school sets aside ₹5,000 for unexpected expenses, like repairs or additional prizes.



6. **Analyse cash flow:** They check when expenses occur, like paying for tents and security before ticket sales start, to ensure they have enough money upfront.
7. **Make decisions:** The school decides how much to spend on games and food stalls, balancing priorities within the budget.
8. **Communicate the budget:** Finally, the principal shares the budget with teachers and student volunteers, ensuring everyone knows their spending limits.

By following these steps, the school can successfully organise the fair while managing their funds wisely!

4.2.1 Importance of Budgeting in Financial Services

Budgeting is an important aspect of the financial services industry. This helps financial service sectors like banks, investment firms, and other insurance companies and institutions **analyse** and properly **allocate their money** according to their needs.

- Budgeting allows companies to **plan how to spend their money effectively**. It ensures they invest in areas that will give them good returns, meet customer needs, and stay ahead of their competitors.
- The budgeting process helps managers **think about any changes** that might happen and what steps they need to take. It also helps them understand how to solve problems when they come up.
- Budgeting encourages managers to **work together** and understand how different teams within the organisation function. This teamwork can lead to a bigger positive impact on the entire organisation.
- When employees know that their performance is connected to their pay and bonuses, they are more **motivated to meet budget goals**. Participation in the budgeting process makes everyone feel involved.
- Budgeting plays an important role in effectively **managing their debt**. It helps organisations to set money aside to pay debt and other obligations, helping the organisation stay debt-free and avoid another debt. It also helps to find areas where spending can be cut or redirected expenses.



Knowledge Check

I. Fill in the Blanks:

1. Budgeting helps you decide how much to spend, save, and _____.
2. If you get ₹500 as pocket money, you might budget it by saving ₹200, spending ₹200 on school supplies, and keeping _____ for fun activities.
3. Companies often use _____ or budgeting apps to organise their money plans.
4. Fixed costs are expenses that don't change, like rent, employee _____, and insurance.

5. Cash flow refers to the money moving _____ and _____ of the business.
6. Budgeting helps financial services like banks and investment firms analyze and properly _____ their money according to their needs.
7. The budgeting process helps managers think about changes and what _____ they need to take.

II. Write True or False for the questions given below:

1. Budgeting is only important for personal finances and not for companies. _____
2. Variable costs are expenses that remain the same regardless of how well a business is doing. _____
3. Reviewing the previous budget helps in learning from past mistakes to create a better budget. _____
4. It's unnecessary to plan for extra expenses because they rarely happen.
5. Communicating the budget with the team ensures everyone knows how much they can spend and what to prioritise. _____
6. Budgeting only helps in spending money and does not help in managing debt. _____
7. Teamwork in budgeting can lead to a bigger positive impact on the entire organisation. _____
8. Budgeting is not important for companies to stay competitive in their industry. _____

Answers:

- I. 1. invest 2. ₹100 3. spreadsheets 4. salaries 5. in and out 6. allocate 7. steps
II. 1. False 2. False 3. True 4. False 5. True 6. False 7. True 8. False



Activity 5: Create a Commission Based Plan

Objective: Understand different commission types in a financial institution.

Instructions:

- You may divide the class into small groups
- Each group will create a name for their insurance agency and decide the type of insurance agency it is.
- The group needs to decide on one commission structure for their sales agents.
- The group will explain the reason for choosing the specific commission schemes and present the advantages and disadvantages of the specific type of commission they chose.



Let's Recap

- **Financial services** refers to the products and services offered by financial institutions like banks, insurance companies, and companies that support people and businesses in managing their money.
- **Pricing** is a crucial factor in the business's success; it should not be too high or too low and should be set at a **profitable and fair price**.
- **Pricing** depends on **demand, cost analysis, industry cost analysis, dynamic pricing**, and **regulations** related to pricing.
- Pricing strategies can be set using **cost-based, value-based and competition-based**.
- **Percentages and Markup** calculations are important for **understanding interest rates, fees and pricing strategies**.
- **Markup** is the **difference** between **the cost of a financial asset** and **its selling price**.
The formula is:
$$\text{Markup Percentage} = \frac{\text{Selling Price} - \text{Cost}}{\text{Cost}} \times 100$$
- The **commission** is the fee or percentage of the **amount paid** or charged by a broker or investment advisor for **handling purchases and sales of products for their clients**.
- The types of commission: **Straight Commission, Tiered Commission, Residual Commission, Territory Volume Commission, Profit- Based Commission**.
- **Budgeting** is the process of planning on how to spend the money. It helps companies determine if they have enough money and prioritize their expenses according to needs and wants.



