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16

SAVING AND INSURANCE

Apart from production and consumption, saving is also a very important economic activity. We all want to lead our present and future life properly. To do so, we produce things and consume them. But if we consume everything today from our production, then nothing will remain to start the activities tomorrow. That is why it is important to consume less than what we produce today. Saving is necessary to keep continuing our production activities in future. But we also know that future is uncertain and unpredictable. Nobody can tell with certainty as to what will happen to our health, life, property etc in future. They must be properly taken care of , so that, the production and consumption activities are carried out smoothly in future. It is in this context that, insurance is necessary to protect life, health, property etc. against any damage.

OBJECTIVES

After completing this lesson, you will be able to:

- *understand the meaning of and need for saving;*
- *explain the use of saving;*
- *understand the concept of interest;*
- *know the meaning of insurance and its need;*
- *acquaint yourself with Life Insurance, Health Insurance and Automobile Insurance.*

16.1 MEANING OF SAVING

Actually people earn money to fulfill both their present and future needs. If they spend their whole income today then nothing will remain for future and then they won't be able to satisfy their wants tomorrow. But if there is saving, then it can be used in future. So saving is the amount of income which is carried forward to future after meeting the current expenditure on goods and services and other things. This means that saving is the surplus of income over consumption. We can write that

$$\text{Saving} = \text{Income} - \text{Consumption}$$

Study the table 16.1 given below. The table gives the statement of income and expenditure of a person, say Mr. X, on monthly basis for a year. See that we have started with the month April and ended with the month March. This is because, in India, accounting year spans from April of this year to March of next year.

Table 16.1 Income and Expenditure of Mr. X on monthly basis for last Year

Month	Income (Rs.)	Expenditure (Rs.)	Saving (Rs.)
April	15,500	14,300	1200
May	15,500	15,000	500
June	15,500	15,500	0
July	15,500	15,500	0
August	15,500	15,500	0
September	15,500	15,000	500
October	15,500	14,000	1500
November	15,500	15,500	0
December	15,500	15,000	500
January	15,500	15,300	200
February	15,500	15,400	100
March	15,500	15,000	500
Total	**1,86,000**	**1,81,000**	**5,000**

You see that last year's total income of Mr. X was Rs.1,86,00. His total expenditure was Rs. 1,81,000. So he saved Rs. 5,000 last year, i.e

$$1{,}86{,}000 - 1{,}81{,}000 = \text{Rs.}5000$$

Note that, we have taken into account the whole accounting year and not one or two months, to calculate saving. This is because, there are some expenditures which are made towards the end of the year and not necessarily every month. For example, we spend money on food, daily use goods etc. regularly. But expenditure on fees, tax to government etc. are calculated on yearly basis. So, it is better to take income and expenditure of the whole year to calculate saving.

16.2 HOW SAVING IS USEFUL?

Saving is useful in the following ways.

(i) Start from the last example. Mr. X saved Rs.5000 last year. This implies that, in the beginning of the current year he starts with an extra Rs. 5000. So his income will increase by at least Rs.5000 this year, provided his income and expenditure do not change. This means that, saving increases the future income of the person.

(ii) Saving can act as a kind of security for future. How? Suppose Mr.X falls ill in the beginning of this year. So he could not go to work for a week. How he can sustain for a week? There is no need to worry. He can always use his last year's saving to carry on for some time till he recovers from illness and start going to work and earn again.

INTEXT QUESTIONS 16.1

1. Define Saving?
2. If income is 1000 and saving is 200 then what is the amount of consumption?

16.3 WHERE YOU KEEP YOUR SAVING

It is a common practice in almost every household that, coins and currency notes of small denominations such as 50 paisa, Re.1, Rs. 2 are put in a small saving box. All the members of the household find pleasure in contributing to this mini saving activity. After some time, say a month or some months, when the box is opened, the family finds good amount of money existing in the box which becomes very useful to buy some new thing. It is a kind of tradition for families to have such a saving box.

A family saving box is an informal way of saving. It cannot be used for saving a big amount. It is also not safe to keep money in this manner because of the threat of theft. The money kept in the box also remains idle or unused till the time box is opened. Since it is a private affair, nobody else, except the particular family can use it. Finally, no reward is given in return for saving in this manner.

The most important thing is that, money needs a secured place to be kept. It is also needed for use. It should not be left idle. Think that you have a saving of Rs. 5000. If you do not use it for a long period, then it remains idle and useless like a dead wood. Your are neither using it for yourself nor are you allowing anybody. Keeping all these things in mind society has provided institutions where you can keep your savings. They are post offices and commercial banks.

