Chapter II

Investment Opportunities
CHAPTER – II

2.1 INVESTMENT OPPORTUNITIES

Many types of investment media or channels are available for making investments. Some media are simple and direct, whereas others are complex necessitating detailed analysis and investigation. Some are popular, whereas others are relatively new. Some are appropriate for one type of investors, while others may be suitable for the rest of the types of investors. Whatever it is, the ultimate aim of the investor is to drive a variety of investments that fulfill his preference for risk and expected return.

The investor will select the portfolio, which will maximize his utility. Securities present a wide range of risk varying from risk-free instruments to highly speculative instruments like shares and debentures. Of the various securities available for investment, the investors will have to select those securities that will maximize his expected return. However, while doing so he has give considerations to certain things. It is not only the construction of a new portfolio that will promise the highest expected return; but also, it is the satisfaction of the need of the investor.
One investor may face a situation when he requires extreme liquidity as well as safety of securities. Such an investor will have to choose a security with low return. Another investor would not mind high risk but he would like a high return. He can put his savings in growth shares, because he is willing to accept risk. Another important factor to be considered is the temperament and psychology of the investor. Some investors are willing to take risks, while others are not willing to invest in risky securities even if the return is high. One investor may prefer safe government bonds, whereas another may be willing to invest in blue chip equity shares of the company. Hence, to fulfill the requirements of different kinds of investors, many alternative investments exist. These can be categorised in many ways.
KINDS OF INVESTMENTS

1. Direct Investment Alternatives, and
2. Indirect Investment Alternatives.

1. Cash,
2. Savings Account,
3. Savings Certificates,

1. Preference Shares,
2. Equity Shares,
3. Convertible Securities
4. Real Estate,
5. Commodities,
6. Art, Antiques & Other Valuables.
2.1.1 DIRECT INVESTMENT ALTERNATIVES

Direct Investment Alternatives are those where the individual makes his own choice and investment decision. These include the following:

1. Fixed Principal Investments,
2. Variable Principal Securities and
3. Non-Security Investments,

We shall now detail them as below;

1. FIXED PRINCIPAL INVESTMENT

Fixed Principal Investments are those whose principal amount and the terminal value are known with certainty. There will not be any change in the terminal value. These investments include the following:

i) CASH

Cash has a definite and constant value. It does not earn any return, while in hand. It is the safest investment. However, only a small portion is to be kept as cash because it does not carry any interest or earn any return.

b. FIXED DEPOSIT

A fixed deposit is one, which is repayable after the expiry of a predetermined period fixed by the customer himself. The period varies from 45 days to 3 years. The banker will issue a receipt, which is called
Fixed Deposit Receipt. This receipt is non-transferable. This means that the amount is payable is on maturity only to that deposit holder in whose name the deposit receipt stands. Thus, a fixed deposit account can be opened even in the name of a minor. The deposit amount is payable along with the interest at the rate as agreed upon. But a customer has the option to foreclose the deposit even before the date of maturity. In such a case, the customer will not be entitled to the agreed rate of interest.

A deposit can be opened for a period of more than 3 years and in that case the rate of interest remains the same at 13%. It is popularly known as “Term Deposit”.

The present rates applicable to fixed deposit in most of the nationalized banks with effect from 01.04.2002 are as follows*.

Table 3.2.1 – Interest Rates for Fixed Deposit

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Term of the Deposit</th>
<th>Interest p.a.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>15-45 days</td>
<td>4.75</td>
</tr>
<tr>
<td>2</td>
<td>46 &amp; up to 179 days</td>
<td>5.25</td>
</tr>
<tr>
<td>3</td>
<td>180 days to less than 1 year</td>
<td>6.25</td>
</tr>
<tr>
<td>4</td>
<td>1 year to less than 2 years</td>
<td>6.75</td>
</tr>
<tr>
<td>5</td>
<td>2 years to less than 3 years</td>
<td>6.75</td>
</tr>
<tr>
<td>6</td>
<td>3 years &amp; above</td>
<td>7.25</td>
</tr>
</tbody>
</table>

* State Bank of India
ii) SAVINGS CERTIFICATES

National Savings Certificate (NSC) is an assured return scheme, armed with powerful tax rebates under Section 88 of the Income Tax Act, 1961. Interest is payable at 9.5 percent, compounded half-yearly for a duration of 6 years.

The NSC has the backing of the Government of India. Therefore, the investment is assured. Since the NSC has the backing of the Government of India, your income at the prescribed rate of interest is assured. This is a safe long-term savings option.

NSCs are issued in denominations of Rs.100, Rs.500, Rs.1000, Rs.5000 and Rs.10,000. There is no prescribed upper limit on investment in NSCs. The maturity period (duration) of a NSC scheme is 6 years. NSCs cannot be traded in the secondary market. But they can be transferred from one person to another through the post office on payment of a prescribed fee.

