Unit-1

Foundations for Finance

Finance:

Finance is defined as the management of money and includes activities such as investing, borrowing, lending, budgeting, saving, and forecasting.

Financial Planning:

Financial Planning is one of the major planning that is required to be conducted by the management. Financial Planning includes all the activities which are related to the procurement of funds, investing those funds, and the return expected from the investment done. Financial Planning also ranges from tax planning which is an important activity.

Meaning of Financial planning:

Financial planning is defined as a document that has records of a business owner or firm's financial situation along with planning on the spending of money to achieve a certain goal by working by a well-devised plan. Financial planning may be made independently or by an experienced planner.

Features

There are a number of features of financial planning that are important for firms and individuals. These are listed below:

- **Foresight:** A plan made without foresight will only result in a disaster. Foresight is needed in planning for estimating risks and the need for liquid and other assets. It may not be 100% accurate but it should be able to give an estimate of the future risks.
- **Flexibility:** A plan made should be flexible as it will help in the future to make adjustments according to the needs.
- **Optimal Usage of Funds:** A financial plan should be able to utilize idle money and assets so that they can prove to be fruitful in the future. It does not involve funds kept aside for unforeseen circumstances but the assets that could be otherwise utilized.
- **Simplicity:** Financial planning should be simple in terms of structure and should be able to provide a sound allocation of resources that can be easily understood even by a layman.
- **Liquidity:** It is also a very important aspect of financial planning which involves keeping current assets in the form of money. This will help in easy allocation and payment of various kinds like salary, fees, and other kinds.

Need for Financial Planning:

Financial Planning is process of framing objectives, policies, procedures, programmes and budgets regarding the financial activities of a concern. This ensures effective and adequate financial and investment policies. The importance can be outlined as-

1. Adequate funds have to be ensured.
2. Financial Planning helps in ensuring a reasonable balance between outflow and inflow of funds so that stability is maintained.
3. Financial Planning ensures that the suppliers of funds are easily investing in companies which exercise financial planning.
4. Financial Planning helps in making growth and expansion programmes which helps in long-run survival of the company.
5. Financial Planning reduces uncertainties with regards to changing market trends which can be faced easily through enough funds.
6. Financial Planning helps in reducing the uncertainties which can be a hindrance to growth of the company. This helps in ensuring stability and profitability in concern.

Financial goals:

A financial goal is a target to aim for when managing your money. **It can involve saving, spending, earning, or even investing.**

Creating a list of financial goals is vital to creating a budget. When you have a clear picture of what you're aiming for, working towards your target is easy. That means that your goals should be measurable, specific, and time-oriented.

Types of Financial Goals

There are several types of financial goals:

1. Short-term goals
2. Mid-term goals
3. Long-term goals

1. **Short-term financial goals:**
   These are smaller financial targets that can be reached within a year. This includes things like a new television, computer, or family vacation.
2. **Mid-term financial goals:**
   Typically, mid-term goals take about five years to achieve. A little more expensive than an everyday goal, they are still achievable with discipline and hard work. Paying off a credit card balance, a loan, or saving for a down payment on a car are all mid-term goals.
3. **Long-term financial goals:**

This type of goal usually takes much more than 5 years to achieve. Some examples of long-term goals are saving for a college education, retirement, or a new home.

Economics:

Economics is the study of scarcity and how it affects the use of resources, the production of goods and services, the growth of production and well-being over time, and many other important and complicated issues that affect society.

Scope of Economics:

Economics deals with a wide variety of things. It comprises multiple principles and theories whose implications influence the economy of a country. When it comes to the scope of economics, it can be understood by the two branches of economics – Microeconomics and Macroeconomics.

Microeconomics:

Microeconomics is concerned with studying the micro elements of the economy of a nation. It deals with the individual units of an economy. Microeconomics studies the concept of product pricing along with the pricing of production factors, and the behaviour of households, individuals, and firms. It enables us to analyse how these units allocate their scarce resources, their distribution, and utilization. The scope of microeconomics includes:

- Demand & Supply
- Production
- Consumption
- Economic welfare

Macroeconomics:

Macroeconomics deals with the macro units of an economy. It is the aggregate study of the elements of a country's economy. Macroeconomics studies the entire economy of a nation as a whole. It deals with the overall production, total consumption, aggregate demand, and aggregate supply of a nation's economy. Unlike microeconomics, macroeconomics deals with individual units on an aggregate basis. The scope of macroeconomics includes:

- National income
- General price level
- Distribution
- Employment

Key concepts influencing decision making both micro and macro:

The micro-business environment is defined as the conditions that have a direct impact on a business. They are related to a specific area of operation in your company and can all business processes. These factors can change the daily proceedings and general performance of a firm. Micro-environment factors include customers, suppliers, resellers, competitors, and the general public.

