ICanDo
Financial Planning

Swapna Mirashi

ACADEMIC FOUNDATION
NEW DELHI

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Foreword

The global financial crisis has challenged many of our convictions and beliefs about the financial sector. But some fundamental notions have survived even such a deep Schumpeterian catharsis. Among the survivors is the belief that financial literacy is important in both developed and developing economies alike. There is virtually no country that has developed and matured without a corresponding deepening of the financial sector. And such deepening is possible only when individuals and households are financially literate and are able to make informed choices about their savings and investments. Indeed it is possible to argue that the sub prime problem would not have grown to the explosive proportions that it did if people had been financially more 'literate'.

2. India clocked average growth of nine percent in the period 2004-08 before the global financial crisis interrupted the growth trajectory. One of the key drivers of this growth has been the increased savings rate in the economy. The increase in savings itself has been a consequence of the changing demographics and the welcome trend among households of shifting from physical savings to financial savings. In order for us to achieve the double digit growth that we aspire to, it is critical that the savings rate in the economy not only reaches the pre-crisis level but surpasses it. This will require both supply and demand side conditions to be met. On the supply side, our financial markets need to design and supply product that households with low but growing incomes can use. On the demand side, we need to make people financially literate so that they know what they want and are equipped to make choices from among the wide array of financial products on offer in the market.

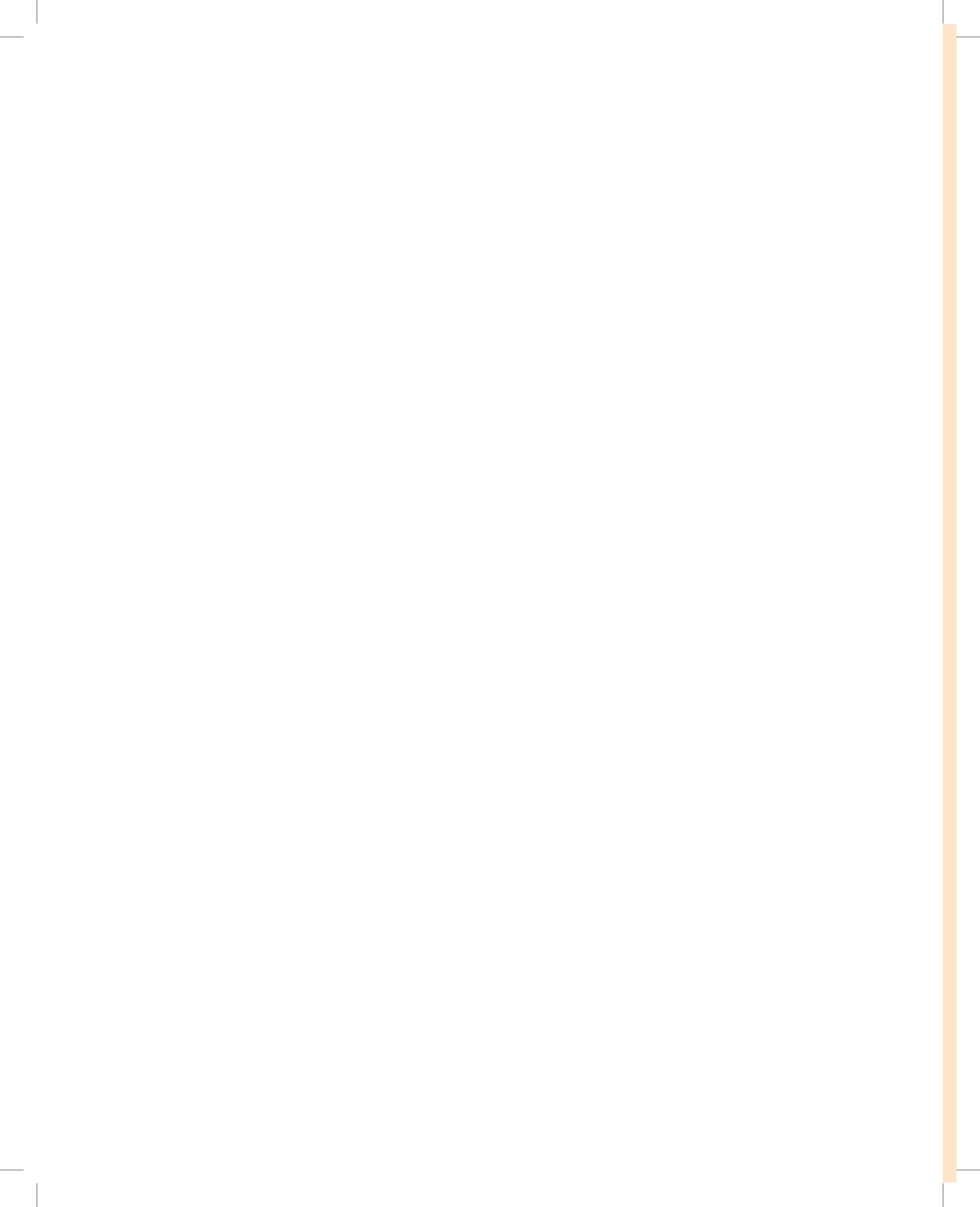
3. Nurturing and encouraging these supply and demand side initiatives is at the heart of the Reserve Bank's 'Financial Inclusion' initiative. We want our financial markets to innovate products that combine 'safety, return and liquidity' to meet the needs of low and middle income households. We also want our households to be financially literate so that they can make decisions on what, when, how and where to save. There are obviously several ways of widening and deepening financial literacy and the mode and method depend on the targeted audience. The Reserve Bank endeavours to reach out to every type of audience through its several initiatives.

4. This book in your hands, *ICanDo* Financial Planning, is a valuable addition to the several ongoing efforts of the Reserve Bank towards enhancing financial literacy. It is aimed at youth who are just about getting into jobs and careers, and who will have to wade through a complex array of financial products and make judgements. It is an attempt towards educating the readers on the importance of thrift and equipping them with the skills of planning and budgeting for a financially secure future. Written in an easy style and simple language with live examples, the book's central message is that people can improve their financial security through defining their financial goals, then drawing up and implementing a savings and investment plan to achieve those goals.

5. There are several books and readings available on financial planning. This book's USP is that it allows you to read it and use it in a flexible way since each topic and chapter is practically self-contained. I hope you will find this book to be a rewarding learning experience and helpful in your financial planning.

D. Subbarao
Governor
Reserve Bank of India

Mumbai
March 22, 2010



Wish more, at the toss of a coin!

“We need to repair and renovate our house,” Ramesh suggested to his father.

“But we do not have money for that this year,” his father objected. “Your sister is getting married this year and so are you. Plus there hasn’t been that good earning from the farm. We will have to spend more money on irrigating the land. And do not forget the medical bills. Your mother needs an elaborate treatment for her asthma. House repair can wait till the next year.”

Ramesh realized that it was indeed not possible at the moment to think of any further expense. But he also believed that repairing their house was a big need too.

Ramesh, a 25-year-old mechanical engineer, had set up a small farm equipment repairs business in his village just a year ago. With a bank loan, his engineering degree from a reputed college and a 2 year work experience in a factory in a big town, Ramesh was confident about making his venture successful. His business kicked off well as farmers no more needed to travel outside the village for repairs and were happy with Ramesh’s services. And now, Ramesh wished he could make those little changes that could improve his family’s quality of life.

But Ramesh’s family did not have much fund in saving. And just one year in business, he was barely managing to repay the installments on time from his profits.

‘House does need repairs. Am I going to get my bride in this old tattered house?,’ Ramesh thought to himself, as his father left. ‘But father has a point. Where can we get all this money from?’

He was not sure if he should borrow the money from friends. ‘It will not look good.’

Just as he was consumed by the thought, he was reminded of somebody who could help. He ran towards a well in front of the village school, reached for a coin in his pocket and tossed it.

*

It was not long ago. Just more than a year back, as Ramesh was heading back home from the big town where he worked, he passed by this well. The sight of the well, in front of his primary school, took him back to the fond memories of his childhood and the well. Just then something happened that bothered him. He saw a few school kids throwing biscuit wrappers in the well. Before he could stop them, the damage was done and the kids had run away. When Ramesh peeped in the well, he saw a whole lot of garbage dumped inside. Ramesh was disheartened. This was a sacred well for him. It used to be clean and had quenched his thirst many a times in the harshest of summers. Ramesh decided to clean it up and protect it from any further littering.

The very second day in village, Ramesh spent cleaning the well and constructing a garbage bin in front of the school. Just as he sat down to relax under a tree, he saw a thick fog emerge from the well. As the fog scattered, a man in white robe emerged. The man looked regal, with a bright aura around his majestic figure.

“Hello well-wisher,” the man said in an authoritative tone, “you made me happy by doing good to my home-this well.”

“Who are you? And do you stay in here?” Ramesh quizzed.

“Well, not always but you can say this is my holiday home,” the man answered, with a smile. “As for who I am, they call me Sri Wishkar as I fulfil wishes of do-gooders. Why don’t you give me a chance to fulfill your 3 wishes as a token of gratitude?”

Ramesh was taken aback. He did not know what to say. But simple yet smart that he was, he asked for some time to think. “Can I think about it and ask as and when I need something?” he asked.

“OK” Sri Wishkar agreed, after a pause. “Just toss a coin, whenever you have a wish for me and I shall appear to grant it to you. I owe you 3 wishes. Keep doing good, young man,” said Sri Wishkar, and disappeared.

*

"Hey well-wisher. You kept me waiting. It has been a year. Tell me what I can grant you?" Appearing from the well Sri Wishkar asked Ramesh.

Ramesh told him his wish of renovating his house, and voila, it was granted to him in no time. Ramesh got a repaired and renovated house.

Years passed by. Ramesh's small business did well, just as it did in the beginning. He had earned himself a good life, a happy family and a reputation of being a wise gentleman in the village and around. His daughter was studying law in a nearby metro town. And his son wished he could study medicine abroad. Studying abroad meant huge expenses. Ramesh was just not ready for them. But his son was a bright student and he did not want to compromise on his children's future.

Ramesh's good deed that had allowed him 3 wishes from Sri Wishkar, came to his rescue this time as well. Sri Wishkar granted him his children's higher education (and subsequently a bright future).

"You are a smart man Ramesh," Sri Wishkar commented after granting Ramesh his second wish. "But, I hope you do not make me wait another 20 years for your third wish." Both laughed.

"Oh no, my lord, you have indeed helped me in time of my need," Ramesh answered, "I would not have been able to do what I did, had it not been for you. Now, I want you to grant me my third wish as well."

Wishkar listened as Ramesh spoke. He was curious what his smart do-gooder had on his wish list now.

"I am thankfully doing well," Ramesh started to talk. "My small business is good enough to support me and my wife currently. My children, thanks to you, would do well for themselves with their priceless education. What I now wish from you is that you provide for my wife's financial needs when I am no more to take care of her. I do not want to leave that to my children. You never know how situations develop. I want my wife to live with dignity and peace. I hope you can grant me this last wish of mine."

"Of course, wise man!" Sri Wishkar was delighted at Ramesh's request. "You have used my powers judiciously and I am happy that I granted you your wishes. May there me many such Ramesh in this world," said Sri Wishkar as he disappeared.

*

Ramesh, with his good deeds and wisdom, could get his family a stable, peaceful living and a bright future. We may not bump into Sri Wishkar (though that should not refrain us from doing good deeds) and have our wishes fulfilled at the toss of a coin. But that should not hold us back from having a stable, peaceful living, and a brighter and wealthier future. All we need to do is foresee life's challenges and opportunities and plan for them, coupled with an 'ICanDo It' attitude.

This handbook would be your partner in planning for your financial well-being. So if Ramesh had Sri Wishkar by his side, you now have 'ICanDo' by yours. Wishkar granted Ramesh his 3 wishes. ICanDo will help you plan to achieve all your financial wishes (goals). But just as Ramesh, you would need to use your wisdom and ICanDo's powers judiciously to see its benefits.

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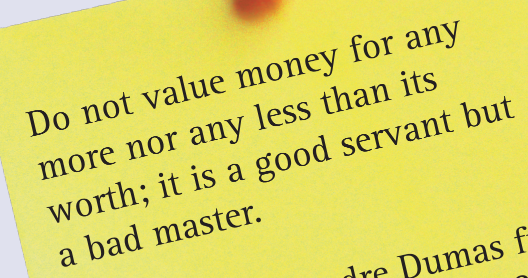
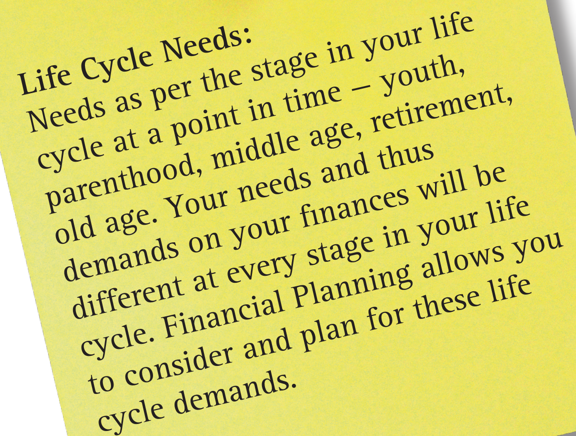
Introduction

Financial Planning



Having your own money in your hand every month does not guarantee you the lifestyle you deserve throughout your life. Circumstances and needs always keep changing. Today's sound financial situation does not guarantee an equally sound future. And hence, no or improper financial planning can be disastrous. A loss of income, even temporary, can eat into your savings or can lead to debt. An uninsured loss can wipe out your accumulated wealth. Insufficient savings can force a reduced lifestyle during retirement. Frequent or unplanned borrowings can leave negative money i.e., debts for future. Also, poor tax planning can result in paying higher taxes than what you are liable to pay. All this, combined with changes in your life cycle needs and/or external economic changes can make you and your future generations financially vulnerable.

You would need to plan and manage your current income (the money you earn today) and your future income (money you can expect to earn in future) according to your life cycle needs. A proper financial planning will help you achieve financial freedom, when you would no longer need to work for money, instead your money would work for you.



What is Financial Planning?

Financial planning is a process of planning and managing your money (current finances) to meet your life goals. Your current finances would mean everything that constitutes your money today—income, expenses, savings, assets and liabilities. Your life goals could be higher education, buying a house, planning for retirement, saving for marriage/child's education.

Proper and timely planning of your personal finance is important to achieve financial security throughout your life cycle, and to build wealth.

Right Time to Start Financial Planning

The moment you get to know about financial planning or realize that you need to have a plan, is the right moment to start financial planning. The earlier this moment arrives in your life the better. **Therefore, young people who have just started to earn can make the best of this tool.**

Yet 'better late than never' is an equally appropriate phrase for those who have not yet started planning their finances, but now wish to have money for everything—children's education, clearing debts, secure retirement and emergencies.

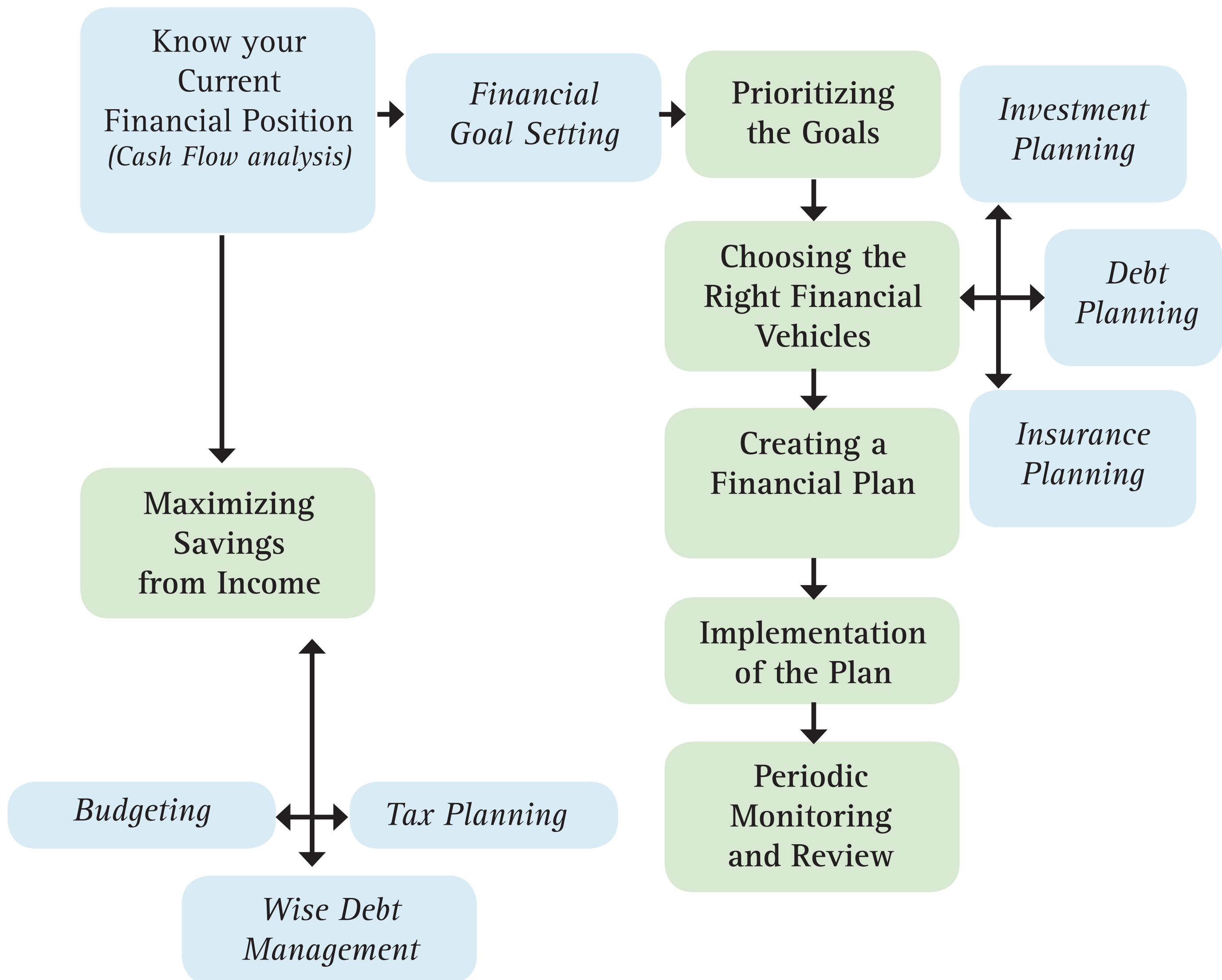
Who Should do your Financial Planning?