NSCs do not offer any scope of premature withdrawal except on death or forfeiture by pledge or by court order. However, NSCs can be transferred from one person to another through the post office on the payment of a prescribed fee. They can also be transferred from one post office to another on payment of a prescribed fee.

NSCs are a popular choice for savings due to their assured return and backing by the Government of India. They offer a secure long-term investment option with the added benefit of tax rebates.
office to another. If a certificate is lost, destroyed, stolen or mutilated, the post-office on payment of the prescribed fee can issue a duplicate. NSCs are held physically in the form of certificates issued to the investors by post office.

**Tax Implications**

NSCs offer tax benefits as per the provisions of the Income Tax Act, 1961. Rebates are available under Section 88 of the Income Tax Act, 1961 on both the principal as well as interest income.

Moreover, the annual interest income (till five years) is deemed reinvested under Section 88, and is eligible for a 20 percent tax rebate. The interest income every year also qualifies for exemption under section 80 L of the Income Tax Act.

2. **VARIABLE PRINCIPLE SECURITIES**

The variable principal securities are those whose terminal values are not known with certainty. They include the following:

i) **PREFERENCE SHARES**

Preference shares unlike bonds have an investment value, as it resembles both bonds as well as common stock. It is a hybrid between the bond and common stock. It resembles a bond as it has a prior claim on the assets of the firm at the time of liquidation. Like the common
stock, the preference shareholders received dividend and have similar features as common stock and liabilities at the time of liquidation of a firm.

They carry the right of a fixed rate of dividend. Preference shareholders are to be paid prior to the payment of ordinary shareholders. Even though preference shares have a fixed return, the price of preference shares is determined by demand and supply forces. Preference shareholders do not have the right to vote at annual general meeting or decide on company policy. Preference shares may be issued with or without a maturity period. But, they are not frequently issued now a days.

Features of Preference Shares

- **Claims** : Preferences Shareholders have a claim on assets and income prior to ordinary shareholders.

- **Dividend** : The dividend rate is fixed in the case of preference shares. Preference shares may be issued with cumulative rights, i.e., dividend will accumulate until paid off. Dividends paid to preference shares are not tax deductible.

- **Redemption** : Both redeemable and irredeemable preference shares can be issued in India. Redeemable preference shares have a maturity date, while irredeemable preference shares are perpetual.
Conversion: A company can issue convertible preference shares. That is, after a stated period, such shares can be converted into ordinary shares.

ii) Equity Shares

Equity shares are also called common shares and are from the point of view of investment, more risky than both bonds and preference shares. They, however, afford greater advantage than both the other securities, and in the capital market enjoy a better position. The holders of these shares are the real owners of the company. They bear the rights and enjoy the benefits. In a bad year when the company has made little or no profits, they receive no dividends. Conversely in good times, they large dividends and bonus shares. These shareholders are the ones entitled to vote and decide on company policy. In liquidation, they divide among themselves the assets leftover after all others including preference shareholders have been paid. They stand to lose their investment if there are no assets left after the others have been paid off. On the other hand, they stand to make a lot of money if the assets remaining are far in excess of their original investments.

It is equity shares that are traded in the market, often at several times their face value. It is these shares that appreciate in good time and fall during bad times.
Equity shares can be sub-divided into;

(a) **Income shares**: These shares do not appreciate in value much, but the dividends paid on them are high. Consequently, there is usually a limit on how much these shares will grow.

(b) **Growth Shares**: The earnings of growth shares are higher than those in the same industry. Consequently, their appreciation is higher. The results will be low, as the company would be reinvesting the bulk of their profits in company in order for it to grow.

**Features of Equity Shares**

- **Claims**: Equity shareholders have a residual claim on the company’s income and assets. They are the legal owners of the company.

- **Dividend**: In the case of equity shares, neither the dividend rate is known, nor does dividend accumulate. Dividends paid on equity shares are not tax deductible.

- **Redemption**: Equity shares have no maturity date.

- **Voting Rights**: Ordinary shareholders are required to vote on a number of important matters. The most significant proposals include: election of directors and change in the memorandum of association, etc. Each ordinary share carries one vote. Thus,
ordinary shareholder has equal to the number of shares held by him.

- **Limited Liability**: The liability is limited to the amount of their investment in shares. If a shareholder has already fully paid the issue price of shares purchased, he has nothing more to contribute in the event of a financial distress or liquidation.

iii) **CONVERTIBLE SECURITIES**.

