I

Identification: in banking it concerns customer identification involving verification of customer account and bona fides if the transaction is not being done in person; or bank identification in inter bank transfers through identification numbers assigned by the payment system agency, specially for electronic transfers.

Illiquidity: a financial position of a bank when its current assets cannot be converted into cash to meet its payment obligations or current liabilities; or when its assets are no fungible and cannot be redeployed; illiquidity may occur because of insufficient provisioning for contingent cash requirements, or a mismatch of the maturity structure of assets and liabilities, or unforeseen financial market trends, or a liquidity squeeze imposed by the central bank; it may occur irrespective of the overall financial strength and soundness of a bank, that is, the bank may be solvent, its capital may be intact, but it may not have sufficient liquidity to ride out the payment requirements; the only recourse available then is to borrow at penalty cost from the market, or from the central bank, or liquidate assets at losses. Illiquidity of an enterprise, a business, or a company may occur for same reasons with similar consequences.
(see Insolvency)

Impaired Capital: capital of a company or a bank is impaired when its paid-up capital is less than its stated value; impairment occurs if the profit of a company is eroded due to carried forward losses, or a bank's capital may be eroded due to excessive loan losses.

Impaired Loan: is a nonperforming loan with over dues of principal and interest for 90 days and beyond; or when a loan is secured by impaired collateral or with a loan security of doubtful value, which turns out to be insufficient to cover the accumulated overdues; impaired loan may be retained on the books of the bank, but eventually may have to be classified as bad loan, if the nonperformance persists and recoveries through collateral cannot cover the loan losses.

Impaired Loan Portfolio: the loan portfolio of a bank is considered to be impaired, when the proportion of impaired loans becomes large relative to the total size of the loan portfolio, thereby exceeding the ability of the bank to sustain eventual loan losses from its income, reserves and bank's capital, thus endangering solvency of the bank.

Impermissible Nonbank Activities: are activities prohibited by the banking charter or the memorandum of association, or the banking code, or rules and regulations of the central bank, restricting banking activities to routine banking business, and prohibiting banks to engage in businesses other than banking even though it may be highly profitable.

Implicit Costs: are costs of a business that can not be directly charged or attributed to the business activity, but nonetheless are part of the total costs of doing the business, such as costs of litigations, penalties, gratuities, or protection premium that must be paid, like *bhatta* for the business to continue its operations.

Implicit Deposit Insurance: an undeclared deposit insurance mechanism within a bank without a formal arrangement with an insurance company or an organization, such as through establishing a fund financed by debit to the expense account or by a deduction from interest payable to the depositors; such arrangements, however, are not common in banking systems.

Implicit Guarnatee;

- ***in bankin;*** the implicit commitment of the authorities to shore-up or support an ailing bank if it is too large to risk a general banking panic; or the bank management having the perception that because of the large size of the bank, the authorities will mount a rescue effort so as not to undermine public's confidence in the banking system.
- **of *exchange rate or interest rates;*** commitment of the central bank to maintain a desired level of exchange rate, or a desired level of interest rates, amounting to an implicit guarantee to private investors, and private capital inflows.

Implicit Interest: the element of interest built into a fee or a bank charges; or a rate of interest not separately declared; for example, in case of a quotation for a usuance bill to be discounted, there may be an element of interest which is not explicitly declared; in foreign exchange transactions, there may be an element of interest, especially if there is a negative (currency delivery time lag).

Implicit Interest Charge: interest or mark up charges which are not separately quoted but are payable only in certain cases such as default or delay. For example, where payment or reimbursement is delayed an additional interest, may be payable.

Implicit Tax: rules and regulations that may add to the cost of an activity or a transaction or an asset holding the same way as a direct levy or an explicit tax; for example, the requirement that banks must hold a certain proportion of their assets in low-yield treasury bills or government papers is an implicit tax on banking profits, since banks can use same funds to earn higher returns elsewhere.

Imprudent Lending: is to extend loans and credits without observing the norms, or credit procedures, or without appropriate evaluation of credit risks, collateral quality and borrower's creditworthiness; imprudent lending may be done deliberately, or may occur because of lack of know-how and expertise in credit operations and decision making.

Imputed Income: of a corporation, a company or individual is calculated for financial evaluation or tax assessment purposes, consisting of declared income from various sources and benefits received which have a well-defined counterpart cash value or financial cost which the recipient would have incurred otherwise.

Inappropriate Lending: lending based on factors which are contrary to the prudent credit guidelines and policies and routine banking practices; for example, lending to a business concern without reference to the financial strength, capabilities, or creditworthiness of the business, inadequate evaluation or assessment of collateral; credit line in excess of financing needs.

Incentive: inducement, encouragement or financial reward offered to promote certain types of activities that may not be undertaken otherwise; offered by the government to businesses, banks, manufacturers or traders; offered by organizations to their clients; offered by management to staff. Several categories of incentives such as:

- tax incentives; these are tax breaks and holidays offered to businesses and companies.
- financial incentives offered through banking system such as cheap credits to priority sectors.
- investment incentives offered to investors to promote certain types of investment.
- employment incentives offered to employers to promote employment mix and site; offered to employees for better performance.
- consumer incentives offered to purchasers to promote certain types of products.
- product or marketing incentives to increase production, turnover and sales.

Incipient Run: early stages of run on a bank when depositors tend to withdraw their deposits in excess of their requirements to keep the money elsewhere; this may be due to lack of confidence, triggered by the perception of impending insolvency or closure.

Income Statement (profit and loss statement): is a statement showing the operating performance of a bank or business over a given period of time, usually a year; income statement of a trading and manufacturing business has three parts:

- one part showing gross profit, which is the difference between sales and cost of goods sold.
- next part showing net profit from operations, the difference between gross profit and operating expenses.
- next part showing net income before tax, which is net profit from operations plus any other income less 'other expenses', if any, with a final figure of net income after tax.

The income statement of a bank includes the following:

- the net interest margin, difference between interest earned and interest paid,
- operating income comprises of treasury income and miscellaneous fee earnings commissions to arrive at operating profit,
- from operating profit, operating expenses are deducted to arrive at gross profit,
- finally, net profit is arrived at after deducting taxes and other reserves.

Income Stream: the flow and sources of income of a company may be from its regular business operations of or from other avenues such as return on investments, rents on properties owned by the company, or profits on sale of assets.

Income Tax: is the tax levied on incomes of individuals or businesses on annual basis; it is stipulated in the tax law and its amendments, tax rules, regulations, and directives, and its revenue in most countries is the central part of the government budget; income tax on business is levied on the income shown in the financial statements filed with the tax-assessing and collecting authority; personal income tax of salaried persons are deducted at source by the employer, and deposited with tax authority for eventual payment; while tax on other specified types of income, such as those self-employed is assessed according to the income tax regulations, and is payable at specific dates during the tax year but adjusted at the end of the tax year when the final assessment of income and tax takes place.

Inconvertible:

- ***Assets:*** fixed assets or other assets that can not be converted into cash or into other assets.
- ***Bond:*** bonds that can not be converted into another instrument or liability.
- ***Currency:*** a currency cannot be converted into another currency freely in the market, except by the authorized banks under strict rules governing foreign exchange, and on rates officially posted by the central bank; in Pakistan, Pak rupee was inconvertible for many years until the relaxation and liberalization of foreign exchange rules and restrictions in the recent years.
- ***Paper Money:*** consists of currency issued by the central bank or the government that cannot be converted or exchanged by the issuing authority into gold or other precious metals, though it is legal tender.
- ***Security:*** a security which cannot be traded for cash or exchanged

Indebtedness: the state of being in debt; when a borrower is indebted to lender indebtedness continues until the debt is paid off.

Indemnity: is an undertaking to compensate for any loss or expense caused by factors as specified; it differs form a warranty which is an undertaking to compensate against nonperformance or illiquidity; it also differs form a guarantee where the guarantor's liability is secondary and contingent; whereas in an indemnity, the indemnifier's liability is primary.

Indenture: a deed or a formal agreement made between two or more parties containing terms and conditions of a contract such as a bond indenture; Earlier on, these documents had indented edges for identification; it usually refers to bond indenture, mortgage or deed of trust.

Independent Audit: an audit conducted, on a special request and for a particular purpose, by auditors who are not the usual auditors of the company, for various purposes such as purchase, acquisition or merger of company or, investigation of a bank fraud, forgery or misappropriation in an account; independent audits can be requested by purchasers, owners or directors of company in the first case, or by central bank or regulating agencies in the second type of cases.

Independent Agency: is an organization, an agency or an institution responsible for recovery of debt retained by a lender for a fee or commission for their services in cases where recovery procedures are difficult, or if debtor is not available, or liquidation and winding up of business is complicated involving lengthy procedures and legal action.