EXERCISE

Objective Type Questions**MCQ:**

1. Which of the following is NOT a service provided by financial institutions?
 - a. Deposits and loans (Banks)
 - b. Insurance coverage (Insurance companies)
 - c. Social media management (Banks)
 - d. Digital money transfer (Companies like Paytm)
2. What is the primary function of financial services?
 - a. To manage advertising campaigns
 - b. To help people and businesses manage their money
 - c. To manufacture goods
 - d. To control the financial market
3. Which of the following factors influences the pricing of banking services?
 - a. Competitors' pricing
 - b. Government regulations
 - c. Demand for the product or service
 - d. All of the above
4. What is dynamic pricing in the banking sector?
 - a. Fixed pricing for all services
 - b. Prices that change based on market conditions
 - c. A strategy to keep prices the same forever
 - d. A pricing model for long-term loans only
5. What is the main focus of value-based pricing in the banking sector?
 - a. To base prices on production costs only
 - b. To set prices based on how much value customers perceive in the product or service
 - c. To match competitors' prices
 - d. To follow cost-plus pricing principles
6. Which of the following is a disadvantage of cost-plus pricing?
 - a. It ignores customer demand
 - b. It requires in-depth customer research
 - c. It adjusts prices based on market conditions
 - d. It leads to unpredictable pricing
7. How does a bank apply a foreign transaction fee on international remittances?
 - a. By charging a fixed fee per transaction
 - b. By adding a percentage fee on the converted amount
 - c. By setting different rates based on the recipient's country
 - d. By offering the fee as a discount to the sender
8. How do cash-back and discounts help banks attract new customers?
 - a. By offering higher interest rates
 - b. By providing extra benefits from card usage
 - c. By reducing fees for loans
 - d. By providing free insurance
9. What is an example of a variable cost for a business?
 - a. Rent
 - b. Employee Salaries
 - c. Marketing Expenses
 - d. Insurance
10. Why is it important for businesses to review the previous year's budget?
 - a. To decide how much to spend on entertainment
 - b. To learn from past mistakes and improve the new budget
 - c. To compare the company's performance with competitors
 - d. To avoid spending money on unnecessary items
11. How do companies typically handle

- compensation in a straight commission structure?
- Employees receive a fixed salary plus commission.
 - Employees only earn a commission, with no fixed salary.
 - Employees earn a commission based on profits, not sales volume.
 - Employees receive commission and additional bonuses for exceeding targets.
- What do banks gain by studying how customers use cash-back rewards?
 - Improved customer service
 - Insights into customer preferences and spending habits
 - Higher profit margins from loan products
 - Reduced overhead costs
 - What type of commission does an employee earn regardless of the price or amount of the sale?
 - Ramped commission
 - Flat commission
 - Straight commission
 - Profit-based
 - In which type of commission structure do employees earn more as they reach higher sales targets?
 - Profit-based commission
 - Ramped commission
 - Straight commission
 - Flat commission
 - What is the main advantage of a profit-based commission structure?
 - It encourages salespeople to focus on high sales volume
 - It motivates employees to make profitable sales instead of just increasing sales numbers
 - It provides a fixed salary regardless of performance
 - It helps employees earn commission without making
 - any sales.
 - Which type of commission is typically used in industries like real estate, insurance, insurance, and car sales?
 - Flat commission
 - Ramped commission
 - Straight commission
 - Profit-based commission
 - What is the main purpose of budgeting?
 - To spend money freely
 - To plan how to use money for spending, saving, and investing
 - To avoid spending money
 - To invest money only
 - What is the main advantage of a profit-based commission structure?
 - It encourages salespeople to focus on high sales volume
 - It motivates employees to make profitable sales instead of just increasing sales numbers
 - It provides a fixed salary regardless of performance
 - It helps employees earn commission without making any sales
- Fill in the blanks:**
- The expense a company has to pay to get the funds it needs for its business is called _____.
 - When launching new products, banks must consider how pricing will impact _____, costs, and ROI.
 - To increase their market share, banks may offer _____ or deals to attract new customers.
- One line Answers:**
- How is the foreign transaction fee applied in international remittances?
 - What is budgeting?
- Short Answer Type Questions**
- Explain the value-based pricing model.
 - What role does risk play in the pricing of financial services?
 - How does competition affect the pricing strategies in financial services?
 - What is the difference between cost-based and value-based pricing?

28. Why is it important to understand customer willingness to pay when pricing financial services?
29. How do regulatory frameworks impact the pricing of financial services?
30. What is dynamic pricing, and how is it applied in financial services?

Long Answer Type Questions

31. Explain the importance of budgeting in financial services, including its role in cash flow management, goal setting, and decision-making.
32. Explain the main objectives of pricing in financial services and how they influence a company's profitability.
33. Discuss scenarios where cost-plus including its role in cash flow management, goal setting, and decision-making.

ANSWER KEY

Objective Type Questions

MCQ:

1. c. Social media management (Banks)
2. b. To help people and businesses manage their money
3. d. All of the above
4. b. Prices that change based on market conditions
5. b. To set prices based on how much value customers perceive in the product or service
6. a. It ignores customer demand
7. b. By adding a percentage fee on the converted amount
8. b. By providing extra benefits from card usage
9. c. Marketing expenses
10. b. To learn from past mistakes and improve the new budget
11. b. Employees only earn commission, with no fixed salary.
12. b. Insights into customer preferences and spending habits

- a. b. Flat commission

13. b. Ramped commission
14. b. It motivates employees to make profitable sales instead of just increasing sales numbers
15. c. Straight commission
16. c. To plan how to use money for spending, saving, and investing
17. b. It motivates employees to make profitable sales instead of just increasing sales numbers

Fill in the blanks:

18. cost of capital
19. sales
20. discounts

One line Answers:

21. It is applied as a percentage of the amount converted into local currency.
22. Budgeting is the process of planning how to use your money for spending, saving, and investing.