Convertible securities are the oldest hybrid securities. They combine the basic attributes of fixed interest and variable income securities. Individual issues of convertibles are all alike in some characteristics but vary significantly in other attributes. Each convertible security provides that it may be exchanged for another security that conveys different rights, privileges, restrictions and limitations. Nearly all-convertible securities carry prior rights – those of debt obligation or preference share - plus a privilege to convert into equity of the issuing company. They tend to provide both higher flows of income (i.e. interest or dividends) and smaller price fluctuations than the equity into which they may be converted. Once converted into equity, they cannot be exchanged for bonds or preference share of the issuing company.
A company can issue convertible securities to ensure the success of its debt issue. Convertible securities, particularly convertible debentures, have become quite popular in India recently.

a) CONVERTIBLE DEBENTURE

A convertible debenture is a debenture that can be changed into specified number of ordinary shares at the option of the owner. The most notable feature of this debenture is that it promises a fixed income associated with debenture as well as chance of capital gains associated with equity share after the owner has exercised his conversion option. Because of this combination of fixed income and capital gains in the convertible debenture, it has been called a hybrid security. A company can also issue convertible preference share.

Features of Convertible Debentures

When a company issues a convertible debenture, it clearly specifies, conversion terms, which indicate the number of equity shares in exchange for the convertible debenture, the price at which conversion will take place and the time when the conversion option can be exercised.

1. **Conversion Price**: The conversion price is the total price at which an ordinary share is issued and allotted to the debenture holder. This includes the premium over the par value. The determination of the conversion price is based on a number of factors including
the existing book value, the market price, expected appreciation in the value of equity shares, etc. however, the critical factor is the yield to the investor.

2. **Conversion Ratio**: The conversion ratio is the number of equity shares received in exchange for a convertible bond. In other words, the conversion ratio is:

\[
\text{Conversion Ratio} = \frac{\text{Face Value of the Bond}}{\text{Conversion Price}}
\]

3. **Quantum of Conversion**: The quantum to be converted is normally specified in terms of a percentage of the face value of the debenture or bond. The amount to be so converted is translated into the number of equity shares based on the conversion price. Hence, the increase in the capital base will be dependent on the percentage conversion and the conversion price. For a specified percentage, the higher the conversion price, lower will be the addition to capital base.

4. **Convertible Value**: The conversion value is the value of the convertible based on the right to receive equity shares. The conversion value of a convertible is the conversion ratio times the market price per share of the equity.
5. **Market Price**: This is price the market places on a convertible because of its two features – its conversion value and its investment value. The convertible bond can be thought of as a combination of a bond plus an option to buy firm’s equity shares. If the value of the equity share raises, the value of the option and hence that of the convertible bond will rise. If the value of the equity falls, the value of the convertible as a bond provides a floor below which the price of the conversion will not fall. This opportunity to be protected from a decline in the equity price by the investment value and yet be able to benefit from a rise in the equity share price caused the convertible to sell at a premium.

6. **Timing of conversion**: This relates to the period during which the conversion option is exercisable. This can range anywhere from one year from the date of allotment to up to five years. However, from the company’s point of view, the longer duration is preferable from two counts: (a) low pretax financing cost till conversion, (b) postponement of earnings dilution and the attendant higher dividend outgo.

b) **CONVERTIBLE PREFERENCE SHARES**

In addition to convertible debentures, companies may issue convertible preference shares. As its name implies, the convertible preference shares may be converted into the equity of the issuing
company. Though they are similar to convertible debenture, however, there are some important differences. The differences are primarily the same as those between non-convertible preference share and non-convertible debt. Preference share is treated as an equity investment. Thus, the company is not under any legal obligation to pay the dividend. In addition, the preference share is a perpetual security and does not have to be retired, as debt must be.

The convertible preference share's value as non-convertible preference share is related to the dividend it pays and to the appropriate discount factor which is the yield earned on competitive debt. This is essentially the same as the convertible debenture's value as debt, except that preference share has no definite maturity date. However, this value does not set a floor or the price of a convertible preference share because at that price it is competitive with non-convertible preference share.

3. NON-SECURITY INVESTMENT

i) REAL ESTATE

Real Estate is emerging as a lucrative medium term investment opportunity, in addition to being the most competitive long-term option. Investment in property is now being viewed as a serious alternative to other forms of investment, with low interest rates and the stock market not showing any big signs of recovery.
The risks are similar to that of other speculative markets or sectors. Vacancy risk, large minimum investment size, future depreciation in value, falling capital values and low liquidity are a few of the risk associated with real estate investments.

Diversification of investments into various property classes, and perhaps different geographical markets, is a preferred route for secure long-term investments.

The rupee returns are comparable with other countries in South East Asia. While the current rental yields vary from 5.5% for prime residential to 11% for retail and office premises. The total (pre-tax) returns expected form this sector is between 8 - 18%.

