Fund Allocation In Deregulated Regime

Shakti Kumar

Fund Allocation in Deregulated Regime

By
Shakti Kumar

PRATIMA PRAKASHAN
DELHI-110092

FUND ALLOCATION IN DEREGULATED REGIME

(BY SHAKTI KUMAR)

ISBN: 978-93-81713-30-3

Promoted By: Association for Innovtion, India

Publisher: Pratima Prakashan,

R/2, Ramesh Park, Gurudwara Road, Laxmi Nagar, Delhi-110092

Website:www.ijheps.org

Print: 2013

Dedicated to

Rameshwar Ram

My Father,

Preface

==========

Fund is allocated among different financial products to earn. It is invested either in stock market or in bank or in real estate. The present book makes an effort to show that most of the investors invest in debt fund to minimize low risk in India in deregulate regime. Debt fund is able to provide economies to scale benefit to retail investors through minimizing transaction costs and better market accessibility. It pools the retail investor's money which is managed by fund managers to maximize the yields. In this case, the investors do not have to pay transaction and brokerage fees as paid as in demat account. It provides the trained, skilled, well informed professionals who understand the linkages between different markets and its dynamism. Funds manager is able to hedge the portfolios using options and powerful techniques. For the said reasons, Indian banks prefer debt rather to equity fund.

In deregulated regime since 1991, the rate of inflation is high enough to reduce the real return. Throughout the deregulated regime, it shows positive difference between fixed deposit and sensex return suggesting FD scheme to be opted.

Investors have either to invest in equity fund or in debt fund. Risk takers having high income should invest in equity fund and risk averter having fixed and low income should invest in debt fund. Middle income group should take less risk and should invest in debt fund whose expense ratio is low. Middle income group should take less risk and should invest in debt fund whose expense ratio is low.

In such a volatile situation of financial market in the deregulated regime, one has to rethink about the middle income group, middle class and child labour because their economic situation gets affected by liquidity of the economy. Therefore, issues of poverty, child labour and middle class has been included in study.

Most of chapters included in this book have been published in various journals in author's name.

I am thankful to my colleagues teaching in Dr. RML Avadh University, Faizabad, India.

Shakti Kumar

CONTENTS

Chapters ……	Page No.
1. Fixed Deposit and Sensex Returns in Deregulated Regime	7
2. Financial Inclusion of Banking Finance to Agriculture	11
3. Gain from Deregulated Saving Deposit in India	15
4. Deregulated Saving Deposit and Interest Rate Differential	19
5. Monetary Policy and Deregulated Saving Deposit	23
6. Competition and Deregulated Saving Deposit	27
7. Success of Deregulated Saving Deposit in India	31
8. Income Inequality, Expenditure Tax and Poverty Relation	41
9. Legislature and Marginal Group	44
10.Middle Income Group and Debt Fund	48
11. Fund Allocation in Mutual Fund	51
12.Risk and Performance of Mutual Fund	55
13. Debt Fund and Indian Banks	59
14. Law Income and Child Labour in South Asia	64
15. Summary	79

CHAPTER-1

FIXED DEPOSIT AND SENSEX RETURNS IN DEREGULATED REGIME

Investors have options either to invest in fixed income scheme or floating income scheme. Debt fund, fixed deposit, saving deposit, recurring deposit are parts of fixed income scheme while equity, real estate and gold are parts of floating income scheme. The present study makes an effort to compare fixed deposit and sensex returns.

LITERATURE REVIEW

Equity mutual fund is risk adjusted return in which individual fund does not earn higher returns from following the momentum strategy in stock **(Carhart, 1997)** because of investment constraints **(Almazan, 2004).** Restriction on competing products is the reason of the development of money market and short term bond funds **(Klapper, 2000).** Therefore, an investor should invest in small equity fund whose trading activity is high **(Dahlquist, 2000)** or whose expense ratio is low **(Malkiel, 1995) .** Funds that heavily underperform have very high expense ratio, while funds that are successful do not increase revenues by raising their fees but benefit from increased size of their funds **(Elton 1996, Carhat 1997).** Actively managed equity funds charge higher fees than index tracking funds or bond and money market funds, reflecting the higher costs of employing investment management staff to achieve diversification and strategy **(James et al. 1999).** Funds charge lower fees when they have smaller boards and a large proportion of independent directors (**Tufano and Sevick, 1997).** Larger and more mature funds as well as no load funds have lower expense ratio **(Malhotra and Mcleod, 1997).** Aggressive growth funds charge higher entry and exit fees to discourage redemption because they hold more of the smaller, less liquid stocks **(Chordia, 1996).** However, despite the basic academic advice offered to investors to prefer low expense index funds, actively managed funds continue to be popular **(Gruber, 1996).** To decrease the risk it is advised to use derivative. Bond mutual fund uses derivatives more than equity mutual funds. Use of derivative is negatively correlated with fund age and positively correlated with fund size (Johnson **and Yu 2004)** and it is positively correlated

with asset turnover **(Koski and Pontiff, 1999).** Derivatives are used for trading rather than hedging **(Minton et al. 2009).**

METHODOLOGY

Index formula of (P_1 /P_0 *100) has been followed to get the value of the invested money. It has been adjusted with inflation by depreciation the inflated value.

ANALYSIS

Table-1 and figure-1 clearly strengthens the view that return on fixed income scheme is better than that of on floating income scheme.

There are various reasons to choose fixed deposit scheme in the place of equity. **First,** the risk in equity can not be eliminated completely. **Second,** sensex market does not give uniform return on yearly basis. **Third**, investors must have cash ready to be deployed according to market value. **Fourth**, right timing of sensex is unknown to be invested. Therefore, whenever there is market euphoria, equity allocation of the fund should be reduced. **Fifth**, if fund is allocated at over extended valuation in sensex, the return will suffer for a longer period. **Sixth**, if P-E ratio rises, better to sell and if P-E ratio falls ,better to buy equity. However, one should buy stock only when its value is lower than its price.

CONCLUSION

In deregulated regime since 1991, the rate of inflation is high enough to reduce the real return. Throughout the deregulated regime shows positive difference between fixed deposit and sensex return suggesting FD scheme to be opted.

Figure-1: Fixed Deposit and Sensex (Rs.) of Rs. Ten thousand

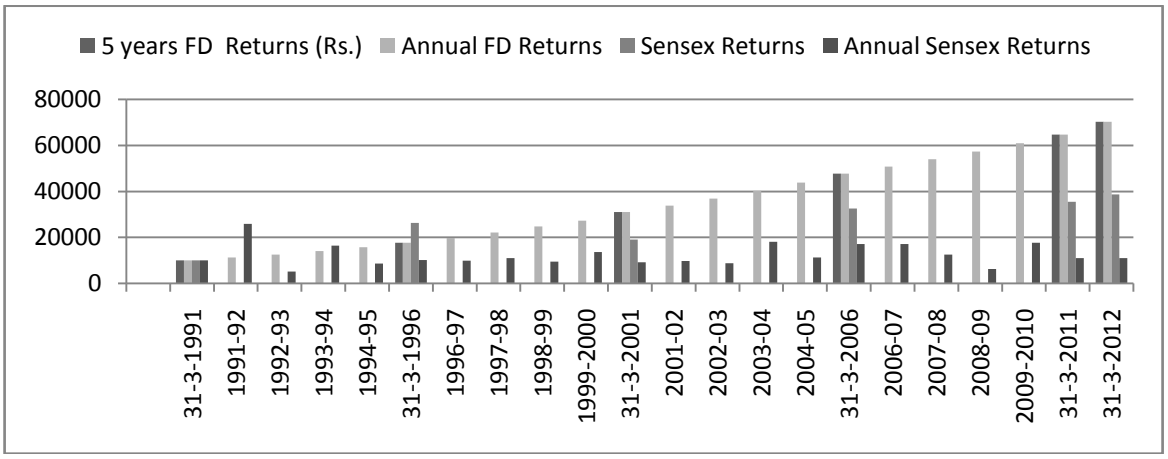


Table-1: Inflation adjusted return from Fixed deposit and Sensex

Year	Inflation (%)	Fixed Deposit Rate (%)	Sensex	Value of Rs. 100000 in FD Scheme (Inflation adjusted)	Value of Rs. 100000 in sensex Scheme (Inflation adjusted)	Difference between FD and Sensex return
1991-92	13.74	12.00	4285	96611.2	86260	10351.2
1992-93	10.06	11.00	2281	111813.4	47877.05	63936.36
1993-94	8.35	10.00	3779	125333.2	80827.39	44505.82
1994-95	12.60	11.00	3261	132668.6	66513.75	66154.84
1995-96	7.99	12.00	3367	156426.3	72298.17	84128.11
1996-97	4.61	11.00-12.00	3361	180822.5	74820.49	106002
1997-98	4.40	10.50-11.00	3893	200701.8	86854.33	113847.4
1998-99	5.95	9.00-11.00	3740	217192.5	82087.98	135104.5
1999-2000	3.27	8.50-9.50	5001	243485.8	112893.1	130592.8
2000-01	7.16	8.50-9.50	3604	254726.5	78085.26	176641.2
2001-02	3.60	7.50-8.50	3469	285653.6	78042.38	207611.3
2002-03	3.41	4.25-6.00	3049	300870.9	68728.8	232142.1
2003-04	5.46	4.00-5.25	5591	307772.5	123354.3	184418.2
2004-05	6.48	5.25-5.50	6493	320816.2	141709.5	179106.7
2005-06	4.36	6.00-6.50	11280	348594.3	251766.4	96827.9
2006-07	6.60	7.50-9.00	13072	368515.3	284929.9	83585.38
2007-08	4.62	8.25-8.75	15644	410197	348220.5	61976.53
2008-09	8.06	8.00-8.75	9702	428517.7	208168.5	220349.2
2009-10	3.81	6.00-7.00	17527	477467.5	393447.4	84020.09
2010-11	9.56	8.25-9.00	19455	487623.1	410620.8	77002.25
2011-12	9.00	9.00	17404	534800.2	369606.5	165193.7

Source: RBI, BSE

REFERENCES

1. **Carhart, M.M., (1997),** "On Persistence in Mutual Fund Performance", J. of Finance, Vol. 52, No. 1, PP-57-82
2. **Almazan A., Keith C.B., (2004),** "Why Constrain Your Mutual Fund Manager?" J. of Financial Economics
3. **Berk J.B. and Green R.C., (2004**), "Mutual Fund Flows and Performance in Rational Markets", J. of Political Economy
4. **Malkiel B.G., (1995),** "Returns from Investing in Equity Mutual Funds ", J. of Finance, 50(2), pp-542-572
5. **Elton E.G., (1996),** "The Persistence of Risk Adjusted Mutual Fund Performance", J. of Business, 69(2), pp-133-157
6. **Dalquist M., Engstroem S. and Soederlind P., (2000),** "Performance and Characteristics of Swedish Mutual Funds", J. of Financial Quantitative Analysis,
7. **Rao K.L.,(2011),** "Analysis of Individual Investors' Behaviour towards Mutual Fund Schemes ", J. of Banking Financial Services and Insurance Research, VOL. 1, Issue-7, 65
8. **Michael J.T., (2009),** "Use of Interest Rate Derivatives by S.S. Based Domestic and Global Bond Mutual Funds", J. of Management Research, Vol. 1(2), 6
9. **James E., Ferrier G. and James S., (2009),** "Mutual Funds and Institutional Investments: What is most efficient ways to to Set up Individual Accounts in a Social Security System", World Bank Policy Research Paper
10. **Tufano P. and Sevick M., (1997), "**Board Structure and Fee Setting in the Us Mutual Fund Industry", Journal of Financial Economics, 46, pp-321-55
11. **Sirri E.R. and Tufano P. , (1993),** " Competition and Change in the Mutual Fund Industry", Financial Series Samuel B. ,Harvard Business School
12. **Chordia T., (1996),** " The Structure of Mutual Fund Charges ", J. of Financial Economics, Vol. 41, pp-3-39

CHAPTER-2

FINANCIAL INCLUSION OF BANKING FINANCE TO AGRICULTURE

There is no labor transfer at required level from agriculture to industry or service sector in India despite being only contributor of positive net factor income from abroad to national income. This dependency on agriculture reflects poverty due to existence of large number of marginal and small farmers. Their financial activities must be included in banking to improve their economic conditions.

LITERATURE REVIEW

The history of Agricultural Credit in India is as old as Manusmriti1 is. Rate of interest was based on Caste of borrower[2] during the period of Manusmriti. The study of Ray Chaudhuri and Habib reveals that specialized Caste groups dealt with a particular aspect of Banking Finance during Manusmriti period.

Usuary played an important role in village economy. "Right from the beginning of **feudalism Usuary** had a significant role in village economy.[4] The study by Balbinder Singh (2000) shows that **Rautas** mortgaged lands against loans with **Ranka during Muhammad Jalaludin Khalji's period**. During**, Akbar period** people borrowed to meet the revenue demand from moneylenders**.**[5] During the **Moughal period** itself, a specific characteristic of Credit was popular, that was **Hundi** which is still popular. Hundi system plays a role of bill of exchange including discount rates, insurance charges and transmission cost of money.[6] The rate of interest during this period was very high.

The Zamindari, Mahalwari and Ryotwari in non-specified form were popular in Moughal period. The peasants were enforced to pay the interest rate even in drought season by selling the grass. Balbinder Singh in his study has recognized the exploitation of peasants by moneylenders and Zamindars.[7] Peasants borrowed from merchants, retainers, Zamindars and moneylenders even at the rate of 150.00 per cent per annum[8] because they had no alternate revenue to survive. Here Balbinder Singh says that borrowing at high interest rate shows low credit and bargaining powers of debtors.

The Banking Finance system was popular even during **British period.** In fact, Britishers started expansioning their business even in rural areas which linked traders with landlords and peasants.[9] High shares to Britishers in agricultural production and unbearable interest, charged by moneylenders gave birth of **Sahukar, Bania and Mahajan** who became the source of credit for cultivators.[10]The emergence of Banking Financers and sub Banking Financers developed capitalist agricultural class on whom peasants were dependent. This was the root cause of peasant's exploitation. The right of property and transferability of land did the farmers no good and the land gradually began to pass from the cultivators to moneylenders[11]. Despite the prohibition of land to non-farming Castes, lands were transferred to moneylenders.[12]

OBJECTIVE

To know, why financial inclusion should be extended to agriculture in banking finance?.

METHODOLOGY

Both the primary and secondary sources of data have been used to meet the objective.

ANALYSIS

Finance made available by banks to agriculture or industry or service sector is banking finance. The contribution of industry and service sectors in national income of India has been increasing over the period but that of agricultural sector is decreasing. Even two-third of total population is still dependent on agriculture for livelihood. It shows that most of the agricultural products are being consumed by producers whose Business Farm Income (BFI) is much lower than people engaged in industry and service sector. Financial inclusion should be extended to agriculture in banking finance to enhance their **BFI**.

It is only the agricultural sector which has been contributing positive net factor income (NFI) from abroad to India since its independence except 1969-70. Industry and service sectors have been contributing negative (NFI) throughout the period since 1951. Financial inclusion should be extended to agriculture in banking finance to enhance their **NFI**.

All three sectors are interlinked in both the backward and forward process of production system. Financial inclusion should be extended to agriculture in banking finance to strengthen their **linkages** to enhance productivity.

People engaged in agricultural sector are the part and parcel of Indian nationals and therefore they should feel their participation in the economic growth of India. It is only possible when they shall be included in the banking activities especially in banking finance. Financial inclusion should be extended to agriculture in banking finance to strengthen their **patriotism feelings and contribution in economic growth of the nation.**

Small savings by big number of people generate large volume of money to be invested. Agricultural sector in India is the hub of the small savings. It needs to be channelized which is only possible through their financial inclusion. Therefore**, f**inancial inclusion should be extended to agriculture in banking finance to collect **small savings** to be invested.

A number of financial products are popular in these days. Their penetration in rural areas is required to maintain credit cycle in the agricultural sector. Use of these financial products in the agricultural sector will generate financial awareness and liquidity on demand. Therefore, financial inclusion should be extended to agriculture in banking finance to avail **liquidity on demand.**

Banking finance is required to save peasants from exploitation made by landlords, debt trap and non-productive credit**.** Financial inclusion should be extended to agriculture in banking finance to **save peasants from exploitation.**

Two-third of Indian population is living in agro-based rural areas. They play major roles in money circulation, monetary policy and hence liquidity in the economy. These factors affect the inflation. Therefore**, f**inancial inclusion should be extended to agriculture in banking finance to **control inflation.**

CONCLUSION

Financial inclusion should be extended to agriculture in banking finance to increase business farm income, to earn more net factor income from abroad, to decrease poverty, to provide liquidity on demand, save peasants from exploitation, to control inflation, to generate their feelings and contribution in economic growth of the nation and to collect small savings.

