International Journal of Science and Research (IJSR)
ISSN (Online): 2319-7064
Index Copernicus Value (2013): 6.14 | Impact Factor (2013): 4.438

Investment and its Role in Economic Development

Sangeetha D.

Assistant Professor – GRG School of Management Studies, Coimbatore, India

Abstract: ***The Indian economy is likely to expand by 6.4 percent in 2015 as compared to 5.5 percent last year. "The positive outlook is mainly led by an increase in growth in India," the UN Economic and Social Commission for Asia and the Pacific (ESCAP) said in its 'Survey of Asia and the Pacific 2014: Year-end Update'. Attainment of this is possible with the contribution of investment by the public and the industries. This study focuses on the problems related to investment and financial forecasting in our country and its relation to the economic growth. The study also enumerates the factors which will help in providing the solutions for the problems faced.***

Keywords: Household savings, Investment, Savings, Economic growth and Risky assets

1. Introduction

One of the way in which we connect the future is through investments. Investment is the planning what secures most of the people from the uncertainty of future. In finance, an investment is a monetary asset purchased with the idea that the asset will provide income in the future or appreciate and be sold at a higher price. Today‘s earnings sacrificed for tomorrows living is called Investment. Investment plays a crucial role which differentiates the developed, developing and underdeveloped countries. Investments will definitely act as an indicator to project the GDP, Inflation, WPI, National income, etc., of a country, that is why developing countries like India is accepting Foreign Direct Investment into the country though many people, political parties inside the country are against it. The developing countries like India face the enormous task of finding sufficient capital in their development efforts. Most of these countries find it difficult to get out of the -vicious circle of poverty of low income, low saving, low investment, low employment etc. With high capital output ratio, India needs very high rates of saving and investments to make a leap forward in her efforts of attaining high levels of growth. Household savings plays a vital role in the contribution of investment. Household disposable income consists essentially of income from employment and from the operation of unincorporated enterprises, plus receipts of interest, dividends and social benefits minus payments of current taxes, interest and social contributions.

2. Significance of the Study

As Rao (1980)' has rightly pointed out, "increase in saving, use of increased saving for increased capital formation, use of increased capital formation for increased saving for a further increase in capital formation constituted the strategy behind economic growth. This study will enhance in knowing the importance of financial investment, what percentage and where it has to be invested and also its relation to the growth of the Indian economy.

3. Types of investment

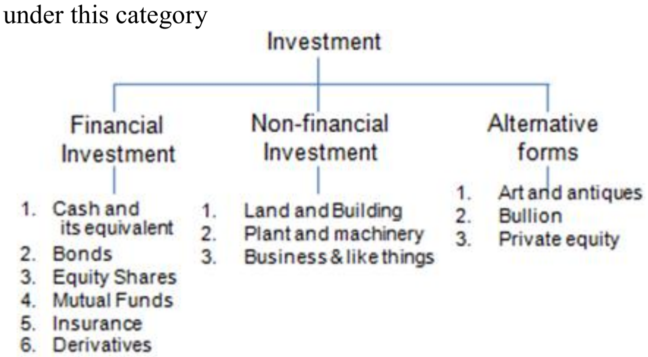
The various avenues of investment are Fixed deposit, Recurring deposit, post office savings, Chit,Shares, Mutual Funds, Bonds, Land and Building, Art, Gold, Insurance, Treasury bills, Promissory note, etc.

According to the financial divisions Investment in divided into 3 types

1. Financial Investment
Investment made on the cash and cash equivalents

2. Non financial Investment
Investment made on the fixed or long term assets

3. Alternative forms
Investment made on the art, private equity etc.,will come under this category



4. Elements of Investments

A. Return:
Investors buy or sell financial instruments in order to earn return on them. The return includes both current income (current yield) and capital gain (capital appreciation).

B. Risk:
Risk is the chance of loss due to variability of returns on an investment. In case of every investment, there is a chance of loss. It may be loss of investment; however risks and returns are inseparable.

C. Time:
Time is an important factor in investment. Time period depends on the attitude of investors who follow a_buy_ & _hold_policy.