The capital appreciation potential is seen to be high only for residential property. The residential sector has emerged as an appropriate short-term investment alternative for small individual investors. Retail and office space continues to be the target for medium scale investors. Large institutional investors are targeting Grade-A office space [typically targeted towards the software/IT firms.]

Also, there are many kinds of real estate investments. Some are very speculative while others are more conservative. The major classifications are:
- Unimproved land
- Improved Real Estate
- New and used residential property
- Vacation homes
- Low Income housing
- Certified historic rehab structures
- Other income-producing real estate such as office buildings, shopping Centers and industrial or commercial properties

ii) COMMODITIES

Investments in commodities includes gold, silver and diamond.

a. GOLD

Gold is one of the most valuable assets in any economy. It has been used in India primarily as a form of saving by the housewives. Although it is said to appreciate many times yet in India it is more of a sense of security and a fixed asset rather than for the use of sale or for the purchase of making profit or income on this investment. Gold may be called a hedge against inflation or a well or reservoir for future use or substitute for the rupees, which are used as a means of transfer or exchange. Gold to the investor in recent years has been important mainly because of rise in prices due to inflation. It has been used more
for speculation rather than for a long-term investment and for quick profits. Gold may be invested in, either in the form of gold shares, which are banned in India, gold coins, gold bars and gold Jewellery.

b. SILVER

Silver is solid in the form of weight by kg in India. Silver may be owned in the form of coins, utensils, glasses, bowls, plates, trays or Jewellery. This, like gold, has been a hedge during inflation. The price of silver, although less than gold, also keeps on rising in the same way as gold. At the time of resale of these investments (after using the plates, etc.), the silversmith takes away the expenses of polish and non-silver, which is used in shaping these beautiful vessels. As a result, the investor is able to get only 60% of the value of silver. Silver coins have a higher return in the form of value. Silver bars are also legal and can be used for selling. The sale price of silver bars is the price recorded for pure silver. The price of silver and gold is quoted daily in the stock exchange list.

c) DIAMONDS

Diamonds purchased in raw form and through a wholesaler may be the best investment potential. Since the price of diamonds keep on increasing in the same way as the price of gold, they have good investment value. The price of diamond increases as the diamond caret
becomes higher. In gold 10 grams is the measure, silver is sold in kgs and diamond is valued in carets. Diamond is to be judged in terms of weight, size, shape and lure. The investor must be careful that he is not cheated. It is extremely risky form of investment because to a large extent the value of diamond is based on judgement. The marked up retail price is also very high. Investing in diamonds should be done only through professional advice and when an investor has money to hold for a number of years. Immediate acquisition and sale of diamond will not fetch price increase. Holding a diamond for some years will give it an appreciation. Money speculators for earning profit use it.

iii) ART, ANTIQUES AND OTHER VALUABLES

a. ANTIQUES

For antiques demand is more and supply is very rare as this increased its value. It has been found that the longer the time of holding this investment the greater the value of this asset. Antique may be in the form of paintings, coins, stamps, flower vases, watches or cars. The basic advantage of an antique is that the investor can sell it at any price, which he propounds. but it is very difficult to find these antiques to give a price for which it is worthy. A careful study of this subject and professional advice will give the investor a good return. Antiques are very risky for long period investment. There are many whole time
antique dealers. For them the sale of only one piece makes a fortune. This sale may, however, take a whole year, before it has left his collection. These risks must also be guarded against before planning to invest in antiques.

b) OTHER COLLECTIBLE

Collectibles can include anything from paintings, to stamps, to automobiles, to Barbie dolls. There is virtually no end to what people collect with the anticipation that the price for these items will raise in the future, primarily because of a perceived future rarity of the item. While there have been cases of windfall profits, be aware that there are a couple of inherent problems with these investments. First of all, they rarely if ever pay the investor an ongoing income stream such as the interest from a bond or the dividends from a stock; therefore, the investment can be "dead money" while being held. Secondly, there often is a very limited market for resale of the items, resulting in both poor liquidity and marketability.

2.2 INDIRECT INVESTMENT ALTERNATIVES

1. PUBLIC PROVIDENT FUND - 1968

Scheme introduced by Central Government in 1968. The Scheme enables the members of the public to make contributions to the Fund
and obtain Income Tax rebate under the relevant provisions of the Income Tax.

Minimum / Maximum Investment (W.E.F. 15.11.2002)

- Minimum Rs.500/- per annum in multiples of Rs.5/-
- Maximum Rs.1,00,000/- per annum

Duration

- 15 years
- Can be extended for one or more blocks of 5 years.
- Account can be discontinued but repayment of subscriptions along with interest only after 15 year.