The macro-environment is a more general situation that touches the whole economy. It impacts the operations of business groups, how they perform, make decisions, and build strategies. It is very dynamic in that businesses must continuously track how it changes and in carries external factors that the company has no control over, but specifically affects it. Such factors include economic factors, demographic forces, technological changes, natural and physical factors, political and legal environments, and social and cultural aspects.

1. **CUSTOMER, SUPPLIERS, AND RESELLERS**

Companies make their marketing decisions based on their target customers. And once they have a customer base, they will make decisions based on how the **customers** react to the product. Be it B2B, B2C, international or local, a business' marketing campaign constantly shifts to meet the demands of their customers. Businesses rely on the stability of demand, prospects of sale growth, relative profitability, and intensity of competition to make these decisions.

The **supplier** of a particular product is the largest and maybe most significant influence on the success of the business. They form a key link between the business and retailer, making the delivery process possible, insurance for necessary resources in your business, and essential determinant for pricing changes and decisions.

The **reseller** is a direct link to the customers. They include middlemen such as wholesalers and retailers. They, too, have a critical part to play in the success of a business. If, for instance, a particular retailer has an excellent reputation, it will be easy for them to pass your product to the consumer. They are crucial for promotion, sale, distribution, marketing, and financial mediation.

2. **COMPETITORS AND THE GENERAL PUBLIC**

Every business that sells a product/service similar to what you are offering is your competition. Hence, their tactics, and sales matter to you. It is therefore vital to look at how their product and prices affect your and make changes appropriately. The main factors to consider in this case include desire competition, a product from the competition, and brand competition.

Again, every business model seeks to impress the general public. Every step they take must be seen for this perspective too. It is very vital to make decisions that consider others because their reactions may be the only thing that pushes you up or drags your brand through mad. Hence, business decisions take note of public opinion, the Media, and environmental pollution.

Banking in India:

The banking industry handles finances in a country including cash and credit. Banks are the institutional bodies that accept deposits and grant credit to entities and play a major role in maintaining the economic stature of a country. Given their importance in the economy, banks are kept under strict regulation in most countries. In India, the Reserve Bank of India (RBI) is the apex banking institution that regulates the monetary policy in the country.

Types of Bank Deposits:

On the basis of purpose they serve, bank deposit accounts may be classified as follows:

- Savings Bank Account
- Current Deposit Account
- Fixed Deposit Account
- Recurring Deposit Account

1. Savings Bank Account:

As the name suggests this type of account is suitable for people who have a definite income and are looking to save money. For example, the people who get salaries or the people who work as laborers. This type of account can be opened with a minimum initial deposit that varies from bank to bank. Money can be deposited at any time in this account.

Withdrawals can be made either by signing a withdrawal form or by issuing a cheque or by using an ATM card. Normally banks put some restriction on the number of withdrawal from this account. Interest is allowed on the balance of deposit in the account. The rate of interest on savings bank account varies from bank to bank and also changes from time to time. A minimum balance has to be maintained in the account as prescribed by the bank.

2. Current deposits Account:

Big businessmen, companies, and institutions such as schools, colleges, and hospitals have to make payment through their bank accounts. Since there are restrictions on the number of withdrawals from a savings bank account, that type of account is not suitable for them. They need to have an account from which withdrawal can be made any number of times.

Banks open a current account for them. Like a savings bank account, this account also requires a certain minimum amount of deposit while opening the account. On this deposit, the bank does not pay any interest on the balances. Rather the account holder pays a certain amount each year as an operational charge.

These accounts also have what we call the overdraft facility. For the convenience of the accountholders banks also allow withdrawal of amounts in excess of the balance of the deposit. This facility is known as an overdraft facility. It is allowed to some specific customers and up to a certain limit subject to previous agreement with the bank concerned.