There is no one more qualified to do your financial planning than yourself. Professionals like financial planners, wealth managers or even chartered accountants can help you with some parts or all of your financial planning. But the effectiveness of your financial plan and its significance to you would be only as much as your involvement in making it.

Key components of financial planning

The outcome of financial planning is a financial plan. Like a roadmap, a financial plan should guide you through the key milestones of your road trip towards financial freedom. The key components of financial planning are:

1. Cash flow planning or money management.
2. Tax planning.
3. Investment planning.
4. Insurance planning.
5. Retirement planning.
6. Debt planning and management.



Common Financial Myths and Mistakes
(Things That Can Set You Back)

Many a times on a road journey, a small ditch or a diversion can cause a big delay or inconvenience. Similarly, even small misconceptions about certain financial concepts/practices may delay your financial planning process. Being aware of these in the beginning will help you avoid them for a smoother ride.

Common Financial Mistakes

1. Spending frivolously
It may not seem like much at the time, but even small expenses when added up can lead to a big hole in your pocket. Those colas and lattes, upgrading the cell phones, regular movie tickets and hot corns all amount to a huge unnecessary expense. A Rs.50 cappuccino by the sea with friends every evening will amount to Rs.1500 in a month. A first-day-first-show Rs.200 movie ticket every Friday and Rs.20 corn effectively means an outflow of Rs.880 from your wallet. Saving this 'additional' amount every month can allow you Rs.28,560 for something bigger over a year.

2. Mindless use of credit cards
Using credit card means spending borrowed money. Credit cards are a convenient way to carry money. But they come with double-digit interest rates. If the payments on your credit card are not made on time, the money you will have to pay back will be much more than what you spent on your card and that too within months. Young people are most susceptible to fall for this mistake. Paying your credit card bills always in full and on time, would help you get the best of this handy tool.

3. Caring little for regular savings
Contributing regularly to savings account, either for emergencies or for investment, is one of the best wealth building habits, often ignored by many. Notwithstanding the nominal returns on savings, building a healthy corpus by saving regularly is essential for sustenance and growth.

4. Investing based on half knowledge or imitation
Wise investment decisions should be based on one's risk profile, needs and priorities, and financial goals. As these differ from individual to individual, investment strategies also should be different. Just because an investment strategy has worked for someone (even for best of friends), does not mean it would work for you. Investment decisions should be made only after thoroughly knowing your investment needs and matching them with the options available to you.

Common Financial Myths

1. Attitudinal Myths:

Myth A: I have a lot of money (or very little money), hence financial planning is not for me.

Truth: Everyone benefits from financial planning. Whether you have a lot or little money, you cannot achieve your financial goals consistently without a plan. Financial planning not only helps you achieve your goals, it also helps you monitor and review your progress with your finances.

Myth B: Financial planning seems to be a tedious and time-consuming process and I am far too busy to spend my time on planning.

Truth: Anything new seems to be tedious at first. But it is worth 'investing' some of your time on acquiring this skill as it would enable you to worry less about and enjoy more of your hard-earned money. Seeking professional help from chartered accountants, financial planners will make the beginning easier. You should still ideally spend some time planning finances or overseeing and discussing from time to time with your planner, as no one would understand your needs and goals better than you do.

Myth C: If I earn enough now, I would have enough money during retirement.

Truth: The only way to retire rich is to plan and manage your finances well today, no matter how much or less you earn today. There are many cases of millionaires retiring paupers and of modest earners retiring rich. The difference lies in the way they manage their cash, cash flows, investment, debt and insurance.

2. Investment Myths:

Myth A: Investing in mutual funds is risk-free and guarantees huge returns.

Truth: No investment is risk-free, it can be either high risk or low risk and the risk is generally proportional to the returns it offers. Mutual funds are managed by professional wealth managers or portfolio managers, whose main task is to create an investment portfolio by wisely balancing the risks and returns. Thus, the objective of the fund manager becomes to minimize risks and maximize returns for the investors. But the risks cannot be totally eliminated and the returns can never be promised. Hence, it is advised to read the offer document of the fund carefully to understand what are the risks involved, and what returns one can expect.

Myth B: Investing in stock markets is very risky and best avoided.

Truth: Stocks are categorized as high risk–high returns investment channel. They have over the years proved to be one of the most profitable investments. Stocks have a significant role of growth to play in a diversified investment portfolio. For young people, with a good risk appetite, it should be one investment that should not be missed. But some look at stock investment as a get-rich-quick formula and 'invest' blindly, without proper knowledge. Such people should certainly avoid stock market investments, at least until they gather some know-how about it. For more details, please refer to Section III—Investments.

3. Tax Planning Myths

Myth A: Whether I do my tax planning in the beginning of the year or towards the end of it, it is one and the same as long as it is done before March 31st.

Truth: Legally, for the income tax department, it is one and the same. But financially, if you are doing tax planning (or you think so) just before the year ends, you are at a great loss. Tax planning makes thinking about your future financial needs mandatory today and hence is one opportunity to plan and invest for your financial security—insurance, retirement or long-term investments.

Tax planning in the beginning of the year has two distinct advantages—a short-term advantage of saving you tax and a long-term benefit of making the most of the investment opportunities that are still

in line with your financial goals. Whereas hastily putting money in any tax saving instrument at the end of the year merely saves you some tax. Besides, proactive tax planning also allows you an option of systematic investment over the year rather than running around and arranging funds for investment at the end of the year.

Myth B: Investing in mutual fund qualifies for deductions from my taxable income.

Truth: Specific type of mutual funds known as Equity Linked Saving Scheme (ELSS) that have a lock-in period of 3 years are counted amongst tax saving investment option. All other types of mutual funds do not qualify for income tax deductions.

4. Credit Card Myths:

Myth A: Number of credit cards in my wallet shows how rich I am—the more the number, the richer I am.

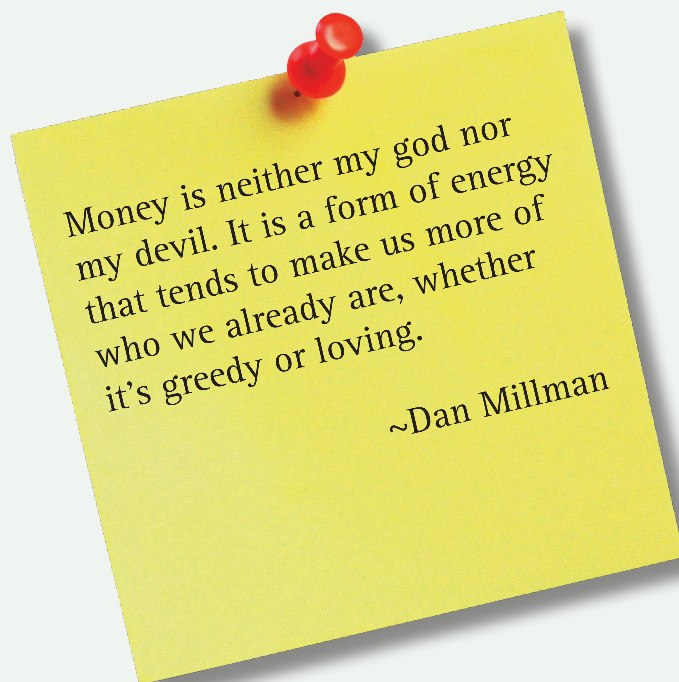
Truth: This is a common misunderstanding especially amongst young people. More credit cards mean you can spend more of 'borrowed' money, which may tempt you to spend more. If you spend more than what you can repay the next month, you will just pay the minimum amount (amounts, on multiple credit cards). Paying only the minimum amount means that the next time you will have to pay more (much more) than what you spent, due to the high interest applied. This may lead you to further borrowing and more debt, which means lesser money for you in the future. Credit cards do not make you any richer than what you are. But using credit limits much higher than what you can repay in the near future will surely leave you with much lesser money as well as peace of mind.

Myth B: It is okay to pay the minimum amount mentioned in my credit card statement every month.

Truth: Paying only the minimum amount means (heavy) interest being charged on the balance amount, which you anyway must pay sooner or later, with much more interest later. The sooner you repay all the money spent on credit card, the more beneficial the card will be for you. Paying only the minimum amount every month is one bad habit that many young people get themselves into—leading to mounting debts on them. It is best to avoid it. If you have got into this bad habit, the sooner you get out of it, the better it is for you and your finances.

Introduction

ICanDo Financial Planning
The Book



ICanDo Financial Planning intends to initiate the reader in and take him/her through the financial planning process. It is not just any book on financial planning. The uniqueness of this book lies in its hands-on approach. It is simple content, systematic exercises and inspiring experience sharing, should be helpful to the beginners as well as those conversant with personal finance.

This step-by-step manual intends to empower the young reader to construct a complete personal financial portfolio.

ICanDo Financial Planning touches upon 5 main parts of personal finance in 5 sections:

1. ICanDo Money Management.

2. ICanDo Financial Goal Setting.

3. ICanDo Investment.

4. ICanDo Planning and Managing Debt.

5. ICanDo Financial Risk Management.

Each Section of the book intends to bring about a proper understanding of the topic by:

1. providing relevant information in a simple language under the head '**I Know**',

2. providing Mrs. Bharati's experiences to learn from and believe that I should and '**I Can**' too,

3. providing worksheets and steps to start financial planning straightaway under the head '**I Do**', and

4. reinforcing important points by summarizing them at the end of the section in the box '**Key Points**'.

In the last few pages, the book lists a few common financial goals and recommends steps in planning for these goals.

What the Book Covers and What It Does Not?

The book is a step-by-step manual for financial planning. It covers all the important general steps in personal financial planning through its smart worksheets or checklists. The worksheets are flexible in nature and they should be broadly applicable to the majority of people.

Information-wise, the book provides relevant content that is important for making sense of the financial planning process. It touches upon most of the personal finance concepts and practices. But the book does not intend to develop thorough and in-depth understanding of any one concept/practice. Further reading is recommended in such a case, based on individual interest and preference.

This book covers the general concepts in investment, insurance and debt and their significance to financial planning. It does not cover the individual topics in details nor does it in any way recommend or advice any particular type or brand of these products. You would need to do further reading for this.

ICanDo charts a course for planning, going step-by-step. It does not recommend a specific plan. Instead, it encourages you to design a personal financial plan, individual to your needs and profile.

The book does not provide specific details about financial products and services. You are thus expected to refer financial newspapers or other media and/or check with relevant financial agencies to get such details as rate of interest, minimum payment, fees, EMI etc.

How to Use ICanDo Financial Planning?

This handbook is structured in such a way that it allows you complete freedom to choose how you want to use the book depending upon your:

- objective for referring the book,
- level of familiarity/proficiency with personal finance,
- topic/subject of interest or concern, and
- planning needs.

ICanDo may be used in its totality as a complete self-training manual in financial planning. Or it may be used in its parts on individual topics of personal finance and also as:

- An information booklet—refer only 'I Know'.
- A workbook—refer only 'I Do'.
- A journal of experiences in financial planning—refer only 'I Can'.

Beginners in personal finance may find it useful to read the book the way it is presented, while referring wherever needed, the glossary of terms in the last few pages.

If you are more familiar with financial planning, you may want to start with the worksheets and refer the content under 'I Know' as per need.

You may also choose a topic within financial planning that is of current interest or concern to you e.g., investment or debt or cash flow/money management.

Look Out for these through the Book

This is a 'Think About It' box that appears together with a light bulb throughout the book. Look out for this box and its content to get further insights into the topic or some ideas about how you can go about doing something yourself related to the topic under discussion.

This yellow note appears through the text in different sizes. It essentially highlights some important concepts. It may give a brief explanation of a term in personal finance or it may sum up some important part of the content for your easy reference.

Meet Mrs. Bharati*

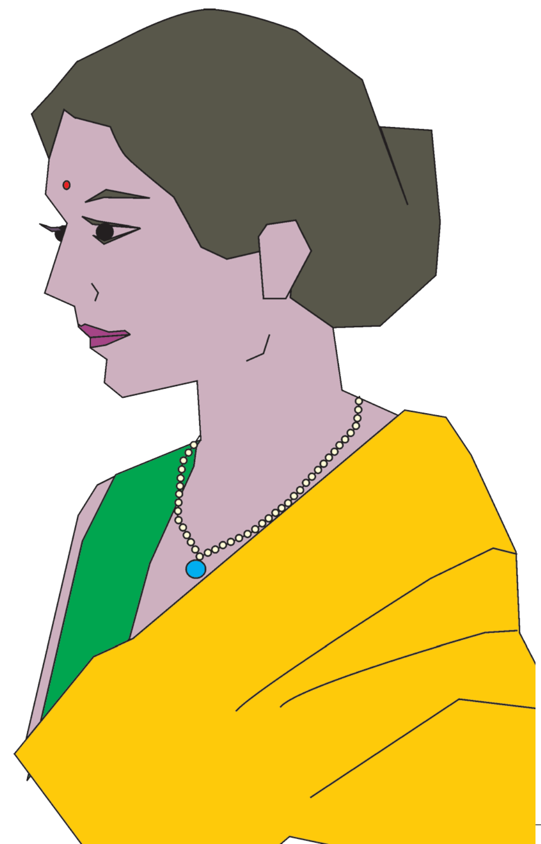
She is an accomplished award-winning entertainer—a television writer-director. She produces and hosts a very popular TV show on personal finance—Common Money Sense. In the show, she shares her experiences with her personal finance and how she picked up some tricks of the trade. She is known to have helped many viewers come out of their financial problems or/and build wealth through her 'Ask Mrs. Bharati' segment at the end of the show.

Formally educated in arts, she has no educational or professional background of finance. But has a very common sense approach to personal finance, which even financial experts approve and a common man understands. She says, "anyone can plan and manage his/her own financial matters to build wealth. What it takes is the intent, some time and a whole lot of common sense."

Her own finances have greatly benefited from her conscious money management and her common sense. Today, at 43, she is carefree, doing what she wants on her terms, happily married with 2 kids. Her husband, a former HR professional, has chosen to retire early and is now a full-time amateur painter-photographer. And their money is the only 'employed' member in their family.

Meet Mrs. Bharati, the anchor of ICanDo Financial Planning, who will take you through the various aspects of financial planning. Look for the insights she has gathered over the years through her own experience with her finances.

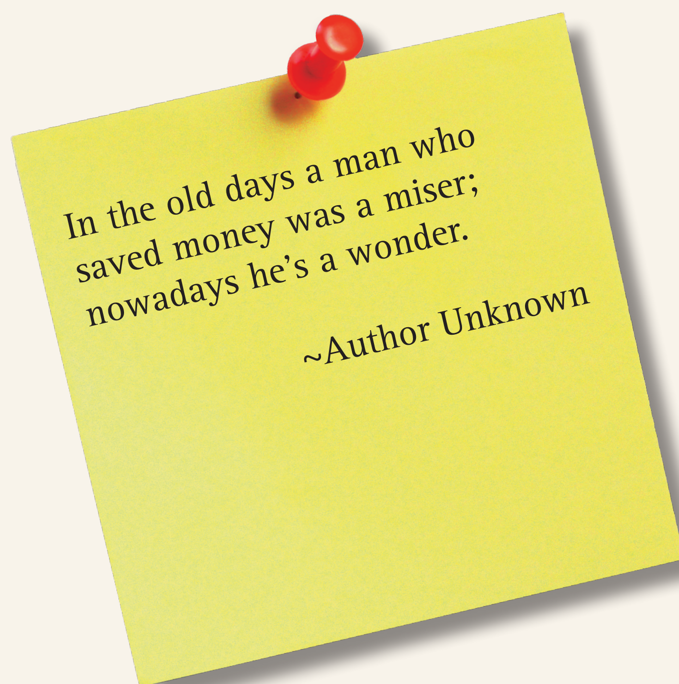
In this book, you would come across a few stories from Mrs. Bharati's 'Common Money Sense' and also some viewers' financial queries and Mrs. Bharati's solutions to them. The idea of citing the cases in this book is to illustrate a few typical situations and understand the approach or the line of thought to deal with such situations. Readers are encouraged to solve the cases themselves before checking Mrs. Bharati's answers.



**Please note that Mrs. Bharati is a fictional character. Even the cases given in the book are fictional and any resemblance to anyone is coincidental. 'Common Money Sense' is also coined only for the purpose of this book*

Part I

Money Management



I Can—Mrs. Bharati's Common Money Sense

Have you faced days when you had a lot to do and very little time at hand. I doubt if there is any young person who does not face this situation on majority of days. Of course there are some days for some of us when we have a lot of time at hand but almost nothing concrete to do.

I am no exception! In my college days as a teenager, I was 'busy' taking care of some very basic human needs of food (frequenting the canteen), clothing (following the latest trends and fashion) and shelter (looking for a safe place after bunking classes). As responsible youth, we had very important matters to discuss like, reviewing the latest movie, breaking news of love affairs and heartbreaks on campus, checking out the latest campus styles etc. Elders at home and college would often nag that I was wasting too much time, when it could be better utilised. But so busy was I in all my important activities that I had very little time to think about how much time I really had.