REFERENCES

1. First written Codification of Indian Society by Manu
2. Singh Balwinder (2000), " Agricultural Credit : Sources, Problems and Emerging Issues". , p-2
3. Raychaudhury T. and Habib I. (1984), " Cambridge Economic History of India", Vol. 1, p-345
4. Ghosh A. (1988), " Emerging Capitalism in Indian Agriculture", p-248
5. Raychaudhury T. and Habib I. (1984), " Cambridge Economic History of India", Vol. 1, p-248
6. Raychaudhury T. and Habib I. (1984), " Cambridge Economic History of India", Vol. 1, p-346
7. Raychaudhury T. and Habib I. (1984), " Cambridge Economic History of India", Vol. 1, p-342
8. Raychaudhury T. and Habib I. (1984), " Cambridge Economic History of India", Vol. 1, p-348
9. Ghosh A. (1988), " Emerging Capitalism in Indian Agriculture", p-279
10. Ghosh A. (1988), " Emerging Capitalism in Indian Agriculture", p-292
11. Maheshwari B.P. (1971), " Industrial and Agricultural Development in India", p-5
12. Ulyanovsky R. (1981), " Agrarian India between the world wars, progress Publishers, Moscow, p-41

CHAPTER-3

GAIN FROM DEREGULATED SAVING DEPOSIT IN INDIA

Deregulation raises the level of competition in which price of product depends on market situation. The saving account deposit may be regarded as oligopolistic market in Indian economy. There are three major players in the Indian economy to affect the circulation of money-RBI, banks and account holders. Former player uses monetary policy rates (i.e. CRR, OMO, SLR, Bank rate, Repo rate and Reverse repo rate) to achieve the desired level of money circulation. Banks use lending and deposit rates to get desired amount of liquidity from the account holders. These are the account holders who keep money in the either types of banks account (i.e. current, saving, recurring or tem deposit). Deregulation of all lending rates has been completed in July 2010 when Benchmark Prime Lending Rate (BPLR) was replaced by Base Rate System (BRS). Deregulation of deposit rates on all types of account has been completed on November 2011. The deregulation of saving account deposit, which was fixed at 3.0 Per cent since 2003, was completed in November 2011. Money deposited in Saving Bank Account in India is a short run subject, liability to banks, repayable on demand, one-fourth of total deposit, Household dominated (83.6 per cent) and Rural fragranced (36.2 per cent).

LITERATURE REVIEW

Chong (2010) says that deregulation of interest rate on saving account deposit increases the efficacy of monetary policy by improving the correlation between retail bank deposit rates and market interest rates and increasing the degree of long-term pass-through for retail bank deposit rates. **Stigler (2010)** shows that deregulation means state's withdrawal of its legal power to direct the economic conducts (pricing, entry and exit) of non-governmental bodies. **Guo and Diaye (2010)** find that an increase in real interest rate raises the level of consumption. **Feyzioglu (2009)** finds that households may move deposit out of the banks to earn higher returns if given more choice regarding saving options. Greater flexibility and choice for household portfolio allocation will exert more competitive pressure on banks. **Geng and Diaye (2011)** say that with the greater flexibility

and choice over saving vehicles, households will be able to achieve a more efficient allocation of saving and extract higher returns from their portfolio. Increases in financial rate of returns contribute to a decline in the share of household disposable income that is saved.

OBJECTIVES

To know whether the real interest rate (RIR) given to Saving Account Holders (SAH) is negative.

METHODOLOGY

Real interest rate (RIR) will be calculated by deducting annual inflation rate from interest rate given on SAD.

ANALYSIS

Saving account deposit rate was almost fixed at 3.5 per cent in the regulated regime up to November 2011. Gain to consumer in real term is negative as shown as in table-1 and figure-1 because the inflation rate is more than the interest rate given to saving account holders. Banks pay low interest rate on saving account deposit because (i) it is repayable on demand; (ii) it is short term subject with liability for bankers (iii) bankers are unable to know its core deposits (iv) Saving deposit bears transaction and facility cost. Account holders need to be given higher interest rate because (i) amount in saving account is deposited not for transaction but for saving purpose (ii) only 20.00 per cent of total amount deposited in saving account is demanded and rest is left to lend (iii) Banks earn interest on 80.00 per cent of total amount deposited in saving account. In such a demand and supply situation, if inflation rate is taken into consideration, the real gain to account holders becomes negative. It is so because of regulated regime in which households are asked either to deposit or leave. It **discourages small savings** and it is in against the **financial inclusion** of poor households especially in rural areas. Therefore, it is suggested to deregulate the interest rate to enhance the real gain to consumer by improving the level of competitions among banks.

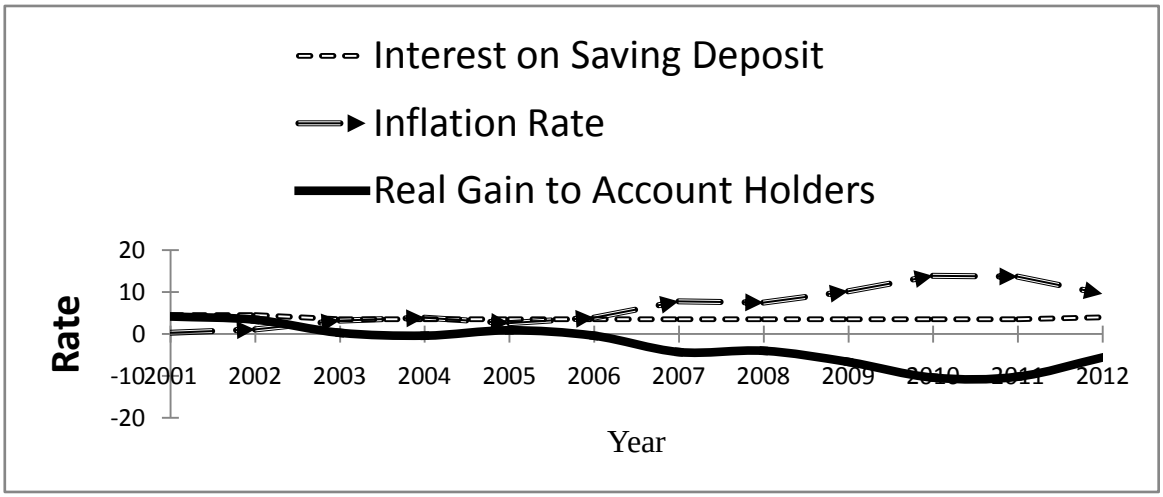
Table-1: Real interest rate on saving account deposit given to account Holders

Year	Interest rate on Saving Deposit (%)	Annual Inflation rate (%)	Real Interest rate (%)
March 2001	4.5	0.3	4.2
March 2002	4.5	1.1	3.4
March 2003	3.5	3.2	0.3
March 2004	3.5	3.9	- 0.4
March 2005	3.5	2.6	0.9
March 2006	3.5	3.9	- 0.4
March 2007	3.5	7.8	- 4.3
March 2008	3.5	7.5	- 4.0
March 2009	3.5	10.2	-6.7
March 2010	3.5	13.9	- 10.4
March 2011	3.5	13.7	- 10.2
March 2012	4.0	9.6	- 5.6

Note: Annual inflation rate is based on Consumer Price Index of Agricultural Labour with 1986-87 = 100

Source: (1) Statistical Tables Relating to Banks in India, RBI, Various Issues and (2) Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

Figure-1: Real Gain to Saving Account Deposit Holders in India



CONCLUSION

If inflation rate is taken into consideration, the real gain to account holders becomes negative. It is so because of regulated regime in which households are asked either to deposit or leave. It **discourages small savings** and it is in against the **financial inclusion** of poor households especially in rural areas. Therefore, it is suggested to deregulate the interest rate to enhance the real gain to consumer by improving the level of competitions among banks.

REFERENCES

1. **Chong, Ben Soon (2010),** "Interest Rate Deregulation: Monetary Policy Efficacy and Rate Rigidity," Journal of Banking & Finance, Vol. 34, Issue 6, June, Page: 1299-1307
2. **Feyzioglu T., Potter N. and Takats E. (2009),** "Interest rate Liberalisation in China", IMF Working Paper 09/ 171
3. **Geng N. and Diaye P.N. (2011),** "Determinants of Corporate Investment in China: Evidence from Cross Country Firm – Level Dta", IMF Working Paper
4. **Guo K. and Diaye P.N. (2010)** "Determinats of China's Private Consumption: An International Perspective", IMF Working paper, 10/93
5. **Stigler (2010),** Journal of Economic Literature, Vol. 31, pp-1263-1279

CHAPTER-4

DEREGULATED SAVING DEPOSIT AND INTEREST RATE DIFFERENTIAL

The saving account deposit may be regarded as oligopolistic market in Indian economy. There are three major players in the Indian economy to affect the circulation of money-RBI, banks and account holders. Former player uses monetary policy rates (i.e. CRR, OMO, SLR, Bank rate, Repo rate and Reverse repo rate) to achieve the desired level of money circulation. Banks use lending and deposit rates to get desired amount of liquidity from the account holders. These are the account holders who keep money in the either types of banks account (i.e. current, saving, recurring or tem deposit). The deregulation of saving account deposit, which was fixed at 3.0 Per cent since 2003, was completed in November 2011.

LITERATURE REVIEW

Chong (2010) says that deregulation of interest rate on saving account deposit increases the efficacy of monetary policy by improving the correlation between retail bank deposit rates and market interest rates and increasing the degree of long-term pass-through for retail bank deposit rates. **Stigler (2010)** shows that deregulation means state's withdrawal of its legal power to direct the economic conducts (pricing, entry and exit) of non-governmental bodies. **Feyzioglu (2009)** finds that households may move deposit out of the banks to earn higher returns if given more choice regarding saving options. Greater flexibility and choice for household portfolio allocation will exert more competitive pressure on banks. **Lardy and Douglas (2011)** say that interest rate liberalization must precede capital account liberalization to lower the risk of households transferring their deposits out of the banks and undermining the stability of the domestic banking system**. Geng and Diaye (2011)** say that with the greater flexibility and choice over saving vehicles, households will be able to achieve a more efficient allocation of saving and extract higher returns from their portfolio. Increases in financial rate of returns contribute to a decline in the share of household disposable income that is saved.

OBJECTIVES

To know the responses of Saving Account Deposit to interest rate differential (IRD).

METHODOLOGY

Interest rate differential will be calculated by deducting rate of interest on SAD from interest rate given on term deposit.

ANALYSIS

The amount deposited in the saving account responses to interest rate differential. It suggests that there is scope to enhance interest rate given on saving account deposit. Table-1 and figure-1 show that the share of saving account deposit in total deposit is inversely related with interest rate differential. It suggests that **widening of IRD leads to reduction in the share of SAD in total deposit**. It shows that amount of saving deposit responses the interest rate given on SAD. One can reveal that account holders deposit in **SAD** for the purpose of saving not for the purpose of transaction. Therefore it may be suggested that SAD may be treated as well as **TAD** (term account deposit) to attract saving by raising interest rate on SAD in deregulated regime. Since there is $\mathbf{r_{SAD}} < \mathbf{r_{TAD}}$ and $\mathbf{b_{SAD}} < \mathbf{b_{TAD}}$ **,** shows that SAD is less elastic than TAD and hence monetary policy can be penetrated in better ways with SAD rather than TAD.

Figure-1: Responsiveness of Amount of Saving Account Deposit to Interest Rate Differential (IRD)

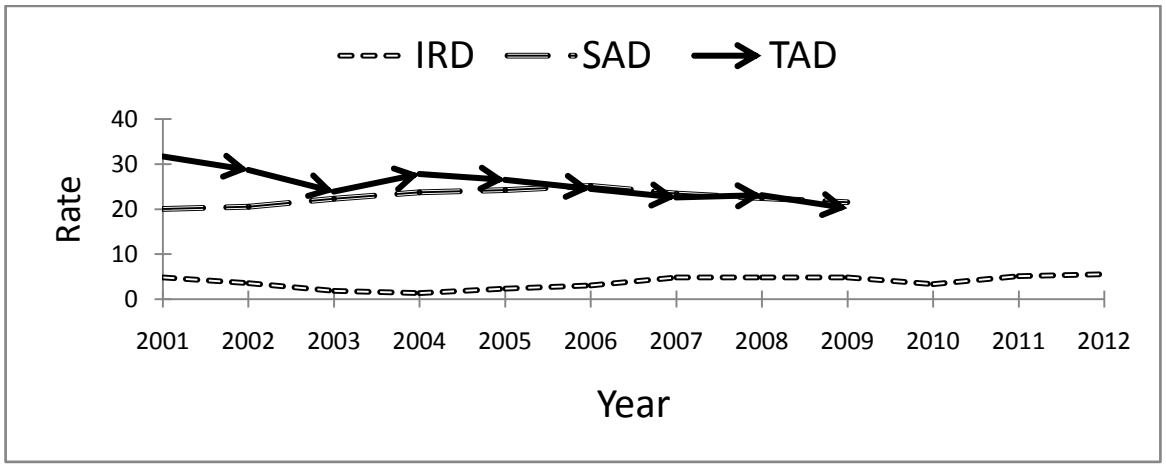


Table-1: Interest rate differential and share of SAD in total deposit in India

Year	Interest rate on Saving Deposit (%)	Interest rate on Term Deposit (%)	IRD (%)	Share in total deposit			
				Saving Deposit (%)	Term Deposit (%)	Other Deposit (%)	Total Deposit (%)
2001	4.5	9.3	4.8	20.0	31.7	48.3	100
2002	4.5	8.0	3.5	20.5	28.7	50.8	100
2003	3.5	5.3	1.8	22.3	23.9	53.8	100
2004	3.5	4.8	1.3	23.7	27.8	48.5	100
2005	3.5	5.8	2.3	24.2	26.5	49.3	100
2006	3.5	6.5	3.0	25.1	24.5	50.4	100
2007	3.5	8.3	4.8	23.4	22.6	54	100
2008	3.5	8.3	4.8	22.4	23.1	54.5	100
2009	3.5	8.3	4.8	21.5	20.2	58.3	100
2010	3.5	6.8	3.3	-	-	-	-
2011	3.5	8.6	5.1	-	-	-	-
2012	4.0	9.5	5.5	-	-	-	---
Correlation Co-efficient (r) with IRD	0.20623	0.950196					

Source: (1) Statistical Tables Relating to Banks in India, RBI, Various Issues and (2) Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

REGRESSION ANALYSIS

SAD share = 24.51 – 0.5644 IRD --- $R^2 = 0.222$, F = 2.00,

TAD share = 27.32 – 0.564 IRD …$R^2 = 0.04$, F = 0.348

$r_{SAD} < r_{TAD}$ and $b_{SAD} < b_{TAD}$

CONCLUSION

The share of saving account deposit in total deposit is inversely related with interest rate differential. It suggests that **widening of IRD leads to reduction in the share of SAD in total deposit**. It shows that amount of saving deposit responses the interest rate given on SAD. SAD is less elastic than TAD and hence monetary policy can be penetrated in better ways with SAD rather than TAD.

REFERENCES

1. **Chong, Ben Soon (2010**), "Interest Rate Deregulation: Monetary Policy Efficacy and Rate Rigidity," Journal of Banking & Finance, Vol. 34, Issue 6, June, Page: 1299-1307
2. **Feyzioglu T., Potter N. and Takats E. (2009),** "Interest rate Liberalisation in China", IMF Working Paper 09/ 171
3. **Geng N. and Diaye P.N. (2011),** "Determinants of Corporate Investment in China: Evidence from Cross Country Firm – Level Dta", IMF Working Paper
4. **Guo K. and Diaye P.N. (2010)** "Determinats of China's Private Consumption: An International Perspective", IMF Working paper, 10/93
5. **Stigler (2010),** Journal of Economic Literature, Vol. 31, pp-1263-1279
6. **Strahan P.E. (2002) "The** Real Effect of U.S. Banking Deregulation", Journal of Economics, Vol. 101, pp-639-70
7. **Lardy N. and Douglas P. (2011), "**Capital Account Liberalisation", PIIE Working Paper-11-6

CHAPTER-5

MONETARY POLICY IN THE REGIME OF DEREGULATED SAVING DEPOSIT

The saving account deposit may be regarded as oligopolistic market in Indian economy. There are three major players in the Indian economy to affect the circulation of money-RBI, banks and account holders. Former player uses monetary policy rates (i.e. CRR, OMO, SLR, Bank rate, Repo rate and Reverse repo rate) to achieve the desired level of money circulation. But it depends on elasticity of saving deposit. This elasticity gets affected by deregulation of interest rate. The deregulation of saving account deposit, which was fixed at 3.0 Per cent since 2003, was completed in November 2011. Money deposited in Saving Bank Account in India is a short run subject, liability to banks, repayable on demand, one-fourth of total deposit, Household dominated (83.6 per cent) and Rural fragranced (36.2 per cent).