3. **Fixed Deposit Account:**

Some bank customers may like to put away money for a longer time. Such deposits offer a higher interest rate. If money is deposited in a savings bank account, banks allow a lower rate of interest. Therefore, money is deposited in a fixed deposit account to earn interest at a higher rate.

This type of deposit account allows the deposit to be made of an amount for a specified period. This period of deposit may range from 15 days to three years or more during which no withdrawal is allowed. However, on request, the depositor can encash the amount before its maturity. In that case, banks give lower interest than what was agreed upon. The interest on a fixed deposit account can be withdrawn at certain intervals of time. At the end of the period, the deposit may be withdrawn or renewed for a further period. Banks also grant a loan on the security of the fixed deposit receipt.

4. **Recurring Deposit Account:**

While opening the account a person has to agree to deposit a fixed amount once in a month for a certain period. The total deposit along with the interest therein is payable on maturity. However, the depositor can also be allowed to close the account before its maturity and get back the money along with the interest till that period.

The account can be opened by a person individually, or jointly with another, or by the guardian in the name of a minor. The rate of interest allowed on the deposits is higher than that on a savings bank deposit but lower than the rate allowed on a fixed deposit for the same period.

Deposit Insurance:

Deposit insurance or deposit protection is a measure implemented in many countries to protect bank depositors, in full or in part, from losses caused by a bank's inability to pay its debts when due. Deposit insurance systems are one component of a financial system safety net that promotes financial stability.

Pradhan Mantri Jan Dhan Yojana (PMJDY):

Pradhan Mantri Jan-Dhan Yojana is a government scheme launched by the government of India to provide easy access to financial services such as Remittance, Credit, Insurance, Pension, Savings and Deposit Accounts to poor and needy section of our society.

The scheme was launched in August 2014, and according to the Ministry of Finance, over 4 crore banks accounts have been opened till September 2014.

Under the PMJDY scheme, some of the financial services that are offered to individuals are pension, insurance, and banking.
Under PMJDY zero balance account can be opened by individuals. However, in case individuals would like to have access to the cheque facility, maintenance of a minimum balance is mandatory. No charges will be levied on the individual to open an account under the PMJDY scheme.

How to open a Jan Dhan Yojana Account?

To open a Jan Dhan Yojana Account, you need to get the application form, that is available in both English and Hindi and is available on the official website of PMJDY (**https://www.pmjdy.gov.in/scheme**). Fill it up and submit it along with the necessary documents. The application form is called the financial inclusion account opening form. It consists of three sections where in you need to provide details of yourself, nominee and the bank where the account is being opened.

PMJDY Eligibility

In order for individuals to open a PMJDY account, the below given criteria must be met:

- You must be citizen of India
- You should be at least 10 years of age
- You should not have a bank account

Documents required to open PMJDY account

In case individuals wish to open an account, viable documents must be submitted. The list of documents required for PMJDY account under the scheme are mentioned below:

- Passport
- Permanent Account Number (PAN) Card
- Aadhaar
- The National Rural Employment Guarantee Act (NREGA) issued job card.
- Driving licence
- Voter ID
- Identity card with photo which has been issued by the central or state government departments, public sector undertakings, scheduled commercial banks, public financial institutions and statutory or regulatory authorities.
- A photograph which has been attested along with a letter from a Gazetted officer must be submitted.

Benefits of the PMJDY scheme

Given below are the main benefits of PMJDY scheme:

- Interest is offered on the deposits that are made towards the savings account opened under the scheme.

- Individuals need not maintain a minimum balance under the scheme. However, in case they wish to avail cheque facilities, a minimum balance must be maintained.
- In case individuals maintain the account in a good manner for 6 months, an overdraft facility is provided.
- Individuals receive Accidental Insurance cover of Rs.1 lakh under the RuPay scheme.
- In case the account was opened between 20 August 2014 and 31 January 2015, life cover of Rs.30,000 is provided in case the beneficiary passes away.
- Under the scheme, insurance products and pension access are provided.
- In case individuals are beneficiaries of government schemes, Direct Benefit Transfer option is provided.
- An overdraft facility of Rs.5,000 is provided to one account in the household. The facility is usually provided to the lady in the house.
- The Personal Accident cover can be claimed only after the RuPay Card holder has made a successful non-financial or financial transaction. Transactions made within 90 days of the accident are considered to be PMJDY eligible transactions under the scheme. However, the transaction must be made at an E-COM, POS, ATM, Bank Mitra, bank branch, etc.
- Account holders can check their balance using the mobile banking facility.