As time flew, I graduated from college and joined the workforce. My mornings—the rush hours—would often vanish before I could recover from sleep. Getting ready and rushing to catch a bus, and then tolerating all the speed breakers and traffic jams before reaching the office, barely on time. At office of course I used to be busy as a bee. And then back to the crazy bus ride before reaching home, half drained. Before I knew it the days were gone. Weekends meant doing all the work I could not do over the week—including catching some peaceful sleep and some recreation—movie, shopping, sport, hair cut etc. This routine continued for a few years and left me with time to do only the things that seemed urgent. As I looked around at people I knew—my friends, colleagues—it seemed like the same story with everyone. There simply was no time.

Many of us thus felt pressured, many had to overlook their small health problems and carry on, many slept little, most had no time to even sit down and have a peaceful meal.

I soon began to realize that because of this 'busy' life, I was also spending unnecessarily—taking taxis just to make it on time, picking up junk food on the way to munch on (instead of a good breakfast at home), drinking too much coffee, calling for pizza, making numerous phone calls to people to explain why I could not make it at all or not make it on time for an appointment. Frequent medication for even slight aches and pains, also meant more expenses. The biggest component though was poor maintenance of the things I had, including my health and fitness. I just didn't have the time to take care of my health and things like my clothes, computer, phone, bags and shoes and even my scooter, which I would use on weekends. So they would give up way too soon prompting me to rush to buy another one or pay huge repair bills.

What made this all worse was my ignorance about it. There was no way to notice this, as I did not have the time to keep account of the expenses. I just realized it by chance when for many months I seemed to spend all my money before I received my salary. And it seemed to be almost similar story for most of my young friends and colleagues.

Over the years I have come to believe that management of Time and Money management go hand in hand. You are most likely to have similar attitudes towards money and time. And you are most likely to manage your money the way you manage your time and vice versa.

You'd spend more money if your time just goes by in managing day to day or just the urgent tasks. See it for yourself! See how you are spending time—if you see anything similar to my story, you are most likely spending more money than you probably should or would by sparing some time to mange the time and money.

I realized that I was spending unnecessarily only after I started to keeping a regular account of my expenses. It seemed quite tough to keep up the practice initially—I would at times forget to make a timely note of small expenses or goof up with recording expenses on credit. But I persisted as I discovered the power of such a simple thing as making a timely note of the amount I spent everyday. This simple thing allowed me to track my money—where it came from and where it went. And there was a huge motivation, this simple practice subsequently would help build up my reserves. I call this very effective process of **record keeping** and **accounting**, analyzing my spending pattern and **making a budget** to **build savings** as **SMART MONEY MANAGEMENT.**

We have witnessed the power of this simple yet powerful practice of money management through good times and bad. What I have also witnessed is people finding the practice quite ineffective. But my observation over the years tells me that these are the people who resort to monitoring their expenses and budgeting only in tough economic times and wanting immediate solutions when in problem. Money management is all about recording your money behavior and learning from them. It requires a few trials and should have scope for some errors, until you understand your own spending pattern and figure out a way to save in your budget. Thus such sporadic practice, that too in bad times yields little results.

My husband and I have been practising prudent money management for close to 15 years and so diligently that now it is become almost our second nature. By God's grace, we've been having a comfortable living and growing inflow of money. But I can tell you that had it not been for managing money prudently we would not have been living so carefree in our mid forties, with two young kids.

Recently I read a quote and found it very appropriate. It read, 'the wealthiest of the world are not the ones who started with the highest paying jobs, but they are those who knew how to use their money prudently, no matter how much or less money they began with.' I am teaching my kids (aged 12 and 8 years) this valuable skill of managing money, so that they get a head start and do not struggle with their money in the most 'happening' years of their lives, the way we did. I hope every young person discovers this sooner than later and every parent educates her/his children on money management. It sure will be an important survival skill in times to come.

I Know – About money management

No matter how much (or less) you know about investments, stock markets, credit cards and insurance, if you do not know your money well, you are most likely to fail with your financial planning.

The first and perhaps the most important step in financial planning is to know your money i.e., your financial position well and then be able to manage it wisely.

What makes up 'your money' or financial position?

1 **Your income and expenses:** What you earn and what and how much you spend determine how much money you have on hand after meeting your needs (and some wants). This 'balance' is an important indicator of your financial position. It can be used as a guideline to plan your finances. A healthy positive balance every month indicates a trend towards a good financial position and a zero or negative balance most of the months corresponds to a weak financial trend (especially if you are not building assets on the way).

   A healthy positive balance from your income will allow you to build funds for meeting your financial goals.

2 **Your assets and liabilities:** The amount of assets—items of value—you hold, is a precise indicator of your current and future financial position. Assets tend to add to your income (either now or in future) e.g., investments—in gold/silver, deposits, stocks, mutual funds, art/antique, land etc. Or they help reduce expenses, as in case of owning a house—it saves you taxes and rent. Thus, assets help to strengthen your financial position. On the other hand, liabilities weaken your financial position. Debt—something that you owe is a liability. And so is an old vehicle that needs a lot of fuel and repairs, for the work it is doing.

   More assets and lesser liabilities would help you better your financial position and strengthen your money.

I Know – About money management

You may now appreciate that 'your money' or your financial position is determined not from your income alone.

There are not one but four factors constituting 'your money': income, expenses, assets and liabilities. How well or badly you manage these four together will decide your financial health.

Consider the following cases:

Asif, 23—earns a monthly salary of Rs.10,000 from his call centre job. His average monthly spending on livelihood and looking good is about Rs.9200. He currently has no investments and has an amount of Rs.3200 overdue on his credit card.

Babu, 30—earns Rs.4,000 per month as a bank clerk. He spends a maximum of Rs.2000 in a month. He has Rs.4800 in his savings account but has not made any significant investments yet. He has to pay an EMI of Rs.800 towards home loan.

Chanda, 26—is a housewife who gets Rs.4500 from her husband every month towards household expenses. She makes it a point to put Rs.500 in her savings account as soon as she gets her 'allowance'. She has managed to build a reserve of Rs.3000 so far.

David, 19—a third year commerce student has built an investment portfolio of Rs.5000 in mutual funds. He started investing a part of his allowance, cash prize and gifts on his 19th birthday, 6 months back.

If income were the only indicator of your financial situation, then Asif's situation can be considered the strongest. But does he seem to be doing well with his money? Is his financial position really strong? Can he take care of any financial emergency like a job loss or drop in income?

In fact, looking at the overall picture, Asif even with his fat paycheck, is in the worst financial situation at present. His expenses are almost as much as his income. And his credit card debt has got him into a financial mess. Considering his meager monthly 'balance' and high interest rate on credit card debt, Asif would need more than 6 months to payback the debt, if nothing else changes.

The other three, despite their lesser incomes/allowance, seem to be doing decently in their own way—building saving reserves and assets. Whereas Babu has a decent saving and asset-building home loan, Chanda has her own savings account. David, with age on his side, has started investing and is arguably in the best situation at the moment.

To sum up, income alone is no indicator of your financial position. The four cornerstones of your financial foundation are:

1. **Income** in relation with your
2. **Expenses,**
3. **Assets and**
4. **Liabilities**

And hence, no matter how much or little you are earning currently, how you manage the four cornerstones would decide how strong and stable your financial foundation will be.

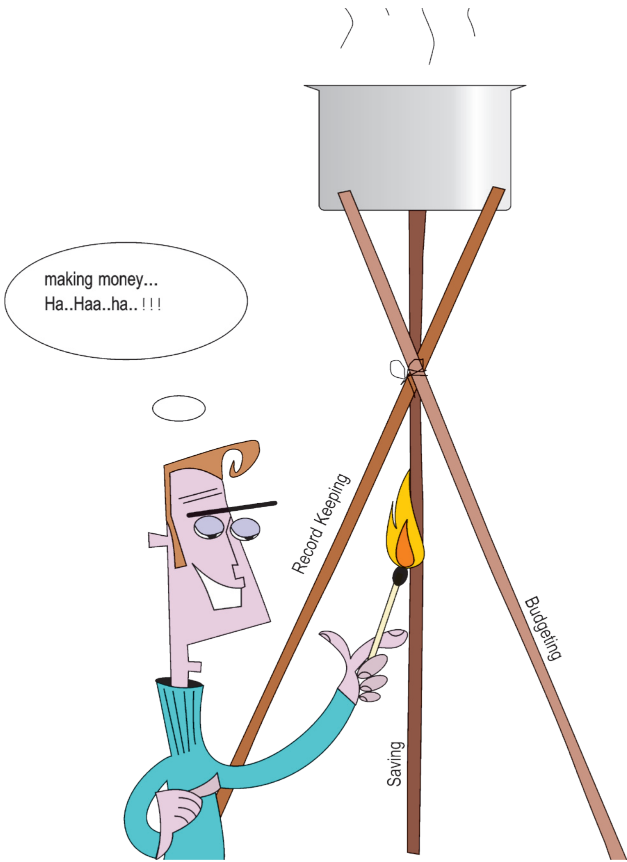
So how do you get the 4 cornerstones of your financial foundation in place? Use the tripod of money management–Record Keeping, Budgeting and Saving

1. Record keeping–timely recording of expenses and meticulous keeping of important documents and records; bills, receipts, tax documents, statement of savings, investments and credit cards, warranty/guarantee cards.
2. Budgeting–making and following a plan to put your money to optimum use. A plan that would enable you to-

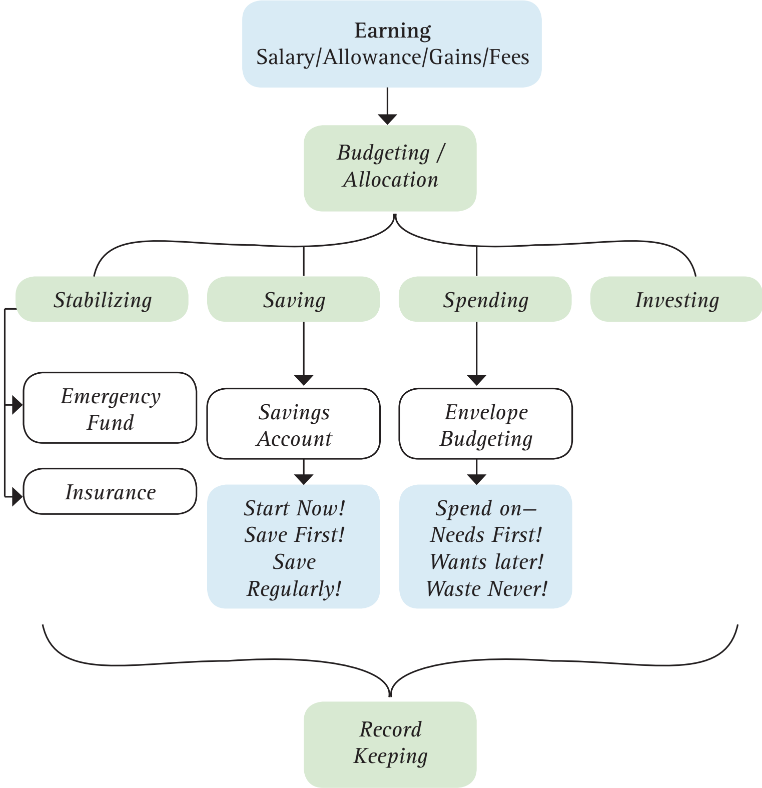
- reduce liabilities,
    - to spend wisely,
        - to save, and

- invest and add to your income.

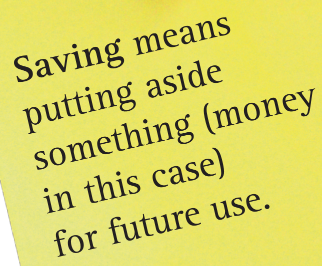
3. Saving-building reserves to be able to-
- face financial emergencies, and
    - invest and build assets.



I Know – The money management process



I Know – About Saving



Life's needs keep changing, with growing age and changing life stage. Whether your occupation (a job or a business) is earning you a lot or little today, it would not be earning you the same all your life. It is best to be aware and prepared for these changes– in your needs and your income. Saving is one such way that allows you to face such changes with little financial impact.

Saving of money becomes possible only if you manage your income and expenses prudently. A healthy reserve or fund you build up by saving regularly enables you to build assets and reduce liabilities. Hence, saving is that common thread that links the four cornerstones of a strong financial foundation.
The very first step towards taking charge of laying a sound financial foundation is thus making a commitment to SAVE.

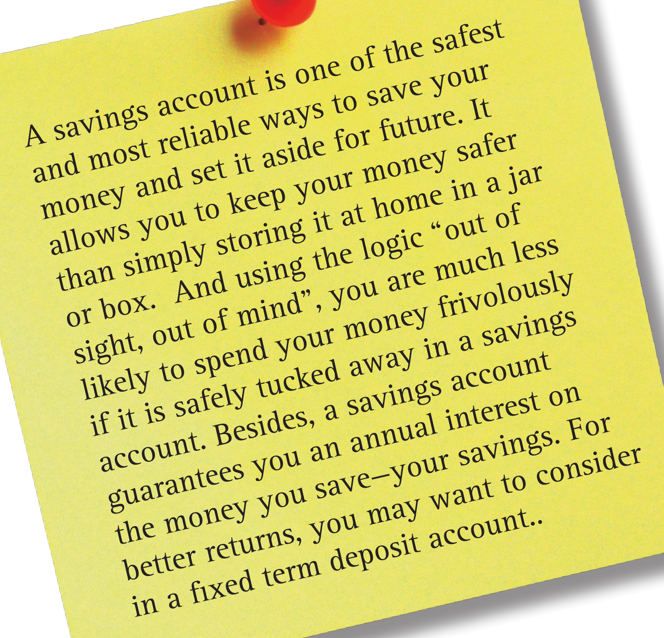
The Savings Mantra – Start NOW! Save First! Save Regularly!

Start saving NOW: There is no better time to start saving (if you are not already saving) than NOW. 'Time is Money' and certainly so. The earlier you start saving and get into the habit of saving, the stronger your chances are to face uncertainties and the changing demands of life.

Save First: The surest way to save is to make 'saving' your first and most important expense. Set aside a portion of your income as soon as you get your paycheck.

Save Regularly: The commitment of saving regularly, month after month, would enable building a healthy savings from smaller incomes as well.

Step 1 – Open a Savings Account and Follow the Savings Mantra!



If you do not have a savings account, open one NOW.

Visit a branch of private bank, state bank, cooperative bank or post office, whatever is closer and convenient to you. Or call a bank's call centre for details.

What you may need for opening a savings account?

1. Fill up an account opening form and attach a passport size photograph.

2. Proof of identification and/or proof of residence like a ration card, election card, PAN card with electricity bill or a passport.

3. A minimum deposit amount ranging from Rs.10 to Rs.2500 may be required in your account while opening and later you may be required to pay a small annual fee for your savings account.

What you may get to operate your savings account with?
1. An account number—that is unique to you.
2. A cheque book (withdrawal slips) to be able to withdraw money from your account. Deposit slips to be able to deposit money in your account.
3. An ATM/ Debit card with a PIN—Personal Identification Number (password)
4. A passbook that you may need to update with every transaction or a monthly account statement from your bank/Post Office.
5. A User ID and password for internet banking.

I Know – About Record keeping

Ashok's bike, which was parked on the road, was hit accidentally by a tanker. It got damaged and Ashok found that repairing it would cost a lot of money. So he thought of claiming insurance to lessen his financial burden in repairing the damaged bike. He had bought the vehicle three years back. He then got so busy with his job that he just forgot where the insurance policy papers were. Then one weekend, he searched his entire room and finally discovered the insurance papers, only to find that the insurance policy has lapsed as he had not paid the premium on last year. A simple negligence, cost Ashok his half month's pay.

Such and many simpler situations occur that cost us money and time unnecessarily. Some effort on our part, of organizing and safe-keeping of important records can take a lot of pressure—financial and emotional—off us.

The benefits of record keeping are plenty.

An up to date record keeping will enable you to:

1. Track your money— income (where it comes from) and expenses (where it goes)

2. Provide you an easy reference of your wealth—assets (savings, investment, insurance etc) and liabilities (credit card debt, home loan, educational/ vehicle loan).

3. Organize financial activities like budgeting, saving/investment, tax-paying.

4. Provide an evidence of a financial transaction—repayment of loan, depositing money in bank account, purchase of an asset, etc. This is especially important in case any discrepancy arises over it.

5. Simplify the claim process in case of an emergency (insurance) or damaged good (warranty card).

6. Provide evidence for your entitlement to an after-sales service or other benefits.

7. Keep some faithful person informed about your financial transactions

Whether you want to get your current finances in order or you wish to plan your financial future, a proper record keeping is the step to start with.

Record keeping means organizing and keeping your important documents, records up-to-date so that you can track them whenever you need.

An efficient record keeping can be done by following 2 steps:

1. Identifying important records: Dig out all the papers and records that you may have collected over a period of time. Begin sorting. Not all records that you have are necessary to retain over a longer term. Identify the records that are critical from the point of view of them saving you time and money in future, if need be. (Refer to a suggested list of records mentioned on the next page).

2. Develop a method to organize them: The records should be organised in such a way that they become available just when you need them. You may want to use paper filing system, safe boxes or briefcase to store your physical records. Records of your expenses, savings, investments and a handy summary of where all the other records are, can be maintained on a paper or in electronic format on a computer.

Make sure that you keep updating the records, adding new relevant ones and disposing ones which have lost their value like the 1-year warranties.

Also keeping a simple calendar of payments due (like credit card bills, insurance premiums, savings deposit, loan repayment, etc.) will prove a very worthy financial habit.

I do – The Money Management Process Step 2

Step 2 – Record Keeping

A list of financial records and important financial papers that need to be kept safe is given below. It can be used as a starting point to create a personalized record keeping list for yourself/your household. Use basic filing system—paper or electronic—to maintain and access these records easily.

1. An **Account Book** - A month wise record of day-to day expenses and income. This is important for planning future spending and for financial analysis. (For maintaining your accounts, refer the worksheets in this section.)