LITERATURE REVIEW

Chong (2010) says that deregulation of interest rate on saving account deposit increases the efficacy of monetary policy by improving the correlation between retail bank deposit rates and market interest rates and increasing the degree of long-term pass-through for retail bank deposit rates. **Glower (2009)** says that many countries of South Asia like Singapore, Philippines, Indonesia, Sri Lanka, Malaysia, Thailand and Republic of Korea have been successfully experienced with interest rate deregulation to support economic development. **Ojo** (1988) finds that deregulation in oligopolistic financial market increases lending rate to increase cost of capital to discourage investment. **Kwan (2003**) study shows that banks earn rents from deposit interest rate rules and deregulation will lower both the rent and bank market value. **Humphrey (1997)** suggests that deregulation raises bank funding costs and lowers profits. In response, a bank raise fees for deposit services, reduces branch operating cost and shifts to higher earning assets. **Strahan (2002)** finds that deregulation of restrictions on branching reduces the sensitivity of state economies to shocks to their own banks' capital. **Stigler (2010)** shows that deregulation means state's withdrawal

of its legal power to direct the economic conducts (pricing, entry and exit) of non-governmental bodies. **Guo and Diaye (2010)** find that an increase in real interest rate raises the level of consumption. **Feyzioglu (2009)** finds that households may move deposit out of the banks to earn higher returns if given more choice regarding saving options. Greater flexibility and choice for household portfolio allocation will exert more competitive pressure on banks. **Lardy and Douglas (2011)** say that interest rate liberalization must precede capital account liberalization to lower the risk of households transferring their deposits out of the banks and undermining the stability of the domestic banking system**. Geng and Diaye (2011)** say that with the greater flexibility and choice over saving vehicles, households will be able to achieve a more efficient allocation of saving and extract higher returns from their portfolio. Increases in financial rate of returns contribute to a decline in the share of household disposable income that is saved. **Obamuyi (2009)** says that behavior of interest rate is important for economic growth in view of the relationships between interest rates and investment and investment & growth. Literature review is unable to place the study showing how the level of competition will be enhanced by deregulating saving account deposit rate in India. Therefore, the relevance of the present study is very high.

OBJECTIVES

To know the elasticity of saving Account Deposit (SAD) rate with respect to lending rate to know whether the monetary policy be implemented effectively through SAD.

METHODOLOGY

The elasticity of SAD and TAD rate w.r.t. lending rate will be calculated with the help of correlation co-efficient. If the correlation co-efficient between interest rate on TAD and lending rate becomes more than the correlation co-efficient between interest rate on SAD and lending rate , it can be said that monetary policy is effective more with SAD not with TAD.

ANALYSIS

The central bank with the help of policy rates such as Repo rate, Reverse Repo rate, CRR, SLR, OMO, Call rate etc. tries to control lending rate through which monetary policy is transmitted. This lending rate is associated with the rate given on saving account deposit. Table-1 shows that correlation co-efficient between interest rate on saving deposit (SAD)

and ARL is less than that of TAD. Therefore, it is suggested that monetary policy can be transmitted in better ways with SAD because it is less elastic.

CONCLUSION

Deregulation of interest rate on saving account deposit increases the efficacy of monetary policy. Correlation co-efficient between interest rate on saving deposit (SAD) and ARL is less than that of TAD. Therefore, it is suggested that monetary policy can be transmitted in better ways with SAD because it is less elastic.

Table-1: Transmission of monetary policy through Lending rate over SAD and TAD

Year	**Interest rate on SAD (%)**	**Interest rate on TAD (%)**	Average Lending rate (ALR) (%)
2001	4.5	9.3	11.50
2002	4.5	8.0	11.50
2003	3.5	5.3	10.75
2004	3.5	4.8	10.25
2005	3.5	5.8	10.25
2006	3.5	6.5	10.25
2007	3.5	8.3	12.25
2008	3.5	8.3	12.25
2009	3.5	8.3	12.25
2010	3.5	6.8	11.75
2011	3.5	8.6	8.25
2012	4.0	9.5	9.50
Correlation Co-efficient with ALR	**r_{SAD} = 0.093641**	**r_{TAD}= 0.0995**	-

Source: (1) Statistical Tables Relating to Banks in India, RBI, Various Issues and (2) Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

REFERENCES

1. **Chong, Ben Soon (2010),** "Interest Rate Deregulation: Monetary Policy Efficacy and Rate Rigidity," Journal of Banking & Finance, Vol. 34, Issue 6, June, Page: 1299-1307
2. **Feyzioglu T., Potter N. and Takats E. (2009),** "Interest rate Liberalisation in China", IMF Working Paper 09/ 171
3. **Geng N. and Diaye P.N. (2011),** "Determinants of Corporate Investment in China: Evidence from Cross Country Firm – Level Dta", IMF Working Paper
4. **Glower, Carlos J. (1994),** "Interest Rate Deregulation: A Brief Survey of the Policy Issues and the Asian Experience", Asian Development Bank, Occasional Papers, July
5. **Guo K. and Diaye P.N. (2010)** "Determinats of China's Private Consumption: An International Perspective", IMF Working paper, 10/93
6. **Humphrey D.B. and Pulley L.B. (1997),** "Bank's Response to Deregulation: Profits, Technology and Efficiency", Journal of Money, Credit and Banking, Vol. 29, pp-73-93
7. **Kwan S.H.(2003) ,** " Impact of Deposit Rate Deregulation in Hong Kong on the market value of Commercial banks ", Journal of Banking and Finance, Vol. 27, pp-2231-2248
8. **Lardy N. and Douglas P. (2011),** "Capital Account Liberalisation", PIIE Working Paper-11-6
9. **Obamuyi T.M. (2009**), Journal of Economics and International Finance, Vol. 1(4), pp-93-98
10. **Ojo M.O.(1988),** " Agricultural Performance and Policy Structural Adjustment Programme in Nigeria", Conference Paper presented in Annual Conference of the Nigerian Economic Society at Obafemi Awolowo University, Nigeria
11. **Stigler (2010),** Journal of Economic Literature, Vol. 31, pp-1263-1279
12. **Strahan P.E. (2002)** "The Real Effect of U.S. Banking Deregulation", Journal of Economics, Vol. 101, pp-639-70

CHAPTER-6

COMPETITION AND DEREGULATION OF SAVING ACCOUNT DEPOSIT

Deregulation raises the level of competition in which price of product depends on market situation. The saving account deposit may be regarded as oligopolistic market in Indian economy.

LITERATURE REVIEW

Chong (2010) says that deregulation of interest rate on saving account deposit increases the efficacy of monetary policy by improving the correlation between retail bank deposit rates and market interest rates and increasing the degree of long-term pass-through for retail bank deposit rates. **Glower (2009)** says that many countries of South Asia like Singapore, Philippines, Indonesia, Sri Lanka, Malaysia, Thailand and Republic of Korea have been successfully experienced with interest rate deregulation to support economic development. Ojo (1988) finds that deregulation in oligopolistic financial market increases lending rate to increase cost of capital to discourage investment. **Kwan (2003**) study shows that banks earn rents from deposit interest rate rules and deregulation will lower both the rent and bank market value. **Strahan (2002)** finds that deregulation of restrictions on branching reduces the sensitivity of state economies to shocks to their own banks' capital. **Stigler (2010)** shows that deregulation means state's withdrawal of its legal power to direct the economic conducts (pricing, entry and exit) of non-governmental bodies. **Guo and Diaye (2010)** find that an increase in real interest rate raises the level of consumption. **Feyzioglu (2009)** finds that households may move deposit out of the banks to earn higher returns if given more choice regarding saving options. Greater flexibility and choice for household portfolio allocation will exert more competitive pressure on banks. **Lardy and Douglas (2011)** say that interest rate liberalization must precede capital account liberalization to lower the risk of households transferring their deposits out of the banks and undermining the stability of the domestic banking system**. Geng and Diaye (2011)** say that with the greater flexibility and choice over saving vehicles, households will be able to achieve a more efficient allocation of saving and extract higher returns from their portfolio. Increases in financial rate of returns contribute to a decline in the share of household

disposable income that is saved. **Obamuyi (2009)** says that behavior of interest rate is important for economic growth in view of the relationships between interest rates and investment and investment & growth. Literature review is unable to place the study showing how the level of competition will be enhanced by deregulating saving account deposit rate in India. Therefore, the relevance of the present study is very high.

OBJECTIVES

To Assess Competition Level in the Regime of Deregulation of Saving Account Deposit Rate in India.

METHODOLOGY

To know the competition level, the Spread Rate (difference between rate of interest on saving account and policy rate) will be calculated. Higher the Spread rate, more the healthy competition.

ANALYSIS

The level of competition is directly associated with the spread rate. This rate is higher in the case of TAD (Time Account Deposit) than SAD(Saving Account Deposit). In most of the cases the spread rate in SAD is negative as shown as in table-1 and figure-1. The spread rate in TAD is high because it has been deregulate since 1997. Therefore it is suggested that competition level among banks can be raised by raising the spread rate in SAD over both the Repo and Reverse Repo rate.

Figure-1: Spread Rate of Term and Saving Account Deposit

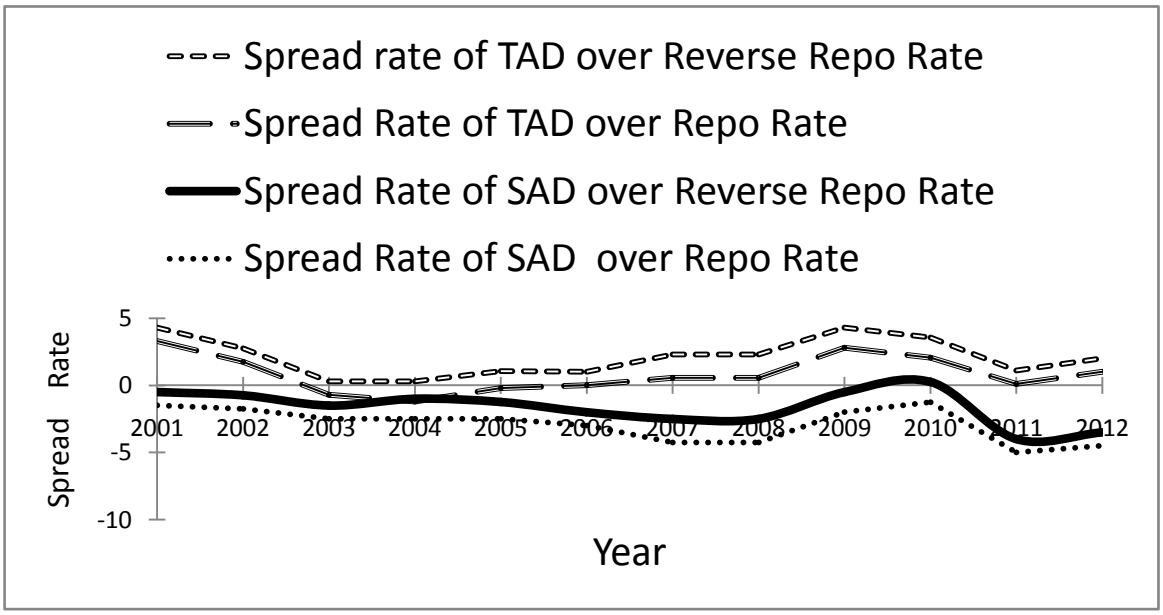


Table-1: Table-4: Spread rate to know the level of competition in India

Year	Interest rate on Saving Deposit (%) (1)	Interest rate on Term Deposit (%) (2)	Reverse Repo Rate (**RRR**) (%) (3)	Repo Rate (**RR**) (%) (4)	**Spread Rate** (%)			
					TAD over (RRR) (2-3)	TAD over (RR) (2-4)	SAD over (RRR) (1-3)	SAD over (RR) (1-4)
2001	4.5	9.3	5.0	6.0	4.3	3.3	-0.5	-1.5
2002	4.5	8.0	5.25	6.25	2.75	1.75	-0.75	-1.75
2003	3.5	5.3	5.0	6.0	0.3	-0.7	-1.5	-2.5
2004	3.5	4.8	4.5	6.0	0.3	-1.2	-1	-2.5
2005	3.5	5.8	4.75	6.0	1.05	-0.2	-1.25	-2.5
2006	3.5	6.5	5.5	6.5	1	0	-2	-3
2007	3.5	8.3	6.0	7.75	2.3	0.55	-2.5	-4.25
2008	3.5	8.3	6.0	7.75	2.3	0.55	-2.5	-4.25
2009	3.5	8.3	4.0	5.5	4.3	2.8	-0.5	-2
2010	3.5	6.8	3.25	4.75	3.55	2.05	0.25	-1.25
2011	3.5	8.6	7.5	8.50	1.1	0.1	-4	-5
2012	4.0	9.5	7.50	8.50	2	1	-3.5	-4.5

Source: Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

CONCLUSION

The level of competition is directly associated with the spread rate. In most of the cases the spread rate in SAD in India is negative as shown as in table-1 and figure-1. Therefore it is suggested that competition level among banks can be raised by raising the spread rate in SAD over both the Repo and Reverse Repo rate.

REFERENCES

1. **Chong, Ben Soon (2010),** "Interest Rate Deregulation: Monetary Policy Efficacy and Rate Rigidity," Journal of Banking & Finance, Vol. 34, Issue 6, June, Page: 1299-1307
2. **Feyzioglu T., Potter N. and Takats E. (2009),** "Interest rate Liberalisation in China", IMF Working Paper 09/ 171
3. **Geng N. and Diaye P.N. (2011),** "Determinants of Corporate Investment in China: Evidence from Cross Country Firm – Level Dta", IMF Working Paper
4. **Glower, Carlos J. (1994),** "Interest Rate Deregulation: A Brief Survey of the Policy Issues and the Asian Experience", Asian Development Bank, Occasional Papers, July
5. **Guo K. and Diaye P.N. (2010)** "Determinants of China's Private Consumption: An International Perspective", IMF Working paper, 10/93
6. **Kwan S.H.(2003)** , " Impact of Deposit Rate Deregulation in Hong Kong on the market value of Commercial banks ", Journal of Banking and Finance, Vol. 27, pp-2231-2248
7. Lardy N. and Douglas P. (2011), "Capital Account Liberalisation", PIIE Working Paper-11-6
8. **Obamuyi T.M. (2009),** Journal of Economics and International Finance, Vol. 1(4), pp-93-98
9. **Ojo M.O.(1988),** " Agricultural Performance and Policy Structural Adjustment Programme in Nigeria", Conference Paper presented in Annual Conference of the Nigerian Economic Society at Obafemi Awolowo University, Nigeria
10. **Stigler (2010),** Journal of Economic Literature, Vol. 31, pp-1263-1279
11. **Strahan P.E. (2002)** "The Real Effect of U.S. Banking Deregulation", Journal of Economics, Vol. 101, pp-639-70

CHAPTER-7

SUCCESS OF DEREGULATED SAVING DEPOSIT IN INDIA

There are three major players making monetary policy successful-RBI, banks and account holders. Former player uses monetary policy rates (i.e. CRR, OMO, SLR, Bank rate, Repo rate and Reverse repo rate) to achieve the desired level of money circulation. These are the account holders who keep money in the either types of banks account (i.e. current, saving, recurring or tem deposit). The success of monetary policy depends on real gain to account holder, responsiveness of saving deposit to interest rate differentia, elasticity and the level of competition in the era of deregulated deposit rate.

Deregulation of all lending rates has been completed in July 2010 when Benchmark Prime Lending Rate (BPLR) was replaced by Base Rate System (BRS). Deregulation of deposit rates on all types of account has been completed on November 2011. The deregulation of saving account deposit, which was fixed at 3.0 Per cent since 2003, was completed in November 2011. Money deposited in Saving Bank Account in India is a short run subject, liability to banks, repayable on demand, one-fourth of total deposit, Household dominated (83.6 per cent) and Rural fragranced (36.2 per cent).

LITERATURE REVIEW

Chong (2010) says that deregulation of interest rate on saving account deposit increases the efficacy of monetary policy by improving the correlation between retail bank deposit rates and market interest rates and increasing the degree of long-term pass-through for retail bank deposit rates. **Glower (2009)** says that many countries of South Asia like Singapore, Philippines, Indonesia, Sri Lanka, Malaysia, Thailand and Republic of Korea have been successfully experienced with interest rate deregulation to support economic development. **Ojo (1988**) finds that deregulation in oligopolistic financial market increases lending rate to increase cost of capital to discourage investment. **Kwan (2003)** study shows that banks earn rents from deposit interest rate rules and deregulation will lower both the rent and bank market value. **Humphrey (1997**) suggests that deregulation raises bank funding costs and lowers profits. In response, a bank raise fees for deposit services, reduces branch operating cost and shifts to higher earning assets. **Strahan (2002)** finds that

deregulation of restrictions on branching reduces the sensitivity of state economies to shocks to their own banks' capital. **Stigler (2010)** shows that deregulation means state's withdrawal of its legal power to direct the economic conducts (pricing, entry and exit) of non-governmental bodies. **Guo and Diaye (2010)** find that an increase in real interest rate raises the level of consumption. **Feyzioglu (2009)** finds that households may move deposit out of the banks to earn higher returns if given more choice regarding saving options. Greater flexibility and choice for household portfolio allocation will exert more competitive pressure on banks. **Lardy and Douglas (2011)** say that interest rate liberalization must precede capital account liberalization to lower the risk of households transferring their deposits out of the banks and undermining the stability of the domestic banking system. **Geng and Diaye (2011)** say that with the greater flexibility and choice over saving vehicles, households will be able to achieve a more efficient allocation of saving and extract higher returns from their portfolio. Increases in financial rate of returns contribute to a decline in the share of household disposable income that is saved. **Obamuyi (2009)** says that behavior of interest rate is important for economic growth in view of the relationships between interest rates and investment and investment & growth. Literature review is unable to place the study showing how the level of competition will be enhanced by deregulating saving account deposit rate in India. Therefore, the relevance of the present study is very high.

