

THE POMEGRANATE ENTERPRISE

FINANCIAL LITERACY SERIES LEVEL 4 (AGES 18 – 29)



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CONTENTS

Financial Literacy Series	ii
How to become the master of your financial future	3
Introduction to our characters and story	6
Personal income, expenses and savings	10
Business income, expenses, profit and loss	40
Banking and bank finance	79
Equity investment and the information age	108
Financial Instruments	113
Financial markets	129
Digital banking and fintech	137
Taxation	139
Insurance	143
Blockchain and cryptocurrency	148
Career planning	153
Fraud	159
Personal Investment portfolio	164
Glossary	169
Solutions	180

THE FINANCIAL LITERACY SERIES

Welcome to the State Bank of Pakistan’s Financial Literacy Series (NFLP-Y, or the National Financial Literacy Program for Youth) Level 4 (*The Pomegranate Enterprise*). This storybook and workbook is aimed at youth, ages 18 – 29 years old, but will be useful to people of all ages.

This book will help you develop your financial literacy skills. Financial literacy refers to the skill of a person in handling financial and commercial matters, such as in relation to earning, spending, saving, borrowing, investing, buying, selling, budgeting and planning. A person who is financially literate will make better decisions and plans in relation to financial matters. Everyone can benefit from having stronger financial literacy skills!

In this book, you will follow the stories of two families as they deal with financial and commercial matters that we all come across in life. The families will deal with matters such as expenses, income, saving, buying, selling and borrowing.

We encourage you to read and study this workbook by yourself or, if possible, with your family and friends. The heroes in our storybook deal with different financial and commercial matters as a family. You and your family may enjoy reading this book together.

The books in this series are:

Financial Literacy Series Level 1 (*One Pomegranate, Two Pomegranates*)
Ages 5 – 8

Financial Literacy Series Level 2 (*The Pomegranate Tree*) Ages 9 – 12

Financial Literacy Series Level 3 (*Pomegranate Juice*) Ages 13 – 17

Financial Literacy Series Level 4 (*The Pomegranate Enterprise*) Ages 18 – 29

We wish you happy reading and great success in everything you do!

HOW TO BECOME THE MASTER OF YOUR FINANCIAL FUTURE

Financial security and insecurity

Imagine a brother and sister, Jamil and Jamila.

They are both in their mid-thirties. They went to similar schools and universities and have similar jobs. They each have only one child. The incomes of their family units are about the same.

Yet, their lives are very different...

Jamila lives in her own house. She has a good amount of savings. She and her husband have already saved half the money needed for their son's university expenses. Her family has a small car that they bought a year ago. They are *financially secure*.

Jamil lives in a rented house. He has no savings. He and his wife are worried that their daughter may not be able to go to university. He has borrowed money from friends and relatives. Sometimes, he avoids family gatherings because people will ask him to repay their loans to him. He and his family are *financially insecure*.

Are such stories familiar to you? Do you know people who started from the same social, economic and educational background but ended up in very different financial situations?

What is the secret to Jamila's financial success? What is the reason for Jamil's financial problems?

Is it a financial 'gene'?

Has Jamila been born with a special financial 'gene' that allows her to make good financial decisions? Is Jamil doomed to suffer financial problems because he does not have the same special financial 'gene'?

We don't think so. The reason is that financial planning is so simple that almost anyone can do it well. People who are not good at financial planning can, with some focused learning and practice, become good at managing their financial futures.

Almost anyone in the world can learn how to ride a bicycle. Similarly, almost anyone in the world can learn how to become good at managing their financial future.

Is it mathematics?

Is Jamila especially good at mathematics? Are only people with strong knowledge of mathematics able to become strong in financial planning?

We don't think so. Financial planning needs mastery of only five basic mathematics operations: (1) addition; (2) subtraction; (3) multiplication; (4) division; and (5) using percentages.

In other words, almost all financial planning needs mastery of mathematics skills you learned in primary school.

You will need advanced mathematics skills only if you decide to become one of a few types of finance specialists.

If you have reached a level of education that allows you to read this note, you would most definitely have the mathematical skills needed to become good at financial planning.

Two core principles of financial planning

If you want to become good at financial planning, you need to master and apply two core principles. If you master these simple principles and apply them in daily life with discipline, you will become very good at financial planning!

Let's think about each of these principles in turn.

MAKE GOOD FINANCIAL TRADE-OFF DECISIONS

What is a 'trade-off'? A trade-off is an exchange of one thing for another. For example, if you have money to pay the bus fare only one way and you decide to take the bus to your destination, you will not be able to take the bus on your way back.

Almost all of financial planning involves trade-off decisions. For example:

1. If you spend more money, you will have less money to save.
2. If you want to save more money, you must either increase your income or decrease your expenses.
3. If you invest money in a business today, you will have less money to spend today but, if the business is profitable, you will have more money to spend tomorrow.
4. You can decide to save money at home and have no income on those savings or put that money in a savings account and have an income on that saving.
5. A business may decide to spend money on marketing, but then it will have less to spend on production.
6. A business may borrow money today to expand or it may not borrow money and give up on expansion until later.

Sometimes we make good trade-off decisions and sometimes we make poor trade-off decisions. At its core, financial planning involves consistently making good trade-off decisions in relation to financial matters.

Let's think again about Jamila and Jamil. In their lives, they must have made thousands of financial trade-off decisions. They made these decisions about the income they make, the expenses they have, the money they save, their borrowings,

the gifts they give, the investments they make and many other things.

No doubt, both Jamila and Jamil made both good and poor financial trade-off decisions. But, most likely, Jamila consistently made more good trade-off decisions and Jamil consistently made poor trade-off decisions. Over time, their numerous financial trade-off decisions led them to very different places.

Because Jamila consistently made more good financial trade-off decisions, she was probably thinking about them and learning from her mistakes. Because Jamil consistently made more poor financial trade-off decisions, he was probably not thinking about them and not learning from his mistakes.

Good financial planners make financial trade-off decisions after thinking about them. Weak financial planners make financial trade-off decisions without thinking about them. Often, they are not even aware that they are making a poor decision!

UNDERSTAND FINANCIAL RELATIONSHIPS

All activities and concepts in financial planning are related to each other. For example, for an individual, income minus expenses equals savings. As another example, in a business, income minus expenses equals profit. So, in some ways, savings and profits are parallel to each other. They create reserves for future expenses or investments.

Many financial relationships involve time. A good financial planner will think about financial matters over time. For example, if you have a savings goal of Rs. 1,000 but you can only save Rs. 100 per month then, if you save Rs. 100 every month for 10 months, you will reach your savings goal in 10 months. If you cannot save Rs. 100 one specific month, then you should decide whether:

- ▶ the *overall savings goal* should be reduced to Rs. 900;
- ▶ the *time to reach the savings goal* should be extended to 11 months; or
- ▶ the *amount of the savings goal for the remaining months* should be increased.

A good financial planner will always think about relationships. For example:

If you spend Rs. 100 extra in one month, what impact will that have on your savings goal?

1. If you spend money on an income-making project (for example, buying a sewing machine to stitch clothes for sale), what impact will that have on future income?
2. If a business invests Rs. 100,000 in machinery today, how long will it take for it to make back that money from the sale of goods produced by that machinery?
3. If you eat your last egg today, what expenses will you need to bear to have something to eat for breakfast tomorrow?

Acquire the simple discipline of becoming a good financial planner. It will serve you well throughout your life!

INTRODUCTION TO OUR CHARACTERS AND STORY

In order to create practical examples to help you apply the materials of this book, we have provided a story of two related families. Their story begins in the first book of our series and continues to this book. Here is a short introduction to the characters and their story up to what happens in this book. Over the remaining chapters of this book, their story will unfold further.



Shereen is 22 years old. When we meet her in this book, she has just graduated from university with a Bachelor's in Business Studies.

Her cousin, Ali, is also 22 and has just graduated from university with a Bachelor's in Computer Science.

They are celebrating their graduation!



Daniyal is Shereen's younger brother. He is 20 years old. He is studying medicine at university and expects to obtain his MBBS in three years.

Safdar is Shereen's father and Ali's uncle. He has a fruit and juice business in the city. His wife, Rabia, teaches mathematics in secondary school.



Nusrat is Safdar's sister and Ali's mother. She lives on a small farm in the village. She makes a small amount of money from the farm and has a small government pension as her deceased husband used to be a soldier.





Many years ago, when they were 10 years old, Shereen and Ali started a small pomegranate business. Pooling together their pocket money, they bought a pomegranate sapling from a local nursery. They planted the sapling in Nusrat and Ali's farm and it grew into a beautiful tree. Safdar sold the pomegranates in his fruit shop in the city and his customers loved the delicious fruit.

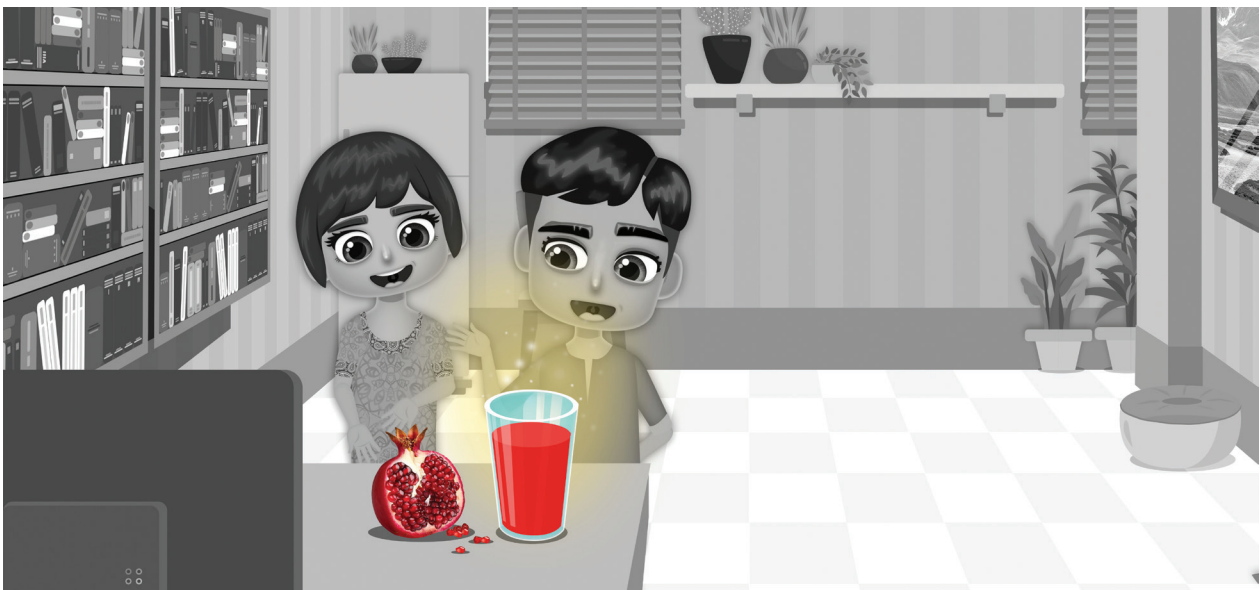
Before growing the tree, Ali had dropped out of school. But, when Shereen helped with calculations to save money, buy the sapling and work out transport prices, Ali was inspired and he went back to school.



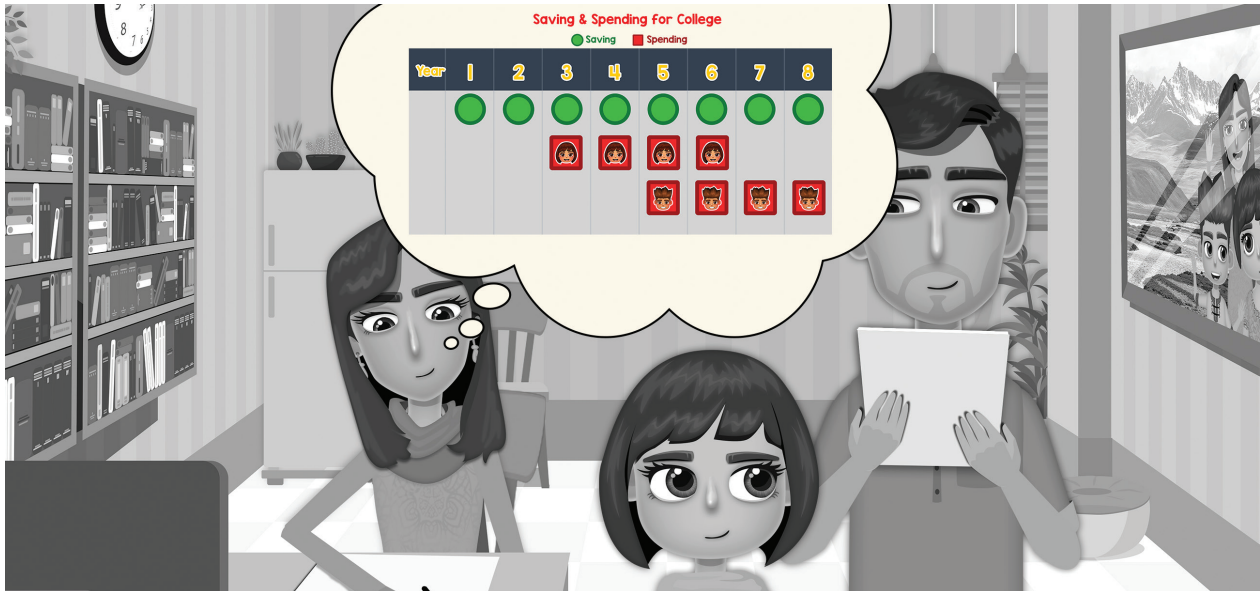


With a small loan from Safdar, Shereen and Ali expanded their business to plant a beautiful orchard of 7 pomegranate trees at the farm. With his mother Nusrat's help, Ali harvested and transported baskets of the ripe, red pomegranates to the city to sell at Safdar's store.

Shereen and Ali were careful with their money, saved what they could and made intelligent decisions about the expenses in their business. They planned so well that they were able to invest in a juice maker when they were about 15 years old. They started to dream of expanding their pomegranate juice business.



At the same time, Rabia, Shereen's mother, began to dream of sending her children to university. Her son, Daniyal, was interested in becoming a doctor. Shereen wanted to study business. Rabia wanted a positive future for the children and she knew that the best way to ensure such a future would be to help them graduate with university degrees. The family developed a savings plan for the children's university.



Nusrat made a similar plan for Ali, who became a star pupil after rejoining school.

Going to university meant, however, that neither Shereen nor Ali could dedicate their time to expanding their business. Recognizing the sacrifice being made by their parents, the children decided to focus on their studies. But they continued to help Safdar with his business.

With the children's help, Safdar took a bank loan and added a juice business to his fruit shop. In the village, Nusrat took over the pomegranate fruit business, tending to the orchard and carrying on her son's profitable venture. That meant each family had extra income to save for the costs of university.

Today, all the savings and hard work of the family members have paid off! Shereen and Ali have just graduated from university. What lies in the future?



PERSONAL INCOME, EXPENSES AND SAVINGS

Introduction

In this section, we will consider income, expenses and savings from an individual or family perspective.

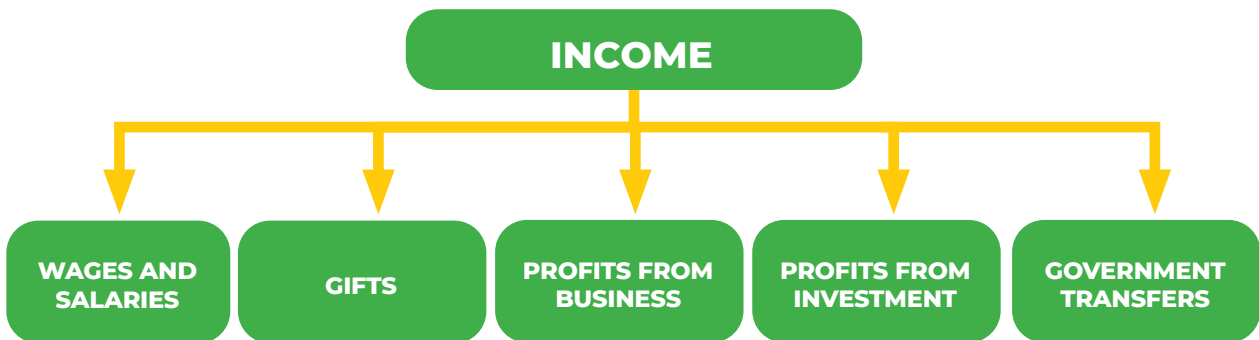


Shereen, age 22, has recently completed her Bachelor's in Business Studies. She has done well and is considering her next move in life. Her brother, Daniyal, is 20 years old and has 3 years to go before he completes his MBBS. Her parents, Safdar and Rabia, have enough savings to get Daniyal through university but will have very little savings after that.

Her cousin, Ali, also 22 years old, has also recently completed his Bachelor's in Computer Science. Ali's mother, Nusrat, has depleted her savings to get her son through university.

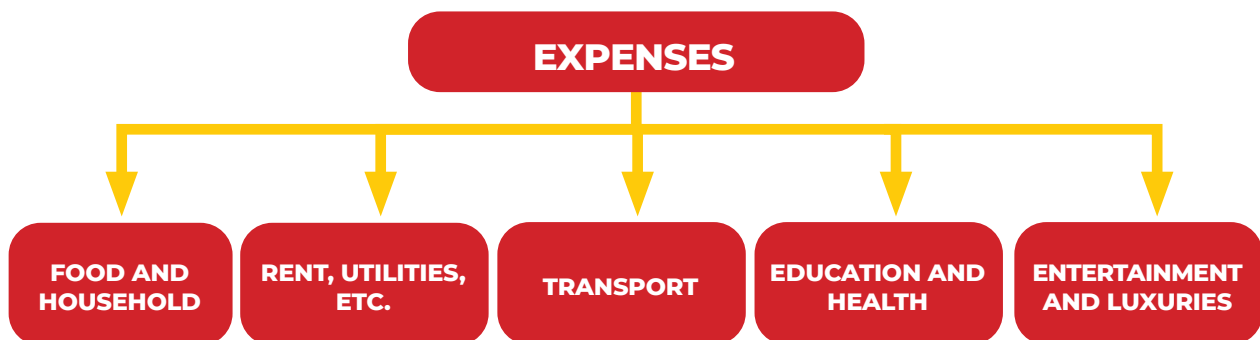
Income and expenses

Individuals and families have **income** from different sources and **expenses** of different types.



Income may include:

- ▶ Wages and salaries (e.g., Rabia has a salary as a teacher)
- ▶ Gifts from others (e.g., Safdar and Rabia give the children pocket money)
- ▶ Profits from business (e.g., Safdar gets a profit from his fruit shop)
- ▶ Profits from investment (e.g., profit received on savings in a savings account)
- ▶ Government transfers (e.g., government pensions, subsidies, benefits)



Expenses may include:

- ▶ Food and household expenses
- ▶ Rent, electricity and gas
- ▶ Transport expenses
- ▶ Education fees and doctor fees
- ▶ Entertainment, luxuries and gifts

Fixed and variable income and expenses

Your items of income and expense may be **fixed** or **variable**.

An item of fixed income or expense is the same over different periods. For example, if you need to pay rent for your house of Rs. 10,000 every month, then rent is a fixed expense.

An item of variable income or expense changes over different periods. For example, if you have profit from a business of Rs. 50,000 in one month, Rs. 70,000 in the second month and Rs. 70,300 in the third month, then profit is an item of variable income.

Fixed and variable income and expenses have some advantages and disadvantages:

	Type	Advantage	Disadvantage
1.	Fixed income (e.g., wages or salaries)	It is regular and predictable.	It is not so easy to increase this type of income.
2.	Fixed expense (e.g., house rent)	It is regular and predictable and it does not increase with inflation .	It is payable at fixed intervals (e.g., every month) and it is usually not easy to defer or delay payment.
3.	Variable income (e.g., profit from a business)	There is greater opportunity to increase this kind of income.	It is not regular or predictable, it may go down or even disappear in different periods.
4.	Variable expense (e.g., food and fuel)	In some cases, it is possible to forgo or defer the expense (e.g., if meat prices go up too much, you could eat less meat).	These types of expenses usually increase with inflation.

Classifying the family's income and expenses



Classify the following as types of fixed and variable income or expense (we've done the first one for you).

1. Rabia receives a monthly salary as a school teacher

fixed income

2. Safdar fills gasoline in his vehicle 2-3 times a month

3. Daniyal has the same university fee payable every quarter

4. Nusrat receives a pension from the government every month

5. Shereen likes to buy adventure novels from time to time

6. Safdar's income comes from the profit from his fruit and juice business

The solution to this exercise can be found on page 180

Classifying your income



What are some of your, your family members' or your friends' sources of income for one month and are they fixed or variable?

	Source	Fixed/Variable	Details
1.	Wages and salaries		
2.	Gifts		
3.	Profits from business		
4.	Earnings from investments		
5.	Government transfers		

Classifying your expenses



What are some of your, your family members' or your friends' items of expense for one month and are they fixed or variable?

	Source	Fixed/Variable	Details
1.	Food and household		
2.	Rent, utilities, etc.		
3.	Transport		
4.	Education and health		
5.	Entertainment and luxuries		

Introduction to inflation

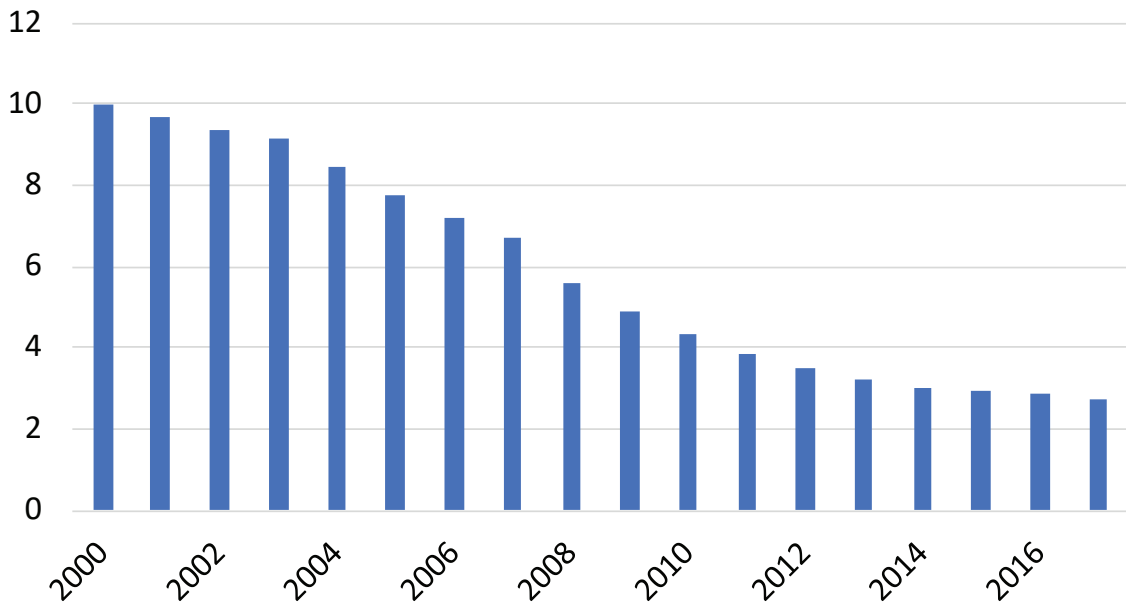
Inflation is the steady rise in prices of goods and services over time. The inflation rate of a country is the rate at which the price of a basket of commodities goes up each year. The following is a chart of the inflation rate in Pakistan between 2000 and 2017.



Source: The World Bank

This means that, using Pakistan’s inflation rate, if Rs. 100 enabled you to buy 10 pomegranates in the year 2000, the same Rs. 100 would enable you to buy about 2.7 pomegranates in the year 2017!

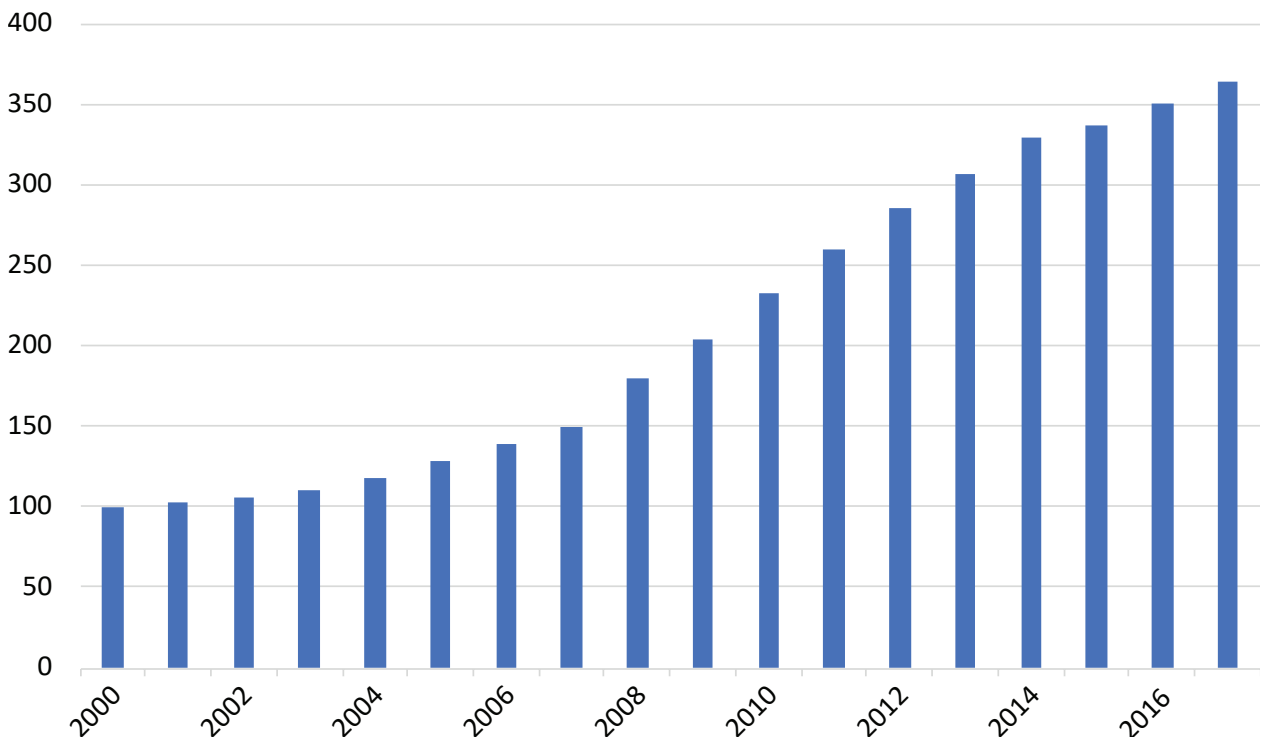
**Pomegranates You Can Buy with Rs. 100
(Using Pakistan’s Inflation Rate)**



Source: Based on World Bank projections

It also means that, using Pakistan’s inflation rate, if you bought 10 pomegranates for Rs. 100 in the year 2000, you would pay about Rs. 364 for the same 10 pomegranates in 2017!

**Price (Rs.) of 10 Pomegranates
(Using Pakistan’s Inflation Rate)**



Source: Based on World Bank projections

Thinking about inflation



Inflation relates to increases in prices.

Separate out the true and false statements below.

		True	False
1.	Rabia has a fixed salary of Rs. 25,000 per month. If there is inflation, she will be able to buy more things with that salary.	<input type="checkbox"/>	<input type="checkbox"/>
2.	Shereen can buy a book for Rs. 200 today. If there is inflation, the same book will cost more in the future.	<input type="checkbox"/>	<input type="checkbox"/>
3.	Shereen wants to save money to buy a book in 1 year. The book costs Rs. 200 today. If there is 10% inflation of the price of the book every year, she will need to save Rs. 220.	<input type="checkbox"/>	<input type="checkbox"/>
4.	Safdar increases his fruit sales prices at the rate of inflation every year. This means the income from his shop will go down every year.	<input type="checkbox"/>	<input type="checkbox"/>
5.	Inflation usually has more of a negative impact on people who earn a fixed income (e.g., salaries) than people who have a variable income (e.g., profit from a business).	<input type="checkbox"/>	<input type="checkbox"/>

Evaluating the impact of inflation



Respond to the questions below in relation to the following scenarios.

1.	Rabia receives a monthly salary as a school teacher
2.	Safdar fills gasoline in his vehicle 2-3 times a month
3.	Daniyal has the same university fee payable every quarter
4.	Nusrat receives a pension from the government every month
5.	Shereen likes to buy adventure novels from time to time
6.	Safdar's income comes from the profit from his fruit and juice business

From the point of view of the family's income, which income item listed above is **most likely to go up** if there is inflation? Why?

.....

.....

.....

From the point of view of the family's expenses, which expense item listed above **will not be negatively affected** by inflation? Why?

.....

.....

.....

From the point of view of the family's income, which TWO income items listed above are **most likely to be negatively affected** by inflation? Why?

.....

.....

.....

The solution to this exercise can be found on page 181

Trade-offs between salary and profits

Trade-offs between salary and profits

Shereen Ali, I am so happy we both did so well in university! You have been a great support to me ever since we decided to grow a pomegranate tree and sell the fruit!

Ali You know that was a turning point in my life. Our little savings plan inspired me to go back to school. And now I have learned about programming and so many other things!

Shereen It was a turning point for me too. I discovered I really enjoyed creating a little business. It made me realize that girls can do well at business, not just boys!

Ali Is that what you want to do next? Join your father's business?

Shereen You know I love that business. I know I can help him grow it. If I join, in the long-term we can get a lot more income from the business. But in the short-term our family will be better off if I join a company and bring home a salary every month.

Ali Why don't you discuss this with them? Your father brings in profit from the business and your mother has a salary. And, even if you join the business, can you do something else to make some extra income?

Shereen Good idea! I will discuss this with abba and ammi. And I could easily give tuitions in business studies. That way, I will 'earn and learn'.

Ali Haha! I like that! 'Earn and learn'! You know I really love Safdar mamu's fruit and juice business. I hope one day I can get involved. But my mother put all our savings into my education. Safdar mamu helped a lot too! Today, my mother only has a small pension and a little bit of farm income. I am going to get a job in programming.

Shereen That will be great! Programming jobs pay very well. And you will learn a skill that will be very important in the information technology age.

Ali Maybe once I have more experience and our savings have increased to a comfortable level, I will think about business. Maybe I will join you!

Shereen That is a good plan!

Let's think about some of the financial trade-offs Shereen and Ali discuss.

Shereen mentions that in the *short-term* her family will be better off if she joins a company and brings home a *salary* every month. She also says that, if she joins her father, in the *long-term*, they can get a lot more *profit* from the business. Can you identify two important trade-offs she is thinking about?

One trade-off is between the fixed income of a salary from a company and the variable income of profits from a business. If she draws a salary, she can immediately contribute to the family's finances. If she joins her father's business, any income she makes will reduce the profits from her father's business.

Another trade-off is between the short-term and the long-term. She believes that, in the short-term, working for a company and drawing a salary will provide greater income, but, in the long-term, building the business will provide greater income. This makes sense because in a fixed income job you get paid a salary regularly for your effort. But, in a business, you often need to make a lot of effort and the financial rewards only come in later. Sometimes, they may not come in at all.

Note that Shereen also very smartly decides to give tuitions in business studies. This will allow her to bring in some extra income and to 'earn and learn'.

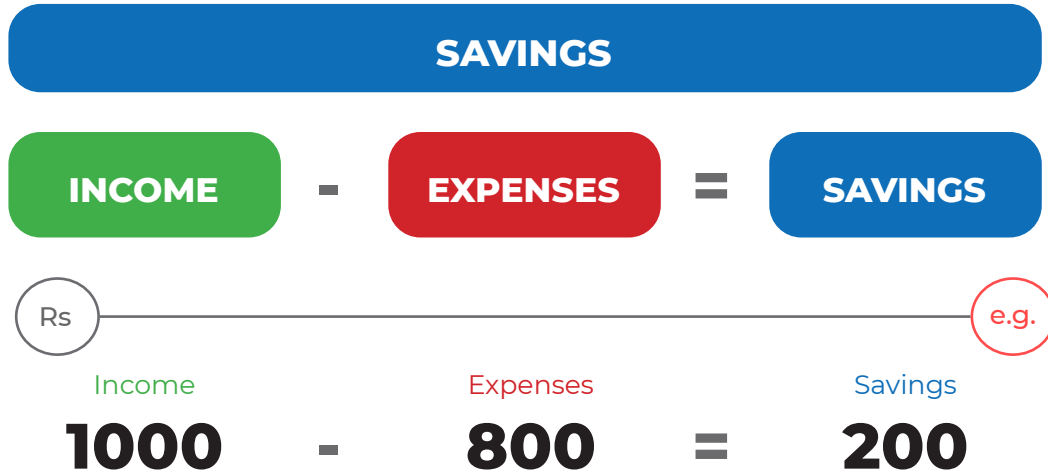
Ali takes a different approach. Even though he is interested in business, he decides to go for a job in programming. What are the differing factors in Shereen's and Ali's family financial situation that make a programming job a sensible trade-off for Ali?

Shereen's family have two sources of income: her mother's salary from teaching and her father's profit from his business. Ali's mother has no savings left and only a small pension and a little bit of farm income. Ali's immediate family has a lot more short-term financial pressure and a high-paid programming job will provide immediate income.

Note also that Ali is going for a programming career. As Shereen points out, Ali will learn a skill that will be very important in the information technology age.

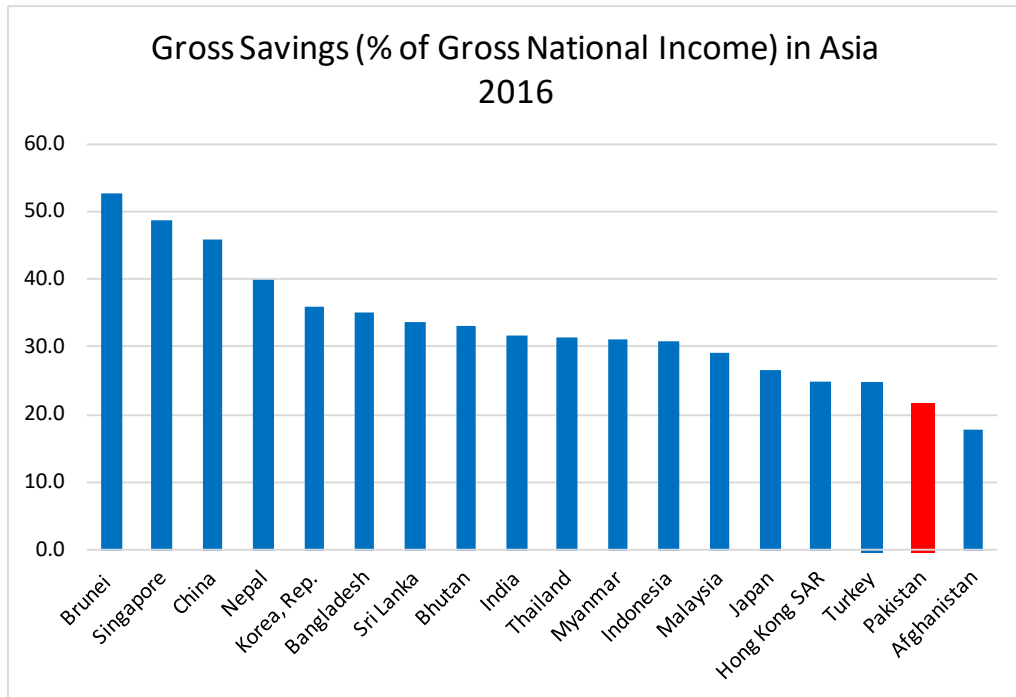
Introduction to savings

So far, we have principally discussed personal income and expenses. The third core element of personal finance is **savings**, which at the simplest level may be represented as follows:



Individuals and families that seek to expand their income and reduce their expenditures are most likely to have savings. Having positive savings and growing savings every month is the most essential aspect of a financially secure individual or family. Similarly, having a substantial and positive savings rate is the most essential aspect of a financially secure country.

At present, Pakistan has a low savings rate. We don't do very well by global or Asian standards. We also fare poorly when we are compared with our close Asian neighbors. Our 2016 gross savings as a country was about 22%. From our neighbors, this puts us slightly ahead of Afghanistan (18%), but well behind India (32%), Bhutan (33%), Sri Lanka (34%), Bangladesh (35%) and Nepal (39%).



Source: The World Bank

Pakistan's low savings rate means that its people are not saving enough. If we take as our goal as individuals and families to save more, we will create financial security for ourselves. And, when you put together improved savings rates by all Pakistanis, we will also create a financially secure nation.

Introduction to savings plans

It is very difficult for an individual or family to save regularly and grow its savings steadily without a **savings plan**. A savings plan allows you to meet a **savings goal** (i.e., how much money to save, for what purpose and over what period).

Savings Plan						
How much money you want to save	1.	Savings goal	10,000			
The period of time over which you will save	2.	Period	Now	Month 1	Month 2	Month 3
Your savings in a given period	3.	Income	-	25,000	25,000	25,000
	4.	Expenses	-	21,000	25,000	22,000
	5.	Savings per month	-	4,000	0	3,000
The sum of your savings	6.	Total savings	3,000	7,000	7,000	10,000

For example, Rabia makes a savings plan to buy a tablet for Rs. 10,000 within the next 3 months.

She currently has a saving of Rs. 3,000.

She has monthly income of Rs. 25,000.

In the first month, she can save Rs. 4,000. Her total savings grow to Rs. 7,000.

In the next month, her expenses are Rs. 25,000, the same as her income. She has no savings. Her total savings stay at Rs. 7,000.

In the third month, she cuts her expenses to Rs. 22,000 and saves Rs. 3,000.

Therefore, after 3 months, her total savings reach Rs. 10,000 and she is able to buy the tablet.

Savings and withdrawals

Sometimes, you need to take money out of savings. This is called a withdrawal. You can use the term 'withdrawal from savings' even if you save at home.

Savings Plan					
1.	Savings goal	10,000			
2.	Period	Now	Month 1	Month 2	Month 3
3.	Income	-	25,000	25,000	25,000
4.	Expenses	-	21,000	27,000	22,000
5.	Savings per month	-	4,000	(2,000)	3,000
6.	Total net savings	5,000	9,000	7,000	10,000

The sum of your savings for that period and all prior periods LESS the total amount of your withdrawals for that period and all prior periods.

In finance, negative numbers are often written in brackets (this means we have to subtract these numbers).

For example, Rabia makes a savings plan to buy a tablet for Rs. 10,000 within the next 3 months.

She currently has a saving of Rs. 5,000.

She has monthly income of Rs. 25,000.

In the first month, she can save Rs. 4,000. Her total savings grow to Rs. 9,000.

In the next month, her expenses are Rs. 27,000, which is Rs. 2,000 MORE than her income. She has to withdraw Rs. 2,000 from her savings to meet her expenses. Her total net savings go down to Rs. 7,000 (Rs. 9,000 – Rs. 2,000).

In the third month, she cuts her expenses to Rs. 22,000 and saves Rs. 3,000.

Therefore, after 3 months, her total net savings reach Rs. 10,000 and she is able to buy the tablet.

Making a savings plan

As a first step towards making a savings plan for Shereen and her family, let's help them set up a savings goal.

They have two parts to their savings goal:

1. Daniyal is doing his MBBS and he has 3 years of university expenses
2. The family has bought some land and they want to build a house in the next 5 years

Let's start with what they have already done.

University and House Building Expenses (Rs.)							
Expense	Present	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Assumptions							
1.	Present university expense	300,000					
2.	Present house building expense	2,000,000					
3.	Assumed inflation rate	5%	5%	5%	5%	5%	
Projections							
4.	Daniyal's university expense		315,000	330,750	347,288	-	993,038
5.	House building expense		-	-	-	-	2,552,563
6.	Total		315,000	330,750	347,288	-	3,545,601

The estimated present expense of the house the family wants to build.

One year of university expenses at present.

The assumed inflation rate.

The present expense of a year in university is Rs. 300,000. To take inflation into account the family has projected the following:

1. University expenses year 1: Rs. 315,000 (i.e., $300,000 \times 1.05$)
2. University expenses year 2: Rs. 330,750 (i.e., $300,000 \times 1.05 \times 1.05$)
3. University expenses year 3: Rs. 347,288 (i.e., $300,000 \times 1.05 \times 1.05 \times 1.05$)

They have also projected that they will build the house in year 5. To take inflation into account the family has projected the following:

4. House building expense: Rs. 2,552,563 (i.e., $2,000,000 \times 1.05 \times 1.05 \times 1.05 \times 1.05 \times 1.05$)

It is actually quite easy to project inflation rates and mark-up rates. Simply (1) take the original amount and (2) multiply it by the rate expressed as "1.XX" (so 5% is expressed as 1.05) and (3) do this for the number of years. For example:

5. Rs. 100 at an inflation rate of 10% becomes in year 1: Rs. 110 (100×1.10)
6. Rs. 100 at an inflation rate of 10% becomes in year 2: Rs. 121 ($100 \times 1.10 \times 1.10$)

Calculating annual savings



To pay for Daniyal's remaining university expenses and build the house, the family have projected they need Rs. 3,545,601 over a 5-year period. To be safe, they set their savings goal at Rs. 3,600,000.

Calculate the EQUAL annual savings they will need to make to save Rs. 3,600,000 in 5 years.

University and House Building Expenses (Rs.)								
	Expense	Present	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Assumptions								
1.	Present university expense	300,000						
2.	Present house building expense	2,000,000						
3.	Assumed inflation rate	5%	5%	5%	5%	5%	5%	
Projections								
4.	Daniyal's university expense		315,000	330,750	347,288	-	-	993,038
5.	House building expense		-	-	-	-	2,552,563	2,552,563
6.	Total		315,000	330,750	347,288	-	2,552,563	3,545,601
7.	Annual savings		<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>

The solution to this exercise can be found on page 182

Calculating withdrawals and net savings



In Years 1, 2 and 3, will need to withdraw from savings and spend it on university expenses for Daniyal.

In Year 5, they will withdraw the money needed to build their house.

Complete the table to show how much they need to withdraw and how much savings they will have left each year.

University and House Building Expenses (Rs.)							
Expense	Present	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Assumptions							
1.	Present university expense	300,000					
2.	Present house building expense	2,000,000					
3.	Assumed inflation rate	5%	5%	5%	5%	5%	
Projections							
4.	Daniyal's university expense		315,000	330,750	347,288	-	993,038
5.	House building expense		-	-	-	-	2,552,563
6.	Total		315,000	330,750	347,288	-	3,545,601
7.	Annual savings						
8.	Withdrawals		<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
9.	Total net savings		<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>

Saving at home vs. saving at the bank

A question that comes up next is if the family should save money at home or in a bank.

Saving Options



Saving at home vs. bank



Help the family decide in which ways saving at home or in a bank is better.

	At home	In a bank
1. Safer		
2. Makes money		
3. Easy to transfer money to another city		
4. Easy to access money		

Based on these factors which place is better for the family to save their money?

The solution to this exercise can be found on page 183

Benefits of saving at a bank

The benefits of saving money in a bank:

Your money earns an income

The **mark-up** offered by banks on a **savings account** allows you to earn an income on your **deposited** savings. For example, if you deposit Rs. 100 in a savings account with an annual mark-up of 10%, you will earn an income of Rs. 10 in the coming year.

Your money is safe

Banks spend a lot of money on making sure that their operations and computer systems are safe. Your savings are much more secure from theft and natural disasters when deposited in a bank. In addition, the State Bank of Pakistan has a system of deposit insurance in place. Under this system, money deposited in banks is insured up to a specified level by the State Bank.

Your money is easy to transfer

It is easy to transfer money from one person to another by using bank accounts. Mobile and **branchless banking** have also made everyday banking tasks like **funds transfer** and bill payment much more convenient to perform.

Your money is easy to get to if you want to spend it

It is easier to get to your money if you save it at home, but this means leaving the house with a lot of money in your pocket every time. Having a bank account allows you the convenience of using a **debit card** to **withdraw** money from an **ATM** or directly paying a seller through your current account.

In summary:

Banks keep your money **safe**, they make it **easy for you make transfers** and payments, they **pay you** for every rupee you keep in a savings account and they allow you **convenient access** to your money through ATMs and mobile banking.

Personal and family budgets

A personal or family **budget** is an estimate of income, expenses and savings over time.

A business budget is an estimate of income, expenses and profit or loss over time.

After setting a savings goal of Rs. 3,600,000 over 5 years, Shereen and her family prepare a budget.