Indexation: is the adjustment for inflation of wages, salaries, pensions, entitlements, or prices of specific commodities and services to keep the parity of nominal relative values in a current year; or what is the same, to keep the relative real values constant over a period of time with reference to a base year, using various types of price indices for specific categories of items being adjusted.

- ***indexation of commodity prices;*** adjustment for increase in the price of a specific product or commodity by the producer, manufacturer or the trader by the rate of inflation by the wholesale price index to cover the parallel increases in the cost of production and to sustain profitability.
- ***indexation of wages;*** adjustment of wages and salaries specifically tied to the increase in the cost of living by the cost of living index to maintain the real purchasing power of wage and salary incomes in times of inflation; that is, maintaining relative real wage or salary constant over time.

Indexed Bonds: are bonds issued with a provision that interest rate on the bond would be linked to a standard price index, or to the index of prevailing interest rates; the interest amount payable includes an element of adjustment due to changes in indexed rate relative to the base year.

Indexed Debentures: debentures which carry a provision that their values would be adjusted relative to a price index; since debentures are long term debt instruments, the investors need protection against inflation or interest rate changes.

Indexed Financial Contract: a long term financial contract linked to an index so that in case of inflation its value may be accordingly adjusted.

Indexed Instruments: are mostly debt instruments linked to an index, for example the amount payable or receivable adjusted by a price index. Index-linked securities are particularly attractive to investors when a high rate of inflation is expected.

Indexed Securities: are short to medium term debt securities whose value at maturity or interest rate on the security is linked to a major interest rate, or an index of commodity prices, exchange rate, or other such indicators; these securities may be positively or negatively indexed, i.e. their value may increase or decrease if the reference index or the value of underlying instrument changes; indexed securities may have return characteristics similar to direct investments in the underlying instrument, but may be more volatile than the underlying instruments.

Indexed Obligation: is a financial obligation linked to an index; for example final amount payable adjusted by a price index to cover inflation.

Indicators of Financial Depth: for a company, these are parameters to determine a company's financial strength; as shown by the debt to equity ratio, capital to asset ratio; for an economy, it is indicated by the ratio of M2 to GDP.

Indirect Cost: are expenses that cannot be attributed to an activity, or not incurred exclusively to facilitate the activity concerned; cost of an item not directly related to its production or acquisition.

Indirect Loan: is a loan granted to a borrower for use by a third party, where the real beneficiary would be other than the borrower; for example, a loan given to the staff of a company where the loan is effectively the liability of the company.

Indirect Secured Installment Loan: a loan where installments payments are to be made from a regular source linked with the collateral or asset created from the loan itself; for example, a house building loan to the staff of a company where loan charge is with the company, but installments are to be paid from rent of the house; or a simple loan where installments would be made from periodic profits on a term deposit with the condition that the deposit would not be withdrawn as long as the loan is not fully repaid.

Industry or Sector Risk: are lending risks pertaining to a specific line of business activity or to an industry due to concentration of lending activities of the bank; such over-exposure of the bank in relatively risky industries or sectors is risky, because adverse business and financial trends associated with the sector may seriously affect bank's borrowers and impair their ability to repay their loans, causing loan losses or lowering the quality of loan portfolio of the bank; for example, if a bank's lending is concentrated in textile sector, and if the local textile industry is facing business adversities in its markets overseas, this may jeopardize local textile manufacturers or traders, thus transmitting industry risk into a credit risk faced by the lending bank.

Industrial Bank: a financial institution established as a joint stock company or a state-chartered body, specializing in short term and long term financing of industrial units in different sectors; such a bank, however, may not be allowed to undertake normal commercial banking business.

Industrial Development Finance Institutions: banks or specialized financial institutions established with the basic objective of providing long term finance for industrial development. Such institutions may provide short-term finances to industrial companies, and perform limited banking functions. *(see Development Finance Institutions)*

Industrial Finance: is loans and other credit facilities provided to establish industrial units and also to finance their operations.

Industrial Organization: the underlying structure of an industrial establishment specifying management, lines of authority and system of control of its operation; establishment and operation of various production processes and their integration into a synchronized unit; management of materials, inputs, labor, stocks and inventories, together with cost and quality control; the quality and superiority of industrial organization is a major source of competitive edge over others in a given industrial line of activity.

Industrial Structure: of a country consists of companies and businesses engaged in manufacturing, production, supply and distribution of goods and services in various lines of industrial activities, classified into sectors or sub-sectors according to the scale of organization, type of activity, concentration, location and coverage.

Industrial Trust: a trust involved in industrial activities, where an industrial unit is owned and managed under overall supervision of the trustees; profits earned are used in furtherance of the objectives of the trust, such as education, health and social services.

Inflation: is a persistent increase in the price level thus enhancing expensiveness; commonly known as *ifrat-e-zar* which is rather misleading; it is measured by the consumer price index (CPI), the wholesale price index (WPI), or the general price index (GPI); the price increase results in a corresponding decrease in the *real value* of a unit of money, and thus a decrease in the real purchasing power of income, salaries, and wages. Inflation causes a decrease in the real net worth of financial assets, such as money balances and deposits with the banking system, and inexorably distorts consumption and savings in an economy with far reaching and severe consequences that may take years to overcome. Inflation is

of various types; it may be cost-push inflation, stemming from rising prices of raw materials, indexed wages, or increase in energy costs; or it may be demand pull inflation, if domestic supply of goods and services is inadequate to meet the demand; or it may be foreign inflation if import prices rise as happens in the wake of massive devaluations provided imports are a substantial portion of domestic supplies and are critical to the domestic economy such as oil imports. Thus, in an economy, inflation may emerge from various sources; however, the root cause of inflation is the excess of aggregate demand over aggregate supply; that is, a persistent excess of expenditures over production and income levels, financed from savings or borrowings, whether domestic or foreign. The excess demand may originate in the private sector or the public sector, or both. For the private sector, there are various limitations on excess of expenditures specially on consumption expenditures since it depends on income levels, taxes, and costs of private borrowings; whereas excessive investment expenditures depend on private asset base, profitability and their expectations related to investment activities. For the public sector, however, these limitations are not serious, because it can incur persistent public sector deficits, and as sovereign borrower, it can finance its excess demand both from domestic and foreign borrowings. Further, if the excess demand, originating mainly from the public sector is funded through deficit financing and borrowings from the central bank, it involves creation of money and excessive issue of currency, without sufficient backing of central bank's reserves of gold and foreign exchange. This results in excessive money supply, or *ifrat-e-zar* in a proper sense of this term, leading to an increase in the general price level. In this sense, excessive money supply, or *ifrat-e-zar*, often described as the phenomenon of "too much money chasing too few goods", is a critical link in the chain of consequence of excessive and wasteful expenditures in the first place, as is the case in Pakistan, but not the basic cause of inflation nor its starting point. If the excess demand of public sector is financed from borrowings form domestic banking system, or from the general public, or from overseas, the inflationary impact will not be the same as in the first case, though it will result in expansion of the banking credit and money supply and hence inflation. Inflation is a common feature almost in all countries at moderate levels, but persistently higher rates of inflation cause economic and financial chaos, a rapid erosion of purchasing power, a depreciation of nominal and real exchange rates, and a redistribution of real income and wealth against fixed income group who invariably suffer a major loss in their real income. Hence, inflation is seen as a regressive tax which affects the fixed income and lower income groups much harshly than others, with devastating social consequences.

Inflation Feedback: is the re enforcement of inflationary trends as it may occur through indexation of wages and salaries, or through indexation of costs, fees and charges in service industries; or through indexation of prices of consumer essentials and food items; or through indexation of strategic raw materials; this type of feedback sustains inflationary spiral, and if not curbed at the source, it may cause intensification of inflationary trends.

Inflation Risk (portfolio): is the risk of erosion of real net worth of an investment portfolio; a decline in the real return on securities held in the portfolio. Inflation us a major risk to even a well diversified investment portfolio because inflation erodes away real return of an investment in securities, through some types of securities may be more exposed to such a loss; for example real returns on bonds and reserves may be less than real returns on stocks in inflationary times, thereby providing a relative edge in stocks to portfolio investors; for a portfolio investor safeguarding the net asset value of the portfolio is the main element in risk diversification, than holding a particular type of stock or bond.

Inflation Tax: is the reduction in the real income and real purchasing power of fixed-income groups, mainly salary and wage earners because of inflation, causing a reduction in consumption and eventually the aggregate demand; the impact of inflation is similar to income tax; mainly a cut in the real income of fixed-income groups, whose earnings are not indexed to inflation, thereby releasing command on real resources that may be available to other groups for alternative uses; thus, inflation tax is a highly regressive tax creating a redistribution of real income in favor of mercantile group, landlords, and property owners.