OBJECTIVES

The present study deals with following objectives:

*Whether the real interest rate (**RIR**) given to Saving Account Holders (**SAH**) is negative.*

*To judge whether the amount of Saving Account Deposit responses to interest rate differential (**IRD**).*

*To know the elasticity of saving Account Deposit (**SAD**) rate with respect to lending rate*

To know whether the monetary policy be implemented effectively through SAD.

Does the deregulation create healthy competition in Indian economy?

METHODOLOGY

The following methodologies, on the basis of secondary data, will be applied to meet the above objectives: Real interest rate (RIR) will be calculated by deducting annual inflation rate from interest rate given on SAD. Interest rate differential will be calculated by deducting rate of interest on SAD from interest rate given on term deposit.The elasticity of

SAD and TAD rate w.r.t. lending rate will be calculated with the help of correlation co-efficient. If the correlation co-efficient between interest rate on TAD and lending rate becomes more than the correlation co-efficient between interest rate on SAD and lending rate , it can be said that monetary policy is effective more with SAD not with TAD.To know the competition level, the Spread Rate (difference between rate of interest on saving account and policy rate) will be calculated. Higher the Spread rate, more the healthy competition.

ANALYSIS

The present study tries to find out the solution of four issues. First issue deals with the real gain to consumers on Saving Account Deposit in the regulated regime. Second issue shows that saving deposit responses the interest rate differential and hence it may be given higher interest rate. Third issue finds that amount deposited in saving account is less elastic than that of term deposit and hence it is suggested that monetary policy can be transmitted with saving deposit. Fourth issue shows that the level of competition can be increased by deregulation of interest rate on saving deposit.

I: Gain in Regulated Regime of Saving Deposit

Saving account deposit rate was almost fixed at 3.5 per cent in the regulated regime up to November 2011. After that, it became free in regulated regime since December 2011. Gain to consumer in real term is negative as shown as in table-1 and figure-1 because the inflation rate is more than the interest rate given to saving account holders. Banks pay low interest rate on saving account deposit because (i) it is repayable on demand; (ii) it is short term subject with liability for bankers (iii) bankers are unable to know its core deposits (iv) Saving deposit bears transaction and facility cost. Account holders need to be given higher interest rate because (i) amount in saving account is deposited not for transaction but for saving purpose (ii) only 20.00 per cent of total amount deposited in saving account is demanded and rest is left to lend (iii) Banks earn interest on 80.00 per cent of total amount deposited in saving account. In such a demand and supply situation, if inflation rate is taken into consideration, the real gain to account holders becomes negative. It is so because of regulated regime in which households are asked either to deposit or leave. It discourages small savings and it is in against the financial inclusion of poor households especially in rural areas. Therefore, it is suggested to deregulate the interest rate to enhance the real gain

to consumer by improving the level of competitions among banks. This level of competition is subject to three factors – interest rate differential, elasticity and spread rate.

Table-1: Real interest rate on saving account deposit given to account Holders

Year	Interest rate on Saving Deposit (%)	Annual Inflation rate (%)	Real Interest rate (%)
March 2001	4.5	0.3	4.2
March 2002	4.5	1.1	3.4
March 2003	3.5	3.2	0.3
March 2004	3.5	3.9	- 0.4
March 2005	3.5	2.6	0.9
March 2006	3.5	3.9	- 0.4
March 2007	3.5	7.8	- 4.3
March 2008	3.5	7.5	- 4.0
March 2009	3.5	10.2	-6.7
March 2010	3.5	13.9	- 10.4
March 2011	3.5	13.7	- 10.2
March 2012	4.0	9.6	- 5.6

Note: Annual inflation rate is based on Consumer Price Index of Agricultural Labour with 1986-87 = 100

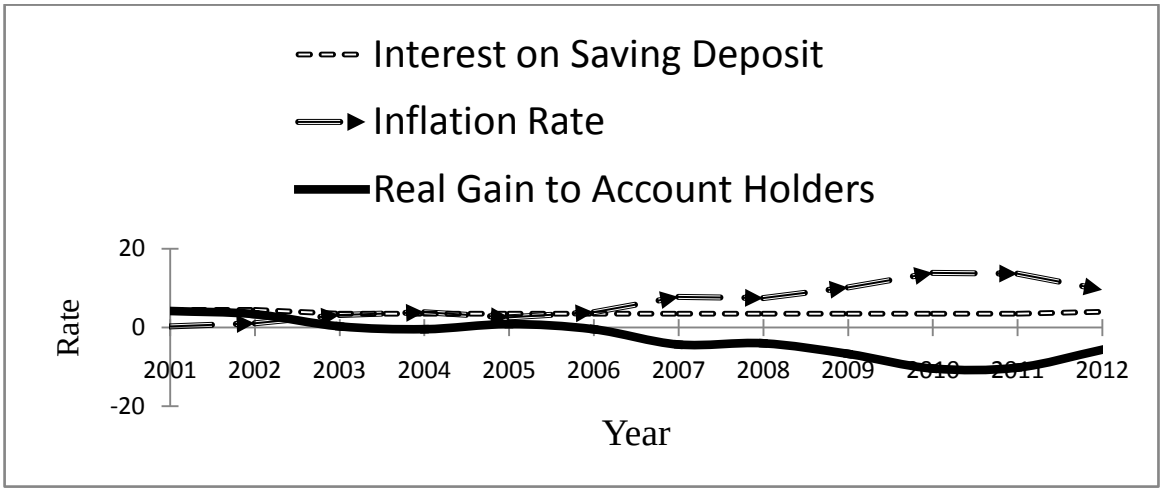
Source: (1) Statistical Tables Relating to Banks in India, RBI, Various Issues and (2) Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

Table-2: Interest rate differential and share of SAD in total deposit in India

Year	Interest rate on Saving Deposit (%)	Interest rate on Term Deposit (%)	IRD (%)	Share in total deposit			
				Saving Deposit (%)	Term Deposit (%)	Other Deposit (%)	Total Deposit (%)
2001	4.5	9.3	4.8	20.0	31.7	48.3	100
2002	4.5	8.0	3.5	20.5	28.7	50.8	100
2003	3.5	5.3	1.8	22.3	23.9	53.8	100
2004	3.5	4.8	1.3	23.7	27.8	48.5	100
2005	3.5	5.8	2.3	24.2	26.5	49.3	100
2006	3.5	6.5	3.0	25.1	24.5	50.4	100
2007	3.5	8.3	4.8	23.4	22.6	54	100
2008	3.5	8.3	4.8	22.4	23.1	54.5	100
2009	3.5	8.3	4.8	21.5	20.2	58.3	100
2010	3.5	6.8	3.3	-	-	-	-
2011	3.5	8.6	5.1	-	-	-	-
2012	4.0	9.5	5.5	-	-	-	---
Correlation Co-efficient (r) with IRD	0.20623	0.950196					

Source: (1) Statistical Tables Relating to Banks in India, RBI, Various Issues and (2) Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

Figure-1: Real Gain to Saving Account Deposit Holders in India



Regression analysis

SAD share = 24.51 – 0.5644 IRD --- R^2 = 0.222, F = 2.00,

TAD share = 27.32 – 0.564 IRD …R^2 = 0.04, F = 0.348

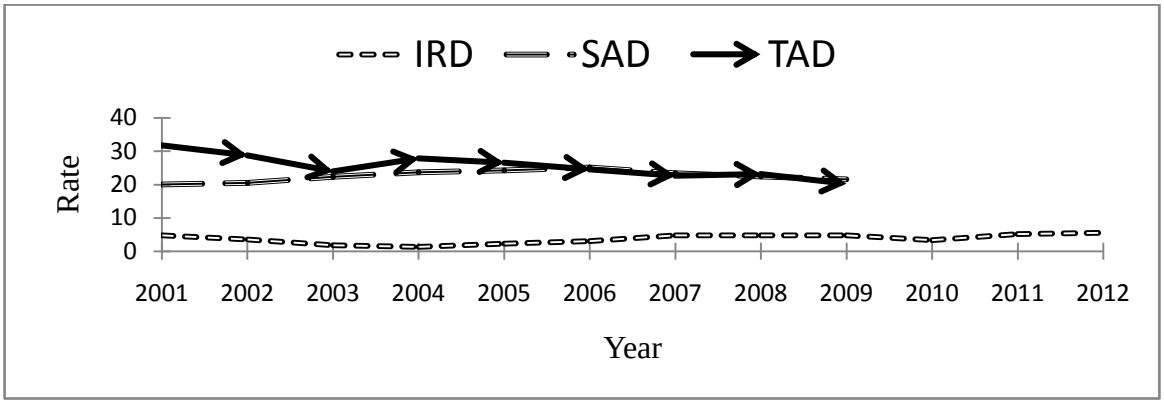
$r_{SAD} < r_{TAD}$ and $b_{SAD} < b_{TAD}$

II: Interest Rate Differential and Saving Deposit

The amount deposited in the saving account responses to interest rate differential. It suggests that there is scope to enhance interest rate given on saving account deposit. Table-2 and figure-2 show that the share of saving account deposit in total deposit is inversely related with interest rate differential. Table-2 and figure-1 collectively suggest that widening of IRD leads to reduction in the share of SAD in total deposit. It shows that amount of saving deposit responses the interest rate given on SAD. One can reveal that account holders deposit in SAD for the purpose of saving not for the purpose of transaction. Therefore it may be suggested that SAD may be treated as well as TAD (term account deposit) to attract saving by raising interest rate on SAD in deregulated regime. Since there is $r_{SAD} < r_{TAD}$ and

$b_{SAD} < b_{TAD}$, shows that SAD is less elastic than TAD and hence monetary policy can be penetrated in better ways with SAD rather than TAD.

Figure-2: Responsiveness of Amount of Saving Account Deposit to Interest Rate Differential (IRD)



III: Elasticity of Saving Deposit

The central bank with the help of policy rates such as Repo rate, Reverse Repo rate, CRR, SLR, OMO, Call rate etc. tries to control lending rate through which monetary policy is transmitted. This lending rate is associated with the rate given on saving account deposit. Table-3 shows that correlation co-efficient between interest rate on saving deposit and ARL is lesser than that of TAD. Therefore, it is suggested that monetary policy can be transmitted in better ways with TAD because it is less elastic.

Table-3: Transmission of monetary policy through Lending rate over SAD and TAD

Year	Interest rate on SAD (%)	Interest rate on TAD (%)	Average Lending rate (ALR) (%)
2001	4.5	9.3	11.50
2002	4.5	8.0	11.50
2003	3.5	5.3	10.75
2004	3.5	4.8	10.25
2005	3.5	5.8	10.25
2006	3.5	6.5	10.25
2007	3.5	8.3	12.25
2008	3.5	8.3	12.25
2009	3.5	8.3	12.25
2010	3.5	6.8	11.75
2011	3.5	8.6	8.25
2012	4.0	9.5	9.50
Correlation Co-efficient with ALR	r_{SAD} = 0.093641	r_{TAD}= 0.0995	

Source: (1) Statistical Tables Relating to Banks in India, RBI, Various Issues and (2) Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

V: Spread Rate of Saving Deposit

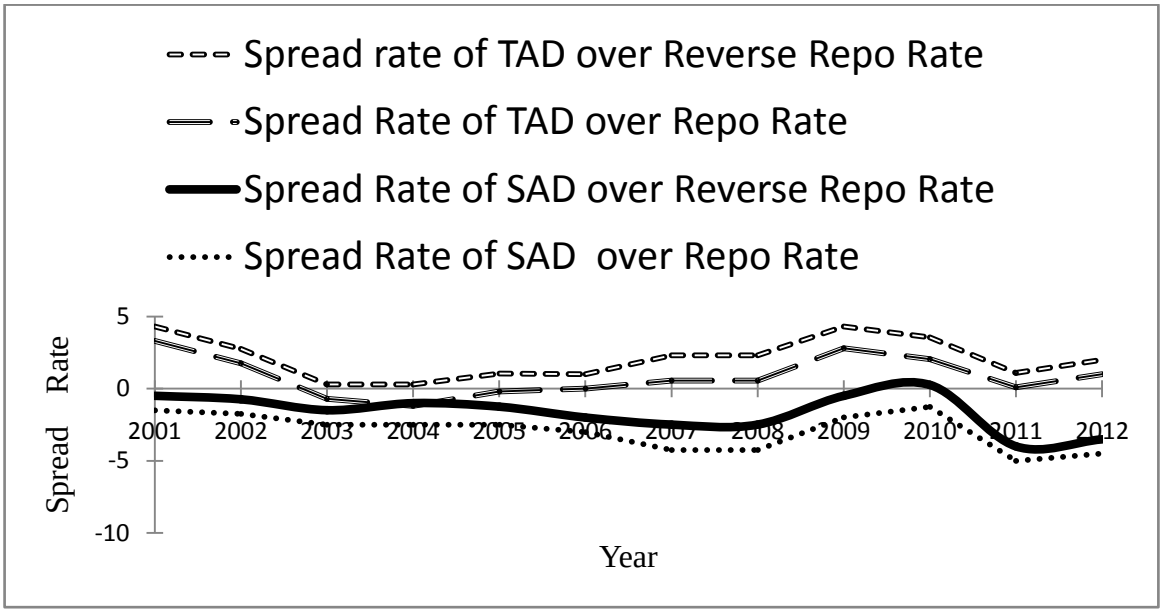
The level of competition is directly associated with the spread rate. This rate is higher in the case of TAD than SAD. In most of the cases the spread rate in SAD is negative as shown as in table-4 and figure-3. The spread rate in TAD is high because it has been deregulate since 1997. Therefore it is suggested that competition level among banks can be raised by raising the spread rate in SAD over both the Repo and Reverse Repo rate.

Table-4: Table-4: Spread rate to know the level of competition in India

Year	Interest rate on Saving Deposit (%) (1)	Interest rate on Term Deposit (%) (2)	Reverse Repo Rate (RRR) (%) (3)	Repo Rate (RR) (%) (4)	Spread Rate (%)			
					TAD over (RRR) (2-3)	TAD over (RR) (2-4)	SAD over (RRR) (1-3)	SAD over (RR) (1-4)
2001	4.5	9.3	5.0	6.0	4.3	3.3	-0.5	-1.5
2002	4.5	8.0	5.25	6.25	2.75	1.75	-0.75	-1.75
2003	3.5	5.3	5.0	6.0	0.3	-0.7	-1.5	-2.5
2004	3.5	4.8	4.5	6.0	0.3	-1.2	-1	-2.5
2005	3.5	5.8	4.75	6.0	1.05	-0.2	-1.25	-2.5
2006	3.5	6.5	5.5	6.5	1	0	-2	-3
2007	3.5	8.3	6.0	7.75	2.3	0.55	-2.5	-4.25
2008	3.5	8.3	6.0	7.75	2.3	0.55	-2.5	-4.25
2009	3.5	8.3	4.0	5.5	4.3	2.8	-0.5	-2
2010	3.5	6.8	3.25	4.75	3.55	2.05	0.25	-1.25
2011	3.5	8.6	7.5	8.50	1.1	0.1	-4	-5
2012	4.0	9.5	7.50	8.50	2	1	-3.5	-4.5

Source: Weekly Statistical Supplement and Handbook of Statistics on the Indian Economy, RBI

Figure-3: Spread Rate of Term and Saving Account Deposit



CONCLUSION

If inflation rate is taken into consideration, the real gain to account holders has become negative. It is so because of regulated regime in which households are asked either to deposit or leave. It **discourages small savings** and it is in against the **financial inclusion** of poor households especially in rural areas. Therefore, it is suggested to deregulate the interest rate to enhance the real gain to consumer by improving the level of competitions among banks. The share of saving account deposit in total deposit is inversely related with interest rate differential. It suggests that **widening of IRD leads to reduction in the share of SAD in total deposit**. It shows that amount of saving deposit responses the interest rate given on SAD. SAD is less elastic than TAD and hence monetary policy can be penetrated in better ways with SAD rather than TAD. Deregulation of interest rate on saving account deposit increases the efficacy of monetary policy. Correlation co-efficient between interest rate on saving deposit (SAD) and ARL is less than that of TAD. Therefore, it is suggested that monetary policy can be transmitted in better ways with SAD because it is less elastic. The level of competition is directly associated with the spread rate. In most of the cases the spread rate in SAD in India is negative as shown as in table-1 and figure-1. Therefore it is suggested that competition level among banks can be raised by raising the spread rate in SAD over both the Repo and Reverse Repo rate.