2. **Income/Employment Records** - Salary slips, payment slips, experience certificate.

3. **Income Tax Records** - Tax Deducted at source certificate, acknowledgement of filed returns/ tax paid, tax exemption documents.

4. **Insurance Policies and Receipts of Premiums Paid.**

5. **Bank Records** - Bank statements/updated passbooks, Deposit slips, Cheque books. Also ATM/debit cards and their PIN.

6. **Debt Records** - Credit terms, repayment proof.

7. **Credit Card Records** - The card itself, bills paid on credit card will prove helpful to check any discrepancy in the credit card statement.

8. **Purchase Records** - Bills (especially of high value items) warranty cards, service commitments.

9. **Record of Investments and Assets Purchased.**

10. **Your Financial Goals, Budgets and Plans.**

Step 3 – Record your assets and liabilities

Worksheet 1.1

Record your assets and liabilities			
Assets	Amount	Liabilities	Amount
Total Savings in all the Savings Accounts		Borrowings Home Loan Educational Loan Personal Loan Vehicle Loan Business Loan Credit card debt Other bills on credit	
Investment Real estate/Land Gold FDs/NSC/ RD etc. Mutual Fund Bonds/ Debt Shares Others			
Insurance Life Health			
Retirement Plan Pension fund PF/PPF Others			
Others		Others	
Total of Assets	Amount A	Total of Liabilities	Amount L

Step 4 – Keep an account of income and expenses

The following worksheets are a simple format for keeping of accounts.

(Write in the space provided in the table, use separate sheets for different months. You may want to note down daily expenses in a simple notebook and then summarize them in the format given below)

Account for the month ________________

Worksheet 1.2

Month's Income Summary Sheet
(Where money comes from?)

Items	Amount in Rs.
Income from occupation Salary/Profits/Commission/Fees	
Interest on savings	
Interest/Dividends/ income from investments	
Gifts/ prize money	
Tax Reimbursements	
Any other income	
Total Income (Amount 1)	

Month's Expense Summary Sheet
Where does money go?

Worksheet 1.3

Items	Amount in Rs.
Your individual expenses	
Contribution towards household expenses	
Flexible/ one-time Expenses Recreation Travel/ Holiday Gifts/ Social Occasion	
Emergency Expenses Medical/Others	
Important Payments Tax Insurance Loan Installment Saving for Emergencies Credit card payments Others	
Any other expense for the month	
Total Expenses (Amount 2)	

Step 5 – Understanding your financial position from the records

Use your up-to-date accounts (Worksheets 1.2 and 1.3) to understand your financial performance. The following worksheet can help you interpret your accounts.

Worksheet 1.4A

What's your balance for the month ________________?

1. Month's total income	Rs. Amount 1
2. Month's total expenses	Rs. Amount 2
3. Balance left this month	Rs. Amount 1—Amount 2

Worksheet 1.4B

What does your balance tell you?
(Place a tick alongside the statement that best describes your situation for the month.)

- ☐ My balance is positive—I **SAVED** this month.
- ☐ My balance is zero —**I SPENT all my money** this month.
- ☐ My balance is negative —Oops! I **BORROWED** this month.

Worksheet 1.5

How does your year's monthly balance look like?

(Color the box for the month—green, yellow or red as per the Worksheet 1.4. Use this worksheet every month for the year, to see your financial performance for the entire year.)

Month	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Balance												

All or mostly green boxes for the year tell you that you are doing well with your money. But all red or a mix of red and yellow boxes mean that you are in a danger zone and you should plan to quickly get out of it.

The following worksheet will help you see your financial position by comparing your wealth—assets and liabilities (Worksheet 1.1) with your financial performance monthly balance of income after expenses (Worksheet 1.5) .

Worksheet 1.6

How do you seem to be placed financially?

(Place a tick alongside the statement/s that is/are true to you, as seen from your records—refer all the previous worksheets in this section)

- ☐ My monthly balance chart for the year looks mostly green i.e., at least 9 months in a year it is green.
- ☐ My monthly balance chart has never been in the red.
- ☐ I have a savings account, different from my salary account..
- ☐ I always put my savings in my savings account.
- ☐ I have built or I am beginning to build assets.
- ☐ I have managed to keep my liabilities to the minimum.
- ☐ I have more assets than liabilities, and always (almost) more income than total expenses.
- ☐ I pay my credit card bills fully before/on the due date.

If you have been able to place a tick in every box above, then you have laid a very strong financial foundation and financial planning should be easy for you. If you have less than 5 ticks, then there is a call to gear up and get your financial acts in place.

In either case, a sincere attempt at financial planning using the worksheets in this book would help you meet your goals.

I Know – About Budgeting

A budget can help you take control of your money and manage it well. Whether you make a thousand rupees a month or tens of thousands, budget can be a guide that tells you where you are going financially with respect to the direction you want to.

Everyone can benefit from a budget!

A well-crafted budget can help you identify areas where you are spending more or unnecessarily. You can thus further reduce your expenses, improve savings, build assets and thus meet your financial goals faster. Hence, a budget can help everyone, irrespective of one's financial position and income.

A few thoughts for effective budgeting:

1. Have a clearly defined purpose or objective for your budget. For instance knowing your monthly expenses and balance, reducing wasteful / unnecessary expenses, increasing saving.

2. Keep the budgeting process simple.

3. Do a monthly review of your budget.

4. Anticipate and have a plan to tackle the 'budget busters' (they are many and invariably there)—unknown/ surprise expenses that can put your budgets haywire.

The power of money multiplies when its use is maximized. Money is not just to spend on present needs and wants nor is it to simply save.

With your money, you should be able to:

(i) meet your needs and monthly household expenses,

(ii) build a healthy saving to meet your future goals,

(iii) build a financial safety net to stabilize your financial present and future - deal with emergencies without a significant financial impact, and

(iv) set aside money to grow through investments

How do you find money for everything?

A. Trim the extras
Almost every household would have spending areas that can be cut or reduced. These areas often eat into probable savings. It would be easy to identify these trim-able spending areas, if you classify your expenses in 3 main groups;

1. **Needs or essentials –** bills you must pay to run your household and to keep your family healthy and comfortable. Utilities (electricity, gas, water), housing-rent/home loan installments, groceries, health, transport, insurance, education, are your needs. Things that make your life simpler and more convenient can also be regarded as needs.

2. **Wants –** all other 'nice to have' expenses for entertainment, travel/holidays, gifts, looking good, fun and celebrations, etc

3. Wastes - excessive tea/coffee, cigarettes, alcohol, gambling, spending on wants beyond your means. Wastes eat a major chunk of your money bit by bit at a time.

Spending Mantra – spend on needs first, wants later and waste never!

Step 6 – Budgeting! Trim the extras!

Enlist in the space given below, all the expenses that make the 'Individual Expenses' and 'Other Expenses' in Worksheet 1.3. Ask yourself whether each of the expense in the list is a need, want or a waste. Refer to the text on previous page for details. And write down this category in the adjoining column.

Worksheet 1.7

Categories of expenses

Individual Expenses—Description	Is it a Need/Want/Waste?
1. E.g. Haircut	Need
2. E.g. Cigarette Packets	Waste
3.	
4.	
5.	
6.	
Other Expenses—description	Is it a need /want/ waste?
1.	
2.	
3.	

In future expenditures eliminate the items that you have classified as wastes and start trimming the wants. You will soon see that your expenses would reduce and monthly balance and saving would improve.

How do you find money for everything?
A. Trim the extras **B. Allocate**

Allocation of your earning is an effective way to maximize the use of your money. Allocation, an important part of budgeting, means to plan before hand how you can find money from your income to spend, save, stabilize and invest.

Allocation guidelines

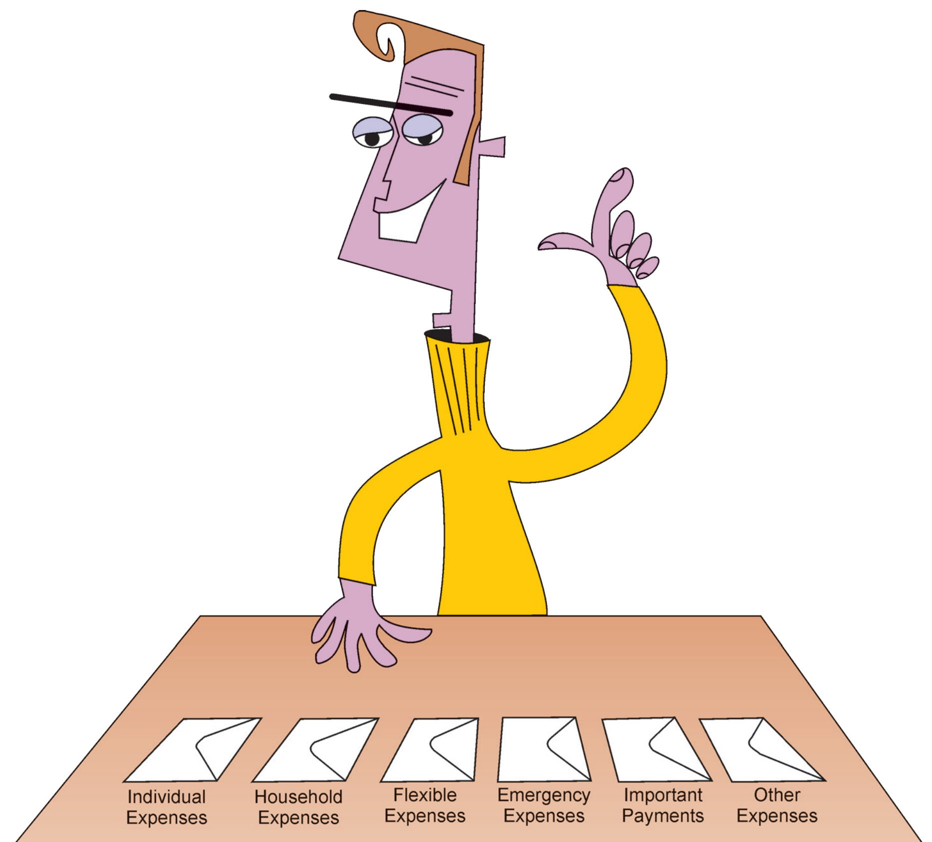
To begin with, you could use the following guideline to allocate your income. Later as you follow the process consistently, you would figure out the allocation formula that works best for you and your family. Your average justified past spending that you would have figured out from your accounts could be your basis to allocate.

	Category	Allocation
(i)	Spending	50% of income
(ii)	Savings towards goals	20% of income
(iii)	Stabilizing finances	20% of income
(iv)	Investing (long-term saving)	10% of income

Envelope Budgeting

Envelope budgeting is a simple, easy-to-follow method of budgeting. In this system, on a regular basis (i.e., monthly, weekly) a certain amount of money is set aside (allocated) for a specific purpose or category, in an envelope marked for that purpose.

Envelope budgeting is an ideal method for beginners to start budgeting and also for those who have problems sticking to a budget.



Step 7 – Envelope Budgeting! Allocate!

The process of envelope budgeting is listed below in a step-by-step manner. Note that a general process is mentioned below for transactions in cash. You can use the same process using digital/electronic worksheets to suit your needs and modes of payments—by cheques or electronic transactions.

(Use the following checklist to make and follow a personalized budget. Check each box alongside the step by placing a tick mark ☑in it once you perform the step.)

1. Make budget calculations on a paper ☐
   (Use your expense records—Worksheets 1.3 and 1.7 and the allocation guidelines mentioned on the previous page.)

2. Deposit the amount you would be saving in your savings account. ☐
   (Do not forget to update your passbook/register with the recent balance.)

3. Make payments towards stabilizing finances on the due dates —insurance premiums, an emergency account, debt repayment etc. ☐

4. Put the portion you have allocated for investing in an identified instrument or store it separately in an envelope for investing later, when you have enough funds. ☐

5. Identify your various expense groups and make one envelope for each. ☐
   (Housing (rent/loan), utilities, health care, food and grocery, transportation, clothing, home furnishings, personal care, individual allowances, recreation, gifts/social occasions, interest charges and fees, salaries of maids/workers)

6. Mark the envelopes using words or pictures to represent the individual expense groups. ☐

7. Divide your cash according to your budget calculations. ☐

8. Place the allocated cash in respective envelopes of the spending groups ☐

9. Maintain a record of all the transactions mentioned in this process in a register or an account book. ☐

10. At the time of paying a bill or buying, withdraw money from the envelope marked for that purpose. ☐

11. At the time of shopping, especially for wants, see if there is sufficient cash in that envelope to make the purchase. If there is, go ahead, make the purchase. Otherwise do not make the purchase, at least not until the next allocation is made and the envelope marked for that has enough money to make the purchase. *This becomes an automatic regular control.* On the other hand, if you do not spend everything in the envelope in a cycle, then the next allocation adds to what is already there resulting in more money for the next cycle. ☐

12. Follow the same process of allocation and use of your earnings every month. Keep updating your accounts. ☐

Tech Savy

Microsoft Office's Excel Spreadsheet or Microsoft Money can help you do the budget and to keep track of your income, spending, savings and investments.

The waste of money cures itself, for soon there is no more to waste.

~M.W. Harrison

Help Us Save!!!

Rama calls for help

My husband and I are both doctors, working for a private hospital. We get a net pay of about Rs.30,000 and Rs.24,000 in our individual salary accounts. Though this seems to be a good amount of money, by the end of the month there is hardly anything left in any of the accounts. We are a family of 5—us, our 2-year-old son and my parents-in-law. My in-laws manage the household. My husband and I are so busy that we hardly get any time to look after our household and our finances. The problem is that for last three months, we have been having a payment overdue on our credit card, and no money in any of our accounts to pay the bills. I am beginning to worry, how we are going to manage further. With our son growing up, the expenses are also increasing. Please suggest us a simple and less time- consuming process to save.

Rama has a problem that many busy professionals have. Can you suggest her three simple things she and her family need to do to be able to save money? Use the space below. Look for Mrs. Bharati's explanation at the end of the section

Is Money Management for Me?

Zakir says

I read your story and about money management. I am convinced that everyone needs to practice conscious money management. And I shall do it too, once I get a well paying job. I am 23-year-old and unemployed. I am on a lookout for a permanent job but there are very few vacancies. Meanwhile, I do some sundry work like courier delivery, help at a stationery shop, etc. But they do not pay much money and it is quite irregular.

Do you think Zakir will benefit by managing money even now? If you do, list down your reasons in the space below. Look for Mrs. Bharati's list at the end of the section.

Abbas says,

I am managing a very profitable family business of glass trading. My needs and responsibilities are less and in comparison my salary is much more. I am 25 years old, the only son of my parents who have no financial liabilities and a good bank balance. Our family has so much wealth that I can survive even if I do not do anything for the rest of my life.

Abbas sure seems to be in a great situation. But he too needs to practice prudent money management. Do you agree? Look for Mrs. Bharati's advice to Abbas at the end of the section.

Mrs. Bharati's Common Money Sense
Answers to the cases

Dear Rama,

Since you seem to be so short of time, I would keep my answer to the point.

1. **Open a separate savings account and save first.**
   You may have 2 accounts, but if you do not have a separate savings account (a self-controlled 'deposit only' account) it will be a tough task to save. A salary account cannot be a savings account, unless you make it so and decide not to withdraw from it. Hence, open a fresh account and both you and your husband deposit a percentage of your salaries in that account as soon as you get them.

2. **Withdraw a fixed amount for spending at the beginning of the month and use envelope budgeting.**
   Refer to previous pages for a detailed process of envelope budgeting. The envelopes would help you track and control your expenses according to different heads. Try not to withdraw anything during the month. Without spending much time on analysis, you would automatically realize within a month or two as to how much you are spending and on what. It would help further if someone in the family can maintain an account of expenses.

3. **No credit cards for now.**
   Since you are so busy that you may not be able to keep track of your spending, you should stop using your credit card for now. At least till you get control of your finances. Physical transactions of money are much easier to track and control than the electronic ones. Try this—next time you go shopping, decide to pay by cash rather than by a credit/debit card. You would immediately realize when you are spending more than you should.

4. **Get everyone in the household committed to saving.**
   When you are a family of 5, saving can not be an individual goal. You are thinking in the right direction, so get everyone in the family involved and see your savings build up.

Best wishes,
Mrs. Bharati

Dear Zakir,

I appreciate that you read this section and that you are convinced in-principle about money management. What you possibly missed out from the text is that money management can benefit everyone, including people like you. Whoever uses/handles money can benefit by practicing money management process, including small children who receive pocket money. The whole premise of money management is that everyone can build wealth, no matter how much or less he/she earns. Now let us see its significance to your current situation.

1. Since your income is irregular, keeping an account of your income and expenses is very relevant to you. By doing so, you would understand what your actual monthly expenses are and how you fund them in the situations when you earn money and in those when you don't. What you would eventually understand from this is whether you can save from the months you make money and manage the shortfall when you don't. This way you might not need to borrow much. This would help you become financially independent faster (if you are currently borrowing from your parents) and/or reduce your liabilities (if you are borrowing from outside).

2. If you start 'practicing' money management from now on, you would be in a much better position to understand and manage money, when you start your employment. This way you can start building wealth right away.

3. If you practice the savings mantra, even if that means putting aside just Rs.50 in a month (in a Post Office savings account), you can see wealth building in time, bit by bit, as you would have never expected. Feature this,

Saving per year	Rs.600
Annual Interest @ 5%	Rs.30 (in the first year, this amount will increase in subsequent years as a result of compounding)
In 5 years you will have	Rs.4500 (approximate)

Therefore, do not waste time, start money management (and other financial planning steps) to get maximum benefits.

Best wishes,
Mrs. Bharati

Dear Abbas,

You are indeed in a very good financial position. And as your needs and responsibilities are also limited, you surely are well placed. My advice is in 3 parts.

