Glossary of Banking Terms

Accrued interest

The accrued interest on a bond is the amount of interest accumulated on a bond since the last coupon payment. The interest has been earned, but because coupons are only paid at set intervals the investor has not gained the money yet. In India day count convention for G-Secs is 30/360.

Bid price/yield

The price/yield being offered by a potential buyer for a security.

Competitive Bid

Competitive bid refers to the bid for the stock at the price stated by a bidder in an auction.

Coupon

The rate of interest paid on a debt security as calculated on the basis of the security’s face value.

Coupon frequency

Coupon payments are made at regular intervals throughout the life of a debt security and may be quarterly, semi-annual (twice a year) or annual payments.

Face value

Face value is the amount that is to be paid to an investor at the maturity date of the security. Debt securities can be issued at varying face values, however in India they typically have a face value of Rs.100. The face value is also known as the repayment amount at par. This amount is also referred as redemption value, principal value (or simply principal), maturity value or par value.

Floating-rate Bond

Bonds whose interest rate varies with changes in a pre-specified market interest rate.
Gilt/Government Securities

Government securities are also known as gilts or gilt edged securities. “Government security” means a security created and issued by the Government for the purpose of raising a public loan or for any other purpose as may be notified by the Government in the Official Gazette and having one of the forms mentioned in The Public Debt Act, 1944.

LAF

Liquidity Adjustment Facility (LAF) is a facility by which the RBI adjusts the daily liquidity in the domestic markets (India) either by injecting funds or by withdrawing them out.

Maturity Date

The date when the principal (face value) is paid back. The final coupon and the face value of a debt security is repaid to the investor on the maturity date. The time to maturity can vary greatly from short term to long term (30 years).

Non-competitive Bid

Non-competitive bidding means the bidder would be able to participate in the auctions of dated government securities without having to quote the yield or price in the bid. The allotment to the non-competitive segment will be at the weighted average rate that will emerge in the auction on the basis of competitive bidding. It is an allocating facility wherein a part of total securities are allocated to bidders at a weighted average price of successful competitive bid.

Open Market Operations:

Central banks buy bonds in exchange for money, thus increasing the stock of the money, or sell bond; thus reducing the money stock. This operation is known as Open Market Operation.

Price

The price quoted is for per Rs. 100 of face value. The price of any financial instrument is equal to the present value of the expected cash flow. The price one pays for a debt security is based on a number of factors. Newly-issued debt securities usually sell at, or close to, their face value. On the secondary market, where already-issued debt securities are bought and sold between investors, the price one pays for a bond is based on a host of variables, including market
interest rates, accrued interest, supply and demand, credit quality, maturity date, state of issuance, market events and the size of the transaction.

**Primary Dealers**

In order to accomplish the objective of covering the government borrowing needs as cheaply and efficiently as possible, a group of highly qualified financial firm/banks are appointed to play the role of specialist intermediaries in the government security market between the issuer on the one hand and the market on the other. These are generally called Primary dealers or market makers. In return of a set of obligations, such as making continuous bids and offer price in the marketable government securities or submitting reasonable bids in the auctions, these firms receive a set of privileges in the primary/secondary market.

**Private Placement**

A private placement is a direct offer by a company to subscribe to a security issued by it, which is not available to any person other than the person to whom the offer is made. Section 67(3) of Company Act, 1956, while specifying what does not constitute a public offer, lays down two basic conditions, viz., (a) the share and debentures should not be available for subscription to persons other than those receiving the offer, and (b) the offer should be made to less than 50 persons.

**Repo Rate**

Repo rate is the return earned on a repo transaction expressed as an annual interest rate.

**Repo/Reverse Repo**

Repo means an instrument for borrowing funds by selling securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities, with an agreement to repurchase the said securities on a mutually agreed future date at an agreed price which includes interest for the fund borrowed.

Reverse Repo means an instrument for lending funds by purchasing securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities, with an agreement to resell the said securities on a mutually agreed future date at an agreed price which includes interest for the fund lent.
Secondary Market

The market in which outstanding securities are traded. This term differentiates from the primary or initial market when securities are sold for the first time. Secondary market refers to the buying and selling that goes on after the initial public sale of the security.

Tap Sale

Under Tap sale, a certain amount of securities is created and made available for sale, generally with a minimum price, and is sold to the market as bids are made. These securities may be sold over a period of day or even weeks; and authorities may retain the flexibility to increase the (minimum) price if demand proves to be strong or to cut it if demand weakens. Tap and continuous sale are very similar, except that with Tap sale the debt manager tends to take a more pro-active role in determining the availability and indicative price for tap sales. Continuous sale are essentially at the initiative of the market.