Inflationary Impact: reduction in the real value of money, the real purchasing power of salaries and wages, and if widespread, may cause substantial changes over time in the social distribution of wealth and income, as has happened in Pakistan.

Inflationary Policies: economic and financial policies of the government that may cause inflation or re enforce existing inflationary trends such as sustained large budget deficits financed by credit creation or deficit financing; increase in wages and salaries allowed beyond productivity increase and in excess of current price trends, negative real interest rates, or subsidized credits.

Inflow of Funds: are receipts in the form of cash or credit into the accounts of a company or business from various sources such as sales or business transactions, receivable, loan disbursements, or loan repayments, or payments from shareholders.

Informal Account: unregulated account or record of transactions without any formality conducted without adhering to basic accounting principles, rules, and procedures; for example, financial transactions between friends and relations; debts due in such cases may not be supported with proper documentation and may not have legal cover.

Informal Banking: is an unregulated banking segment prevalent in many countries, providing deposit and lending facilities on personal cognizance or social collateral; such practices are part of local traditions and customs: for example, money deposited with *mohallah commetties* borrowings from local money lenders or funds transferred through *hundi*, an informal bill of exchange.

Informal Deposit Services: provided by nonbank financial institutions on informal basis; may also be provided by banks, on occasions and in special circumstances, such as deposit taking services outside the normal banking practices; for example, accepting deposits at the customer's place of business or after banking hours; however, under prudential regulations of State Bank of Pakistan such services are not allowed for commercial banks.

Informal Finance: is financing arranged from sources other than banks or financial institutions; usually provided by money lenders, chit funds, friends, or relatives; the criteria for such advances may be consideration of personal relationship rather than principles of sound lending where formalities of obtaining charge documents or the transaction may not be properly followed.

Informal Financial Sector: is the unregulated financial sector of an economy which functions without checks or controls by monetary authorities or may even be illegal; for example, paralleled market of deposit takers who offer higher rates of interest paid on monthly basis but without any security or legal binding for the payment of the principal amount or foreign exchange transactions conducted through nonbanking channels; the informal sector in Pakistan is large and has considerable financial impact on trade, businesses and formal financial sector.

Informal Markets: buying, selling of goods and services outside the recognized and regulated markets; unrecorded transactions conducted to avoid tax, registration or reporting; or conducted legally but through informal channels.

In-Home Banking: extending banking facility to customers, enabling them to conduct certain banking transactions from home or office; providing information about the bank or about their account through computer terminal at the residence or office of the customer; to originate certain transactions; for example, payments and transfers from the account; this facility, however, is available in the developed countries only as it requires a fault-free on-line communication network.

Initial Public Offer (IPO): is the sale of shares by a company which has gone public, that is, opened its shareholdings and equity base to general public for the first time to increase its market capitalisation, and has newly listed on stock exchange to offer its shares for sale to the general public; a time-honored process of enhancing capital base of a company well beyond the equity of original owners of the company.

Inputs: are the intermediate goods like raw materials and products used in the production process to create finished goods as output; inputs include labour, machinery or equipment used in production; for a company, inputs are specific to its processes of production; likewise, the output of the unit of production is also specific to the company or to the producer regardless of its use as a final commodity, or as input by other companies as one link in the chain of production; for example for a car manufacture, steel is an input, whereas the same steel is the output of steel manufacturer; likewise for a wheat farmer, seeds and fertilizers are inputs, but fertilizer is the output of fertilizer company whereas wheat, the output of the farmer, is input for flour mills; for operational purposes, a way has to be found to measure units of inputs needed per unit of output, specially for those inputs which are physically indivisible such as a machine or equipment or a building.

Inside Director: an officer of the company who is also a director and member of the executive Board of the company; since inside director has confidential information about the company, he is not allowed to have his own private business with the company, since information could be used for personal gains which is a major conflict of interest; in contrast to an outside director, who is neither an employee or a direct shareholder; for example, a director nominated by a lending bank or a corporate shareholder of a company which has borrowed from the bank or obtained equity finance from investors or shareholders.

Insider: a person who has access to confidential information about the activities and policies of company not available to outsiders; may be an employee, an executive, a major shareholder, a director of the company, or has close relatives or friends in the company with access to confidential information.

Insider Control: control on or substantial influence over the policies and business of a company by an insider who is a director, and executive, or a key employee, having access to vital information on strategic business decisions.

Insider Information: confidential insider information concerning net worth, financial status, or strategic business decisions such as sale of a company or a corporation, merger, or recapitalization is highly valuable and if leaked out prematurely, it may drastically affect the market valuation of the company or the market value of shares outstanding or its profitability; may substantially enrich those few senior executives or top management privy to such information, if they decide to misuse this information for their personal gain and conduct stock or business transactions ahead of others.

Insider Lending: are loans and advances provided by financial institutions to their affiliates, subsidiaries or group-linked or group-owned companies in case the lending institution is owned by a conglomerate or a large holding company, on terms and conditions that may be below market levels, thereby reducing the cost of borrowing, or bailing out the borrower in case it is facing serious financial difficulties.

Insider Loan, Credit: are loans, advances or lines of credit extended to subsidiaries, group-owned companies, shareholders, or privileged persons on soft terms; these advances may be personal loans; or extended through guarantees, comfort letters or sureties not otherwise available to outsiders.

Insider Trading: business transactions or trading activities of an insider specially in the securities market capitalizing on privileged information about the company business or the value of the security not available to outsiders; this is a major abuse of inside information specially in the securities market, is unlawful and is strictly prohibited in many countries.

Insolvency: of an enterprise, a business, a company, or a bank occurs when the shareholders' funds including capital and reserves are insufficient to cover losses accumulated over a period because of sustained unprofitability of the business; in this sense, insolvency gradually builds up over time and is rooted into the structure of business operations; it does not occur overnight owing to contingencies or sudden adversities of the market trends; the only recourse is substantial re-capitalization by the owners, or by new investors if they could be persuaded to invest; otherwise the business may end-up in receivership for re-organization, restructuring and consolidation; if none of these recourses are feasible, then insolvency may lead to bankruptcy and closure, spreading the losses beyond owners to the creditors or clients.

Insolvency of a Bank: occurs if the bank's capital is wiped-out; or if the shareholders' funds and reserves are insufficient to cover massive losses mainly arising from seriously impaired loan portfolio, a widespread default among its borrowers, and unrecoverable debt repayments; in such a situation the only recourse available to the bank is substantial re-capitalization by its owners, otherwise the bank would have to close its operations and end-up in receivership, followed by eventual bankruptcy or closure if a restructuring and consolidation is not feasible. In this sense, insolvency and financial distress of a bank are similar, but far more serious than illiquidity; typically a bank becomes insolvent first, and illiquid later on; since the insolvency of a bank may have ripple-effects and undermine the confidence of the public in the banking system, the central bank plays a key role in managing insolvency, and assisting it as the lender of the last resort if the bank can be rescued, through injection of liquidity and fresh capital; but this may not be possible in case of systemic insolvency. *(see Illiquidity, Financial Distress)*

Insolvency of Banking System: occurs when a large number of banks in a country are facing insolvency, also called systemic insolvency, for similar reasons as given above; but while insolvency of a single bank may be manageable by the central bank, and receivership or bankruptcy may be averted if the owners of the bank are willing and capable of substantial re-capitalization, or new investors may be found, but systemic insolvency is beyond the resources of a central bank because total re-capitalization needs are massive; hence, in a systemic insolvency, a number of banks need to be restructured, consolidated or even closed down causing widespread financial losses.

Insolvency of an Enterprise: is a dire financial condition of an enterprise, where the capital base of the enterprise has eroded away owing to sustained losses, or when the liabilities to outsiders exceed the total assets; a situation where the claims of creditors cannot be paid without substantial injection of fresh shareholders' funds.

Insolvent Financial Institutions: is similar to the insolvency of a bank; that is, a financial institution is insolvent when its capital base and shareholders' funds are eroded owing to persistent losses; but the difference is that unlike the insolvency of a bank where the central bank may step in as the custodian of the banking system, for a nonbank financial institution, this type of stewardship may not be available to the ailing institution and its owners may not be able to mount a rescue effort to prevent bankruptcy or closure.

Insolvent Partnership: a partnership business whose liabilities are larger than its assets and is unable to pay its debts when due, from its own resources. The liabilities of the individual partners are generally unlimited unless any particular partner has limited liability; banks when lending to partnership firms insist on obtaining a joint and several liability letter to make the partners personally and collectively liable for the loans or credits extended to partnership.