Traditional and New Banking Models:

Traditional Banking models:

The traditional banking business model is characterized by four primary activities: revenue streams from traditional banking services, relationship lending, core deposit funding, and ”bricks-and-mortar” street-level branches. Traditional relationship management, which most banks rely on, is a method for maintaining a low cost of funds and a high lending margin.

A characteristic of the traditional banking model is the use of deposits to fund the bank’s asset portfolio. This reduces both funding costs and liquidity risk, because relationship depositors are more likely to maintain their deposit balances even if they are paid below the market interest rate.

Bank branches are an important feature of the traditional banking model. Brick-and-mortar branches help attract new deposit customers, provide a physical location for servicing both loan and deposit customers, and allow bankers to launch and maintain in-person relationships with their customers.

In the traditional banking model, core deposits are the primary source of funding. These are deposits from household and business customers, which makes them ideal for financing the relationship loans made by traditional banks. The stability of these deposits encourages relationships that are beneficial to the bank in at least two additional ways: persistent relationships encourage long depositors to purchase multiple services and products from the bank; and the bank gleans soft information enabling targeted marketing.

New Banking Models:

New Banking models are online only financial technology companies that operate solely digitally or via mobile apps. These banks are digital banks without any physical branches offerings services that traditional banks don't. In India these firms don't have a bank license of their own, but rely on partner banks to offer licensed services as RBI doesn't allow banks to turn 100% digital yet.

Debit and credit cards:

1. **Debit cards:** Debit cards are issued by banks against current or savings account. When the card holder swipes his/her debit card to make a payment or withdrawal money from an ATM, the money is directly deducted from the card holder's account. This could pose a problem during emergencies, in case the account holder does not have sufficient balance in the account.
2. **Credit cards:** A credit card gives the card holder a credit limit from where he/she can borrow funds to make payments as and when required. The cardholder needs to pay back the borrowed amount within a stipulated time, following which the limit is restored. Interest is charged on the outstanding amount only in case of delayed payments.

Digital Payment System:

Digital payments are transactions that take place via digital or online modes, with no physical exchange of money involved. This means that both parties, the payer and the payee, use electronic mediums to exchange money.

The Government of India has been undertaking several measures to promote and encourage digital payments in the country. As part of the '**Digital India**' campaign, the government has an aim to create a 'digitally empowered' economy that is '**Faceless, Paperless, Cashless**'. There are various types and methods of digital payments.

The Bank for International Settlements(BIS) Committee on Payment and Market Infrastructures (CPMI) defines payment systems transactions to include the total transaction undertaken by all payments systems in the country.

Internet Banking:

The Internet banking portal, enables its retail banking customers to operate their accounts from anywhere anytime, removing the restrictions imposed by geography and time. It's a platform that enables the customers to carry out their banking activities from their desktop, aided by the power and convenience of the Internet.

NEFT:

NEFT is an electronic money transfer system that was introduced by the RBI (Reserve Bank of India). The NEFT full form in banking jargon is 'National Electronic Funds Transfer.' It is one of the most secure and fastest mediums used by individuals to transfer money. With this medium, you can send money within just a few minutes. There is no time limitation to using this mode to send cash as it is available 24*7 and 365 days.

Details required for NEFT.

- Name of the account holder to whom you want to send funds
- Account number
- Bank name
- Branch name
- Branch IFSC code
- Amount details

Features and Benefits of NEFT

- It is one of the fastest and most secure methods to transfer money.
- It allows to send money from one account to another within the same bank, as well as between accounts from other banks.
- You can use this method 24*7 and 365 days.
- The amount will be deposited into the beneficiary's account within just a few minutes.
- You can do a transaction just by logging into your net banking account. As a result, your time and effort will be saved.
- It is a paperless facility.

RTGS:

The term real-time gross settlement (RTGS) refers to a funds transfer system that allows for the instantaneous transfer of money and/or securities. RTGS is the continuous process of settling payments on an individual order basis without netting debits with credits across the books of a central bank.