Safdar & Rabia's Family Budget (Rs.)							
		Year 1	Year 2	Year 3	Year 4	Year 5	Total
Income							
1.	Safdar's income from fruit business	800,000	900,000	1,000,000	1,100,000	1,200,000	5,000,000
2.	Rabia's income from teaching	300,000	330,000	360,000	390,000	420,000	1,800,000
3.	Profit from savings in the bank	40,200	78,492	114,762	186,762	6,266	426,481
4.	Total income	1,140,200	1,308,492	1,474,762	1,676,762	1,626,266	7,226,481
Expenses							
5.	Rent	180,000	200,000	230,000	265,000	300,000	1,175,000
6.	Food & household items	150,000	165,000	185,000	210,000	240,000	950,000
7.	Electricity, water & mobile bills	120,000	130,000	145,000	160,000	175,000	730,000
8.	Transport	85,000	92,000	100,000	110,000	120,000	507,000
9.	Health	12,000	18,000	24,000	30,000	38,000	122,000
10.	Clothes, entertainment, gifts, etc	180,000	200,000	230,000	265,000	300,000	1,175,000
11.	Total expenses	727,000	805,000	914,000	1,040,000	1,173,000	4,659,000
Savings							
12.	Savings	413,200	503,492	560,762	636,762	453,266	2,567,481

Analyzing personal and family budgets



After setting a savings goal of Rs. 3,600,000 over 5 years, Shereen and her family prepare a budget.

Can you help Shereen analyze the budget?

Safdar & Rabia's Family Budget (Rs.)							
		Year 1	Year 2	Year 3	Year 4	Year 5	Total
Income							
1.	Safdar's income from fruit business	800,000	900,000	1,000,000	1,100,000	1,200,000	5,000,000
2.	Rabia's income from teaching	300,000	330,000	360,000	390,000	420,000	1,800,000
3.	Profit from savings in the bank	40,200	78,492	114,762	186,762	6,266	426,481
4.	Total income	1,140,200	1,308,492	1,474,762	1,676,762	1,626,266	7,226,481
Expenses							
5.	Rent	180,000	200,000	230,000	265,000	300,000	1,175,000
6.	Food & household items	150,000	165,000	185,000	210,000	240,000	950,000
7.	Electricity, water & mobile bills	120,000	130,000	145,000	160,000	175,000	730,000
8.	Transport	85,000	92,000	100,000	110,000	120,000	507,000
9.	Health	12,000	18,000	24,000	30,000	38,000	122,000
10.	Clothes, entertainment, gifts, etc	180,000	200,000	230,000	265,000	300,000	1,175,000
11.	Total expenses	727,000	805,000	914,000	1,040,000	1,173,000	4,659,000
Savings							
12.	Savings	413,200	503,492	560,762	636,762	453,266	2,567,481

Will the family meet their 5-year savings target of Rs. 3,600,000? If not, by how much will they be short?

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If they need to increase income to meet their budget, which item of income will be easiest to increase?

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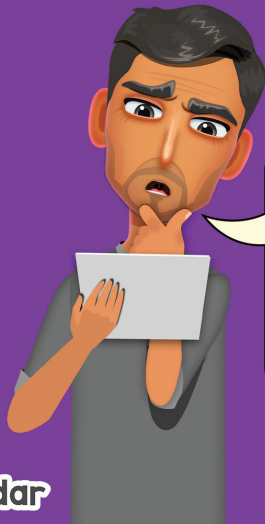
If they need to decrease expenses to meet their budget, which item of expenses will be easiest to decrease?

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A family resolution

A family savings resolution



Safdar

Well, my family, we had set a savings goal of Rs. 3,600,000 over five years. This will allow us to get Daniyal through university and build a house. But when we did our 5-year budget, we learned that we will be short of our goal by slightly over Rs. 1,000,000!

We are not the kind of family that just gives up, are we?



Rabia



Shereen

No, we are not! I'm going to join abba's business and over the next 5 years we will bring in more than Rs. 800,000 of extra profit!

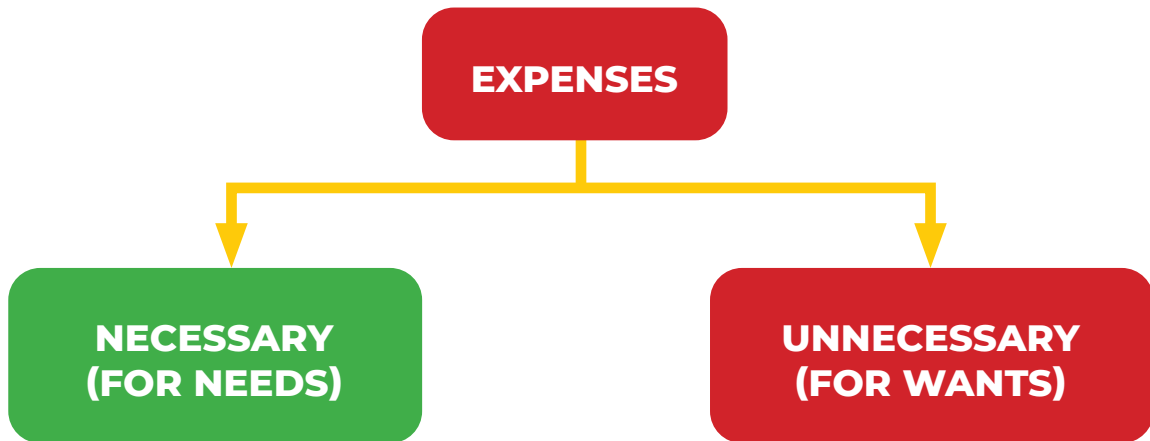
Excellent! That will leave a gap of about Rs. 200,000. I will manage our expenses so we decrease our expenses by Rs. 40,000 a year!



Rabia

Analyzing expenses: necessary and unnecessary

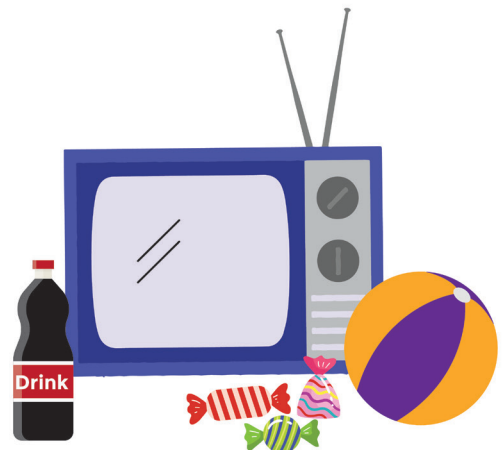
You can have two kinds of expenses. You can have **necessary expenses** and you can have **unnecessary expenses**.



Some things are very important and you must have them. Having these things meets human **needs**. For example, going to school and eating lunch are both needs. **Expenses that meet needs are necessary expenses.**



Some things are not important, but make you happy so you want to have them. These are called **wants**. For example, buying a new toy and eating ice cream are both wants. **Expenses that meet wants but not needs are unnecessary expenses.**



If you don't have enough money, it is better to cut unnecessary expenses than necessary expenses.

Dealing with unnecessary expenses



Rabia has committed to cut at least Rs. 200,000 in 5 years from the family expenses in order for the family to meet their savings goal. That means Rs. 40,000 a year.

Help Rabia reduce the family's annual expenses and save Rs. 40,000.

Safdar & Rabia's Family Expenses (Rs.)		
		Year 1
Other Expenses		
1.	Rent	180,000
2.	Food & household items	150,000
3.	Electricity, water & mobile bills	120,000
4.	Transport	85,000
5.	Health	12,000
6.	Total	547,000
Clothes, Entertainment, Gifts, etc		
7.	Clothes	40,000
8.	Pocket money for children	36,000
9.	Family travel	26,000
10.	Dining out	18,000
11.	Sweets, ice cream, etc.	12,000
12.	Gifts for relatives	12,000
13.	Charity	12,000
14.	Cigarettes	12,000
15.	Bangles, earrings, etc	12,000
16.	Total	180,000
17.	Total expenses	727,000

**Which expenses will you cut?
Which are the least necessary expenses?**

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Dealing with your unnecessary expenses



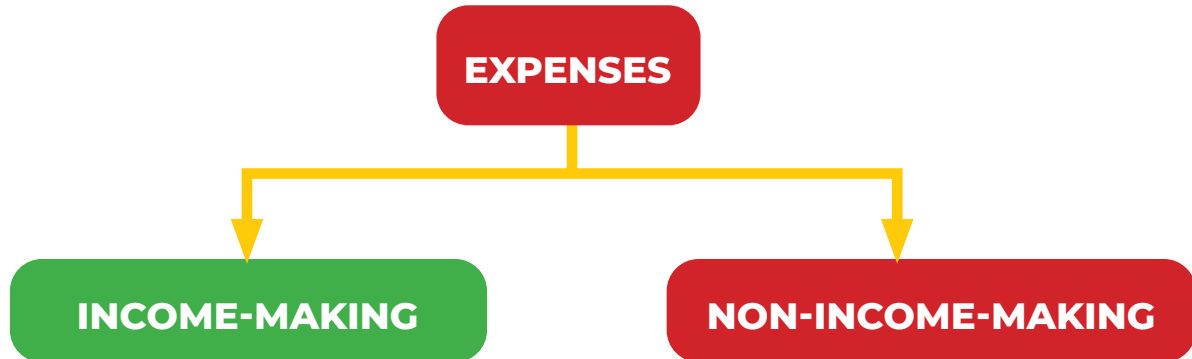
List some of your, your family members' or your friends' expenses.

Can you tell if these expenses are necessary or unnecessary?

	Necessary	Unnecessary
1.	<input type="checkbox"/>	<input type="checkbox"/>
<hr/>		
2.	<input type="checkbox"/>	<input type="checkbox"/>
<hr/>		
3.	<input type="checkbox"/>	<input type="checkbox"/>
<hr/>		
4.	<input type="checkbox"/>	<input type="checkbox"/>
<hr/>		

Analyzing expenses: income-making and non-income-making

You spend money on many things. Some of **your expenses will help** you make money. Other expenses will not.



Income-making expenses are expenses which help you make money.

Non-income-making expenses are expenses that do not earn you any money.

Analyzing expenses: income-making and non-income-making

Imagine that you spend money to grow a fruit tree.

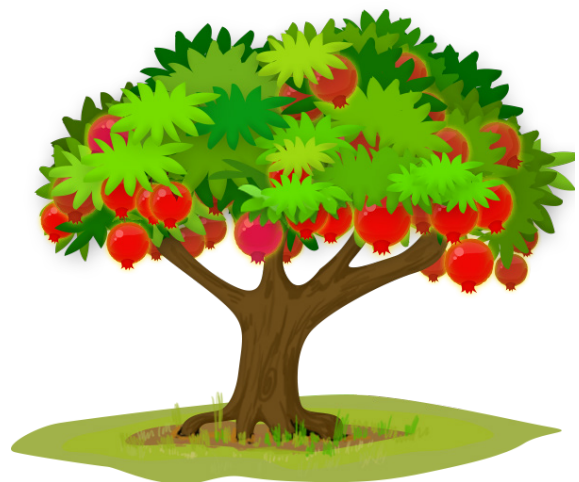
1. You could grow a fruit tree and make money by selling the fruit.
2. You could also grow a fruit tree and enjoy eating the fruit without selling any of it.
3. You could also grow a tree without edible fruit just to enjoy its beauty.

Which type of expense will be easier for most people to bear?

Most people will find it easier to spend money to grow the fruit tree if they can make money by selling the fruit. This is because it is an **income-making expense**.

If they sell the fruit, some of the money they spend to grow the tree will come back to them.

If they eat the fruit, they will enjoy it, but the money they spend to grow the tree will not come back to them. But they will save money because they will buy less fruit.



Analyzing expenses: income-making and non-income-making



Choose whether or not the following expenses will allow Shereen's family to earn money.

		Earns money	Does not earn money
1.	Shereen buys some books on financial planning to help her father plan his fruit expansion.		
2.	Shereen spends money to print a poster that invites students to take tuitions from her.		
3.	Ali spends money to put fertilizer on a fruit tree from which he will sell the fruit.		
4.	Ali spends money to put fertilizer on a fruit tree from which he will eat the fruit.		
5.	Nusrat buys a sewing machine to make clothes to sell.		
6.	Nusrat buys a sewing machine to make clothes for Ali and herself.		

The solution to this exercise can be found on page 185

BUSINESS INCOME, EXPENSES, PROFIT AND LOSS

Introduction

In this section, we will consider business income, expenses, profit and loss.



Shereen, age 22, has recently completed her Bachelor's in Business Studies. She has decided to join her father Safdar's fruit and juice business.

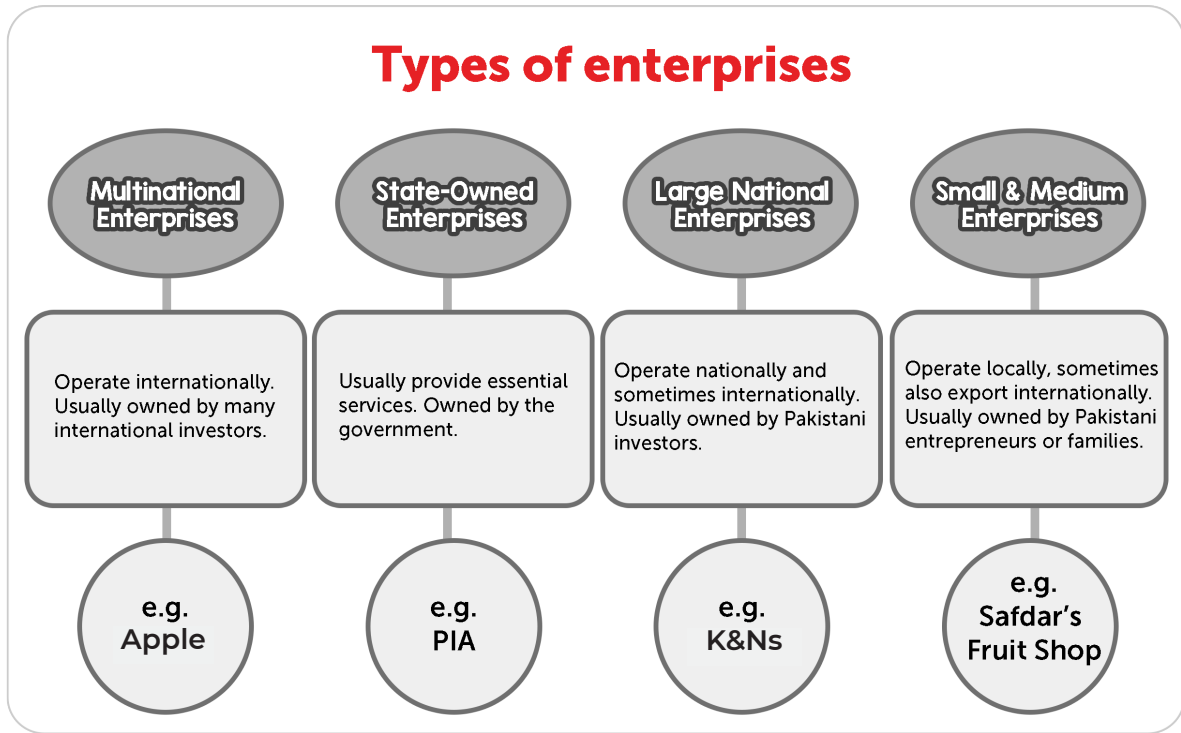
The family has recently put together a savings plan with a goal to save Rs. 3,600,000 in 5 years to pay for Daniyal's remaining university years and build a house. But the family budget shows that they will be about Rs. 1,000,000 short of the goal.

Rabia has committed to cut Rs. 200,000 from family expenses over the 5-year period. Safdar and Shereen have committed to make up the rest by expanding the business. They will need to increase their profit by Rs 800,000 over the 5 year period.

Shereen's cousin, Ali, also 22 years old, has also recently completed his Bachelor's in Computer Science. He has just taken up a job in programming. But he remains very interested in the fruit and juice business.

Introduction to enterprises

An enterprise, venture or business provides goods and services and expects to make a profit from this activity. Here are some important types of enterprises.

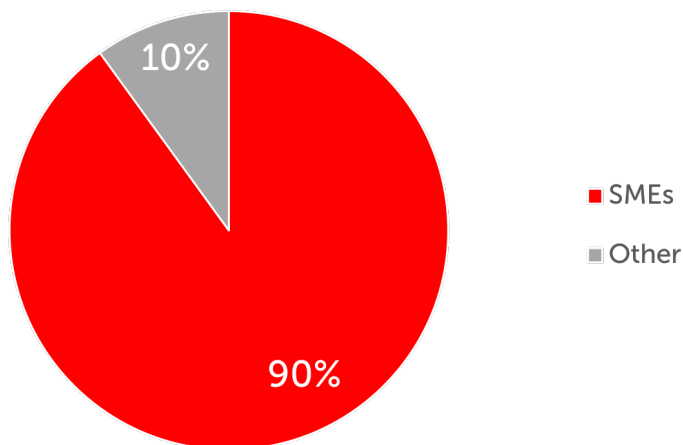


- ▶ **Multinationals:** These are large enterprises that usually operate in many countries in the world. They are usually owned by various investors from around the world.
- ▶ **State-Owned Enterprises:** These often provide essential services, such as transportation, electricity and gas. They are owned by the government.
- ▶ **Large National Enterprises:** These operate in many parts of the country and sometimes internationally too. They are usually owned by local investors.
- ▶ **Small and Medium Enterprises:** These range from very small (e.g., a local tea shop) to medium-sized businesses (e.g., a bakery with 12 shops). The investors in these businesses often also manage them.

Introduction to small and medium enterprises

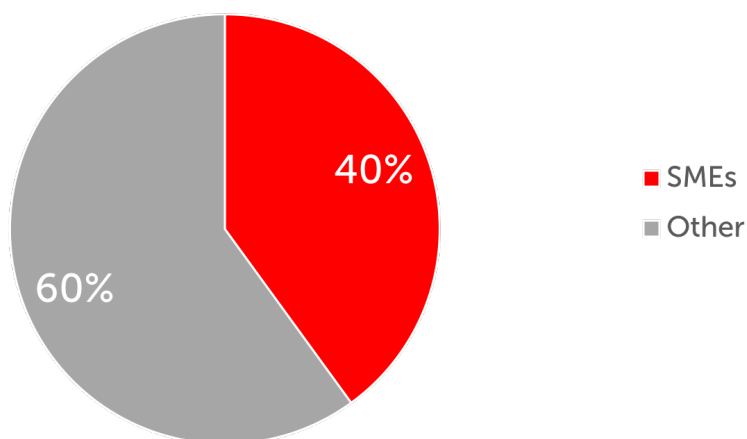
There are over 3.2 million enterprises in Pakistan and most of them are small or medium enterprises or SMEs!

SME Share of All Pakistani Enterprises



Source: Small and Medium Enterprises Development Authority

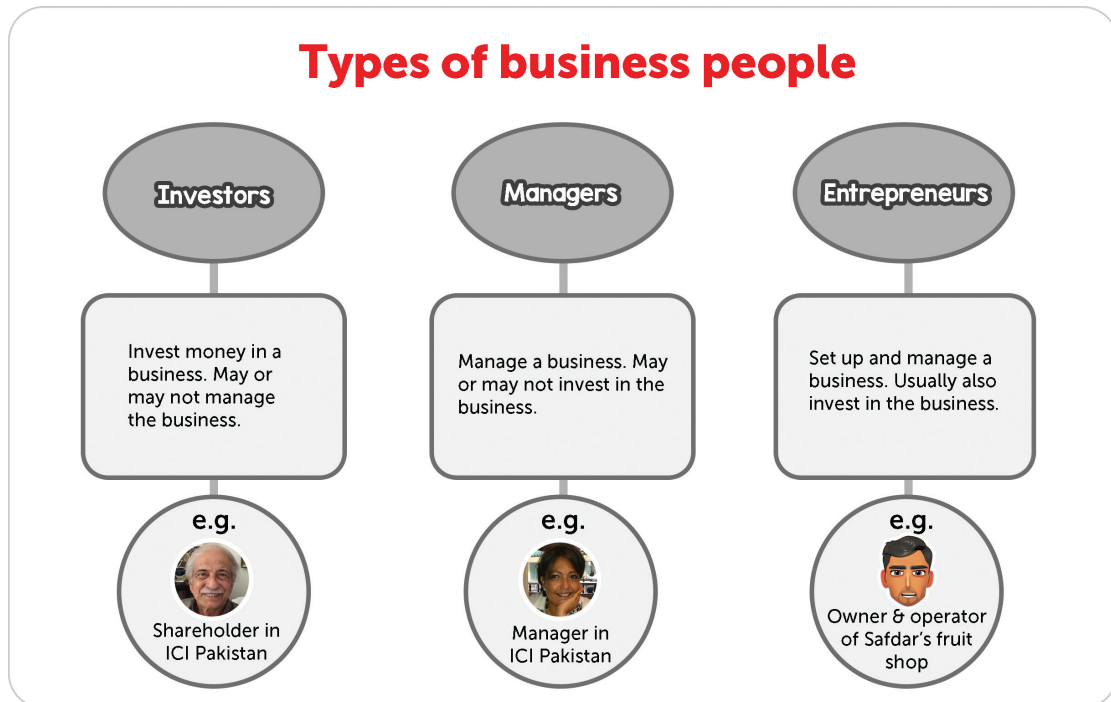
SME Share of Pakistani Gross Development Product



Source: Small and Medium Enterprises Development Authority

Small and medium enterprises are a very, very important part of the national economy. They have a lot of possibility to grow, add value and even export their goods and services.

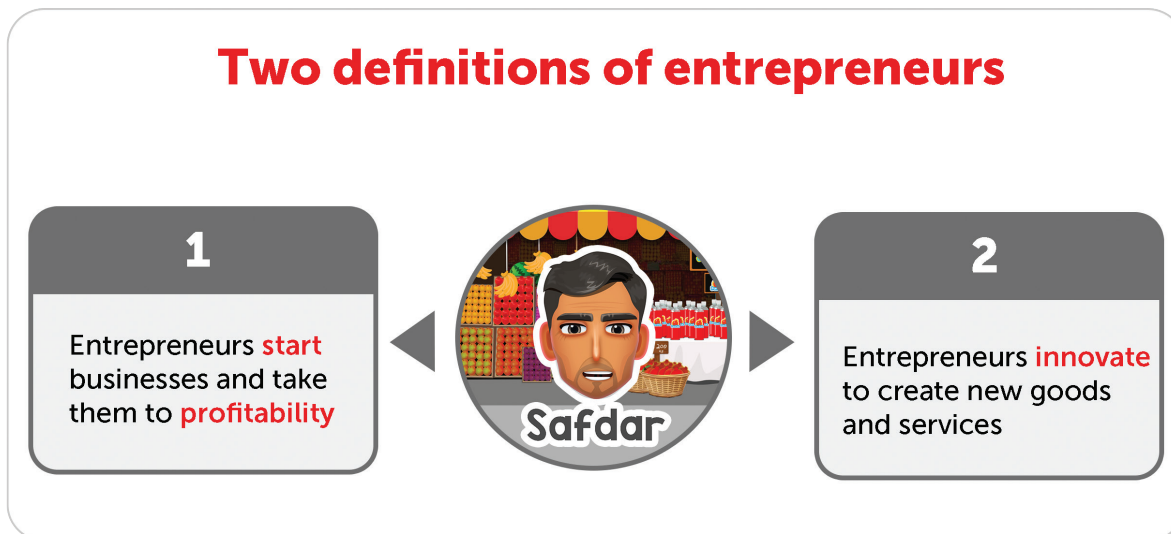
Types of business people



- ▶ **Investors:** They put money into or invest in businesses. Their investments are most important for a business to get started and grow. They may or may not be involved in managing the business.
- ▶ **Managers:** They are usually professionals who manage a business. They are most important for the growth of a business after it has been started. They may or may not invest in the business.
- ▶ **Entrepreneurs:** They are the founders of a business and usually also act as early investors in and managers of the business. They are most important for the founding and the early growth of a business.

The two roles of entrepreneurs

There are two popular descriptions of the role of entrepreneurs.



- **Taking a business to profitability:** Entrepreneurs start businesses and help them get to profitability. For example, a baker may set up a bakery, market his or her bread and cakes and work hard to make sure the business becomes profitable as soon as possible. He or she may simply copy what someone else has done, but still needs to use a lot of skill and hard work to make the business profitable.
- **Innovating to develop new goods and services:** Entrepreneurs also innovate to develop new goods and services. For example, a baker may set up a bakery, develop a new kind of pastry, market the pastry and work hard to make sure the business becomes profitable as soon as possible. He or she needs to use a lot of skill and hard work to develop the new pastry and make the business profitable.

Both types of entrepreneurs play an essential role in the growth of businesses. And the best entrepreneurs are good at both innovation and making businesses profitable!

Are you an investor, manager or entrepreneur?



For each ROW of three statements (Row 1 (yellow), Row B (white) and Row C (blue)), select the statement you

- ▶ agree with most (3 points);
- ▶ agree with second most (2 points); and
- ▶ agree with least (1 point).

Then total the points for each of the COLUMNS A, B and C.

State- ment Row		Points Column A		Points Column B		Points Column C
Row 1	I like starting new projects and coming up with new ideas.		I like to work in large and well-known institutions.		I like to profit from putting money in property, currencies and shares.	
Row 2	I like being my own boss and doing lots of different types of work.		I like to work in well-ordered teams with each team member having clear responsibilities.		I like to balance doing daily work and keeping time to benefit from changes in the market.	
Row 3	I am willing to put money in a business if there is a great reward and I can work in the business to make sure I get that reward.		A good, regular salary is very important for me.		I am willing to put money in 2-3 businesses from which I can get my money back easily.	
Total						

For feedback, see page 186

Income, expenses, profit and loss

Think about the relationship between income, expenses and profit and loss.



In the case of an individual, if income is greater than expenses, one will have savings.

In the same way, in the case of a business, if income is greater than expenses, it will have a profit.

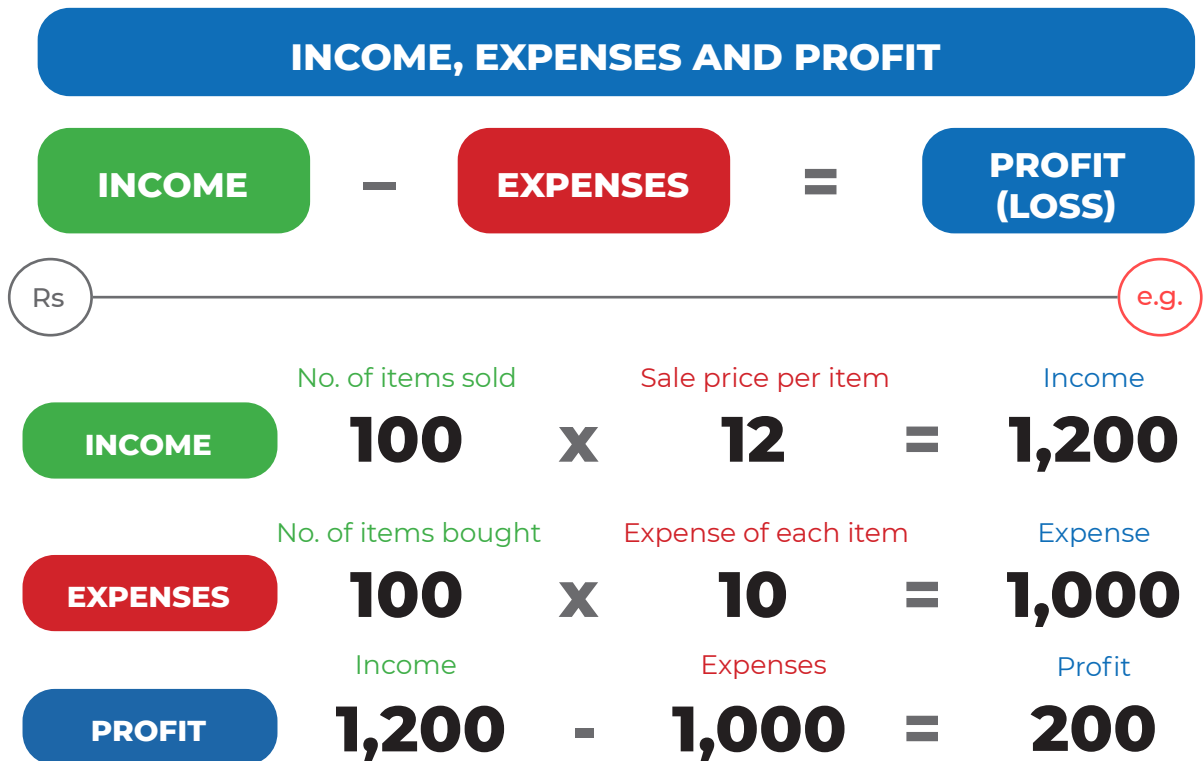
But, in the case of a business, if expenses are greater than income, it will have a loss.

Usually, a loss is written within brackets. In our example, profit is written as “200” and loss is written as “(100)”.

The most basic business calculations

The most basic calculations in a business relate to:

1. **Income** – price of goods sold \times quantity of goods sold; and
2. **Expenses** – expense of goods bought \times quantity of goods bought.



In the case of income, multiply the number of goods sold by the price at which you sold these goods. In our example, 100 items were sold at Rs. 12 each. This resulted in income of Rs. 1,200.

In the case of expenses, multiply the number of goods bought by the price at which you bought these goods. In our example, 100 items were bought for Rs. 10 each. This resulted in expenses of Rs. 1,000.

This is the basic calculation of a business. But there are other expenses too: salaries, equipment, rent, etc. We have provided you a simple example here. We will later look at a slightly more complex set of calculations.

Business loss, break even and profit

Because it takes time to get customers, businesses often start with losses, then go to break even and then to profits.

	Year 1	Year 2	Year 3	Year 4	Year 5
Income	1,000	1,500	2,000	2,500	3,000
Expenses	1,300	1,600	2,000	2,400	2,600
Profit (Loss)	(300)	(100)	0	100	400

	<div style="border: 1px solid red; background-color: red; color: white; padding: 5px; display: inline-block;">Loss</div>	<div style="border: 1px solid blue; background-color: blue; color: white; padding: 5px; display: inline-block;">Break Even</div>	<div style="border: 1px solid blue; background-color: blue; color: white; padding: 5px; display: inline-block;">Profit</div>
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- ▶ **Loss:** Often, in the early years of a business, expenses will be more than income. This will result in a loss. To have enough money to cover losses, business owners will invest money in the business.
- ▶ **Break Even:** Once there are enough customers and income increases, a well-managed business will get to break even. At this point, income and expenses equal each other. Business owners will plan for businesses to get to break even as fast as possible.
- ▶ **Profit:** If businesses are well-managed, as they grow customers and income, their expenses will increase at a slower rate. This will result in profits. Business owners will reinvest some of the profit in the business for it to grow in the future or to cover losses that may happen in the future.

Profit margin

Imagine that in one year: (1) Business A has Rs. 1,000 of income and Rs. 900 of expenses; and (2) Business B has Rs. 500 of income and Rs. 400 of expenses. Which business is more profitable? This is where the calculation of **profit margin** comes in!

Comparison of Two Businesses (Rs.)			
Income, Expenses & Profit		Business A	Business B
1.	Income	1,000	500
2.	Expenses	900	400
3.	Profit	100	100
4.	Profit margin	10%	20%

The profit margin of a business is calculated by, expressing as a percentage, its profit divided by its income (profit / income as %).

In our example:

1. Both businesses have a profit of Rs. 100 (income – expenses).
2. Business A has a profit margin of 10% (100 / 1,000).
3. Business B has a profit margin of 20% (100 / 500).

Both businesses have an equal level of profit (Rs. 100). But Business B has a much higher profit margin (20%) than Business A (10%). Business B is much more profitable than Business A.

Profit margin calculations tell you, that for every rupee a business makes, what percentage is profit. It is a basic but very useful ratio used for comparing the profitability of businesses.

Analyzing profit margin



In connection with making their family budget, Safdar and Shereen have made 5-year financial **projections** or financial estimates of the fruit and juice business.

Calculate their profit margin in each of Years 1 – 5.

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total income	10,875,000	12,547,500	14,346,400	16,800,000	19,500,000
Expenses						
2.	Total expenses	10,075,000	11,647,500	13,346,400	15,700,000	18,300,000
Profit (Loss)						
3.	Profit	800,000	900,000	1,000,000	1,100,000	1,200,000
4.	Profit margin					

Analyzing income, expenses and profit

Safdar and Shereen's 5-year financial projections show quite a low profit margin (not higher than 8% per year). When they discover that they need to make a greater profit to reach the family's savings goal, they analyze their projections in detail.

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total fruit (kg)	27,500	28,875	30,320	32,000	34,000
2.	Fruit price per kg	250	260	270	300	330
3.	Total fruit income	6,875,000	7,507,500	8,186,400	9,600,000	11,220,000
4.	Total fruit for juice (kg)	10,000	12,000	14,000	16,000	18,000
5.	Juice price per kg	400	420	440	450	460
6.	Total juice income	4,000,000	5,040,000	6,160,000	7,200,000	8,280,000
7.	Total income	10,875,000	12,547,500	14,346,400	16,800,000	19,500,000
Expenses						
8.	Total fruit (kg)	39,000	42,000	46,000	50,000	55,000
9.	Fruit expense per kg	200	210	220	235	250
10.	Total fruit expense	7,800,000	8,820,000	10,120,000	11,750,000	13,750,000
11.	Salary	-	-	-	-	-
12.	Rent	240,000	264,000	326,400	550,000	750,000
13.	Juice bottles & packaging	1,135,000	1,463,500	1,700,000	2,000,000	2,300,000
14.	Electricity, gas & other expenses	900,000	1,100,000	1,200,000	1,400,000	1,500,000
15.	Total expenses	10,075,000	11,647,500	13,346,400	15,700,000	18,300,000
Profit (Loss)						
16.	Profit	800,000	900,000	1,000,000	1,100,000	1,200,000

As we can see, the business' income comes from two calculations:

- ▶ Sales of fruit (calculated by multiplying (1) kg of fruit sold by (2) price of fruit per kg)
- ▶ Sales of fruit juice (calculated by multiplying (1) kg of juice sold by (2) price of juice per kg).

Similarly, the business' core expense comes from one core calculation:

- ▶ Expense of fruit purchased (calculated by multiplying (1) kg of fruit purchased by (2) price of fruit per kg).

The other components of expenses are:

- ▶ **Rent:** Rent for the fruit shop, where the juice is also bottled.
- ▶ **Salary:** There is no salary expense as the business is not paying anyone a salary.
- ▶ **Juice bottles & packaging:** Expenses for the bottles and packages for the fruit and juice.
- ▶ **Electricity, gas & other expenses:** Expenses for energy and other items.

Analyzing income, expenses and profit



Help Shereen analyze the projections by answering the questions below.

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total fruit (kg)	27,500	28,875	30,320	32,000	34,000
2.	Fruit price per kg	250	260	270	300	330
3.	Total fruit income	6,875,000	7,507,500	8,186,400	9,600,000	11,220,000
4.	Total fruit for juice (kg)	10,000	12,000	14,000	16,000	18,000
5.	Juice price per kg	400	420	440	450	460
6.	Total juice income	4,000,000	5,040,000	6,160,000	7,200,000	8,280,000
7.	Total income	10,875,000	12,547,500	14,346,400	16,800,000	19,500,000
Expenses						
8.	Total fruit (kg)	39,000	42,000	46,000	50,000	55,000
9.	Fruit expense per kg	200	210	220	235	250
10.	Total fruit expense	7,800,000	8,820,000	10,120,000	11,750,000	13,750,000
11.	Salary	-	-	-	-	-
12.	Rent	240,000	264,000	326,400	550,000	750,000
13.	Juice bottles & packaging	1,135,000	1,463,500	1,700,000	2,000,000	2,300,000
14.	Electricity, gas & other expenses	900,000	1,100,000	1,200,000	1,400,000	1,500,000
15.	Total expenses	10,075,000	11,647,500	13,346,400	15,700,000	18,300,000
Profit (Loss)						
16.	Profit	800,000	900,000	1,000,000	1,100,000	1,200,000

In Year 1, which business has greater income per kg of fruit sold, the sale of fruit or the sale of juice? Why?

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In Year 3, what is the total fruit expense expressed as a percentage of total income?

%

In Year 5, what is the total kg of fruit purchased and the total kg of fruit sold? What might be some reasons for the difference in these numbers?

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The solution to this exercise can be found on page 187


Analyzing the whole fruit and juice businesses

Safdar and Shereen next look at the cost per kg of both fruit sold as whole fruit and as juice.


Analysis of Profit per kg of Fruit in Year 1 (R.s)						
Income						
	Income	Fruit sold as whole fruit			Fruit sold as juice	
1.	Income per kg	250.00			400.00	
Expenses						
	Expense	Expense per kg	% for whole fruit	% for juice	Fruit sold as whole fruit	Fruit sold as juice
2.	Cost of fruit per kg				200.00	200.00
3.	Wasted fruit per kg	0.40	73%	27%	0.29	0.11
4.	Juice bottles & packaging	30.27	20%	80%	6.05	24.21
5.	Electricity, gas & other expenses	24.00	50%	50%	12.00	12.00
6.	Expense per kg				218.35	236.32
Profit (loss)						
7.	Profit per kg				32	164
8.	Profit margin				13%	40.9%




Shereen We get a lot more income from fruit sold as juice than from fruit sold as whole fruit!




Safdar Plus the juice business has a much better profit margin - more than double that of the whole fruit business!




Shereen But juice bottling and packaging costs are 4 times higher than packaging costs for whole fruit.



Safdar And, even though electricity and other costs are 50/50, we actually sell almost 3 times more whole fruit than juice. So, actual electricity and other costs for juice are much higher!



Shereen Abba, it clearly makes sense to grow the juice business!



Safdar I agree, but we must control bottling and electricity costs. And also reduce wastage of fruit!

Business expansion analysis

Having decided to expand the bottled juice business, Safdar and Shereen do a business expansion analysis. They compare the current business to an expanded bottled juice business.

Business Factor	Current Business	Expanded Business
Brand	Minimum branding. Juice is bottled but sold as “ generic ” product.	Will need to develop a popular, recognizable brand name and values.
Channel	Sold only through Safdar’s fruit shop.	Can be sold through Safdar’s fruit shop. Can also be sold through other shops in the city and through wholesalers.
Operating Expenses – Cost of Goods (Fruit)	There is no saving on fruit expense because amount of fruit purchased is low.	With more fruit purchased, fruit expenses may be lowered a little bit.
Operating Expenses – Cost of Goods (Bottling)	Expense of bottling per bottle is high because simple low-quality bottling equipment is used.	High-quality bottling equipment will bring down expense of bottling per bottle.
Operating Expenses – Cost of Goods (Transport)	No transport expense because bottled juice is sold through Safdar’s fruit shop.	Will need to add transport expense.
Other Operating Expenses – Marketing	No marketing expense.	Will need to spend on marketing to sell throughout the city.
Other Operating Expenses – Rent	No extra rent as bottling is done in Safdar’s shop.	In the short-term, no extra rent as expanded bottling can be done in Safdar’s shop.
Other Operating Expenses – Salaries	No salaries.	In the short-term, will need to hire two people.
Taxes	Small level of income taxes.	Higher level of income taxes.
Capital Expenses – Equipment	Juice making and low-quality bottling equipment already purchased.	Will need to purchase high-quality bottling equipment.

Business expansion analysis



If Safdar expands the bottled juice business, which expenses will go up and which will go down?

	Go Up	Go Down
1. Overall fruit expense		
2. Fruit expenses per bottle of juice sold		
3. Overall bottling expense		
4. Bottling expenses per bottle of juice sold		
5. Overall marketing expense		
6. Overall transport expense		
7. Equipment expense		

What is the most important difference between the type of expenses that will **go up** and the type of expenses that will **go down**?

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If Safdar wants to profitably expand the business its expenses will increase. To maintain a profit, what will need to happen to either number of items sold or price of items sold?

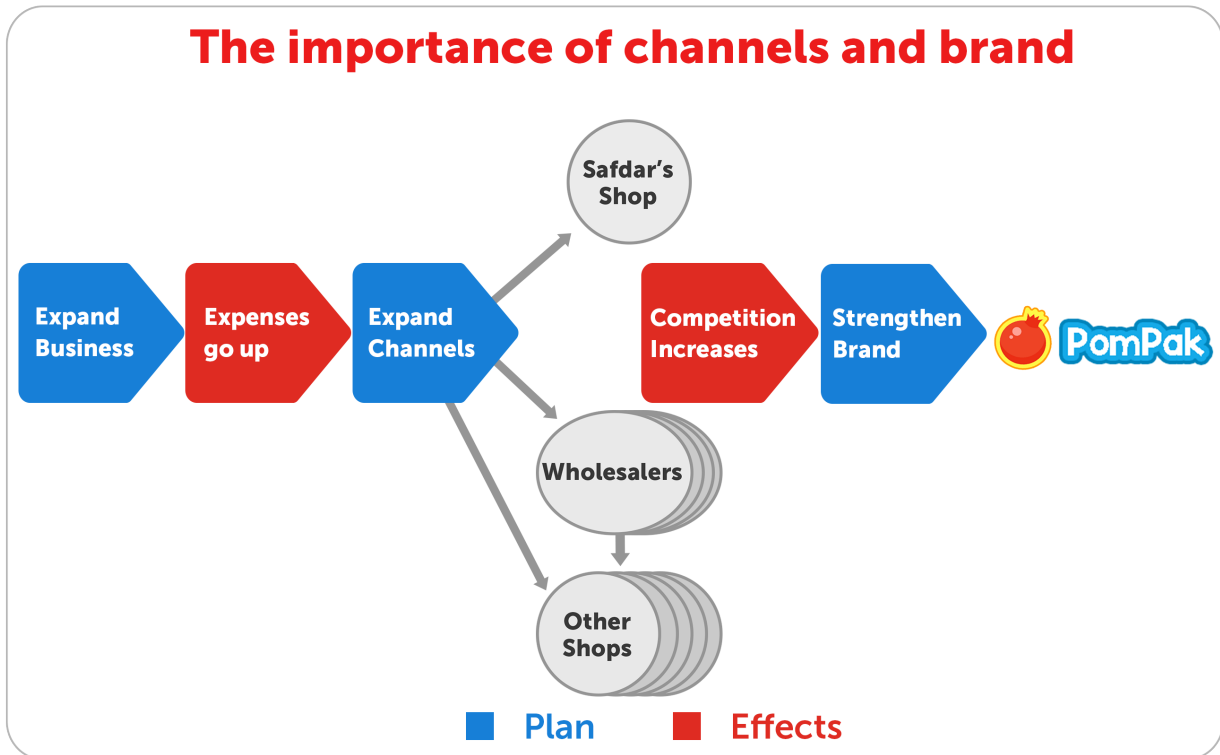
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The importance of channels and brand

If Safdar wants to expand his business, channels and brand will become much more important.



1. If Safdar plans to expand his bottled juice business, his expenses will go up.
2. To cover these expenses and make a profit, he will need to increase the number of items sold or the price of items sold, or both.
3. To sell more items, he will need to increase his channels, or the pathways he uses to sell his bottled juice.
4. He could increase his channels by selling his bottled juice BOTH in his own shop and in other shops in the city. He could also sell his bottled juice to wholesalers, who will sell to shops.
5. If he does this, he will face more competition from other sellers.
6. To successfully fight the competition, he will need a popular brand that people like and trust.
7. If he has a popular brand, he could sell more items and possibly charge more per item.

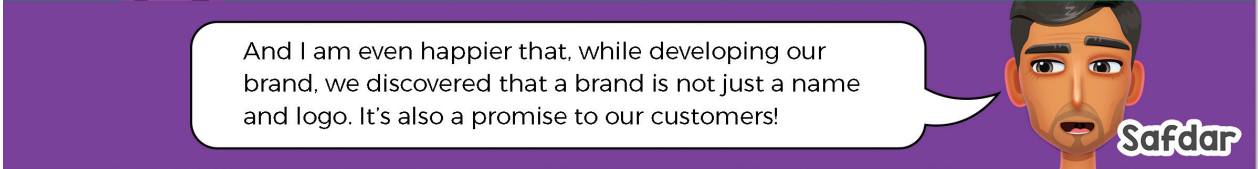
The meaning of brand

With help from Ali, Safdar and Shereen develop a new brand for the bottled juice: **PomPak**.



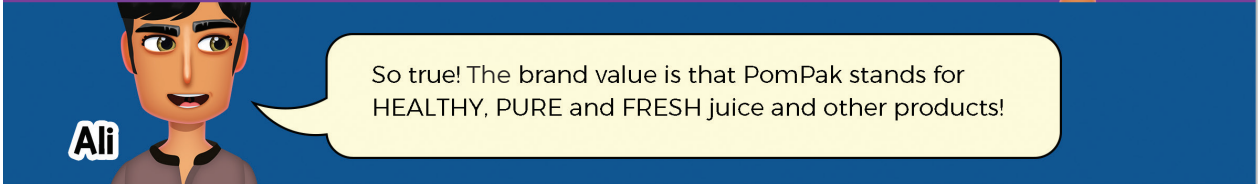
Shereen

I'm very happy! We have a friendly and modern brand name and logo.



Safdar

And I am even happier that, while developing our brand, we discovered that a brand is not just a name and logo. It's also a promise to our customers!