Instability of Financial Markets: is characterized by fluctuations in key interest rates or in market price of securities, stocks, shares, bonds and other financial instruments, adversely affecting financial returns and upsetting financial flows and market balance; or in commodity prices affecting, turnover, sales, liquidity and profitability; or in money and credit markets affecting availability of loan finance or investment finance, thereby adversely affecting businesses and companies, causing a reduction in their level of operations and profitability; or in foreign exchange markets affecting foreign trade and foreign capital inflows.

Installment: is a fixed periodic repayment of the principal, less than the whole amount due, paid by a debtor at successive periods in partial liquidation of a debt as stipulated in the loan agreement.

Installment Credit: on the lending side, a loan disbursed in more than one installment or tranche if the entire loan amount is not needed immediately; therefore, credit approval, actual disbursement of funds is tailored to the specific periodic requirements and funds are disbursed in installments accordingly; on the borrowing side a credit whose repayment are done in pre agreed installments.

Installment Payment: is repayment of a bank loan in periodic installments or partial repayment of debt in periodic payments; or staggered payments for expenditure, as agreed between the concerned party's before-hand, such as purchase of machine or equipment with some down-payment, while the remaining amount is repayable over a period of time.

Institutional Capabilities: overall capabilities of an institution, organization or company to perform by utilizing its managerial, technical and financial resources and capabilities of its staff; the institutional capabilities of a company may exceed or fall short of the objectives or goals if not managed properly.

Institutional Investor: a bank, a finance company, an insurance company, an investment fund or unit trust, a provident fund, a mutual fund, or a business company undertaking large portfolio investment in the financial markets, often exercising considerable influence over the market trends owing to their size and presence in the market; managing large amounts of deposits or savings, collected on retail basis, and investing them in money markets or securities markets; employing sophisticated market techniques, investment strategies, and exercising financial leverage, beyond the capacity of a single investor.

Instruments (Financial): a wide range of financial papers and documents used to facilitate a range of financial transactions such as receipts, payments conversion and transfer of financial obligations such as notes, cheques, drafts, bills and certificates; or instruments that facilitate securities market transactions and are central to funding and investment activities such as bonds, stocks, notes and certificates; financial instruments thus facilitate intermediation activities.

Insufficient Capital: for a financial institution or business, insufficiency of capital arising from a rapid expansion of their turnover, or from inordinate level of losses in their operations, adversely affecting their normal operations and insufficient to cover their long term financing requirements; may reflect the inability of the financial institution or the business to raise equity finance from institutional sources or equity markets.

Insurance Brokerage: providing services as an agent to meet insurance needs of the clients on one side and various insurance covers offered by insurance companies on the other side, involving determination of insurance costs, terms and conditions suitable to both the parties; also refers to the commission and fees charged for brokerage services.

Insurance Company: a company whose primary business is to issue insurance contracts and insurance policies which binds the insurance company in consideration of a premium to indemnify the insured against a contingent loss or an event such as accident or death; earnings of an insurance company are the premia it receives which are invested; the risks are the occurrence of the events and losses covered.

Insurance Coverage: is the amount and the extent to which a person, an item, or an event, or a loss is insured from the exact time and date the insurance is effective. In life policies, insurance coverage refers to the period from which the insurance is effective and the types of risks covered such as death or disability of the insured person; in general insurance, goods, property, or an asset is insured for a given period of time, commencing from the effective date of insurance against specified risks such as from fire, floods, civil commotion, and theft; in trade transactions where the goods may be in transit, insurance covers loss or damage to goods arising out of stated risks during transportation from a given place to a named destination by stipulated carrier and route.

Insurance Policy: is an instrument determines the benefits, coverage, and costs of insurance obtained as specified in the contract of insurance issued by the insurance company or its authorized agent; the policy may be effective at the time when the insurance contract is made or at a later date; or it can be effective prior to the issuance of the policy binder on the strength of an insurance cover note which indicates the time and date of insurance cover.

Insurance Policy Loan: a loan available to an insurance policyholder against the premiums paid or surrender value of policy; usually insurance companies or banks provide loan facility to the insurance policyholders against assignment of or a charge on the insurance policy.

Insurance Trust: is a trust established to receive on behalf of the beneficiary payments from an insurance policy and held in trust for a stipulated period; insurance trust is created to defer tax liability over a number of years, or to wait for the time on the beneficiary is capable of managing finances thus blocked into the trust.

Insured: various types of insurance coverage provided to the insured;

- ***Bank:*** insurance coverage of a bank's property, buildings, machines and equipment, against loss due to fire, civil commotion, theft and similar risks; or coverage for cash in a bank including foreign currency, whether in the strong room, cash counters or in transit.
- ***Deposits:*** bank deposits insured against the risk of insolvency or bankruptcy of the bank; normally covered with a deposit insurance scheme; in countries where such schemes are available, deposits in banks up to a certain amount are insured and if a bank is unable to pay its depositors because of insolvency or bankruptcy, the insurance company or the organization managing such as deposit insurance scheme, would pay the depositors up to the limits prescribed under the scheme; participating banks pay the cost of insurance, by contributing towards a fund in relation to their deposits which are insured; in some countries insurance of bank deposits is compulsory for all banks, while in others it may be on a voluntary basis, but in many countries such schemes are not available.
- ***Export Credit:*** insurance coverage extended to exporters against the risk of non-payment by importers. *(see Export Insurance Scheme)*

Insurer: an insurance company or an organization who insures, provides insurance cover against various risks, and issues insurance policies.

Intangible Assets: are invisible or non-physical assets of a company which add to the company's position in the market and may be instrumental in its success; for example, goodwill, trade marks, patent rights, leases and franchises; certain expenses which are capitalized such as promotional expenses and research costs are also sometimes categorized as intangible assets; these assets may have a value if the business is being sold as a going concern when its name, reputation, capabilities and rights may command a better price. *(see Tangible Assets)*

Intangible Net Worth: is the total value of intangible assets of a company representing the present value of excess earning power over the normal rate of return from tangible assets.

Integrated Banking System: is a system where banking operations and activities are interlinked and are uniformly regulated across the banking institutions, ensuring:

- uniformity in banking practices, procedures and provision of banking facilities, transactions and services through a broad-based network of banks.
- interbank flow of funds to optimize use of financial resources available to the banking system as a whole.
- a reasonable uniformity in the cost structure of banking services by type of financing or funding activity thus enhancing the efficiency of the banking system.

Integrated Financial Markets: are based on financial and operational inter-linkages between various types of markets, such as money market, bond market, government or corporate securities markets, and foreign exchange markets, ensuring harmonious market movements within a range around mainline trends; facilitating movements of funds and participants across various markets within rules, guidelines and procedures stipulated for the operation of these markets.

Integrity of the Borrower: is the financial strength and creditworthiness of the borrower, together with the track record of past practices and performance with regard to commitments, general reputation, and social status.

Integrity of the Banking System: is developed over a long period of sustained financial performance, good banking practices, sound banking record, and general reputation with regard to custodianship and safety of depositors' funds thereby acquiring public confidence, and attracting investors both domestic and foreign; refers also to the financial strength and health of banks in banking system.

Inter-Bank Deposits Market: is an inter-bank market for short-term, deposit-based funds facilitating placement of such funds among banks at a market determined cost, depending upon liquidity position of the banks participating in this market and their funding requirements; there is a difference between the inter-bank money market operations and inter-bank deposits market operations since in the inter-bank money market, two or more banks may deal in securities and commercial papers for adjusting respective liquidity position; and in the operations of inter-bank deposits market, placement and receipt of deposits are made for short-term; the rate of interest or return in both the cases, however, depends on the forces of demand and supply of funds in the market.

Inter-Bank Loan: is a loan taken by a bank from another bank; a short-term loan transaction between two banks, where the interest rate is unregulated; however, a long term loan from one bank to another is uncommon as resources available for long term are invested in securities and other assets.

Inter-Bank Market: is a market where banks amongst themselves raise or place funds, usually for short-term, at a rate of interest determined by the market forces reflecting availability or scarcity of funds, but usually higher than the prime rate, either to meet their liquidity requirements or to deploy surplus liquidity; banks may also discount securities and commercial papers in inter-bank markets.

Inter-Bank Rate: is the interest rate prevailing in the inter-bank money market; a short-term rate determined on the basis of market forces on a given day; it may change on a daily basis and is outside the direct purview of the controlling agencies such as the central bank; a good indicator of short-term bank liquidity levels.

Inter-Branch Accounts: is an account for handling inter-branch receipts and payments where branches debit or credit each other through one account opened in the branch books named as Head Office or Main Office Account, instead of opening and maintaining individual accounts for all other branches; all transactions pertaining to other branches are debited or credited in this account and the branch originating the transaction sends an advice to the other branch for counterpart entry; central office of the bank, where a centralized account is maintained for this purpose, is also advised of all the originating and responding entries regarding inter-branch transactions for reconciliation purposes.