16.3.1 Post Office Savings Bank

Any individual can keep his/her unspent money in post office saving bank. You can find a post office in almost every locality. So it is close to anybody's reach. Any citizen of the country can open an account in his/her name in any post office by depositing a minimum Rs. 50 only. A person can keep money for any period of time and he/she is allowed to withdraw any amount from his/her account at any time subject to the condition that a minimum balance of Rs. 50 is left in the account. A pass book is provided by the post office to keep record of the transactions made by the holder of the account holder. The post office also allows a nominal rate of interest on saving bank account. If a person wants to issue a cheque book, then he/she has to keep a minimum balance of Rs. 500 in his/her account.

16.3.2 Savings Account in Commercial Bank

We have already said that commercial banks accept deposits from the public. An individual who wants to save money can open a saving account in the bank. The minimum amount necessary to open an account and minimum balance to be left after withdrawal of money are prescribed by the concerned bank where the person saves money. Like the post office, a bank also provides a pass book to the depositor which shows details of deposits and withdrawals and the balance available. A commercial bank allows a nominal rate of interest on the saving bank account.

16.4 USES OF SAVING

Savings can be used for the purposes of lending and borrowing as well as development of the economy.

(i) Lending and Borrowing

A person, who saves, can become a lender, because he has surplus money available with him presently. Many people in the society want to consume more than what their present income could allow for various reasons. These people can borrow money at the time of need and repay it in future.

(ii) Development of the Economy

When many individuals save money in post offices and banks, a very large amount of money becomes available for use by the society. We know that small drops taken together make an ocean. Similarly, an individual may be saving very less depending on how much he is earning and how much he is spending. But when many individuals start saving, they are added together to make a large amount. For a society, a large amount of money is required to build roads, office buildings, railway stations, street lights, amusement parks, schools etc. Because of this the whole country is benefited in future. So saving by an individual eventually becomes useful in the process of development of the economy.

16.5 INTEREST AS RETURN ON SAVING

One can use his/her saving to earn money which is called return on saving. This return is termed as Interest. How does this become possible? We know that a person who has saved money can become a lender by providing that money to a borrower who wants to borrow now. For the use of this saving, the lender can charge some money from the borrower which is called interest earned by the lender and paid by the borrower. Normally the borrower pays back the lender's money (his saving) along with the interest money on a specified future date. Note that when a borrower takes money from a lender, we say that the lender provided loan to the borrower. This means that when a lender gives his/her saving to a borrower then it is converted into a loan. The loan amount has to be returned by the borrower to the lender in future along with interest.

Example: Let Ms. Sarita has a saving of Rs.1000. Mr.Aashish wanted to borrow that money. So Sarita became a lender and Aashish, a borrower. It was decided that, Aashish would have to repay the loan amount of Rs.1000 to Sarita after a year. It was also decided that Ashish will have to pay Rs.120 as interest. Accordingly, after a year, Aashish paid a total sum of Rs.1120 (1000+120) to Sarita. Hence, by lending her saving, Sarita earned Rs.120 as interest on her saving besides getting back the same amount she saved.

16.5.1 Rate of interest

Now a question arises- how much amount did Sarita earn for every 100 Rupees she gave to Aashish?

Ans. Sarita gave Rs.1000 as loan to Aashish for a year.. She earned Rs.120 on this amount. So earning on Rs.100 = 120 × 100/1000 = Rs.12.

Hence Sarita earned Rs.12 per Rs.100 as interest, i.e 12% per year.

When we find value out of 100, we call it percentage. Hence, we can say that Sarita earned at a rate of 12 percent per year. This 12% per year is called the rate of interest paid by the borrower, (Aashish) and received by the lender, (Sarita). Rs.120 is the total interest money on the loan amount of Rs.1000. This loan amount is also called the Principal amoumt.

Rate of interest is defined as the earning by the lender/payment by the borrower for the use of every 100 Rupees given by the lender to the borrower for a period of one year.

16.5.2

Since people keep their savings in the post offices and banks, they receive interest. The Post office offers around 3.5 percent rate of interest while bank offers around

4 percent rate of interest per year to individuals. When you receive interest on your savings in a post office or bank, your money grows. Hence when money is saved today, it grows to a higher amount tomorrow.

INTEXT QUESTIONS 16.2

1. Define rate of interest?
2. Distinguish between lender and borrower?
3. What is the rate of interest if you earn Rs. 20 in a month by lending Rs. 200?

ACTIVITY

Visit your nearby post office and enquire about opening of a saving bank account?

16.6 INSURANCE

We are living in a world of uncertainty. This means we do not know what will happen in future. Many things are not in our control. Take the following examples.

(a) A farmer depends on a good rainfall so that he can produce large quantity of grains. But the farmer has no control over rainfall. If there is good rainfall he gets good crop. But if there is no rainfall there will be drought and the farmer will incur heavy loss.