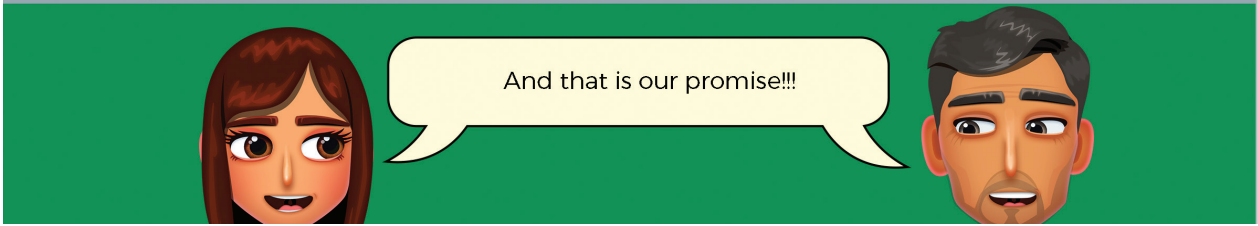


Ali

So true! The brand value is that PomPak stands for HEALTHY, PURE and FRESH juice and other products!

Brand name and values

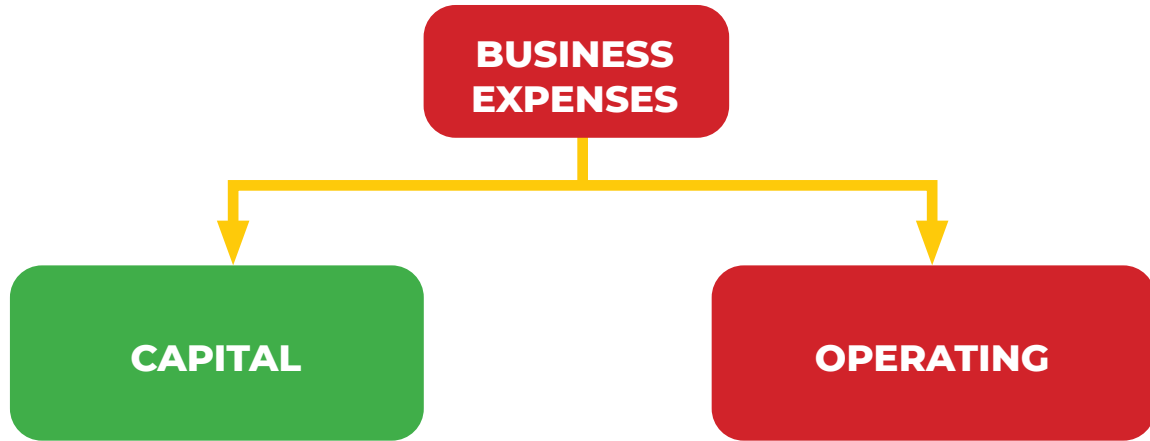
Name and Logo	Value
	<ul style="list-style-type: none">▶ Healthy▶ Pure▶ Fresh



And that is our promise!!!

Capital expenses and operating expenses

While working out their brand and marketing plan, Safdar and Shereen also put their numbers together. They look at both capital and operating expenses.



A **capital expense** is money spent by a business to purchase things that can be used over a long period of time. For example, land, buildings and production machinery are types of capital expenditures.

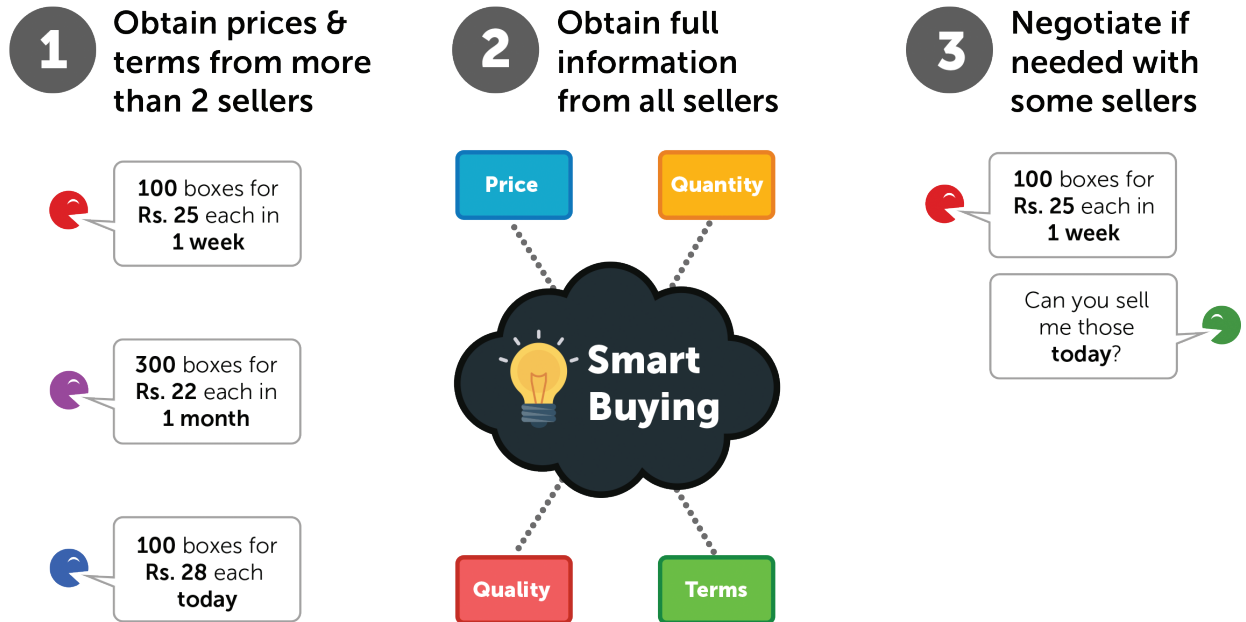
An **operating expense** is money spent by a business to operate on a regular basis. For example, a fruit shop will have operating expenses in the form of rent, fruit purchases and salaries.

The biggest capital expense for the bottled juice business is bottling and refrigeration equipment. If this equipment does not work well, it could result in big losses for the business. Safdar and Shereen research this possible expenditure as smart buyers.

Purchasing as a smart buyer

There are three major steps to becoming a smart buyer.

Smart Buying

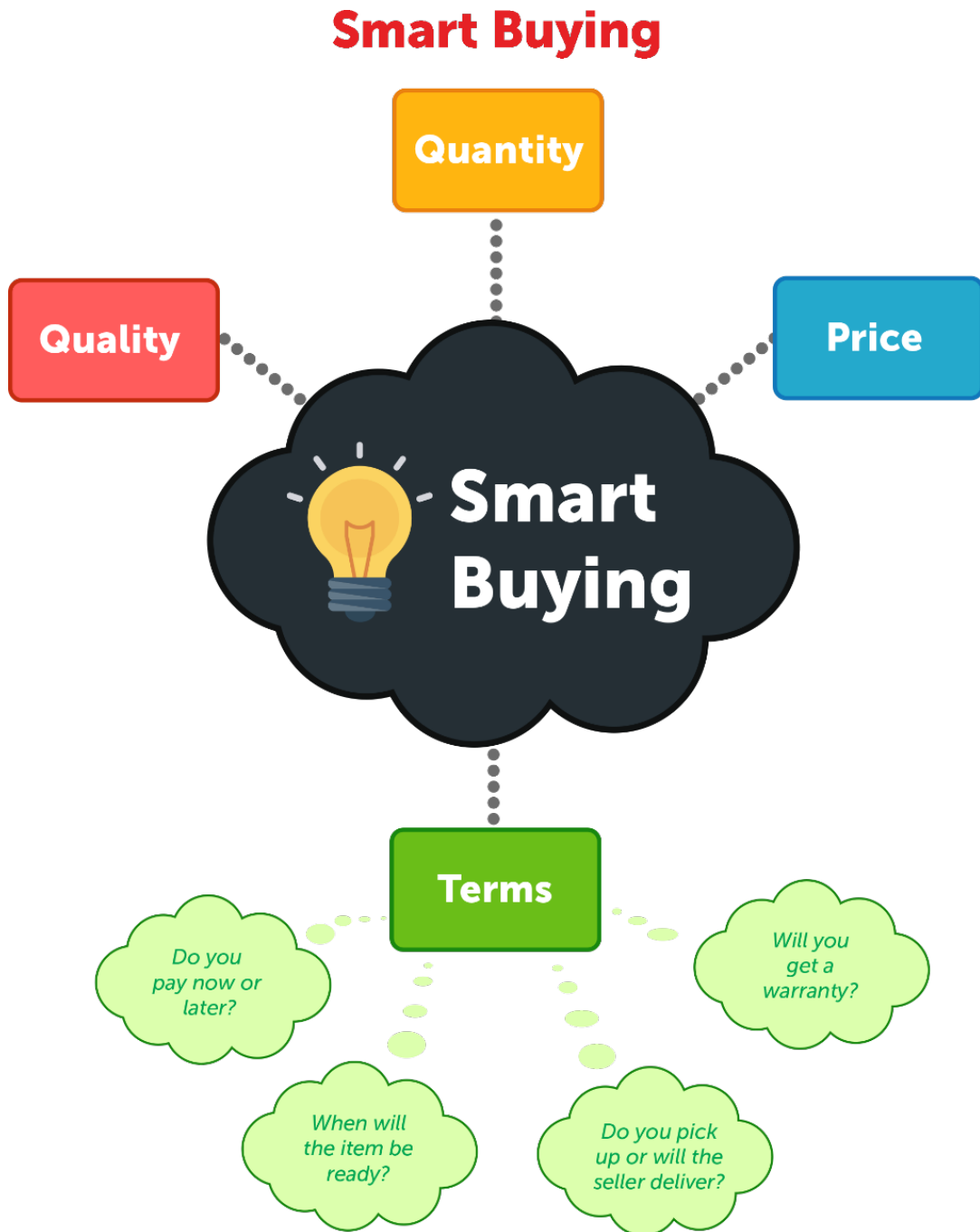


Things to check before buying something:

1. It's a good idea to get prices and terms from more than one seller.
2. It's a good idea to get all the information you need:
 - a. *Price* – what price the seller is offering.
 - b. *Quantity* – what amount of the product you want to buy.
 - c. *Quality* – what quality of product you are looking for.
 - d. **Terms** – all the conditions attached to the purchase.
3. Negotiate with sellers to lower price and improve quality and terms.

Smart buying terms

It is important to check the seller's terms before buying something.



Terms to check before buying something:

1. When is the payment for the purchase due? Can you pay now or later?
2. When will the product be ready?
3. Do you need to pick it up or will it be delivered?
4. Will you get your money back if the product is faulty or damaged?

Identifying smart buying practices



As smart buyers, Safdar and Shereen check with three sellers. The sellers have different points to make.

Can you tell what each statement or question is about?

	Quality	Quantity	Price	Terms
1. "We will deliver in 1 week"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
2. "I will sell this equipment to you for my cost plus 20%"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
3. "If the equipment does not work we will fix it for free"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
4. "We will give you the best performing equipment"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
5. "Will you pay 50% on signing?"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
6. "I will supply you 2 refrigeration units"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
7. "We will deliver and install the equipment for you"	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Are you a smart buyer?



Figure out what kind of a buyer you are by answering these 5 true or false questions.

	True	False
1. I almost always get prices from more than one seller.	<input type="checkbox"/>	<input type="checkbox"/>
2. I almost always check the quantity of what I am buying.	<input type="checkbox"/>	<input type="checkbox"/>
3. I almost always check the quality of what I am buying.	<input type="checkbox"/>	<input type="checkbox"/>
4. I almost always check when I need to make a payment.	<input type="checkbox"/>	<input type="checkbox"/>
5. I almost always check if I can get my money back if the product I buy is faulty.	<input type="checkbox"/>	<input type="checkbox"/>
6. Total true check marks.	<input type="checkbox"/>	

Type of Buyer	No. of True Check Marks
Very smart buyer	5
Smart buyer	4
Average buyer	3
Careless buyer	0-2

If you have 4 or more true check marks, you are a smart buyer!

Selecting the right seller and equipment



Help Safdar and Shereen select the right seller and equipment.

Seller	Price (Rs.)	Quality	Terms
A	3,500,000	Highest	4-year guarantee Free delivery only
B	4,000,000	Very high	5-year guarantee Free delivery and installation
C	2,500,000	Low	3-year guarantee Free delivery and installation

NOTE: Safdar and Shereen know that the staff of Seller A have made a mistake in pricing but probably will not find that out! Safdar and Shereen know that the correct price should be Rs. 4,500,000 not Rs. 3,500,000.



Which seller and equipment should they select? Should they select seller A and buy the equipment for Rs. 3,500,000? What is your reasoning?

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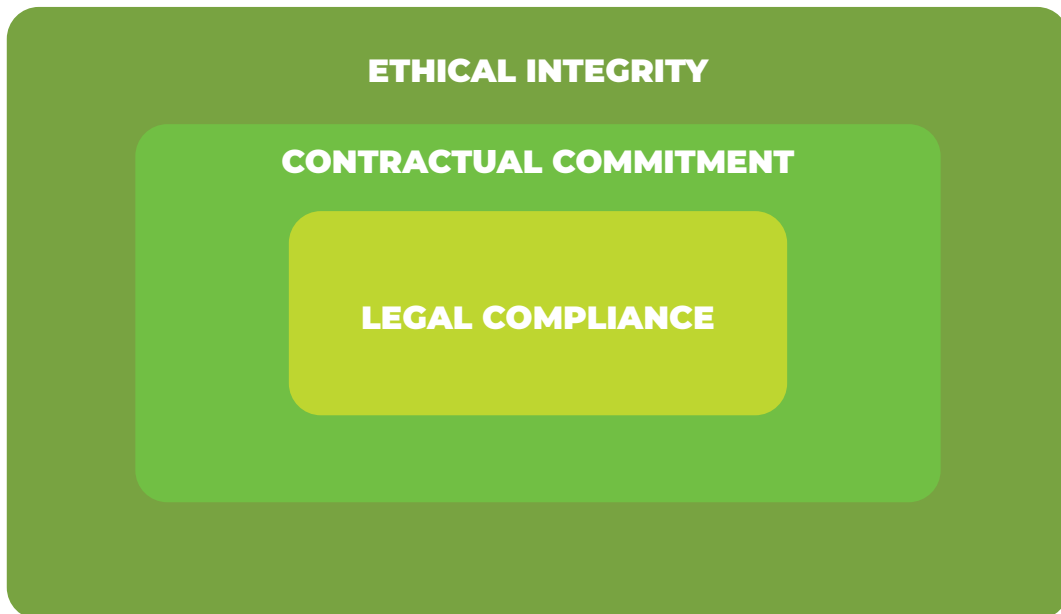
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What are your boundaries?

What are your boundaries: (1) legal compliance; (2) contractual commitment; or (3) ethical integrity?



Legal compliance: This involves staying within the boundaries of the law. For example, not engaging in corruption, fraud, theft and other specifically prohibited actions. *Would you violate the law? Would you violate the law if you are likely not to get caught? In Pakistan, many people don't pay their taxes fully. How about you?*

Contractual commitment: Contracts are between specific persons. They typically provide penalties if you violate them. *Would you violate your contracts? What if you contract to sell the only product you have for Rs. 1,000 and the penalty for violation is Rs. 100? Would you violate your contract and pay the penalty if someone offered you Rs. 1,200 for the same product? How about if someone offered you Rs. 1,500?*

Ethical integrity: Ethical integrity involves acting in a morally correct manner even if there is no specific legal requirement or contractual commitment. *If a seller makes a mistake in pricing would you tell him? If a competitor is likely to win some business, would you lie to win it instead?*

We believe that all individuals and businesses should comply with the law, respect their contracts and act ethically. They should do this because it is the right thing to do, not because of business reasons. But this also happens to make business sense!

Investment: fairness vs. practicality

In financial planning, we often need to think about fairness and practicality.

FAIRNESS
Are my actions fair to all involved?

PRACTICALITY
Will my actions help me meet my goals?

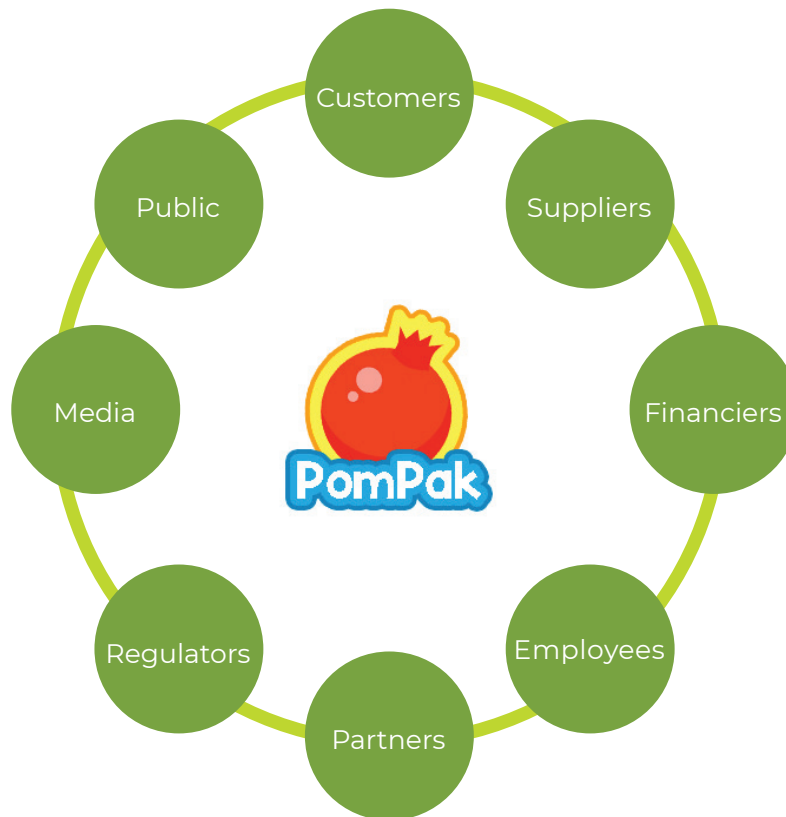
Most of the time, it is BOTH fair and practical to take an action.

Action	Fairness	Practicality
If one business partner puts in more work than the other, the first business partner gets extra shares or benefits.	This is fair because the first business partner has put in more work.	This is practical because if you do not give extra shares or benefits to the first business partner, they may put in less work.
If you have a commitment to one person (e.g., to sell a product), don't break that commitment even if you find a short-term benefit elsewhere (e.g., someone offers you more money for the same product).	This is fair because you have made a commitment and the first person trusts you will live up to your agreement.	This is practical because if you break your commitment, you will lose the trust of the first person. Over time, other people may also lose trust in you.

Making money vs. building a business

What is the difference between making money and building a business?

The web of relationships



You can make money by violating the law, violating your contracts and acting unethically. Many people do!

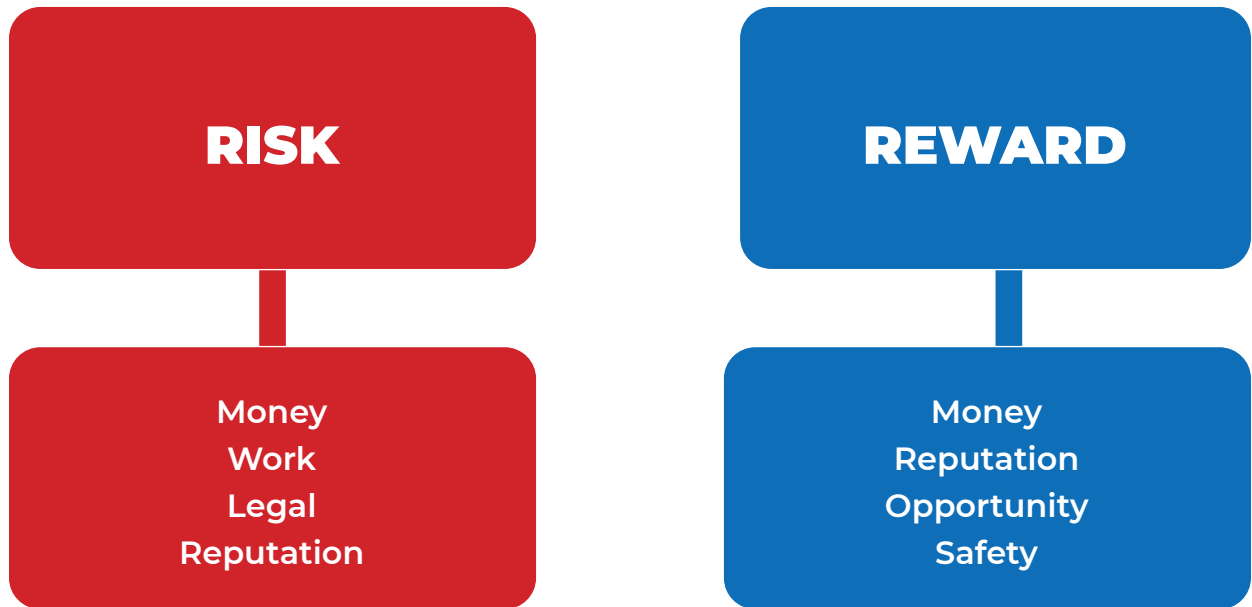
But making money is a one-time activity. *If you want to build a business, you need to develop and sell a product or service consistently over a long period of time. This involves building long-term relationships of trust. It means building a web of relationships.*

You could build a business by violating the law, violating contracts and acting unethically. But these kind of businesses usually fail. Businesses face many different kind of risks. If a business violates the law, it could face criminal and civil charges. If a business violates contracts, it could face lawsuits. If a business acts unethically, it could destroy its web of relationships.

That is why complying with the law, respecting contracts and acting ethically makes good business sense!

Risk and Reward

In business, you take a risk and expect a reward. What is the relationship between risk and reward?



Taking a risk does not always lead to a reward!

Only take a risk after planning and calculation!

Don't take risks that you cannot afford!

Your reward should be greater than the risk you take!

Take calculated, affordable risks that lead to important rewards!

Business risk management

We have just noted that a business faces risks if it violates the law or its contracts or acts unethically. Let's now place these risks in a fuller set of risks that a business faces.

Types of business risk



- ▶ **Legal risk:** Changes in laws may lead to a profitable business becoming unprofitable. Businesses could face legal risks from violations of law or contracts.
- ▶ **Financial risk:** Businesses could face financial risk if they cannot get financing or if financing expenses are too high. They could also face risks if they buy products overseas and the currency exchange rate goes down. They also face risks if they don't manage their money well.
- ▶ **Operational risk:** There are many, many operational risks. Key staff members could resign, retire or die. Buildings, equipment, inventory or business records may get destroyed. A business may lose key suppliers or customers.
- ▶ **Reputational risk:** Customers or suppliers begin to look at you as unreliable or untrustworthy. The media could publicise your failure. It is very, very difficult to recover from this kind of risk.
- ▶ **Competitive risk:** New competitors could come into the market and old competitors could launch new products and services. Competitors could cut prices. New technology may change your business.

You can reduce all risks by *careful business and financial planning*. You can deal with some risks by *complying with the law, respecting contracts and acting ethically*. You can deal with some risks through *insurance*.

Risk management analysis



Test your understanding of risk management. For each business situation, select the type of risk most clearly involved.

1. Your manufacturing equipment burns down. What kind of risk does this situation represent?

Reputational Risk Operational Risk Competitive Risk Legal Risk

2. A Facebook campaign spreads to your customers that you are selling out-of-date products.

Reputational Risk Operational Risk Competitive Risk Legal Risk

3. A foreign company sells products such as yours at low prices and with many varieties.

Reputational Risk Operational Risk Competitive Risk Legal Risk

4. The government passes a law requiring your business to obtain costly new licenses.

Reputational Risk Operational Risk Competitive Risk Legal Risk

5. The Pakistani Rupee goes down in value compared to the US Dollar, and the price of importing an essential raw material goes up.

Reputational Risk Financial Risk Competitive Risk Legal Risk

6. Your main supplier of packaging materials goes out of business.

Reputational Risk Operational Risk Competitive Risk Legal Risk

Managing risk through insurance

Unplanned expenses relating to loss of life, property or assets can have a major effect on your financial future. To manage and protect against such financial risks, we use insurance. Insurance is a mechanism by which risk is transferred from an individual or a business to an insurance company.

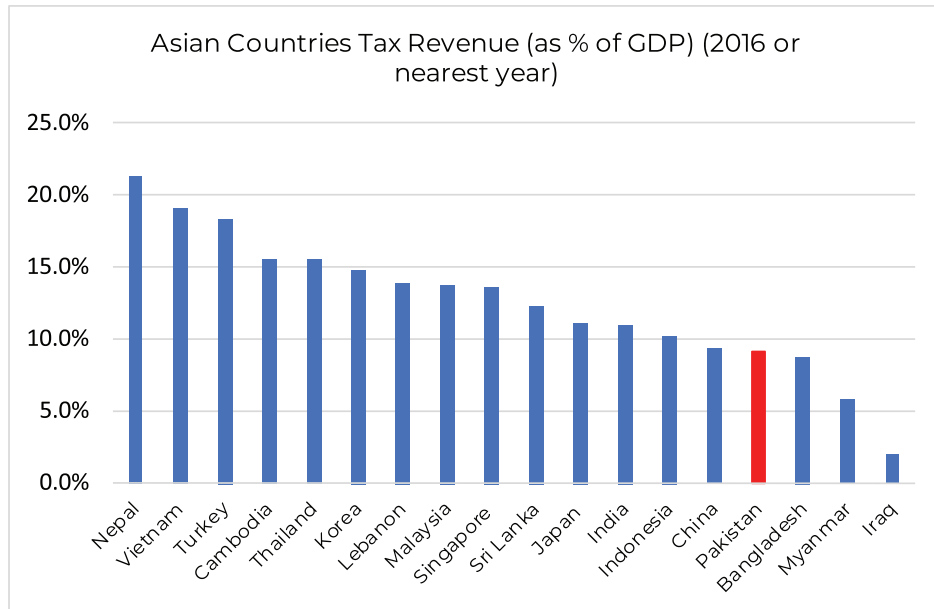
An insurance policy is a contract in which one party (insurer) agrees to pay another party (insured) in the event of a loss, in return for a small monthly fee or 'premium'. Premiums are affordable as the insurance company 'pools' many clients' risks. In the long-run, insurance is cheaper than having to replace assets using your own personal or business savings.

Types of Insurance				
	Type of Insurance	Personal	Business	Description
1.	Property	✓	✓	Pays for expenses of repair or replacement of property if the property is damaged, destroyed or stolen.
2.	Home	✓		Pays for expenses of repair or replacement of a home if the home is damaged or destroyed.
3.	Health	✓	✓	Pays for hospital and medical expenses in the case of an illness.
4.	Life	✓		In the event of the death of the insured, a named beneficiary receives the amount of the policy. Term life insurance can also be used as a savings tool, which pays out after a specified term is over.
5.	Automobile	✓	✓	Pays for automobile repairs and personal injury expenses in the case of an automobile accident.
6.	Livestock		✓	Pays the owner in case of death of livestock caused by natural causes, disease, accident or injury.
7.	Crop		✓	Pays the farmer in case of damage to crops by disasters including, rain, flooding, insect attack, fire or frost.
8.	Worker's compensation		✓	Pays a worker for any losses caused by injury at work and protects the employer from legal complications.

Managing risk through purchasing insurance is an important part of financial planning. Although generally used as a protection against risks, insurance products can also be used for investment purposes.

An introduction to taxes

Governments collect tax from individuals and businesses. The money collected through taxes is used to fund government expenses such as defence, development, education and health. In Pakistan, taxes are collected at both the federal and provincial level. But Pakistan ranks very low in its annual tax collections.



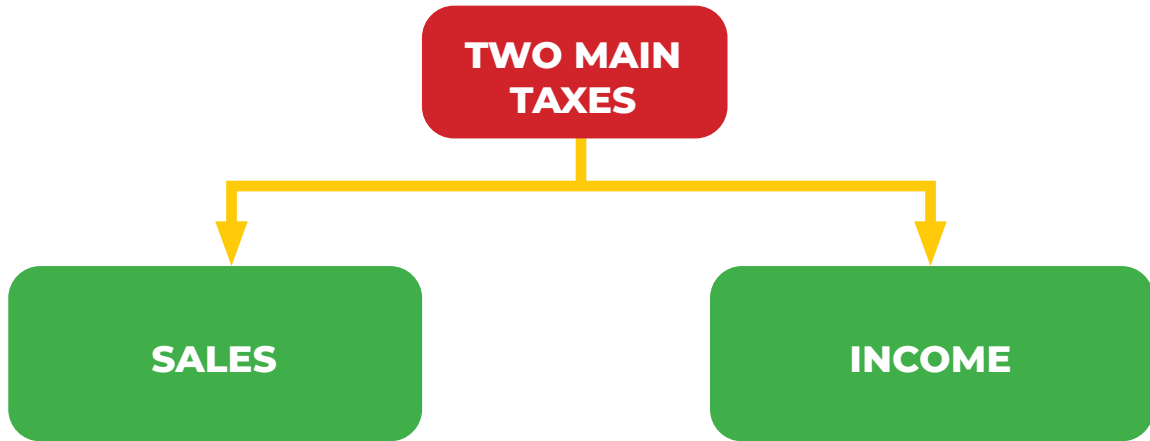
Source: The World Bank

Less than 1% of Pakistanis pay tax. As a result, the government always has very limited money to invest in development, education and health.

Until individuals and businesses in Pakistan decide to pay taxes, it will be extremely difficult for any government to invest properly in development, education and health.

Sales and income taxes

The Government of Pakistan imposes many different types of taxes on individuals and businesses. Two important taxes are sales tax and income tax.



SALES TAX

Sales tax is a tax imposed by government on the sales of certain goods and services. This tax is required to be collected by the seller from the buyer at the point of purchase and passed on to the government.

For example, if the bottling equipment seller sells equipment to Safdar's business, it will be required to charge a sales tax that is a % of the price of the equipment. The money so collected must be passed on to the government.

INCOME TAX

Income tax is a tax imposed by government on the income of individuals or the profits of businesses or companies. This tax is a % of the income of individuals or the profits of businesses or companies. This tax is required to be reported and paid by the individual or business on whom the tax is imposed.

For example, Safdar's business is set up as a company and it must pay income tax. Every year, it reports its profits to the government and pays a % of its profits to the government as income tax.

Tax analysis



Test your understanding of basic taxes by answering the questions below.

1. Which tax does a business collect directly from customers and pay over to the government?

Income Tax **Sales Tax**

2. A furniture business sells a table for Rs. 10,000. It collects Rs. 11,700 from the customer for the price of the table plus tax payable by the customer. What kind of tax is this?

Income Tax **Sales Tax**

3. A business makes a profit of Rs. 400,000 and it pays the government a tax on this profit of Rs. 29,000. What kind of tax is this?

Income Tax **Sales Tax**

4. A business is subject to 15% sales tax and 30% income tax. Calculate how much sales tax and income it will need to pay.

	Category	Amount (Rs.)	Sales Tax (Collected from Customers) (Rs.)	Income Tax (Rs.)
1.	Income from product sales	500,000	<input type="text"/>	
2.	Business expenses	300,000		
3.	Profit	200,000		<input type="text"/>

The solution to this exercise can be found on page 192

Financial projections for the business

After a lot of work, Safdar and Shereen put together financial projections for the new business.

		Fruit and Juice Business (Rs.)				
		Year 1	Year 2	Year 3	Year 4	Year 5
		Income				
1.	Total fruit (kg)	27,500	28,875	30,320	32,000	34,000
2.	Fruit price per kg	250	260	270	300	330
3.	Total fruit income	6,875,000	7,507,500	8,186,400	9,600,000	11,220,000
4.	Total fruit for juice (kg)	40,000	48,000	57,600	69,120	82,944
5.	Juice price per kg	400	420	440	450	460
6.	Total juice income	16,000,000	20,160,000	25,344,000	31,104,000	38,154,240
7.	Total income	22,875,000	27,667,500	33,530,400	40,704,000	49,374,240
		Expenses				
8.	Total fruit (kg)	70,875	80,719	92,316	106,176	122,791
9.	Fruit expense per kg	190	195	200	210	220
10.	Total fruit expense	13,466,250	15,740,156	18,463,200	22,296,960	27,014,064
11.	Salary	800,000	960,000	1,152,000	1,382,400	1,658,880
12.	Marketing	800,000	960,000	1,152,000	1,382,400	1,658,880
13.	Rent	240,000	264,000	326,400	550,000	750,000
14.	Juice bottles & packaging	1,920,000	2,419,200	3,041,280	3,732,480	4,578,509
15.	Transport	800,000	1,008,000	1,267,200	1,555,200	1,907,712
16.	Electricity, gas & other expenses	1,600,000	2,016,000	2,534,400	3,110,400	3,815,424
17.	Equipment	-	-	-	-	-
18.	Total expenses	19,626,250	23,367,356	27,936,480	34,009,840	41,383,469
		Profit (Loss)				
19.	Before tax profit	3,248,750	4,300,144	5,593,920	6,694,160	7,990,771
20.	Income taxes (assumed at 29%)	942,138	1,247,042	1,622,237	1,941,306	2,317,324
21.	After tax profit	2,306,613	3,053,102	3,971,683	4,752,854	5,673,448
22.	Profit margin	10.08%	11.03%	11.85%	11.68%	11.49%

The new equipment will allow juice bottling to be increased by at least 400%.

Salary expenses have been added.

Marketing expenses have been added.

Transport expenses have been added.


Incomes taxes have been added at an assumed rate of 29% per year.

Profit margin is calculated on after tax profit.

But there is one big problem: **Rs. 4,000,000 of capital expenditures have not been counted.** The business just does not have the money to expand. What is to be done?

How do you get funding for expansion?

Safdar and Shereen have found and researched an exciting opportunity to expand the family business. But how do they take PomPak from an idea to a reality? They need Rs. 4,000,000 to purchase equipment. There are three main options available to them.

			
Main funding options			
Option	Business Savings	Loan	Equity
Action	Wait until business cash savings build up, then buy the equipment	Obtain equipment financing to get the equipment	Obtain equity investment
+	Don't need to rely on outsiders	They don't have to give up an ownership interest in the business	They only pay investors if there are profits
-	This may not happen or opportunity may pass	If they cannot pay, the equipment could be taken back and they will still have to pay	They have to give an ownership interest in the business to the investor

What would you do?

This is a question of judgment.

If Safdar and Shereen wait until business cash savings build up and then buy the equipment, this may take years. The opportunity may go away and equipment costs may rise due to inflation.


If they have done proper business projections, and find that they can safely make payments for equipment financing through a loan, this may be the best option. However, more research is needed. They should talk to some banks and other financial institutions.

If they take in equity investment, they will give up an ownership interest in the business. Perhaps it is better to first research the equipment financing option.


Using projections

After completing the initial projections, Shereen looks them over with Ali.


Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
1.	Before tax profit	3,248,750	4,300,144	5,593,920	6,694,160	7,990,771
2.	Income taxes (assumed at 29%)	942,138	1,247,042	,622,237	1,941,306	2,317,324
3.	After tax profit	2,306,613	3,053,102	3,971,683	4,752,854	5,673,448
4.	Profit margin	10.08%	11.03%	11.85%	11.68%	11.49%




Look at how strong the profit is if you expand the juice business!



These numbers are not complete. We haven't included the numbers for equipment expenses. That's 4,000,000 rupees!




I know. But let's say you took financing for 4,000,000 rupees and you paid it back in 5 years. Even if you gave a 20% profit on that each year to the bank, you would still have plenty of profit left over each year.



That's very true! We can easily afford to repay 800,000 or even 1,000,000 per year plus pay a profit to the bank! Our first year profit before financing expenses is over 2,000,000 rupees. Let's discuss this with abba.

Shereen and Ali make their case to Safdar. He agrees.



Shereen and Ali. Good thinking! It will be quite safe to get financing for 4,000,000 rupees. We can easily pay it back from the cash flow of the business. Let's do some homework by talking to some banks.

BANKING AND BANK FINANCE

Introduction

In this section we will consider business banking and borrowing.



Safdar and Shereen, with some help from Ali, have put together financial projections for PomPak. This is an exciting opportunity to expand the family business. Fresh, bottled PomPak fruit juices will be sold throughout the city, not just from Safdar's store.

But to get the business going, they will need to make capital expenses of Rs. 4,000,000 for bottling and refrigeration equipment. The business does not have the cash to do this, and Safdar and Shereen decide to look at equipment financing options.

Their research will take them through Pakistan's banking system and teach them the basics of borrowing.

The State Bank of Pakistan

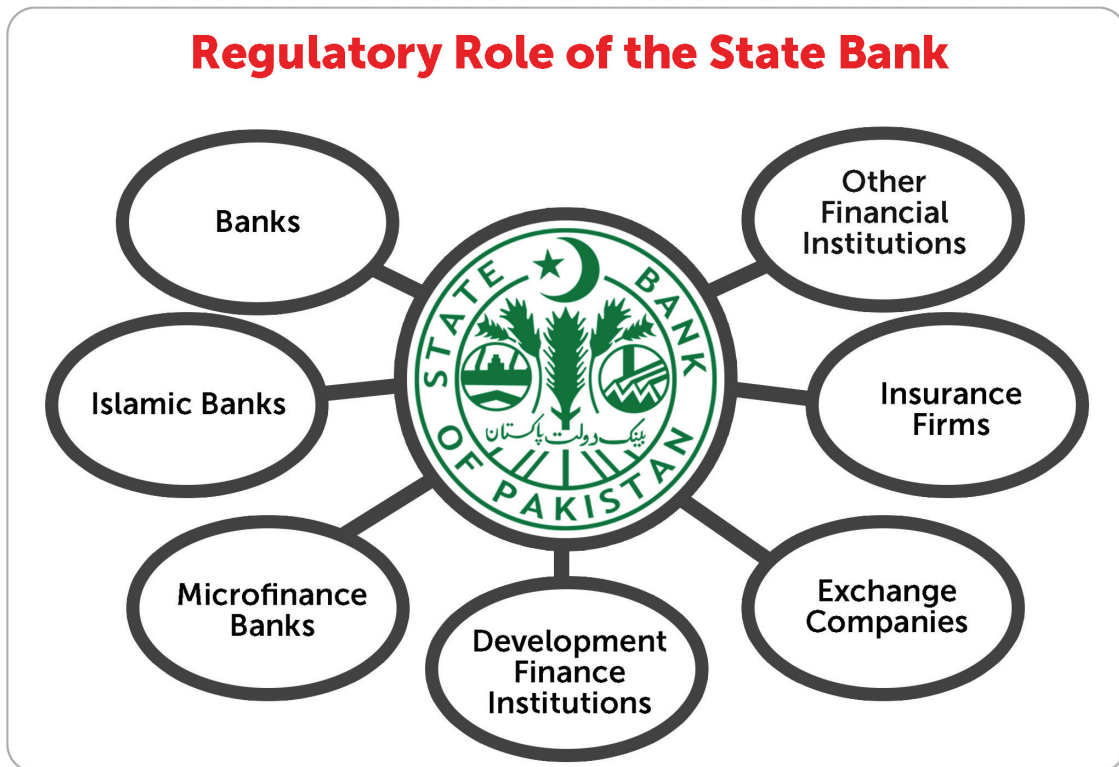
The State Bank of Pakistan is the central bank of the country. It plays a central role in the country's economy.



- ▶ **Issue currency:** The State Bank issues Pakistan's currency and controls the amount of currency in circulation.
- ▶ **Regulate the financial sector:** The State Bank regulates and supervises banks and other financial firms to make sure that they are managed soundly.
- ▶ **Protect consumers:** The State Bank protects the rights and interests of consumers when they deal with banks and other financial institutions.
- ▶ **Manage foreign exchange reserves:** The State Bank manages and invests Pakistan's foreign currency reserves.
- ▶ **Manage the rupee exchange rate:** The State Bank manages the exchange rate between the Pakistani Rupee and other foreign currencies.
- ▶ **Manage money supply to keep prices stable:** The State Bank uses its control of money supply to try to keep prices stable and manage inflation.
- ▶ **Manage money supply to promote growth:** The State Bank uses its control of money supply to try to make borrowing easier and promote growth.
- ▶ **Promote economic development in Pakistan:** The State Bank uses its role as the central bank and as the supervisor of the private sector to promote economic development in Pakistan.

The State Bank of Pakistan

In most countries, the banking system is supervised by the central bank. Similarly, in Pakistan, the State Bank of Pakistan, the country's central bank, regulates banks and other financial institutions.



The State Bank of Pakistan regulates banks and other financial institutions to make sure:

Soundly managed banks: Banks and other financial institutions are soundly managed.

Consumer protection: Customer deposits are secure and their rights are protected.

Fair rates for services: Bank service

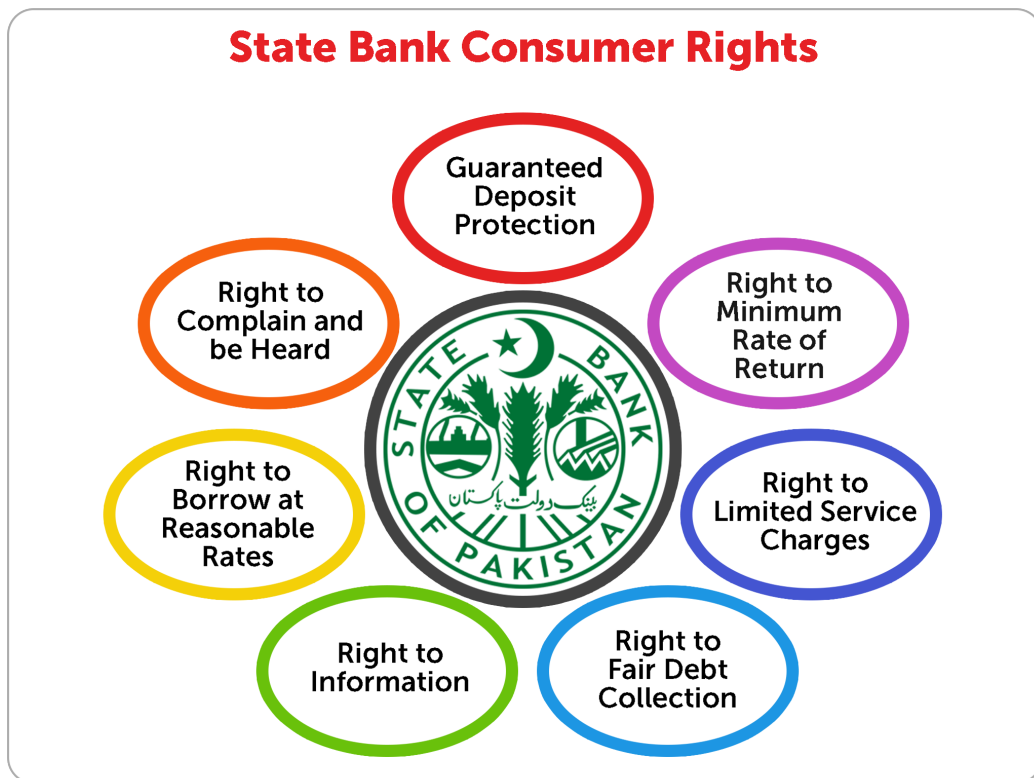
charges to customers are fair and reasonable.

Fair savings rates: Banks provide fair and reasonable savings rates to customers.

Fair lending practices: Banks make loans to customers on a fair and reasonable basis.

State Bank consumer rights

When you open an account, make a deposit with or take a loan from a bank, you become a consumer or customer of banking services. A bank is more powerful than its customers. This makes it easy for a bank to treat its customers unfairly. To protect customers and their money, the State Bank of Pakistan makes sure that banks respect consumer rights.



Guaranteed deposit protection: The State Bank protects a depositor’s money in case a bank closes. The State Bank guarantees that all or part of the money in a deposit will be paid back to the depositor.

Fair rates for services: The State Bank requires banks to charge customers fair and reasonable service charges.

Fair savings rates: The State Bank requires banks to provide their customers with a minimum profit rate on savings accounts.

Fair borrowing rates: The State Bank requires banks to lend money to their customers at fair and reasonable rates.

Right to fair loan collection: The State Bank requires financial institutions to follow strict guidelines in their loan collection efforts. This includes giving borrowers enough time to repay their loans.

Right to information: You have the right to access information regarding your financial activities from banks. Banks are also required to protect your personal information.

Right to complain and be heard: The State Bank requires banks to follow guidelines in handling customer complaints.

To ensure consumer protection through the services mentioned above, the State Bank established the Banking Conduct & Consumer Protection Department (BC&CPD) in 2020, previously known as the Consumer Protection Department (CPD).

Role of BC&CPD

The BC&CPD focuses on two main aspects to protect the rights of consumers.

1. **Development of Guidelines for Financial Institutions:** The BC&CPD establishes guidelines for financial institutions to ensure that consumers are not exploited by new companies emerging because of the rapid pace of financial innovation. The guidelines and frameworks developed by the BC&CPD aim to provide a safe and secure environment for consumers to engage with financial institutions.

2. **Consumer Awareness and Education:** The BC&CPD develops resources to educate consumers and conducts awareness sessions to increase their financial literacy. These resources are available on the State Bank's website and cover topics such as managing finances, avoiding fraud, and understanding financial products.

Role of BMP

The Banking Mohtasib Pakistan (BMP) is an independent grievance forum established by the State Bank to address consumer complaints. The BMP provides a means for bank customers to lodge complaints and have them resolved in a timely and efficient manner.

The BC&CPD handles urgent complaints that require immediate action, while the BMP investigates complaints that require further examination. Consumers can track their complaints through the BMP website and receive updates on their status.

The table below summarizes the responsibilities of the two agencies.