REFERENCES

1. **Chong, Ben Soon (2010),** "Interest Rate Deregulation: Monetary Policy Efficacy and Rate Rigidity," Journal of Banking & Finance, Vol. 34, Issue 6, June, Page: 1299-1307
2. **Feyzioglu T., Potter N. and Takats E. (2009),** "Interest rate Liberalisation in China", IMF Working Paper 09/ 171
3. **Geng N. and Diaye P.N. (2011),** "Determinants of Corporate Investment in China: Evidence from Cross Country Firm – Level Dta", IMF Working Paper
4. **Glower, Carlos J. (1994),** "Interest Rate Deregulation: A Brief Survey of the Policy Issues and the Asian Experience", Asian Development Bank, Occasional Papers, July
5. **Guo K. and Diaye P.N. (2010)** "Determinats of China's Private Consumption: An International Perspective", IMF Working paper, 10/93
6. **Humphrey D.B. and Pulley L.B. (1997),** "Bank's Response to Deregulation: Profits, Technology and Efficiency", Journal of Money, Credit and Banking, Vol. 29, pp-73-93
7. **Kwan S.H.(2003) ,** " Impact of Deposit Rate Deregulation in Hong Kong on the market value of Commercial banks ", Journal of Banking and Finance, Vol. 27, pp-2231-2248
8. **Lardy N. and Douglas P. (2011**), "Capital Account Liberalisation", PIIE Working Paper-11-6
9. **Obamuyi T.M. (2009),** Journal of Economics and International Finance, Vol. 1(4), pp-93-98
10. **Ojo M.O.(1988),** " Agricultural Performance and Policy Structural Adjustment Programme in Nigeria", Conference Paper presented in Annual Conference of the Nigerian Economic Society at Obafemi Awolowo University, Nigeria
11. **Stigler (2010),** Journal of Economic Literature, Vol. 31, pp-1263-1279
12. **Strahan P.E. (2002)** "The Real Effect of U.S. Banking Deregulation", Journal of Economics, Vol. 101, pp-639-70

CHAPTER-8

INCOME INEQUALITY, EXPENDITURE TAX AND POVERTY RELATION

Income inequality can't be completely eliminated from India where without labour transfer from agriculture to other sectors of the economy, the contribution of agricultural sector is decreasing over the period. However, this income inequality may be minimized through effective implementation of monetary and fiscal policy together. It can't be minimized through expenditure tax. Therefore, expenditure tax can't be effective instrument minimizing the income inequality or transferring the income from rich to poor.

Income inequality is positively associated with poverty which is the denial of opportunities to lead a long, healthy, creative life to enjoy a decent standard of living, freedom, dignity, self respect of others**(1997,Human Development Report**) . It is deprivation in well being (**2000, World Bank**). This wellbeing is associated with society (**1987, Amartya Sen**).

LITERATURE REVIEW

Joaquin M. (2010) suggests reducing taxes on food and intermediate inputs to agriculture. **Zhang (2007)** shows that fiscal war disproportionately benefits the higher income group. **James (2012)** finds that both the food and non-food inflation adds to income inequality. **Christaensen and Demery (2006)** shows that wages may not fully adjust to higher food prices in which case poor suffers more given a higher share of food in his consumption basket. **Ravallion(2000)** finds that inflation reduces expenditure. A rise in food productivity lowers income inequality.

OBJECTIVE

To know the expenditure tax reduces the income inequality to be used in minimizing the poverty or not.

METHODOLOGY

Sen formula will be used to associate income inequality with poverty.

ANALYSIS

The **Sen formula** of poverty Index{(P = H.I + (1- I).H.G)} incorporates three factors. First, incidence of poverty (H= q / n) which shows actual number of poor (q) in

the population (n). Second, poverty or income gap ration {(I = $\frac{1}{qZ}\ \sum_{i=1}^{q}\ (Z - Ri)$} which shows income of the poor people falls short of the standard income (Z) . Third, Gini co-efficient {(G = $\frac{2}{q2\,m}$ ($\sum_{i=1}^{q}\ (q + 1 - i)\ (m - Ri)$} which shows inequality with shortage of income (Ri) of the ith individual from average income of the poor (m).

This Sen formula can be modified and be incorporated with the consumption function of the foodgrain by keeping the value of R_i .

$$\mathbf{P = \frac{\sum_{i=1}^{q}\ (Z - (\beta CXi + \gamma SXi)\ 2PX]}{q.z}\ H + [(1- \frac{\sum_{i=1}^{q}\ (Z - (\beta CXi + \gamma SXi)\ 2PX]}{q.z})]\ H.G}$$

It reveals following facts.

Poverty increases with rise in the inequality in income distribution. Both the consumption expenditure of poor consumers and the capacity to stock the agricultural products should be increased to decrease the poverty gap ratio. Greater weightage be given to lower income consumers to transfer income from rich to poor.

It said that **Kaldorian expenditure tax** is imposed to curb **Keynesian effective demand** to increase savings. However, in the present study it has been said that consumption expenditures need not be curbed but to be increased in the case of poor consumers. This expenditure tax may be used to curb effective demand of rich consumers. Even in this case, Kaldorian expenditure tax has no control on secret and undeclared wealth (**Robinson and Sraffa Capital theory of growth**). Therefore, **Kaldorian expenditure tax is not an effective tool to transfer income from rich to poor.**

Other strategies, mentioned below, may be used to increase consumption expenditure of the poor. **Percolation strategy** be adopted in which mechanized equipments are used in investment sector not in consumption sector. **Wage good strategy** for applying labour intensive investment may be followed for better income distribution. **Parasitic consumption strategy** be adopted to withdraw consumption beyond subsistence by ultra employed (e.g.service holders). **Real inflation strategy** may be followed to convert employed above subsistence to employ at subsistence through balanced allocation ratio by deficit financing. **Orthodox financing strategy** (tax, minting money, deficit financing, borrowing from public, low interest rate etc.) may applied to transfer resources from rich to poor**. Capital formation strategy** may be used to invest in capacity to store foodgrains.

PURA (Providing Urban amenities in Rural Areas), as said as by India's former President Dr. Abdul Kalam, may help in removing rural poverty and converting the villages into engines of growth.

CONCLUSION

Consumption expenditure and poverty are interlinked which reveals to increase consumption expenditure of poor basket of society through government intervention rather than expenditure tax because it is not effective on black or hidden money.

REFERENCES

1. **Sen Amartya(1975**), *Employment Technology and Development*, Delhi, Oxford University Press
2. **Joaquim m. (2010),** " Tax Reform Income Distribution and Poverty", ***International Journal of Microsimulation***, 3(1),114-117
3. **Zhang Q.I.(2007),"** An Innovative Tool for Income Distribution Analysis", Journal of Economic Inequality, 1(3), 281-283
4. **James P.W. (2012),** " Inflation and Income Inequality", IMF Working paper, wp/112/147
5. **Christaensen and Demery(2006),"** Down to Earth", Direction in Development, Washington D.C., World Bank
6. **Ravallian M.(2000),"** Prices, Wages Poverty in Rural India" , Food Policy, Vol. 25(357-364)

CHAPTER-9
LEGISLATURE AND MARGINAL GROUP

A marginalized group of the society in any nation is denied social, education, economic and political participation partially or fully. When they raise voice, government tries to put down their voices by providing facilities, programmes and even by making ministers from that community but never make the ruling class. Conversion from marginal to ruling class is possible only through capturing the legislature with de-facto sovereignty.

OBJECTIVE

To know the method by which marginal group of the society can be converted into ruling class.

METHODOLOGY

Marginal group of the society in the present study is one which has been provided reservation in the government services on the basis of social, economic and education backwardness.

LITERATURE REVIEW

Social status of a person is known by the status of the community to which he belong (**Ambedkar, 1946).** Reservation in Job is given to the poorest people (**Cornell and Kalt, 1992).** People belonging to reserved category live on fixed income which disables them to have social security and creates dismal employment opportunity for them(**Dwyer, 2000)**. Act should intend to protect the tribe's land and to allow the creation of legal structures designed to help the tribe's govern themselves (**Canby, 1988)**. A community which depends on outside decision making, continues on poverty (**Kalt, 1996)**. The people belonging to depressed class became bonded labour because ownership of land, man and resources are not equally distributed in India (**Heggarde, 1972)**. They suffered from variety of economic constraints because their route stands at lowest strata in Hindu Social system **(Davis, 1959).** Programmes intended to provide economic opportunities for reservation residents have failed in India (**Mantonya and Milan, 2007**). Therefore, it is suggested that the future course of action of the Tribal Community is to enforce the government not only to

nationalise but also to declare land an industry **(Ambedkar, 1946).** So that economic equality be made in the society and Tribal community be converted into ruling class. Proper opportunity should be given to all members of the society which is only possible in an ideal society **(Ambedkar, 1947**). A strategy in the modern market economy should be applied with three steps (**Kalt, 1996)** (a) education directed to skills (b) financing to entrepreneurs efforts and (c) networking between potential entrepreneurs and their counterparts. Above that social and economic equality should be brought into effect to bring them into mainstream because social and economic inequality is detrimental to the health of the society (**Lal and Clement, 2005**). It has been rightly observed that successful tribes are not always the ones that own favourable natural resources of the ones that have educated tribal numbers or that have been able to gain financial capital (**Deogaonkar, 2004**). The relatively successful tribes need three indispensable ingredients (a) sovereignty (b) capable government (c) a match between the type of government a tribe has and that tribe's cultural norms regarding legitimate political power (**Kalt, 1996).**

ANALYSIS

A community can be marginalized on number of fronts. There are three **interlinked fronts** on which majority of the Indian populace have been marginalized and provided reservation in the Government services-**Social, Economic and Education**.

Socially marginalized group of society is prohibited from participation in public life which lowers their morals, dignity and prestige. It creates the problem of social security and employment opportunity. It hampers national unity and integration as whole. They are treated as slaves. Slaves are discarded by the society for whom they work and no way can they get a respectable job (**Annie Besent, 1909, Indian Review**).

Economically marginalized group of society is prohibited from participation in economic activities. It increases poverty, income inequality, economic disparity, employment problems, labour shortages. It lowers the possibility of transfer of labour from agriculture to service and industry. It lowers national income, savings and investment.

Educationally marginalized group of society is prohibited from participation in educational activities. It lowers the availability of skilled labour to nation. It creates problems in availability of skilled human capital.

A community which is marginalized on above mentioned three interlinked fronts carries following **characteristics-**

(1) They are out of the political power because they are not united.

(2) They live on fixed income.

(3) They are out of the business activities.

(4) They are out of the decision making bodies at national level.

(5) They are out of the ownership of land, industry, capital and production system.

(6) Their representation is almost negligible in higher education, judiciary and defence.

(7) They don't have de-facto-sovereignty.

(8) They get subsistence wage.

(9) They are mostly engaged in the agricultural sector.

(10) They are socially subdivided into caste.

NATIONAL PROBLEMS

The nation whose majority of population is suffered from above characteristics, there can be following **national problems**-(1) Labour transfer will be very slow to match the decrease the share of agriculture in the national income (2) Agricultural sector will be predominated in the occupational structure (3) Income inequality will further rise across the social group, across the occupational sectors and across the profession. (4) Rural poverty will pull the leg of development (5) Nation will lack an ideal society comprising the social freedom and brotherhood. (6) Threat of national integration.

EFFORTS TO SOLVE THE NATIONAL PROBLEMS

A number of the thinkers thought over the national problems associated with marginal group of the society in India. Shahuji maharaj, Jyotibha Phule,Periyar, Narayana Guru and Dr. B.R. Ambedkar are popular among them. They focused on educate, agitate and unite formula to convert them into ruling class through capturing the legislature. The prominence of legislature can be understood with the statement of Dr. Ambedkar **(Poona Pact, 1932**) "**Gandhi has adopted an extreme course of starving to death not to secure a separate settlement for tribal community but to prevent them from securing a united number of representative chosen by their own people who will speak in the legislature on their behalf which will have a dominance influence over their future**." On the basis of the Poona Pact, the marginal group of the society has been provided reservation in the

government services with limited scope. However, no reservation policy has been implemented in Judiciary, Defence, and Upper house of the legislature, agricultural and industrial sector. Reservation in promotion has been not extended to Research institutes, University, Autonomous body and Undertaking and Banking.

STRATEGY

Their problems can only be solved when they shall **capture the legislature with de-facto sovereignty because politics is the master key.**

FINDINGS AND CONCLUSION

Successful marginal group of the society is not the one that owns favourable programmes offered by government or have educated numbers or that have been able to gain financial capital but the relatively successful society is that which has **captured the legislature with de-facto sovereignty.**

REFERENCES

1. **Ambedkar B.R. , (1946),** *Who were Shudra*?, p-29
2. **Cornell S. and Kalt J.P.** (1992)," Reloading the dice: Improving the chances for economic development on American Indian Reservation" , published in Cornell and Kalt's ***What Can Tribes Do?***
3. **Dwyer K. (2000),** *American Indians and Disability*
4. **Canby W.C. (1988),** *American Indian Law in nutshell*
5. **Kalt J.P. (1996),** *Testimony presented before the United States Senate Committee on Indian Affairs*
6. **Heggarde O.D. (1972),** "Ambedkar's Social Theory of Labour Exploitation jn Government of India" , **Ambedkar and Social Justice ,** Vol. –II, p-48
7. Rhice Davis (1959), *Buddhist India*, p-38
8. Ministry of Rural Development, Government of India, 2010- 11
9. Ministry of Tribal Affairs, 2010-11
10. **Mantonya K. and Milan W.** (2007), "Economic Development in Indian Country: Traits That Lead to Sustainability', ***Journal of Rural Research and Policy*** , No.3
11. Ambedkar B.R. (1946), *State and Minorities*, p-15
12. Ambedkar B.R. (1947), *Annihilation of Caste*, p-41
13. Report of the Indian Round Table Conference, 1930-33, p-8
14. **Kalt J.P. (1996),** *Testimony presented before the United States Senate Committee on Indian Affairs*
15. **Lal A.K. and Clement R.W**. (2005)," Economic Development in India: The Role of Individual Enterprise", ***Asia Pacific Development Journal***, Vol. No. 12, No. 2

CHAPTER-10
MIDDLE INCOME GROUP AND DEBT FUND

Investors having fixed income should invest in debt fund. They should not invest in Demat or equity fund. Equity fund is highly volatile and risky. Debt fund is little volatile and less risky. Middle or low income group can't bear the high risk associated with equity fund.

LITERATURE REVIEW

Equity mutual fund is risk adjusted return in which individual fund does not earn higher returns from following the momentum strategy in stock (**Carhart, 1997**) because of investment constraints (**Almazan, 2004**). Therefore, an investor should invest in small equity fund whose trading activity is high (**Dahlquist, 2000**) or whose expense ratio is low (**Malkiel, 1995**) . Investors are advised to prefer low expense index funds; actively managed funds continue to be popular (**Chordia T., 1996**). The literature review finds no place of middle income group and debt fund suggesting study.

OBJECTIVE

To asses comparative advantages between Debt and equity fund where middle income group should invest.

METHODOLOGY

Fixed income group will be treated as middle income group.

ANALYSIS

India's mutual fund industry provides two options to retail investors-debt or equity as shown as in table-1. Equity fund depends on growth performance of the Indian economy. It is very much flexible. In this case, gain to investors depends on performance of the industries registered to stock exchange. Smart investors invest in a diversified equity fund to decrease the risk. Here, gain is directly associated with gain. On the other hand, an investment in debt fund is less risky and gain is almost guaranteed. In general, in this case, the investors invest in government security (G-sec). To minimize the risk it is suggested to invest in a short term debt – fund. If the rates of debt instruments (i.e. G-Sec, Certificate of Deposit and so on) raise, the gain to investor's increases.

India's mutual fund industry is able to provide economies to scale benefit to retail investors through minimizing transaction costs and better market accessibility. Mutual fund pools the retail investor's money which is managed by fund managers to maximize the yields. In this case, the investors do not have to pay transaction and brokerage fees as paid as in demat account. In the case of Demat account; the fund of an investor is managed by broker who is not professional as fund manager is. At the same time, some segments of debt instruments are not available to brokers but to institutions for transacting business.

India's mutual fund provides the trained, skilled, well informed professionals who understand the linkages between different markets and its dynamism. Funds manager is able to hedge the portfolios using options and powerful techniques. Most mutual funds are available in the form of SIP (Systematic Investment Plans) which allows investors to invest via fixed, small periodic payments. Through SIP a fund manager is able to buy more units when its price is low and fewer units when market is rising. SIP offers twin benefits of Rupees cost averaging and the power of compounding.

Table-1: A comparative study gain between Equity Fund and Debt Fund

Issues	Mutual Fund	
	Equity Fund	Debt Fund
Volatility	Highly volatile	Less volatile
Gain depends on	Market growth	Government declaration
Possibility of no gain	yes	No
Possibility of Loss	Yes	No
Possibility of very high gain	yes	Lower than equity fund
Suitable for	Rich investors	Middle
Who should invest	flexible income investor	Fixed income investor

CONCLUSION

Investors have either to invest in equity fund or in debt fund. Risk takers having high income should invest in equity fund and risk averter having fixed and low income should invest in debt fund. Middle income group should take less risk and should invest in debt fund whose expense ratio is low. Middle income group should take less risk and should invest in debt fund whose expense ratio is low.