Treasury Bills

Debt obligations of the government that have maturities of one year or less is normally called Treasury Bills or T-Bills. Treasury Bills are short-term obligations of the Treasury/Government. They are instruments issued at a discount to the face value and form an integral part of the money market.

Underwriting

The arrangement by which investment bankers undertake to acquire any unsubscribed portion of a primary issuance of a security.

Weighted Average Price/yield

It is the weighted average mean of the price/ yield where weight being the amount used at that price/yield. The allotment to the non-competitive segment will be at the weighted average price/yield that will emerge in the auction on the basis of competitive bidding.

Yield

The annual percentage rate of return earned on a security. Yield is a function of a security’s purchase price and coupon interest rate. Yield fluctuates according to numerous factors including global markets and the economy.
**Yield to maturity (YTM)**

Yield to maturity is the total return one would expect to receive if the security is being held until maturity. Yield to maturity is essentially the discount rate at which the present value of future payments (investment income and return of principal) equals the price of the security.

**Yield curve**

The graphical relationship between yield and maturity among bonds of different maturities and the same credit quality. This line shows the term structure of interest rates. It also enables investors to compare debt securities with different maturities and coupons.

**AER** - Annual earnings rate on an investment.

**Annuity** - A life insurance product which pays income over the course of a set period. Deferred annuities allow assets to grow before the income is received and immediate annuities (usually taken from a year after purchase) allow payments to start from about a year after purchase.

**APR** - The annual percentage rate of interest, usually on a loan or mortgage, usually displayed in brackets and representing the true cost of the loan or mortgage as it shows any additional payments beyond the interest rate.

**Bank Statements** - This is a statement from the bank giving details of transactions in the relevant account. It can be requested at any intervals required, usually monthly.

**Bear Market** - A bear is somebody who believes that the market is falling and a bear market is a falling market. See bull market for the opposite.

**Bounced Cheque** - when the bank has not enough funds in the relevant account or the account holder requests that the cheque is bounced (under exceptional circumstances) then the bank will return the cheque to the account holder. The beneficiary of the cheque will have not been paid. This normally incurs a fee from the bank.

**Bonds** - These are securities which pay interest at specified intervals and the principle amount of the loan is paid at maturity.
**Bull Market** - A bull is somebody who believes that the market is rising and a bull market is a rising market. See bear market for the opposite.

**Cashback Mortgages** - This is when the mortgage provider lends the money for the mortgage and, in addition, a lump sum to pay for, for example, building work to be carried out.

**Central Clearing Time (in England and Wales)** - This is the time that it takes for the monies from a cheque to be taken out of the payee's account and put into the payer's account. This is three working days in England and Wales, as long as the cheque was paid in before 16.30.

**Certified Documents** - These are photocopies of original documents that have been signed by a professional i.e. a solicitor, accountant, teacher, doctor or bank official. The professional also states, on the document, "original seen" since they must be able to verify that these are genuine copies and therefore have to have seen the original, they also date the document and put their full name, profession and their address.

**Charges** - This is the money paid to the bank for services rendered. Charges include overdraft fees, charges for bouncing cheques, interest on overdraft and any charges that a business account might normally incur.

**Charge Cards** - Cards which can be used like a credit card but the charge has to be paid off on the due date. They usually have a high limit or no limit.

**Cheque Book** - A small, bound booklet of cheques. A cheque is a piece of paper produced by your bank with your account number, sort-code and cheque number printed on it. The account number distinguishes your account from anyone elses, the sort-code is your bank's special code which distinguishes it from any other bank. In times gone by, anything with the correct details and a verifiable signature could act as a cheque. Even an elephant was once used!

**Cheque Clearing** - This is the process of getting the money from the cheque-writer's account into the cheque receiver's account.
**CHIP and PIN** - A Chip is a small electronic insert placed into a cheque or credit card. The PIN is a four digit personal identification number which is used with the card by the card-holder.

**Clearing Bank** - This is a bank that can clear funds between banks. For general purposes, this is any institution which we know of as a bank or as a provider of banking services.

**Contract Hire** - This is a way of hiring an item of large capital value where the maintenance is the responsibility of the company that hires out the item. A fixed monthly figure is paid and the item can be sold, usually to an unconnected third party.

**Credit Rating** - This is the rating which an individual (or company) gets from the credit industry. This is obtained by the individual's credit history, the details of which are available from specialist organisations (Equifax and Experian are the two big operators in the U.K. www.equifax.co.uk and www.experian.co.uk).