A serious minded investor will have to consider the following important categories of investment opportunities:
- Protective investments.
- Tax oriented investment.
- Fixed income investment.
- Speculative investment.
- Emotional investment.
- Growth investment

International Journal of Science and Research (IJSR)
ISSN (Online): 2319-7064
Index Copernicus Value (2013): 6.14 | Impact Factor (2013): 4.438

Nowadays investment among the individual citizens has grown up, because of many reasons like , increase in inflation, change in the life style of the people, Future expectations and plans, necessity etc.,. But still people lack something in their investment decision like not predicting the exact requirement for the future. This study will focus on identifying the pitfalls in the investment decision.

5. Contribution of Savings and Investment towards Indian Economy

When it becomes investment, safety, flexibility, taxability and liquidity are the four major aspects which an investor considers before he makes the investment decision and all these are measured in different yard sticks by different people. Volatility variation in the different avenues made the people to change their pattern of investment , because earlier people‘s choice of investment was on fixed return avenues but nowadays they shifted their pattern to the floating avenues.

According to Enabling the prospects, Ernst & Young‘s 2014 Indian Attractiveness Survey. Of the respondents who have an emerging markets strategy, nearly a fifth said that India accounts for more than 20% of their total capital allocated for the developing world and around 50% of the international investors are considering increasing their presence in India. The India‘s savings and investment peaked at 36.8% and 38.1% of GDP, respectively, in FY08. In FY13, the overall savings rate dropped to 30.1% of GDP and investment to 34.8% of GDP. The 120-basis-point fall in the savings rate, from 31.3% in FY12 to 30.1% of GDP in FY13, was on the back of a 90-basis-point decline in household savings (which comprise 73% of total savings) to 21.9% of GDP in FY13 from 22.8% in FY12. Corporate savings, which account for 23% of total savings, fell marginally to 7.1% of GDP in FY13 from 7.3% in FY12. Public sector savings remained constant at 1.3% of GDP in FY13.

Household savings have averaged around 22% of GDP, but there has been a major shift in the composition (from financial savings to physical savings) because of high inflation and lower returns on financial instruments such as bank deposits, stocks and insurance vis-a-vis physical investments like gold and real estate. Similarly, gross capital formation fell to 34.8% of GDP in FY13 from 35.5% in FY12 and a peak of 38.1% in FY08. The widening gap between the savings and investment rate resulted in an all-time high current account deficit of 4.8% of GDP in FY13. Analysts, however, expect the savings-investment gap to narrow from 4.7% of GDP in FY13 to 2.3% of GDP in FY14 because of lower gold imports.

Table A: Average Annual Saving per Household Table A: Average Annual Saving per Household

Age of Chief Earner of Household (in years)	*Average Annual Savings per Household (in Rupees)*
Less than 25	8,515
26-35	13,465
36-45	15,522
46-55	20,444
56-65	21,196
More than 65	17,011
Average	16,139
Source: Max Life New York - NCAER Survey (2007)	

In India, bank deposits comprise over 50% of total financial savings, followed by insurance and provident fund. However, in the five years between 2008-09 and 2012-13, average deposit rates remained below the consumer price index-based inflation. With the annual average CPI-based inflation touching double digits during the period, bank deposits have yielded negative returns in real terms. On the other hand, returns from gold and real estate far exceeded CPI inflation as investors preferred to park money in these assets to hedge against inflation. Bank deposit growth has also dropped in line with financial savings — it accounted for 56% of gross financial savings in FY13, down from 57.4% in FY12.

Equities account for a miniscule 3% of overall financial savings and, given the volatility in the stock markets, retail investors have stayed away from the market. They still have some preference for stocks of public sector (PSU) companies.