Features and Benefits of RTGS Transactions

The main features and benefits of RTGS transactions are mentioned below:

- Realtime online fund transfer
- Used for high value transactions

- Safe and secure
- Reliable and backed by the RBI
- Immediate clearing
- Funds credited on a one-on-one basis
- Transactions executed on an individual and gross basis

IMPS (Immediate Payment service):

For transferring funds real time and 24X7X365 interbank was a major challenge faced in banking industry. Only NEFT & RTGS were available to user for fund transfer during banking hours.

Immediate Payment Service (IMPS) public launch happened on 22nd November 2010 by Smt. Shyamala Gopinath, DG RBI at Mumbai and this service is now available to the Indian public.

IMPS provides robust & real time fund transfer which offers an instant, 24X7, interbank electronic fund transfer service that could be accessed on multiple channels like Mobile, Internet, ATM, SMS. IMPS is an emphatic service which allow transferring of funds instantly within banks across India which is not only safe but also economical. Currently on IMPS, 677 members are live which includes banks.

Mobile banking:

Mobile banking refers to the use of a mobile device to carry out financial transactions. The service is provided by some financial institutions, especially banks. Mobile banking enables clients and users to carry out various transactions, which may vary depending on the institution.

Importance of Mobile Banking

This digital system is now used by all of us and has a number of benefits. In this section, we will discuss the reasons that add to the importance of mobile banking. Let us get started.

1. **24 x 7 banking services**

This is one of the biggest benefits of mobile banking. As a bank customer, you may have an urgent need for transferring or withdrawing money. This is where digital services like mobile banking play a huge role. There is no need to visit the bank branch, wait in long queues or delay an urgent transaction. You can do that instantly through your mobile phone. You can even do bill payments anytime.

2. **Instant Transactions**

Instant transactions are one of the biggest plus points of this type of banking. If you rely on visiting the bank branch, you will be unable to conduct urgent transactions outside bank hours. You can instantly transfer funds at any time of the day regardless of day and night or bank holidays.

3. **Availability of all banking services**

Through mobile banking, you can avail yourself of almost every banking service. You do not need to visit the bank branch. For instance, you can transfer money, make payments, create an FD in seconds, pay bills and get your bank statements through this service. These features are so easily available that most of us can use them without help.

4. **Breaks the linguistic barrier**

Mobile apps of many financial institutions are available in multiple languages. This makes it easier for most people to perform mobile banking on their own. This reduces any confusion that you would otherwise face. These multilingual banking apps make the country more banking centric as the rural population is also actively using them.

5. **Improved security in Mobile Banking Apps**

These applications tighten security through features like multiple pins, face id, fingerprint lock and multi-factor authentication. Through these security features, your bank accounts become more secure against thefts. In case your phone gets lost or stolen, banks offer the facility to disable the application remotely. Some banks even allow you to share location to detect the location of fraud.

Mobile wallet:

A mobile wallet is a digital wallet that stores payment card information on a mobile device. Mobile wallets are a convenient way for a user to make in-store payments and can be used at merchants listed with the mobile wallet service provider.

AEPS (Aadhar Enabled Payment System):

AePS is a bank led model which allows online interoperable financial inclusion transaction at PoS (MicroATM) through the Business correspondent of any bank using the Aadhaar authentication.

Objectives:

- To sub-serve the goal of Government of India (GoI) and Reserve Bank of India (RBI) in furthering Financial Inclusion.
- To sub-serve the goal of RBI in electronification of retail payments.
- To enable banks to route the Aadhaar initiated interbank transactions through a central switching and clearing agency.
- To facilitate disbursements of Government entitlements like NREGA, Social Security pension, Handicapped Old Age Pension etc. of any Central or State Government bodies, using Aadhaar and authentication thereof as supported by UIDAI.
- To facilitate inter-operability across banks in a safe and secured manner.

- To build the foundation for a full range of Aadhaar enabled Banking services.

UPI (Unified Payment Interface)

Unified Payments Interface (UPI) is a system that powers multiple bank accounts into a single mobile application (of any participating bank), merging several banking features, seamless fund routing & merchant payments into one hood. It also caters to the "Peer to Peer" collect request which can be scheduled and paid as per requirement and convenience.

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