Interest: is the user charge for borrowed money; it is a fixed amount of money, pre-determined in ex-ante manner, payable by the user for a specified amount of funds borrowed as a loan or credit, the principal, for a specified period of time; user charge for the loan funds thus obtained is called interest and is expressed as a rate, a percentage, typically for a year. The repayment of the principal and interest may be done in periodic payments by the borrower in installments as agreed, or in a lump sum at the end of the period.

Interest Bearing: those accounts, deposits, investments and securities which have an element of interest, as against those items which do not have interest such as current account deposits, or inters free loans.

Interest Coverage: is adequacy of income earned from utilization of borrowed funds to make interest payments.

Interest Coverage Ratio: provides a measure of the coverage of interest payments due from operating income, defined as earnings before interests and taxes (EBIT); indicates the margin of safety available to a firm with regard to interest burden on its borrowings; the higher of the firm but since repayments of principal is not included this does not approximately indicate the overall borrowing strength or solvency of a company shown by fixed charge coverage ratio. *(see Debt Ratios, Debt Management Ratios)*

Interest Expenses: is the total amount of interest on borrowings paid or payable by a borrower for a given period of time, say a year; for banks, this is a major item of expense and represents the interest payments to depositors, which is a direct cost of deposits as shown in the income statement.

Interest Income: is income earned from charging interest on funds advanced by a bank or any other financial institution; this is the main source of income for the commercial banks; it may be earned, realized from the borrower, and credited to the bank's income account; or entered in the accrued and unrealized interest account, but normally added to the principal amount borrowed, thus increasing the total liability of the borrower; in certain cases and after lapse of some time, unrealized or accrued interest is not credited to income account, rather it is kept in suspense account until recovery.

Interest Margin: is the interest income less interest expense; it is the difference between the total interest income and interest expenses, or the difference between average interest rates on loans advanced average interest rates on deposits; also called banking spread.

Interest on Average or Minimum Balance: is interest payment due on average balance in an account or on the daily balances in a given period, say a month; a basis for calculating interest payable on credit balances usually in savings accounts.

Interest Rate: is cost of using borrowed money expressed as a rate or a percentage of the principal amount for a period of time usually one year, the annual interest rate; the pre-determined fixed rate of return on saving deposits paid by banks, the deposit interest rate; the pre-determined rate of return on interest bearing securities or financial instruments, specified ex-ante, as a rate on principal amount. In Islamic Finance, there is no pre-determined interest rate, fixed ex-ante, or guaranteed ex-ante; instead, depositors share in the profit of bank; where financing by bank is done on the basis of sale and buy-back agreements for goods and bills under which the sale price is determined by adding a mark-up on the purchase price. *(see Islamic Finance)*

Interest Rates: are of various types on the deposits and loans, prevailing at a given time, depending on the terms and maturity structure, the type of financial institution concerned, and the market conditions.

Interest Rate Cap: is an upper limit on interest rate payable by a borrower, specified in a contractual agreement designed to cover the risk of an increase in interest rate on a floating rate loan or advance, and is the opposite of interest rate floor; the lending institution or a third party, such as a finance guarantee company, may undertake to cover this risk for a fee, thus protecting the borrower against future increase in interest rate beyond a ceiling, an upper limit, and paying the difference between the increased rate and the agreed rate on the loan.

Interest Rate Ceiling: is a restriction as to the maximum rate of interest which can be offered on deposits of various types or which can be charged by bank and financial institutions on loan and advances of different types.

Interest Rate Controls: is imposed by the government or the central bank restricting the movement of interest rate within a specified range; or specifying level of specific interest rates both on the deposits and lending; this controls may be temporary as a part of monetary and credit control program, or may be statutory, designed to regulate the structure of interest rates across the board, or may be specific to certain specific type of lending or deposit mobilization activities.

Interest Rate Differential: is the difference between the rate of interest applicable to similar financial activity or transaction but originating from different sources arising mainly because of controls, rules and regulations, or from different financial risks underlying the financial activities of the sources of origin, or from market rigidities and imperfections; in such a situation there would be a tendency for the funds to flow towards those activities or centers which can offer better interest rates if there are no restrictions on such transactions, thus reducing or eliminating the differentials; it also means the difference between the interest paid and interest rate charged on funds for the same tenure; for example, if a bank pays interest on a 6-month deposit at the rate of 8 per cent and charges 12 per cent on a loan for six months the interest differential for the bank is 4 per cent.

Interest Rate Floor: a lower limit stipulated in a contractual agreement to protect a lender against falling interest rates, or an interest rate option designed to protect earning assets against a decline in interest rates; for example, a financial institution, or a company for a fee may undertake to compensate its customer if the interest on certain securities falls below a standard rate, such as LIBOR; if the rate of interest on securities falls below LIBOR, then the company would pay the difference, but if the interest on security is at par or above LIBOR, then no payment would be made.

Interest Rate Futures: are financial contracts designed to hedge against interest rate risk by transferring the risk to investors willing to accept it for a return; these interest rate risks are covered with forward contracts, where the purchaser of the contract loses or gains if interest rates fluctuate; however, there is no futures market in Pakistan.

Interest Rate Liberalization: is removal or relaxation of restrictions on interest rates charged for loans and advances, or paid on deposits and other financial instruments, thus allowing the market forces to determine the interest rates depending on the cost of funds and returns on their uses; a major policy change away from a regime of fixed interest rates to optimize mobilization and allocation of financial resources on market rates and a re-aligning of the process of financial intermediation.

Interest Rate Options: are forward contracts to buy or sell a financial instruments at a price and at a future rate stipulated in the contract; also called fixed income option since the rate of interest of the financial instruments is fixed which pays fixed interest income to the holder of the instrument; the contract provides only an option, a right to buy and sell, rather than a binding obligation; the options are traded on securities exchanges, or over-the-counter market if issued by banks for government bonds, money market instruments or mortgage backed securities.

Interest Rate Risk: the risk arising from fluctuations in the market rate of interest as against a fixed rate of interest stipulated in a financial contract or embedded in a financial instrument, thereby causing a major change in the costs or returns.

- ***for the borrower***, the interest rate risk arises if the loan is obtained on floating rate of interest, pegged to a benchmark or an index of market based interest rate; if the market rates rise, the cost of borrowing will increase proportionally.
- ***for the lender,*** the opposite of borrowers' risk; namely, the risk in variable interest loans is that market interest rate will decrease over the period of loan repayment, causing a loss to the lender.
- ***for the investor***, the risk that fluctuations in interest rates my adversely affect market value of the security; for example bond, prices fall when interest rates rise, and vice-versa; or the return on investment may decrease in line with a decrease in market interest rate depending on the type of investment, maturity, size of differential and the type of exposure.
- ***for the saver***, the risk that a decline in interest rate will cause a loss if the saving instrument stipulates fluctuating instead of fixed interest rate and savers are unable to move funds into other types of saving instruments or actively participate in other segments of financial markets.

Interest Rate Spread: is the difference between interest rate on two opposite transactions; for example, if the interest rate on deposits is 10 per cent per annum and on lending is 15 per cent, then the spread is 5 per cent; if 12 per cent interest is charged to the borrower for a re-finance facility and the funds are reimbursed by the central bank at 9 per cent, then the spread for the lending bank is 3 per cent.

Interest Rate Structure: represents a heirarchy if interest rates, interlinked or pegged by underlying market trends, and are affected by monetary and financial policies, central bank rules, regulations, and discount rates, and overall financial and economic trends. A movement in the structure of interest rates is typically caused by a change in the central bank discount rate based on changes in major financial or economic trends; whereas changes in individual rates of interest may occur because of changes in underlying market conditions concerning only the relevant segment of the financial system. This rate structure is two-sided; one concerning rates of interest on deposits; the other concerning lending; and the difference between the two sides of this structure can be broadly interpreted as gross banking margin; but movements in both structures are interlinked and changes occur more or less uniformly depending on the changes in the base rate or the prime rate.

Interest Rate Subsidy: is extended by the government through specialized financial institutions or the banking system in general to certain priority sectors or borrowers such as exporters, small and medium enterprises, or an interest subsidy for agricultural and industrial development through below cost loans to the borrowers.

