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A study on the Small Saving schemes In India and their impact on general masses

PUMMY SINHA

ASSISTANT PROFESSOR (Contractual) DEPT. OF ECONOMICS DIGBOI COLLEGE DIGBOI

ABSTRACT Saving is that part of income which is not spent either to secure the future or to spend those part of income in some precautionary situations. When income is not spent on consumer goods and services, it is usually saved or invested on some fixed capital, such as factories, machineries etc. in the cases of firms; cars, improvement in the existing house etc.in the cases of households. Saving therefore increases the availability of fixed capital, which ultimately leads to economic growth. Saving and the rate of interests are positively related. This paper is mainly concerned with the different kinds of small saving schemes and their rate of interests from 2014-2016 of India and their impact on the general masses. And it also showcases the main causes behind the fall in the interest rates of the small saving schemes.

KEYWORDS : Saving, small saving scheme, rate of interests

1.1 INTRODUCTION

For any economic unit, saving is the excess of income over expenditure, which is not spent. The main aim behind saving is to set aside a portion of current income for future use. The portion of income which is saved depends on the preference of the saver for future over present consumption and their expectations of future income. Savings can be done in various methods. For development to take place at a faster pace, traditional methods of saving needs to get changed. Apart from bank rates, small saving schemes are popular because of its high and appealing interest rates prior to April 2016.

But from 1st April 2016, the new interest rates of the small saving scheme are closely aligned with the markets and are reviewed quarterly instead of annually.

Except from the below poverty line, people from all classes are considered as savers. The Government of India have introduced various small saving schemes as there is great potential for collection of huge amount of savings from small savers and the small savings can be trapped in the form of Postal Saving Banks. There are 150000 postal saving banks throughout the country which has been becoming possible for all the people living in the remotest corner, outside the city. The success of these small saving schemes depends upon the active working of the agents.

Saving on one hand directly helps the people in times of needs and crisis. Whereas indirectly, saving on the part of the people, initiates growth of the economy.

This paper mainly focusses on the small saving schemes, their impact on the general people and also the reasons behind the fall in their interest rates in the recent days.

1.2 OBJECTIVES

I. To examine the rate of interest of different kinds of small saving schemes of India from 1st April 2014 to 1st April 2016 and their impact on the general masses.

ii. To examine the main causes behind the fall in the rate of interest of the small saving schemes in India from 1st April 2016.

1.3 METHODOLOGY

This paper is mainly written on the basis of secondary data collected from the journals and e-magazines. Some of the data has been collected from the "THE HINDU" newspaper. Moreover the data has been represented by using tables and bar charts.

1.4 REVIEW OF LITERATURE

Shah, Pramod N. (1992) made an analysis of saving behaviour in India during the period from 1950 to 1985. The study highlighted the trend in the overall period of 35years (1950-1985) by dividing into 4 distinct phases as low saving phase (1950-1968), the initial years of increasing savings (1968-1976), high saving phase (1977-1980) and Stagnation phase (1980-1985).

Mohbarsha Ramlal (1994) in his study savings in India examined the economic significance of small savings in India. His study highlighted small saving schemes in India as one of the country's most viable financial options.

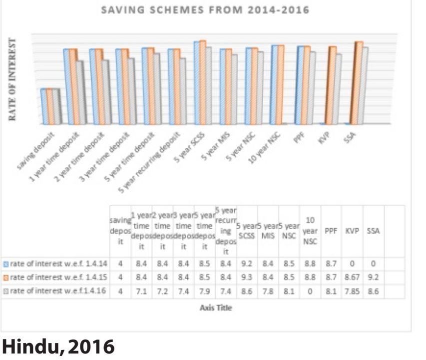
Talukdar, Umesh (2003) in his work on the pattern of rural saving and its investment in the economic development of Assam with special reference to Nalbari District, Assam critically analysed the various aspects of saving and investment and its role in the economic development of Assam.

Joseph, M.A. (2004) who had made a study on the mobilisation of saving through mutual funds, highlighted the importance of mutual funds in mobilisation of saving from people. The study also analysed the merits and demerits of mutual funds as a means of mobilisation of saving to the investing community.

Kshetrimayum, Ranjan (2014) had made a study on the role of agents in the small savings schemes in Manipur and he also studied the causes of low performance of small saving schemes in Manipur. He examined the types of savers registered under the agents of small saving schemes.

1.5 RESULTS AND DISCUSSIONS

There are different kinds of Small Saving Schemes suitable for various segments of the populations. The Government of India have reduced the rate of interest for many of the small saving scripts. This can be shown as under:-



	saving deposit	1 year time deposit	2 year time deposit	3 year time deposit	5 year time deposit	5 year recurring deposit	5 year SCSS	5 year MIS	5 year NSC	10 year NSC	PPF	KVP	SSA
rate of interest w.e.f. 1.4.14	4	8.4	8.4	8.4	8.5	8.4	9.2	8.4	8.5	8.8	8.7	0	0
rate of interest w.e.f. 1.4.15	4	8.4	8.4	8.4	8.5	8.4	9.3	8.4	8.5	8.8	8.7	8.67	9.2
rate of interest w.e.f.1.4.16	4	7.1	7.2	7.4	7.9	7.4	8.6	7.8	8.1	0	8.1	7.85	8.6

Source: The Hindu, 2016

In the above table and figure, all the available interest rates have been shown. This move of reducing interest rates by the Finance Minister of India had disappointed many small savers. In the above table, the rate of interest w.e.f. 01.04.2014 and w.e.f. 01.04.15 had been reviewed annually, whereas the rate of interest w.e.f. 01.04.16 have been reviewed quarterly. The finance ministry had decided to reduce interest rates on many of its small saving schemes including Public Provident Fund (PPF), Sukanya Samriddhi Yojna (SSY), National Savings Certificate (NSC), and Senior Citizen Savings Scheme (SCSS). These rates have been effective since April 1, 2016 which is subjected to a quarterly revision based on a new formula to determine these rates.