Rate of Interest

8% per annum w.e.f 01.03.2003 credited in account on 31 March every year calculated on minimum balance between 5th day and end of the month.

Tax Benefits

- Benefits available u/s 88 of the I.T.Act.
- Interest totally exempt from Income Tax.
- Amount standing to the credit is fully exempted from Wealth Tax.

Other Facilities

- Subscription in lump sum or maximum 12 installments.
- Only one instalment in one month can be made.
- Discontinued account can be revived on payment of Rs.50/- per
year along with arrears of subscription of Rs.500/- per annum w.e.f 15.11.2002.

- Nomination available in the name of one or more person.
- Nominee cannot continue account of the deceased subscriber in his/her own name.

2. INSURANCE

Life Insurance made its debut in India well over 100 years ago. Today, it is widely accepted as one of the most attractive financial instruments in an individual’s portfolio, which provides an assurance of security with attractive returns.

Life insurance is a contract for payment of a sum of money to the person assured (or failing him or her, to the person entitled to receive the same) on the happening of the event insured against. Usually the contract provides for the payment of an amount on the date of maturity or at specified dates at periodic intervals or at unfortunate death, if it occurs earlier. Among other things, the contract also provides for the payment of premium periodically to the corporation by the assured. Life insurance is universally acknowledged to be an institution, which eliminates ‘risk’, substituting certainty for uncertainty and comes to the timely aid of the family in the unfortunate event of the death of the breadwinner. By and large, life insurance is civilization’s partial solution to financial
uncertainties caused by untimely death.

Life insurance, inshore, is concerned with two hazards that stand across the life path of every person: that of dying prematurely leaving a dependent family to fend for itself and that of living to old age without visible means of support.

PLANS MARKETED BY LIC

LIC offers a basket of schemes to meet the various needs of an individual and his family

I) BASIC LIFE INSURANCE PLANS

1. Whole Life Assurance Plan: A low cost insurance plan where the Sum assured is payable on the death of the life assured, whenever it occurs.

2. Endowment Assurance Plan: Under this plan, the Sum assured is payable on maturity or on death of the life assured, if earlier.

II. TERM ASSURANCE PLANS

1. Two-Year Temporary Assurance Plan: Term assurance for periods of up to 2 years is available under this plan. The sum assured is payable only on death of the life assured during the policy term.
2. **Convertible Term Assurance Plan**: The plan provides for term assurance for 5 to 7 years with an option to purchase a new Limited Payment Whole Life Policy or an Endowment Assurance Policy at the end of the selected term provided the policy is in full force.

3. **Bima Sandesh**: This Term Assurance Plan provides for return of premiums paid, on the life assured surviving the policy term.

4. **Bima Kiran**: In addition to benefits available under Bima Sandesh Plan, this plan provides Loyalty Addition, in-built accident cover and Free Term Cover after maturity, if the policy is in full force on the date of maturity.

**III. PLANS FOR CHILDREN**

Various Children’s Deferred Assurance Plans are available, viz., CDA, Jeevan Balya and Jeevan Kishore. Jeevan Sukanya is a plan specially designed for girls. The Children’s Money Back Assurance Plan is an annual premium plan designed to provide for children’s higher educational expenses with added attractions of Guaranteed Additions, Loyalty Additions and optional family benefit.

**IV. PENSION PLANS**

These plans provide for immediate or deferred pension for life. Pension payments are made till the death of the annuitant (unless the
policy has provision of a guaranteed period). There is also an option, which provides return of the purchase price on death of the annuitant. We have Jeevan Suraksha plan which provides pension for the spouse also. Premium paid up to Rs.10,000 is exempted for income tax under section 80 CCC(1).

V OTHER PLANS

1. Jeevan Griha (Double & Triple Cover) : For the people desirous of obtaining a housing loan with the policy acting as collateral security and to ensure repayment of the loan in the event of the premature death of the borrower.

2. Mortgage Redemption : Suitable for borrowers repaying loan in instalments as it ensures that the outstanding loan is repaid in the event of the borrower’s death.

3. Bhavishya Jeevan : This is a special investment plan which is coming with profit and for the specific and is very beneficial. This is also for a term period of 15 to 20 or 25 years.

4. New Jana Raksha : Ideal for people with no regular income. It provides for death cover for a period of 3 years from the first unpaid premium, provided at least 2 full years’ premiums have been paid.

5. Double Endowment : This is an Endowment Assurance plan with double the sum Assured payable on maturity.
6. **Fixed Term (Marriage) Endowment/Educational Annuity**: A plan suitable for making provision for start-in-life, marriage or education of children.