Interest Rate Swap: a contractual agreement between two counter-parties to exchange the respective liability for interest, but leaving the principal amount unexchanged. Swap pricing depends on the term structure of interest rate, spread and transaction cost of the swap and credit risk; but there are no fees or front-end charges in swap transaction, since at the outset the net present value of fixed or floating streams of payments is zero on which the swap is based. Swap is a hedging instrument based on hedger's expectations of future interest rates; a common type of swap is a coupon swap where one counter-party agrees to pay a fixed rate over the term of the swap in exchange for floating rate payment by the other counter-party; another type of swap is a basis swap involving exchange of a floating rate obligation for a floating rate instrument in the same currency; whereas a cross currency swap involves exchange of a fixed rate obligation in one currency for a floating rate obligation in another currency. *(see Swap)*

Interest Sensitive Assets (Liabilities): assets and liabilities whose financial value fluctuates with the changes in interest rates, mostly floating rate obligations, loans, deposits, and money market instruments; or interest rate indexed assets and liabilities where fluctuations in the interest rate are built into the rate structure of the assets, liabilities.

Interest Sensitive Funds: are funds which earn a floating rate of interest and are subject to changes in interest rate either at maturity or at the time of repricing based on an interest rate index or a benchmark interest rate. The borrowing and placement of such funds are directly influenced by changes in interest rates.

Interlocking Management: when CEO or the senior executives of one business organization also control or manage a number of subsidiaries of the parent organization, thereby exercising substantial influence on the business and operations of the entire group.

Interlocking Ownership: when a holding company, an institution, or an individual have substantial ownership in a number of businesses or companies, or have controlling shares, it is an interlocking ownership.

Intermediary Bank: is a bank acting as a third party channeling or facilitating transactions such as in cross border transactions; a third party bank may act as an intermediary either as a preference of a customer or if the originating bank and receiving bank do not have correspondent relation; or a bank arranging swap transactions on a fee basis such as interest rate swap or currency swap; or performing the function of an intermediary between suppliers and users of funds.

Intermediation: in general terms, it is an act of reconciliation, negotiation or settlement of a dispute between two parties handled by a third party who acts as an intermediary; but in banking, it is mobilisation of funds from the savers, the suppliers of funds, and lending to the borrowers, the user of funds.
(see Financial Intermediation)

Intermediation Costs: for a bank or a financial institution intermediation costs include mainly the cost of funds raised through deposits and borrowings, cost of lending and management of the loan portfolio, together with the cost of provisions for bad and doubtful loans, but excluding loan loss charges since these are one time charge to profit or shareholders' funds and an unusual cost item, and administrative costs including overheads; in this sense, for a bank intermediation costs are the same as banking costs; but for the financial system as a whole, intermediation costs also include system wide loan losses of all categories of financial institutions such as specialized development finance institutions, thus substantially increasing the costs well beyond routine banking costs. *(see Banking Costs)*

Intermediation Margin: is the difference between the interest cost paid to supplier of funds, and the interest or cost charged from the user of funds; in a business transaction, the margin of profit for intermediary services performed by a third party or an intermediary, known or unknown to the other two parties; also called gross margin on bank lending

Internal Audit: is an in-house system of audit in a company or a bank by its own staff members; the main objective is the routine periodic audit for detection and rectification of irregularities; functions as a watch-dog to ensure financial discipline of the company, particularly in expenditure control, income recording, cash leakages in transactions.

Internal Bond: is a bond issued by government or its agencies, in the local currency for sale within the country, as against external bonds which may be intended for foreign investors, and may be issued in other currencies or foreign markets as well.

Internally Generated Funds, Resources: are funds or resources made available from the operation of the company itself as against borrowings from outside; funds thus generated may be used in the routine operations of the business and a part may be set aside as reserves or retained income for special purposes, contingencies or for future expansion.

Internal Rate of Return (IRR): is a rate of discount pertaining to investment in an asset or in a project, where the present value of expected cash inflow from the investment is equal to the present value of expected costs of the investment; the IRR; if calculated for a number of investment proposals, IRR facilitates investment decision making as it provides a method of ranking alternative investments.

International Debt: *(see External Debt)*

Inter-State Banking: are banking operations between states within a country which has many states with their own banking laws and regulations; for example, in the USA, banking transactions involving more than one state or transactions between banks of different states.

Interventionist Approach: if the government policies, rules and regulations loose their neutrality between market participants or between market-based results and begin to favor one over the other, then the government is said to have adopted an interventionist approach, or assumed an interventionist role; for example, in the operations of financial markets and banking system, interventionist approach implies enunciation of rules, regulations and directives aimed at controlling or affecting financial intermediation activities such as the system of directed credit adopted to affect the flow and use of credit; it may involve segmentation of certain banking functions based on the type of a bank, or the type of institution; interest rate controls and credit ceilings; for the financial markets, interventionist approach means controlling or redirecting the market mechanism to favor certain outcome or certain trends which may not materialize otherwise if left for markets to determine.

Interventionist Role: is the role of the central bank or the government authorities to maintain financial or economic stability through interventions in the operations of the banking system and financial markets, or in selected economic activities.

Inventory: consists of the stock on hand, or merchandise in transit with title thereto, at a particular point in time; in trading companies, it refers to the stock of merchandise on hand for resale; in manufacturing companies, it includes raw material, work-in-process and finished goods; merchandise sent on consignment may also be treated as part of inventory; inventory of financial assets such as securities, shares or other assets owned and held by a company or individual.

Inventory Cost: is the cost of purchase or acquisition of goods for sale, or the cost of raw materials and inputs acquired for final product paid, plus all related costs; for example, packing, cartage, transport, taxes and duties paid, incurred up to the time goods are stored or received at the company premises.

Inventory Cycle: is the process of turning the raw material into finished goods via work-in-process, semi-finished goods, and final products available for sale; the cycle begins with the acquisition of raw materials inventoried, and ends with sale of inventoried products.

Inventory Days on Hand: in manufacturing companies the volume of inventory retained in the factory in relation to the number of days it would last; a longer period of inventory retention would be a comfortable proposition for the factory manager but is more costly for the company; whereas lesser days inventory on hand that is, lesser time between the receipt of inventory and its use, would be less costly, but needs more efficient inventory management.

Inventory Finance: are loans or advances obtained to finance the cost of inventory for a short period, covering the inventory cycle against inventoried items pledged as collateral or against receivables; the loan is paid-off at the time of sale.

Inventory Period: is the time span during which inventory is acquired, processed and turned into finished product and held for sale; inventory period is an important factor in determining production costs, since a longer inventory period would block the resources of the company increasing the costs, and a shorter inventory period would minimize the costs; one of the important factors of Japanese automobile manufacturers' success is their shortened inventory period as compared with their overseas competitors.

Inventory Turnover: is the number of times the inventory is acquired and sold in a given period say a year, or how many times cash spent on purchases is turned back into cash by sales; a higher turnover of inventory may indicate larger sale revenue and more income from given resources but it may also mean inadequate inventory level; a low turnover may point to overstocking, obsolescence or poor quality of marketing.

Inventory Turnover Ratio: is the ratio of sales to inventories, indicating the effectiveness of sales strategy of a business and its inventory management which is a major factor in keeping the cost of sales down, thus enabling the company to keep prices lower and enhance its price competitiveness in the market; from the perspective of asset management, this ratio provides a measure of effectively cash resources are prevented from being tied up in inventory, and thus reducing overall financial costs of sales and inventory.
(see Turnover Ratios, Ratios)

Inventory Valuation: is the determination of the value of inventory through several accounting methods for valuation such as LIFO, FIFO, weighted average method, but the standard accounting practice is to value the inventory at cost, based on one of the above methods or market price, whichever is appropriate.
(see LIFO, FIFO)

Inverted Yield Curve: the inversion of the yield curve occurs when short term interest rates are higher than those for the long term; if a diagram is drawn showing percentage of yield on an investment on the vertical axis, and maturity periods on the horizontal axis and applicable yields are marked period-wise, then the points joined in a curve will have an inverted or concave appearance; this phenomenon is observed when interest rates are rising.

Investment(v): is acquisition of financial, physical or technology based assets by an investor for their potential future income, returns, yield, profits, or capital gains, which, unlike interest rate, cannot be pre-determined or guaranteed in ex-ante manner, instead, are determined or realized ex-post only if the venture, the business or the investment activity is successful and generates positive cash flow, income, returns or profits; in the process, investor accepts a variety of risks and a potential for loss associated with the investment being undertaken.

Investment (n): is the amount invested; it is financial volume of assets held as investments for various maturities or duration such as property, stock of companies or bonds.