Agency	Responsibilities
Banking Conduct & Consumer Protection Department (BC&CPD)	Establish guidelines for financial institutions and educate consumers through awareness sessions and resources
Banking Mohtasib Pakistan (BMP)	Address consumer complaints and provide a means for consumers to lodge and track their complaints

Links:

- BC&CPD Resources: <https://www.sbp.org.pk/cpd/cpd-edu.asp>
- BMP Complaints: <https://www.bankingmohtasib.gov.pk/>

Knowing the State Bank



Figure out how much you know by answering these 5 true or false questions.

True

False

- 1. The State Bank issues Pakistan's currency (rupees).

- 2. The State Bank loans money to businesses and individuals.

- 3. The State Bank manages Pakistan's foreign currency reserves.

- 4. The State Bank sets electricity and gas prices in Pakistan.

- 5. The State Bank owns all the banks in Pakistan.

- 6. The State Bank regulates all the banks in Pakistan.

- 7. The BC&CPD protects the rights of financial institutions.

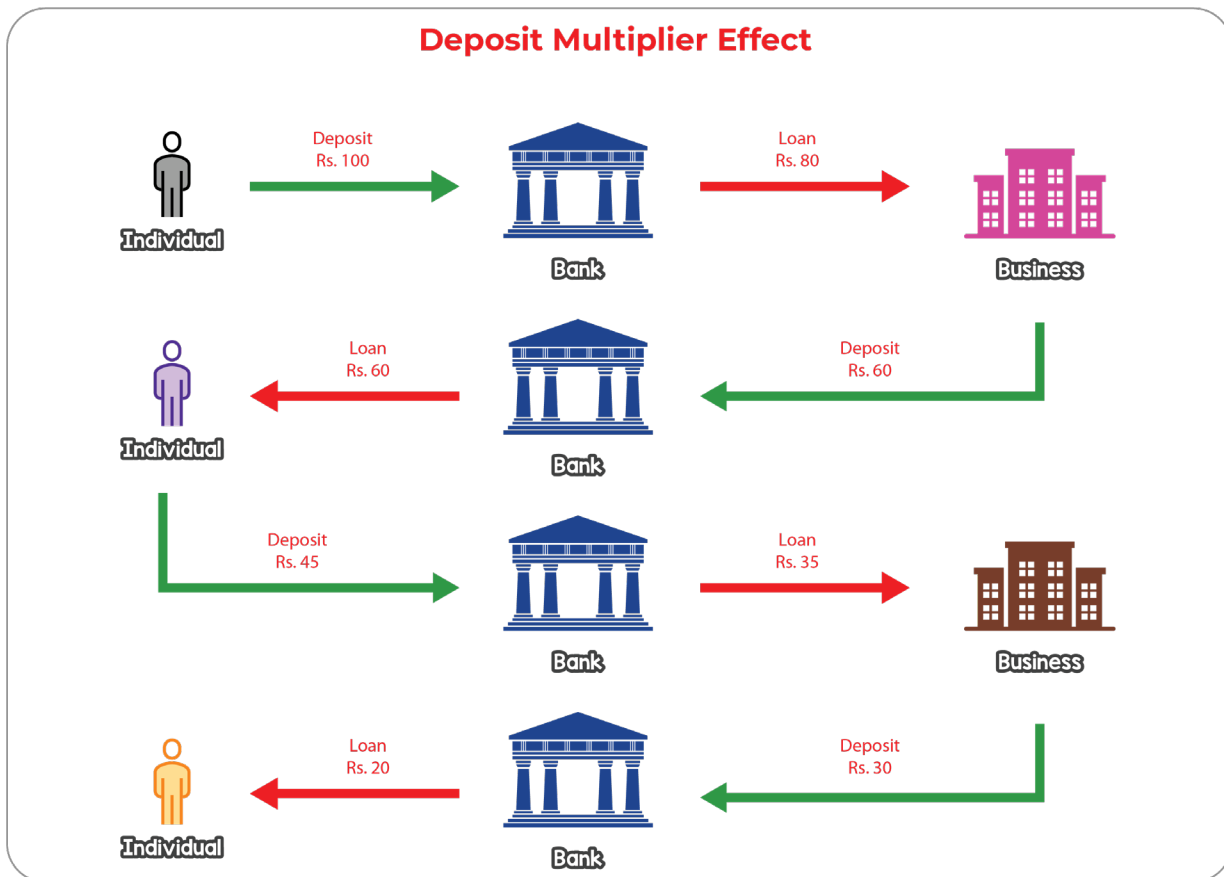
- 8. The BC&CPD and BMP work together to establish guidelines, educate consumers, and address complaints.

- 9. The BMP provides a means for bank customers to lodge complaints and have them resolved in a timely and efficient manner.

- 10. The BC&CPD only focuses on developing guidelines for financial institutions.

The Deposit Multiplier Effect

When you save money in a bank, it has a 'deposit multiplier effect.'



When you save money in a bank, the bank will lend a portion of that money to other individuals and businesses.

The borrowers will use that money to buy goods and services. A portion of the income generated from this new economic activity will go back into banks as savings.

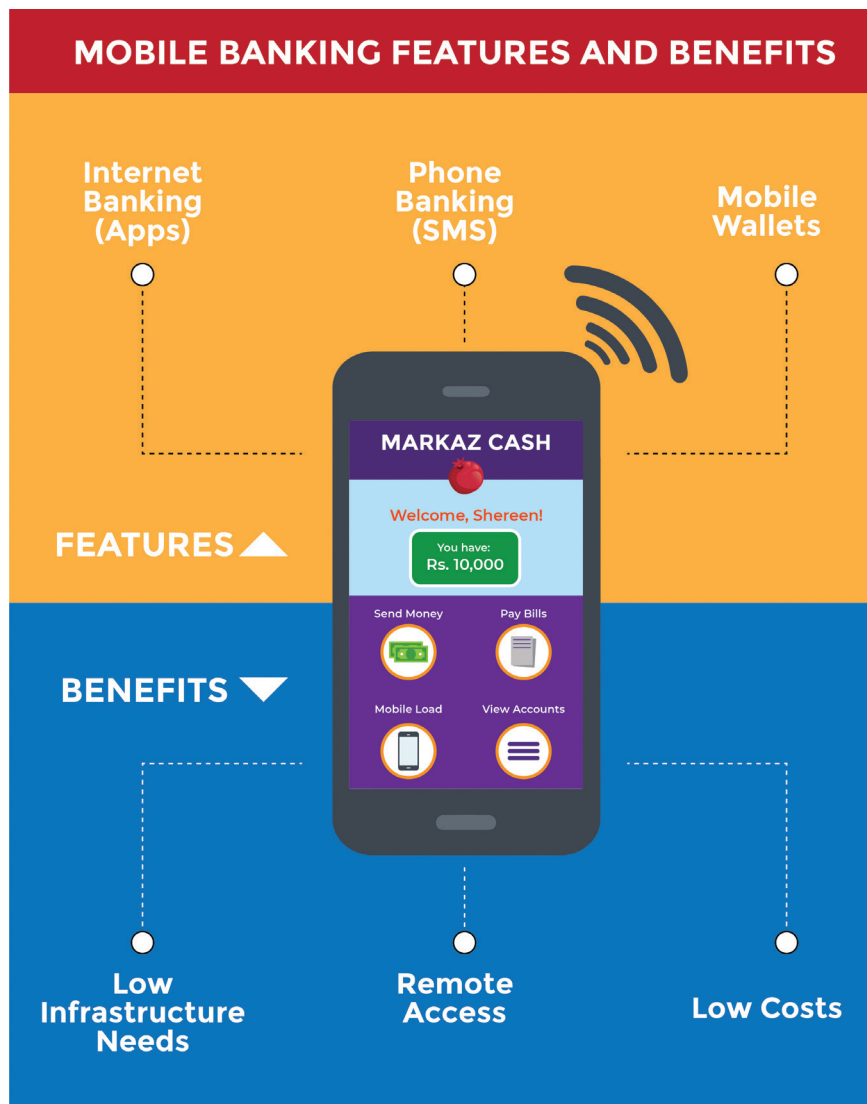
The banks will then have additional money to lend out to other individuals and businesses. This will, in turn, generate further economic activity which will result in more money being deposited into banks as savings. And the process will repeat itself.

Therefore, each Rupee saved in a bank has a 'deposit multiplier effect' – it leads to additional economic activity.

In this way, saving money in a bank not only provides benefit to the person doing the saving but also to the economy as a whole.

Mobile banking

Mobile banking offers customers many advantages.



With mobile banking you can use your mobile phone to perform basic banking activities such as:

- ▶ Check account details,
- ▶ Pay utility or mobile bills,
- ▶ Transfer money between your accounts or to others, and
- ▶ Find your nearest bank branch or ATM.

As mobile banking does not require a physical branch to use, banks normally charge lower rates from mobile banking customers.

Major differences between conventional finance and Islamic finance

Pakistan has two finance systems in place: conventional finance and Islamic finance. The State Bank regulates both sectors. Individuals and businesses in Pakistan are free to choose which system they use.

The following chart identifies the key differences between the two systems.

Key differences between conventional finance and Islamic finance		
Aspect	Conventional Finance	Islamic Finance
Sources of law	Parliament, which looks to international practices in finance and trends in financial sector laws.	The Shariah , constituting the Holy Quran and Hadith (sayings) of the Prophet Muhammad (peace be upon him), as supplemented by juristic interpretations by Islamic scholars.
Purposes	To enable individuals and businesses to engage in commercial and financial activities according to rules that balance (1) economic efficiency and (2) compliance with applicable laws, including those relating to contracts, disclosure and fair dealing.	To encourage individuals and businesses to act in accordance with the shariah and to promote (1) social solidarity, (2) justice, (3) social welfare, (4) fair and ethical dealings, (5) importance of contracts and (6) development of the economy and enterprise.
Focus	The focus in conventional finance is on the financial system itself, and its efficient and fair working. There is a lesser regard for the linkages it may have to the real economy.	Islamic finance is principally focused on the real economy and the actual production of goods and services. Under Islamic finance principles, the finance economy should serve the real economy.
Interest-based loan financing	Interest-based loan financing (i.e., provision of a fixed profit or return on the loan of money itself) is permitted. In this kind of financing, the lender may require repayment of the loan amount plus interest without regard to profit or loss in the business of the borrower.	Profit on financial investments is permitted if all requirements of applicable permissible Islamic contracts are met. But interest-based financing is not permitted.
Profit-and-loss sharing	Financial institutions may provide financing on a profit-and-loss sharing basis. But they may also loan money using interest-based loan financing which need not link to the profit or loss in the business of the borrower.	Financing should be made on a profit-and-loss sharing basis. The financing party's return should be linked to the profit or loss in the business of the borrower.
Use of funds	Usually, under conventional financing, the money being advanced may be used for many purposes other than illegal purposes.	Money from Islamic financing may not be used for illegal purposes or for non-Shariah compliant activities, including gambling and dealing in alcohol.

Islamic finance: Profit-and-loss sharing

The use of profit-and-loss sharing in Islamic finance, as opposed to interest-based loan financing in conventional finance, is a most important difference between the two.

Let us think about a simple example to understand the difference between interest-based financing and profit-and-loss sharing.

Let's first look at a business that takes an interest-based loan of Rs. 1,000 on which the loan amount of Rs. 1,000 plus interest of Rs. 200 is payable.

Business with Loan (Rs.)				
	Category	Ownership %	Case 1	Case 2
1.	Income		10,000	10,000
2.	Expenses		6,000	8,800
3.	Profit (Loss)		4,000	1,200
4.	Loan payments		1,200	1,200
5.	Profit (Loss) after loan payments		2,800	0
6.	Business owner share	100%	2,800	0
7.	Lender share	0%	0	0

- ▶ In this situation, the lender does not make an equity investment in the business or take a part from the profit-or-loss of the business.
- ▶ In Case 1, the business makes a profit (before loan payments) of Rs. 4,000. Rs. 1,200 goes to pay the lender. The business owner gets 100% of the profit share (Rs. 2,800).
- ▶ In Case 2, the business makes a profit (before loan payments) of Rs. 1,200. The entire Rs. 1,200 goes to pay the lender. The business owner gets 100% of the profit share (Rs. 0).
- ▶ If the business were to make a loss and not be able to pay the lender, it will still owe Rs. 1,200 to the lender. In fact, because interest payments will continue to apply, the amount of the business owner's obligation to the lender will keep growing until the lender is paid in full.

Now let's take a look at a business in which an investor makes an investment of Rs. 1,000 in exchange for 40% of the ownership of the business.

Business with Investment (Rs.)				
	Category	Ownership %	Case 1	Case 2
1.	Income		10,000	10,000
2.	Expenses		6,000	8,800
3.	Profit (Loss)		4,000	1,200
4.	Business owner share	60%	2,400	720
5.	Investor share	40%	1,600	480

- ▶ In this situation, the investor stands side-by-side with the business owner in terms of risk and reward.
- ▶ In Case 1, the business makes a profit of Rs. 4,000. The business owner gets 60% of the profits of the business (Rs. 2,400) and the investor gets 40% of the profits of the business (Rs. 1,600).
- ▶ In Case 2, the business makes a profit of Rs. 1,200. The business owner gets 60% of the profits of the business (Rs. 720) and the investor gets 40% of the profits of the business (Rs. 480).
- ▶ If the business were to make a loss, the business owner and the investor will be affected by the loss in proportion to their ownership interests.

The basic position of Islamic finance is that the first type of loan financing (interest-based) provides an unfair advantage to the people and institutions that have large amounts of money compared to individuals with personal needs or businesses with funding needs.

Islamic finance provides some flexibility on how risk and reward is divided between providers of money and business owners and operators, but it prohibits pure interest-based financing.

Supporters of conventional finance say that interest-based loan financing is efficient, and it allows business owners to keep 100% of the ownership interest in their business.

Types of Islamic finance

The following is a very brief description of some of the most commonly used types of Islamic finance.

Most Commonly Used Types of Islamic Finance

Name	Description
Mudarabah	<p>This is a type of partnership in which one person provides money and the other person provides expertise and management. At the beginning, the partners agree on the profit-share percentage. If there is a loss, the partner providing expertise and management does not have to pay the partner providing the money.</p> <p>For example, a software development firm decides to develop a new application. A group of investors put in the money. It is agreed that the software development firm will get 60% of the profits and the investors will get 40%.</p>
Musharakah	<p>This is a type of partnership in which people provide money and/or expertise and work. They can agree to divide the profits and management of the business, however they want. If there is a loss, the partners share in it according to the proportion of the money they put into the business.</p> <p>For example, three friends put in money to build houses for sale. Two of the friends also operate and manage the business.</p>
Murabaha	<p>This a type of financing in which the person providing financing buys a product that the other person needs. The person providing the financing then sells the product to the other person at cost plus mark-up. The other person pays over time.</p> <p>For example, a university student needs a motorcycle that costs Rs. 80,000. An Islamic bank buys the motorcycle for Rs. 80,000 and sells it to the student for Rs. 90,000. The student pays over time.</p>
Ijara	<p>This a type of financing in which the person providing financing ('lessor') buys a product needed for use by the other person ('lessee'). The lessor leases the underlying asset on 'periodical rent' which is based on all incurred costs, the lease period involved, the underlying risks and the desired profit. The lessee pays over time and must return the product at the end of the lease. The lessee may also buy the product at the end of the lease.</p> <p>For example, a business needs generators that costs Rs. 1,000,000. An Islamic leasing company buys the generators for Rs. 1,000,000 and leases it to the business for 3 years for total lease payments of Rs. 1,200,000.</p>
Takaful	<p>This is a type of insurance in which people or businesses seeking insurance put together or 'pool' their insurance payments or 'premiums' and make the pooled funds available for losses suffered by the people or businesses in the pool.</p> <p>For example, people want to protect their homes against fire or loss. They pool their premiums with a takaful management company. If their homes suffer a fire or loss, their losses are covered out of the pool.</p>

Islamic Finance: Knowing the difference



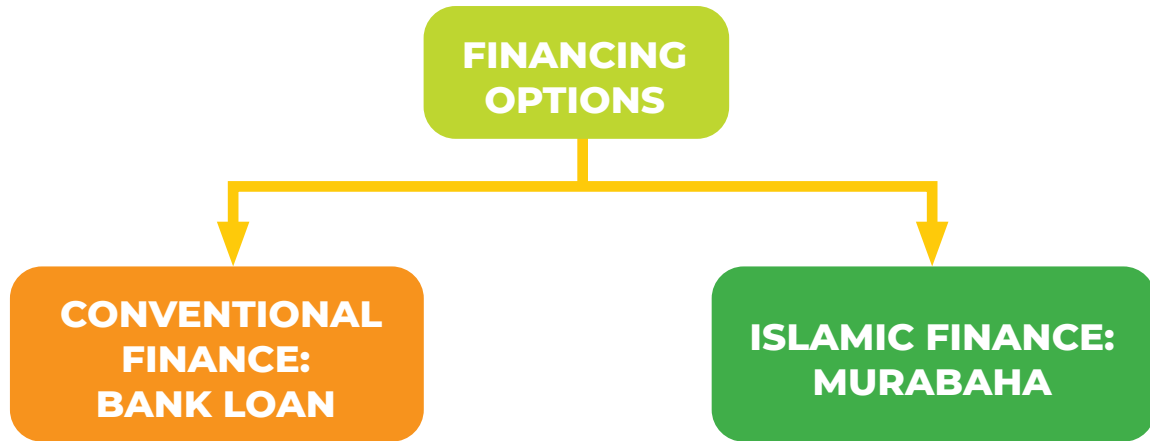
Test your knowledge of Islamic finance. Separate out the true and false statements below.

		True	False
1.	Islamic finance prohibits profit-and-loss sharing while conventional finance prohibits interest-based financing.	<input type="checkbox"/>	<input type="checkbox"/>
2.	Islamic finance has, as one of its main purposes, the creation of a just and ethical society.	<input type="checkbox"/>	<input type="checkbox"/>
3.	Islamic finance views finance as a means to serve the real economy.	<input type="checkbox"/>	<input type="checkbox"/>
4.	Both Islamic finance and conventional finance prohibit people from investing money for illegal purposes.	<input type="checkbox"/>	<input type="checkbox"/>
5.	If you want to buy equipment to use for a limited period and you want to use Islamic financing, you should use ijara financing.	<input type="checkbox"/>	<input type="checkbox"/>
6.	Islamic finance is not flexible towards how investors and business owners share profits.	<input type="checkbox"/>	<input type="checkbox"/>

The solution to this exercise can be found on page 195

Conventional and Islamic financing options

Because PomPak needs financing for equipment, Safdar and Shereen explore two financing options.



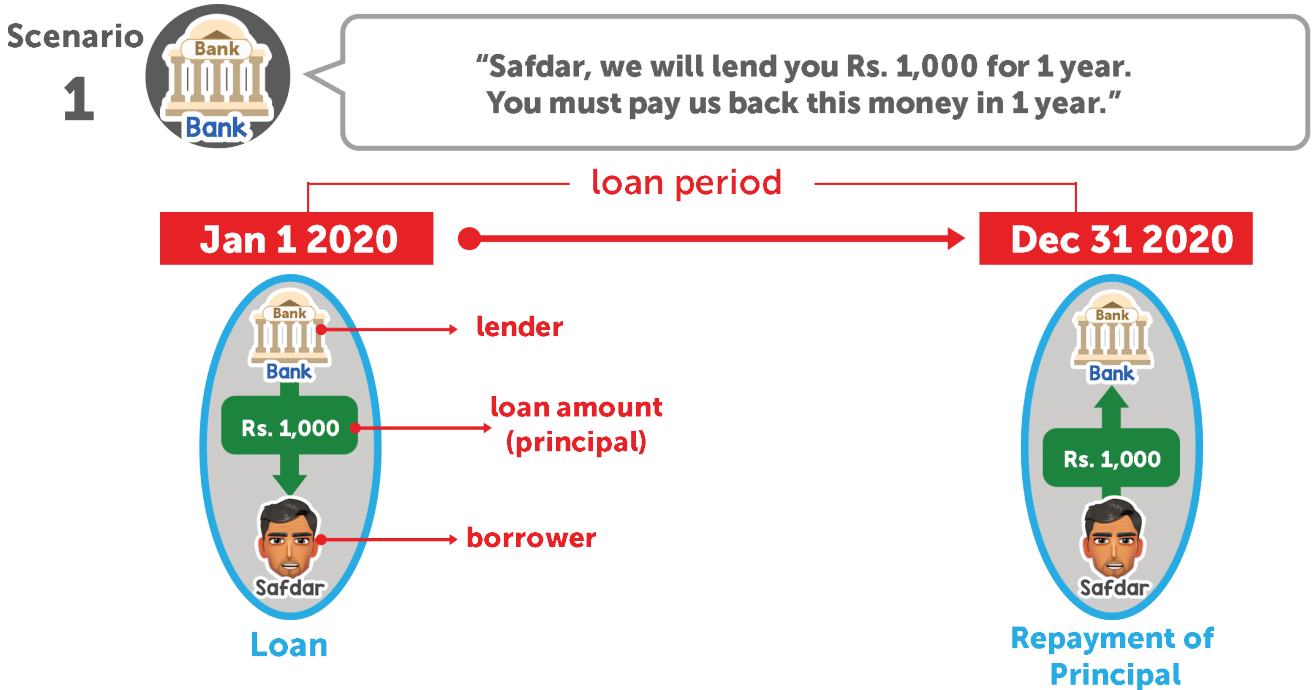
Under conventional finance, PomPak’s equipment financing needs may be met through a bank loan. In this case, the bank will loan Rs. 4,000,000 to the business. In return, the business will repay the bank Rs. 4,000,000 in installments plus pay a mark-up which will provide profit to the bank.

Under Islamic finance, PomPak’s equipment financing needs may be met through a murabaha financing. In this case, the finance company will buy the equipment for Rs. 4,000,000. It will then sell the equipment to the business for Rs. 4,000,000 plus a profit margin. In return, the business will repay the finance company the total sales price in installments, which will return the equipment expense and provide a profit to the finance company.

NOTE: Both under conventional finance and Islamic finance, there are other financing options as well, such as lease or ijara financing. Safdar and Shereen decide to explore loan and murabaha financing, which are the two major forms of financing under conventional finance and Islamic finance respectively.

Borrowing: Basic concepts

Borrowing involves a loan of money by a lender to a borrower for a specified period. The borrower must return that money in the specified period.

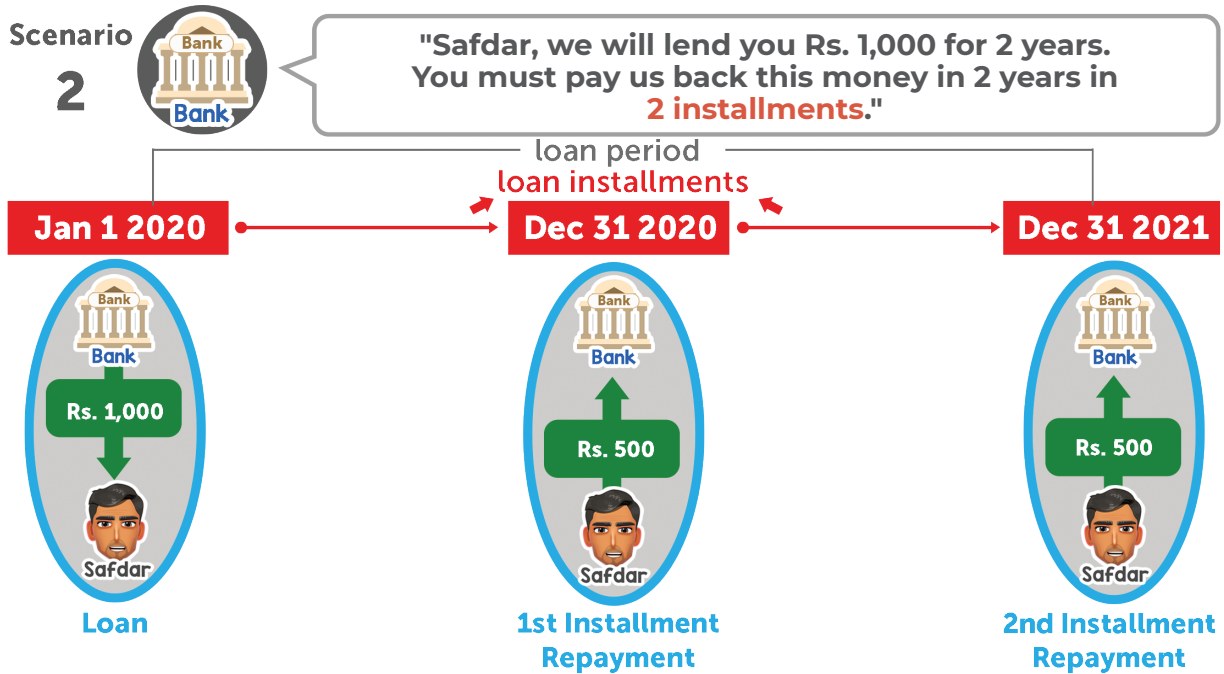


Important Terms

Lender	The person who lends the money and must be repaid.
Borrower	The person who borrows the money and must repay it.
Loan	The act of giving money by a lender to a borrower that must be repaid in a specified time.
Loan amount (principal)	The amount of money lent.
Loan period	The period at the end of which the borrower must repay the loan.
Loan repayment	The paying back by the borrower of the loan amount (or principal).

Borrowing: Repayment in installments

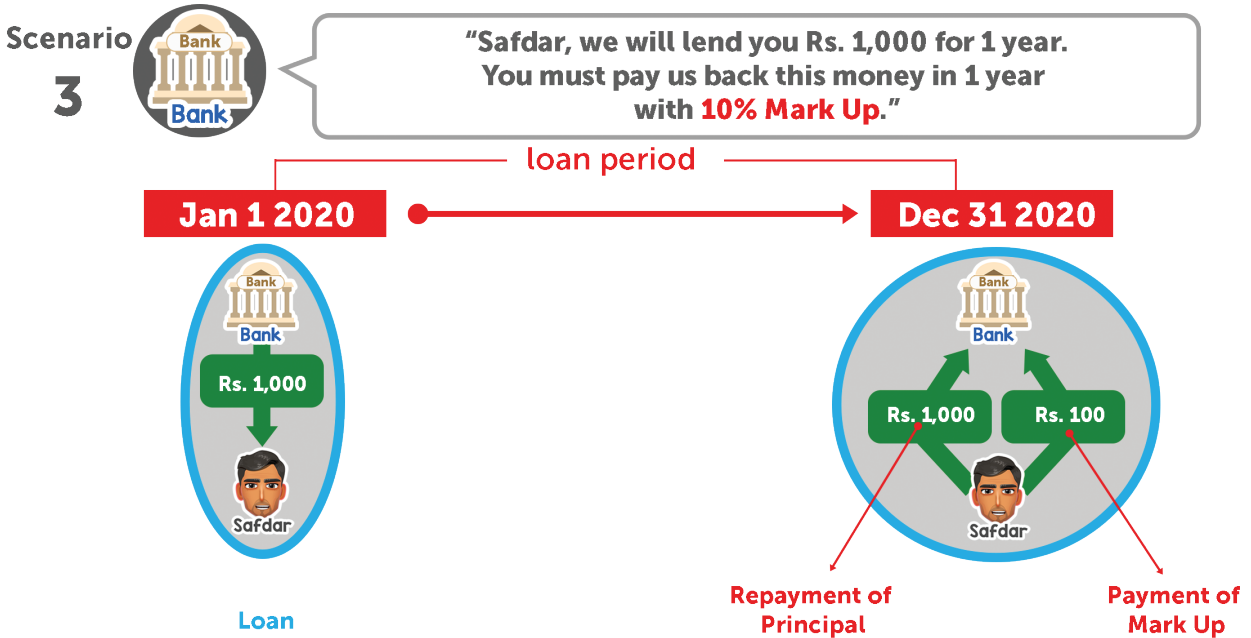
Depending on the agreement between the lender and the borrower, the loan amount must be repaid either at one time or in smaller amounts over a specified times (installments).



1. Sometimes a lender will want the entire loan amount (principal) repaid altogether at the end of the loan period.
2. Other times, a lender may agree that the loan amount (principal) is paid in small amounts over specified times (installments).
3. When the loan amount (principal) is required to be paid in installments, the sum of the amounts paid in installments is equal to the entire loan amount (principal).

Borrowing: Payment of mark-up

In most business loans, the lender will want the borrower to repay the loan amount (principal) PLUS a 'mark-up' on the loan amount.



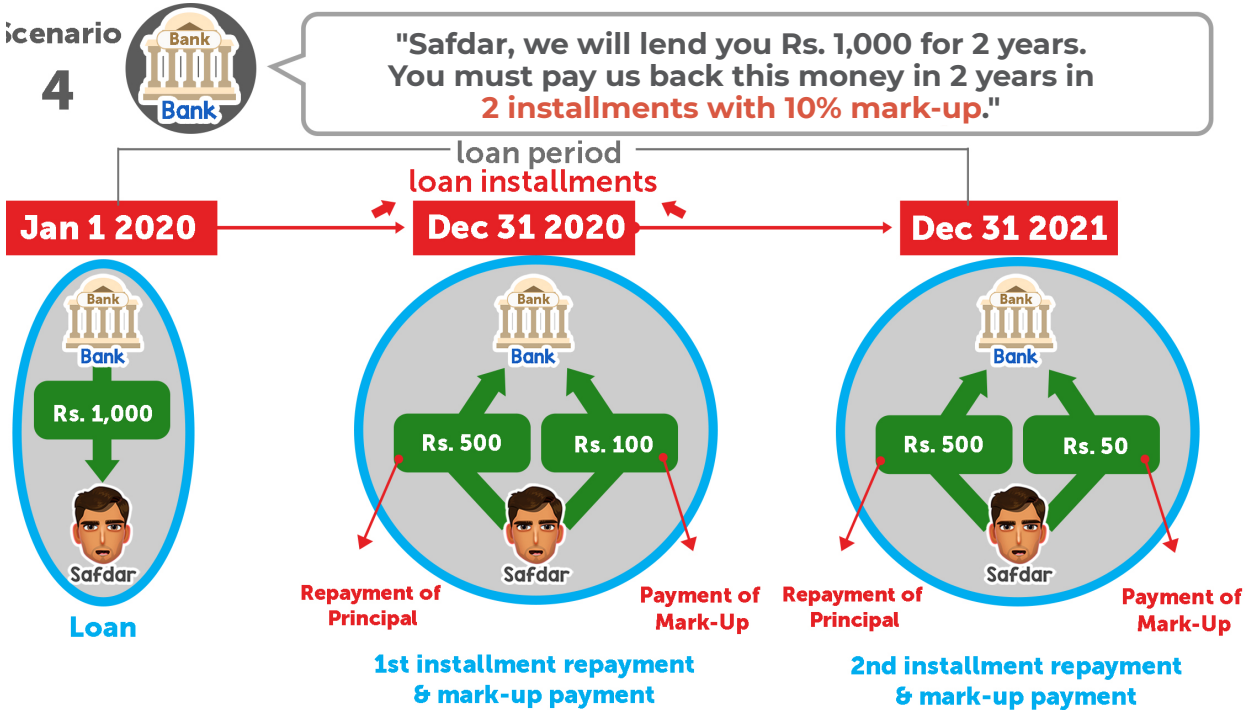
The mark-up or interest on the loan amount is expressed as a percentage of the loan amount, payable over a period.

For example, if a lender gives Rs. 1,000 for one year with a mark-up of 10% per annum, the borrower will, after one year, need to;

1. Repay the loan amount of Rs. 1000 PLUS
2. Pay 10% mark-up of the loan amount (principal) (i.e., Rs. 100).

Borrowing: Installments and mark-up

In most business loans, the lender will want the borrower to repay the loan amount (principal) PLUS a 'mark-up' on the loan amount.



Typically, in such loans if the loan is to be paid in two installments:

1. In the first installment, the borrower will (1) repay the portion of the loan amount to be paid in this installment and (2) all mark-up that is payable to the date of payment.
2. In the second installment, the borrower will (1) repay the portion of the loan amount to be paid in this installment and (2) all mark-up that is payable to the date of payment.

In our example:

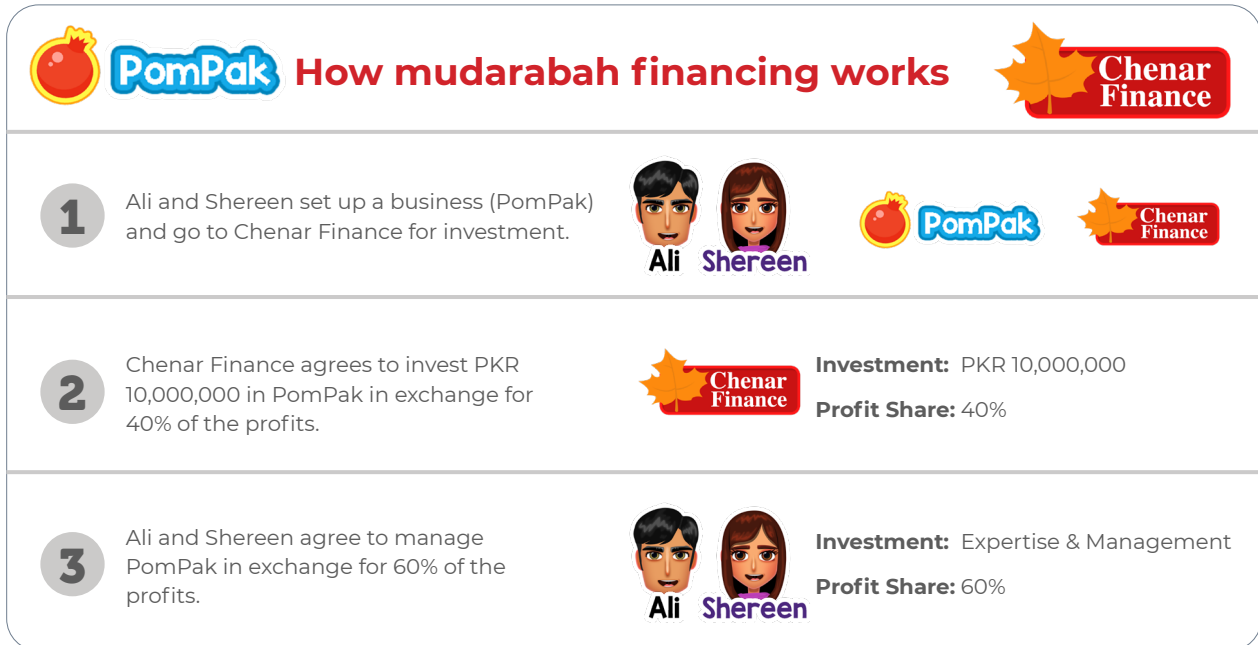
Loan Payable in 2 Installments with Mark-Up (Rs.)				
1.	Date of loan	January 1, 2020		
2.	Loan amount	1,000		
3.	Loan period	2 years		
4.	Mark-up per annum	10%		
	Installment date	December 31, 2020	December 31, 2021	Total
5.	Principal repayment	500	500	1,000
6.	Mark-up payment	100	50	150
7.	Total	600	550	1,150

This mark-up is on one year (1):
Rs. 1000 x 10% x 1 = 100.

This mark-up is on one year (1):
Rs. 500 x 10% x 1 = 50.


How Mudarabah works

Mudarabah is a form of Islamic finance partnership in which one person provides money and the other person provides expertise and management. At the beginning of the partnership, the partners agree on the profit-share percentage.





How Musharakah works

Musharakah is a form of Islamic finance partnership in which people provide money and/or expertise and work. At the beginning of the partnership, the partners agree on the profit-share percentage.







How musharakah financing works

1

Ali and Shereen set up a business (PomPak). They invest, and also ask Safdar for investment.


2

The three agree to invest as follows:

Safdar invests PKR 8,000,000 in PomPak in exchange for 40% of the profits.


Ali invests PKR 1,000,000 in PomPak plus agrees to manage the business in exchange for 30% of the profits.

Shereen invests PKR 1,000,000 in PomPak plus agrees to manage the business in exchange for 30% of the profits.




Investment: PKR 8,000,000

Profit Share: 40%



Investment: PKR 1,000,000 + Expertise & Management

Profit Share: 30%

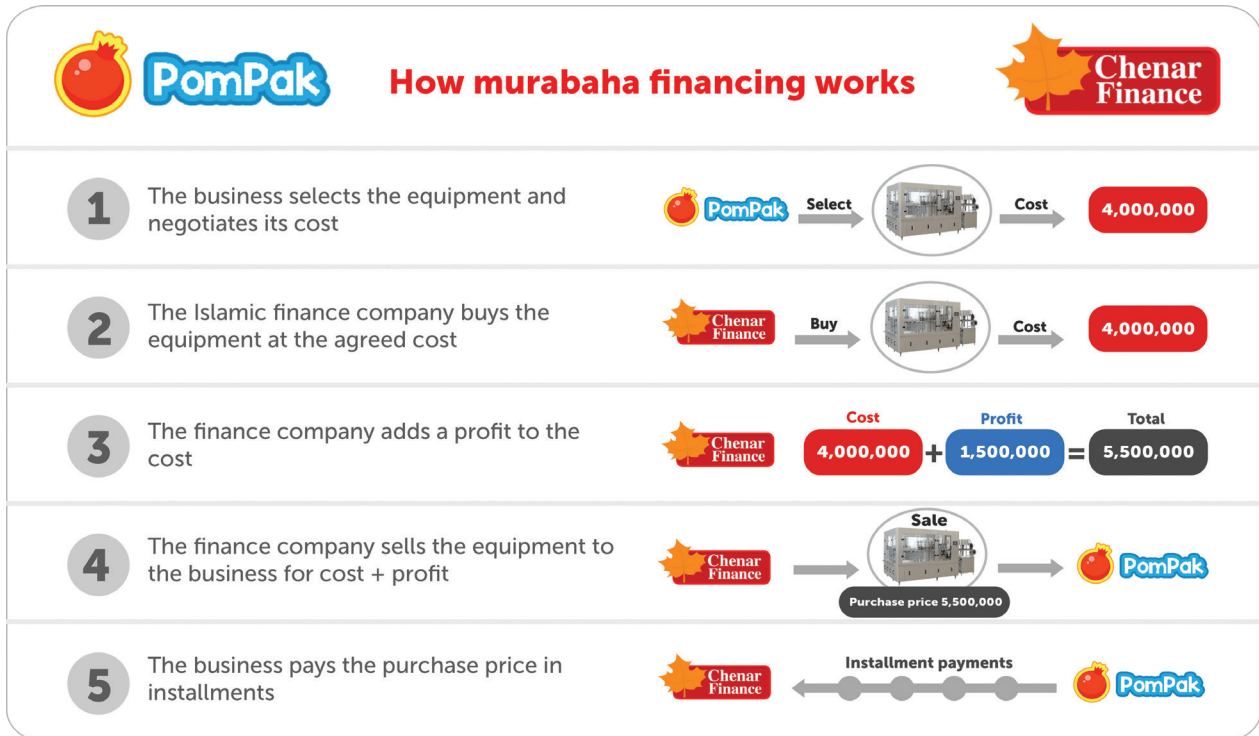


Investment: PKR 1,000,000 + Expertise & Management

Profit Share: 30%

How Murabaha works

Murabaha is a form of Islamic finance in which the finance company buys an asset and then sells it for a profit to the business that needs that asset. The business pays the purchase price in installments.



Completed projections

After much research, Safdar and Shereen settled on an equipment financing plan under which the business will borrow Rs. 4,000,000 and make a total of Rs. 5,500,000 in payments in four annual installments.

Rs. 4,000,000 Equipment Financing Plan

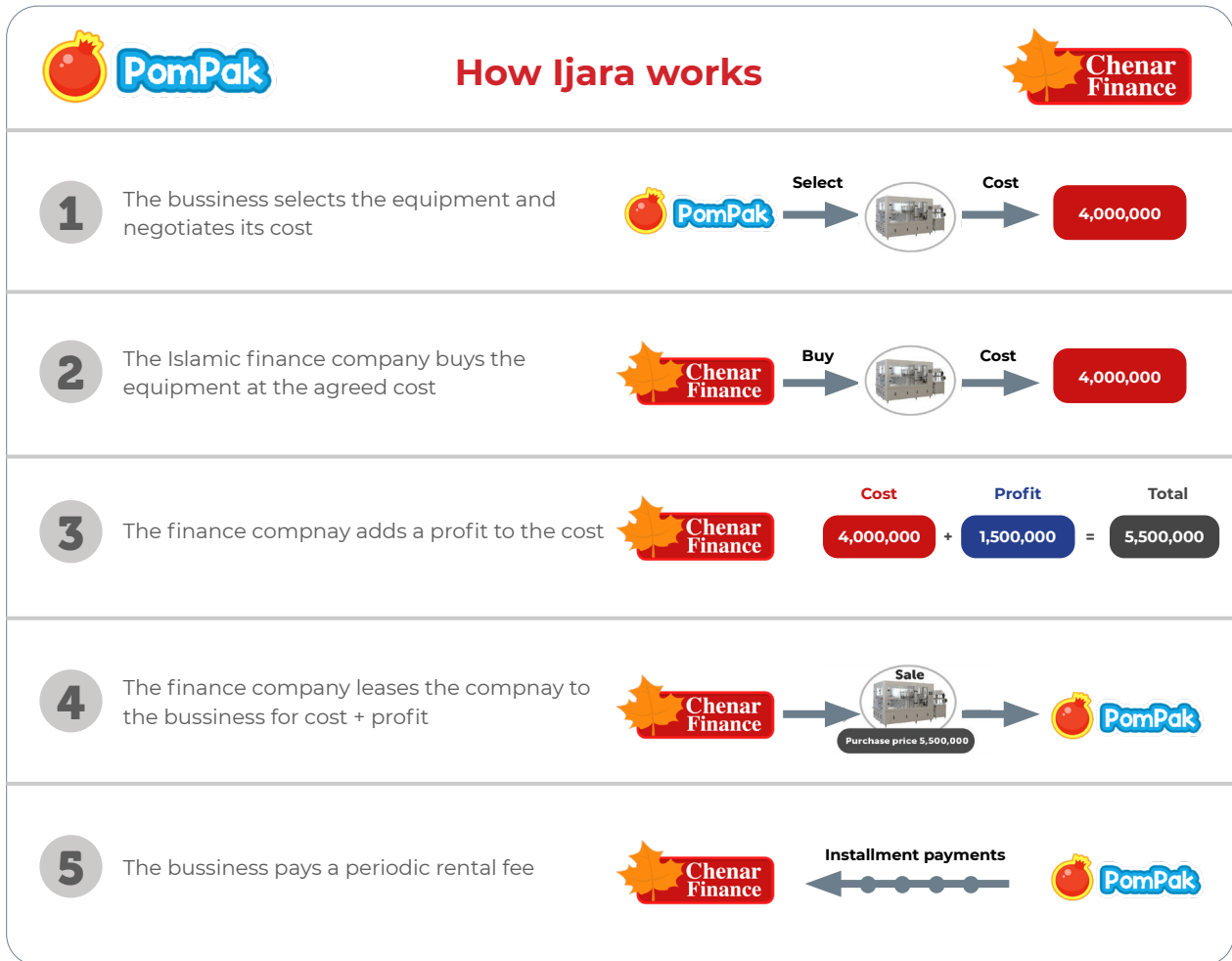
Payment	Year 1	Year 2	Year 3	Year 4	Total
Total	1,600,000	1,450,000	1,300,000	1,150,000	5,500,000

They now complete their projections. The equipment financing brings down profit margins but the business looks very promising.