I. I am assuming that your family's wealth comprises:

1. Physical assets—as most times wealth is in terms of stock portfolio which is largely unsteady and determined by the way stock markets are doing at time.

2. Insurance—life, health, business related. As an emergency can strike off most of your wealth in no time.

3. Balanced Investments—in low risk assured returns type of instruments too.

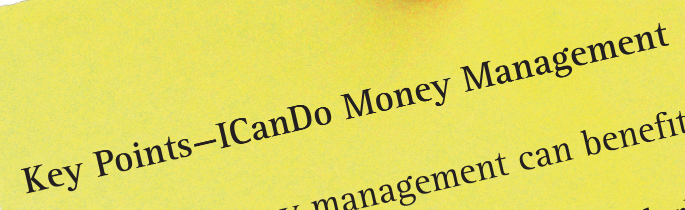
4. Investment in retirement plans—for your parents as well as for you.
   In case any of the above is missing, you need to immediately fix it.

II. Having said that, you are a young man and still have a long life to live with many future responsibilities and growing needs. Therefore, do not assume the wealth to last you, based on your current expenses and liabilities. Remember that expenses and liabilities have a tendency to grow and you need to factor that in your financial plan.

Besides, the optimum use of your wealth can happen when you

III. Besides, the optimum use of your wealth can happen when you:
1. Judiciously spend, as you may be doing now.
2. Save and stabilize your finances.
3. Invest for an equally great life through the entire lifecycle, and
4. Share—if you/your family is/are not currently sharing, you may wish to start doing so. You can fund a needy but deserving student's education, sponsor a child or the elderly, patronize a dying art. There are many ways you can share your wealth, spread smiles and have a great **'social investment'.**

Think about it,
Mrs. Bharati

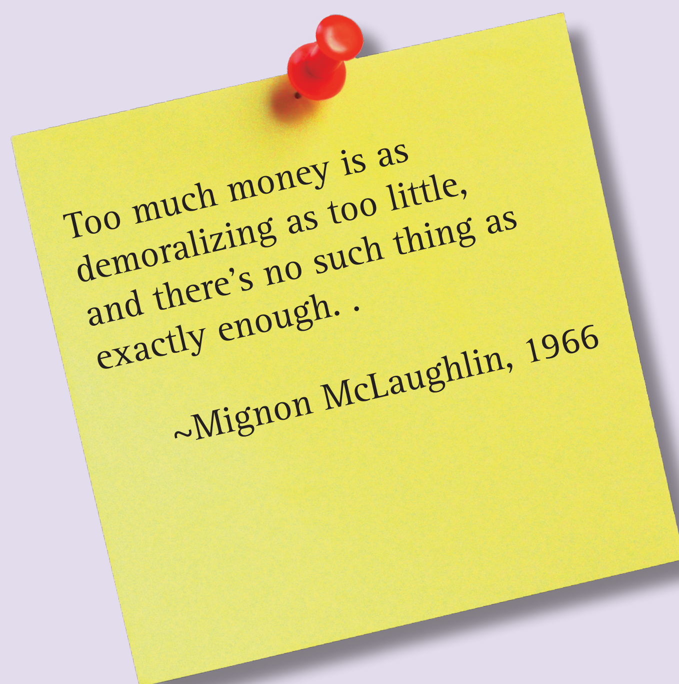


Key Points—ICanDo Money Management

1. Smart money management can benefit everyone.
2. Save first, save now and save regularly.
3. Spend on needs first, wants later and waste never.
4. Money just flies and you lose the count, as a good practice you must keep an account.
5. Spend, save, invest and share—allocate your money with wisdom and care.

Part II

Financial Goal Setting



I Can– Mrs. Bharati's Common Money Sense

The most fun time of my life so far has been the one when I was young and had just become financially independent. It seemed like I had access to everything I wanted without many responsibilities. The present was so beautiful and carefree that I did not have to worry about future. There were many young people like me—we could eat out, watch movies, go shopping, travel and have a gala time. Our income was our pocket money and if we fell short, there were always our parents to back up (though they would do that not without giving a lecture or two on saving money—how boring!)

But then, time flies and it did in my case too. I grew up, as they say, gained some wisdom as I added some more years to my age. I grew over the 'time-pass' (petty, in youth lingo) activities. Everyone does some day or the other. I started to find stories of courage, success and excellence inspiring. I looked at people who made a difference to the world, those who could make things happen and I aspired to be like them. I discovered that shopping, eating out were fun, but happiness lied somewhere else. I discovered my passion; I found my dream—to entertain the world.

I had talent, enthusiasm and willingness to put in hard work and I thought I had it all. So when I knocked on doors of grand opportunities and they never opened for me, I thought that the world was yet not ready for my kind of talent. But I was not ready to give up my dream. So I decided to take one baby step at a time rather than taking a leap. I set 'Goals' to reach my dream. And it worked. I started as a trainee, then an assistant, became a coordinator and then a full-fledged writer-director. Today all the awards, hits and recognition I have, is a result of achieving those small goals I set, one at a time. Such is the power of goal setting.

How I benefited from financial goal setting?
Money is important as it opens opportunities and makes things possible. But like in the case of most other things, the power of money increases or decreases depending on the way we use it. I realized this the most after I got married. The two of us, my husband and I earned good salaries. But as we were setting up everything afresh, we almost had no money by the end of the month and had to wait for our paychecks of next month to buy anything new. Later I realized that most young couples like us, even after months or years of their marriage were mostly living paycheck to paycheck. It was primarily because of the general yuppie (young and upwardly mobile professionals) lifestyle—setting up our homes with all the latest gadgets, filling up our wardrobes with the best brands of clothing and accessories, having extra supplies—spare watches, shoes—upgrading TV and bikes almost with the pace they were launched in the market, eating out more as a need now, 'celebrating weekends', enjoying expensive holidays, *et al.*

Once when I had to request our grocer to extend the credit by a week (till we get our next paycheck), I thought that this had to stop. We, the independent, self-respecting youth could not embarrass ourselves any further. We need to immediately take control of our money, before our 'lifestyle' digs a hole in our future.

So we, my husband and I, set a simple **savings goal.** We decided to put aside 10% of our salaries in a savings account—**as soon as we got our paycheck**—and then forget about it. This was a total of Rs.10,000 between the two of us then.

With the success of our savings goal, we were further motivated to treat our money well and set some more advanced financial goals. But as none of us understood much of personal finance, simplicity remained the key. We decided that we would save Rs. 1 lakh in a fixed deposit account. And any amount we can save beyond this Rs. 1 lakh, we would start investing in other investment channels. So almost a year after we started saving, we took a step ahead and invested. We also simultaneously began reading and learning more about

personal finance in general and investment in particular. Our simple **investment goal*** was to invest 70% of our invest-able amount in shares—high risk but high gains, 10% in bonds/fixed deposits, 10% in gold/silver and 10% in real estate (this was basically the home loan installment that we owed to our bank).

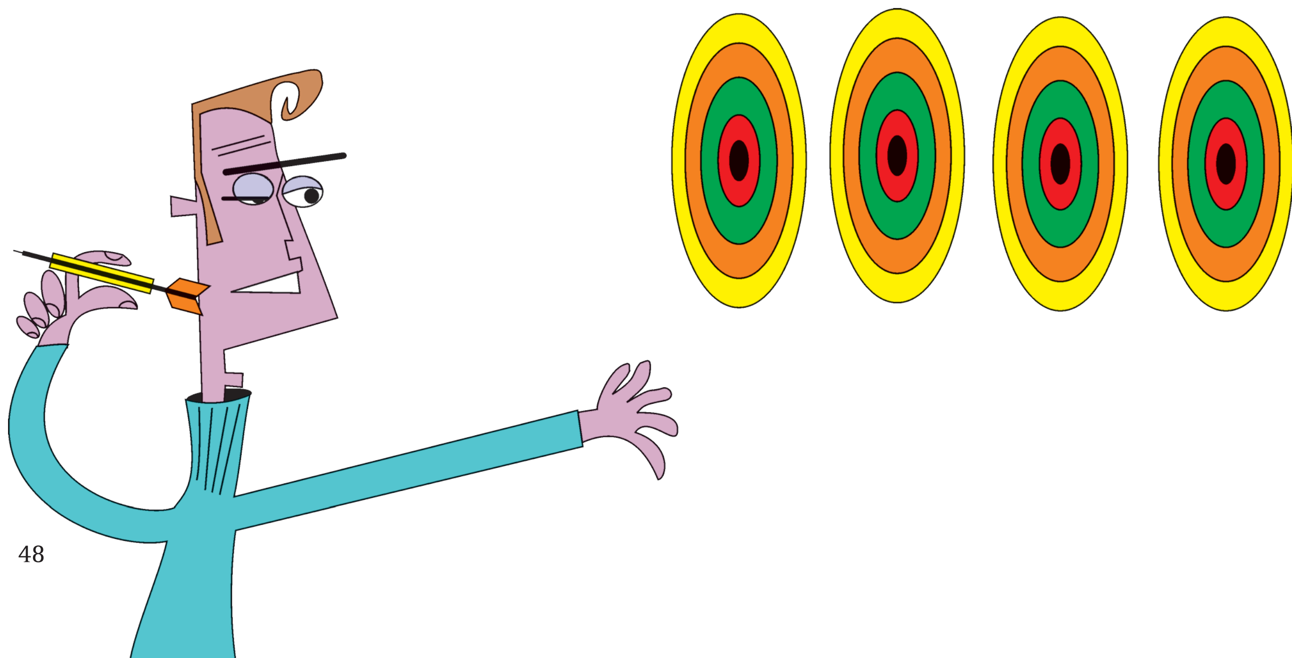
The savings and investment goals got us into a very healthy financial practice of wealth building. Both of us, within just a year, had got into the savings discipline and we did not do badly at investing either. Though I must admit, we had a tough time initially understanding the share markets and the entire game of investing. But after a few ups and downs, regular following of economic news, some reading and a simple course at a training institute helped us get the feel of investing the right way.
My husband once jokingly said that he would like to retire from work at 40 years of age with a property worth Rs. 1crore of our own and a Rs. 1 crore net worth (all savings and investments put together). This became our **retirement goal.**

Today, almost 20 years and two kids later, we are happy that we set those goals as we could work towards them. Now in our mid-forties, I had left a full time profession long back and my husband retired from his work to follow his passion—painting– with our retirement goal more than met. Our friends, who started their married life with us and like us but without any clear goals, are still struggling to get their money equations right. Every change in their lives—birth of child, education, big expenses, job shift/loss, loss in investments—would disturb their money equation and they would spend substantial time in getting it right again—until of course the next change hit them.

I am not saying that we did everything right. But at least having a goal—a target—got us thinking about the direction we needed to work in. And the joy of achieving those simple goals, like my steps towards becoming an established entertainer, got us going and improving.

My family and I, needless to say our finances, have benefited greatly from setting simple financial goals and hence, I would persuade you to give it a try. And when you also discover the power of goal setting, please advise your friends to follow it too. This way we would have the two powerful entities youth and money, moving together towards their dreams, not away from it.

** Please note that age and life cycle stage of the investor would influence the proportion of investments in different channels. Read in detail about this further in Section III on Investments.*



I Know – About Goal Setting

If you do not know where you want to be, you would not know how to get there.

All of us have dreams. But how many achieve theirs? First step in realizing any dream, financial or otherwise is to put it in writing—i.e., to set a goal. Most dreams can be made achievable through a proper goal setting and planning. Financial goal setting allows you to think before hand, where you are trying to get with your finances.

It can be likened with – Setting a target for your cricket match

Goal setting can be likened with setting targets for your cricket match. Your dream, as a cricketer or as your cricket team's captain could be to become the greatest player/team in cricket. What will make this dream become real are the goals you set for yourself/for your team. Goals like winning matches, scoring maximum centuries, taking the highest number of wickets would make your dream look achievable.

Set SMART goals

Be Specific –
e.g. I want to be the highest scorer of runs rather than I want to play well in today's match.
E.g. I want to buy a Bajaj Pulsar bike within a year, rather than I want to own some vehicle some day.

Set a Measurable goal –
E.g. I want to score a century/100 runs today.
E.g. I want to set aside Rs.1000 every month in my savings account, instead of wanting to save a lot of money.

Set an Achievable goal –

Let the goal be Realistic –
E.g. If you are team's lead bowler then, "*I want to take at least one wicket*" seems to be too obvious and easy and may not motivate you enough to taste the best of your potential.

"I want to take all the wickets" seems to be close to impossible.

Hence, a goal in between—maybe three wickets—could be an achievable yet motivating goal.

E.g. if your net earning is around Rs.10,000 a month then saving Rs.1000 is an achievable and energizing goal than a Rs.100 or a Rs. 8000 saving every month.

Set a Timeline
E.g. I want to play international cricket in another five years.
E.g. I want to save Rs.15000 by the end of this year.

I do – The goal setting process: Step 1

The following worksheets provide a step-by-step goal setting approach.

Step 1 – Describe your goal

(Write it on the space provided below, use separate sheets for different goals)
E.g. I want to win this match/tournament/be the man of the match etc.

____ ______________________________

____

Take a cue from the list mentioned below to identify your financial goals. Your goals could be different from those mentioned here based on your lifestyle, lifecycle needs and values.

List 1.1 – Common financial goals
Increasing income/reducing expenses.
Building a cash reserve—savings.
Clearing credit card debt (or repaying any other loan/debt).
Funding higher education.
Buying a vehicle (or any other high value item like PC/laptop etc.).
Funding travel/holiday.
Buying an investment —shares, mutual fund, gold, real estate etc.
Buying/making/repairing the house.
Investing in business.
Getting married.
Becoming a parent.
Planning for a secured old age.

I do – The goal setting process: Step 2

Step 2 –Quantify your goal

(Write your best estimate of the amount of money you will need to achieve your goal in the box provided below)
E.g. I need to make at least 75 runs to achieve my above goal

Rs.

What you need to know to estimate the amount of money needed to reach your goal;
1. In case of Money Management Goals (like those in blue color in list 1.1), you need—knowledge of your money values, current lifestyle, your needs, and your records such as account of income and expenses, bank statements/passbook, credit card statements/bills.

2. In case of Funding Goals (like those in pink color in list 1.1), you need to know– your current savings and the cost of the items you need to fund. Cost of the items can be checked from relevant sources—e.g. stores for a product, educational institutions for a course and travel agencies for holidays.

3. In case of Investment Goals (like those in green color in list 1.1), you need knowledge of market prices of the investments and/or the various components of the investment as in case of house/business.

4. In case of Life Cycle Goals (like those in red color in list 1.1), you would need to know your current cost of living and the impact of the lifecycle changes. E.g. marriage or having a baby would increase your expenses and retirement would commonly mean a drop in income.

Note that in case of Investment goals and Life cycle goals, your cost estimate will be impacted by inflation which is discussed later in the book. (Refer Section 3 page 65)

I do – The goal setting process: Step 3

Step 3 – Define the timeline

Note the timeline - by when do you wish to reach your goal - in the box below.

(Note the timeline in the box below—by when do you wish to reach your goal. E.g. we have one innings/ 50 overs to achieve our goal.)

Days/Months/Years

Why is setting a timeline important?
The challenges and hence the course of action will be different for a 20-20 match, a one-day match and a test match. The same strategy will not work for the three formats. Stamina, perseverance and strategy would play an important role in a test match whereas speed, energy and teamwork will be more important in a short 20-20 match.

Similarly in personal finance, the timeline—whether you wish to achieve your goal in days or months or years will heavily impact:

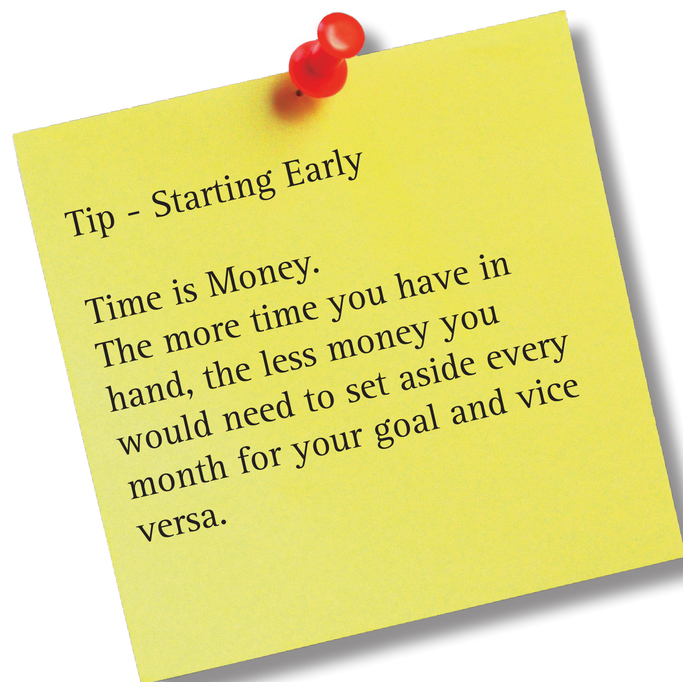
1. The cost, as inflation will play an important role in long term just like weather plays a much more important role in a test match than in a 20-20 match.

2. Your financial plan, e.g. consider the following case
   You are currently saving Rs.5000 a month from your income

   Case A. If you wish to buy a PC worth Rs.20,000 in a year's time, then your financial plan would be to continue to save and fund the PC from the savings.

   Case B. If you wish to buy the PC in 3 months time, then your financial plan will have to look at increasing income or reducing expenses to save more or investing for returns to make up for the Rs. 5000 shortfall or borrow that amount for the time being and repay it through your future savings.

I Know – Time is Money



Consider the case of Ram and Sham. They have been best of friends and interestingly have been having similar life, well almost. They are of the same age, went to the same school, studied at the same polytechnic, got jobs in the same company and worked there on the same level. They even had the same retirement goal—both wished to retire from their jobs when they had a sum of Rs.10,00,000 in their retirement accounts. The only difference was the way they went about achieving the retirement goal.