Investment, types of: classified by:

- ***type of investor***; private investors of all types engaged in private investment activities; or government, its agencies and institutions engaged in public investment activities.
- ***origin of investor***; domestic or foreign investors, who make investments in domestic or foreign currency.
- ***term of investment***; short term investment is usually portfolio based through money markets, or medium and long term investment in physical assets or in stocks, bonds, shares traded in capital markets.
- ***type of investment assets***; a large variety of financial assets available for portfolio investment through securities markets in stocks, shares, bonds, or through money markets in a vast range of financial papers; physical assets such as capital goods, machinery, plant, equipment, building and facilities; technology based assets concerning trademarks of new products, new innovations, new processes or research and development; undertaken directly by investors of all types or indirectly through a variety of investment facilitating institutions.
- ***scale or size of investment***; small and medium scale investment usually undertaken by SMEs, households or individuals; large scale investments undertaken by institutional investors, corporations, companies and large businesses, or the government in the public sector.
- ***sector of activity or uses***; manufacturing, transport, infrastructure, trading and distribution, real estate, or service industries, or in social sectors such as education and health both by the government, the public sector, or by the private sector.
- ***type of investment finance***; such as equity-financed investments, bond-financed investments, loan-financed investments; own-financed investments from existing shareholders' funds, or internally generated funds, as against investment financed from externally generated funds through securities markets, sale of shares or bonds, or borrowings.

Investment Account: an account opened by an investor or customer with a bank or a financial institution and the funds available in the account are invested and managed by the bank at its own discretion, or where the customer is advised about the investment opportunities and the transactions are conducted by the bank on behalf of customers.

Investment Advisor: a professional investor or a brokerage company, who provides advice to the customers on investments and assists with placements in securities markets; these service may cover only advising and counseling on investments, or may be extended to handling, processing and management of investments of the clients.

Investment Banking: a type of banking undertaken mainly by investment banks, where the main business is providing long term finance to investors, equity contribution, underwriting new share issues, and buying of securities from the issuers for subsequent sale, usually at premium; investment banking services include advising the customer on investments or managing investments on behalf of its customers; this type of banking business may be restricted to investment banks established specifically for this purpose, or commercial banks may also be allowed to undertake these activities.

Investment Company: a company whose business is to invest funds principally in securities so as to diversify investment risks over a large portfolio and to provide its customers the benefits of professional fund management; a charge on the transactions on behalf of its customers is the source of income for the investment company.

Investment Fund: a financial institution or an investment unit specializing in the placement and management of investment portfolio on behalf of their clients such as a unit trust fund, a mutual fund, or an investment trust corporation; financing or funding allocated for investment purposes in a budget or in a financing plan; funds generated internally or externally for investment purposes and set aside in a separate account.

Investment Expenditures: are undertaken to enhance the capital base; or expenditures incurred to acquire new facilities, or to modernize existing plant and equipment, or to replace depreciated capital stock, so as to augment productive capacity and increase output at the firm, sectoral, or the country level; or expenses incurred to facilitate new businesses or expansion of existing ones; or amounts invested in new assets to secure future income, return, or profits.

Investment Incentives: a range of incentives extended by the government to seek out and encourage private sector investment, domestic or foreign, primarily aimed at enhancing profitability of new ventures; or to facilitate investments through assistance with long term financing, liberal tax incentives, commitments for easy repatriation of profits and equity for foreign investment, removal of barriers, and a cut-back on administrative and procedural requirements.
(see Incentives)

Investment Loan: loan or credit made available through the specialized financial institution or through general banking system specifically for investment purposes under terms and conditions conducive to investor but generally within market guide posts typically for medium to long term.

Investment Portfolio: of a bank or a financial institution or a business or an individual consists of investments in a variety of assets, mainly financial assets such as shares, stocks, bonds, government or corporate securities, bills, commercial papers and other financial instruments, real estate and investment in property. Good management of investment portfolio is critical for the overall profitability and addition to networth of the investor, even though it may not be the main business activity of the individual or the organization concerned.

Investment Program:

- ***of a company***, a business concern or a large corporation, consisting of investment expenditures within a time slice, typically the budget year, on new facilities, plant, machinery and equipment, involving expansion or replacement expenditures of existing production facilities; or acquisition of new businesses, expansion of the group of companies under a holding company, and buy-outs.
- ***of a government,*** undertaking expenditures as a part of public sector investment program covering a budget year or longer, aimed at expanding the productive base of the economy and the sector or sub-sector involving items like infrastructure, water and power development, expansion of major sectors like agriculture, industry; or investment in human resources through expenditures on education and health facilities.

Investment Risks: are risks associated with an investment activity and culminating into loss for the investor if not properly managed, or a reduction in profits and returns from the levels anticipated by the investor; consisting of risks like delays in the start-up of the business, cost over-runs beyond the control of investor; lack of or delays in the availability of ancillary facilities like power supply, transport facilities; an unanticipated reversal in market trends; labor strife and lock-outs; or nonperformance by others, who are a party to the investment.

Investor Confidence: the confidence of the investors in the creditworthiness of the institutions issuing bonds and securities based on the type of the borrower or the type of securities; such as bonds and securities issued by the government directly or by its agencies and guaranteed by the government; or confidence built up over a number of years by issuing company's financial strength, integrity and capability to earn profits.

Investor Safeguards: are protective legal or financial provisions, mitigating the risks to investors; general safeguards protect the integrity of investment assuring ownership and control, and safety of investments against seizures and lock-out; specific safeguards, mostly financial, are tailor made to each investment activity, providing various types of assurances for returns on investment through guarantees, pledges, or financial covenants.

Invoice: a list of goods sold showing the description of goods, quantities, prices including unit prices, total and the net amount payable after taking into account any deductions on account of discounts and additions of cartage, freight, packing charges, tax, and insurance.

Involuntary Lending: occurs when a lender is forced to extend a loan bypassing its routine rules and procedures of lending; such a situation may arise if the lender's exposure to the borrower is fairly extensive, and at the same time the possibility that the borrower may become insolvent if the loan is not extended; the lender then is faced with the unpleasant choice of compromising its lending standards to keep the borrower afloat, or the disastrous choice of a major loan loss implied in the denial of the loan owing to the bankers' exposure if the borrower then becomes insolvent or bankrupt; some bankers consider this type of loan as throwing away good money after bad money; others regard it risky but potentially a rewarding action if indeed the borrower is able to pull out of imminent insolvency; involuntary lending, however, is a phenomenon better understood in the case of large and influential borrowers such as major corporation or involuntary lending enterprises of strategic significance for the economy as a whole, whose failure may have a serious country-wide impact, forcing the government to arrange syndicated loans on terms and conditions considered out of routine; or sovereign borrowers with massive exposure to commercial loans in foreign currencies extended by multinational banks or even ordinary banks where insolvency is not the issue, rather foreign liquidity crunch of temporary or recurring nature need to be funded through syndicated loans, again, on terms and conditions out of routine arranged under the umbrella of debt rescheduling, or under a multi-bank agreement with new net exposure to the sovereign borrower, which in effect is the amount of involuntary lending.

Islamic Finance: is a system of finance based on Islamic principles and governed by laws and rules called *Shariah;* currently Islamic finance is being practiced in one form or the other in 46 countries and growing rapidly. The central tenet of Islamic finance is prohibition of *riba*, literally meaning an excess and is interpreted to include usury, interest charge, or any pre-determined and guaranteed return tied to the principal amount borrowed and maturity of the loan regardless of the business performance and investment outcome; this prohibition of *riba* conforms to

the Islamic principles of social justice, equity, property rights and injunctions against exploitation of the weak or the disadvantaged. In Islamic finance, profits, based on risk sharing are encouraged, since profits are determined ex-post symbolizing business success entrepreneurship and wealth creation; but interest charge is prohibited as *riba*, if interest is determined as ex-ante and is an accrued cost, irrespective of the outcome of business operations or investment which may not create wealth if there are losses. The tenet of Islamic social justice as applied to finance requires that both the lender and the borrower share rewards, risks and losses in the process of wealth creation. Thus in Islamic finance:

- suppliers of funds are investors instead of creditors, whether they be financial institutions, companies, or individuals; savers or depositors are providers of these funds on profit and loss sharing (PLS) basis.
- liquidity, deposits, or funds held by financial institutions on behalf of savers are potential capital and become earning asset only when converted into equity finance.
- investable funds thus generated can be used only in those businesses that do not violate laws and rules of *Shariah*; and
- to safeguard against moral hazard and risks of asymmetric information, disclosure is asserted with penalties prescribed by *Shariah* for non-compliance.