**Credit Scoring** - This is the process of assessing an individual's credit-worthiness. The process involves taking information from an individual on an application form (for example when applying for a store card) and weighting the answers given. Certain responses will attract higher scores than others and the total score will determine whether or nor the organization wants to do business with the individual, or if they represent too high a credit risk.

**Credit-Worthiness** - This is the judgement of an organization which is assessing whether or not to take a particular individual on as a customer. An individual might be considered credit-worthy by one organisation but not by another. Much depends on whether an organization is involved with high risk customers or not.

**County Court Judgement** - This is when a judge at a county or small claims court finds against an individual and they have a county court judgement made against them. This is recorded nationwide (and by the credit tracking organizations Experian and Equifax) so anyone wanting to know the credit-worthiness of an individual will know that the county court judgement exists. Once it is paid off then the record remains but it is shown as being paid which
reduces the credit risk associated with the person with the county court judgement.

**Direct Debit** - An amount of money taken from a bank account, set up by the recipient and can vary in amount and exact time that it is taken from an account. Mortgages are usually direct debits.

**Endowment Mortgage** - Interest only is paid over the term of this sort of mortgage and the capital is repaid at the end of the term by using the monies from an endowment policy.

**Factoring** - This is when a business sells its invoices to a specialist company or bank which chases payment and pays a percentage of the invoice back to the original business. The business can then continue with its work and problems from cash-flow are reduced by having money from unpaid invoices up-front.

**Hire Purchase** - When an item of large capital value is bought over time by paying a deposit and fixing a period over which the loan will run (usually between 12 and 60 months) and then paying fixed and equal repayments over this period.

**Identity Theft** - This is when criminals use an innocent person's details to open or use an account to carry out financial transactions. It is very easy to do with an individual's personal details, which is why shredding confidential information is so important.

**Identity Verification** - This is often used by financial institutions to verify the customer and usually takes the form of a pass-word and the answer to an obscure personal question such as the customer's mother's maiden-name.

**Interest** - The amount paid or charged on money over time. If you borrow money interest will be charged on the loan. It you invest money, interest will be paid (where appropriate to the investment). Interest rates usually bear a close relationship to the Bank of England's base rate. It is expressed in percent.

**ISAs** - This stands for Individual Savings Accounts. These are available to all UK residents over 18 (mini ISAs are available to 16 and 17-year-olds). Investment
limits apply to the total contributions made in any tax year, not to the total in the ISA itself. ISAs can be cash, stocks and shares or life insurance.

**Lease Purchase** - This is an agreement made on an item of high capital outlay (for example, a car) where the ownership is transferred to the person who is leasing the item at the end of the contract, providing all the terms and conditions of the purchase have been fulfilled.

**Money Laundering** - This is when money gained from crime is put into a bank so that it can be accessed safely by the criminals and terrorists. It makes the proceeds of illegal activities easier to get to.

**Money Transfer** - This is the movement of money from one account to another.

**Money Transfer Abroad** - This is the movement of money from one account to another, the second being in a different country from the first.

**Offsetting** - This is when the credit balances in a current and savings account are netted off against the account holders borrowings (typically a mortgage) so that the rate paid on the borrowing is reduced as a result of the credit held in other accounts, which reduces the amount that is being borrowed.

**Overdraft** - This is when a person has a minus figure in their account. It can be authorized (agreed to in advance or retrospect) or unauthorized (where the bank has not agreed to the overdraft either because the account holder represents too great a risk to lend to in this way or because the account holder has not asked for an overdraft facility).

**Payee** - The person who receives a payment. This often applies to cheques. If you receive a cheque you are the payee and the person or company who wrote the cheque is the payer.

**Payer** - The person who makes a payment. This often applies to cheques. If you write a cheque you are the payer and the recipient of the cheque is the payee.

**PEP** - Personal Equity Plans have been replaced by ISAs. Existing PEPs can be retained but, since April 1999, no new ones can be opened.
**Phishing** - This is when a criminal uses the internet to try to fraudulently obtain details of peoples accounts so that they can use these accounts themselves, usually to take money out of.

**Repayment mortgage** - This is a mortgage where the sum borrowed is paid off by the end of the mortgage term. It involves monthly repayments which consist of the interest on the loan plus some of the capital borrowed.

**Security for Loans** - Where large loans are required the lending institution often needs to have a guarantee that the loan will be paid back. This takes the form of a large item of capital outlay (typically a house) which is owned or partly owned and the amount owned is at least equivalent to the loan required.

**Standing Order** - A regular payment made out of a current account which is of a set amount and is originated by the account holder.

**Tessas** - Tax Exempt Special Savings Accounts.