REFERENCES

1. **Almazan A., Keith C.B., (2004),** "Why Constrain Your Mutual Fund Manager?" J. of Financial Economics
2. **Carhart, M.M., (1997),** "On Persistence in Mutual Fund Performance", J. of Finance, Vol. 52, No. 1, PP-57-82
3. **Chordia T., (1996),** " The Structure of Mutual Fund Charges ", J. of Financial Economics, Vol. 41, pp-3-39
4. **Dalquist M., Engstroem S. and Soederlind P.,(2000),** "Performance and Characteristics of Swedish Mutual Funds", J. of Financial Quantitative Analysis,
5. **Malkiel B.G., (1995**), "Returns from Investing in Equity Mutual Funds ", J. of Finance, 50(2), pp-542-572

CHAPTER-11
FUND ALLOCATION IN MUTUAL FUND

Investors have two options-Demat account or mutual funds- to choose. In the former case investors directly enter the financial market by opening Demat account in which securities are bought or sold with the help of brokers. In the later case capitals of the investors are pooled through selling retail investment products and funds are professionally managed by fund manager. This capital in mutual fund is either invested in equity fund or debt fund. It infers that **an investor has three options – opening Demat account, Choosing equity fund or opting debt fund.**

LITERATURE REVIEW

Mutual fund is the combination of equity, debt and hybrid fund. Equity mutual fund is risk adjusted return in which individual fund does not earn higher returns from following the momentum strategy in stock **(Carhart, 1997)** because of investment constraints **(Almazan, 2004).** Restriction on competing products is the reason of the development of money market and short term bond funds **(Klapper, 2000).** Therefore, an investor should invest in small equity fund whose trading activity is high **(Dahlquist, 2000)** or whose expense ratio is low **(Malkiel, 1995) .** Funds that heavily underperform have very high expense ratio, while funds that are successful do not increase revenues by raising their fees but benefit from increased size of their funds **(Elton 1996, Carhat 1997).** Actively managed equity funds charge higher fees than index tracking funds or bond and money market funds, reflecting the higher costs of employing investment management staff to achieve diversification and strategy **(James et al. 1999).** Funds charge lower fees when they have smaller boards and a large proportion of independent directors (**Tufano and Sevick, 1997).** Larger and more mature funds as well as no load funds have lower expense ratio **(Malhotra and Mcleod, 1997).** Aggressive growth funds charge higher entry and exit fees to discourage redemption because they hold more of the smaller, less liquid stocks **(Chordia, 1996).** However, despite the basic academic advice offered to investors to prefer

low expense index funds, actively managed funds continue to be popular **(Gruber, 1996).** To decrease the risk it is advised to use derivative. Bond mutual fund uses derivatives more than equity mutual funds. Use of derivative is negatively correlated with fund age and positively correlated with fund size (Johnson **and Yu 2004)** and it is positively correlated with asset turnover **(Koski and Pontiff, 1999).** Derivatives are used for trading rather than hedging **(Minton et al. 2009).**

OBJECTIVE

To know how to allocate fund to minimize risk.

METHODOLOGY

Risk (β), expense ratio and NAV (Net Asset Value) has been used in the present study to allocate the fund. A case study of Scheduled Commercial Banks (SCB) has been undertaken for the study to know the pragmatic knowledge about the allocation of fund.

ANALYSIS

Table-1 gives better ideas about allocation of funds. It shows that risk taker rich investors should invest in equity fund and risk averter poor investors should invest in debt fund (G-Sec, Certificate of Deposit and so on). The SCB takes low risk. The Scheduled Commercial Banks (SCB) of India invests more than 80.00 per cent in debt market, as shown as in table-2. Most of the SCB funds were invested in Central Government Securitas (G-**Sec**). SCB invested two-third of its total funds in G-Sec. Less than 10.00 per cent of its fund was invested in equity funds. Perhaps this is the reason why net profit of SCB increased Rs. 24582 Cr. in 2006 to Rs. 57100 Cr. in 2010. As shown as in table-3.

Table-1: A comparative study of gain between Equity Fund and Debt Fund

Issues	**Mutual Fund**	
	Equity Fund	**Debt Fund**
Volatility	Highly volatile	Less volatile
Gain depends on	Market growth	Government declaration
Possibility of no gain	Yes	No
Possibility of Loss	Yes	No
Possibility of very high gain	Yes	Lower than equity fund
Suitable for	Rich investors	Middle
Who should invest	flexible income investor	Fixed income investor

Table-2: Investment by Scheduled Commercial Banks (Rs. Cr)

Allocation of funds	2008		2009	
	Aggregate	**Per cent**	**Aggregate**	**Per cent**
Central Govt. Securities	772565	66.50	920579	64.54
State Govt. Securities	151811	13.06	229030	16.05
Other Trustee Securities	11557	1.00	9897	0.70
Share and Debenture of Joint Stock Companies	91498	7.88	89846	6.31
Other investment	134391	11.56	176893	12.40
Total	1161822	100	1426245	100

Source: Statistical Tables Relating to Banks, RBI

Table-3: Sources of Earnings to SCB (Rs. Cr.)

Items	**2006**	**2007**	**2008**	**2009**	**2010**
Interest earned	185388	231675	308482	388482	415752
Other income	35368	43041	60391	75220	78519
Interest expended	107161	142420	208001	263223	272084
Operating expenses	59201	66319	77283	89581	99769
Provisions and contingencies	29812	34775	40864	58147	65310
Total earnings	220756	274716	368873	463702	494271
Total expenses	166362	208739	285284	352805	371852
Provisions and expenses	29812	34775	40864	58147	65310
Net profit	24582	31203	42726	52750	57109

Source: Statistical Tables Relating to Banks, RBI

CONCLUSION

Investors have two options to invest either in equity or in debt fund. The Indian financial institutions chose debt fund. More than two-third of total collected funds by Scheduled Commercial Banks has been allocated to debt fund. It raises their net profit.

REFERENCES

1. **Carhart, M.M., (1997),** "On Persistence in Mutual Fund Performance", J. of Finance, Vol. 52, No. 1, PP-57-82
2. **Almazan A., Keith C.B., (2004),** "Why Constrain Your Mutual Fund Manager?" J. of Financial Economics
3. **Berk J.B. and Green R.C., (2004**), "Mutual Fund Flows and Performance in Rational Markets", J. of Political Economy
4. **Malkiel B.G., (1995),** "Returns from Investing in Equity Mutual Funds ", J. of Finance, 50(2), pp-542-572
5. **Elton E.G., (1996),** "The Persistence of Risk Adjusted Mutual Fund Performance", J. of Business, 69(2), pp-133-157
6. **Dalquist M., Engstroem S. and Soederlind P., (2000),** "Performance and Characteristics of Swedish Mutual Funds", J. of Financial Quantitative Analysis,
7. **Rao K.L.,(2011),** "Analysis of Individual Investors' Behaviour towards Mutual Fund Schemes ", J. of Banking Financial Services and Insurance Research, VOL. 1, Issue-7, 65
8. **Michael J.T., (2009),** "Use of Interest Rate Derivatives by S.S. Based Domestic and Global Bond Mutual Funds", J. of Management Research, Vol. 1(2), 6
9. **James E., Ferrier G. and James S., (2009),** "Mutual Funds and Institutional Investments: What is most efficient ways to to Set up Individual Accounts in a Social Security System", World Bank Policy Research Paper
10. **Tufano P. and Sevick M., (1997), "**Board Structure and Fee Setting in the Us Mutual Fund Industry", Journal of Financial Economics, 46, pp-321-55
11. **Sirri E.R. and Tufano P. , (1993),** " Competition and Change in the Mutual Fund Industry", Financial Series Samuel B. ,Harvard Business School
12. **Chordia T., (1996),** " The Structure of Mutual Fund Charges ", J. of Financial Economics, Vol. 41, pp-3-39

CHAPTER-12
RISK AND PERFORMANCE OF MUTUAL FUND

Investors have two options-Demat account or mutual funds- to choose. In the former case investors directly enter the financial market by opening Demat account in which securities are bought or sold with the help of brokers. In the later case capitals of the investors are pooled through selling retail investment products and funds are professionally managed by fund manager. This **capital in mutual fund is either invested in equity fund or debt fund**. It infers that **an investor has three options – opening Demat account, Choosing equity fund or opting debt fund.**

LITERATURE REVIEW

Mutual fund is the combination of equity, debt and hybrid fund. Equity mutual fund is risk adjusted return in which individual fund does not earn higher returns from following the momentum strategy in stock **(Carhart, 1997)** because of investment constraints **(Almazan, 2004).** Restriction on competing products is the reason of the development of money market and short term bond funds **(Klapper, 2000).** Therefore, an investor should invest in small equity fund whose trading activity is high **(Dahlquist, 2000)** or whose expense ratio is low **(Malkiel, 1995) .** Funds that heavily underperform have very high expense ratio, while funds that are successful do not increase revenues by raising their fees but benefit from increased size of their funds **(Elton 1996, Carhat 1997).** Actively managed equity funds charge higher fees than index tracking funds or bond and money market funds, reflecting the higher costs of employing investment management staff to achieve diversification and strategy **(James et al. 1999).** Funds charge lower fees when they have smaller boards and a large proportion of independent directors (**Tufano and Sevick, 1997).** Larger and more mature funds as well as no load funds have lower expense ratio **(Malhotra and Mcleod, 1997).** Aggressive growth funds charge higher entry and exit fees to discourage redemption because they hold more of the smaller, less liquid stocks **(Chordia, 1996).** However, despite the basic academic advice offered to investors to prefer low expense index funds, actively managed funds continue to be popular **(Gruber, 1996).** To decrease the risk it is advised to use derivative. Bond mutual fund uses derivatives more

than equity mutual funds. Use of derivative is negatively correlated with fund age and positively correlated with fund size (Johnson **and Yu 2004)** and it is positively correlated with asset turnover **(Koski and Pontiff, 1999).** Derivatives are used for trading rather than hedging **(Minton et al. 2009).**

OBJECTIVE

To know the risk and performance associated with mututal fund.

METHODOLOGY

Risk (β), expense ratio and NAV (Net Asset Value) has been used in the present study to the risk and performance of the fund. A case study of State Bank of India (SBI) has been undertaken for the study to know the pragmatic knowledge about risk.

ANALYSIS

Table-1 gives better ideas about allocation of funds. It shows that risk taker rich investors should invest in equity fund and risk averter poor investors should invest in debt fund (G-Sec, Certificate of Deposit and so on). Table-2 and able-3 infer that equity fund is highly risk than debt fund. Equity fund gives higher return than debt fund.

Table-1: A comparative study of gain between Equity Fund and Debt Fund

Issues	**Mutual Fund**	
	Equity Fund	**Debt Fund**
Volatility	Highly volatile	Less volatile
Gain depends on	Market growth	Government declaration
Possibility of no gain	Yes	No
Possibility of Loss	Yes	No
Possibility of very high gain	Yes	Lower than equity fund
Suitable for	Rich investors	Middle
Who should invest	flexible income investor	Fixed income investor

Table-2: Risk and Performance associated with SBI Equity Mutual Fund

Funds	Risk (β)	Expense ratio	Minimum Investment (Rs.)	NAV		Sectoral Fund Allocation	
				Growth	Dividend	Production	Services
Equity	0.91	2.25	1000	41	27.56	26.69	73.31
Global	0.94	2.08	2000	53.64	27.23	45.96	54.54
Emerging	1.07	2.25	2000	42.29	16.01	32.26	67.74

Multiplier	0.80	2.02	1000	72.95	46.08	32.33	67.67
FMCG	0.64	2.49	2000	-	33.26	0.33	99.67
Pharma	1.02	2.49	2000	45.92	37.96	98.21	1.79
I.T.	0.99	2.49	2000	-	21.79	0.00	100
Contra	0.94	1,86	2000	48.86	16.05	39.60	60.40
PSU	-	2.28	5000	8.35	8.35	20.79	79.21
Arbitrage	0.49	1.84	25000	14.42	12.42	7.80	92.20

Source: SBI Mutual Fund Brochure, February 2012

Table-3: Risk and Performance associated with SBI Debt Mutual Fund

Funds	Risk (β)	Expense ratio	Min Investment (Rs.)	NAV		Asset Allocation (%)				
						CD	CP	NCD	G-sec	Other
Ultra	-	0.33	10000	1000		65.05	27.30	-	-	7.65
S.T.	-	0.63	10000	10.35		35.86	0.77	54.47	-	8.90
MIP	-	1.99	10000	10.33		13.79	5.73	40.14	15.58	20.76
Liquid Premier	-	0.07	50 L	1003		64.42	28.74	-	-	6.84
Children Benefit	-	1.54	1500	23.82		12.24	-	43.64	-	44.12
Income Plus	-	1.25	25000	11.9	10.78	-	-	49.06	-	50.94
Income Magnum	-	1.30	2000	11.31		21.31	-	28.06	29.61	21.02
Gilt Short	-	0.84	25000	20.9	11.27	-	-	-	6.76	93.24
Gilt Long	-	1.19	25000	10.5		-	-	-	57.69	42.31
Floater	-	1.65	10000	10.47		67.64	-	15.08	-	17.28

Source: SBI Mutual Fund Brochure, February 2012

Note: (1) Other source of asst allocation includes -Reserve repo, equity Shares, T-bills, Zero Coupon bond, Short term deposit

(2) Production Sector includes automobile, construction, metals, pharmacy, cement, industrial manufacturing, textiles, fertilizers & pesticides and chemicals

CONCLUSION

Mutual fund gives two options two be invested- equity and debt funds. Equity fund is volatile and highly risky but it gives comparatively more return to investors. Debt fund is less risky, less volatile but gives comparatively low return.

REFERENCES

1. **Carhart, M.M., (1997),** "On Persistence in Mutual Fund Performance", J. of Finance, Vol. 52, No. 1, PP-57-82
2. **Almazan A., Keith C.B., (2004),** "Why Constrain Your Mutual Fund Manager?" J. of Financial Economics
3. **Berk J.B. and Green R.C., (2004**), "Mutual Fund Flows and Performance in Rational Markets", J. of Political Economy
4. **Malkiel B.G., (1995),** "Returns from Investing in Equity Mutual Funds ", J. of Finance, 50(2), pp-542-572
5. **Elton E.G., (1996),** "The Persistence of Risk Adjusted Mutual Fund Performance", J. of Business, 69(2), pp-133-157
6. **Dalquist M., Engstroem S. and Soederlind P., (2000),** "Performance and Characteristics of Swedish Mutual Funds", J. of Financial Quantitative Analysis,
7. **Rao K.L.,(2011),** "Analysis of Individual Investors' Behaviour towards Mutual Fund Schemes ", J. of Banking Financial Services and Insurance Research, VOL. 1, Issue-7, 65
8. **Michael J.T., (2009),** "Use of Interest Rate Derivatives by S.S. Based Domestic and Global Bond Mutual Funds", J. of Management Research, Vol. 1(2), 6
9. **James E., Ferrier G. and James S., (2009),** "Mutual Funds and Institutional Investments: What is most efficient ways to to Set up Individual Accounts in a Social Security System", World Bank Policy Research Paper
10. **Tufano P. and Sevick M., (1997), "**Board Structure and Fee Setting in the Us Mutual Fund Industry", Journal of Financial Economics, 46, pp-321-55
11. **Sirri E.R. and Tufano P. , (1993),** " Competition and Change in the Mutual Fund Industry", Financial Series Samuel B. ,Harvard Business School
12. **Chordia T., (1996),** " The Structure of Mutual Fund Charges ", J. of Financial Economics, Vol. 41, pp-3-39

CHAPTER-13
DEBT FUND AND INDIAN BANKS

The Indian financial institutions chose debt fund. More than two-third of total collected funds by Scheduled Commercial Banks has been allocated to debt fund. The State Bank of India has allocated most of its fund in debt having low risk and has performed well.

LITERATURE REVIEW

Mutual fund is the combination of equity, debt and hybrid fund. Equity mutual fund is risk adjusted return in which individual fund does not earn higher returns from following the momentum strategy in stock (Carhart, 1997) because of investment constraints (Almazan, 2004). Restriction on competing products is the reason of the development of money market and short term bond funds (Klapper, 2000). Therefore, an investor should invest in small equity fund whose trading activity is high (Dahlquist, 2000) or whose expense ratio is low (Malkiel, 1995) . Funds that heavily underperform have very high expense ratio, while funds that are successful do not increase revenues by raising their fees but benefit from increased size of their funds (Elton 1996, Carhat 1997). Actively managed equity funds charge higher fees than index tracking funds or bond and money market funds, reflecting the higher costs of employing investment management staff to achieve diversification and strategy (James et al. 1999). Funds charge lower fees when they have smaller boards and a large proportion of independent directors (Tufano and Sevick, 1997). Larger and more mature funds as well as no load funds have lower expense ratio (Malhotra and Mcleod, 1997). Aggressive growth funds charge higher entry and exit fees to discourage redemption because they hold more of the smaller, less liquid stocks (Chordia, 1996). However, despite the basic academic advice offered to investors to prefer low expense index funds, actively managed funds continue to be popular (Gruber, 1996). To decrease the risk it is advised to use derivative. Bond mutual fund uses derivatives more than equity mutual funds. Use of derivative is negatively correlated with fund age and positively correlated with fund size (Johnson and Yu 2004) and it is positively correlated with asset turnover (Koski and Pontiff, 1999). Derivatives are used for trading rather than hedging (Minton et al. 2009).

OBJECTIVE

To know why the Indian banks prefer debt rather than equity fund?

METHODOLOGY

Risk (β), expense ratio and NAV (Net Asset Value) has been used in the present study to know the risk and performance of the fund. A case study of Scheduled Commercial Banks (SCB) has been undertaken for the study to know the pragmatic knowledge about the allocation of fund.