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total fruit (kg)	27,500	28,875	30,320	32,000	34,000
2.	Fruit price per kg	250	260	270	300	330
3.	Total fruit income	6,875,000	7,507,500	8,186,400	9,600,000	11,220,000
4.	Total fruit for juice (kg)	40,000	48,000	57,600	69,120	82,944
5.	Juice price per kg	400	420	440	450	460
6.	Total juice income	16,000,000	20,160,000	25,344,000	31,104,000	38,154,240
7.	Total income	22,875,000	27,667,500	33,530,400	40,704,000	49,374,240
Expenses						
8.	Total fruit (kg)	70,875	80,719	92,316	106,176	122,791
9.	Fruit expense per kg	190	195	200	210	220
10.	Total fruit expense	13,466,250	15,740,156	18,463,200	22,296,960	27,014,064
11.	Salary	800,000	960,000	1,152,000	1,382,400	1,658,880
12.	Marketing	800,000	960,000	1,152,000	1,382,400	1,658,880
13.	Rent	240,000	264,000	326,400	550,000	750,000
14.	Juice bottles & packaging	1,920,000	2,419,200	3,041,280	3,732,480	4,578,509
15.	Transport	800,000	1,008,000	1,267,200	1,555,200	1,907,712
16.	Electricity, gas & other expenses	1,600,000	2,016,000	2,534,400	3,110,400	3,815,424
17.	Equipment financing	1,600,000	1,450,000	1,300,000	1,150,000	-
18.	Total expenses	21,226,250	24,817,356	29,236,480	35,159,840	41,383,469
Profit (Loss)						
19.	Before tax profit	1,648,750	2,850,144	4,293,920	5,544,160	7,990,771
20.	Income taxes (assumed at 29%)	478,138	826,542	1,245,237	1,607,806	2,317,324
21.	After tax profit	1,170,613	2,023,602	3,048,683	3,936,354	5,673,448
22.	Profit margin	5.12%	7.31%	9.09%	9.67%	11.49%

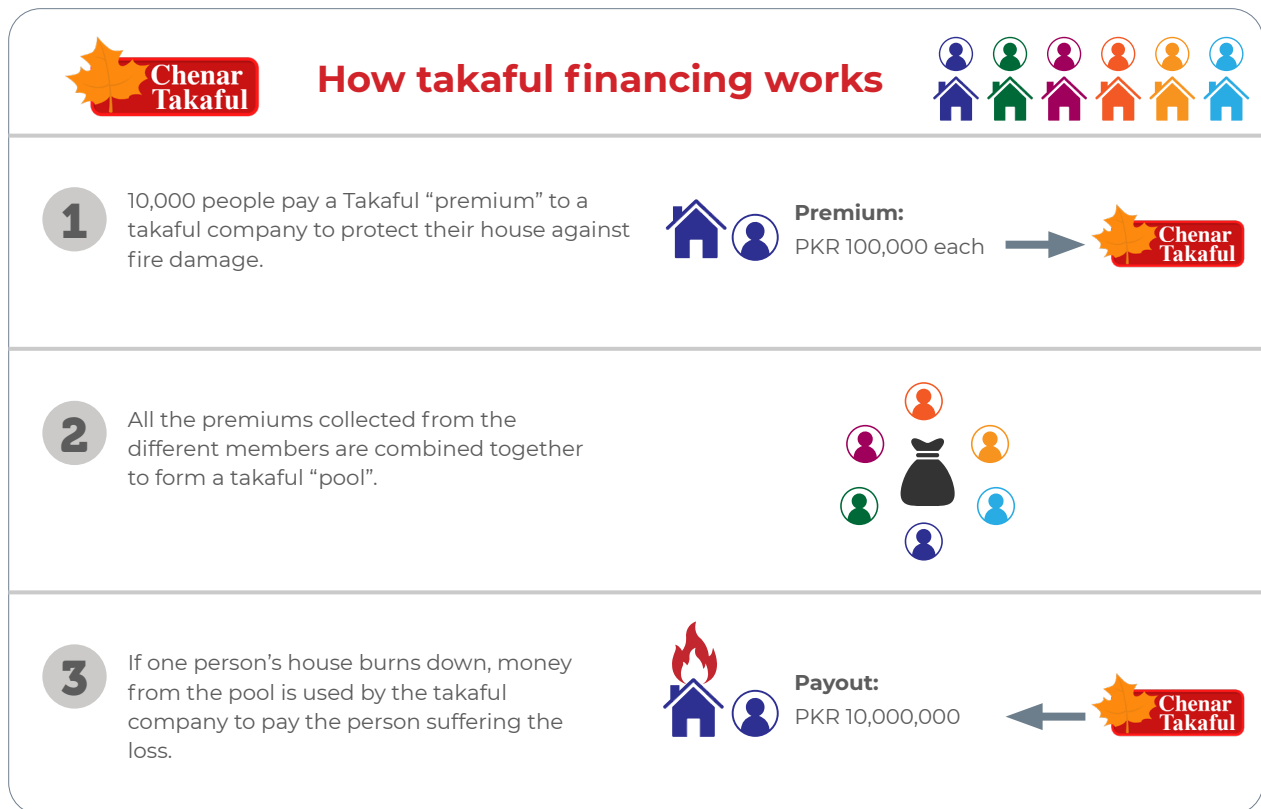
How Ijara works

Ijara is a form of Islamic equipment financing in which the person providing financing buys the equipment and leases it to the other person for a rental fee.



How Takaful works

Takaful is an Islamic alternative to insurance in which people pool their insurance premiums to insure something. The person suffering the loss is made whole.



What is the type of Islamic finance?



Identify the type of Islamic finance that applies to each of these 5 situations.

1.	Safdar invests money in a business but is not involved in the business. Ali agrees to manage the business but does not invest money. They agree to a profit share.	Mudarabah	Musharakah
2.	Safdar, Ali and Shereen all invest money in a business. They also all agree to manage the business. They agree to a profit share.	Mudarabah	Musharakah
3.	PomPak buys equipment from Chenar Finance, and pays the money in installments.	Ijara	Murabaha
4.	PomPak leases equipment from Chenar Finance, and pays a periodic rental fee.	Ijara	Murabaha
5.	100,000 people pool PKR 100,000 each to insure their lives. On the death of one person, that person's family receives PKR 300,000.	Takaful	Mudarabah

The solution to this exercise can be found on page 197

Completed projections

After much research, Safdar and Shereen settled on an equipment financing plan under which the business will borrow Rs. 4,000,000 and make a total of Rs. 5,500,000 in payments in four annual installments.

Rs. 4,000,000 Equipment Financing Plan

Payment	Year 1	Year 2	Year 3	Year 4	Total
Total	1,600,000	1,450,000	1,300,000	1,150,000	5,500,000

They now complete their projections. The equipment financing brings down profit margins but the business looks very promising.

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total fruit (kg)	27,500	28,875	30,320	32,000	34,000
2.	Fruit price per kg	250	260	270	300	330
3.	Total fruit income	6,875,000	7,507,500	8,186,400	9,600,000	11,220,000
4.	Total fruit for juice (kg)	40,000	48,000	57,600	69,120	82,944
5.	Juice price per kg	400	420	440	450	460
6.	Total juice income	16,000,000	20,160,000	25,344,000	31,104,000	38,154,240
7.	Total income	22,875,000	27,667,500	33,530,400	40,704,000	49,374,240
Expenses						
8.	Total fruit (kg)	70,875	80,719	92,316	106,176	122,791
9.	Fruit expense per kg	190	195	200	210	220
10.	Total fruit expense	13,466,250	15,740,156	18,463,200	22,296,960	27,014,064
11.	Salary	800,000	960,000	1,152,000	1,382,400	1,658,880
12.	Marketing	800,000	960,000	1,152,000	1,382,400	1,658,880
13.	Rent	240,000	264,000	326,400	550,000	750,000
14.	Juice bottles & packaging	1,920,000	2,419,200	3,041,280	3,732,480	4,578,509
15.	Transport	800,000	1,008,000	1,267,200	1,555,200	1,907,712
16.	Electricity, gas & other expenses	1,600,000	2,016,000	2,534,400	3,110,400	3,815,424
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18.	Total expenses	21,226,250	24,817,356	29,236,480	35,159,840	41,383,469
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22.	Profit margin	5.12%	7.31%	9.09%	9.67%	11.49%

What is the main reason the profit margin makes a big increase in Year 5? Is this increase likely to continue if other business factors remain the same?

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The solution to this exercise can be found on page 198

Ali's big idea

With financing in place, PomPak has been doing well. Juice bottling and sales are going well and PomPak is getting more popular across the city.



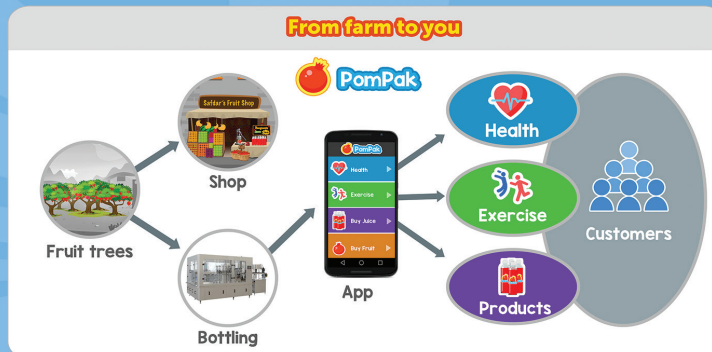
Ali has been doing well in his programming job. But he has also been thinking about PomPak. One day, when the family is visiting the farm, he presents his big idea.

You know the PomPak brand is a promise of healthy, pure and fresh!



Yes, and its working. Many of our customers are people who value health and exercise a lot. And these days people are very worried about where food is coming from and if it is pure and fresh.

So here is my idea. I call it "from farm to you."



We will create an app that will inform and connect people on topics like health and exercise. And they can buy fruit and juice that is healthy, pure and fresh! With fruit coming from the farm to you!!



I really like it! We will create a community. Our brand will become very strong.

I like it too! I will expand the fruit orchard at our farm and also get other small farmers to grow more fruit!



I love it!! We will be promoting health and exercise, we will help small farmers, and we will strengthen our brand.

POMPAK AND THE INFORMATION AGE

Introduction

In this section, we will consider e-commerce in the information age.



Safdar and Shereen have obtained equipment financing, bought the equipment and launched the PomPak brand. The bottled juice is very popular and customers especially like the PomPak brand promise: healthy, pure and fresh.

Ali, who has been working as a programmer, proposes that he join the business and help launch an **app** for PomPak. The entire family is very excited about taking their business into the **information age**!

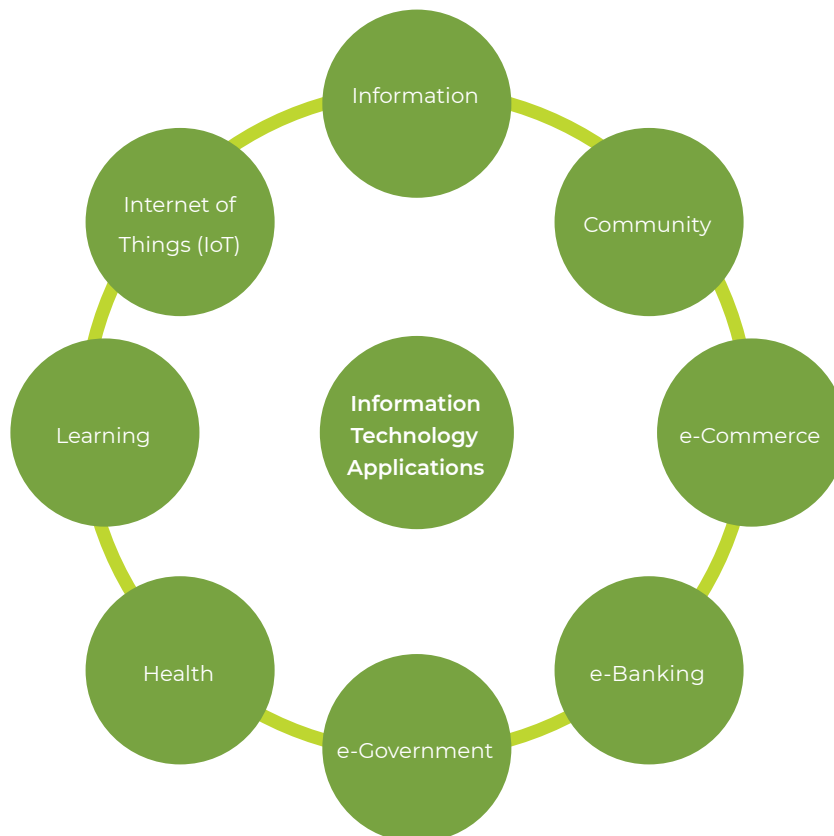
Information technology in the information age

We are now well into the information age. People and businesses that can use information to their advantage do very well in the rapidly changing world in which we live.

A core aspect of the information age is that it is built on **information technology**. In today's world, this means that all content may be converted into **digital content**. Books, photos, videos, audio recordings, bank statements, company information, personal messages and mail etc, may be converted into digital content and transmitted across the world in an instant.

The hardware, software and digital content of the Information Technology revolution is now allowing more and more activities to take place through mobile and computing devices.

Information Technology Applications



Among other applications, information technology is transforming all aspects of human existence:

Selected Information Technology Applications	
Information	Information can easily be posted online. Powerful search engines make that information easily and instantly available.
Community	People can quickly create and grow communities around the world. These communities may be of friends, colleagues or people with similar interests.
e-Commerce	Shopping, ordering, buying and selling is quickly moving online. Because physical stores are not needed, customers around the world may be served at a low expense.
e-Banking	Banking services – including e-payments for transfer of money – are now available online, making it easy for people to manage bank accounts, transfer money and even borrow money.
e-Government	More and more government services are becoming available online. This reduces the time and expense of dealing with the government.
Health	Online health information and assistance is a new wave. Over the next 5 years, more and more health related support will be available online.
Learning	The way we learn is changing through adaptive learning – unique learning pathways for each individual – and vast amounts of digital learning content in the form of learning videos, games and assessments.
Internet of Things	Information Technology is rapidly spreading into physical objects, which allows for these objects to be remotely monitored and controlled.

Ali's big new idea explained

After the family get-together, Ali comes over to meet Safdar and Shereen and explain his idea in more detail.



Most of the customers for PomPak juice buy it because it tastes delicious but also because it is healthy, pure and fresh. Most of these customers have smart phones with digital connections.

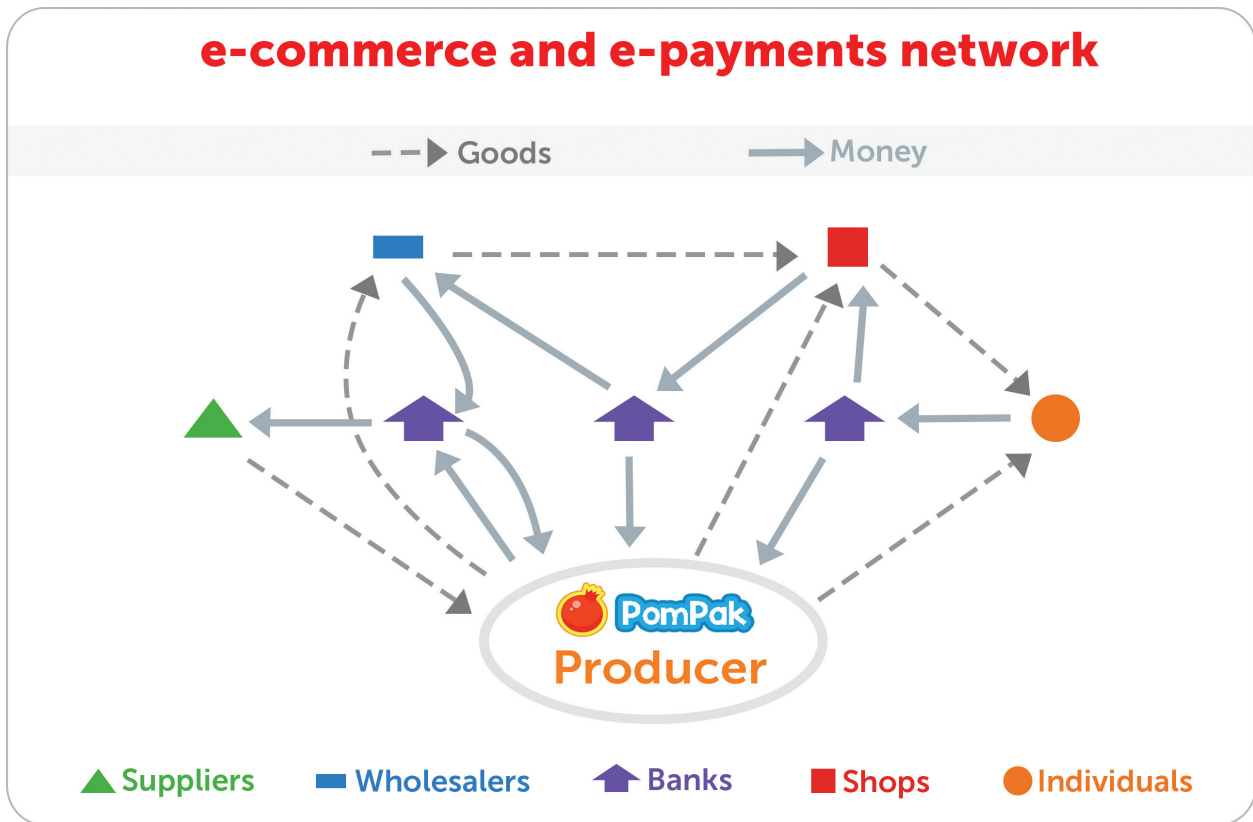
Ali proposes to build an app that will allow customers to buy bottled juice through their phones, tablets and laptops. In this way, a new channel will be opened up for PomPak, and its customers will be able to buy juice more cheaply and conveniently.

But Ali also proposes he will do more. PomPak will provide information on the entire chain by which a pomegranate is grown, harvested, processed, bottled and transported. PomPak will live up to its slogan—"from farm to you"—by providing information on the entire chain.

PomPak will also build a community of people interested in health and exercise. It will provide information on health and exercise and encourage others to do the same. This service will not make any money for PomPak but it will strengthen PomPak's brand promise: healthy, pure and fresh.

PomPak's e-commerce and e-payments network

Next, Ali sketches out the e-commerce and e-payments network that will be put in place.



PomPak will be able to place orders online with its suppliers.

Wholesalers, shops and individual customers will be able to directly order online from PomPak.

PomPak will also set up e-payment facilities with banks and other financial institutions.

In this way, the entire ordering and payment system will be online at very low cost.

PomPak will be able to deal with suppliers and customers globally, cheaply and instantly!

FINANCIAL INSTRUMENTS

Types of Financial Instruments

THE NEED FOR FINANCING: INDIVIDUALS

People need financing for many reasons. Individuals almost always get debt financing. There are different kinds of financing for different kinds of personal needs.

THE NEED FOR FINANCING: BUSINESS

Every business also needs financing because a business spends money before it makes money.



Types of Businesses

This is true if the business is run by an individual or company or any other type of



Individual
(informal)



Partnership
(formal/informal)



Company



Trust



Foundation

business entity

We will discuss below financial instruments for companies, but the basic principles we discuss apply to different types of formal businesses.

Financial Instruments

Internal and External Financing

The financing a business needs can come from internal sources (in other words, from the business itself) or from external sources (such as a lender or investor).

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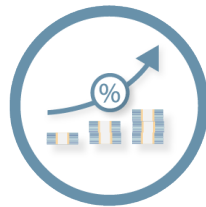


TYPES OF FINANCIAL INSTRUMENTS

Financial instruments may be broadly categorized as debt, equity and other.



Debt



Equity



Other

Debt Financing

Imagine it is January 1 and your business plans to buy three apples for PKR 600 but it doesn't have the money.



Finance needed: Rs 600

It borrows the money from a lender. It agrees that it will pay the money back to the lender on January 31 with 20 rupees extra as markup.

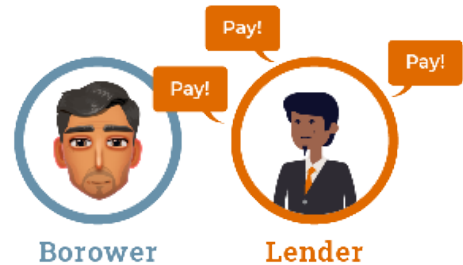
Debt		
Instrument	Amount (Rs)	Amount
Loan	600	Jan-01
Repayment	620	Jan-31

The apples are not sold, and they rot. Because the money has been taken as a loan, PKR 620 must still be paid to the lender on January 31.



Finance needed: Rs 600

Debt		
Instrument	Amount (Rs)	Amount
Loan	600	Jan-01
Repayment	620	Jan-31



This is an example of debt financing.

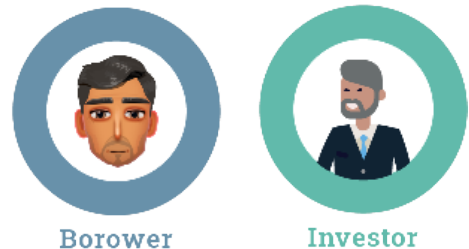
Equity Financing

Now imagine that instead of borrowing money your business obtains PKR 600 as an investment from an investor.

Your business gives a 10% ownership share of the business to the investor.



Debt		
Instrument	Amount (Rs)	Amount
Investment	600	Jan-01
Share	10% Ownership	No time period

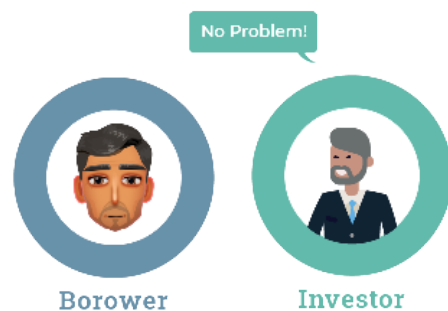


It uses the money to buy 3 apples. This time too, the apples rot.

This time, your business does not have to give any money back to the investor.



Debt		
Instrument	Amount (Rs)	Amount
Investment	600	Jan-01
Share	10% Ownership	No time period



This is an example of equity financing.

After one year, your business makes PKR 10,000 in profits.

Annual Profit (Rs.) = 10,000

The lender's rights are limited to getting back his loan plus mark up.



**Lender's Share
0%**



**Investor's Share
10%**

But the investor owns 10% of your business. He has a share in the profits of the business.

Differences between Debt and Equity

For the person providing the money, debt is lower risk, while equity is higher risk.

But debt has limited reward. Equity has unlimited reward.

Debt returns are limited to the amount of the loan plus markup. Equity returns are measured by the value of the business.

Debt must be repaid in a specified time. Equity is part of the long term capital of the business

Difference between Debt and Equity		
Features	Debt	Equity
Loan	Lower risk	Higher risk
Repayment	Lower reward	Higher reward
Loan	Fixed: Amount of loan plus agreed markup	Not Fixed: Value of % share in business
Repayment	Payment due on specified date	Long term, no fixed time period

Types of Debt Financial Instruments

There are many types of debt financial instruments.

Leases and installment sales are technically not loans, but they have similar fixed income characteristics.



Loans



Bonds
(Treasury Bills)



Credit Cards



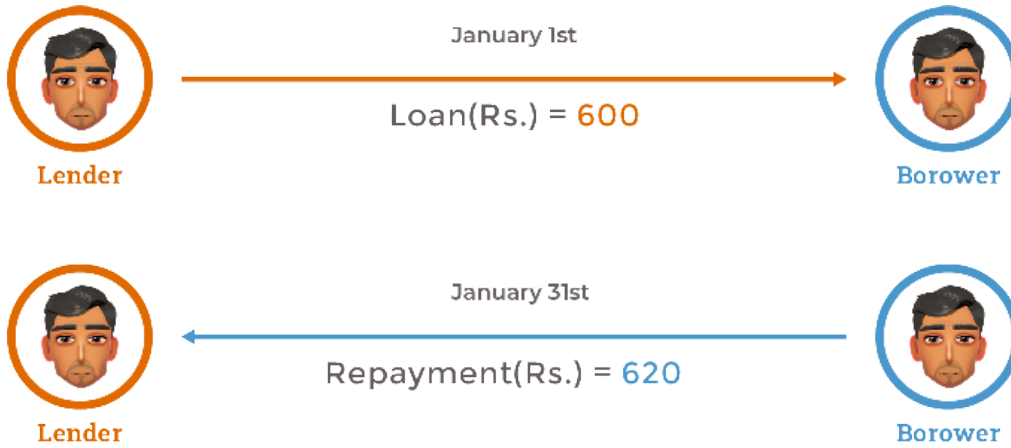
Leases



Installment Sales

LOANS

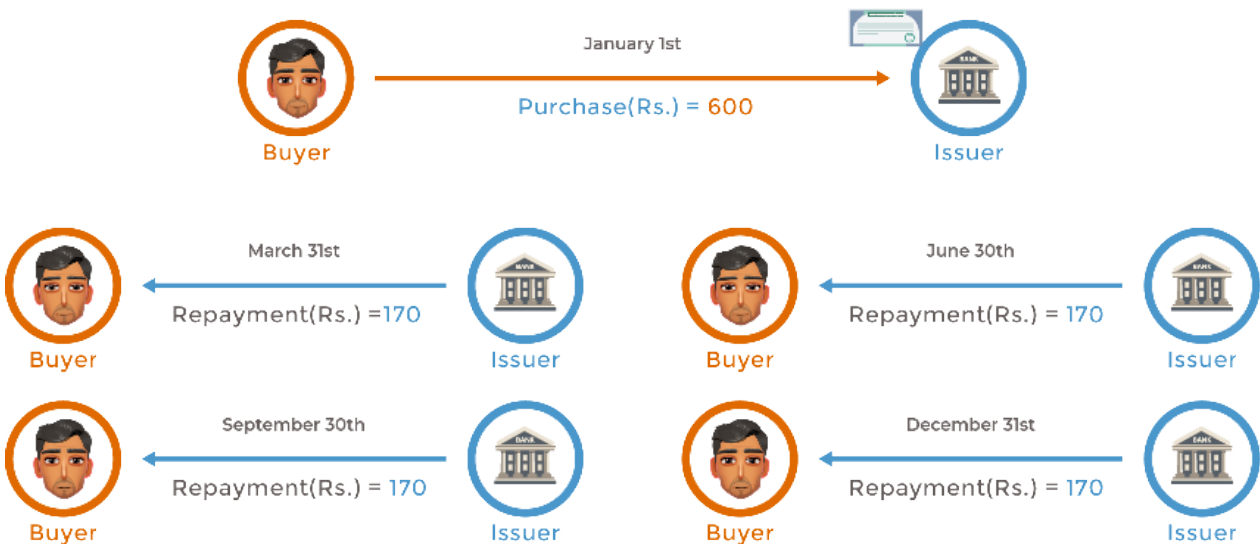
In a loan, the lender makes a loan for a period and expects repayment with an agreed markup.



BONDS AND BILLS

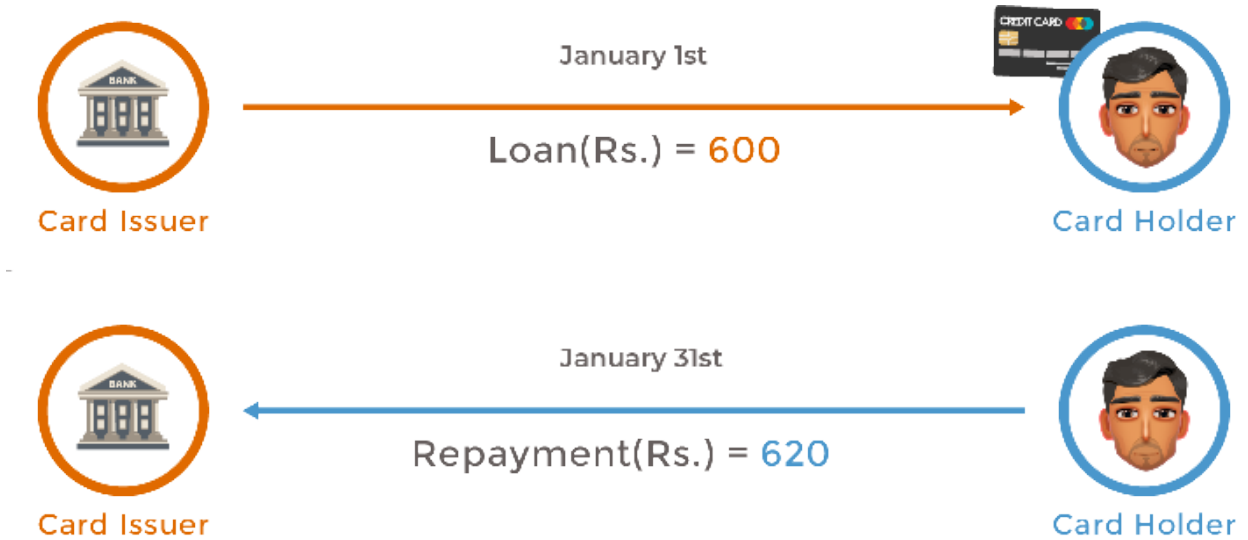
A bond is just like a loan except usually bonds are often listed on a financial exchange and are easier to sell.

A treasury bill is a bond issued by the government. It is sold to a buyer at a price lower than the face amount. The buyer makes a profit because the government pays the full, face amount of the treasury bill.



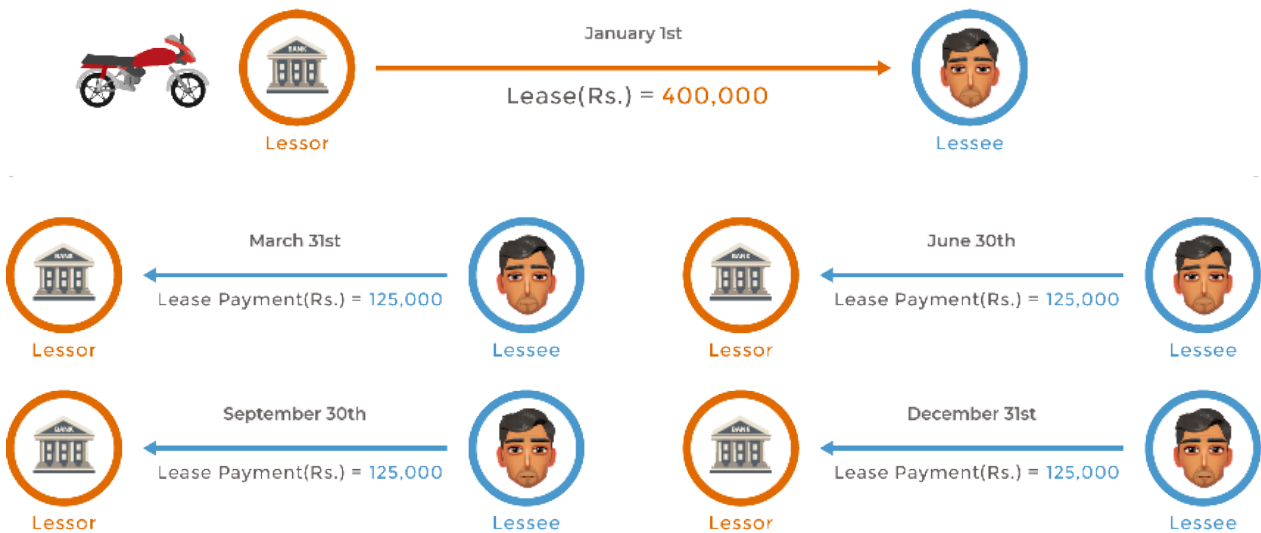
CREDIT CARDS

In a credit card, the card holder takes a loan each time he uses the card and must pay back the money plus a markup next month.



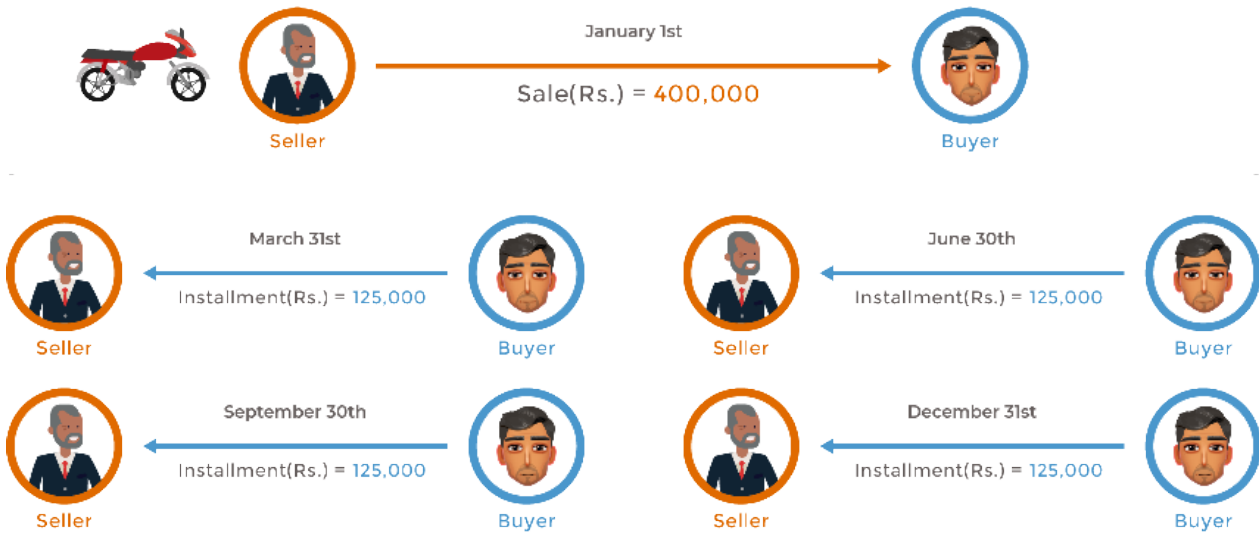
LEASES

In a lease, the financing party buys the asset and leases it to the user. The user makes lease payments which cover the financing party's cost plus a markup.



INSTALLMENT SALES

In an installment sale, the financing party buys the asset and sells it to the user. The user makes installment payments which cover the financing party's cost plus a markup.



Types of Equity Financial Instruments

Equity financial instruments include common shares and preferred shares.

There are also many kinds of funds.



Common Shares



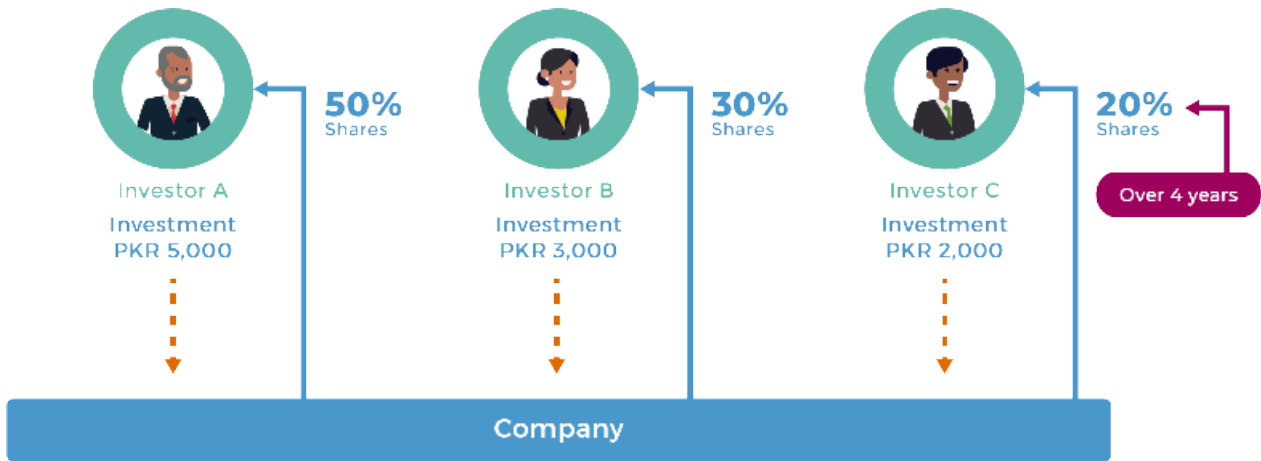
Preferred Shares



Funds

COMMON SHARES

In the case of common shares, investors invest money into a company or venture and receive shares. These represent a percentage ownership interest in the company or venture.



Types of Investors

The investors in a business don't always have to invest money.

For example, some can invest money, others can invest ideas, others can invest time and effort.

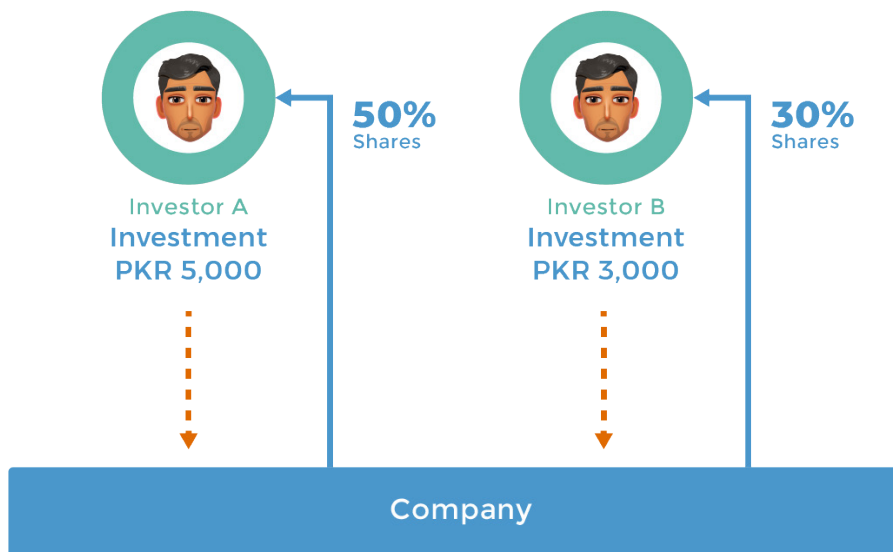
All can have a percentage ownership interest in the company or venture.

When employees get shares for their work, the shares are often given out over several years. That way, if the employee leaves or does not perform, some shares are not issued.

PREFERRED SHARES

In the case of preferred shares, if the company closes down, the preferred shareholders will first get paid their investment and a return before common shareholders are paid.

Preferred shareholders may also have rights to special payments from the company's profits

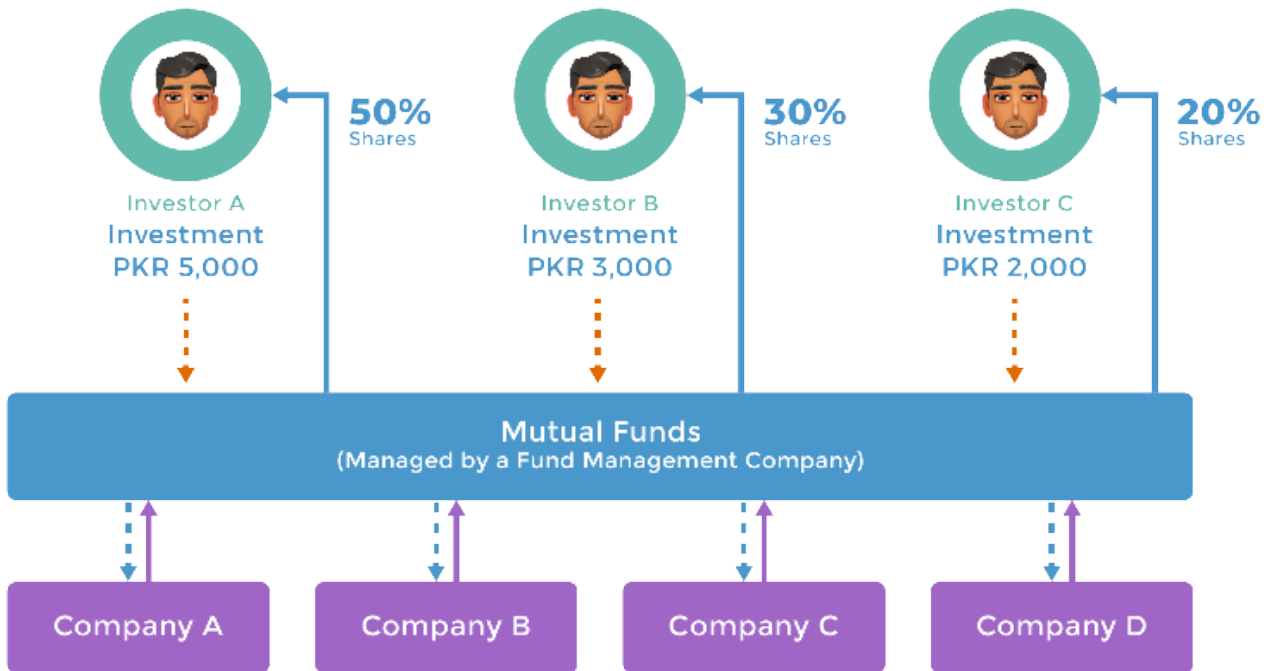


FUNDS

There are also many types of funds. Some funds invest in equity, others in debt, and others in many kinds of financial instruments.

In the case of a mutual fund, investors invest their money in a fund. The fund is managed by a fund management company. It invests the money in the fund in the shares of many companies.

In this way, investors can obtain the services of an expert fund management company and can invest in many companies through one investment.



Other Types of Financial Instruments

There are also many more complicated types of financial instruments.

These may have common features of both debt and equity.

They may be used to manage risks or increase returns.



Forwards



Derivatives



Swaps



Cryptocurrency



Insurance related
Instruments

Key Questions

<p>What is the purpose of the financing?</p>	<p>If you need long-term financing that is higher risk, equity financing is better.</p> <p>If you can confidently repay money in a specified time with a specified markup, debt financing is better.</p>
<p>Is the financial instrument suitable?</p>	<p>After choosing whether you need debt or equity financing, you need to choose what type of financial instrument you prefer.</p> <p>Debt (and fixed income) financial instruments include loans, bonds, credit cards, mortgages, leases, and installment sales.</p> <p>Equity financial instruments include preferred shares and common shares.</p>
<p>What are its risks?</p>	<p>From the point of view of the person who gets financing, debt financing is riskier than equity financing.</p> <p>In the case of debt financing, the borrower must repay the money with a markup in a specified time period.</p>
<p>What are its rewards?</p>	<p>From the point of view of the person who gets financing, equity financing means sharing more rewards than debt financing.</p> <p>In the case of equity financing, the investor gets a share of the business and so the gain may be quite a lot.</p>

Quiz



What type of financing is this or is needed?

Identify the type of financing that applies to each of these 10 situations.

- 1** Ali needs money to pay his university fees.

Loan Financing

Equity Financing

- 2** Shereen and Ali need money to buy a juice machine which will last for three years.

Installment Sales Financing

Loan Financing

- 3** Shereen and Ali need a long-term investor to fund their business expansion, which is quite risky.

Loan Financing

Equity Financing

- 4** Safdar gets financing to open a new shop. He must pay the money back in one year with a 20% markup.

Loan Financing

Equity Financing

- 5** Safdar invests some extra money he has in a Government of Pakistani treasury bill.

Loan Financing

Equity Financing

- 6** Safdar invests some extra money he has in shares of a company listed on the Pakistan Stock Exchange.

Loan Financing	Equity Financing
----------------	------------------

- 7** A bank provides financing for a power plant. The financing must be repaid by the power plant in 12 years.

Loan Financing	Equity Financing
----------------	------------------

- 8** Ali borrows money from a bank to buy a flat in the city.

Mortgage Financing	Equity Financing
--------------------	------------------

- 9** Shereen and Ali agree with an investor that he will get paid on his equity investment in their company before other shareholders are paid.

Common Shares	Preferred Shares
---------------	------------------

- 10** In this kind of financing, a business is required to pay the money back with a markup, even if the use of the money does not lead to a profit.

Loan Financing	Equity Financing
----------------	------------------

The solution to this exercise may be found on page 188

Stock market analysis



Test your understanding of the basics of stock markets by answering the questions below.

1. Which type of company may be listed on the Pakistan Stock Exchange?

Public Limited Company

Private Limited Company

2. A public limited company has 100,000 shares and it is listed on the Pakistan Stock Exchange. It issues 10,000 new shares to investors for Rs. 20 per share. Who receives the money from the new share issuance?

The public limited company

Investors on the stock exchange

3. A public limited company has 100,000 shares and it is listed on the Pakistan Stock Exchange. One investor (Investor A) owns 2,000 shares of the company. Investor A sells through the stock exchange all 2,000 shares to another investor (Investor B) for Rs. 20 per share. Who receives the money from the share sale?

The public limited company

Investor A

Investor B

4. A public limited company has 10,000,000 shares and it is listed on the Pakistan Stock Exchange. Someone buys 100,000 shares (1% of the total) for Rs. 20 per share. What is the total value of the company?

Rs. 200,000

Rs. 2,000,000

Rs. 20,000,000

Rs. 200,000,000

The solution to this exercise can be found on page 191

Foreign exchange, exports and imports

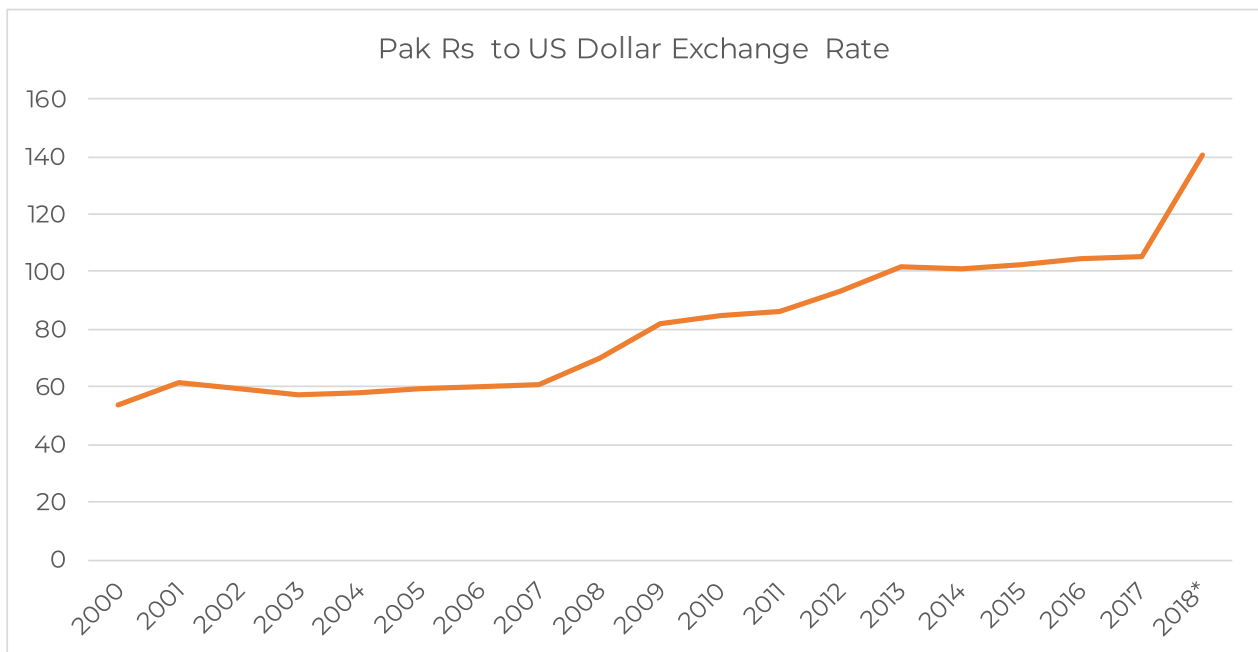
Foreign exchange refers to the exchange of one currency for another currency.