Ram started to save and invest towards his retirement goal on his 20th birthday, just a few months after he started his job. He started by putting his Diwali bonus of Rs.10,000 in a fixed deposit. He then kept on adding Rs. 10,000 a year (i.e. less than Rs.1000 a month).

Whereas Sham waited till he had 'enough' money left to save for his goal, despite Ram's repeated advice. On his 31st birthday, Sham finally followed Ram's advice and plan, and put Rs.30,000 in a fixed deposit. By then, even Ram could contribute Rs.20,000 a year to his 'retirement account'. Thereafter, Ram and Sham kept contributing Rs.20,000 and Rs. 30,000 a year respectively.

So when could the two friends meet their retirement goals? Look out for the answer and detailed calculations of how Ram and Sham's wealth built up on the next page.

I Know – Time is Money

Considering that their Fixed Deposit accounts earned the same rate of interest throughout, say 7% per year, the calculations are given in the table below.

Age	Ram's retirement account	Sham's retirement account
20 years	Rs. 10,000	Nil
30 years	Rs 1,67,507.51	Nil
31 years	Rs.2,09,933.03	Rs.30,000
40 years	Rs.6,42,282	Rs.4,39,647.22
45 years	Rs.10,23,899.92	Rs.8,01,226.68
48years	Rs.13,23,120.29	Rs.10,84,735.43
Total amount put in	Rs.4,50,000	Rs. 5,10,000
No. of years of savings	28 years	17 years
Total amount put in	Rs.4,50,000	Rs. 5,10,000
Total Interest earned	Rs.8,73,120.29	Rs.5,74,735.43

Moral of the story—Time is Money

Ram, by giving his retirement account MORE TIME to build up, had to put in LESS MONEY vis-à-vis Sham. Though the two friends decided to retire at the same age (48 years), Ram, thanks to his extra 11 years of small savings, by putting Rs.60,000 less than Sham, could retire with Rs.2,38,384.86 more than him. Discover the power of compounding on page 138 of this book.

I do – The goal setting process: Outcome

Combine the steps 1-3 of the goal setting process mentioned in the preceding pages and write down your financial goal in bold letters below:

(E.g. I want to buy a Bajaj Pulsar bike that costs Rs.40,000 now within a year.)

____

____

Note all the financial goals that you can think of in the table given below. This table should give you a list of all your goals at a glance.

Goal No.	Description	Cost	Timeline	Priority
1				Low/high/top
2				Low/high/top
3				Low/high/top
4				Low/high/top
5				Low/high/top
6				Low/high/top

Table 1.2—My financial goals

Once you enlist your financial goals, take a look at your current financial position—your income, expenses, savings, investments, debts and liabilities before setting out to start financial planning.

I Know – Before financial planning

On reviewing your financial position against your financial goals, you may find yourself in one of the following situations.

Each situation is different and needs to be tackled differently. Hence, your financial plan will be based on the situation you are in.

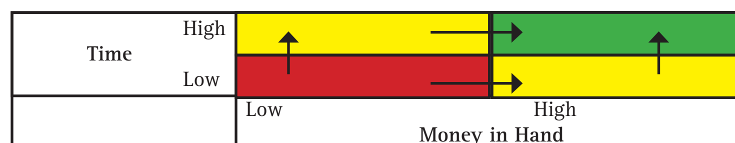


Fig. 1.3 - Financial positions in relation to goals

1. **You have enough money and time on hand to set aside for all your goals.**

   You are in the green position. This is the best situation, when you have both money and time on your side. This is quite a possible case for financially independent young people who are conscious (and cautious) about their spending habits (like you). If this is true for you, then you have a strong chance of accomplishing all your goals sooner than later.

   No matter whatever your situation is right now, you should plan to get into this green position to have the best shot at achieving **financial freedom*.**

2. **You have more money but lesser time to accomplish your goals. Or, you have more time at hand but lesser money to reach your goal.**

   If any of the above statements is true for you, you are in the yellow position. Achieving all your goals at a time may seem like a daunting task in either case. By giving yourself more time to achieve the goals or by increasing your income and/or reducing your expenses, you can jump to the best position—green.

   But for the moment, you will have to make choices, prioritize the goals and go about achieving them one at a time.

3. **You could be in the red position (tight position) when with lesser money on hand you must achieve your goal urgently.**

   This could be the case if you currently have a lot of liabilities/debts and no/less savings. In such a situation, you will have to delay all your other goals for an immediate one—repaying debt and building savings. This would help you to secure and stabilize your present financial position and move from the red position to either of the yellow positions.

**Financial freedom describes a well-planned lifestyle where one no longer requires to work for income to cover his/her expenses.*

Guide Me!!!

Ravi asks

Hi! 1 am 21 years old. I have joined work in the IT sector six months back and earn Rs.25,000 per month salary (i.e., about Rs.12,000 take-home after deductions). Last six months that I received my salary, I almost spent everything—treating friends, buying gifts for my near and dear ones, buying myself some feel good stuff etc But my father, a bank manager, wants me to cut down on the spending and start saving. Save for what? My life looks cool now and I want to enjoy it fully.

Could you reason Ravi and enlist the possible goals a person his age (earning and without any responsibilities yet) should set for him/herself? Use the space below. Look for Mrs. Bharati's explanation at the end of the section.

Help Me!!!

Shravan calls for help

Hi! 1 am a 24-year-old electrician. I earn from contract works that I take up—from households, offices, farms and workshops. My income thus is not steady. Some weeks I earn a lot while others could go with hardly any work. I am the youngest of 4 siblings and live with my ageing parents and a blind elder brother. Both my sisters are married. I had taken loan from a bank for their weddings. Now most of my income is spent in funding our daily needs, health care and in repaying installments of the loan. And even if I save anything, that gets consumed in my not so good days. I am the only earning member of my family and have been feeling pressured lately. I am working overtime and thinking whether I should take up a job. I am so confused, I don't know what to do.

Shravan seems to have too many goals on his mind. Can you help him write his financial goals one by one and then help him prioritize so that he feels less pressured and knows exactly where to start. Use the space below. Look for Mrs. Bharati's explanation at the end of the section.

Advise Me!!!

Gita has goals

I just learnt about financial goal setting and want to give it a shot. 1 am a 21-year-old working in a call center for the last one year. I make good money (Rs. 2.41 lakh p.a.), and I wish to use it wisely. So I have set following goals for myself:

1. Save for further education (2-4 years timeline).
2. Invest in stock markets to help my money grow (immediate).
3. Buy a house—my company gives home loans when I complete 5 years in the job.
4. Fund a holiday to a nearby hill station.
5. Repay credit card debt of Rs. 25000.

Gita seems to have good intentions but is she getting it right? Use the space below to write your understanding of Gita's approach. Look for Mrs. Bharati's explanation at the end of the section.

Mrs. Bharati's Common Money Sense Answers

Dear Ravi,

You are one of those lucky people who does not have any responsibilities and have an opportunity to start building your wealth right away. But many young people, like you, often have this attitude that they regret later because of the lost time and opportunity. In your own words, life looks cool 'now'. What about future? You say you want to enjoy your life 'fully'. You are just 21 now and have more than twice or thrice as much life to live. As a wise and responsible person, you should ask yourself the following questions:

- Will I be earning all my life?
- Will my life always look the same (as today)?
- Will the outside situation (the economy, job market, etc) always improve or at least stay the same?
- Today my father can still support me financially but am I ready myself for any emergency (accidents, job loss, health emergency etc)? Will I have to depend on him forever to bail me out of contingencies?

The good news is that most young people grow out of this phase of 'why think about the future, live the moment'. (Though I do agree that you should make the most of every moment and not **worry** about future.) I am sure that in a couple of years (or at worst 5 years), you will get an answer to your own questions. But the point is, do you want to lose those 5 years i.e., 60 months of income—and as many months of a missed opportunity to build your wealth. Imagine if you save Rs.2,000 a month (i.e. Rs. 24000 a year) in a fixed deposit, you can expect to have a balance of about Rs. 1.5 lakh by then(@6% interest*)

If you still have a question on why a young person of your age should save, I have only one answer. It is actually important only for people your age to save. People my age (past 40s) may just have 10 more years of responsibilities. Whether we cruised through effortlessly or struggled our way till this age, we have managed to get past most of our responsibilities like:

1. Higher education.

2. Marriage.

** Discover the power of compounding on page 138 of the book.*

3. Children—birth, their education, their demands and necessities.

4. Healthcare—expenses and insurance.

5. Our possessions—a bike, then a car, computer, phones, cameras, TV etc.—that just gets bigger and bigger, and of course our house that we made home.

6. Supporting those who supported us—our parents and other near and dear ones.

7. Some of us also chose to quit employment and start their own businesses.

8. Contributing towards our retirement and old age needs so that we can lead a similar lifestyle (if not improved) on our own, in times when we have no income.

9. Not to mention some financial emergencies like income loss, sudden expenses.

So my friend, start thinking about these small realities of life, set your goals and work towards achieving them effortlessly NOW, before it gets too late. Time is money and you have both time and money on hand, so make the most of them to be able to fully enjoy your FULL life.

Best wishes,
Mrs. Bharati

Dear Shravan,

It is good to see you standing by your family and shouldering the responsibilities. But you seem to be having too many things on your mind, financially. I would suggest you a 3-step approach to get out of this confusion:

1. Pen the things on your mind in the form of precise goals.

2. Prioritize them based on urgency and cost of each goal.

3. Go one-by-one—achieving one goal at a time.

The 3 main goals that I can see from your letter are—loan repayment, improving and stabilizing household income and building reserves (savings). According to me, they should be prioritized in the order mentioned.

Loan repayment should be your biggest priority as it is your debt—a commitment to external agency and also a very costly one. If you delay repaying your loan, it will add interest and increase the amount you would need to payback—further increasing your tensions. You will have to figure out a smart way to meet this goal, but this should be the immediate goal.

Stabilizing your household income would be another important goal as unless you have a steady flow of money, you cannot plan well. When you specify a goal accurately, you can work on it effectively. Like in your case, you are just looking at your own income; why not think about 'household' income? This way you can look at the other members of your household contributing to the income in some way.

Building reserves is a very important goal as it can act as a shock absorber and can smoothen your financial situation over a period of time. But Shravan, in your case, this can wait till you have achieved the first two goals as they are more urgent.

Once you list the exact goals and prioritize them, things would start seeming simpler and achievable to you.

Best wishes,
Mrs. Bharati

Dear Gita,

I must appreciate your initiative to learn about and practice goal setting. And I must add that you have done your homework well and set for yourself some reasonable goals. Had it not been for your goal number 5—repaying credit card debt—your work could have passed as a remarkable effort.

But with Rs.25000 debt on your credit card, you should not be thinking about any other goal just yet. Your most urgent goal and the only one till you achieve it, must be to pay back your debt.

Credit card companies charge late fees and heavy interests on a monthly basis on the payments due from you. If you do not timely repay the total amount due, you may end up paying twice or thrice the amount you borrowed within few months.

So think about it seriously. And add another goal to your list:

Always make timely and full payments due on the credit card

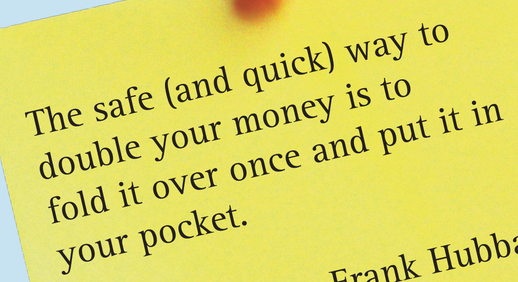
Best wishes,
Mrs. Bharati

Key Points—ICanDo Financial Goal Setting

1. Goal setting is crucial for effective financial planning.
2. Set simple, measurable goals.
3. Set a realistic timeline for the goal.
4. Identify your financial situation and prioritize your financial goals accordingly.
5. Commit to achieving your goals.

Part III

Investment



I Can—Mrs. Bharati's Common Money Sense

When I was in primary school, I had so many friends. Everyone would offer me something from his/her Tiffin (that's a big thing in school). No one in the class got birthday invitations from all classmates. But I did. My birthday was attended by everyone I invited. I loved all the importance I was getting. I loved to act pricey at times. I thought I was very popular in school.

Then we advanced to a different secondary school. And everything changed. I was just another girl in the class. No special favors, no privileges. I was disheartened when no one turned up for my birthday party that year. All my classmates went for another boy's birthday that fell on the same day as mine. I cried badly that day. I would have been 10-11 years old. I complained to my parents about this behavior of my so-called friends. And I still remember what my father said in response. He said, 'you did not invest in your friendship'.

That was the first time I heard the word - 'invest'. I didn't make much sense of it then.

But my parents later explained that the favors in primary school came to me because my mother was our school principal. And even though I had this privilege and everyone's attention early on, I did not capitalize on it. I had a plenty of friends then, but I did not 'invest' in their friendship. Instead, I sort of misused the privilege. I took it for granted. I believed that it would remain forever.

I acted pricey, poked fun at others and took undue advantage of the 'friendships'.

The incidence lasted in my memory not as much for the embarrassment it created on my birthday, as for the lessons I learnt;

'You need to 'invest' to be able to enjoy **continued** privileges.'

'Good times do not last forever.'

'You are in better position to invest in good times, but you make the best investment efforts in your bad times.'

The last lesson has its roots in the efforts I put in later to become a good friend and build my friends' trust in me.

That's when and how I learnt the importance of investing. How I learnt the actual process of investing is another interesting tale.

My first investment was in my provident fund, when I started my employment. That, because it was a compulsory deduction. I think, most of us start that way—with the compulsory contribution to our own retirement fund. Thereafter, whenever I had some surplus saving, I'd do a good old fixed deposit. The real need of understanding investing in its truest and fullest best was after my marriage when we, as a couple started taking our finances seriously. We met our savings goal and were ready to start investing, but hardly had any clear idea of investments then. We were confused between investing and saving and even investing and insurance.

Back in those days (almost 20 years back) information was not so readily available. Media was not much evolved, there was no internet and banks never had a concept of formally educating customers. Only your bank officer friends and insurance agents were your sources of some information. The stock market stories that went out of the broker community were more about losses or unrealistic profits than those about smart investment strategies.

Surprisingly, the most helpful investment learning I received was from a dietician friend of mine. Anu was my college friend who pursued profession as a dietician. She married Raj, a professor of commerce when she was just 20 years of age. They had a humble household income, almost half of ours. But they lived our equivalent lifestyle (theirs was better, they worked 9 to 5 while we slogged longer). The secret was their investments. The commerce professor—dietician duo had got their investment equation right and in Anu's words, put their money to work too. Between the 3 of them i.e. the husband –wife and their money, they made earnings as much as us.

We decided to make Anu and Raj our investment gurus (at least to begin with). Anu, a dietician by passion had a very interesting analogy for investing, which anyone could relate to. She compared investing with cooking. According to her, human beings should eat a balanced diet customized to individual nutrient needs, right from childhood. The nutritional needs in the childhood are very different from that of working adults which are also different for the elderly.

Similarly, when young, your money needs 'growth' aiding (nutrients) returns from investments. As it grows up with age and lifecycle stage, it would need a balance between growth and steady income investments. And as it matures, with you (around retirement), you'd need to give it a steady income first and then growth opportunities.

As you may not get all the required nourishment from a single food group, you'll have to include in your menu, items from various food groups. Just the same, you'd do in case of investment. You'd create a 'portfolio' of investment that has items from different asset classes (like food groups) that can together give your money the nourishment it needs. I was amazed at the similarity.

Then Raj further explained the various investment channels and the kind of returns I could expect. Equity or stock related investments (shares or equity mutual funds) provide growth, while debt investments (FDs, Bonds, Debt mutual funds) offer a steady income potential. Investments in items of value (like gold, land, commodities), would provide my money security as they would inflationproof my money to a large extent and also have growth potential.

For beginners like me, he had a simple thumb rule for creating a balanced investment portfolio based on our age. Raj said that the equity component in my portfolio should not exceed (100 minus my age)% of my total investments. So for me (at 28 years), the rule guides that if my portfolio has equity in excess of 72%, then it needs to be balanced so as not to be risky. I can balance it by increasing my debt investment or decreasing (by selling some shares/mutual fund units) equity component.

I started with that guideline, and believe me this simple thumb rule is proving effective even now (at 43). It's a long way I've come from that and have devised many a investing thumb rules for myself . But so effective is this 'balancing the portfolio' thumb rule that I have been practicing and sharing it with everyone—beginners or experts alike.

Whoever said that investing is complicated and difficult!

I've begun to believe that it's as simple and as creative as cooking a balanced meal. What you need is some knowledge about the food groups (asset classes), some idea about the nutrients (risks and returns) and a good understanding about your nutritional needs (your investment needs). If you have this right, you are ready to dish out an investment portfolio. And while balancing risks, you can be creative with your investment portfolio and learn on the way. You may want to refer to experts and recipes too. Your search for that 'ideal' portfolio for you, may soon be over.

I Know – About Investing

Investment is that activity in financial planning, which can directly help you meet your goals. Yet no other concept in personal finance is so widely misunderstood (if not ignored) as investment.

The idea behind investing your money is to put it to use in such a way that it is likely to earn more money. This happens because someone is willing to pay you interest in lieu of using your money as in the case of fixed or recurring deposits, bonds. Or because the business in which you invested your money (by buying shares) is making profits. Or the value of assets like gold, land etc. increased after you bought them.