7. **Convertible Whole Life**: The policy is issued as a Whole Life Plan with an option to convert it into an Endowment Assurance at the end of the 5 years. A plan suitable for those who cannot afford high premium in the initial years but have prospects of increased income within a few years.

8. **Money Back Plan**: Besides providing life cover during the term of the policy, sum assured is paid in instalments by way of survival benefits during the term of the policy.

9. **Jeevan Surabhi**: A money Back Plan where premiums are payable for a limited period, with periodical increase in insurance cover.

10. **Jeevan Sathi**: This has a maximum assured sum of Rs.50,000/-, if wife is housewife and 2 lakh if wife is working. The minimum assured sum is Rs.10,000. It has maturity after 15, 20, 25 and 30 years at the end of the policy. Lives of husband and wife are under a joint cover and the age of maturity cannot exceed 70 years. If one partner dies, the other partner need not pay any further premium till maturity. This scheme has a very poor return.
11. **Jeevan Chhaya**: This plan of LIC has been provided for the higher education of children. The policy is issued on the life of the parent- it has many benefits. It has bonus for the full sum assured but is paid at the end of the term. \( \frac{1}{4} \)th of the same is payable at the end of each of the last 4 years. In addition to this benefit, the sum assured will be paid on the death of the policyholder during the term of the policy. The policy is for the term period of 20 to 25 years.

12. **Jeevan Mitra**: An Endowment Assurance plan with twice or thrice the sum assured payable on the death of the life assured during the policy term.

13. **Jeevan Shree**: This is one of the most popular policies of the Life Insurance Corporation of India. It offers protection of life with bonuses and additional benefits of a higher return than other endowment policies.

14. **Asha Deep-II**: The plan provides, besides death and maturity payments, benefits in case the life assured suffers from any of the four defined ailments.

15. **Jeevan Sanchay**: This is a Without-Profit Money Back type plan with provision for Guaranteed Additions at the rate of Rs.70 per thousand sum assured p.a. and Loyalty Additions payable on maturity or earlier death.
16. **Jeevan Sneha**: A Money Back Plan exclusively for women. There is provision for Guaranteed Additions at the rate of Rs.70 per thousand sum assured p.a. and Loyalty Additions payable on maturity or earlier death.

17. **Bima Nivesh**: A single premium plan of assurance with compounding Guaranteed Additions at the rate of Rs.85 per thousand sum assured p.a. for first 5 years and Rs.90 per thousand sum assured p.a. for next 5 years. The same premium is payable for a given policy term, irrespective of age at entry.

18. **Jeevan Asha-II**: The plan provides, besides death and maturity benefits, payment towards certain surgical procedures and periodical survival benefit payments. There is also a provision for Guaranteed Additions at the rate of Rs.70 per thousand sum assured p.a.

**Tax Benefits From Life Insurance**

Some important Income Tax Benefits offered from Life Insurance are highlighted below:

a. **Income tax exemption on Maturity/Death Claims proceeds under section 10(10D)**

   Under the provisions of Sub-section 10D of Section 10 of Income Tax Act, 1961, any sum received under a life insurance policy, including the sum allocated by way of bonus on such policy other than any sum
received under Sub-section (3) of Section 80 DD (i.e., amount to be refunded under Jeevan Aadhar Insurance Plan in case the handicapped dependent predeceases the individual) or under a Keymen Insurance Policy, is exempted from income tax.

b. Jeevan Suraksha Plan (u/s. 80CCC)

A deduction to an individual for any amount paid or deposited by him from his taxable income in the above annuity plan for receiving pension (from a fund set up by the Corporation) is allowed. The deduction will be restricted to Rs. 10,000.

c. Jeevan Aadhar Plan (Sec. 80(0)

As per Section 80DD, an amount not exceeding Rs. 40,000 deposited with Life Insurance Corporation of India under Jeevan Aadhar Plan for the maintenance of handicapped dependent is eligible for deduction from the total income.

d. Rebate in respect of contribution of P.F., Insurance Premia etc.

According to Section 88, the amount of income tax payable on the total taxable income is to be reduced by 20% (25% in case of author, playwright etc.) of the aggregate amount paid towards the following (as detailed under the head "Rebate of Income Tax under Section 88") subject to the maximum of Rs. 80,000* in case of an individual and HUF and in case of authors, playwright etc. the maximum limit is Rs. 80,000*.
Therefore, the maximum amount of rebate in income tax payable will be Rs.16,000, (Rs. 17,500 in the case of author, playwright etc.)

*Provided investment in a public sector company engaged in infrastructure including power sector is Rs. 20,000 or more, otherwise Rs.60,000.