When an individual, business or country buys goods or services from overseas (i.e., engages in imports), it will exchange local currency for foreign currency and use that foreign currency to buy these goods or services.

When an individual, business or country sells goods or services overseas (i.e., engages in exports), it will obtain foreign currency from the sale of these goods or services, which it will exchange for local currency.

The exchange rate is the rate at which local currency is exchanged for foreign currency. If the currency of a country has a favorable exchange rate, it will get more units of the foreign currency. Therefore, it will be cheaper for users of that currency to import goods and services.

Pakistan's exchange rate has been dropping steadily and sometimes very quickly. The following is a chart indicating the exchange rate between the Pakistani Rupee and the United States Dollar.



Source: The World Bank

In 2000, it took approximately PKR 53 to purchase USD 1. By late 2018, it took approximately PKR 140 to purchase USD 1.

Because of this condition, individuals and businesses in Pakistan find it difficult to pay for goods and services from overseas and the government finds it difficult to pay for its foreign currency loans.

Pakistan can build up its reserve or stock of foreign currencies by exporting more.

For some businesses, this is not easy to do. For example, a power plant often has to buy expensive machinery from overseas and pay for fuel from overseas. Yet, it sells its power locally. Its ability to earn foreign currency is limited!

For other businesses, this is easier to do. For example, there is no reason PomPak cannot sell its bottled juice overseas. Often businesses that succeed overseas are those that invest in their brand and come up with high-quality products, like PomPak did. In fact, since it launched its app, PomPak has started to receive overseas orders!

Innovative, high quality business with information age marketing plans are a very important part of Pakistan's future!

Foreign exchange analysis



Test your understanding of the basics of foreign exchange by answering the questions below.

- In 2007, the Pakistani Rupee to US Dollar exchange rate was **PKR 60 to USD 1**. In 2013, the Pakistani Rupee to US Dollar exchange rate was **PKR 100 to USD 1**. During this period, did the value of the Pakistani Rupee compared to the US Dollar go up or down?

The value of PKR went up

The value of PKR went down

Cannot tell

- The exchange rate is **PKR 100 = USD 1**. A company imports chocolate bars from USA and sells them in Pakistan. It buys each chocolate bar for USD 1 and sells it for PKR 200. If the exchange rate becomes **PKR 150 = USD 1**, what will happen to its profits per chocolate bar?

Its profits per chocolate bar will increase from Rs. 50 to Rs. 100

Its profits per chocolate bar will decrease from Rs. 100 to Rs. 50

Its profits per chocolate bar will decrease from Rs. 150 to Rs. 100

- The exchange rate is **PKR 100 = USD 1**. A company exports chocolate bars from Pakistan and sells them in USA. It buys each chocolate bar for PKR 100 and sells it for USD 2. If the exchange rate becomes **PKR 150 = USD 1**, what will happen to its profits per chocolate bar?

Its profits per chocolate bar will increase from Rs. 100 to Rs. 200

Its profits per chocolate bar will increase from Rs. 100 to Rs. 150

Its profits per chocolate bar will decrease from Rs. 100 to Rs. 50

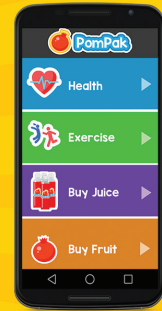
A family celebration

After lots of work the PomPak app is launched!

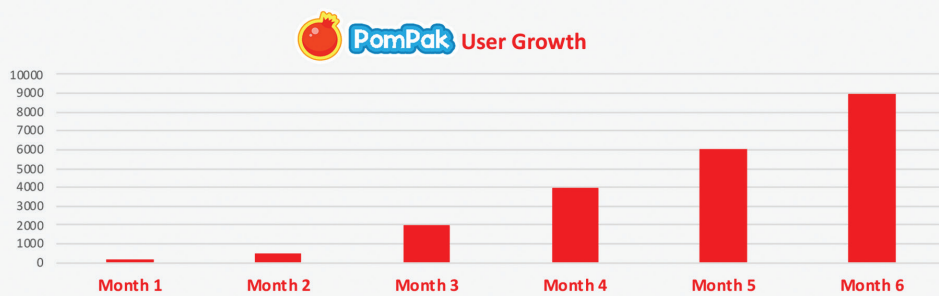
Now available on App Store and Google Play!!!



Download for **Free** now!



After a slow start, the number of users begins to climb very nicely.



Safdar

I am quite amazed! We are getting customers from all over our city. And from elsewhere. We even have some orders from customers in Dubai!

Yes, we are working out the procedures with our bank to set up a foreign currency account.

Shereen

Ali

The nice thing is that some people are using our app for information and some are using it to buy our product. We are building trust!

Our farm is growing nicely. We now have 20 pomegranate trees! And we have brought in our first two new farmers as suppliers.

Nusrat

Rabia

And Daniyal and I are really enjoying posting information on health and exercise in the app for our users!

You will soon need to call me "Dr Daniyal." Thanks for all your planning, saving and work, my lovely family!

Daniyal

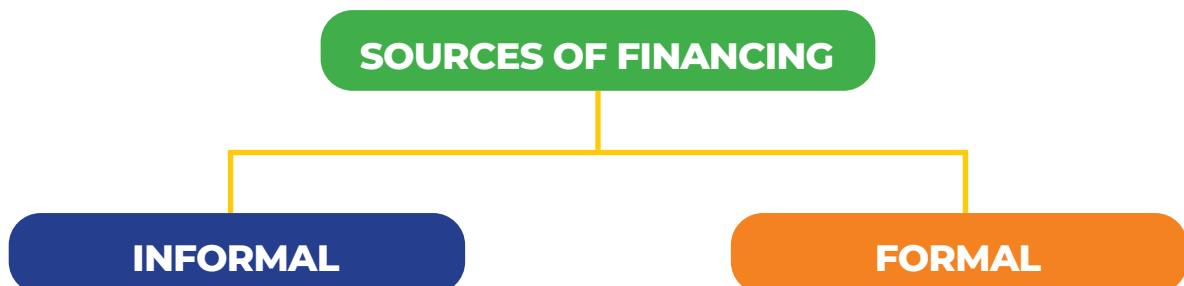
FINANCIAL MARKETS AND SOURCES OF FINANCING

Who needs financing?

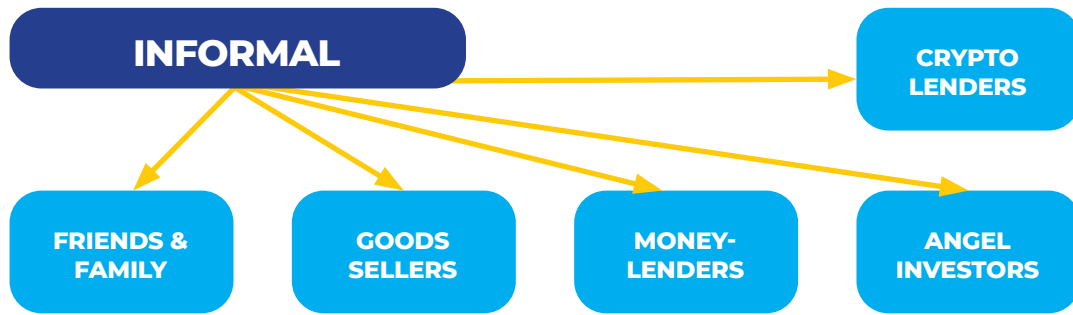
- ▶ Individuals
- ▶ Businesses
- ▶ Governments

There are many sources from which individuals and businesses can get financing. There are also other sources available to governments, but, in this section, we will focus on financing sources for individuals and businesses.

Sources of financing can be formal or informal.



Informal Sources



FRIENDS AND FAMILY

One important part of informal financing is friends and family. Many individuals borrow money from friends and family, and they can be an important source of equity financings for new businesses.

MONEYLENDERS

Some people also get financing from moneylenders. This is not a good idea.

Moneylenders often charge very high rates and you can get in physical danger if you cannot pay on time.

SELLER FINANCING

When you buy something from your local karyana and pay later, that is seller financing. In farms, arthis provide seeds and fertilizer on credit. Usually, when seller financing is provided informally for a business it can be very expensive.

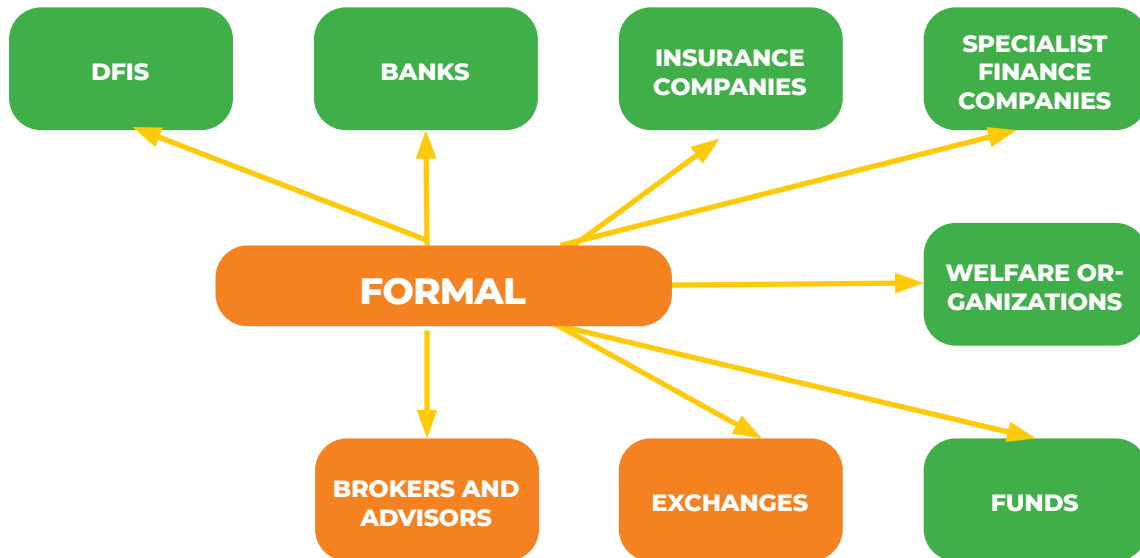
ANGEL INVESTORS

Angel investors are people who invest in the early stage of a business. These investors often invest in technology-related businesses.

These investors stand to gain the most as they enter a venture on the ground floor and rise with the success of the business. This why their returns are very high for a comparatively low investment. The risk for angel investors is also quite high as it is difficult to gauge which enterprise will be successful at such an early stage.

Formal Sources

Formal sources of financing are usually more business-oriented with traditional institutions like banks, funds and welfare organizations.



BANKS

Full-service Banks

Full-service banks provide loans to both individuals and businesses.

Personal loans include home mortgages and vehicle financing.

Business loans include long term capital financing—for example to set up a factory. They also provide working capital loans—for example to buy raw materials.

Some banks also provide equity financing for businesses, but banks are not a major source of equity financing.

Micro-finance Banks

Micro-finance banks provide very small loans to individuals and small businesses. These loans can be for personal use or very small businesses.

DEVELOPMENT FINANCE INSTITUTIONS OR DFIS

DFIs are government-linked financial institutions which provide loan and equity financing for businesses. They usually provide financing for fairly large businesses.

SPECIALIST FINANCE COMPANIES

There are many types of specialist financial institutions.

These include **credit card companies**. Many banks also issue credit and debit cards. Credit card loans have high markups so it is not a good idea to use them except for short term borrowings.

Leasing companies and **installment sales companies** provide financing for individuals and businesses to acquire vehicles and equipment.

Fintech is a quickly growing area of finance. **Fintech companies** use technology to provide financial services at a low cost. So far, only a few such companies provide long-term financing.

INSURANCE COMPANIES

Insurance companies include life insurance companies, which insure individuals.

General insurance companies provide insurance for homes and businesses too. Through some insurance plans and products the insurance premiums are invested to get returns on those investments when the insurance policy expires.

WELFARE ORGANIZATIONS

Welfare organizations or non-profits such as charities and foundations provide funding for good causes.

And government-linked welfare programs such as Benazir Income Support Program are now a major part of welfare funding in Pakistan.

FUNDS

Funds are also a major source of financing.

These include, private equity funds, venture capital funds, pension funds, and mutual funds.

Private equity funds invest in large companies and often help one large business buy another.

Venture capital funds invest in technology companies and other new businesses which can provide a very high return at a high risk.

Pension funds are often very big. They invest the money in pension plans of people. They invest a large amount of their money in government bonds and in large, companies listed on the stock exchange.

Mutual funds take investments from individuals and companies and invest in companies listed on the stock exchange. They are a good way for a person to invest in many companies on the stock exchange by making one investment decision.

EXCHANGES

An exchange, like the Pakistan Stock Exchange, is a financial market and it plays a role in financing.

An exchange, like the Pakistan Stock Exchange, is a financial market with a primary financing role and a secondary financing role.

It plays a **primary financing role** because companies can sell their shares or bonds on the exchange and receive money from investors.

It plays a **secondary financing role** because sellers and buyers of listed shares or bonds can easily sell and buy these instruments at the market price.

BROKERS AND ADVISORS

Brokers and advisors help companies raise money and sell and buy shares on the exchange.

Usually, large companies list on the stock exchange because the legal requirements are quite strict.

Real Estate Investment Trusts, which deal in landed properties, and Modarabas, which are Islamic investment companies, are also listed on the exchange.

And mutual funds, which hold shares in other companies, are also listed on the exchange.

Financing Needs and Requirements

While there are many sources of financing, you need to have a clear plan.

As part of your plan, you need to ask yourself a few questions. The answers to these questions will lead you to the appropriate source of financing for you or your business.

Key Questions

What is the purpose of the financing?

Will debt or equity be more suitable?

What is the size and stage of my business?

Who will be interested in investing in such a business?

Activity



What is the source of financing for each financing need?

Identify the source of financing that applies to each of these 16 situations. Circle the correct option.

- 1** Shereen and Ali need money to buy a juice machine that will last for at least three years.

Installment Sales Company

Bank

- 2** Safdar wants to buy a motorcycle for his employee but cannot pay all cash.

Leasing Company

Seller Financing

- 3** A restaurant buys fruit from a fruit seller and wants to buy now but pay later.

Installment Sales Company

Seller Financing

- 4** Safdar wants to insure the inventory and equipment in his shop.

General Insurance Company

Life Insurance Company

- 5** A fruit seller with a cart wants some money to buy more fruit to sell.

Bank

Microfinance Bank

- 6** Safdar has expanded to four shops and needs financing for all the fruit he will need to buy every day.

Bank	Microfinance Bank
------	-------------------

- 7** Safdar wants to obtain equity financing for his company from as many people as possible.

Stock Exchange	Venture Capital Firm
----------------	----------------------

- 8** Safdar wants to quickly transfer money through his mobile phone.

Fintech Company	Venture Capital Firm
-----------------	----------------------

- 9** Safdar wants to get insurance so that his family are taken care of if something happens to him.

Life Insurance Company	Health Insurance Company
------------------------	--------------------------

- 10** Safdar wants to pay for a dinner he has had at a hotel but does not have cash.

Credit Card	Microfinance Bank
-------------	-------------------

- 11** Safdar wants to borrow money to build a new house.

Bank	Fintech Company
------	-----------------

12 Safdar wants to invest some money he has in shares of a number of companies, but he doesn't know much about the stock exchange.

Mutual Fund	Private Equity Firm
-------------	---------------------

13 Safdar wants to deposit some money and earn a return and after he has saved enough, he will buy a car.

Bank	Leasing Company
------	-----------------

14 Shereen and Ali want to obtain investment for a technology business idea they have just had.

Venture Capital Firm	Friends and Family
----------------------	--------------------

15 Shereen and Ali want to obtain investment for a technology business they have just started. Operations have started and some very early sales are happening.

Venture Capital Firm	Angel Investors
----------------------	-----------------

16 Shereen's and Ali's new technology business is growing but they need equity financing for it to become profitable and become bigger.

Venture Capital Firm	Stock Exchange
----------------------	----------------

The solution to this exercise may be found on page 23.

DIGITAL BANKING AND FINTECH

Digital Banking

Digital banking refers to the delivery of banking services and financial products through digital channels such as online banking, mobile banking, and ATM banking. This allows customers to access and manage their banking accounts, make transactions, and pay bills through their computer, smartphone, or other digital devices.

Almost all traditional banks now also offer digital banking services, however there are some banks that are purely digital banks. These banks offer their financial products primarily through digital platforms or electronic channels.

To benefit from digital banking, a user must have a bank account in a traditional bank and then activate digital banking from the bank. They can then download the app or visit the bank's website, log in, and use the services on offer.

APPLICATIONS AND BENEFITS OF DIGITAL BANKING

Digital banking offers customers a more convenient and efficient way to manage their finances, as they can perform many banking tasks 24/7 without having to visit a physical branch.

Some applications of digital banking are:



STATE BANK'S ROLE AS REGULATOR

The State Bank of Pakistan has launched a licensing and regulatory framework to set up digital banks as a separate category in the banking business.

You can fulfil your banking needs without physically going to the bank. This is service on the go or from the comfort of your home.

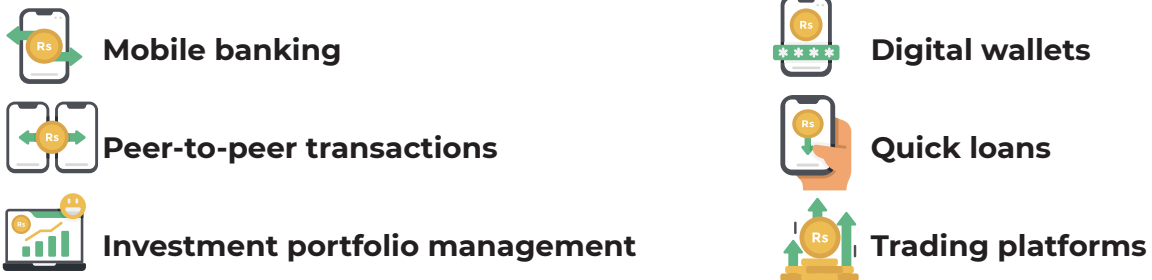
Financial Technology (Fintech)

Digital banking is part of a field called Financial Technology or Fintech. Fintech is a term used to describe all the companies and technologies that offer financial products and services.

Fintech companies use technology and are disrupting the traditional financial services industry with all the ease and benefits that they offer the consumer. The goal of fintech is to make financial services more accessible, efficient, and affordable, often by using new technologies such as blockchain and artificial intelligence. Fintech has the potential to revolutionize the way we access, manage, and invest our money.

APPLICATIONS AND BENEFITS OF FINTECH

With the increase in use of cell phones and digital devices, Fintech has the ability to reach more consumers. The applications of fintech include:



RAAST – PAKISTAN’S FIRST INSTANT PAYMENT SYSTEM

RAAST is Pakistan’s first Instant Payment System. It is a fintech initiative taken by the State Bank of Pakistan that enables instant end-to-end digital payments between individuals, businesses, and government entities.

It provides a single link to a central infrastructure that makes making digital payments accessible across any channel to customers of any financial institution.

SECP’S ROLE AS FACILITATOR AND REGULATOR

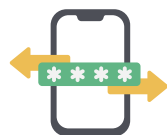
The Securities and Exchange Commission of Pakistan, or the SECP, has set up a Regulatory Sandbox for innovative fintech companies to test their products before being launched full-scale.

Protection From Malicious Activity

As fintech gains popularity, it is important to understand that it is still a new phenomenon. Not all fintech companies are regulated as well as traditional banks and instances of fraud and deception are possible.

Therefore, it is important to be cautious when trusting any fintech firm with money. A wary mindset and good digital hygiene goes a long way.

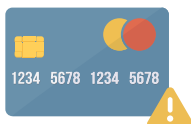
To protect yourself, be aware of your rights and take protective measures such as:



Never share your password or security details with anyone.



Confirm the source of any digital communication and make sure that it is authentic.



Be wary of unusual payment requests.



Set strong passwords.



Use anti-virus programs to protect your device.

TAXATION

What is Taxation?

Taxation is a process by which a government provides services to its citizens. In order to build roads, hospitals, schools, and provide essential amenities, the government needs funds. It acquires these funds from the citizens, by charging a fee—or tax—on any income they earn, or any product, good, or service they buy.

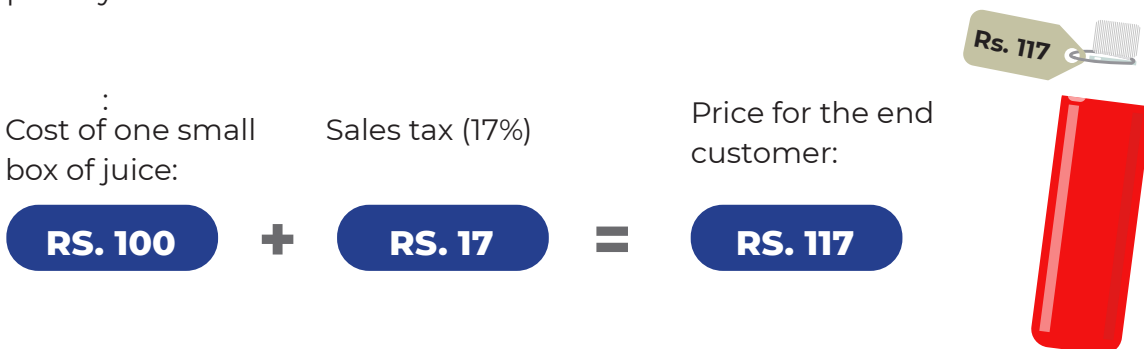
There are two types of taxes: direct and indirect. Let's learn more about the different types of tax that Pakistani citizens must pay.

Indirect Taxes

Indirect taxes are paid by companies and corporations to the government. The government assigns a tax on every product sold and collects that amount from companies.

SALES TAX

Companies collect this tax from the end consumer. This means they set a price for a product and then sales tax or VAT is added on top of that price. The combined cost is paid by the customer:



Sales tax or VAT is added to every service and product manufactured in Pakistan.

EXCISE AND CUSTOM DUTY

Excise Duty is a special tax charged by the government for specific goods manufactured in the country like cigarettes, aerated drinks, and certain types of cars. Excise duty is typically passed on to the end consumer in the form of a higher price for the product, and businesses are required to pay this tax as part of their tax obligations. The purpose of this tax is to keep the production and sale of these products under control.

Custom Duty, on the other hand, is a tax for goods imported from outside the country. If you buy a mobile phone abroad and bring it into Pakistan, you'll have to pay this tax when you go through customs at the airport.

Think of Excise Duty and Custom Duty as a way for the government to regulate the production and import of goods. By paying these taxes, you are helping to finance the country’s public services and infrastructure.

In a nutshell, taxes like Excise Duty and Custom Duty may seem like a hassle, but they play a crucial role in the development of the country and ensuring that public services are available to everyone.

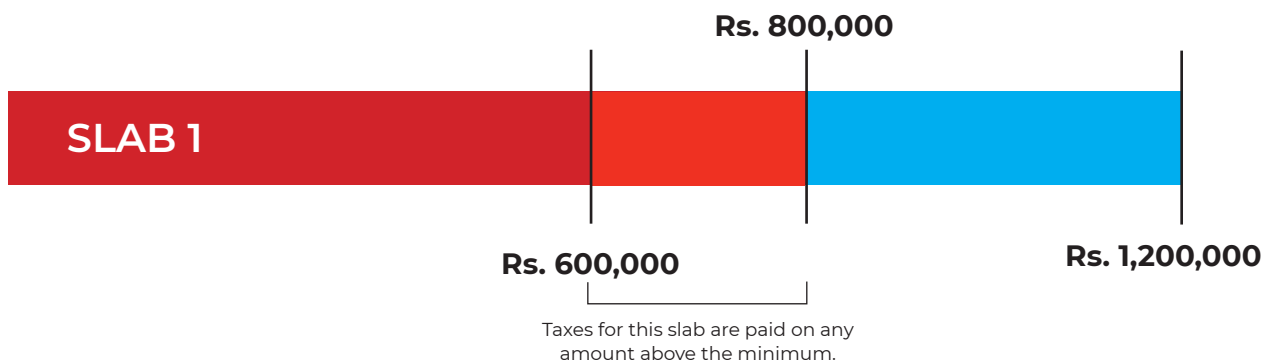
Direct Taxes

INCOME TAX

Income tax is a tax on the money that you earn. It is based on your salary and is calculated as a percentage of your income. In Pakistan, the income tax rate ranges from 5% to 35%, depending on your income level.

The rates are divided into income slabs. Slabs ensure that someone who earns a low salary pays lower taxes than someone who earns a high salary. The slabs are based on annual earnings.

The first and lowest slab is for those people who earn more than Rs. 600,000, but less than Rs. 1,200,000 every year. They pay 2.5% taxes on any amount they earn above the minimum amount. If your annual earnings are Rs. 800,000, for example, you would pay 2.5% tax on Rs. 200,000 (which is the amount over the minimum amount of Rs. 600,000 in this slab). This would be around Rs. 5,000 a year.

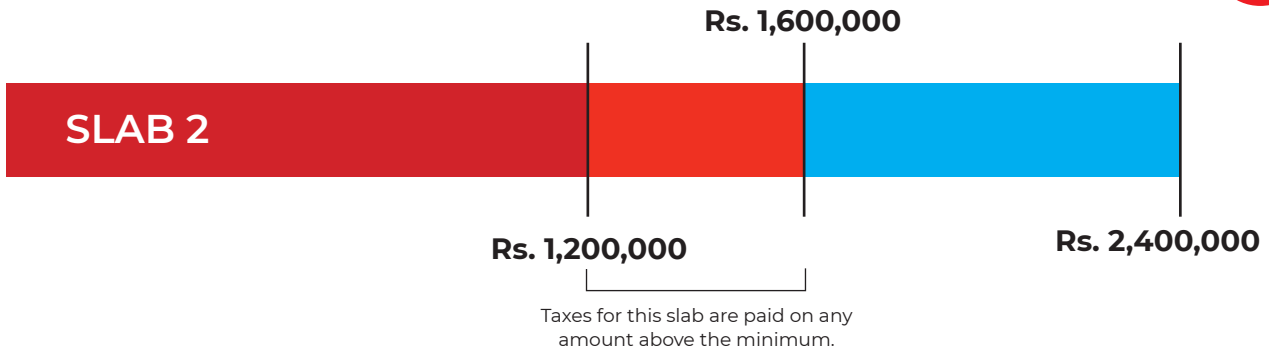


These slabs are revised by the government every year. The rates for 2022 – 2023 are:

Taxable income (PKR)		Tax on column 1 (PKR)	Tax on excess (%)
Over (column 1)	Not over		
0	600,000		0
600,000	1,200,000		2.5
1,200,000	2,400,000	15,000	12.5
2,400,000	3,600,000	165,000	20
3,600,000	6,000,000	405,000	25
12,000,000	12,000,000	1,005,000	32.5
		2,955,000	35

In the table above, the first two columns are the minimum and maximum amounts in each slab. The third column is the fixed tax to be paid in each slab. The final column is the percentage to be paid on anything over the minimum amount.

Calculating tax



In the image above, Daniyal earns Rs. 1,600,000 a year, which is Rs. 133,000 every month. Based on the table explaining the slabs, can you calculate how much tax Daniyal should pay in 2023? Fill out the blanks in the steps below:

Step 1: Identify taxable amount based on the slab:

Salary:	Rs. 1,600,000
Minimum slab amount:	Rs. 1,200,000
Amount in excess:	Rs. 400,000

Step 3: Calculate the taxable income tax amount:

$$\frac{\text{Tax rate on excess} \times \text{Taxable income (excess)}}{100}$$

Step 2: Find fixed tax amount and rate on taxable income:

Fixed tax on minimum	Rs. 15,000
Tax rate on excess	

Step 4: Add the fixed tax and the taxable income tax amount to get the full tax Daniyal owes:

Rs. 15,000 + [result from Step 3] =
Rs. 65,000 per year

The solution to this exercise can be found on page 203

BUSINESS TAX

Businesses, just like individuals, also pay income tax. Businesses pay a percentage of their earnings to the government based on their size and income. Just like individuals, the amount of tax is broken down into slabs. The rates for 2022 – 2023 are:

Company type	2022	2023	2024 & onwards
Banking company	35%	39%	39%
Public company other than a banking company	29%	29%	29%
Any other company	29%	29%	29%
Small company	21%	20%	20%

Businesses pay a minimum amount to the Federal Board of Revenue (FBR) regardless of whether they earn profits or not. This is particularly important for small and medium businesses.

PROPERTY TAX

Both businesses and individuals also pay taxes to their local governments on any property they own. This may be a commercial or residential property.

CAPITAL GAINS TAX

However, if businesses and individuals buy and sell property for investment purposes, then they pay a capital gains tax on the purchase or sale of the property.

Filing Tax Returns

It is the responsibility of every citizen to register their source of income with FBR and to file yearly tax returns.

FEDERAL BOARD OF REVENUE (FBR)

Federal Board of Revenue (FBR) is responsible for revenue generation for the Federal government of Pakistan. It is the mainstay for revenue generation in the country and its performance is pivotal for the government to meet its obligation towards its citizens. Primarily it is responsible to execute the fiscal policy of the government by levying taxes and duties on imports, exports, incomes and profits.

FBR is also a law enforcement agency that investigates financial crimes such as tax crimes, suspicious accumulation of wealth and money-laundering.

FILING OF TAXES

You can file returns with the help of a tax accountant or firm. Or, you can use FBR's online platform to file them yourself. Simply go to <https://iris.fbr.gov.pk/> to sign up. FBR has videos and documents that can walk you through the process of filing returns step-by-step.

ADVANTAGES OF BEING A 'FILER'

Citizens and businesses that register with FBR and file yearly tax returns are known as 'Filers'. Compared to non-Filers, Filers have several distinct advantages:

FILERS	NON-FILERS
Pay less withholding tax on all financial services	Pay 100% more withholding tax on all financial services
Pay a lower tax on property and vehicle purchases and sales, investment dividends, profits on savings	Pay a higher tax on property and vehicle purchases and sales, investment dividends, profits on savings
Small chance of being audited by FBR	High chance of an FBR audit

Insurance

Insurance



Daniyal

Shereen I am really worried. Climate change is real and its effects in Pakistan are so terrible.



Shereen

You're right Ali.. But what can we do?



Daniyal

We have invested so much in this business and it has grown a lot. I am afraid one event like this flood could mean we will lose it all.



Shereen

It's good that you are worrying about the future. Because there is something that we can do. We can get insurance for our warehouse.



Daniyal

Hmmm.. I don't know.. I don't want to be paying insurance companies premiums for years just incase something like this happens to us.

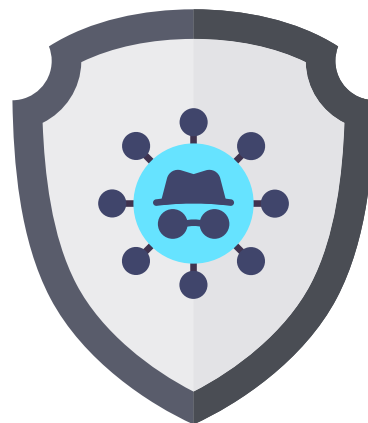


Shereen

It is not as simple as that Ali. Insurance can have many benefits! Let me tell you about them.

ASSESSING INSURANCE NEEDS

Assessing insurance needs is an important step in ensuring you have adequate coverage. This can be done by considering your personal or professional circumstances and financial goals. For example, if you have a family, you may want to consider life insurance to take care of your loved ones in the event of your death. If you own a home or car, you may want to consider property and liability insurance.



Activity



Match the type of insurance with the personal circumstances of the customer:

Circumstances

A

Person A is a new homeowner who wants to protect their investment in case of a fire or other unexpected event.

B

Person B is a freelancer who wants to protect their income in case they are unable to work due to illness or injury.

C

Person C is a world traveler who wants to be protected against the costs of medical treatment or trip cancellation while abroad.

D

Person D is a small business owner who wants to protect their business assets and income in case of a lawsuit or other unexpected event.

Insurance Product

Travel insurance or international health insurance, which would cover the cost of medical treatment or trip cancellation while abroad.



Business or liability insurance, which would cover legal expenses and costs associated with a lawsuit or unexpected event that impacts the business.



Homeowner's insurance or property insurance, which would provide coverage for damage to the home or its contents due to fire, theft, or other unexpected events.



Disability insurance or income protection insurance, which would provide a regular income if the policyholder is unable to work due to illness or injury.



Choosing the right insurance product

Choosing the right insurance product can be a daunting task, but it's important to make the right decision. You can compare insurance policies from different providers, considering factors such as costs, coverage, and the insurance company's reputation for claims payments. A variety of factors can influence the cost of insurance, including type and amount of coverage, and the age and health of the policyholder. It's also important to regularly review and adjust your insurance premiums to ensure they are in line with your changing circumstances and financial goals.

Activity



If you are a 30 yr. old with two children, which insurance cover works best for you? Why?

Terms	Big family insurance	City life insurance
Premium	Rs. 15,000 a year	Rs. 18,000 a year
Coverage	Rs. 7,500,000	Rs. 7,500,000
Term	15 years	15 years
Riders	This plan has a health insurance rider for cover upto Rs. 50,000	This plan has no riders
Tick the option you would choose	<input type="checkbox"/>	<input type="checkbox"/>

The solution to this exercise can be found on page 205

Insurance as an investment tool

Insurance is often sold as an investment tool, providing benefits such as a savings component wherein a certain amount of money is invested in a fund to provide returns to the policyholder. However, it is important to understand that insurance should not be relied upon solely as an investment and that there may be drawbacks to this sort of product, such as high premiums, high fees, and surrender charges if you want to withdraw money before a certain time. When purchasing such a policy always find out the terms and conditions and compare the costs and returns against other investment products.

Conventional insurance vs Takaful

Other products which serve a similar purpose to insurance include General and Family Takaful. This Islamic form differs from conventional insurance and is based on the principles of cooperation and shared responsibility. Whereas conventional insurance relies on the payment of premiums to an insurance company that assumes the risk and pays out in the event of a loss, Takaful participants contribute to a shared pool of funds that is used to provide financial protection for members in case of an insured event. The takaful operator serves as a wakeel or manager of the pool rather than its owner. Takaful is designed to be in compliance with Islamic law and principles, such as the prohibition of interest and excessive uncertainty. Here are some basic differences between conventional life insurance and family takaful.



Takaful	Conventional Insurance
The Takaful contract is a Tabarru or donation-based contract.	Conventional insurance is a contract based on compensation or payment.
Each participant shares some of the risk.	The corporation assumes the risk.
The Waqf pool is the owner of the contribution made. This sum is not owned by the Operator.	The insurance company is the owner of the premiums paid by the insured.
The Participant Takaful Fund exclusively makes investments in shariah-compliant ventures.	company money is invested without regard to whether or not an activity is compliant with Shariah.
There is no allowance for underwriting profit.	If the amount paid for claims is less than the premium collected, insurance companies profit.
Underwriting procedures adhere to the Halal and Haram shariah structure.	Underwriting methods used by insurance firms do not adhere to Halal and Haram framework
The Participants Takaful Fund or Waqf fund will pay out the claims.	The claims are paid for by company money.
Through the Waqf Pool, members receive a surplus.	Company shareholders keep all surpluses.
A Shariah board or advisor is integral to supervise the investment activities of the company.	There is no Shariah supervision in conventional insurance.

Cryptocurrency

Cryptocurrency

Daniyal



Yoo Ali, check this out, my friend Abdullah made \$20,000 by investing in Bitcoin. I am really tempted to put all my savings in Bitcoin and make some money!

Haha Daniyal, do you know anything about cryptocurrency?

Ali



Daniyal



Not really.. All I know is that it is a digital currency and that a lot of people have started buying it.

There is a lot more to cryptocurrencies than just calling it a digital currency.

Ali



Daniyal



Huh? Do you know about cryptocurrency? Can you tell me about it? I guess I really should learn about it before I put all my savings into it.

Ji Daniyal, I know about cryptocurrency. Just like you I was also hearing a lot of amazing things about it and so I started researching what it actually is. Wanna learn about it?

Ali



Daniyal



Yes, please. Tell me what you know.

BLOCK CHAIN & CRYPTOCURRENCIES

Cryptocurrency

Cryptocurrency is a digital or virtual form of currency that uses cryptography for security and operates independently of a central bank.

All currencies maintained by countries, like the US dollar, the Saudi Riyal, and the Pakistani rupee, are regulated by their central banks. These banks implement policies that influence the value of these currencies.

Cryptocurrency, on the other hand, is decentralised. No particular bank regulates or influences its value.

Examples of cryptocurrencies include Bitcoin, Ethereum, and Litecoin.



Bitcoin



Ethereum



Litecoin

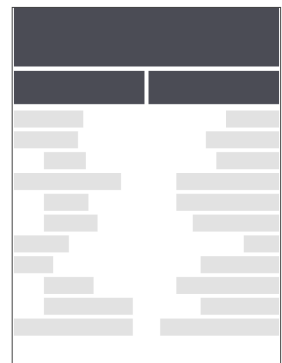
Transactions using cryptocurrencies are recorded in a ledger called a blockchain

What are Blockchains?

A blockchain is a decentralized digital ledger that is distributed across a network. This means no one organization or individual owns the ledger.

Each block in the chain contains a record of multiple transactions and is linked to the previous block, forming a chain of blocks that cannot be altered retroactively without the consensus of the network that holds the records.

No single entity writes or owns the blockchain. Instead, the blockchain is maintained by a network of computers, also known as nodes, that validate and record transactions on the blockchain. This validation process is called consensus and is achieved through algorithms such as Proof of Work or Proof of Stake.



BENEFITS AND APPLICATIONS OF CRYPTOCURRENCY

It is decentralised.

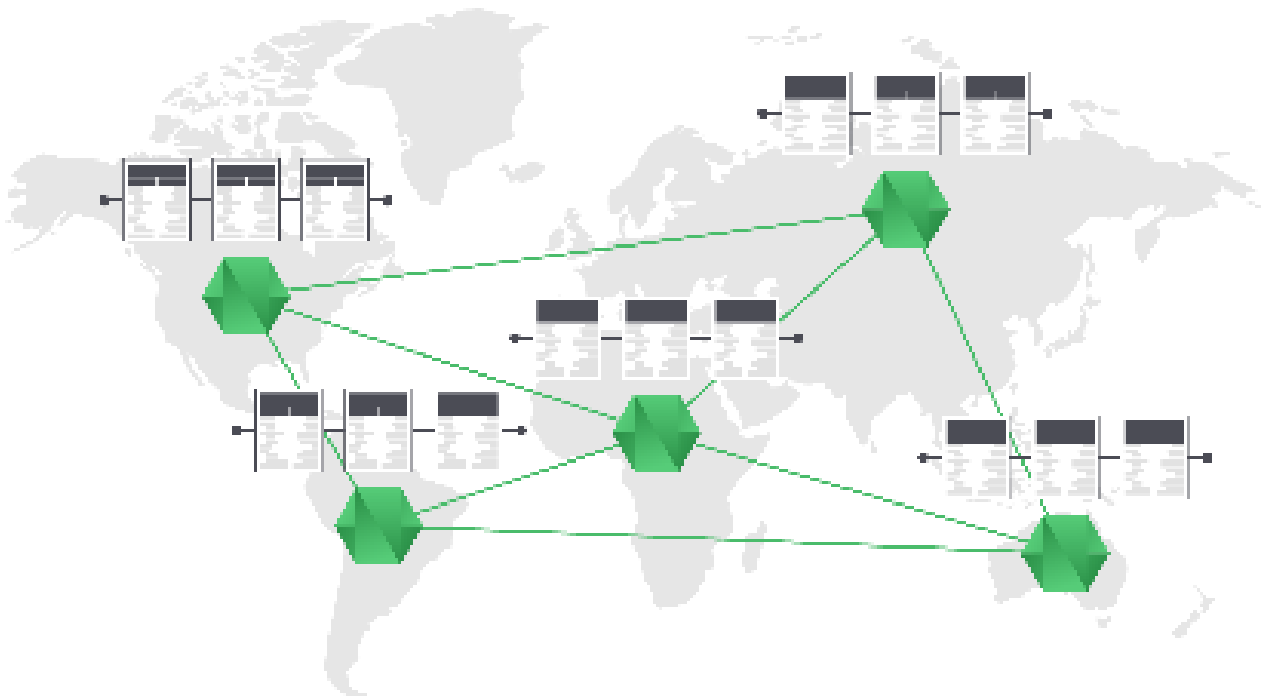
No single bank can influence and control its value. This means only the market forces can affect the price or value of a cryptocurrency.

It uses cryptography for security.

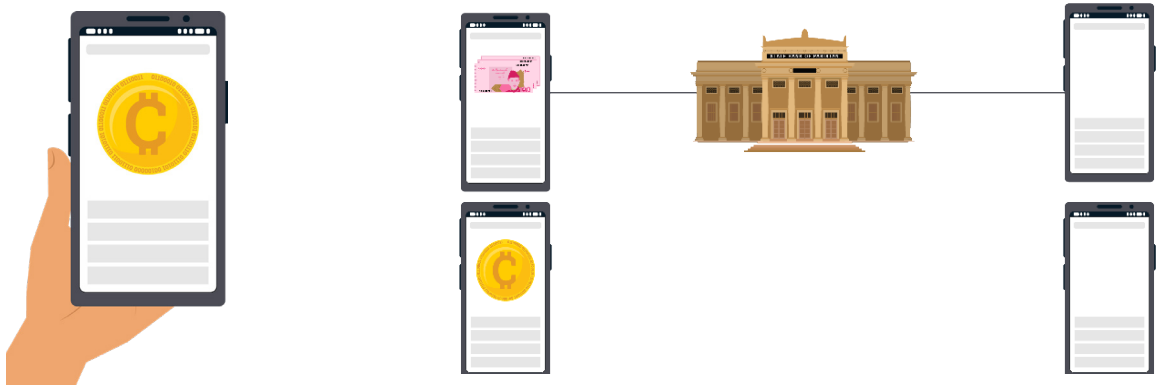
All transactions made through cryptocurrency are secure and cannot be forged due to the use of cryptography.

The records or 'ledger' is maintained across a network of computers.

This means that even if one computer is hacked or compromised, the record or data of cryptocurrencies is preserved. It is maintained across a network of computers all over the world.

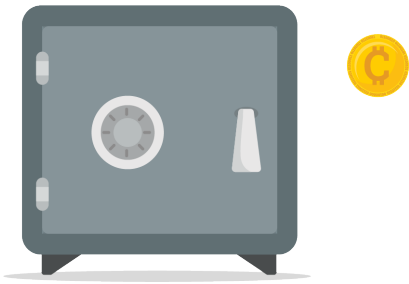


Due to these benefits, cryptocurrency offers many applications. Some applications of cryptocurrency are:



1. Make digital payments: cryptocurrency can be used to make digital payments for goods and services.

2. Decentralised finance: It can be used as a tool for Decentralised Finance, lending and borrowing, without the influence of a central bank or a country's economic policy.



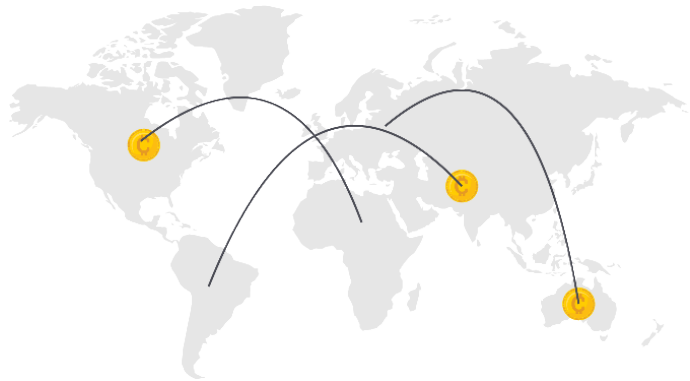
3. Store of value: Cryptocurrency can be used as a store of value. Just like people buy property or gold to save and store their money.



4. Investment: If you buy a cryptocurrency and its value increases, you have made money as you would through any other investment.

5. Cross-border transfers:

Cryptocurrency can be used to make cross-border transfers such as remittances. These transfers are fast, cost-effective, and secure, and they do not need intermediaries like banks or money transfer agencies.



BENEFITS AND APPLICATIONS OF BLOCKCHAINS

The benefits of cryptocurrency are actually the benefits of blockchain technology. These benefits offer a lot of applications for blockchains, the biggest of which is cryptocurrency. Other applications of blockchains are:

1. Non-fungible tokens or NFTs - this is digital property like images, videos, or songs that can be bought and sold.

2. Smart Contracts - as blockchains are both transparent and secure, they are used to make smart contracts.

Smart contracts are programs stored on a blockchain that run when predetermined conditions are met. They typically are used to automate the execution of an agreement so that all participants can be immediately certain of the outcome, without involving an intermediary.