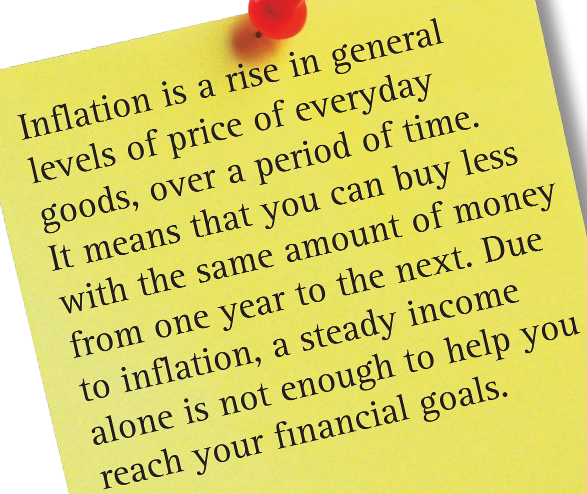
Thus, investing can be thought of as a way to **make your money work for you.**

Box 3A—Note that

1. Investing is different from saving.
2. Investing is not gambling.
3. Investing is only as risky as you want it to be for you!
4. Investing is not a get-rich-quick formula!
5. Like all other aspects of financial planning, investing is for everyone.

Why invest?

1. To stay ahead of **inflation.** Investing ensures that the purchasing power of your money is not just restored but it improves year after year.
2. To meet your **financial goals.** Invest allows you to build wealth by making your money earn steady returns and grow over a period of time.



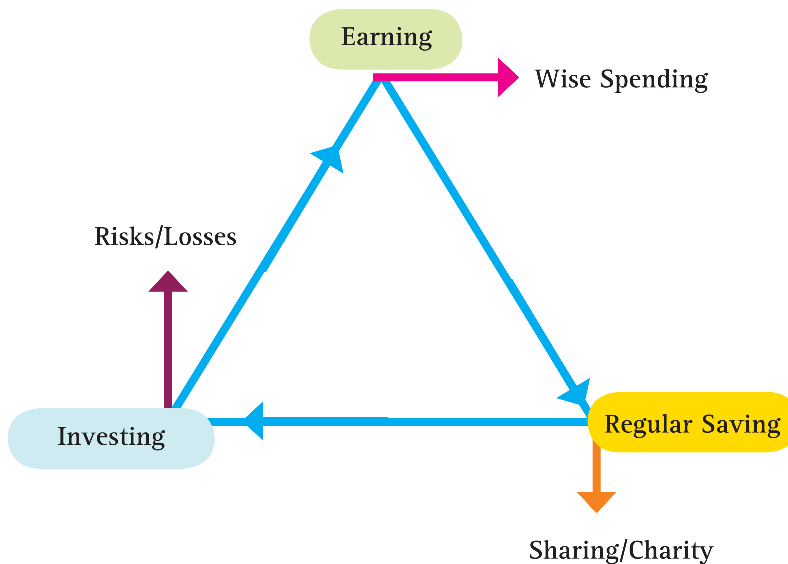
I Know – When to Start Investing

If you are wondering when is a right time to start investing, the answer is simple: Whenever you are ready:

A. with your long term savings—a reserve which you may not need immediately, and which you do not mind keeping out of reach for a while.

B. with a proper understanding about investing—the process of investing, various channels of investment and your own 'risk profile'.

If you are ready with your savings—your 'investable money', this section will help you get ready with a proper know-how of investing.



Money Spinner Explained

The figure alongside explains how you can maximize the use of your money; by spinning it (pun intended).
You can actually make more money with the money you earn by rotating it freely between your earning, saving and investment accounts.

Fig. 3.1 Money Spinner – the wise money management cycle

You can let only that part of your earnings, which is absolutely necessary, go out of the web. By doing so, you can maximize your savings. Invest from these savings, a part each in social (charity/sharing) and financial (investing) investments. And you would set your money spinner in motion. All you have to do now is to keep the money spinner in continuous motion by following the cycle. Of course, factor in some losses in investments, based on how much risk you are taking.

I do – The Process of Investing: Step Zero

Step Zero – Check your readiness– do you have 'investable' money!

Take the following quiz to know whether you have any investable money to start investing. Please note that the amount of money you have to invest is not significant. You can start investing with an amount as low as Rs. 50 per month. Hence, the words like 'healthy' 'good' 'satisfactory' are subjective and completely to your discretion. The quiz intends to answer the significant question—is that Rs.50 investable?

Place a tick in box alongside the statement/s that is/are true about you.

1. I have a healthy balance (income minus expenses) every month. ☐
2. I always allocate a portion of my income for investing (long term saving), savings for goals and for stabilizing my finances separately (refer section 1). ☐
3. I can handle any financial emergency (income loss, heavy expense) for at least 4 months without touching my long term savings. ☐
4. I have no debt or I have a strong plan to repay all the debts without needing my long term savings. ☐
5. I will not have a big problem to manage my regular expenses even if I lose a part of my investable money. ☐
6. I can easily forget about my long term savings for at least a year. ☐
7. I have complete knowledge of my financial position (refer section 1). ☐
8. I have no misunderstandings about investing (refer Box 3A). ☐

If all the above statements are true for you, then you can consider yourself ready with investable money. You can now proceed with studying this section to get proper investment know-how. If any of the above statement is currently not true for you, then refer appropriate section in this book to check how you can get it right and then take the quiz again, until you get all the 8 ticks!

I Know – The Process of Investing

The process of investing can be likened with planning and cooking a tasty and nutritious meal for you. You should not mind spending some time in learning to cook a meal that appeals to your palate but also addresses you nutritional requirements. It has both long-term and short-term benefits. Same is the case with investment. Spend some time to learn about and practice this immensely rewarding part of financial planning.

It can be likened with—Cooking a tasty and nutritious meal for yourself

Common sense says that the process of such a cooking would involve the following steps:

1. Understanding your nutritional needs and taste preferences.
2. Knowing which ingredients can give you what you need.
3. Deciding on a menu—the various items you could cook and how much.
4. Cooking a balanced meal.

Similarly, the process of investment involves:

1. Understanding your investment needs (based on your financial goals.)
2. Understanding risks and returns (an important aspect of investing).
3. Knowing various investment channels and their risk and return potential.
4. Creating a balanced 'portfolio'.

I Know – About Risks and Returns in investing

Some food items are known to be tasty like the bhel puri, pao bhaji, chaat and samosas. But they are categorised as junk food and are hardly considered nutritious. Similary there are some nutritious food items like lauki (bottle gourd) soup, salads and porridge, but how many of us consider them to be 'tasty'? What separates an expert cook from the novice is the art of balancing the two and dishing out a nutritious yet tasty meal—a perfect mix.

Risks and returns in investment can very easily be likened to taste and nutrition in cooking. Saving alone cannot give you the kind of returns that investing can. Also, returns cannot come alone; risks and returns in investing come in a package. Investing involves some risks. But remember that **investing is only as risky as you want it to be for you.**

The process of investment revolves around RISK and RETURNS.

It starts with understanding your risk profile and the returns you expect to get from your investment. It proceeds with using your knowledge of risks and returns of various investment channels. In general, investments with higher risks also stand to earn higher returns, but those returns are not guaranteed. The aim should be working towards balancing risks and returns—taking measured risks and expecting realistic returns.

Before beginning to invest you should really need to answer a few questions to check your risk tolerance. Questions like—how comfortable you would be:

a. If your investment changes in value every day.

b. To see your investment decreasing at times.

c. If your funds are locked for a certain period and you may not get them exactly when you want.

Check out the risks you may face while investing in different types of investment channels and the returns you can expect from these investments, in the next few pages.

I do – Process of Investing: Step 1

The following worksheets provide you with a step by step guidance for investing.

Step 1 – Understanding your investment needs.

(Write on the space provided, refer to your goal setting worksheets in section 2 of this book. You can use separate sheets for different goals and investment needs).

1. My financial goal ____

   ____

2. I would need Rs. (Amt* 1____________) to reach the goal

3. The investable money I have at the moment is Rs. (Amt* 2 ____________)

4. The time I have to meet the goal _T ____________ days/months/years

5. The time in years I have to meet the goal _N ____________ years

   Formula to calculate the time in years N, If your original timeline T is in days then N = **T/365**, if it is in months then N = **T/12**, if in years then **T = N**

6. More investable money I can save during this time Rs. (Amt* 3____________)

7. Balance money I would need to raise Rs. (Amt* 4 ____________)
   Use formula to calculate the balance Amt 4 = Amt 1- amt 2 –amt3

8. To meet the goal, I should get _R ____________ % per year rate of return
   Formula to calculate the rate of return R **Amt4 = $(1+ R/100)^N$**
   The formula is used by Std. X students, so do not allow it to scare you.

9. How much risk am I willing to take? (Tick the statement you find appropriate)

   a. High: I can handle a decline in my investments of up to 20% while I am willing to invest for high returns.

   b. Moderate: I cannot risk my capital (invested money). But I can take a risk on the returns. I do not expect steady returns.

   c. Low: No major risk for me. Even if that means lower returns, I want my money to earn steady returns.

Now let us summarize your investment need and define an investment objective for you. (Refer point 5, 7, 8 and 9 of this worksheet)

**Amt stands for amount*

10. My investment need to meet my financial goal is to:

    gain about Rs.(Amt.4)__________ in (N)_____ years taking high/ moderate/low risk.

    My investment objective to meet this need:

    To invest for (N)______ years in an investment channel or a mix of channels that may be high / moderate/ low in risk involved but can give approximately (R) ______% returns annually.

Once you have clearly defined your investment objective, check if it is realistic. E.g., to invest for 1 year in a low risk investment channel to get a 20% return annually is far from reality.

If your objective sounds realistic, proceed further. If not, revisit this worksheet and your financial goal so that it is realistic and achievable.

I Know – The Various Investment Channels

There are many ways you can invest your money, like there are many ingredients that go into cooking. The options are so vast that it might get even an expert investor confused.

The following chart should make it simpler for you to understand the various channels. It explains four basic ways you can invest your money, and how they are placed in the context of risks and returns.

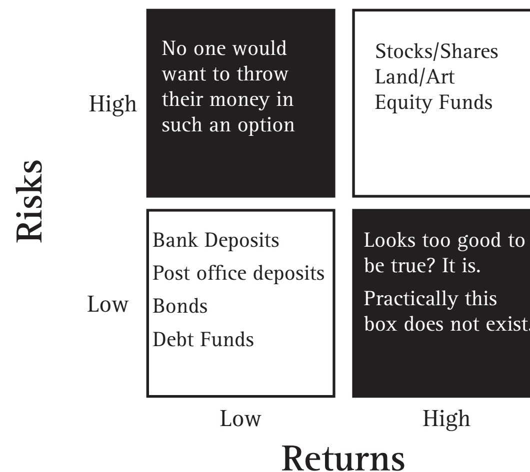


Fig3.2 Various investment channels based on risks and returns

High-risk, high-return channels are growth channels that help you build wealth by enabling your invested money grow significantly over a long-term

Low-risk, low-returns investments generally assure steady but smaller returns, helping you build wealth slowly but steadily.

Commodities like gold, silver or even land are traditionally known to rise in value along with inflation and hence secure your purchasing power despite inflation.

I Know – The various investment channels

There are many, ways you can invest, as the ones mentioned in the quadrant in Fig.3.2. But each one would fall in at least one of three basic categories of investment mentioned below. You mostly invest your money, by:

1. Lending it

If you lend your investable money to government, banks or businesses by buying their **bonds** or opening a **fixed/recurring deposit account,** these organizations will pay you *interest* for allowing them to use your money.

Your money thus can earn steady returns by way of interest.

2. Buying share in business capital and profits

By buying **share in profitable businesses,** your investment can grow in two ways:

a. The company may pay you a **dividend**—your share of profit

b. The shares of the company may **increase in value.**

3. Buying an item of value

You can buy things that may increase in market value, such as **gold, land, house** or collectibles like a **piece of art** or even stamps. You can make money by selling the asset for more than what you paid for.

Although not an investment channel, starting your own business may well be considered as an investment option. If you have the aptitude and necessary skill/talent along with a profitable business idea and a huge risk taking capacity, you may want to consider this as an option.

I know - Investment Channels Risks and Returns

Investment Channel	Types of risks involved	Expected returns*
Lending it to institutions ■ Fixed Deposit (FD) ■ Recurring Deposit (RD) ■ Post Office Small Savings ■ Government Bonds ■ Corporate Bonds ■ Debt Mutual Funds	Interest Rate Risk—The interest rate, though mostly stable may change with economic changes and hence affect your returns. Credit Risk—A small risk of organizations you lend to, not paying back. This risk is lesser while lending to the government. Liquidity Risk—These are generally fixed period investments. It is not easy to withdraw them before maturity.	From 5% up to 10% Other benefits- 1. Relatively stable returns
Buying Shares ■ Offered directly by companies through an Initial Public Offer (IPO) ■ From stock markets ■ Investing through equity mutual funds	Market Risk—the price of stocks is set by the market forces—supply and demand. If there is a high demand for a stock, the price will rise. But if there is more supply than demand for the stock, the price will fall. So expect fluctuation in market prices and thus value of your investment from day to day. Capital Risk—Risk of losing all the money you invested, depending upon what stock you invest your money in.	Around 10-20% Other benefits- 1. Tax exemption on long term capital gains - Gains from trading stocks over a longer term (more than 1 year) are exempt from income tax 2. Being a part owner, you get to vote for some company decisions
Buying items of value ■ Commodities like oil, Gold, silver, etc ■ Land and real estate	Market Risk—as in the case of shares, the market price for assets change based on demand—supply gap. Liquidity Risk—It may be difficult to sell off this investment e.g. selling land or real estate in parts. Or finding takers for art when you want to sell it.	Returns are variable based on what you invest in, where and when. Other benefits- 1.These investments essentially inflation-proof your money. And with prices going up, you can expect to make profits.

Fig. 3.3 Understanding Risk - Returns for different investment channels

* *The rate of returns given is approximate and historical. Check for exact rates at that point in time.*

I do – Process of Investing: Step 2

Step 2 – Investment channels for your investment needs.

(To work the following sheet, refer to your Step 1 worksheet of this section and Fig 3.3. Please use separate sheets for different investment needs.)

1. My investment need to meet my financial goal is to gain about Rs.__________ in _____ years taking high/moderate/low risk.

This is a need for (tick whichever appropriate):

- Securing against inflation ☐
- Earning steady returns ☐
- Growing money ☐

My investment objective to meet this need:

To invest for ______ years in an investment channel or a mix of channels that may be high moderate/low in risk involved but can give approximately (R)______% returns annually.

2. The investment channels suitable for me to meet my investment objective are:

To understand which channels may be appropriate for me, compare the table of risk and returns for different channels (Fig 3.3) with your investment objective. And see if the investable amount (what you have currently and may have on a regular basis later) is sufficient and suitable for this channel of investment.

Place a tick in the box/es alongside the investment channel/s you find best suited for your need.

☐ Fixed deposit ☐ Shares

☐ Recurring deposit ☐ Equity Mutual Fund

☐ Post office schemes ☐ Gold/Silver

☐ Bonds/ Debt Mutual Fund ☐ Land/ Real Estate

☐ Other ____

3. Get more information from authentic sources on the investment channels you've ticked

I do – Process of Investing: Step 3

Step 3 – Summary of all your Investment needs

(Refer to your Step 2 worksheet—all the separate sheets you may have used for different investment needs—of this section. Use a separate sheet, if the rows in the table below are insufficient)

Use the following guideline to fill up the summary table given below.

1. **Investment need:** Write the description of your investment needs in the top rows. On the row below write if it is a need for securing the purchasing power/earning steady returns or growing money.

2. **Expected Returns:** Mark **Low** in the table if you expect an annual return of up to 5%, **Moderate** if you expect an annual return between 5% to 8%, **High** if the expected annual return is above 8%.

3. **Risk Tolerance:** From the previous worksheets, mark the risk you are willing to take for that specific investment need.

4. **Investment term:** Write short-term if you wish to be invested for less than a year, medium-term if it is between 1 to 2 years, and long-term if the investment term is more than 2 years.

5. **Suitable investment channels:** After working the worksheet in step 2, you would have collected basic information on the various investment channels. And maybe you would have even thought of some channels that seem to be most suitable for you. Write these channels in the last column alongside their respective investment needs.

No.	Investment need	Expected Returns	My Risk tolerance	Investment term	Suitable investment channels
1.		High/ low/ moderate	High/ low/ moderate	Short/ medium/ long	
2.		High/ low/ moderate	High/ low/ moderate	Short/ medium/ long	
3.		High/ low/ moderate	High/ low/ moderate	Short/ medium/ long	
4.		High/ low/ moderate	High/ low/ moderate	Short/ medium/ long	

Step 4 – Designing your Investment Portfolio

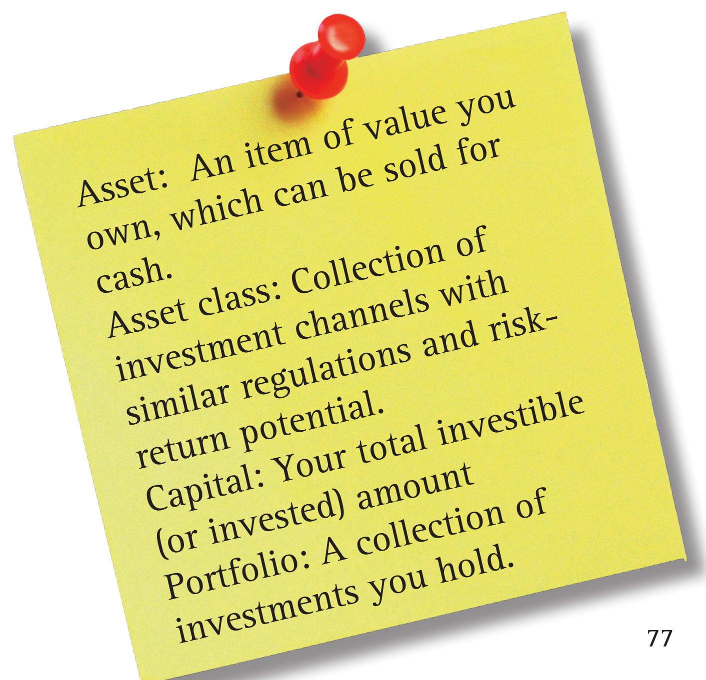
(Write in the table below, refer to your Step 1 and Step 3 worksheets)

Worksheet 3.4 - My Investments at a glance

No.	Investment Need	Investment Channel/ Asset Class*See box	Investible Amount (Amt. 2+Amt. 3)	% of Total Investment (formula below)
1.				
2.				
3.				
4.				
	Total Capital*See box		Rs. Capital	100%

To calculate percentage composition of each asset class in your portfolio:

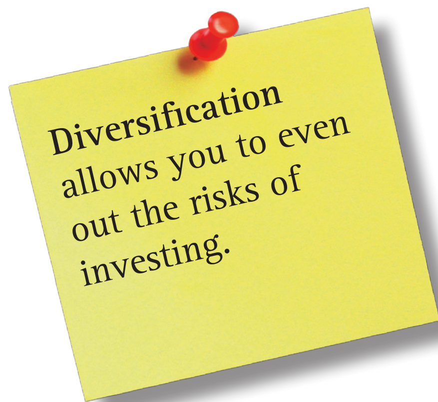
$$\% \text{ of each asset class} = \frac{\text{Amount for that asset class}}{\text{Total Capital}} \times 100$$



Step 4 – Designing your Investment Portfolio

The key to any good investment strategy is to balance the risks and returns—minimize the risks and maximize the returns, to a possible extent.