3. MUTUAL FUND

Mutual funds are a specialized investment vehicle that allows one to pool savings and consolidate them into a fairly large and diversified portfolio of investment. The pooled funds are invested in securities or assets as per the objective of the scheme in which it is collected and the returns or growth is distributed to the investors. Mutual funds are managed by professionals and are well regulated by SEBI, now who keep track of industries or companies and monitor their performance, which an individual investor finds difficult.

Mutual fund is comparatively a new entity in the financial market. Mutual funds were introduced in India 40 years ago as an investment vehicle when UTI launched US-64 - India's first and one of the most popular mutual fund schemes. However, as a financial services industry, mutual funds have had a short history of only in years as Morgan Stanley, Kothari Pioneer Mutual Fund and Taurus Mutual Fund launched their maiden schemes in 1993-94. Since then, a lot of
transformation has taken place and now mutual funds are offering a wide range of new products to their investors.

Mutual fund is the most suitable investment vehicle for the common person who desires to invest funds at regular intervals in a diversified portfolio. Such investment decisions offer an opportunity to invest in a diversified, professionally managed basket of securities at a relatively low cost.

Mutual fund is an investment tool, which is unlike banks, insurance, and other saving schemes. Therefore, the return on the Investment from the mutual fund cannot be compared with other savings tools available in the market.

At times, returns can be high and at times they can be negative. Therefore, the future growth of the mutual fund industry largely depends on removing the misconception in the investor community that mutual funds are not saving tools. Before making an investment, an investor is required to analyse the following important areas.

- What is the risk taking capacity?
- Period of investment horizon
- Expected returns
- Tax liability

As per an analysis made by JM Morgan Stanley, it is expected that the equity mutual fund industry will grow from the present level of Rs.
30,000 crore to Rs. 4,20,000 crore in 10 years i.e., at a compounded growth of 32% in assets under management.

(i) Characteristics of a Mutual Fund

a. A mutual fund actually belongs to the investors who have pooled their funds. The ownership of the mutual fund is in the hands of the investors.

b. A mutual fund is managed by investment professionals and other service providers, who earn a fee for their services, from the fund.

c. The pool of funds is invested in a portfolio of marketable investments. The value of the portfolio is updated every day.

d. The investor’s share in the fund is denominated by “units”. The value of the units changes with change in the portfolio’s value, every day. The value of one unit of investment is called as the Net Asset Value or NAV.

e. The investment portfolio of the mutual fund is created according to the stated investment objectives of the fund.

Advantages to Investors:

The mutual fund concept is basically designed to take care of the interest of the retail investors who do not have adequate knowledge of the capital market. Broadly, investors investing through a mutual fund will have the following advantages:
Professional Management,

Diversification,

Convenient administration,

Return Potential,

Low costs,

Liquidity,

Transparency,

Flexibility,

Choice of schemes,

Tax benefits,

Well regulated,

(iii) Mutual Fund Products

Mutual funds are investment portfolios that invest in financial market instruments. Pooling investor contributions, usually denominated in units, creates these portfolios. There are a variety of ways in which mutual funds are created, to cater to the varied risk and return requirements of investors. Depending on the investment portfolio that is created, and the segments of the various markets in which funds are invested, there is a choice of funds to investors.

Mutual funds can offer further generic choices to the investors in terms of
1. Nature or Participation - Open/Closed end funds,

2. Nature of Income Distribution — Dividend, Growth, Re-investment of dividends, investors can also chose from varying periodically for distribution of dividends — daily, weekly, monthly, quarterly or annual.

**NATURE OF PARTICIPATION**

1.(a) **OPEN ENDED FUNDS**

In an open-ended fund, investors can buy and sell units of the fund, at NAV related prices, at any time, directly from the fund. This is an open-ended fund because; the pool of funds is open for additional sales and repurchases. Therefore both the amount of funds that the mutual fund manages and the number of units, vary every day. The price at which investors buy or sell units is linked to the NAV. Open-ended funds have to balance the interests of investors who come in, investors who go out and investors who stay invested. Open-ended funds are offered for sale at a pre-specified period, say 30 days, the fund is declared open for further sales and repurchases. These transactions happen at the computed NAV related price. An investor in an open-ended fund can liquidate his investments by repurchasing the units from the fund. Investors in open ended funds receive an account statement of their holdings.
A closed and fund is open for sale to investors for a specific period, after which further sales are closed. Any further transaction for buying the units or repurchasing them, happen in the secondary markets, whose closed end funds are listed. Therefore new investors buy from the existing investors and existing investors can liquidate their units by selling them to other willing buyers. In a closed end fund, thus, the pool of funds can technically be kept constant. The AMC, however, can buy out the units from the investors, in the secondary market, thus reducing the amount of funds held by outside investors. The price at which units can be sold or redeemed depends on the market prices, which are fundamentally linked to the NAV. Investors in closed end funds receive either certificated or depository receipts, for their holdings in a closed end mutual fund.