3. Supply chain management - using blockchain to improve transparency and traceability in supply chain operations.

4. Identity management - using blockchain to securely store and manage personal identity information.

5. Digital voting - using blockchain to provide secure and transparent voting systems.

6. Gaming - using blockchain to create and trade in-game items with real-world value.

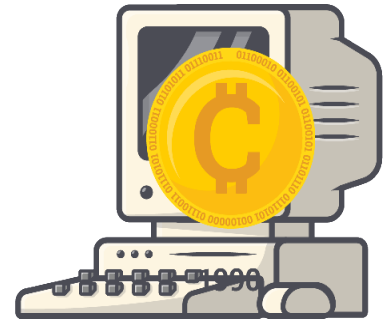
7. Real estate - using blockchain to manage property transactions and ownership records.

8. Healthcare - using blockchain to securely store and share medical records and personal health information.

History of Cryptocurrency

The idea emerged in the 1980s with advancements in the field of cryptography.

The first cryptocurrency, Bitcoin, was launched in 2009 but it gained extreme popularity in 2017 when its value rose from \$1,000 to \$20,000 before falling back to under \$10,000. This reflects the volatility of cryptocurrency.



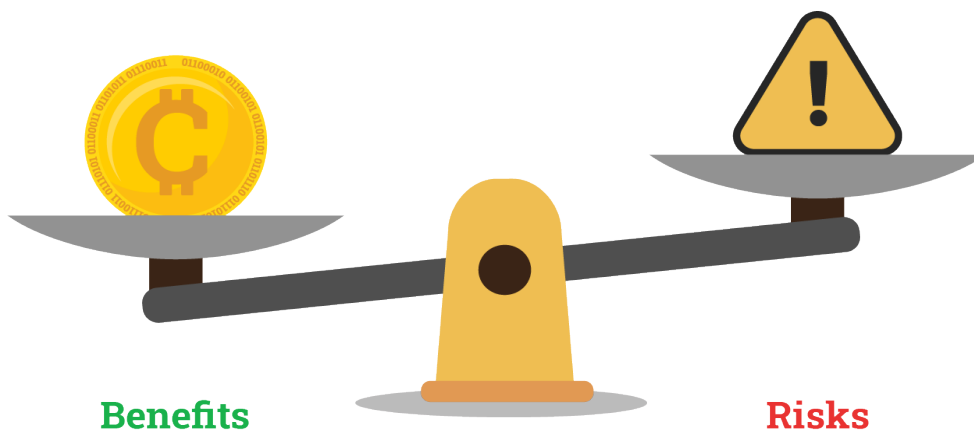
As cryptocurrency is decentralised and does not come under the provision of a central bank, governments across the world are currently letting the free market self-regulate cryptocurrencies. But, as more and more applications of cryptocurrency are coming forward, governments are starting to form policies to regulate and control it, to protect the consumers.

Pakistani State's Stance on Cryptocurrency

The State Bank of Pakistan is aware of the pros and cons of cryptocurrency but believes that its risks far outweigh the benefits.

The State Bank's stance is that cryptocurrency is very volatile and is not a good vehicle for investment or storing of value. Therefore, it only adds instability to the system and has the potential to create chaos and undermine the stability of the market. This hinders the SBP ability to keep Pakistan's economy stable.

Governments across the world are currently letting the free market self-regulate, though that may change in the future.



Career planning

Career planning

Daniyal



Shereen, I'm confused. I love being a doctor, but I sometimes feel like I would also be great at other professions.

Hmm, interesting. What sorts of professions?

Shereen



Daniyal



I'm not sure. I admire how you and Ali grew PomPak into such a great business. I want to do something similar.

Ah yes, I guess the spirit of entrepreneurship runs in the family. Being an entrepreneur does require specific skills like vision-setting and networking.

Shereen



Daniyal



Is there any way for me to use these skills while being connected to the medical field?

There is! You can launch a technology startup with a focus on health. This industry is known as health tech. The world as we know it is rapidly changing, so this would actually be a great way of creating positive change while also dealing with the uncertainty of the future.

Shereen



Daniyal



Wow, I'd love to learn more about this.

CAREER PLANNING

Introduction

Career planning is a crucial aspect of achieving professional success. It involves identifying one’s interests, skills, and goals and determining the steps required to achieve them. In today’s fast-paced and ever-changing world, it is essential to have a set of skills that will be valuable regardless of the industry one works in, for both salaried professionals and entrepreneurs.

These skills become especially important when one considers that as many as 1.1 billion jobs globally could be impacted by technology over the next decade:

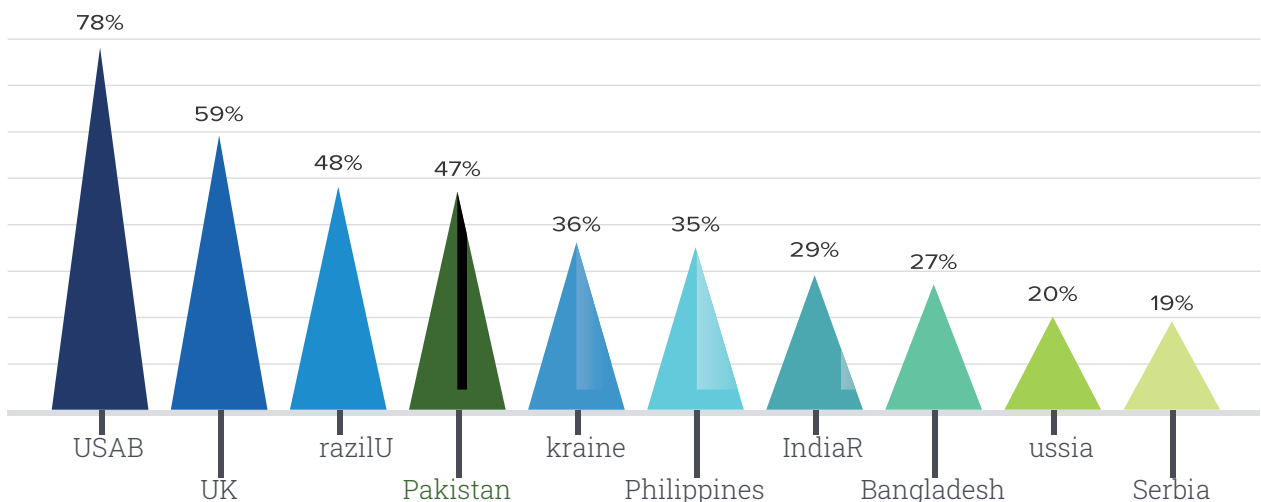
Before discussing these skills, let us take a look at some statistics about the current state of work in Pakistan and the future of work.

State of Work in Pakistan

- ▶ Pakistan’s automation preparedness score is 40%, among the lowest in the Asia-Pacific region.



- ▶ More than 90% of the population in Pakistan lacks basic Information and Communication Technology (ICT) skills.
- ▶ Internet users in the country have increased from around 17 million in 2012 to 83 million in 2022.
- ▶ In 2022, the country generated 500 million US dollars from freelancing, ranking it as the fourth fastest-growing market in the world for freelancers.



Essential Professional Skills

CRITICAL THINKING AND PROBLEM-SOLVING

Critical thinking is the process of analyzing information and ideas to make informed decisions. Problem-solving is the ability to identify problems and find effective solutions.

TECHNOLOGY USE, MONITORING, AND CONTROL

With technology playing an increasingly important role in the workplace, the ability to use, monitor, and control technology is in high demand. A good understanding of technology can help individuals become more efficient and effective. It is important to stay up to date with the latest technological developments in your industry.

CREATIVITY AND IDEATION

Creativity and ideation refer to the ability to generate new and original ideas, and to think outside the box to come up with innovative solutions.

LEADERSHIP AND SOCIAL INFLUENCE

Being able to lead and influence others can help individuals stand out and advance in their careers. In today's collaborative work environment, we will all have peers, managers, and supervisees at different stages of our careers. The skill to effectively negotiate these relationships is sought after in all industries.

DATA ANALYSIS AND INTERPRETATION

The ability to extract relevant information from data is becoming increasingly important. Data analysis and interpretation skills can help individuals make informed decisions, identify trends, and improve their work.

INDUSTRY EXAMPLES: FARMERS AND PLUMBERS

- ▶ Farmers can benefit greatly from developing these professional skills. For instance, knowledge of the latest technology can help farmers increase productivity and profitability. Using digital tools, farmers can predict weather patterns with greater accuracy, enabling them to take appropriate measures to protect their crops from weather-related damage. In addition, farmers can evaluate and modify soil quality. By reading reviews on websites, farmers can also make informed decisions when purchasing expensive machinery, leading to cost savings in the long run.
- ▶ Plumbers can also benefit. For instance, basic digital literacy skills can help plumbers to create an online profile to showcase their work and services. This can make it easier for customers to find them and leave reviews of their work, which can help to build their online presence and expand their customer base. Additionally, effective communication and customer service skills can help plumbers to build strong relationships with their clients, leading to repeat business and positive word-of-mouth referrals.

Activity



Digiskills.pk—launched by the Ministry of Information Technology and Telecommunications—is a website that provides free upskilling courses for the most in-demand skills.



Whenever you have access to the internet, browse this website and identify the three courses that you would like to take to enhance your professional skills:

1. _____
2. _____
3. _____

Specific Skills for Entrepreneurs & Salaried Professionals

ENTREPRENEURS	SALARIED PROFESSIONALS
Have a clear vision for their business and be able to sell their vision to others.	Teamwork and reliability
Willing to take risks and make bold decisions.	Time management
Have knowledge of all areas of business.	Technical skills (such as proficiency in software programs or systems)
Able to network effectively to connect with potential customers, partners, and investors.	Proactively remaining up-to-date with industry standards and practices
Resilience and adaptability (entrepreneurs often face unexpected challenges and must be able to pivot their strategy quickly)	

Fraud

Fraud

Safdar

Shereen, I am so excited about a great investment opportunity that just came up. We don't have to worry about raising funds for the company any longer!

That's amazing, Abbu. What kind of investment is this?

Shereen

Safdar

An old classmate is running a company that is making incredible profits. If I invest 20 lakh in his company right now, I'll receive 60 lakhs in just four months.

That's...interesting. Can you please share the financial documents of the company he must have sent you, along with the company's website?

Shereen

Safdar

Umm, he didn't share any of these details. He just shared a WhatsApp message.

Uff, Abbu. When investing such a large amount, you have to be certain it's not a scam.

Shereen

Safdar

But this is someone I know! He would never deceive me.

That doesn't matter. We all need to be aware of the types of fraud that can occur, and how we can protect ourselves.

Shereen

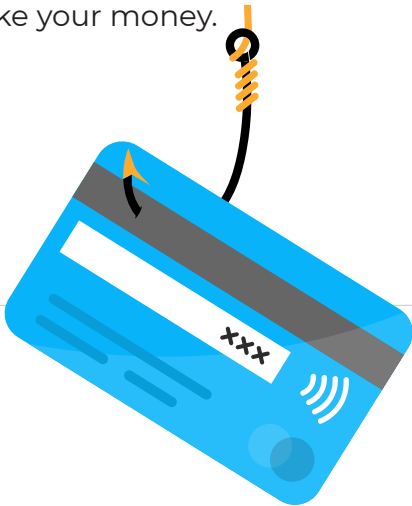
DETECTING FINANCIAL FRAUD

Financial fraud is a crime in which someone deliberately misleads or tricks others to steal their money or financial resources. It is often done by hiding or changing important information through deception and lying. Detecting and preventing financial fraud is an important issue for individuals and businesses.

There are two main categories of fraud: investment scams and identity theft.

INVESTMENT SCAMS

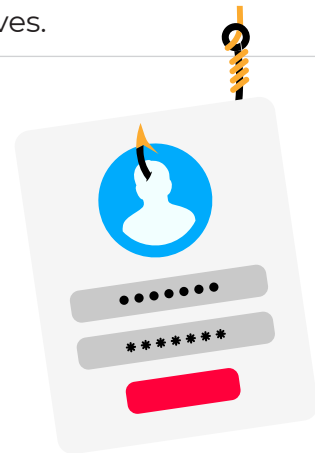
In investment scams, an individual will take a victim's money by promising a very high profits or returns. These scammers can be strangers or acquaintances. They can even be colleagues, friends, or family. These opportunities are not real: the scammers are just trying to take your money.



VS IDENTITY THEFT

Identity theft is when someone steals your personal information, such as your name, address, CNIC, or bank account details, without your permission or by deceiving you. They might tell you they urgently need your details to prevent your money from being seized. They might also say they want to offer you a new type of financial service, like a loan.

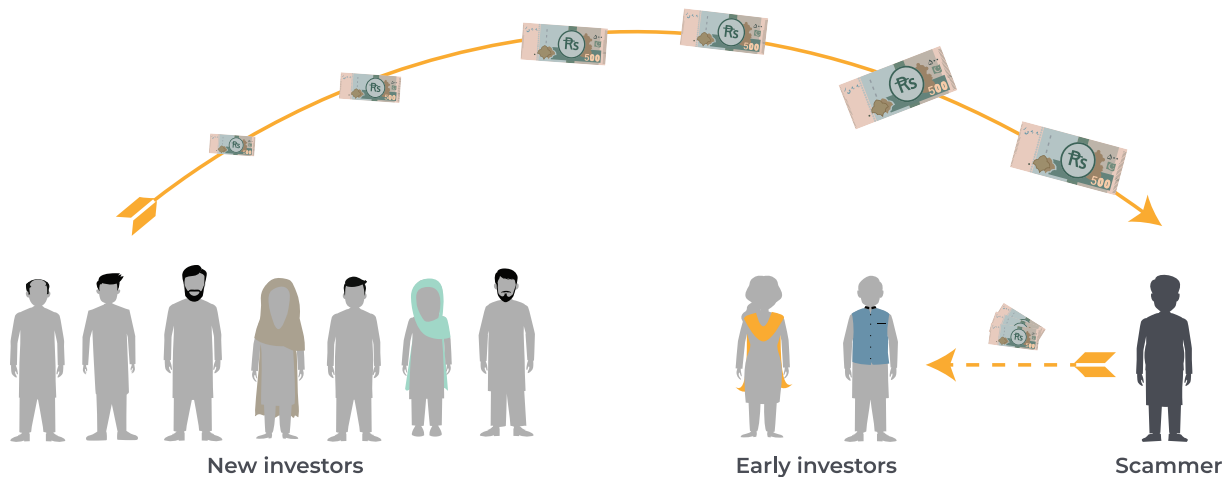
The person is likely a scam artist trying to get important security information. If you give any personal details, they might be able to access your accounts, or be able to make online payments for themselves.



Types of Investment Scams

PONZI SCHEME

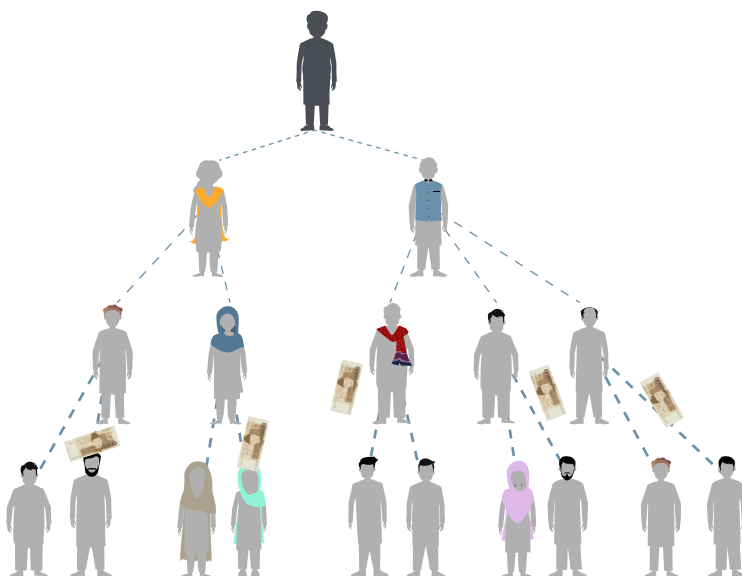
A Ponzi scheme is a specific type of investment scam in which early investors may actually receive high returns initially from the scammer. However, these returns might be paid from the contributions of new investors to give the perception of trustworthiness. Eventually, no new investors will be paid because the scammer will keep all investments for themselves. By the time the scam is discovered, the scammer will have disappeared by going into hiding or by leaving the country.



PYRAMID SCHEME

A pyramid scheme is a scam in which early investors—who are the people at the top of the pyramid—are asked to recruit other investors. These new investors will in turn be expected to recruit even more investors. Each new investor will pay money upwards to existing investors. The money will travel up to the first investors but will eventually dry up at the bottom layer. The whole scheme will finally collapse as

there will not be enough new members to pay everyone at the top.



Pyramid schemes rely primarily on the recruitment of new members to generate profits, rather than on the sale of an actual product or service to consumers. Even if there is a product bought primarily by new investors rather than consumers, the program may still be a pyramid scheme rather than a legal business opportunity.

Types of Identity Theft

Identity theft is when someone steals your personal information, such as your name, address, CNIC, or bank account details, without your permission or by deceiving you. They might tell you they urgently need your details to prevent your money from being seized. They might also say they want to offer you a new type of financial service, like a loan.

The person is likely a scam artist trying to get important security information. It is also phishing: a type of social engineering attack used to steal important user data and information. If you give any personal details, they might be able to access your accounts, or be able to make online payments for themselves.

Let us take a look at the different ways in which identity theft can occur.

FAKING AUTHORITY:

Criminals create fake emails, text messages or websites to trick you into giving your personal information, such as passwords or credit card details. They may also call you and pretend to be a trusted entity like a bank.



HACKING:

Criminals can hack into computer systems to steal personal information or passwords. They can also send links via WhatsApp or text message. If you click on the link, you may allow a virus to be installed on your device and steal or alter your data.

SKIMMING:

A fraudster may install an ATM skimmer that will store your debit card information without your knowledge whenever you use a machine.



STEALING DOCUMENTS:

Criminals may steal your bank statements and other financial mail. They can do so by stealing from the bank, or by going through trash to obtain any personal information that has been thrown away.

Precautions Against Fraud

Everyone can take the following precautions to decrease the chances of becoming a victim of fraud:

- ▶ Treat personal information like a valuable asset, and never provide it at someone's request. Note that sometimes, the scam call or message may even come from an official looking number, known as a Universal Access Number (UAN).
- ▶ If someone uses tactics like fear or the promise of new services to create a sense of urgency, remain composed and careful.
- ▶ Periodically check your accounts and immediately report any unauthorized transactions.
- ▶ Make sure to have different passwords for different apps and websites. Even if one of these passwords is stolen, a person's entire digital identity will not be endangered. Additionally, change your passwords regularly.
- ▶ Use antivirus and anti-malware software on your computer and keep it up to date.
- ▶ Be cautious about financial documents and do not leave them scattered around the house or in the office. If documents have to be thrown away, they should be shredded properly before they are disposed.



Personal Investment Portfolio

Personal investment portfolio

Shereen

Hey Abbu, how was work today?

It was good, but I've been thinking a lot lately. I'm getting closer to retirement and I don't know what to do with my savings.

Safdar

Shereen

Have you considered investing in a portfolio?

Hmm I usually just put my money in committees, or I use it to buy gold, seems safe to me.

Safdar

Shereen

Abbu, you need to think beyond gold and committees. You could consider stocks, bonds and real estate. That way your money will be diversified, and you'll have a better chance of growing your savings.

Sounds like a good idea, why don't you tell me more about it.

Safdar

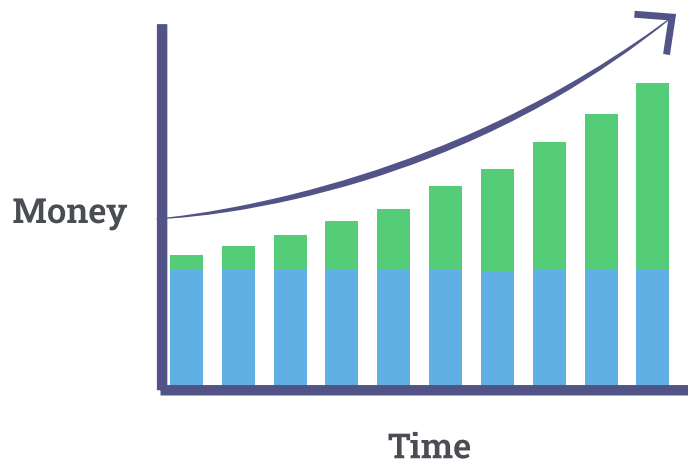
PERSONAL INVESTMENT PORTFOLIO

Types of Assets

When you invest, you place your money in financial assets or securities in the hopes that it will increase in value.

Whether you're just starting out in your career or have been working for a while, investing is a great way of putting your money to work for you.

There are many types of investments, such as stocks, bonds, precious metals, and real estate to name a few. By investing your money, you can benefit from the growth of companies, the stability of government bonds, or the appreciation of precious metals and property.



WHAT IS A PORTFOLIO?

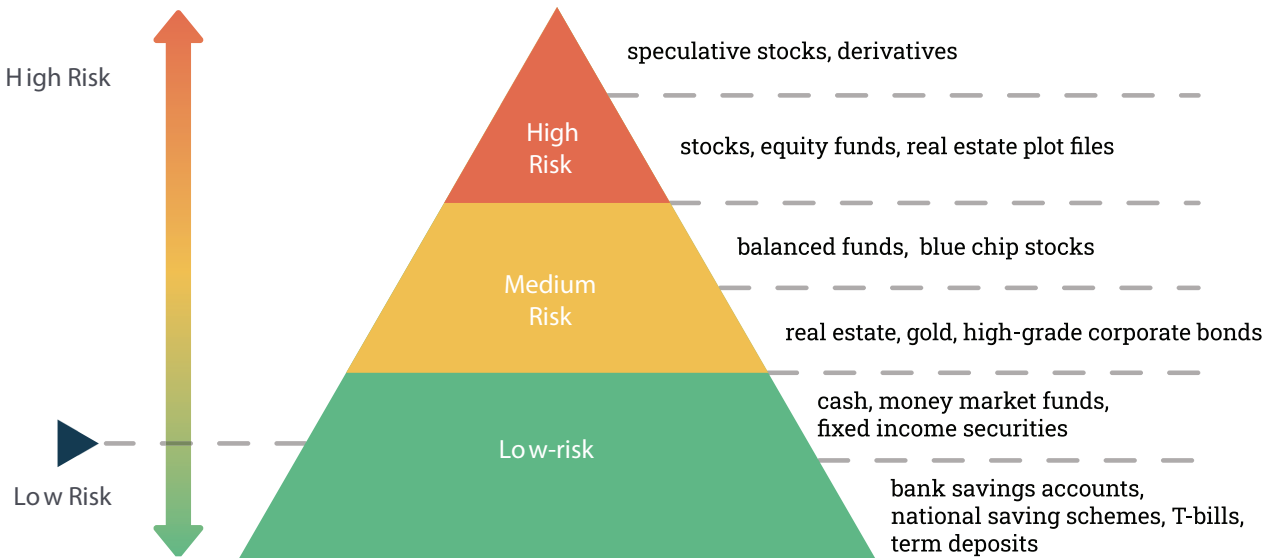
A portfolio is a collection of investments that you own, and it can help you achieve your financial goals. The key to building a successful portfolio is to diversify, which means spreading your money across different types of investments. This helps you reduce risk and potentially earn a higher return.



Risk and Reward

Risk vs reward is a fundamental concept in finance. Taking on more risk usually leads to the potential for higher returns, but it also comes with the possibility of greater losses. The key is to manage that risk by diversifying your portfolio, which simply means not putting all of your eggs in one basket.

One way to think about diversification is through the risk pyramid. At the bottom of the pyramid are low-risk assets like government bonds and cash, which provide stability and security. As you move up the pyramid, you'll find assets with higher potential for growth, but also greater volatility, such as real estate and stocks.



Diversification

By owning a mix of different investments, you can reduce the impact of any one investment that may not perform well. A well-diversified portfolio can help reduce the impact of market volatility on an individual's investments and improve long-term returns.

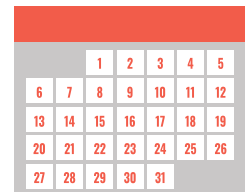
Your portfolio should be tailored to your personal objectives, risk tolerance, and time horizon. For example, if you're young and have a long time horizon, you may be comfortable taking on more



Personal Objectives



Risk Tolerance




Time Horizon


risk in pursuit of higher returns. On the other hand, if you're closer to retirement, you may want to focus on stability and lower risk investments.

Make Your Own Portfolio


A 65-year-old man who is about to retire may have a low risk tolerance. His portfolio consists mainly of national savings certificates or government bonds, fixed deposits, and cash. These types of investments provide a stable and secure source of income, with little potential for growth.




Name: Sa fdar
Age: 65







Low Risk
Tolerance




Goal:
Retirement




Time
horizon



Sta bility



Income

A 25-year-old woman who is just starting her career has a long time horizon. Her portfolio consists mainly of stocks and mutual funds, with a smaller portion in a bank savings account. These types of investments have the potential to deliver higher returns over the long term, but also come with more volatility in the short term.

Managing your portfolio is about more than just buying and selling investments. It's about regularly reviewing your portfolio to make sure it's still aligned with your goals, risk tolerance, and time horizon. It's also about rebalancing your portfolio when necessary to maintain a good balance of risk and reward.

Activity



MATCHING INVESTMENTS WITH RELEVANT PERSONAS

The types of investments given below are either high risk or low risk.

stocks	savings accounts	equity funds	government bonds
fixed income securities	derivatives	cash	speculative stocks

- Place the investments under the correct headings. Which ones are low risk, and which are high risk?

High Risk	Low Risk

- Match three types of investments with the profiles of the investors below.

<p>YASMINE QAMAR</p> <p>Widowed, housewife Age: 58</p>	<p>1. _____</p> <p>2. _____</p> <p>3. _____</p>
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<p>SALAHUDDIN MUSA</p> <p>Entrepreneur Age: 30</p>	<p>1. _____</p> <p>2. _____</p> <p>3. _____</p>
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GLOSSARY

App

Abbreviation of application. Applications are downloadable software, especially for mobile devices. For example, the State Bank of Pakistan has a mobile phone app to check if a bank note is real or fake.

Assets

Any resource that is owned by a person or business that has monetary value of its own. For example, a business may have an asset in the form of a building it owns.

ATM

An Automated Teller Machine or ATM is a machine operated by a bank that allows you to withdraw money.

Assumption

Financial planning involves making reasoned and intelligent estimates (also called projections) about the future. To do so, we use assumptions or intelligent estimates to plan ahead. For example, if we know the cost of a product is Rs. 1,000 today and we want to estimate its cost at the end of 2 years, we may use an assumption that the annual inflation rate is 6%. In this case, we will make a projection that the cost of the product in 2 years will be Rs. 1,123.60 (i.e., $1000 \times 1.06 \times 1.06$).

Balance Sheet

A balance sheet is a financial statement maintained by a business that follows specified financial accounting standards in Pakistan. A balance sheet shows, as of a specified date, the assets, liabilities and equity of the business.

Bank Account

The record which shows how much money a customer has with a bank.

Banking Channels

A bank will reach its customers and provide them with services through many 'banking channels' or pathways. These include branches, kiosks, Automated Teller Machines (ATMs), mobile apps, Internet banking websites, credit and debit cards, retail Point of Sale (POS) systems and customer call centers.

Basket of Commodities

A basket of commodities, or basket of goods, is a collection of consumer products and services which a country uses to track inflation. By tracking the price of everyday items and services like food, clothing and education, a country can keep track of what percentage of their income citizens are spending on these goods over time.

Borrowing

The money or other item of value that you receive for your use and that you plan to give it back to the giver. For example, you could borrow Rs. 5,000 from a bank and return that money to the bank a year later.

Branchless Banking

Traditionally, banks have provided banking services through physical bank branches operated by bank employees. While they continue to do so, they also provide services through branchless banking, i.e., provision of banking services through pathways or 'channels' other than bank branches. Branchless

banking channels include: (1) ATMs; (2) payment cards; (3) mobile phones; and (4) outlets such as post offices and retailers.

Brand

A special name, symbol and promise by which a product or service is offered by a business to its customers. For example, the name “Coca Cola” and its logo and colors are part of a famous international brand. But a brand also represents a promise by a business to its customers. For example, the products sold under the brand name “Coca Cola” taste the same and are made to the same quality standards around the world.

Break Even

Break even means, in relation to a business, the point at which income and expenses equal each other. Often, in the early years of a business, expenses will be more than income. Once there are enough customers and income increases, a well-managed business will get to break even. At this point, income and expenses equal each other. Business owners plan for businesses to get to break even as fast as possible.

Budget

A budget is an estimate of income and expenses over time. In the case of an individual or family budget, the budget will also contain an estimate of savings (income less expenses). In the case of a business budget, the budget will also contain an estimate of profit or loss (income less expenses).

Capital Expenditure

A capital expenditure is money spent by a business to purchase things that can be used over a long period of time. For example, land, buildings and production machinery are types of capital expenditures.

Cash Flow Statement

A cash flow statement is a financial

statement maintained by a business that follows specified financial accounting standards in Pakistan. A cash flow statement shows, for a specified period, the cash coming in and going out of the business.

Channel

A pathway or outlet by which a product or service is offered by a business to its customers. For example, selling a product in a shop you own, selling a product in shops owned by other businesses, selling a product through an agent or selling a product through an e-commerce site are all different channels for the marketing and sale of the product.

Charity

To give money or services to help those in need, without looking for anything in return. For example, it will be an act of charity if you give money for poor earthquake victims to rebuild their homes.

Claim

The process of applying (or the application itself) for compensation, by the insured to the insurer, under the terms of an insurance policy.

Company or Corporation

A company (also called a ‘corporation’) is a legal entity that is used to conduct a business. In Pakistan, companies established in the country are registered with the Securities and Exchange Commission of Pakistan.

Competition

To enter into a contest with others to achieve a goal. For example, in sports, teams contest or compete with each other to win the top positions. In the economy, businesses compete with each other to win customers and increase profits.

Conventional Finance

Conventional finance refers to the system of finance developed in the West and common throughout the

world today. Mark-up based financing is a central part of this system.

Cost of Goods Sold

Cost of goods sold is a category of business expenses which relate to the purchase of goods or raw materials and other direct costs relating to the goods sold. It is often the largest part of the expenses of a business. It is usually not a fixed cost, because, if the business sells less, it will spend less on the purchase of goods or raw materials and other direct costs relating to the goods sold.

Counterfeit

Counterfeit refers to something that is an exact imitation of a valuable original thing, made specifically with the intention to deceive. Counterfeit money is fake currency, printed by criminals to deceive others.

Credit Card

A card issued by a bank that can be used by customers to buy things and make payments. Any money used through a credit card must be repaid by the customer to the bank.

Credit Rating

A credit rating is an evaluation of the credit risk of a potential borrower (an individual, a business or a government), which predicts their ability to pay back the loan. Individuals, businesses and governments with strong credit ratings find it easy to borrow money on good terms. Those with weak credit ratings find it very difficult to borrow money on good terms. These credit ratings are provided by independent credit rating agencies.

Current Account

A bank account offered by banks that allows customers to quickly transfer and withdraw money. Usually, deposits in current accounts do not earn money for the customer.

Debit Card

A card issued by a bank that can be used by customers to buy things and

make payments. Any money used through a debit card comes out of the customer's bank account.

Deflation

Deflation is the rate at which the average price level of a basket of selected goods and services in an economy decreases over a period of time. Often expressed as a percentage, deflation is not necessarily a positive development as it may mean that the economy is slowing down.

Deposit

Money put into a bank by a customer for safe-keeping. Some deposits earn a profit for the customer.

Deposit Multiplier Effect

When you save money in a bank, the bank will lend a portion of that money to other individuals and businesses. The borrowers will use that money to buy goods and services. A portion of the income generated from this new economic activity will go back into banks as savings. The banks will then have additional money to lend out to other individuals and businesses. This will, in turn, generate further economic activity which will result in more money being deposited into banks as savings. And the process will repeat itself. Therefore, each Rupee saved in a bank has a 'deposit multiplier effect' – it leads to additional economic activity.

Digital Content

Digital content, or digital media, is any content product which is available in digital form. This includes music, information, images and videos that are contained as data in computer files and broadcast digitally.

Earnings

The money or other item of value you receive for services, benefits or investments you provide. Earning is a type of income. For example, you may have a job in which your earnings as wages are Rs. 20,000 per month. As

another example, you may invest Rs. 10,000 in a government bond in which you receive earnings as a mark-up or profit of Rs. 1,000 per year.

E-commerce

E-commerce, or electronic commerce, refers to those commercial transactions which are undertaken electronically over the internet. Any business that sells its goods or services over the Internet and receives payments electronically is using e-commerce.

Economy

The system of production, sale and purchase of goods and services and the provision of money and financing in a country.

Enterprise

An enterprise is a business or venture. The three terms 'business', 'enterprise' and 'venture' are often used in place of one another. They involve taking a risk and investing money and effort to gain a reward. While many enterprises seek only profit as the reward, there are also 'social enterprises' that seek both positive social results and financial reward.

Entrepreneur

An entrepreneur is a person who starts and often leads an enterprise, business or venture. This involves taking a risk and investing money and effort to gain a reward. While most entrepreneurs seek only profit as the reward, there are also 'social entrepreneurs' who seek both positive social results and financial reward.

E-payments

E-payments, or electronic payments, refers to any non-cash payment made for an online purchase. Popularized due to the rapid increase in internet shopping and banking, e-payments allow convenience when shopping online.

Equity; Equity Investment

Equity represents the ownership

interest in a business or company. Among other things, equity owners in a business or company have the right to manage and share the profits of the business or company. When we refer to 'equity investment' we mean an investment in the ownership interests in the business or company.

Exchange Rate

The exchange rate is the rate at which local currency is exchanged for foreign currency. If the currency of a country has a favorable exchange rate, it will get more units of the foreign currency.

Expenses

The money you spend. For example, an individual's expenses may include house rent, food and sweets. As another example, a business' expenses may include office rent and salaries of employees.

Finance; Financing

Finance is the system and financing is the process of providing money or 'funds' to individuals, businesses or governments to enable them to buy goods and services. In financing arrangements, the money or funds are usually provided with an understanding that the person providing financing will get the money or funds back, and/or will get a share or profits and/or will get a fixed or variable income.

Financial Economy

The part of the economy that is concerned with the provision, sale and purchase of financial products and services, as opposed to the real economy, which is concerned with actually producing goods and services.

Financial Institution

A business that provides financing and related services. Financial institutions include banks, microfinance banks, development finance banks, leasing companies, stock brokerage firms and currency and money transfer businesses.

Fixed Expense

A fixed expense is an expense that is the same over different periods. For example, if you need to pay rent for your house of Rs. 10,000 every month, then rent is a fixed expense. Individuals, families and businesses can all have fixed expenses.

Fixed Income

An item of fixed income is an item of income that is the same over different periods. For example, if you receive a salary of Rs. 20,000 every month, then you are receiving a fixed income. Individuals, families and businesses can all have items of fixed income.

Foreign Currency

Foreign currency means, for any country, the currency of any other country than its own. For example, for Pakistan, United States Dollars is a foreign currency.

Foreign Exchange

Foreign exchange refers to the exchange of one currency for another currency. For example, when you exchange Pakistani Rupees for United States Dollars you are entering into a foreign exchange transaction.

Funds Transfer

One of the services offered by banks and other financial institutions is the transfer of money or funds on deposit. These transfers may be done nationally or internationally. They may be done between a customer's own accounts and also between one customer and another. With mobile banking, funds transfers have become even easier. Customers may 'buy' funds into a digital account and transfer the funds to another person using their mobile phones.

Generic Product

In business, a generic product is a product sold as a basic, original product with no branding or very little branding. For example, if you sell wheat flour

as 'atta' you are selling it as a generic product. But if you sell wheat flour under a brand name with a quality promise, you are selling it as a branded product.

Gift

The money or other item of value that you receive from a giver who does not want anything back. For example, people give gifts to each other at Eid or other special religious days.

Harvest

The process of gathering fruit or crops when they are ripe or ready to be eaten.

Ijara

This is a type of Islamic financing in which the person providing financing ("lessor") buys a product needed for use by the other person ("lessee"). The lessor leases the product to the lessee at cost plus mark-up. The lessee pays over time and must return the product at the end of the lease. The lessee may also buy the product at the end of the lease.

Income

The money or other item of value you receive. Income may be in the form of: (1) wages from a job; (2) profits from a business; (3) earnings from an investment or bank deposit; (4) gifts from someone; and (5) benefits from the government. For example, you could have a monthly income of Rs. 20,000 from a job.

Income Statement

An income statement is a financial statement maintained by a business that follows specified financial accounting standards in Pakistan. An income statement shows, for a specified period, the income, expenses and profit or loss of the business.

Income Tax

Income tax is a tax imposed by government on the income of individuals or the profits of businesses or companies. This tax is a % of the income of individuals or the profits of

businesses or companies. This tax is required to be reported and paid by the individual or business on whom the tax is imposed.

Inflation

Inflation is the rate at which the average price level of a basket of selected goods and services in an economy increases over a period of time. Often expressed as a percentage, inflation indicates a decrease in the purchasing power of a nation's currency. For example, if in one year gasoline prices are Rs. 100 a litre and the next year they are Rs. 110 a litre, we could say the gasoline prices have inflated (gone up) by 10%.

Information age

Refers to the modern era where advances in the economy are based on Information Technology. Also known as the computer or digital age, the information age is characterized by the rapid advancement, dissemination and availability of information and technology.

Information technology (IT)

IT is the application of scientific knowledge, often in a business context, primarily involving computers, software and network systems. It broadly refers to the use of computer systems for the storing, retrieving and manipulating of data or information.

Installment or Loan Installment

In the case of a loan, an installment represents a part of the loan amount that must be repaid on a specified time. For example, a lender may lend on January 1 Rs. 8,000 and want the loan amount to be repaid in four equal installments at the end of each calendar quarter. In this case, the borrower must repay the money in four installments: (1) Rs. 2,000 on March 31; (2) Rs. 2,000 on June 30; (3) Rs. 2,000 on September 30; and (4) Rs. 2,000 on December 31.

Insurance policy

A contract, representing the purchasing

of insurance, in which one party (insurer) agrees to pay another party (insured) in the event of a loss.

Insured

The party (person or organization) covered by insurance, who makes a claim and to whom compensation is paid in the event of a loss.

Insurer

The party in an insurance contract responsible for paying the compensation amount in the event of a claim.

Intangible Asset

An intangible asset is a business asset that does not have a physical dimension. Intangible assets include intellectual property assets and legal claims and licenses.

Intellectual Property

Intellectual property is an intangible asset that is created by intellectual effort and innovation. Examples include books, movies, software, trademarks and all kinds of designs (for products, buildings, etc.). Intellectual property assets may be protected under different laws including those relating to copyright, patents and trademarks.

Interest

'Mark-up' or interest is a per annum rate applied to a loan that represents the lender's profit or earnings. For example, a lender may lend for one year Rs. 12,000 with a mark-up of 10% per annum. In this case, after one year the borrower will need to (1) repay Rs. 12,000 as the loan amount PLUS (2) pay Rs. 1,200 (10% of 12,000) as the mark-up or interest.

Interest-based financing

Interest-based financing involves provision by a lender of a loan to a borrower in exchange for which the borrower agrees to (1) repay to the lender the principal amount of the loan and (2) pay to the lender a fixed or determined profit, mark-up or interest

on this principal amount. Interest-based financing is permitted under traditional finance but not under Islamic finance.

Invest

To make an investment or put money or something else of value in a business or other project to set it up or help it to grow. For example, if a person puts in Rs. 30,000 to set up a business, we could say: "He invested Rs. 30,000 in the business."

Investment

The money that you use to make more money. For example, an individual may put money into a business as an investment. Buying shares of companies and government bonds are also types of investment.

Islamic Finance

A system of finance based on interpretations of the shariah, the Islamic law. Under Islamic finance, profit on financial investments is permitted if money is used to take risks and promote the real economy. But interest-based financing is not permitted.

Leasing

Leasing means to give someone the right to use a physical property (such as land, a building or a car). Usually, the leasing right is given for a specific purpose and time and a specified fee (called a 'rental fee'). In a leasing arrangement, the person giving the lease is called a 'lessor' and the person receiving the lease is called a 'lessee'. The lessor remains the owner of the physical property.

Liabilities

A liability is a financial debt, loan or obligation owed by a person or company to another party, and is settled through the transfer of money, assets or goods and services.

Licensing

Licensing means to give someone the right to use an intellectual property

(such as software or a movie or book or invention) or other right (such as a government ownership of the radiowave spectrum). Usually, the licensing right is given for a specific purpose and time and a specified fee (called a 'royalty'). In a licensing arrangement, the person giving the license is called a 'licensor' and the person receiving the license is called a 'licensee'. The licensor remains the owner of the intellectual property or right.

Loan

The amount of money that is lent by one person to another. For example, a bank may make a loan to a person so that the person can buy a motorcycle. The amount that is lent is also called the 'principal amount' of the loan.

Loan Amount

The loan amount (also called 'principal') of a loan is the amount of the loan. For example, if a lender lends someone Rs. 12,000, the loan amount or principal is Rs. 12,000.

Loan Period

The period of time over which a loan must be repaid. For example, a lender may lend on January 1 Rs. 8,000 and want the loan amount to be repaid in four equal installments at the end of each calendar quarter. In this case, the loan period is January 1 – December 31 or one year.

Loss

The amount of money you lose in a business. For example, if your business has income of Rs. 5,000 and expenses of Rs. 7,000, you will have a loss of Rs. 2,000. If you gain money in a business, the amount of money you gain is called a 'profit'.

Mark-Up

'Mark-up' is a per annum rate applied to a loan that represents the lender's profit or earnings. For example, a lender may lend for one year Rs. 12,000 with a

mark-up of 10% per annum. In this case, after one year the borrower will need to (1) repay Rs. 12,000 as the loan amount PLUS (2) pay Rs. 1,200 (10% of 12,000) as the mark-up.

Mobile Banking

This is a service offered by banks that allows customers to use their mobile phones to use banking services such as transferring money.

Mudarabah

This is a type of Islamic financing partnership in which one person provides money and the other person provides expertise and management. At the beginning, the partners agree on the profit-share percentage. If there is a loss, the partner providing expertise and work does not have to pay the partner providing the money.

Murabaha

This is a type of Islamic financing in which the person providing financing buys a product that the other person needs. The person providing the financing then sells the product to the other person at cost plus mark-up. The other person pays over time.

Musharakah

This is a type of Islamic financing partnership in which people provide money and/or expertise and management. They can agree however they want to divide the profits and management of the business. If there is a loss, the partners share in it according to the proportion of the money they put into the business.

Necessary Expenses

Expenses that are necessary or important and that cover things you need. For example, an individual's necessary expenses may include expenses relating to food and rent.

Operating Expense

An operating expense is money spent by a business to operate on a regular basis. For example, a fruit shop will have

operating expenses in the form of rent, fruit purchases and salaries.

Pocket money

It is a small amount of money regularly given to children, by their parents, to spend or save for their wants. This is also known as an 'allowance' and given on a weekly or monthly basis.

Premium

The small monthly or annual fee paid by the insured party to the insurer, in return for a promise of compensation in the event of a loss.

Principal

In the case of a loan, the loan amount (also called 'principal') of a loan is the amount of the loan. For example, if a lender lends someone Rs. 12,000, the loan amount or principal is Rs. 12,000.

Private Limited Company

A private limited company is a company whose transfer and listing of shares is restricted by law. Shares of such companies may not be listed on the Pakistan Stock Exchange.

Profit

The amount of money you gain in a business. For example, if your business has income of Rs. 5,000 and expenses of Rs. 4,000, you will have a profit of Rs. 1,000. If you lose money in a business, the amount of money you lose is called a 'Loss'.

Profit Margin

The profit margin of a business is calculated by expressing as a percentage its profit divided by its income (profit / income as %). Profit margin calculations tell you, that for every rupee a business makes, what percentage is profit. For example, if a business has income of Rs. 10,000 and expenses of Rs. 8,000, it will have a profit of Rs. 2,000 (10,000 – 8,000) and a profit margin of 20% (2,000 / 10,000 as %). Profit margin is a basic but very useful ratio used for comparing the profitability of businesses.

Profit share

It is the dividing of profits made by a business or company based on pre-determined percentages between investors. This investment can either be financial or work in terms of time and/or effort.

Projection

Financial planning involves making reasoned and intelligent estimates (also called projections) about the future. To do so, we use assumptions or intelligent estimates to plan ahead. For example, if we know the cost of a product is Rs. 1,000 today and we want to estimate its cost in 3 years, we may use an assumption that the annual inflation rate is 6%. In this case, we will make a projection that the cost of the product in 3 years will be Rs. 1,123.60 (i.e., $1000 \times 1.06 \times 1.06$).

Public Limited Company

A public limited company is a company whose shares may be listed on the Pakistan Stock Exchange. In order for listing to happen, a public limited company needs to satisfy detailed legal requirements.