Table 7: Baseline Projection of the Components of Household Savings over the Twelfth Plan

(As per cent of GDP at current market prices)								
		2011-12	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**Average XII Plan**
1	Currency	1.6	1.6	1.6	1.7	1.7	1.7	1.7
2	Bank deposits	8.6	8.8	8.9	9.1	9.2	9.4	9.1
3	Non- banking deposits	0.1	0.1	0.1	0.1	0.1	0.1	0.1
4	Life insurance fund	2.9	2.9	3	3	3.1	3.1	3
5	Provident and pension fund	1.7	1.7	1.7	1.8	1.8	1.8	1.8
6	Claims on Government	0.8	0.8	0.8	0.9	0.9	0.9	0.9
7	Shares & debentures	1.2	1.3	1.3	1.3	1.3	1.3	1.3
8	Gross Financial Assets (1 to 7)	16.8	17.1	17.4	17.6	17.9	18.2	17.6
9	Gross Financial Liabilities	5.1	5.2	5.3	5.4	5.5	5.5	5.4
10	Net Financial Savings (8 – 9)	11.7	11.9	12.1	12.3	12.5	12.7	12.3
11	Physical Savings	11.5	11.7	11.9	12.1	12.3	12.5	12.1
12	Household total Savings (10+11)	23.2	23.6	24	24.4	24.8	25.2	24.4

6. Does investment match Economics requirement

India is a country with huge varied population we generate annually around 105 Lakh Crores as national annual income with the per capita income of 1165 $ per year, the need of the Country is not satisfied because of various reasons. One among the major reason is Savings and Investment.

Statistics says that only 22% of the income by the people have been converted into savings in India in the year 2014-2015 though it is forecasted as 24% in Twelth Year Plan, but still we are not able to grow in terms of financial stability. In the long term perspective if majority of the savings are not converted to investment it will des future growth due to the requirement of capital formation in various fields. Future growth is made possible by foregoing present consumption to increase investment. Why? The reason might be because of non conversion of this entire savings to investment. People hardly invest around 5% of the money from their income. Even the investment what majority people will choose for this 5% is the one which is riskless like Fixed deposits, Post Office Savings, Investment on Gold, etc., but there are various other avenues which will generate huge revenue but people totally ignore because of their ignorance, thus the investment what we make does not match exactly with the requirements of the economy.

7. Factors to be Considered Before Investing

The problem what we are facing in term of proper investment cannot be solved overnight, it requires a long term planning and practice. This rectification will definitely yield to the individuals growth and the economic growth in the long term. Some of the factors which can be considered before investing are:

1. Investment in Risky Assets
People across the country should cultivate the habit of investing in risk assets. What is a risky asset? Any investment in assets which doesn‘t give a fixed rate of interest is said to be a risky asset such as equities, real estate, high yield and emerging market bonds, etc., Rising rates in such assets suggest faster GDP growth, better ROIs and a greater demand for investment capital. These positive factors, in turn, also drive better corporate earnings growth and improve household, corporate and export-oriented EM balance sheets. The Sensex has given annualized returns of over 17% in the past five years, the BSE PSU index has yielded 2% between February 2009 and 2014.

Before investment the investor can analyse the background of the investment by considering various factors of it. For example, in the case of shares, the safety may be partially gauged from quantitative data such as the past trend in the price of the stock, the financial performance of the company; it also may be supplemented with qualitative factors such as the reputation of the company.

The possibility of reducing risk is also possible now by hedging the risk using derivative products

Advantages of using derivatives

- This allows the sharing or redistribution of risk.
- Derivatives can allow businesses to manage effectively exposures to external influences on their business over which they have no control.
- This allows parties to speculate on the values of underlying assets, without necessarily having any actual interest in the asset itself.

2. Consideration of Inflation.
Though the literacy rate of India is 74.04%(According to 2011 Census), the literacy rate of people dealing with financial planning is very low.

Inflation plays a crucial role in the economic development, its presence is considered in the countries financial forecasting. Earlier wholesale price index was considered for inflation calculation but now we also consider consumer price index, so accordingly the inflation rate for 2015 is 6.28%, which has decreased by 0.42% compared to the year 2014 but normally people when they estimate the financial forecasting for the future they totally ignore the inflation rate of the country, because of which the actual savings rate comes down from the original value, so from the percentage of 22 it will fall down to 16%(with reference to the inflation). This savings is again not entirely transferred into investment. As a crucial analyst when we consider in depth the common inflation rate will not work out for our original calculation of savings percentage because the sector wise inflation rate differs from one year to another year. The table below shows out the sector wise inflation rate for the year 2014.