In earlier days of the mutual fund industry, most mutual funds were close-ended, and were listed in the stock exchanges. One of the reason fund managers chose to have closed end funds, was the apprehension that underlying markets may not be liquid enough to support frequent changes in the size of the investment portfolio. However, closed end funds presented a statement of other problems. Investors perceived mutual funds to be akin to equity shares, because the
issue process was similar to that of equity shares: a limited initial offer period and subsequent listing on stock exchanges. This perception created unrealistic return expectations from mutual funds. The next problem was the discount at which mutual funds were priced, to the NAV, in the secondary markets. Most mutual fund units were priced at steep discounts, ranging from 15% to 45%. Since the mid-1990s, mutual funds have been opening repurchase windows, at NAV linked prices, for their closed end funds; may closed end funds have also been converted into open-ended funds. As at the end of March 2001, 74% of the assets managed by the Indian Mutual Fund industry are in open-ended funds.

2. NATURE OF INCOME DISTRIBUTION

a. DIVIDEND OPTION

Investors, who choose a dividend option on their investments, will receive dividends from the mutual fund, as and when such dividends are declared. Dividends are paid in the form of warrants, or are directly credited to the investors’ bank accounts.

Mutual funds provide investors the option of receiving dividends at pre-determined frequencies, which can vary from daily, weekly, monthly, quarterly, half-yearly and annual. Investors can choose the frequency of dividend that suits their requirements. Not all mutual funds provide all of
these frequencies as choices, though. Investors can choose an income distribution frequency from the choices available in a particular mutual fund product. Investors choosing this option, have a fixed number of units invested in the fund, and earn incomes on this investment. The NAV of these investors’ holdings will vary with changes in the value of the portfolio, and the impact of the proportion of income earned by the fund, to what is actually distributed as dividend.

b. **GROWTH OPTION**

Investors who do not require periodic income distributions can choose the growth option, where the incomes earned are retained in the investment portfolio, and allowed to grow, rather than being distributed to the investors. Investors with longer-term investment horizons, and limited requirements for income, choose this option. The return to the investor who chooses a growth option is the rate at which his initial investment has grown over the period for which he was invested in the fund. The NAV of the investor choosing this option will vary with the value of the investment portfolio, while the number of units held will remain constant.
c. **RE-INVESTMENT OPTION**

Mutual funds also provide another option to investors in the form of re-investment. Investors re-invest the dividends that are declared by the mutual fund, back into the fund itself, at NAV that is prevalent at the time of re-investment. In this option, the number of units held by the investors will change with every re-investment. The value of the units will be similar to that under the dividend option.

The choice of income options depends not only on the investor’s requirements for income and growth, but also on his tax status. The differential tax treatment of dividends and capital gains will also impact the choice made by the investor.

(iv) Products Types Available with Respect to Investment Objectives:

Depending on the investment portfolio that is created, the following are the types of products that are offered by mutual funds.

- Equity Funds
- Debt Funds, and
- Balanced Funds

(a) **EQUITY FUNDS**

Equity funds are those that invest pre-dominantly in equity shares of companies. There are a variety of ways in which an equity portfolio can be created for investors.
There are thus the following choice in equity funds:

- Simple Equity Funds.
- Primary Market Funds.
- Sectoral Funds
- Index Funds,
- Other Equity Funds

**DEBT FUNDS**

Debt funds are those that predominantly invest in debt securities. Since most debt securities pay periodic interest to investors, these funds are also known as income funds. However, it must be remembered that funds investing in debt products can also offer a growth option to their investors. What is important is that the portfolio is predominantly made up of debt securities. The universe of debt securities comprises of long term instruments such as bond issued by central and state governments, public sector organisations, public financial institution and private sector companies and short term instruments such as call money lending' commercial papers, certificates of deposit and treasury bills. Debt funds tend to create a variety of options for investors by choosing one or more of these segments of the debt markets in their investment portfolio:

**BALANCED FUNDS**

Funds that invest both in debt and equity markets are called balanced fund. A typical balanced fund would be almost equally
invested in both the markets. The variations are funds that invest predominantly in equity (about 70%) and keep a smaller part of their portfolios in debt securities. These funds seek to enhance the income potential of their equity component, by bringing in debt. Similarly, there are pre-dominantly debt funds (over 70% in debt securities), which invest in equity, to provide some growth potential to their funds. A balanced fund also tends to provide investors exposure to both equity and debt markets in one product. Therefore, the benefits of diversification get further enhanced, as equity and debt markets have different risk and return portfolios.