A case study of State Bank of India (SBI) has been undertaken for the study to know the pragmatic knowledge about risk.

ANALYSIS

The risk and performance of both the debt and equity fund has been shown in table-1 and table-2. Equity fund is highly risk than debt fund. Equity fund gives higher return than debt fund. A comparative performance of debt and equity fund has been shown in table-3. Table-4 and table-5 clearly show that SCB prefers debt fund rather than equity fund to invest. The SCB takes low risk. The Scheduled Commercial Banks (SCB) of India invests more than 80.00 per cent in debt market, as shown as in table-2. Most of the SCB funds were invested in Central Government Securitas (G-Sec). SCB invested two-third of its total funds in G-Sec. Less than 10.00 per cent of its fund was invested in equity funds. Perhaps this is the reason why net profit of SCB increased Rs. 24582 Cr. in 2006 to Rs. 57100 Cr. in 2010.

Table-1: Risk and Performance associated with SBI Equity Mutual Fund

Funds	Risk (β)	Expense ratio	Minimum Investment (Rs.)	NAV		Sectoral Fund Allocation	
				Growth	Dividend	Production	Services
Equity	0.91	2.25	1000	41	27.56	26.69	73.31
Global	0.94	2.08	2000	53.64	27.23	45.96	54.54
Emerging	1.07	2.25	2000	42.29	16.01	32.26	67.74
Multiplier	0.80	2.02	1000	72.95	46.08	32.33	67.67
FMCG	0.64	2.49	2000	-	33.26	0.33	99.67
Pharma	1.02	2.49	2000	45.92	37.96	98.21	1.79
I.T.	0.99	2.49	2000	-	21.79	0.00	100
Contra	0.94	1,86	2000	48.86	16.05	39.60	60.40

PSU	-	2.28	5000	8.35	8.35	20.79	79.21
Arbitrage	0.49	1.84	25000	14.42	12.42	7.80	92.20

Source: SBI Mutual Fund Brochure, February 2012

Table-2: Risk and Performance associated with SBI Debt Mutual Fund

Funds	Risk (β)	Expense ratio	Min Investment (Rs.)	NAV		Asset Allocation (%)				
						CD	CP	NCD	G-sec	Other
Ultra	-	0.33	10000	1000		65.05	27.30	-	-	7.65
S.T.	-	0.63	10000	10.35		35.86	0.77	54.47	-	8.90
MIP	-	1.99	10000	10.33		13.79	5.73	40.14	15.58	20.76
Liquid Premier	-	0.07	50 L	1003		64.42	28.74	-	-	6.84
Children Benefit	-	1.54	1500	23.82		12.24	-	43.64	-	44.12
Income Plus	-	1.25	25000	11.9	10.78	-	-	49.06	-	50.94
Income Magnum	-	1.30	2000	11.31		21.31	-	28.06	29.61	21.02
Gilt Short	-	0.84	25000	20.9	11.27	-	-	-	6.76	93.24
Gilt Long	-	1.19	25000	10.5		-	-	-	57.69	42.31
Floater	-	1.65	10000	10.47		67.64	-	15.08	-	17.28

Source: SBI Mutual Fund Brochure, February 2012

Note: (1) Other source of asst allocation includes -Reserve repo, equity Shares, T-bills, Zero Coupon bond, Short term deposit

(2) Production Sector includes automobile, construction, metals, pharmacy, Cement, industrial manufacturing, textiles, fertilizers & pesticides and chemicals

Table-3: A comparative study of gain between Equity Fund and Debt Fund

Issues	Mutual Fund	
	Equity Fund	Debt Fund
Volatility	Highly volatile	Less volatile
Gain depends on	Market growth	Government declaration

Possibility of no gain	Yes	No
Possibility of Loss	Yes	No
Possibility of very high gain	Yes	Lower than equity fund
Suitable for	Rich investors	Middle
Who should invest	flexible income investor	Fixed income investor

Table-4: Investment by Scheduled Commercial Banks (Rs. Cr)

Allocation of funds	2008		2009	
	Aggregate	Per cent	Aggregate	Per cent
Central Govt. Securities	772565	66.50	920579	64.54
State Govt. Securities	151811	13.06	229030	16.05
Other Trustee Securities	11557	1.00	9897	0.70
Share and Debenture of Joint Stock Companies	91498	7.88	89846	6.31
Other investment	134391	11.56	176893	12.40
Total	1161822	100	1426245	100

Source: Statistical Tables Relating to Banks, RBI

Table-5: Sources of Earnings to SCB (Rs. Cr.)

Items	2006	2007	2008	2009	2010
Interest earned	185388	231675	308482	388482	415752
Other income	35368	43041	60391	75220	78519
Interest expended	107161	142420	208001	263223	272084
Operating expenses	59201	66319	77283	89581	99769
Provisions and contingencies	29812	34775	40864	58147	65310
Total earnings	220756	274716	368873	463702	494271
Total expenses	166362	208739	285284	352805	371852
Provisions and expenses	29812	34775	40864	58147	65310
Net profit	24582	31203	42726	52750	57109

Source: Statistical Tables Relating to Banks, RBI

CONCLUSION

From above one may conclude that debt fund is able to provide economies to scale benefit to retail investors through minimizing transaction costs and better market accessibility. It pools the retail investor's money which is managed by fund managers to

maximize the yields. In this case, the investors do not have to pay transaction and brokerage fees as paid as in demat account. It provides the trained, skilled, well informed professionals who understand the linkages between different markets and its dynamism. Funds manager is able to hedge the portfolios using options and powerful techniques. For the said reasons, Indian banks prefer debt rather to equity fund.

REFERENCES

1. **Carhart, M.M., (1997),** "On Persistence in Mutual Fund Performance", J. of Finance, Vol. 52, No. 1, PP-57-82
2. **Almazan A., Keith C.B., (2004),** "Why Constrain Your Mutual Fund Manager?" J. of Financial Economics
3. **Berk J.B. and Green R.C., (2004),** "Mutual Fund Flows and Performance in Rational Markets", J. of Political Economy
4. **Malkiel B.G., (1995),** "Returns from Investing in Equity Mutual Funds ", J. of Finance, 50(2), pp-542-572
5. **Elton E.G., (1996),** "The Persistence of Risk Adjusted Mutual Fund Performance", J. of Business, 69(2), pp-133-157
6. **Dalquist M., Engstroem S. and Soederlind P., (2000),** "Performance and Characteristics of Swedish Mutual Funds", J. of Financial Quantitative Analysis,
7. **Rao K.L.,(2011),** "Analysis of Individual Investors' Behaviour towards Mutual Fund Schemes ", J. of Banking Financial Services and Insurance Research, VOL. 1, Issue-7, 65
8. **Michael J.T., (2009),** "Use of Interest Rate Derivatives by S.S. Based Domestic and Global Bond Mutual Funds", J. of Management Research, Vol. 1(2), 6
9. **James E., Ferrier G. and James S., (2009),** "Mutual Funds and Institutional Investments: What is most efficient ways to to Set up Individual Accounts in a Social Security System", World Bank Policy Research Paper
10. **Tufano P. and Sevick M., (1997),** "Board Structure and Fee Setting in the Us Mutual Fund Industry", Journal of Financial Economics, 46, pp-321-55
11. **Sirri E.R. and Tufano P. , (1993),** " Competition and Change in the Mutual Fund Industry", Financial Series Samuel B. ,Harvard Business School
12. **Chordia T., (1996), "** The Structure of Mutual Fund Charges ", J. of Financial Economics, Vol. 41, pp-3-39

CHAPTER-14

LAW, INCOME AND CHILD LABOUR IN SOUTH ASIA

July 2012 international conference, held in Washington, reconfirmed "**slowing down of the global pace of reduction of child labour**." The reason behind it was the breaking down of the socio-economic conditions of the world, in general and of the South Asia, in the particular. Therefore, the goal of the UNO to "**Secure Right of Child**" and "**Decent Work for All**" has been retargeted to achieve in 2016 rather than in 2015.

South Asia shares more than fifty per cent of the world child labour with the highest intensity in the agriculture which is the source of food and employment. India, Pakistan, Bangladesh, Sri Lanka and Nepal are characterized with the highest concentration of labour force in this sector with declining share of agriculture in GDP. All these facts suggest applying **Lewis theory** to transfer labour from agriculture to industry but **South Asia has failed.** What steps have been taken yet, in this direction, needs literature review?

LITERATURE REVIEW

The pace of quantum change of the child labour depends on national policies and actions in the area of eradication of child labour (**Miriam, 2003**). National actions should be directed towards raising of awareness regarding negative effects of the child labour (**Olivelra, 2003**).There should be penal provision of country's law for banning child labour(**Mehrotra and Biggeri, 2002).** Hiring a live-in person to undertake domestic household chores is an integral part of South Asian tradition (**Sharma, 2001).** If law and actions do not work for combating child labour through raising income, government fails. Indian Government has failed to free the bonded child labour that is bound to work in the exchange for a loan to his family (**Coursen, 2003**). Therefore, Poverty and income stability are key determinants of children's work **(Dalep, 2010).** Poverty is the major cause of child labour **(Maitra and Ray, 2010**). Child labour falls with rise in GDP per capita (**Joelle, 2010).** Poverty alone is not the only factor but there are some other factors that compel children to work **(Heather, 2011).**

The above literature reviews suggest that Child labour exists mostly in the country which is poor. Therefore, one should go through the socio-economic conditions of South Asian countries. **Table-1** shows these conditions showing population, number of children, literacy rate, enrolment ration, per capita GDP and poverty ratio. It clearly infers that poverty exists in the South Asia which is characterized with concentration of labour force along with declining share of agriculture in GDP despite having agriculturally dominated area.

No literature is available showing law, income and child labour in an area which is characterised with concentration of labour force in agriculture along with declining share in GDP without labour transfer from agriculture to industry. Therefore, the present study has been carried out to find out the solution to combat child labour in South Asia, meeting above characteristics.

The present study has been divided in **four parts.** First part deals with **Quantum of child** labour in South Asia. Second part delves with **country's law** followed in South Asia. Third part shows a **model** how country's law combats child labour. Fourth part describes about **conclusion and policy implication.**

Part-I: Quantum of Child Labour in South Asia

South Asia comprises 216.85 Lacs child Labourers which is 7.36 per cent of total children and 1.56 per cent of its total population (13870 Lacs) as shown in **table-2.** Sri Lanka comprises lowest proportion of children (age ranges between 5-14 years) as well as child labour available in South Asia while this proportion is highest for India. The ILO study of the intra country child labour shows that India shares only 6.00 per cent as child labour in total number of children. This figure is almost one-third of India for Sri Lanka. It infers that Child labour gets affected not only by population but other factors also.

Table-1: Socioeconomic characteristics of South Asian countries in 2008

Socioeconomic Conditions	**Sri Lanka**	**Pakistan**	**India**	**Nepal**	**Bangladesh**
Population (mn)	19.1	168	1134	27	153
Children (5-14 years) Lacs	31.80	400	2100	62.25	350.60
Literacy rate of youth (15-24 years age) in %	95.6	65.1	76.4	70.1	63.6
Net Primary **enrolment ratio** (%) male:female	98:97	74:57	90:87	91:87	87:91
Per capita GDP (US $)	4595	2370	3452	1550	2050
Below **Poverty** Line population (%)	25.0	32.6	28.6	42.0	49.8

Source: 1. UNDP *Human Development Report 2008*

2. ILO. International Programme on the Elimination of Child Labour

Table-2: Magnitude of Child Labour in South Asia (Lacs) as a proportion of Total Children (5-14 years of age group)

Country	**Total no. of children (TC)**	**Child Labour (CL)**	**CL as % of TC**
Sri Lanka	31.80 (1.10)	4.75 (2.05)	14.94
Pakistan	400.0 (13.58)	33.0 (14.29)	8.25
India	2100.0 (71.31)	126.0 (54.58)	6.00
Nepal	62.25 (2.11)	16.60 (7.19)	26.66
Bangladesh	350.60 (11.90)	50.50 (21.89)	14.40
Total	2944.65 (100)	230.85 (100)	7.36

Source: 1. Bangladesh Bureau of Statistics; Report on National Child Labour Survey 2002/2003, ILO , Baseline Survey on Child Labour in Bangladesh, 2006

2. Registrar General, Government of India: Census of India, 2001

3. Report from Migration and Employment, Nepal, 1997

4. Federal Bureau of Statistics, Pakistan, 1996

5. Department of Census and Statistics, Sri Lanka, 1999

6. ILO, International Programme on the Elimination of Child Labour

It would be better to know factors generating Child Labour separately for all countries as well as follows-

1. Major factors responsible for Child Labour in **Pakistan**

(a) High population growth rate with average family size of eight.

(b) Popularity of subsistence agricultural activities which provide livelihood to three - fourths part of total population.

(c) High poverty and low productivity per labour

(d) Comparatively smaller number of educational facilities than requirements

(e) Discriminatory social attitude between girls and boys to have education

2. Major factors responsible for Child Labour in **Bangladesh**

(a) Vicious cycle of parental poverty

(b) Rapid growth rate of population

(c) Lack of enforcement of minimum wage

(d) Low quality of education

(e) Lack of enforcement of legal provisions

(f) Gender discrimination

3. Major factors responsible for Child Labour in **Sri Lanka**

(a) One-fifth of total population belongs to below poverty line.

(b) Lack of sufficient number of schools to meet the demand

(c) Girls are forced to stay home

(d) Lack of support and guidance from parents.

4. Major factors responsible for Child Labour in **Nepal**

(a) Lack of enforcement of legal provision

(b) Parental poverty and subsistence livelihood

(c) Illiteracy of parents

(d) Low perceived value of education

(e) Civil war. Parents send their children to work in urban areas for fear of them being caught in cross –fire or victim of Maoists.

5. Major factors responsible for Child Labour in **India**

(a) Parental poverty and illiteracy

(b) Lack of enforcement of legal activities

(c) Discrimination between male and female child

(d) Dependency of parents on agriculture for livelihood

(e) High growth of population

(f) Less number of schools and infrastructure

From above one can easily entail that there are number of factors responsible for generating Child Labour in the South Asia. **First**, there is **parental poverty** almost in all countries of the South Asia. **Second**, **illiteracy** is common to all South Asian countries. **Third**, existed **social and economic** circumstances encourage having more number of children. **Fourth**, lack of access to basic and meaningful **qualitative educational** facilities deprive children to have even primary education.

Part-II: Constitutional Protection

In the era of global economic liberalization, the motive of corporate has been diversified from welfare to profit generating. Particularly for this sector, Child Labour has become a source of profit at the cost of socio-economic welfare of the global economies. In this case, Constitutional protection of Child Labour is required to save the social as well as economic welfare of the global economy. In the present study, an effort has been made on **three types (ILO, SAARC and Government) of constitutional protections** of Child Labour in South Asia.

I. ILO Constitutional Protection

UN millennium goal is to "**securing rights for children"** and to provide "**Decent Work for All**" by 2015. In this connection, ILO takes Child Labour not an isolated issue but as an integral part of national efforts for economic and social development. The following major steps are taken by the ILO to get this goal-

(a) ILO convention no. 05 **(1919):** In the first International Labour Conference, the minimum age of child to work in industry was decided.

(b) ILO convention no. 29 **(1930):** Adopted first Forced Labour Convention.

(c) ILO Abolition of Forced Labour Convention no. 105 **(1957)**

(d) ILO convention no. 138 **(1973):** Minimum age of child labour was decided.

(e) UN Convention on the Rights of the Child (UNCRC)-**1989**

(f) International Programme on the Elimination of Child Labour (IPEC, **1992):** awareness programmes were organized in all South Asian countries regarding prevention of Chil Labour and resettlement of rehabilitated children.

(g) Stockholm declaration (**1996**): Child Labour was declared as a crime.

(h) ILO declaration on Fundamental Principles and Right at Work (**1998):** Four major steps were taken in this declaration-freedom of association, abolition of forced labour, end of discrimination in the workplace and elimination of child labour.

(i) ILO Worst Forms of Child Labour Convention no.182 **(1999):** focused on eradication of child labour working in hazardous industries which are damaging them physically, mentally or morally.

(j) Prevention of trafficking of Child Labour-2**000**

(k) World Day against Child Labour **(2002):** 12th June has been declared as world Day against Child Labour.

(l) Global Economic Study on the costs and benefits of eliminating Child Labour **(2004)** : Through combating Child Labour , the benefit can be raised seven times more than cost and hence global benefit will be US$ 5.1 Trillion.

Despite these efforts made by ILO, All South Asian countries have not taken it seriously to combat Child Labour as shown in table-6. Sri Lanka has ratified all five conventions while India has only three Conventions to combat child labour.

Table-6: ILO conventions on Child Labour and their ratification status in South Asia

Country	**ILO convention no. 138**	**ILO convention no. 182**	**ILO convention no. 29**	**ILO convention no. 105**	**UNCRC**
Sri Lanka	√	√	√	√	√
Pakistan	√	√	√	√	√
India			√	√	√
Nepal	√	√	√		√
Bangladesh		√	√	√	√

Source: ILO, International Programme on Elimination of Child Labour

Note: UNCRC-United Nations Convention on the Rights of the Child

II. SAARC Constitutional Protection

Among South Asia countries, Sri Lanka is the only one which has ratified all ILO Conventions related to combating Child Labour. **Colombo Resolution (1992, SAARC), Rawalpindi Resolution (1996, SAARC)** and **Male Resolution (1997, SAARC)** made pathways to reach milestone of **Kathmandu Resolution (2002, SAARC**). During the 11th SAARC summit (January, 2002) in Kathmandu, all SAARC members (Bangladesh, India, Nepal, Pakistan, Sri Lanka, Bhutan and Maldives) undertook following steps to eradicate Child Labour.