Real Economy

The part of the economy that is concerned with actually producing goods and services, as opposed to the financial economy, which is concerned with the provision, sale and purchase of financial products and services.

Retailers

A person or business that sells goods. As opposed to a supplier or wholesaler, a retailer normally sells directly to the consumer. For example, a grocery store can be referred to as a retailer of goods.

Reward

Something you get for your effort, achievement or investment. In finance, calculation of reward is typically balanced by calculation of risk. You should not take a financial risk unless there is a greater financial reward. For

example, if you invest money in shares on the stock market you take the risk that the price of the shares will go down. You should take this risk only if you can estimate that you could also get a high reward if the price of the shares will go up.

Risk

The chance or danger that something bad may happen or a loss may occur. In finance, risk is often used to refer to the chance that there may be a financial loss. For example, if you invest money in shares on the stock market you take the risk that the price of the shares will go down. In finance, calculation of risk is typically balanced by calculation of reward. You should not take a financial risk unless there is a greater financial reward.

Risk Management

A business faces many risks, including legal, financial, operational, reputational and competitive risks. Risk management refers to the discipline of managing these risks in a planned way, including through financial planning, complying with laws and contracts and insurance.

Sales Tax

Sales tax is a tax imposed by government on the sales of certain goods and services. This tax is required to be collected by the seller from the buyer at the point of purchase and passed on to the government.

Savings

The money or other item of value that you own and keep for use at a later time. For example, if in one month you have income of Rs. 1,000 and you have expenses of Rs. 800, you will have a saving of Rs. 200. You could save money at home or in a bank.

Savings Account

A bank account offered by banks that allows customers to save money and earn a profit on the saving.

Savings Plan

The plan to save some money. A savings plan has a goal (i.e., how much money you want to save over a period of time). The goal may be met over a period of time. For example, if your goal is to save Rs. 3,000 and you save Rs. 1,000 every month, you will meet your goal in three months.

Shares

Shares represent a unit of equity ownership in a business or company. For example, a company may issue 100 shares, each of which represents 1% of the equity ownership in the company.

Shariah

'Shariah' literally means a way or path. In Islam, Shariah refers to the divine guidance and laws given by the Holy Quran and the Hadith (sayings) of the Prophet Muhammad (peace be upon him), as supplemented by juristic interpretations by Islamic scholars. Shariah embodies all aspects of the Islamic faith, including beliefs and practices. Islamic Shariah or the divine law of Islam is derived from the following four sources: (1) the Holy Quran; (2) the Sunnah of the Holy Prophet (Peace Be Upon Him); (3) Ijma' (consensus of the Ummah); and (4) Qiyas (reasoning by analogy).

Takaful

This is a type of Islamic insurance in which people or businesses seeking insurance put together or 'pool' their insurance payments or 'premiums' and make the pooled funds available for losses suffered by the people or businesses in the pool.

Tangible Asset

A tangible asset is a business asset that has a physical dimension, such as land, buildings, machinery, inventory and cash.

Tax

A tax is a charge imposed by a government on individuals and

businesses. The money collected through taxes is used to fund government expenses such as defence, development, education and health.

Terms

The details at which a seller will sell you something. For example, a seller may sell you a schoolbag for Rs. 500. She may say she can only give it to you one week later. She may also say she will give you the money back if there is something wrong with it. The timing of the sale of the bag and the promise to give back the money are the 'terms' of the sale.

Trade-Off

A trade-off is an exchange of one thing for another. For example, if you have one egg and you eat it today for breakfast, then you will not have it available to eat tomorrow. You have traded off your opportunity to eat the egg tomorrow for your desire to eat the egg today.

A trade-off decision is a decision you make in relation to a trade-off situation. For example, when you decide to eat the egg today, you are making a trade-off decision.

Unnecessary Expenses

Expenses that are unnecessary or unimportant. These expenses usually are for things you 'want' but may not 'need'. For example, an individual's unnecessary expenses may include expenses relating to sweets and toys.

Variable Expense

A variable expense is an expense that changes over different periods. For example, if you have food expenses of Rs. 8,000 in one month, Rs. 7,000 in the second month, and Rs. 7,300 in the third month, then food is a variable expense. Individuals, families and businesses can all have variable expenses.

Variable Income

Variable income is an item of income that changes over different periods. For example, if you have profit from a business of Rs. 50,000 in one month, Rs. 70,000 in the second month, and Rs. 70,300 in the third month, then profit is an item of variable income. Individuals, families and businesses can all have items of variable income.

Wages

An amount of money an employee is paid based on the number of hours or days they have worked.

Wholesaler

A person or business that acts a middleman by buying large amounts of goods from suppliers, storing them and reselling in large quantities to retailers.

Withdrawal

Money taken out by a customer from a bank. Any money withdrawn by a customer comes out of the customer's bank account.



SOLUTIONS

Personal income, expenses and savings

CLASSIFYING THE FAMILY'S INCOME AND EXPENSES (QUESTION ON PAGE 13)

1.	Rabia receives a monthly salary as a school teacher	Fixed income
2.	Safdar fills gasoline in his vehicle 2-3 times a month	Variable expense
3.	Daniyal has the same university fee payable every quarter	Fixed expense
4.	Nusrat receives a pension from the government every month	Fixed income
5.	Shereen likes to buy adventure novels from time to time	Variable expense
6.	Safdar's income comes from the profit from his fruit and juice business	Variable income

THINKING ABOUT INFLATION (QUESTION ON PAGE 18)

Inflation relates to increases in prices. Separate out the true and false statements below

		True	False
1.	Rabia has a fixed salary of Rs. 25,000 per month. If there is inflation, she will be able to buy more things with that salary.	<input type="checkbox"/>	<input checked="" type="checkbox"/>
2.	Shereen can buy a book for Rs. 200 today. If there is inflation, the same book will cost more in the future.	<input checked="" type="checkbox"/>	<input type="checkbox"/>
3.	Shereen wants to save money to buy a book in 1 year. The book costs Rs. 200 today. If there is 10% inflation of the price of the book every year, she will need to save Rs. 220.	<input checked="" type="checkbox"/>	<input type="checkbox"/>
4.	Safdar increases his fruit sales prices at the rate of inflation every year. This means the income from his shop will go down every year.	<input type="checkbox"/>	<input checked="" type="checkbox"/>
5.	Inflation usually has more of a negative impact on people who earn a fixed income (e.g., salaries) than people who have a variable income (e.g., profit from a business).	<input checked="" type="checkbox"/>	<input type="checkbox"/>

EVALUATING THE IMPACT OF INFLATION (QUESTION ON PAGE 19)

Respond to the questions below in relation to the following scenarios.

1.	Rabia receives a monthly salary as a school teacher
2.	Safdar fills gasoline in his vehicle 2-3 times a month
3.	Daniyal has the same university fee payable every quarter
4.	Nusrat receives a pension from the government every month
5.	Shereen likes to buy adventure novels from time to time
6.	Safdar's income comes from the profit from his fruit and juice business

From the point of view of the family's income, which income item listed above is most likely to go up if there is inflation? Why?

Safdar's income from his fruit and juice business. It will be negatively impacted by inflation because his expenses will go up. But IF he is able to pass on the increase in expenses to his customers in the form of higher prices, his income will go up. Note that it is not always easy for a business to pass on increases in expenses to customers in the form of higher prices.

From the point of view of the family's expenses, which expense item listed above will not be negatively affected by inflation? Why?

Daniyal's university fees because he pays the same amount every quarter. His parents will not need to pay more, even though inflation will decrease the value or buying power of the rupee.

From the point of view of the family's income, which TWO income items listed above are most likely to be negatively affected by inflation? Why?

Rabia's salary and Nusrat's pension, because these are types of fixed income. The income does not increase even though inflation decreases the value or buying power of the rupee. People with fixed income suffer as inflation rises.

CALCULATING ANNUAL SAVINGS (QUESTION ON PAGE 27)

To pay for Daniyal's remaining university expenses and build the house, the family have projected they need Rs. 3,545,601 over a 5-year period. To be safe, they set their savings goal at Rs. 3,600,000.

Calculate the EQUAL annual savings they will need to make to save Rs. 3,600,000 in 5 years.

University and House Building Expenses (Rs.)							
Expense	Present	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Assumptions							
1.	Present university expenses	300,000					
2.	Present house building expense	2,000,000					
3.	Assumed inflation rate	5%	5%	5%	5%	5%	
Projections							
4.	Daniyal university E\ expenses		315,000	330,750	347,288	-	993,038
5.	House building expense		-	-	-	2,552,563	2,552,563
6.	Total		315,000	330,750	347,288	-	3,545,601
7.	Annual savings		720,000	720,000	720,000	720,000	3,600,000

To save Rs. 3,600,000 in 5 years at an EQUAL annual rate, the family will need to save Rs. 720,000 per year ($3,600,000 / 5$).

CALCULATING WITHDRAWALS AND NET SAVINGS (QUESTION ON PAGE 28)

University and House Building Expenses (Rs.)								
	Expense	Present	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Assumptions								
1.	Present University Expenses	300,000						
2.	Present House Building Expense	2,000,000						
3.	Assumed Inflation Rate	5%	5%	5%	5%	5%	5%	
Projections								
4.	Daniyal University Expenses		315,000	330,750	347,288	-	-	993,038
5.	House Building Expense		-	-	-	-	2,552,563	2,552,563
6.	Total		315,000	330,750	347,288	-	2,552,563	3,545,601
7.	Annual Savings		720,000	720,000	720,000	720,000	720,000	3,600,000
8.	Withdrawals		315,000	330,750	347,288	-	2,552,563	3,545,601
9.	Total Net Savings		405,000	794,250	1,166,963	1,886,963	54,399	54,399

In Years 1, 2 and 3, the family will withdraw the money needed for university expenses for Daniyal.

In Year 5, they will withdraw the money needed to build their house.

In each year, the total net savings will be (1) the new savings for that year plus all savings for prior years (2) less all withdrawals in that year and all prior years.

By the end, the family will have a saving of Rs. 54,399, which is the amount they added to the savings goal to make it Rs. 3,600,000.

SAVING AT HOME VS. BANK (FOR QUESTION SEE PAGE 29)

Help the family decide in which ways saving at home or in a bank is better.

		At home	In a bank
1.	Safer		<input checked="" type="checkbox"/>
2.	Makes money		<input checked="" type="checkbox"/>
3.	Easy to transfer money to another city		<input checked="" type="checkbox"/>
4.	Easy to get to money	<input checked="" type="checkbox"/> *	

Based on these factors which place is better for the family to save their money?

	<input checked="" type="checkbox"/>
--	-------------------------------------

* However, with e-payments, it is getting easier to access money as virtual currency.

ANALYZING PERSONAL AND FAMILY BUDGETS (QUESTION ON PAGE 32)

After setting a savings goal of Rs. 3,600,000 over 5 years, Shereen and her family prepare a budget.

Can you help Shereen analyze the budget?

Safdar & Rabia's Family Budget (Rs.)							
		Year 1	Year 2	Year 3	Year 4	Year 5	Total
Income							
1.	Safdar's income from fruit business	800,000	900,000	1,000,000	1,100,000	1,200,000	5,000,000
2.	Rabia's income from teaching	300,000	330,000	360,000	390,000	420,000	1,800,000
3.	Profit from savings in the bank	40,200	78,492	114,762	186,762	6,266	426,481
4.	Total income	1,140,200	1,308,492	1,474,762	1,676,762	1,626,266	7,226,481
Expenses							
5.	Rent	180,000	200,000	230,000	265,000	300,000	1,175,000
6.	Food & household items	150,000	165,000	185,000	210,000	240,000	950,000
7.	Electricity, water & mobile bills	120,000	130,000	145,000	160,000	175,000	730,000
8.	Transport	85,000	92,000	100,000	110,000	120,000	507,000
9.	Health	12,000	18,000	24,000	30,000	38,000	122,000
10.	Clothes, entertainment, gifts, etc	180,000	200,000	230,000	265,000	300,000	1,175,000
11.	Total expenses	727,000	805,000	914,000	1,040,000	1,173,000	4,659,000
Savings							
12.	Savings	413,200	503,492	560,762	636,762	453,266	2,567,481

Will the family meet their 5-year savings target of Rs. 3,600,000? If not, by how much will they be short?

No. They will be short by Rs. 1,032,519 (3,600,000 – 2,567,481).

If they need to increase income to meet their budget, which item of income will be easiest to increase?

It will be easiest to increase Safdar's income from the fruit business as this is profit and the business could be grown. Rabia's income is salary from teaching, and this cannot be easily increased. The profits from savings is a small amount and cannot be easily increased except through more savings.

If they need to decrease expenses to meet their budget, which item of expenses will be easiest to decrease?

It will be easiest to decrease "clothes, entertainment, gifts, etc." as these items seem to be less necessary than expenses for rent, food and household items, electricity (etc.), transport and health.

DEALING WITH UNNECESSARY EXPENSES (QUESTION ON PAGE 35)

Which expenses will you cut? Which are the least necessary expenses?

There is no one right answer to this question, but some of the expenses in "Clothes, entertainment, gifts, etc." are more unnecessary. For example:

Some savings could be had from sweets, toys and bangles earrings, etc.

Savings could also be had from clothes, especially if clothes can be stitched at home.

Perhaps travel expenses could be cut a little bit.

Some people believe that cigarettes are a completely unnecessary expense, but smokers believe they are a completely necessary expense!

Is charity (money to deserving people) necessary or unnecessary? Charity is an important expense!

How about pocket money? What would a child feel?

Often, it is useful for family members to share cuts in expenses!

ANALYZING EXPENSES: INCOME-MAKING AND NON-INCOME MAKING (QUESTION ON PAGE 39)

Choose whether or not the following expenses will allow Shereen's family to earn money.

		Earns money	Does not earn money
1.	Shereen buys some books on financial planning to help her father plan his fruit expansion.	<input checked="" type="checkbox"/>	
2.	Shereen spends money to print a poster that invites students to take tuitions from her.	<input checked="" type="checkbox"/>	
3.	Ali spends money to put fertilizer on a fruit tree from which he will sell the fruit.	<input checked="" type="checkbox"/>	
4.	Ali spends money to put fertilizer on a fruit tree from which he will eat the fruit.		<input checked="" type="checkbox"/>
5.	Nusrat buys a sewing machine to make clothes to sell.	<input checked="" type="checkbox"/>	
6.	Nusrat buys a sewing machine to make clothes for Ali and herself.		<input checked="" type="checkbox"/>

Notes:

When Shereen buys books on financial planning, she does not make any money from this in the short-term. But, in the long-term, the money she and her family spend on education and learning is likely to have a financial reward!

The same activity can help you either make money or not. For example, when Ali buys fertilizer for a tree and Nusrat buys a sewing machine, in one case they make money and in the other case they do not. This depends on their plans and future actions.

When Nusrat buys a sewing machine to make clothes for Ali and herself, she does not make money. But in doing so, she may cut her expenses and have extra **savings** as she will not need to buy ready-made clothes or pay a tailor.

Business income, expenses, profit and loss

ARE YOU AN INVESTOR, MANAGER OR ENTREPRENEUR?

(QUESTION ON PAGE 45)

For each ROW of three statements (Row 1 (yellow), Row B (white) and Row C (blue)), select the statement you agree with most (3 points), agree with second most (2 points) and agree with least (1 point). Then total the points for each of the COLUMNS A, B and C.

State- ment Row		Points Column A		Points Column B		Points Column C
Row 1	I like starting new projects and coming up with new ideas.		I like to work in large and well-known institutions.		I like to profit from putting money in property, currencies and shares.	
Row 2	I like being my own boss and doing lots of different types of work.		I like to work in well-ordered teams with each team member having clear responsibilities.		I like to balance doing daily work and keeping time to benefit from changes in the market.	
Row 3	I am willing to put money in a business if there is a great reward and I can work in the business to make sure I get that reward.		A good, regular salary is very important for me.		I am willing to put money in 2-3 businesses from which I can get my money back easily.	
Total						

What was your total score for (1) Column A, (2) Column B and (3) Column C?

If your highest total score is in Column A, **you think like an entrepreneur**. Many entrepreneurs like starting new things, coming up with new ideas, being their own boss and working on many different things. They prefer to put money in businesses in which they are involved.

If your highest total score is in Column B, **you think like a manager**. Many managers like working in large institutions, obtaining a good, regular salary and working in teams in which people have well-defined responsibilities.

If your highest total score is in Column C, **you think like an investor**. Many investors focus on market values and finding profitable opportunities. They recognize that they can make money not only through work but by making sure their savings and investments make money.

ANALYZING PROFIT MARGIN (FOR QUESTION, SEE PAGE 50)

In connection with making their family budget, Safdar and Shereen have made 5-year financial **projections** or estimates of the fruit and juice business.

Calculate their profit margin in each of Years 1-5.

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total Income	10,875,000	12,547,500	14,346,400	16,800,000	19,500,000
Expenses						
2.	Total Expenses	10,075,000	11,647,500	13,346,400	15,700,000	18,300,000
Profit (Loss)						
3.	Profit	800,000	900,000	1,000,000	1,100,000	1,200,000
4.	Profit Margin	7.36%	7.17%	6.97%	6.55%	6.15%

ANALYZING INCOME, EXPENSES AND PROFIT (QUESTION ON PAGE 53)

In Year 1, which business has greater income per kg of fruit sold, the sale of fruit or the sale of juice? Why?

In Year 1, the sale of juice has greater income per kg of fruit sold. The sales price per kg of fruit sold as fruit is Rs. 250. The sales price per kg of fruit sold as juice is Rs. 400.

In Year 3, what is the total fruit expense expressed as a percentage of total income?

70.5% ($10,120,000 / 14,346,400 \times 100$).

This category of expenses, which relates to the purchase of goods or raw materials and other direct costs (relating to the goods sold), is called **Cost of Goods Sold**. It is often the largest part of the expenses of a business. It is usually not a fixed cost, because, if the business sells less, it will spend less on the purchase of goods or raw materials and other direct costs relating to the goods sold.

In Year 5, what is the total kg of fruit purchased and the total kg of fruit sold? What might be the reasons for the difference in these numbers?

The total kg of fruit purchased is 55,000 kg. The total kg of fruit sold is 52,000 kg. The reasons for the difference in these numbers may include: (1) some fruit may have not been sold but could be sold in the future; and (2) some fruit may have rotted, been lost or otherwise wasted. Good businesses work hard to reduce the gap between what they purchase and what they sell.

BUSINESS EXPANSION ANALYSIS (QUESTION ON PAGE 56)

If Safdar expands the bottled juice business, which expenses will go up and which will go down?

	Go Up	Go Down
1. Overall fruit expense	<input checked="" type="checkbox"/>	<input type="checkbox"/>
2. Fruit expenses per bottle of juice sold	<input type="checkbox"/>	<input checked="" type="checkbox"/>
3. Overall bottling expense	<input checked="" type="checkbox"/>	<input type="checkbox"/>
4. Bottling expenses per bottle of juice sold	<input type="checkbox"/>	<input checked="" type="checkbox"/>
5. Overall marketing expense	<input checked="" type="checkbox"/>	<input type="checkbox"/>
6. Overall transport expense	<input checked="" type="checkbox"/>	<input type="checkbox"/>
7. Equipment expense	<input checked="" type="checkbox"/>	<input type="checkbox"/>

What is the most important difference between the type of expenses that will go up and the type of expenses that will go down?

The **overall expense** of fruit, bottling, marketing, transport and equipment will go up. But the **per unit expense** of fruit and bottling will go down. Typically, when a business expands, overall expenses go up. But if the expansion is well planned, per unit expenses will go down.

If Safdar wants to profitably expand the business what will need to happen to either number of items sold or price of items sold?

If Safdar wants to profitably expand the business, he will have extra expenses. To cover these expenses, he will need to increase the number of items sold or the price of items sold or both.

IDENTIFYING SMART BUYING PRACTICES (QUESTION ON PAGE 62)

As smart buyers, Safdar and Shereen check with three sellers. The sellers have different points to make.

Can you tell what each statement or question is about?

		Quality	Quantity	Price	Terms
1.	"We will deliver in 1 week"				<input checked="" type="checkbox"/>
2.	"I will sell this equipment to you for my cost plus 20%"			<input checked="" type="checkbox"/>	
3.	"If the equipment does not work we will fix it for free"				<input checked="" type="checkbox"/>
4.	"We will give you the best performing equipment"	<input checked="" type="checkbox"/>			
5.	"Will you pay 50% on signing?"				<input checked="" type="checkbox"/>
6.	"I will supply you with 2 freezers"		<input checked="" type="checkbox"/>		
7.	"We will install the equipment for you"				<input checked="" type="checkbox"/>

SELECTING THE RIGHT SELLER AND EQUIPMENT (QUESTION ON PAGE 64)

Help Safdar and Shereen select the right seller and equipment.

Seller	Price (Rs.)	Quality	Terms
A	3,500,000	Highest	4-year guarantee free delivery only
B	4,000,000	Very high	5-year guarantee free delivery and installation
C	2,500,000	Low	3-year guarantee free delivery and installation

NOTE: Safdar and Shereen know that the staff of Seller A have made a mistake in pricing but probably will not find that out! Safdar and Shereen know that the correct price should be Rs. 4,500,000 not Rs. 3,500,000.

Which seller and equipment should they select? Should they select seller A and buy the equipment for Rs. 3,500,000? What is your reasoning?

This is a matter of judgment. We believe that the best choice is Seller B and its equipment.

Safdar and Shereen should not buy Seller A's equipment at the price of Rs. 3,500,000

even if Seller A will never find out about the mistake. This is unethical.

If Seller A's price is corrected to Rs. 4,500,000, the price is high. In addition, the guarantee is for only 4 years and there will be installation costs.

Seller C's price is the lowest, but the quality of the equipment is low and the guarantee is for only 3 years.

We believe Seller B's price is a median price, and the quality is very high. In addition, Seller B will provide a 5-year guarantee and deliver and install the equipment.

RISK MANAGEMENT ANALYSIS (QUESTION ON PAGE 70)

Test your understanding of risk management. For each business situation, select the type of risk most clearly involved.

1. Your manufacturing equipment burns down. What kind of risk does this situation represent?

Reputational Risk **Operational Risk** **Competitive Risk** **Legal Risk**

This is an operational risk, as it impacts your production and operations. This risk can be managed through insurance.

2. A Facebook campaign spreads to your customers that you are selling out-of-date products.

Reputational Risk **Operational Risk** **Competitive Risk** **Legal Risk**

This is a reputational risk as your reputation for selling quality products is being attacked in social media. It often takes a lot of changes in product quality and media campaigns to manage this kind of risk.

3. A foreign company sells products such as yours at low prices and with many varieties.

Reputational Risk **Operational Risk** **Competitive Risk** **Legal Risk**

This is a competitive risk. A foreign competitor is competing with you both on price and variety. Managing this risk often requires developing new, better or cheaper products.

4. The government passes a law requiring your business to obtain costly new licenses.

Reputational Risk **Operational Risk** **Competitive Risk** **Legal Risk**

This is a legal risk. A law has resulted in an increase in your cost of doing business. It is a good idea to obtain the new licenses otherwise the risk could be greater if you operate without them.

5. The Pakistani Rupee goes down in value compared to the US Dollar, and the

price of importing an essential raw material goes up.

Reputational Risk **Financial Risk** **Competitive Risk** **Legal Risk**

This is a financial risk. It can be managed by long-term purchase contracts and/or keeping enough foreign currency in your bank account.

6. Your main supplier of packaging materials goes out of business.

Reputational Risk **Operational Risk** **Competitive Risk** **Legal Risk**

This is an operational risk, as it involves your production and operations. This risk can be managed by using more than one supplier.

PROPERTY INSURANCE FOR THE BOTTLING EQUIPMENT (QUESTION ON PAGE 72)

Safdar and Shereen are planning to buy bottling equipment for Rs. 4,000,000. As smart buyers, they check out the price of property insurance for the equipment from 3 insurance companies. The insurers offer different premiums and coverage amount (maximum amount that will be paid out).

	Insurer	Annual Premium (Rs.)	Coverage (Rs.)
1.	A	120,000	4,000,000
2.	B	45,000	3,000,000
3.	C	76,000	3,800,000

Which insurance policy has the best combination of premium and coverage? Why?

Insurer C offers the best combination of premium and coverage. If we express premium as a percentage of coverage we get:

Insurance Policy Analysis (Rs.)			
Seller	Premium	Coverage	Premium %
A	120,000	4,000,000	3.0%
B	45,000	3,000,000	1.5%
C	76,000	3,800,000	2.0%

Because the business will have to pay the premium, the lowest percentage of premium to coverage amount is cheapest.

In this case, insurer B has the lowest premium (1.5% of coverage amount). But the coverage amount is quite low. If there is a full loss of the equipment, the business will

have to bear Rs. 1,000,000 of the loss (full value Rs. 4,000,000 – coverage amount Rs. 3,000,000).

The coverage amount offered by insurer A is the full value of the equipment (Rs. 4,000,000) but the premium (3% of coverage amount) is high.

The coverage amount offered by insurer C is close to the full value of the equipment (Rs. 3,800,000) and the premium is lower (2% of coverage amount).

TAX ANALYSIS (QUESTION ON PAGE 75)

Test your understanding of basic taxes by answering the questions below.

Which tax does a business collect directly from customers and pay over to the government?

Income Tax

Sales Tax

Sales tax is collected by a business directly from customers and paid over to the government. Income tax is paid by a business on its profits.

A furniture business sells a table for Rs. 10,000. It collects Rs. 11,700 from the customer for the price of the table plus tax payable by the customer. What kind of tax is this?

Income Tax

Sales Tax

The extra Rs. 1,170 is a sales tax. It is required to be collected by the seller from the buyer on the sale of most kinds of products and paid over to the government.

A business makes a profit of Rs. 400,000 and it pays the government a tax on this profit of Rs. 29,000. What kind of tax is this?

Income Tax

Sales Tax

Income tax is a tax that an individual pays on income and a business pays on profit. The Rs. 29,000 is paid by the business on its profit of Rs. 100,000 and is an income tax.

A business is subject to 15% sales tax and 30% income tax. Calculate how much sales tax and income, the business will need to pay.

	Category	Amount (Rs.)	Sales Tax (Collected from Customers) (Rs.)	Income Tax (Rs.)
1.	Income from Product Sales	500,000	75,000	
2.	Business Expenses	300,000		
3.	Profit	200,000		60,000

Banking and Bank Finance

KNOWING THE STATE BANK (QUESTION ON PAGE 84)

Figure out how much you know by answering these 5 true or false questions.

	<div style="background-color: #4CAF50; color: white; border-radius: 15px; padding: 5px; display: inline-block;">true</div>	<div style="background-color: #F44336; color: white; border-radius: 15px; padding: 5px; display: inline-block;">false</div>		
1.	The State Bank issues Pakistan's currency (rupees)	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The State Bank issues Pakistan's currency and controls the amount of currency in circulation.
2.	The State Bank loans money to businesses and individuals	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The State Bank does not loan money to businesses and individuals. It regulates banks and other financial institutions which loan money.
3.	The State Bank manages Pakistan's foreign currency reserves	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The State Bank manages and invests Pakistan's foreign currency reserves.
4.	The State Bank sets electricity and gas prices in Pakistan	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The State Bank is not responsible for setting electricity and gas prices in Pakistan.
5.	The State Bank owns all the banks in Pakistan	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The State Bank does not own the banks in Pakistan. It regulates banks and other financial institutions in the country.
6.	The State Bank regulates all the banks in Pakistan	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The State Bank regulates and supervises banks and other financial firms to make sure that they are managed soundly.

ISLAMIC FINANCE: KNOWING THE DIFFERENCE (QUESTION ON PAGE 91)

Test your knowledge of Islamic finance. Separate the true and false statements below.

	True	False
1. Islamic finance prohibits profit-and-loss sharing while conventional finance prohibits interest-based financing.		<input checked="" type="checkbox"/>
2. Islamic finance has, as one of its main purposes, the creation of a just and ethical society.	<input checked="" type="checkbox"/>	
3. Islamic finance views finance as a means to serve the real economy.	<input checked="" type="checkbox"/>	
4. Both Islamic finance and conventional finance prohibit people from investing money for illegal purposes.	<input checked="" type="checkbox"/>	
5. If you want to buy equipment to use for a limited period and you want to use Islamic financing, you should use ijara financing.	<input checked="" type="checkbox"/>	
6. Islamic finance is not flexible towards how investors and business owners share profits.		<input checked="" type="checkbox"/>

Both Islamic finance and conventional finance allow profit-and-loss sharing. Conventional finance also allows interest-based loan financing, while Islamic finance prohibits interest-based loan financing.

The purposes of Islamic finance are to encourage individuals and businesses to act in accordance with the shariah and to promote (1) social solidarity, (2) justice, (3) social welfare, (4) fair and ethical dealings and (5) development of the economy and enterprise.

Islamic finance is principally focused on the real economy and the actual production of goods and services. Under Islamic finance principles, the finance economy should serve the real economy.

Under conventional financing, the money being advanced may be used for many purposes other than illegal purposes. Money from Islamic financing may not be used for illegal purposes or for non-Shariah compliant activities, including gambling and dealing in alcohol.

Ijara is a type of financing in which the person providing financing buys a product that the other person needs. The person providing the financing then leases the product to the other person at cost plus mark-up. The other person pays over time and must return the product at the end of the lease.

Islamic finance is generally quite flexible towards how investors and business owners share profits. It is much less flexible on sharing of losses. The reason for this is that it tries to protect individuals and business owners from having to bear an unfair share of the losses.

WHAT IS THE TYPE OF ISLAMIC FINANCE? (FOR QUESTION, SEE PAGE 102)

Identify the type of Islamic finance that applies to each of these 5 situations.

1.	Safdar invests money in a business but is not involved in the business. Ali agrees to manage the business but does not invest money. They agree to a profit share.	Mudarabah	Musharakah
EXPLANATION: Mudarabah is a form of Islamic finance partnership in which one person provides money and the other person provides expertise and management. At the beginning of the partnership, the partners agree on the profit-share percentage.			
2.	Safdar, Ali and Shereen all invest money in a business. They also all agree to manage the business. They agree to a profit share.	Mudarabah	Musharakah
EXPLANATION: Musharakah is a form of Islamic finance partnership in which people provide money and/or expertise and work. At the beginning of the partnership, the partners agree on the profit-share percentage.			
3.	PomPak buys equipment from Chenar Finance, and pays the money in installments.	Ijara	Murabaha
EXPLANATION: Murabaha is a form of Islamic finance in which the finance company buys an asset and then sells it for a profit to the business that needs that asset. The business pays the purchase price in installments.			
4.	PomPak leases equipment from Chenar Finance, and pays a periodic rental fee.	Ijara	Murabaha
EXPLANATION: Ijara is a form of Islamic equipment financing in which the person providing financing buys the equipment and leases it to the other person for a rental fee.			
5.	100,000 people pool PKR 100,000 each to insure their lives. On the death of one person, that person's family receives PKR 300,000.	Takaful	Mudarabah
EXPLANATION: Takaful is a form of Islamic insurance in which people pool their insurance premiums to insure something. The person suffering the loss is made whole.			

COMPLETED PROJECTIONS (FOR QUESTION, SEE PAGE 105)

After much research, Safdar and Shereen settled on an equipment financing plan under which the business will borrow Rs. 4,000,000 and make a total of Rs. 5,500,000 in payments in four annual installments.

Rs. 4,000,000 Equipment Financing Plan

Payment	Year 1	Year 2	Year 3	Year 4	Total
Total	1,600,000	1,450,000	1,300,000	1,150,000	5,500,000

They now complete their projections. The equipment financing brings down profit margins but the business looks very promising!

Fruit and Juice Business (Rs.)						
		Year 1	Year 2	Year 3	Year 4	Year 5
Income						
1.	Total fruit (kg)	27,500	28,875	30,320	32,000	34,000
2.	Fruit price per kg	250	260	270	300	330
3.	Total fruit income	6,875,000	7,507,500	8,186,400	9,600,000	11,220,000
4.	Total fruit for juice (kg)	40,000	48,000	57,600	69,120	82,944
5.	Juice price per kg	400	420	440	450	460
6.	Total juice income	16,000,000	20,160,000	25,344,000	31,104,000	38,154,240
7.	Total income	22,875,000	27,667,500	33,530,400	40,704,000	49,374,240
Expenses						
8.	Total fruit (kg)	70,875	80,719	92,316	106,176	122,791
9.	Fruit expense per kg	190	195	200	210	220
10.	Total fruit expense	13,466,250	15,740,156	18,463,200	22,296,960	27,014,064
11.	Salary	800,000	960,000	1,152,000	1,382,400	1,658,880
12.	Marketing	800,000	960,000	1,152,000	1,382,400	1,658,880
13.	Rent	240,000	264,000	326,400	550,000	750,000
14.	Juice bottles & packaging	1,920,000	2,419,200	3,041,280	3,732,480	4,578,509
15.	Transport	800,000	1,008,000	1,267,200	1,555,200	1,907,712
16.	Electricity, gas & other expenses	1,600,000	2,016,000	2,534,400	3,110,400	3,815,424
17.	Equipment financing	1,600,000	1,450,000	1,300,000	1,150,000	-
18.	Total expenses	21,226,250	24,817,356	29,236,480	35,159,840	41,383,469
Profit (Loss)						
19.	Before tax profit	1,648,750	2,850,144	4,293,920	5,544,160	7,990,771
20.	Income taxes (assumed at 29%)	478,138	826,542	1,245,237	1,607,806	2,317,324
21.	After tax profit	1,170,613	2,023,602	3,048,683	3,936,354	5,673,448
22.	Profit margin	5.12%	7.31%	9.09%	9.67%	11.49%

Financial Instruments

TYPES OF FINANCING (QUESTIONS ON PAGE 122)

What type of financing is this or is needed?

Identify the type of financing that applies to each of these 10 situations.

- 1** Ali needs money to pay his university fees.

Loan Financing	Equity Financing
----------------	------------------

EXPLANATION: Financing for personal needs (such as payment of university fees) is almost always loan financing. In the case of financing of university fees, the idea is that a graduate student will earn enough to pay back the loan with markup.

- 2** Shereen and Ali need money to buy a juice machine which will last for three years.

Installment Sales Financing	Loan Financing
-----------------------------	----------------

EXPLANATION: To purchase equipment, installment sales or lease financing is usually used. Loan financing may also be used, but that is usually used for larger value equipment financing.

- 3** Shereen and Ali need a long-term investor to fund their business expansion, which is quite risky.

Loan Financing	Equity Financing
----------------	------------------

EXPLANATION: Shereen and Ali need a long-term investor to fund their business expansion, which is quite risky. This is ideal for equity financing as this is long-term financing. The investor has a share in the business but cannot ask for the money back on a due date.

- 4** Safdar gets financing to open a new shop. He must pay the money back in one year with a 20% markup.

Loan Financing	Equity Financing
----------------	------------------

EXPLANATION: Safdar must pay the money back in one year with a 20% markup. This is debt or loan financing. It has a specified repayment period with a specified repayment amount.

- 5** Safdar invests some extra money he has in a Government of Pakistani treasury bill.



EXPLANATION: A Government of Pakistani treasury bill is a type of debt or loan financing. It has a specified repayment period with a specified repayment amount.

- 6** Safdar invests some extra money he has in shares of a company listed on the Pakistan Stock Exchange.



EXPLANATION: Shares of a company represent an equity interest in the company. This is the case for both shares in a private company and shares in a company listed on the Pakistan Stock Exchange.

- 7** A bank provides financing for a power plant. The financing must be repaid by the power plant in 12 years.



EXPLANATION: This is a type of debt or loan financing. It has a specified repayment period with a specified repayment amount. Banks mostly provide loan financing although they also provide a limited amount of equity financing.

- 8** Ali borrows money from a bank to buy a flat in the city.



EXPLANATION: Individuals can obtain mortgage financing from a bank to buy or build a house or flat. In this kind of financing, the bank has a right to take over the house or flat if the financing is not repaid.

- 9** Shereen and Ali agree with an investor that he will get paid on his equity investment in their company before other shareholders are paid.



EXPLANATION: As the investor makes an equity investment in the company, he will receive shares. As his shares have a right to payment on his equity investment before other shareholders are paid, they are preferred shares.

- 10** In this kind of financing, a business is required to pay the money back with a markup, even if the use of the money does not lead to a profit.



EXPLANATION: Loan financing involves a specified repayment period with a specified repayment amount. The loan must be repaid even if the use of the money does not lead to a profit.

STOCK MARKET ANALYSIS (QUESTIONS ON PAGE 124)

Test your understanding of the basics of stock markets by answering the questions below.

Which type of company may be listed on the Pakistan Stock Exchange?

Public Limited Company

Private Limited Company

The shares of public limited companies may be listed and traded on the Pakistan Stock Exchange. Under Pakistan law, public limited companies are subject to stricter rules on reporting and management than private limited companies.

A public limited company has 100,000 shares and it is listed on the Pakistan Stock Exchange. It issues 10,000 new shares to investors for Rs. 20 per share. Who receives the money from the new share issuance?

The public limited company

Investors on the stock exchange

In this case, the public limited company has issued (or sold to investors) 10,000 NEW shares for Rs. 20 per share. The public limited company will receive Rs. 200,000 as the total share sale price (10,000 x 20).

A public limited company has 100,000 shares and it is listed on the Pakistan Stock Exchange. One investor (Investor A) owns 2,000 shares of the company. Investor A sells through the stock exchange all 2,000 shares to another investor (Investor B) for Rs. 20 per share. Who receives the money from the share sale?

The public limited company

Investor A

Investor B

In this case, Investor A has sold 2,000 EXISTING shares of the public limited company to Investor B. Therefore, Investor A will receive Rs. 40,000 as the total share sale price (2,000 x 20).

A public limited company has 10,000,000 shares and it is listed on the Pakistan Stock Exchange. Someone buys 100,000 shares (1% of the total) for Rs. 20 per share. What is the total value of the company?

Rs. 200,000

Rs. 2,000,000

Rs. 20,000,000

Rs. 200,000,000

The company has 10,000,000 shares. 1 share is worth Rs. 20. Therefore, the total value of all the shares of the company is Rs. 200,000,000 (10,000,000 x 20).

FOREIGN EXCHANGE ANALYSIS (QUESTIONS ON PAGE 126)

Test your understanding of the basics of foreign exchange by answering the questions below.

In 2007, the Pakistani Rupee to US Dollar exchange rate was PKR 60 to USD 1. In 2013, the Pakistani Rupee to US Dollar exchange rate was PKR 100 to USD 1. During this period, did the value of the Pakistani Rupee compared to the US Dollar go up or down?

The value of PKR went up

The value of PKR went down

Cannot tell

In this case, the value of the Pakistani Rupee compared to the US Dollar went down. In 2007, you could buy USD 1 for only Rs. 60. In 2013, you could buy USD 1 for Rs. 100. This means it takes many more Pakistani Rupees to buy the same USD 1.

The exchange rate is PKR 100 = USD 1. A company imports chocolate bars from USA and sells them in Pakistan. It buys each chocolate bar for USD 1 and sells it for Rs. 200. If the exchange rate becomes PKR 150 = USD 1, what will happen to its profits per chocolate bar?

Its profits per chocolate bar will increase from Rs. 50 to Rs. 100

Its profits per chocolate bar will decrease from Rs. 100 to Rs. 50

Its profits per chocolate bar will decrease from Rs. 150 to Rs. 100

	Category	USD Price & Exchange Rate	Income, Expense, Profit (Rs.)
Exchange rate: PKR 100 = USD 1			
1.	Product Income		200
2.	Product Expense	USD 1 x 100	100
3.	Profit		100
Exchange rate: PKR 150 = USD 1			
4.	Product Income		200
5.	Product Expense	USD 1 x 150	150
6.	Profit		50

When the exchange rate is PKR 100 = USD 1, the company's cost of goods per chocolate bar is Rs. 100 (USD 1 x Rs. 100), its sales price is Rs. 200 and its profit is Rs. 100 (Rs. 200 – Rs. 100).

When the exchange rate is PKR 150 = USD 1, the company's cost of goods per chocolate bar is Rs. 150 (USD 1 x Rs. 150), its sales price is Rs. 200 and its profit is Rs. 50 (Rs. 200 – Rs. 150).

Usually, a lower value of the Pakistani Rupee will result in less profit for IMPORTERS.

The exchange rate is PKR 100 = USD 1. A company exports chocolate bars from Pakistan and sells them in USA. It buys each chocolate bar for Rs. 100 and sells it for USD 2. If the exchange rate becomes PKR 150 = USD 1, what will happen to its profits per chocolate bar?

Its profits per chocolate bar will increase from Rs. 100 to Rs. 200

Its profits per chocolate bar will increase from Rs. 100 to Rs. 150

Its profits per chocolate bar will decrease from Rs. 100 to Rs. 50

	Category	USD Price & Exchange Rate	Income, Expense, Profit (Rs.)
Exchange rate: PKR 100 = USD 1			

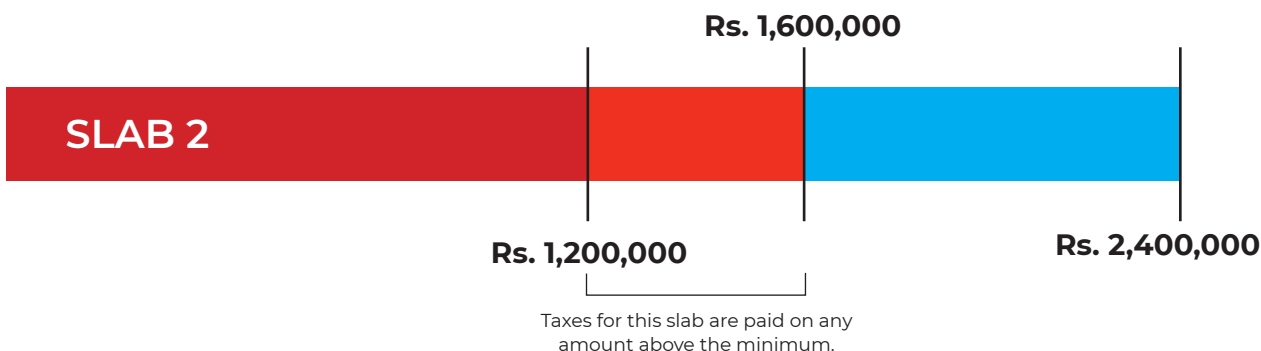
1.	Product Income	USD 2 x 100	200
2.	Product Expense		100
3.	Profit		100
Exchange rate: PKR 150 = USD 1			
4.	Product Income	USD 2 x 150	300
5.	Product Expense		100
6.	Profit		200

When the exchange rate is PKR 100 = USD 1, the company's cost of goods per chocolate bar is Rs. 100, its sales price is Rs. 200 (USD 2 x Rs. 100) and its profit is Rs. 100 (Rs. 200 – Rs. 100).

When the exchange rate is PKR 150 = USD 1, the company's cost of goods per chocolate bar is Rs. 100, its sales price is Rs. 300 (USD 2 x Rs. 150) and its profit is Rs. 200 (Rs. 300 – Rs. 100).

Usually, a lower value of the Pakistani Rupee will result in more profit for EXPORTERS.

CALCULATING TAX (QUESTION ON PAGE 141)



In the image above, Daniyal earns Rs. 1,600,000 a year, which is Rs. 133,000 every month. Based on the table explaining the slabs, can you calculate how much tax Daniyal should pay in 2023? Fill out the blanks in the steps below:

Step 1: Identify taxable amount based on the slab:

Salary:	Rs. 1,600,000
Minimum slab amount:	Rs. 1,200,000
Amount in excess:	Rs. 400,000

Step 3: Calculate the taxable income tax amount:

$$12.5 \times 400,000$$

100

Step 2: Find fixed tax amount and rate on taxable income:

Fixed tax on minimum	Rs. 15,000
Tax rate on excess	12.5

Step 4: Add the fixed tax and the taxable income tax amount to get the full tax Daniyal owes:

Fixed tax	15,000
Tax on excess	+ 50,000
Total	65,000

ASSESSING INSURANCE NEEDS (QUESTION ON PAGE 145)



ASSESSING INSURANCE NEEDS (QUESTION ON PAGE 146)

If you are a 30 yr. old with two children, which insurance cover works best for you?

Terms	Big family insurance	City life insurance
Premium	Rs. 15,000 a year	Rs. 18,000 a year
Coverage	Rs. 7,500,000	Rs. 7,500,000
Term	15 years	15 years
Riders	This plan has a health insurance rider for cover upto Rs. 50,000	This plan has no riders

Tick the option you would choose



MATCHING INVESTMENTS WITH RELEVANT PERSONAS (QUESTION ON PAGE 168)

The types of investments given below are either high risk or low risk.

- Place the investments under the correct headings. Which ones are low risk, and which are high risk?

High Risk	Low Risk
stocks	savings accounts
derivatives	government bonds
speculative stocks	fixed income securities
equity funds	cash

- Match three types of investments with the profiles of the investors below.

YASMINE QAMAR

Widowed, housewife
Age: 58

1.

2.

3.

SALAHUDDIN MUSA

Entrepreneur
Age: 30

1.

2.

3.

A PROJECT OF THE STATE BANK OF PAKISTAN
& THE ASIAN DEVELOPMENT BANK