(b) People have houses in which they live. But they do not have any control over some untoward incident that may take place, such as fire, theft causing loss to the property.

(c) Now a days lots of people have automobiles in the form of two wheelers and cars. As the number of vehicles has increased, number of theft cases or accidents on roads has also increased. No body can predict about accidents which cause damage and loss.

(d) We all fall ill and incur expenditure on medical treatment. No body can predict when illness will come. Due to illness we cannot work. Because of this, we may lose our earnings during the period of illness.

In this way a lot of examples of uncertainties can be given. Interestingly, winning a lottery is also uncertain. This is an unexpected gain. However, the loss of earning or damage to property occurring due to uncertainty is a matter of concern. Uncertainty involves risk of loss or damage. We can take precautions to some extent but it is not possible to avoid them totally.

Whoever suffers a loss due to the reasons as said above, he/she would like to be compensated in monetary terms either fully or partially for that loss or damage. Insurance ensures some compensation against loss/damage to the person concerned.

Insurance is just like a good or product. Anybody who thinks that he/ she has some chance to incur loss/ suffer damages to his/her belongings, he/she can have "insurance" by paying some money. The seller of 'insurance' is called "insurer" and buyer of insurance is called "insured". The money paid by the "insured" or buyer of insurance is called "premium". Normally the premium is paid for a specified number of years. If any loss occures during this period then the insured person get due compensation from the insurer.

Definition of Insurance

Insurance can be defined as **a financial product which can be purchased to partly or fully recovered any loss happening due to event beyond the control of the insured party.**

Normally the seller of insurance is a insurance company. When the insured person incurs any loss, the insurance company pays back some amount of money to compensate him/her for the loss. This is called insurance claim. Hence insurance allows a person to reduce risk due to uncertainty.

INTEXT QUESTIONS 16.3

1. Differentiate between insurer and insured?
2. Give two examples of uncertainty?
3. Is insurance a product?

16.7 SOME SELECTED INSURANCE PRODUCTS

Let us discuss in brief the following insurance products

(i) Auto Insurance

(ii) Health Insurance

(iii) Life Insurance

(i) Auto Insurance

People who have scooters, bikes, cars etc. can buy auto insurance from a concerned insurance company. Since automobile is a durable good and has a long life span, say 10 to 15 years, the insurance policy is made in the following way.

(a) In the first year, the auto is new. So the insurance company charges higher money as premium from the insured person.

(b) In subsequent years, the vehicle becomes old and its value falls gradually. So the company will charge less premium from the insured person.

(c) Whenever there is any damage caused to the automobile, the company gives the claim calculated on the basis of terms and conditions mentioned in the insurance policy.

(ii) Health Insurance

Under health insurance scheme, a person who buys this insurance, can get back some amount of money out of his/her total expenditure on medical treatment. In this case also, the insurance company asks the interested person to pay a nominal amount as premium every year. Whenever the insured person falls ill and spends money on medical treatment, the insurance company gives some amount to reduce the burden of the person. Normally the premium is low, if a person buys the health insurance at a younger age. The premium amount increases as the person grows older.

(iii) Life Insurance

A person can buy life insurance for a particular time period. The time period could be 10 or 25 years. Every year the insured person has to pay a certain amount of premium to the insurance company. The company gives back the claim to the person after the time period is over. The amount can also be paid in installments by the insurance company on yearly basis also. If the person dies in between, the claim is given to his/her nominee, whom the person had named while buying life insurance.

WHAT YOU HAVE LEARNT

- Saving is the income which remains after consumption.
- People save for security in future and to earn interest on their saving.
- Lender is the person who has saved money and gives it to borrower as loan at some rate of interest.
- Borrower is the person who borrows money by paying the interest rate.
- People save their money in post offices and banks.
- Insurance is a product which people buy to reduce the risk of loss or damage to their life, health, automobiles etc.

TERMINAL EXERCISE

1. Define saving? Give two of its uses?
2. How saving is calculated? Why do people save?
3. Write a short note on post office saving bank?
4. Why people buy insurance?
5. Explain auto insurance?
6. Distinguish between health and life insurance?

ANSWERS TO INTEXT QUESTIONS

Intext Questions 16.1

1. Saving is defined as surplus of income over consumption.
2. 800

Intext Questions 16.2

1. Rate of interest is the payment made by the borrower for use of every 100 rupees given by the lender for one year.
2. Lender – The person or institution who gives money on loan.

   Borrower – The person or institution who takes money on loan from the lender.
3. 120 per cent

Intext Questions 16.3

1. Insurer is the seller of insurance.

   Insured is the buyer of insurance.
2. drought, illness
3. yes

MODULE-6

PRESENTATION AND ANALYSIS OF DATA IN ECONOMICS

17. Collection and Presentation of Data
18. Analysis of Data