There has been a significant cut in the interest rate offered by ***Public Provident Fund (PPF)***, India's most popular small saving scheme. Compared to 2015, PPF is earning 8.10% in 2016. However, interest rates on PPF continues to remain tax-exempt on maturity and investment up to Rs.150000 will keep getting exemption under section 80C.

Government's pet scheme for girl child, ***Sukanya Samriddhi Yojna (SSY)*** has seen a rate cut to 8.6% from 9.2%. But there is still a gap of 0.50% between this scheme and PPF, which would likely keep its popularity intact. Interest earned on SSY is also tax exempt on maturity and investment up to Rs.150000 under section 80C.

Post Office Monthly Income Scheme (POMIS) is having a steep cut in interest rate from 8.4% to 7.8% which has been effective April 1 2016. Following this rate cut, POMIS, has gone out of favour with many of the investors.

From 20th December 2015, Government of India stopped issuing 10 year NSCs. Even there has been a rate cut in the ***5 year- National Savings Certificate (NSC)*** from 8.5% to 8.1%. But there is tax exemption under 80C.

Again Kisan Vikas Patra (KVP) had promised to get doubled in 100 months prior to April 2016. After 1st April 2016, this tenure has increased to 110 months, which means we have to wait for 10 months more to get the same benefits. Effectively this scheme has been earning 7.85% now.

1.5.1 Impact on General Masses

So this is a proposed move which has disappointed millions of small savers, who have invested in government saving schemes of less than five-year tenure. As a result of linking of small saving interest rates to government securities (G-Secs) rates and revision of rates every quarter instead of every year, the people who have invested in schemes like Public Provident Fund (PPF), Post Office Monthly Income Scheme (POMIS), Post office Fixed Deposit Scheme and Post Office Savings Account could end up getting lower returns. However schemes like PPF, 5- Year NSC and social sector schemes relating to girl child and senior citizens like SSY and Senior Citizens Saving Scheme (SCSS) is exempted from tax.

1.5.2 MAIN CAUSES BEHIND THE FALL OF SMALL SAVING INTEREST RATES

Interest rates has been re-calibrated every quarter and government has also linked the returns of these small savings schemes to the market rate prevailing on government securities. The market linking of the returns of these schemes means that their rates of return fall significantly below their current levels. However the main causes behind the slashed interest rates are as under:-

- Interest rate cuts has been expected to help the economy move to a lower overall interest rate regime eventually and thereby help all, particularly low income and salaried classes. The banks said that some schemes like the small saving schemes had higher interest rates which makes difficult for them to transmit the RBI's interest rate cuts.

- Another important reason behind the fall in the interest rate is that the small saving rate should also reflect the general interest rates in the economy.

- In order to increase the overall economic growth of the country, interest rates of these schemes had been slashed even while protecting their social goals and promoting long term savings.

- The decision to cut down interest rates hasn't gone down well with the middle class. This is happening only because general people have no idea in the context of what the economist term as ***money illusion.*** *Money illusion involves a confusion between "nominal" changes and "real" changes that reflect inflation (Belsky & Gilovich).* Money illusion is essentially a situation where people don't take inflation into account while calculating their return on investment.

Let us explain this with the help of an example. The Senior Citizens Savings Scheme (SCSS) offered an interest rate of 9.3%. The rate of inflation that prevailed from 2008 to 2013 was 10% or more. Hence the real rate of return on the scheme was negative. This was the case with small savings schemes as well as the bank fixed deposits. In fact the real rate of return was well into the negative territory i.e. minus 0.7% (9.3% minus 10%).

In another situation, inflation as measured by the consumer price index stood at 5.2% in February 2016. Let us again repeat the SCSS example and see how the real return stack up. The interest rate offered by SCSS from April 1, 2016 is 8.6% for those who do not have to pay any income tax, the real rate of return is 3.4% (8.6% minus 5.2%)

Hence the situation is substantially better than it was in the past. Investors are actually making a real rate of return on their investments. Also for saving instruments like PPF, where no tax needs to be paid on accumulated interest, the real returns are higher.

1.6 Conclusion

Saving is one of the most prominent factor behind the growth of a particular economy. It not only secures the future living of the masses but also leads to growth of the entire economy. This paper mainly focused on the rate of interests of different small saving schemes in India, which were once very much appealing to the common masses. These rate of interests got revised annually prior to April 2016, but after April 2016, these rate of interests are revised quarterly. Moreover the high and appealing interest rates of these schemes declined and got aligned with the market like the banks. This paper also emphasized on the impact of these declining rate of interest on the common masses, which was really disappointing for the people, investing in less than 5-year plans. However only some of the schemes, were freed from taxation, and that too with lower returns. Lastly the paper also focused on the reasons behind the fall in the interest rates of these small saving schemes which was mainly due to help the poor and salaried people, to increase the growth of the economy and also to show the people the actual meaning of money illusion.

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