(a) The SAARC convention on preventing and combating the Trafficking in women and children for prostitution.

(b) The SAARC convention on Regional Arrangements for the promotion of child welfare in South Asian countries.

On the basis of these two conventions, the SAARC members developed Regional plans of action to eradicate Child Labour.

III. Government Constitutional Protection

The respective governments with combined efforts of ILO or UNICEF or NGOs took various steps to combat Child Labour.

Pakistan:

(1) **Article 11(1)** of the constitution of Pakistan forbids slavery and states that no law permits or facilitates its introduction into Pakistan in any form. **Article 11(2)** prohibits all forms of forced labour and traffic in human beings. **Article 11 (3)** prohibits employment of children below 14 years of age.

(2) The Employment of **Children Act (1991)** prohibits employment of children in any organized sector, particularly in hazardous industry.

(3) The **Bonded Labour System Abolition Act (1992)** abolishes bonded labour with immediate effect.

(4) The Prevention and Control of **Human Trafficking Ordinance (2002)** defines human trafficking as buying or selling a person for exploitative entertainment. In this case parents and any person involved in trafficking are liable to get punishment of seven years.

(5) The National Policy and Plan of **Action (2002)** prevents Child Labour by offering alternate education and ensuring primary education and skills training to the target children.

(6) The Government of Pakistan has established a Fund for the education of working children and rehabilitation of freed bonded labour.

(7) The Government **Reduction Strategy Paper (2003)** of Pakistan gives due consideration to the issue of child labour through Poverty eradication.

(8) The Ministry of Education launched the National Plan of Action for education for all **(2003)** for achieving universal primary education by 2015.

(9) The National Commission for Child Welfare and Development has initiated a national pilot project for rehabilitation of children involved in labour.

Bangladesh:

(1) Both the Employment of **Children Act (1938)** and **Factories Act (1965)** prohibit employment of children under 12 and 18 years of age respectively.
(2) In 1990, Bangladesh passed the Primary Education Act.
(3) In 1993, it made compulsory primary education for the children of 6 or above years old.
(4) The preparatory phase of the **Time-Bound Programme** has been launched in March 2004.

Sri Lanka:

(1) Under the Constitution of Sri Lanka, 1978, **Article 27 (13)** the Government promotes special care for the interest of children to ensure employment.
(2) The Draft Constitution (2000), **Article 22** protects children from abuse to have free education.
(3) **Section 360** of the Penal Code stops (a) prostitution and sexual abuses of children , (b) forced labour (c) removal of organs of children (d) child trafficking
(4) School attendance became compulsory w.e.f. 1997 regulation of Education.
(5) President **Task Force (1996**) controls Child Labour.
(6) **National Child Protection Authority (1999)** rehabilitates protected child.

Nepal:

(1) The Constitution of Nepal confers fundamental right to education to children.
(2) **Children's Act (1992)** protects the rights and interests of Nepalese children and ensures their physical, mental and intellectual development.
(3) The **Labour Act (1992) and Labour Rules (1993**) prohibit employment of children in any hazardous industries.
(4) The **Child Labour Prohibition and Regulation Act (1999)** makes provision for punishment to employers of children.
(5) Citizen's **Right Act (1955)** stops child trafficking.

India:

A number of constitutional protections have been given to child labour in India. These are enumerated as well as below:

(1) ***Indian Factory Act (IFA, 1881)***: It fixed the minimum age of employment at seven and maximum no. of working hours at nine per day with four months holidays in a year. IFA-1891 & 1954 disallowed the employment of children during night time.

(2) ***Whitely Commission (1929):*** Rege Committee (1944) and Gurupadswamy Committee (1979) recommended regulating child labour. Based on these committees, child labour Prohibition and Regulation Act was passed by Government of India in 1986.

(3) ***Indian Constitution (1950):*** Article-14, 15, 15(3), 19(1), 21, 21(A), 23, 24, 45, 36-e, 39-f and Directive Principles are certain constitutional protections which are adopted in India to prevent child labour. Through implementation of these constitutional provisions, India reiterates its commitment to the protection, safety and well being of children. Both the article-24 and Directive Principles prohibit the child labour in factories, mines and other hazardous occupations. Article-24 clearly states "**no child below the age of fourteen years shall be employed to work in any factory or mines or in any hazardous employment."** Article-45 makes provision of free & compulsory education for upto 14 years age group of children. Article-39-e lies down that no child be forced by economic necessity to enter unsuited occupations. Article-39-f makes a provision to provide healthy opportunities to children to maintain their dignities.

(4) ***Bonded Labour Abolition Act (1976):*** It purports to abolish all debt agreements and obligations arising out of India's longstanding bonded labour. It orders the economic rehabilitation of freed bonded labourers by the state.

(5) ***Child Labour Prohibition and Regulation Act (1986):*** It bans employment of children working in hazardous occupations. It defines child as a person who has not completed 14 years of age. It lays down penalties for violation of this provision. This Act accepts that chilld labour can not be abolished so long as poverty exists.

(6) ***The National Child Lanbour Policy (1987):*** All the released children from employment in hazardous industries are provided educational services, non-formal, under the centrally sponsored National Child Labour Project (NCLP). It is operational in 100 districts in 13 states, in the areas of high concentration of child labour throughout the country.

(7) ***Ratification of UNCRC -1989 (1992):*** India ratified United Nations Convention on the Right of the Child (UNCRC) in 1992 according to which India is bound to have international standard of children right. It provides following principles for examining the implementation of the convention:- (a) the principle of non-discrimination (Article-2), (b) best interest of the child (Article-3), (c) the right to life, survival and development (Article-6) and (d) respect for the views of the child (Article-12).

(8) ***Unnikrishnan vs State of Andhra Pradesh (1993):*** The Supreme Court of India lays down a provision according to which right to education for children to be considered a fundamental right. It brought state initiatives to educate child labour.

(9) ***M.C.Mehta vs State of Tamilnadu (1996):*** When gross violation of Article-24 takes place due to employment of child labour, Article-32 is imposed to stop child labour. The Supreme Court of India gave direction for immediate identification of children in hazardous occupations and their subsequent rehabilitations, including providing appropriate education to the released children.

(10) ***Ratification of UN convention:*** India has ratified only three conventions namely ILO Convention No.29, 105 and UNCRC.

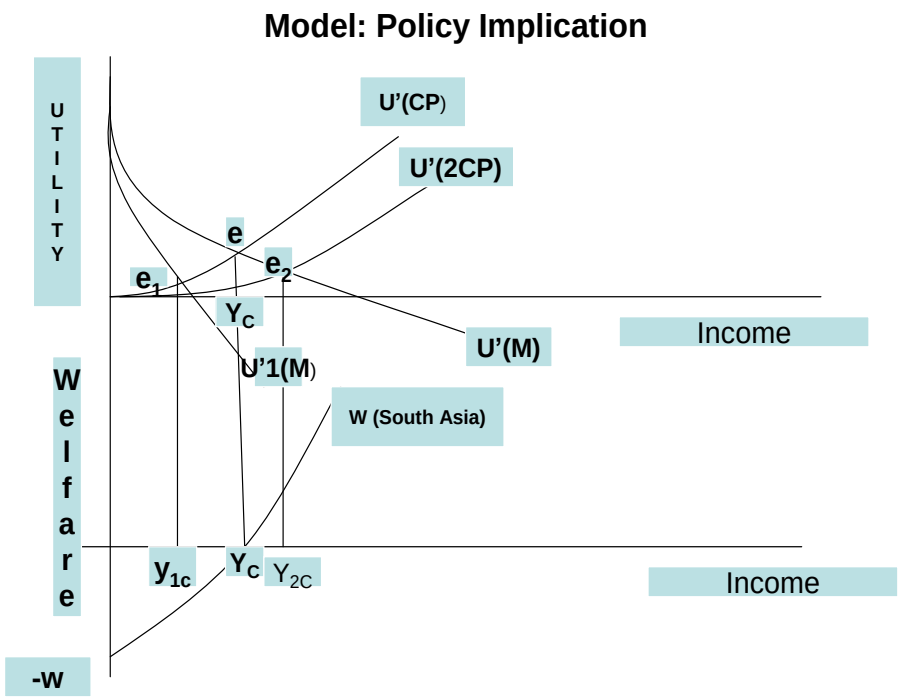
Part-III: Model showing effect of constitutional protection on Quantum of child labour

The effective implementation of the Constitutional Protection (CP) and declining magnitude of Child Labour (M) will raise the welfare (W) of the households of the South Asia (SA). In this case, one can rightly observe that:

$$\mathbf{W\ (SA) = U\ (CP) - U\ (M)}$$

According to **Marshallian** theory, at equilibrium, **W' = 0** and hence **U' (CP) = U' (M).** It shows a critical state of the income distribution, where total welfare will be maximum. However, **U" (CP) > 0** and **U" (M) < 0** infers that second condition of welfare maximization does not exist. It entails that once a critical state of income ($\mathbf{Y_C}$) is achieved, the welfare of the South Asian households is bound to increase with declining magnitude and rising Constitutional Protection.

Graph-1: Model to increase welfare through combating Child Labor



21

The Graph-1 entails following two facts:

(i) When constitutional protection is effectively implemented, the welfare of the household rises because welfare is positively associated with it. It raises human capital through encouraging children to attend school. In this case, **U' (CP)** moves rightward to **U' (2CP)** in

a range where income effect outweighs substitution effect and hence critical income rises to Y_{2C} . It shows that welfare can be raised through raising income of the family.

(ii) A rise in the magnitude of the child labour decreases welfare of the household. In this case, **U' (M)** shifts downward to **U' (1M)** at e_1 in a range where substitution effect outweighs income effect and hence it encourages parents to send their children to work because critical income declines. It further raises child labour.

Criticism of Constitutional Protections

Despite efforts made through constitutional enforcement, there exists child labour exploitation in South Asia due to following **flaws**.

(1) Almost all laws, in practice, are enforced only in organized sector where only 8 per cent of total child labourers are employed. It ignores unorganized sector where 92 per cent of total child labourers are employed.

(2) So long as the child is not forced to work in an exploitative environment, the state does not take legal action.

(3) The Act provides a list of hazardous occupations. It does not define what constitutes hazardous work (except 1936 Indian Factory Act.).

(4) It does not clarify what the child labour should happen once the employer is prosecuted. However, after the initiative of the Supreme Court of India a provision of rehabilitation of child labour has been started but separate budgetary provision has not been made yet.

(5) Under the law, the employer is supposed to notify the Labour Department of any children working in the establishment. This is akin to asking the murderer to report the crime.

(6) The implementation of Act depends on ill-equipped state's bureaucratic machinery.

(7) The education of the child is important more for society rather than parents. Therefore, law empowers state to take punitive actions against parents who do not send their children to school. In practice, law should empower parents to do so.

(8) Illiteracy is common in South Asian countries. It is a hurdle in getting benefits of constitutional protections.

(9) Fees and fines charged to employers for violating law is a small part of profit generated by employing Child Labour. It encourages employers to employ Child Labour.

(10) Constitutional Protections are unable to encourage political wills to combat Child Labour.

CONCLUSION AND POLICY IMPLICATION

Law of South Asia passes on the responsibility of combating child labour from society or nation to parents. Parental income in South Asia is not sufficient to meet out the children's needs. Therefore, rather to pass on the responsibility from nation to parents, it should be collectively carried out because children are the assets of the parents, society and nation as whole.

REFERENCES

1. **Coursen N. and Zama N. (2003),** "Small Change: Bonded Child Labour in India's Silk Industry", Human Right Watch Publications, Vol. 15, No. 2
2. **Dalep E. (2010),** "Economic and Cultural Forces in the Child Labour Debate: Evidence from Urban Bangladesh ", *Journal of Development Studies,* Vol. 37, Issue-4, pp-1-22
3. **Heather C.F. (2011),** "Child Labour: A Review of Recent Theory and Evidence with Policy Implications", *Journal of Economic Survey*, Vol. 25, Issue-2, p-234
4. **Joelle S.L. (2010),** "A Cross National Study of Child Labour and its Determinants", *the Journal of Developing Areas,* Vol. 44, No. 1, pp-325-344
5. **Maitra P. and Ray R. (2010),** "The Joint Estimation of Child Participation in Schooling and Employment", OXFORD, Vol.30, pp-41-62
6. **Mehrotra S. and Biggeri M. (2002),** *The Subterranean Child Labour Force: Subcontracted home based manufacturing in Asia,* UNICEF, P-73
7. **Mirium, B. (2003),** Quantitative *study on Child labour in Guatemala: Final Report,* ILO, P-96
8. **Olivelra A.M. (2003**), *National Survey on Child and Adolescent Labour in Nicaragua*, ILO, P-148
9. **Sharma S. (2001),** *Nepal Situation of domestic Child Labour in Kathmandu: A Rapid Assessment,* ILO, P-153

CHAPTER-15
SUMMARY

Fund is allocated among different financial products to earn. It is invested either in stock market or in bank or in real estate. The present book makes an effort to show that most of the investors invest in debt fund to minimize low risk in India in deregulate regime. Debt fund is able to provide economies to scale benefit to retail investors through minimizing transaction costs and better market accessibility. It pools the retail investor's money which is managed by fund managers to maximize the yields. In this case, the investors do not have to pay transaction and brokerage fees as paid as in demat account. It provides the trained, skilled, well informed professionals who understand the linkages between different markets and its dynamism. Funds manager is able to hedge the portfolios using options and powerful techniques. For the said reasons, Indian banks prefer debt rather to equity fund.

In deregulated regime since 1991, the rate of inflation is high enough to reduce the real return. Throughout the deregulated regime shows positive difference between fixed deposit and sensex return suggesting FD scheme to be opted.

Investors have either to invest in equity fund or in debt fund. Risk takers having high income should invest in equity fund and risk averter having fixed and low income should invest in debt fund. Middle income group should take less risk and should invest in debt fund whose expense ratio is low. Middle income group should take less risk and should invest in debt fund whose expense ratio is low.

Deregulation of interest rate on saving account deposit increases the efficacy of monetary policy. Correlation co-efficient between interest rate on saving deposit (SAD) and ARL is less than that of TAD. Therefore, it is suggested that monetary policy can be transmitted in better ways with SAD because it is less elastic.

The share of saving account deposit in total deposit is inversely related with interest rate differential. It suggests that **widening of IRD leads to reduction in the share of SAD in total deposit**. It shows that amount of saving deposit responses the interest rate given on

SAD. SAD is less elastic than TAD and hence monetary policy can be penetrated in better ways with SAD rather than TAD.

The level of competition is directly associated with the spread rate. In most of the cases the spread rate in SAD in India is negative as shown as in table-1 and figure-1. Therefore it is suggested that competition level among banks can be raised by raising the spread rate in SAD over both the Repo and Reverse Repo rate.

Financial inclusion should be extended to agriculture in banking finance to increase business farm income, to earn more net factor income from abroad, to decrease poverty, to provide liquidity on demand, save peasants from exploitation, to control inflation, to generate their feelings and contribution in economic growth of the nation and to collect small savings.

If inflation rate is taken into consideration, the real gain to account holders becomes negative. It is so because of regulated regime in which households are asked either to deposit or leave. It **discourages small savings** and it is in against the **financial inclusion** of poor households especially in rural areas. Therefore, it is suggested to deregulate the interest rate to enhance the real gain to consumer by improving the level of competitions among banks.

Consumption expenditure and poverty are interlinked which reveals to increase consumption expenditure of poor basket of society through government intervention rather than expenditure tax because it is not effective on black or hidden money.

Investors have two options to invest either in equity or in debt fund. The Indian financial institutions chose debt fund. More than two-third of total collected funds by Scheduled Commercial Banks has been allocated to debt fund. It raises their net profit.

Mutual fund gives two options two be invested- equity and debt funds. Equity fund is volatile and highly risky but it gives comparatively more return to investors. Debt fund is less risky, less volatile but gives comparatively low return.

.

About the Author

Shakti kumar is currently working as Assistant Professor in the Department of Economics and Rural Development, Dr. R.M.L. Avadh University, Faizabad (Uttar Pradesh). He was Lecturer in Ramjas College, University of Delhi. He did his graduation from St.Stephens College, University of Delhi., Post Graduation from C.E.S.P. (JNU, New Delhi), M.Phil from C.S.R.D. ((JNU, New Delhi) and Ph.D. from C.S.R.D.(JNU, New Delhi). He qualified UGC- JRF. His special interest is in Mathematical Economics and Money & Banking. He has published research papers in many journals and presented papers in national and international conferences.

ISBN 978-93-81713-30-3

9 789381 713303 >

ISBN: 978-93-81713-30-3

PUBLISHER: PRATIMA PRAKASHAN

PROMOTED BY: ASSOCIATION FOR INNOVATION