Appendix Table 1: Inflation

Consumer Price Index (2010=100) (All India)	**2013-14**
General Index (All Groups)	9.5
Food, beverages and tobacco	11.1
Fuel and light	7.4
Housing	10.4
Clothing, bedding and footwear	9.3
Miscellaneous	6.8
Excluding Food and Fuel	8.1
Other Price Indices	**2013-14**
1. Wholesale Price Index (2004-05=100)	
All Commodities	6.0
Primary Articles	9.8
of which : Food Articles	12.8
Fuel and Power	10.2
Manufactured Products	3.0
Non-Food Manufactured Products	2.9
2. CPI- Industrial Workers (IW)	9.7
of which : CPI- IW Food	12.3
3. CPI- Agricultural Labourers	11.6
4. CPI- Rural Labourers	11.5

From the above we will understand the clear role of inflation. The basic needs of a human like food, shelter and clothing rates are comparatively higher than the average inflation rate, so the consumer is not actually spending Rs.6.37 additionally, but he has to contribute extra Rs.11 for food, Rs.10.40 for housing and Rs.9.3 for clothing, so this average inflation rate is in no way connected to the actual consumption rate of the people. The people are expected to earn more than 10% every year on their basic pay in order to maintain their same standard of living, which is not possible by majority of the people residing in India since the average salary increment is less than 10%, so there arises a lack.

3. Investing for a long term period

Brijesh Damodaran, founder and managing partner, Zeus Wealth Ways, says equity investors should look at stocks from an ownership point of view as returns over the long term would be higher. For debt funds, he recommends investing for a duration of over 12 months.

Analysts say investments made with a long-term perspective would fetch better returns. As diversification is important for long-term wealth creation, investors must understand their risk profile, create a portfolio framework, and monitor it regularly.

The advantage of long-term investing is found in the relationship between volatility and time. Investments held for longer periods tend to exhibit lower volatility than those held for shorter periods. The longer you invest, the more likely you will be able to weather low market periods. Assets with higher short-term volatility risk (such as stocks) tend to have higher returns over the long term than less volatile assets such as money markets.

Advantages of Long term Investment

1. Risk premium capture (risk transfer)

Market aversion to short duration risks can generate a range of premiums that might be captured by long-term investors.

Three key advantages held by long -term investors are:

a) Capacity to adopt and hold positions where payoff timing is uncertain;
b) Ability to exploit opportunities generated by short-term investors; and,
c) Latitude to invest in unlisted and /or illiquid assets.

8. Conclusion

To attain a strong economy the people of the country should work towards it and the primary activity what they should concentrate is investment within the country. Making a proper analysis before investing is also necessary for the achievement of the same. This article has made an attempt to understand clearly of what saving and investment is and its importance in the economic growth and also it has tried to give some clear picture of different factors to be considered before investing. The advantage of investing in risky assets and consideration of inflation rate was also discussed in the article with its affects and role in the economic growth. these factors will definitely help in the development of the economy.

References

[1] Mishkin, Frederic S, ―The Economics of Money, Banking, and Financial Markets", *Boston: Addison-Wesley*, (2004) p. 517.
[2] Levi, Maurice, ―The Macroeconomic Environment of Business (Core Concepts and Curious Connections"), *New Jersey, USA: World Scientific Publishing*, (2014) ISBN 978-981-4304-34-4.
[3] Kraay.A, ―Household Savings in China", *The World bank Economic Review*, September 2000; 14,3.
[4] www. rbi.org.in/DBIE/dbie.rbi.
[5] www.inflation.eu/inflation-rates/india/inflation-india.aspx
[6] 6.www.archive.financialexpress.com/news/budget-2014-indias-falling-savings-inflation-investments-and-returns/1226932.