Islamic finance is therefore more like equity-based trade financing, or trading company finance like supplier's credit, or investment financing as in market based investment banking, but the critical difference is replacement of interest charge with profit and risk-sharing on both sides of the balance sheet of the financial institution thereby ensuring stability of the system; on the liability side of the financial institutions, deposit liabilities are replaced with Profit or Loss Sharing (PLS) funds where savers or depositors, the suppliers of funds take the PLS risk; on the asset side, loan portfolio is replaced by investment portfolio with equity holdings or partnership where the risk of investment is shared by the intermediary institution as investors, and these risks are passed on to the PLS account holders or clients undertaking investments.
(see Financial Instruments, Islamic Finance)

Instruments of Islamic Finance: these instruments both on the supply side of funds and usage side of funds are predicated on the basic principle of Islamic finance that financiers should participate in the funding arrangement on equal footing covering both profits and losses, instead of participating only on the basis of a pre-determined return; on the side of supply of funds, savers and depositors maintain profits and loss sharing (PLS) accounts with financial institutions regardless of the tenure of the deposits; this stipulation considerably restricts the

variety of deposit instruments available to the savers; on the side of usage of funds, there are several instruments as described below stipulating that the financier participates in the profits and losses of the business venture being financed through various types of sale contracts. This principle adds business risks to financial risks because the mode of financing through these instruments is such that the financier has to assume business risks associated with the funding activity thereby enhancing the overall risks of the financial exposure. This participation, however, ensures proper use of funds and the risk of misuse is considerably mitigated; but the drawback is that such funding activities force the financier to become first an active trader and then a financiers; besides these are transactional finance unlike a line of credit which is a source of readily available finance regardless of the business activity being funded. These financial instruments need customization for each type of transaction regarding their terms of participants, thereby significantly adding to the cost of funding activities and their risks; therefore funding cannot be bundled into financial packages through these instruments to meet the diversified needs of modern day business activities.

- ***Bay'el-mua'ajjel:*** is trade financing through a sales contract executed by the financier as a seller for spot delivery of traded items but with deferred payment as a lump sum or in installments for an agreed period; thus the seller also assumes the role of financier; but to be a seller the financier must have the title to the goods being sold and must have their possession; in effect, the financier must be a trader first then a financier; under the contract the seller can ask a price for credit sale higher from the price of cash-sale; in case of credit sale the sales proceeds provide the profit margin or the cover for the financed amount on pre-determined terms; therefore, the price of credit sale includes cash price plus a premium or mark-up for deferred payment which is predetermined and bundled into credit price; the maturity period is defined as per credit sale agreement and it may vary from a short period of a few months to a few years depending on item traded or the financing cycle; finally, since the traded item has already been delivered on spot, it cannot serve as security except if it is a fixed asset; therefore, in case of non-performance by the buyer the only recourse available to the seller, the financier, is the general business operation of the buyer or any other security specified in the sales contract; but the rules of *bay'el-mua'ajjel* stipulate that in the event of the default of deferred payment, the buyer may be asked to pay a penalty, but not to the seller rather to a charity; hence default penalty does not accrue to the creditor, and does not redress his loss; in effect, the seller has no meaningful recourse against default even though the buyer may have furnished a security or a lien on other assets, because by the time default occurs these assets may or may not remain performing assets.

- ***Murabaha:*** is similar to *bay'al-mua'ajjel*, therefore, all the above stipulations apply; it is a trade financing instrument for item-based trade with a mark-up or cost plus sale, where the financier as a seller undertakes to supply specific items being traded under a contract for sale to the client at a mutually agreed price including the cost and a mark-up or profit margin; as in *bay'al-mua'ajjel*, the financier becomes party to the trade, purchases the traded item from the original supplier or the manufacturer, takes title and possession of the goods being traded, and then sells it to the buyer; the financier may make this customer, the buyer, his agent to buy the goods on his behalf and take possession, though the transaction remains the risk of the financier; the price, however, is fixed and agreed at the time the contract is executed and the financier is allowed to charge a mark-up on cost plus basis and this may include a *consideration* for deferred payment; but after the goods have been delivered and if the seller has not been paid and there is a default there is no meaningful resource available to the financier as explained above, except the general resource of business operations of the buyer.

- ***Bay'es sala'am:*** is trade financing under a sales contract for advance payment on deferred delivery; it is similar to a forward contract where the buyer pays the seller the full cash price in advance for future delivery of goods and thus becomes financier to the seller for the contract period; after the goods have been produced and delivered the financing buyer can sell at the market price; thus, in effect, the financier becomes a trader in commodity futures market which are very risky markets, and thereby the financier assumes a major business risk in case deferred supply does not materialize, or delivery occurs when the commodity market has taken a downturn and the final sale price is below the price paid at the time of advance payment; *sala'm* is often described as raw material purchase financing or agricultural credit based on the crop cycle, but inherently this financing carries both the risk of non-performance as well as the risk of future market price; there is no effective or specific security against non-performance because traded item may or may not get produced or delivered; it does not exist at the time of contract, it is yet to be produced or manufactured; however, the financier may secure a pledge on other assets or business operations of the client, the future supplier; the maturity period may or may not be specifically dated in the contract depending on the production cycle of the item concerned but and may not be enforceable.

- ***Mudareba:*** is a profit sharing arrangement similar to investment funds where one party provides investment funds, the investors, and the other party consists of the managers who manage investments on the basis of a proportional share in profits. Investments are allowed only in activities

approved by *Shariah* with profit, loss and risk sharing arrangements stipulated for each investment activity; *mudariba* may be a multipurpose investment company or a single purpose company created to finance a large investment such as investing in a factory or a plant; in case of multipurpose *mudariba*, the selection of investment activities is done carefully to ensure that profit accruing to *mudariba* is not tainted with interest or interest-like income from the business activities of the clients; for example, investment by *mudariba* in those investment trust units is not permissible where interest-bearing instruments are part of the unit's investment portfolio like bonds or guaranteed notes payable with interest; the profit from investment is shared among the investors in strict proportions based on the size of their investment and agreed to among them at the time of participation; but investors are not allowed a pre-determined *amount* from profit; if there is a loss, it is limited to the invested amount, the exposure of the investor. Thus, *mudariba* is not activity-based investment financing, rather it is participation in a pool of investments where risks of investment are spread over a large number of investment items in the portfolio funded by *mudariba*; the share-holders can sell-off the shares back to *mudariba* or in the secondary market if it exists; therefore, a multipurpose *mudariba* is more like a close-ended mutual fund where the net-worth of *mudariba* depends on investment performance of its managers, and secondary market conditions.

- ***Mushareka:*** is a mode of equity finance with active participation of investor in the management as well; it is similar to a joint venture where the investors as owners contribute capital and fixed assets, machinery, equipment, and working capital, together with technical and managerial expertise; thus, *musharika* is a true partnership in investment as well as in business operations for medium to long term period; it is activity based investment financing where financing and investing both are combined into a single activity, making the financier a shareholder but the exposure is not limited to financed amount since it is a joint venture and not a limited liability company; therefore, *musharika* may have open ended liability where both the share in profits and liabilities of loss may not be proportional to the amount invested; in case of business failure and if *musharika* goes under, all liabilities in excess of remaining assets are to be shared proportionally by the partners.

- ***Ijara:*** is lease financing under a leasing contract charted out along the lines almost identical to currently prevailing leasing practices and procedures and therefore, is the same as routine leasing business; lease is for a specific item whose ownership is retained by lessor, with pre-specified leasing costs over the lease period, where privileges and obligations of both the parties to the lease are spelled out in leasing contract which legally binding on both the parties, with usual recourse and remedies.

- ***Istisna'a:*** it is project based investment financing with ownership, where funding and project implementation are combined into a single activity on profit and loss sharing basis; for example, *Istisna'a* could be housing finance with contractual obligation tendered by the financier to produce and deliver a housing unit to the buyer at a pre-agreed price, whose payment by the buyer may be in full or in part at the time of contract as advance payment, and the remainder as deferred payment on delivery, or as installment over a contractual time period; but unlike mortgage payment where interest and principal amounts are separately stipulated, this pre-agreed price at the time of contract presumably includes costs of construction plus a profit margin; the time of delivery is specified, so is payment date if it is deferred payment, or installment dates if it is installment payment. The difference between *Istisna'a* and mortgage finance is that in **Istisna'a** the financier is foremost a supplier or a builder who extends financing to the potential buyer on mutually agreed on pre-determined terms and conditions of payment for the purchase bundled into the purchase price of the dwelling together with contractual performance stipulations; whereas in mortgage finance the financier may or may not be builder or contractor, and title of ownership is with the buyer and it provides the collateral for mortgage loan.

Issue Guarantee: a third party, entering into a guarantee obligation, thereby committing to the liability of the obligation for nonperformance by the original party concerned.

Issuer: the authority or the organization issuing a security, a bond, a certificate, a debt instrument or a share; may be a government, a public sector authority, or a corporation who has the financial base and is licensed to undertake new issue the issuer is responsible for managing the securities and, in case of debt securities, to pay interest when due and pay the principal amount on maturity on its holdings of the new issue.

Itemized Cost: reporting the cost of all individual items of an article or service in a given statement; for example, itemized cost of 'goods available for sale' will show separate costs for inventory, wages and factory overheads; and factory overheads may again have itemized costs of facility operations such as fuel and power, maintenance, taxes and other items.