This is possible through what is known as diversification of your investment portfolio. It may seem to be a very complex thing. But simply put, it says 'do not put all the eggs in one basket'.



To start with, if you have lesser funds for investing, it would make sense to stick to just one or two types of investments. But as you go on building the portfolio, it is important to diversify.

A well-diversified portfolio is like a balanced whole meal. It should constitute investments in different channels to serve the 3 main investment needs:

1. Securing the purchasing power of your money over a long term.

Invest in—Gold, silver, land. Largely known to counter inflation, these assets can even appreciate significantly and give bigger gains in long term.

2. Earning steady returns with a practically no (or low) risk to the invested money.

Invest in—FD/RD (deposits), bonds, post office savings schemes, debt mutual fund.

3. Allowing your money to grow by taking some measured risks.

Invest in—Shares, equity mutual fund.

The proportion of each would depend on your risk tolerance and the time/stage at which you start investing (i.e., with the time you have with you to stay invested)

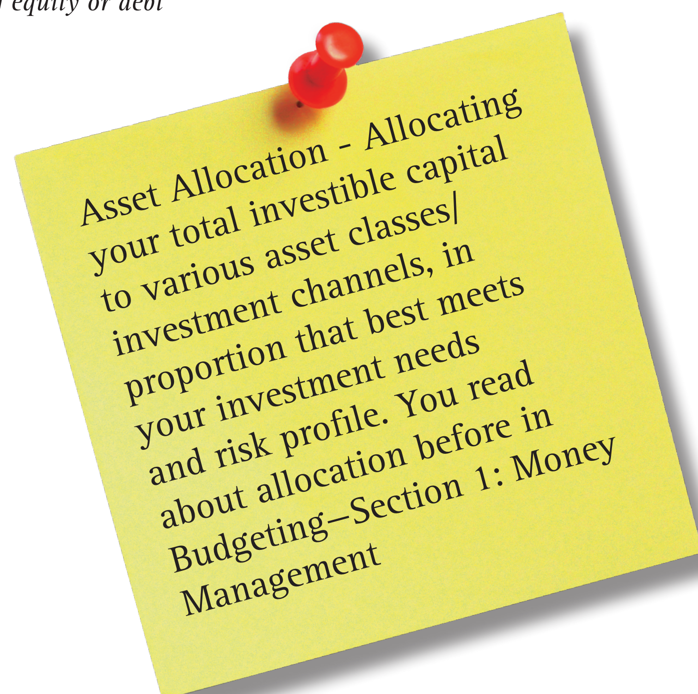
For older people, such as retirees, bonds/deposits are an important type of investment because they give steady, assured returns at a higher rate than savings accounts. But for long-term younger investors, 'growing money' to have a wealthier future may make more sense. Therefore, a smaller portion of investments earning steady returns and a bigger portion of the ones that would help you 'grow your money', is advisable early in life, with the balance gradually switching as you reach retirement.

I do – Process of Investing: Step 5

Step 5 – Balancing your investment portfolio.

(Use the following checklist to check and balance risks and returns in your investment portfolio—refer worksheet 3.41. Place a tick alongside the tasks you have completed. This checklist can help you before starting investment and also after investing to review and balance the portfolio at a 6 to 12 months interval.)

1. I am investing only the 'investable' amount in this portfolio. ☐
2. I have more than one asset class in my portfolio. ☐
3. The composition of my portfolio is in line with my risk tolerance. ☐
   If it is not then balance it. Reduce equity portion to reduce risk.
4. The percentage of equity in my portfolio, does not exceed (100 minus my age). ☐
   If it does, then understand that you may be taking more risk than you should at your age. If you wish to balance this, sell some of your high risk–return equity portion.
5. The portfolio is in line with my investment needs. ☐
6. First time check of the portfolio. My current asset allocation is right for my investment needs. ☐
   If it is not, then work out the proportion that best meets your needs You'll need to maintain this allocation - your target asset allocation
7. For periodic reviewing later, My allocation is according to my target asset allocation ☐
   If it is not, then balance it by selling/adding equity or debt



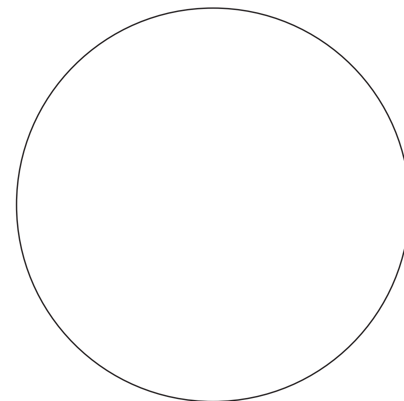
I do – Process of Investing: Step 6

Step 6 – Asset Allocation in your investment portfolio.

(Refer to worksheet 3.41. Use the circle to create your own pie chart of asset allocation in your investment portfolio. Take a clue from the sample provided. You can use Microsoft Office Excel to create a pie chart. You would need to refer to this every time you review your portfolio)

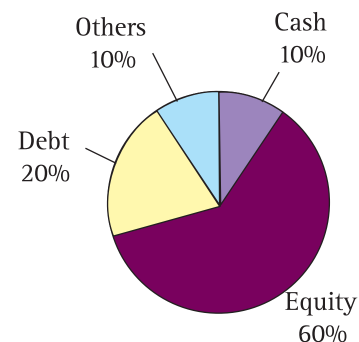
Worksheet 3.6– Target Asset allocation in your Investment Portfolio

No.	Investment channel/ Asset Class	% of total investment
1.	Cash	
2.	Debt	
3.	Equity	
4.	Others Land/gold/ Commodities	
	Total	100%



Debt: All investments that involve lending your money to earn steady returns, including provident fund and investments in debt mutual funds.

Equity: Investments in shares/ stocks with an intent to grow your money by making profits, including your company's employee stock options and investments in equity mutual funds.



Sample

I do – Process of Investing: Step 7

Step 7 – Tracking your investment portfolio.

Given below are worksheets to track the individual asset classes in your investment portfolio. Use these worksheets every month—make your own separate worksheets for each month. Use Microsoft Office Excel or a pen and paper.

Month: ____________________

Asset Class I – Cash

No.	Description	Amount
1.	Cash in hand	Rs.
2.	Savings account 1	Rs.
3.	Savings account 1I	Rs.
4.	Savings account III	Rs.
	Total Cash **(Amount C)**	Rs.

Asset Class II – Other items of value

No.	Asset	Holding at start of month		Bought this month		Sold this month		Net holding amount at month end*
		Units	Value (amt)	Units	Amount	Units	Amount	
1.	Gold		Rs.		Rs.		Rs.	Rs.
2.			Rs.		Rs.		Rs.	Rs.
3.			Rs.		Rs.		Rs.	Rs.
4.			Rs.		Rs.		Rs.	Rs.
	Total of asset class II **(Amount O)**							Rs.

** Net holding amount = Holding at start of month + Value of asset bought –Value of asset sold this month at month end*

Month: ____________________

Asset Class III – Equity **Target portfolio allocation = __________%**

No.	Description	Amount Invested	Interest/ Dividend	Maturity period/ date	Value at maturity	Today's Value*
1.		Rs.	Rs.			Rs.
2.		Rs.	Rs.			Rs.
3.		Rs.	Rs.			Rs.
4.		Rs.	Rs.			Rs.
	Debt Mutual Fund	Amount Invested as at the start of month	Transaction this month (+if bought/ - if sold) Units	Amount	Units	Net amount**
5.		Rs.		Rs.		Rs.
6.		Rs.		Rs.		Rs.
	Total of Debt **(Amount D)**					Rs.

Worksheet Guidelines

1. Stock/ Equity mutual fund—enlist all the stocks and/or mutual fund that you have invested in.

2. No. of Shares/Units—write the number that you have at the beginning of the month.

3. Value at start of the month—Net value at last month end will be your value at start of this month.

4. Transactions this month—if you have bought the same shares/mutual fund write a (+) before the no. of units and the amount. If you have sold any units write a (-) sign. If you have both bought and sold you may want to write the transactions one below the other in the same cell of the table. Use a different row if you have bought a new share/mutual fund

5. Net holding at month end (in units/amount) = Your initial investment + transaction this month if it is a buy (+) transaction, the units/amount will be added to the initial, if it's a sell (-) it would be subtracted from the initial investment.

**Note for calculating today's value of your debt investment:*
Today's value = Amount invested + All the dividends received so far
(Assuming, that you haven't touched your debt investment since you invested in it)
***Net amount in debt mutual fund is calculated the same way as net amount in equity mutual fund. Refer to the previous worksheet.*

Month: ____________________

Asset Class IV – Debts **Target portfolio allocation = __________%**

No.	Description	Amount Invested	Interest/ Dividend	Maturity period/ date	Value at maturity	Today's Value*
1.		Rs.	Rs.			Rs.
2.		Rs.	Rs.			Rs.
3.		Rs.	Rs.			Rs.
4.		Rs.	Rs.			Rs.
	Debt Mutual Fund	Amount Invested as at the start of month	Transaction this month (+if bought/ – if sold) Units	Amount	Units	Net amount**
5.		Rs.		Rs.		Rs.
6.		Rs.		Rs.		Rs.
	Total of Debt **(Amount D)**					Rs.

**Note for calculating today's value of your debt investment:*
Today's value = Amount invested + All the dividends received so far
(Assuming, that you haven't touched your debt investment since you invested in it)
***Net amount in debt mutual fund is calculated the same way as net amount in equity mutual fund. Refer to the previous worksheet.*

Step 8 – Profit/Loss Review of your Equity Portfolio

Use the table below to review your equity portfolio for returns on your equity investments. It is advisable to do this review at least every 6 months or more often if you do frequent transactions (buy/sell). Use Microsoft Office Excel or a pen and paper for every review. Refer guidelines given on the next page.

Review Date:

No.		1.	2.	3.	4.		5.	6.
Stock name						Mutual Fund		
S A L E	No. of shares sold							
	Sale date							
	Sale Rate							
Amount recovered A = No. X Sale rate								
Purchase	Purchase date/s							
	Purchase cost/s							
Amount invested I = No. X Purchase Cost								
Profit/Loss R = A – I								
% Returns								

Worksheet Guidelines

1. Use the worksheet only for the no. of shares/mutual funds you have sold during your review period. Calculate the amount invested for only such number of shares. E.g., if you bought 100 shares of ABC Co., but sold only 50 during the review period, then calculate only for 50 shares.

2. To correctly determine profit/loss for shares of the same company bought and sold at different times or prices, use the 'FIFO—First In, First Out' rule. Consider the dates and prices of the shares purchased first in your sequence of transactions and move one by one. E.g. in the above example, if the 100 shares you have bought at different times, say;

   40 shares @ Rs. 12 on April 1, and

   60 shares @ Rs. 11 on April 10 and

   sold 50 shares @ Rs. 15 on October 31,

   then entry into your worksheet columns should look as the one shown below.

No.	1.
Stockname	ABC Co.
No. of shares sold	50
Sale date	31/10/09
Sale rate	Rs.15
Amount recovered	Rs.750
Purchase date/s	1/4/09, 10/4/09
Purchase cost/s	40@ Rs.12; 10@ Rs.11
Amount Invested	Rs.590
Profit/Loss	Rs. 160
% Returns	27.11%

   You may want to use separate columns for the same stock bought/sold on different dates/prices for simplicity of calculations.

3. You may want to add all the fees and taxes you paid while buying the shares to your amount invested. Similarly subtract the fees and taxes from the amount recovered while selling those shares.

4. Note that the % returns are for that period of time during which you are holding those shares. In the above example it is 27.11% for the 7 months between purchase and sale.

I do – Process of Investing: Step 9

Step 9 – Review of your investment portfolio

Use the table below to review your entire investment portfolio for asset allocation as on the review date. It's advisable to do this review at least every 6-12 months, and then balance your investment portfolio as per your target allocation. Refer to Step 6 worksheet for target allocation and Step 7 worksheet of your review month for value of your individual asset classes. Also, refer the guidelines below.

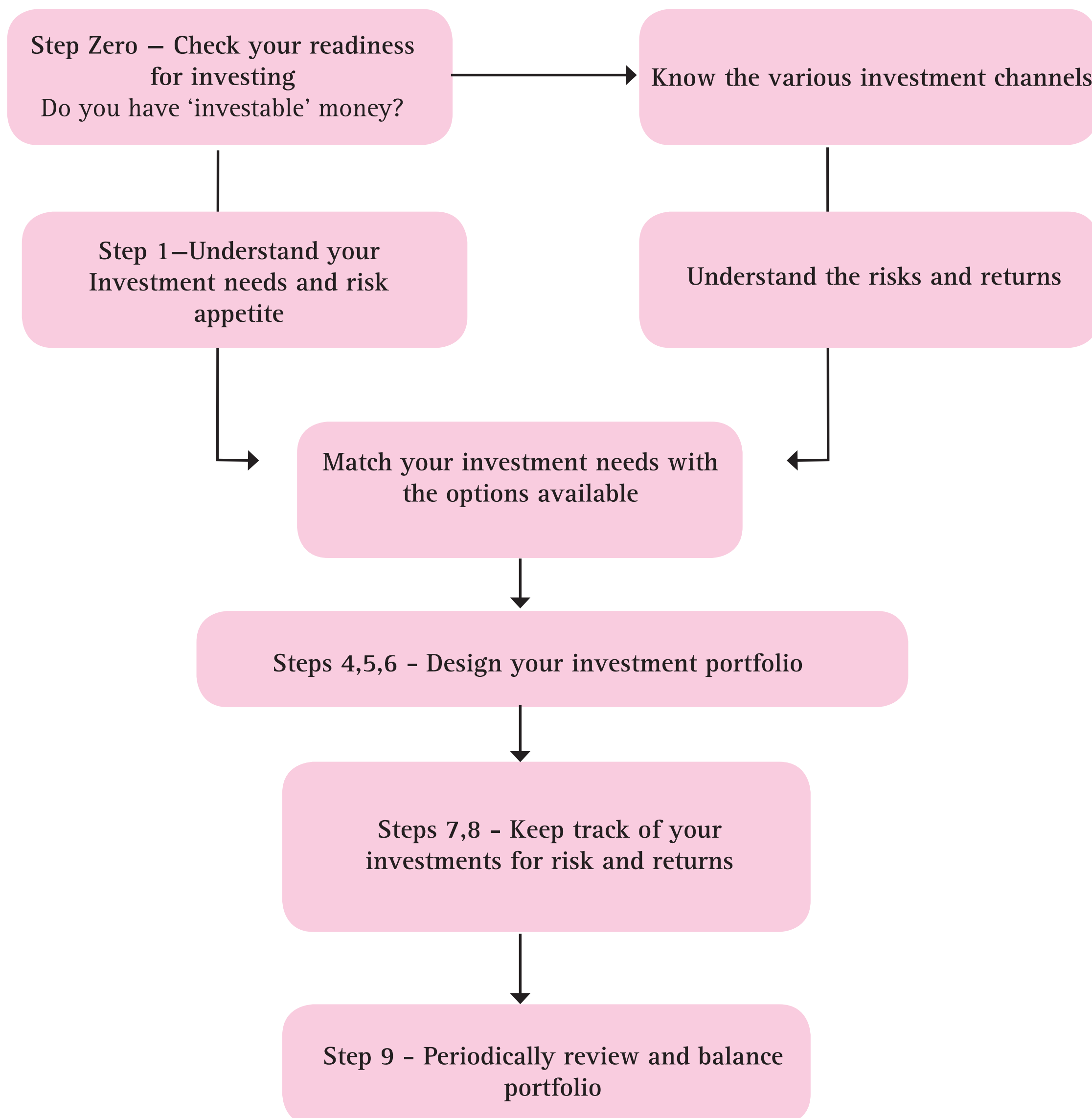
Review Date:

No.	Investment channel/ Asset Class	Target asset allocation Refer Step 6	Value of Asset class Refer Step 7	Current asset allocation
1.	Cash		Amount C Rs.	
2.	Debt		Amount D Rs.	
3.	Equity		Amount E Rs.	
4.	Others Land/gold/Commodities		Amount O Rs.	
	Total	100%	Rs.	100%

Note that the target asset allocation would change with your age.

Other factors remaining constant, if your allocation % in the yellow and blue columns does not match, then you would need to balance your investment portfolio. Refer Step 5 for guidelines.

I Know – Process of Investing Recap



Can I Start Investing NOW?

Asma says

I am a 19-year-old economics student. Ever since I read about investing, I wished I too could invest. But I do not know how to start, as I do not have any source of income. I am a full time student and get a pocket money of Rs.1000 a month from my parents for my needs. Most of this money is used for petrol in my scooty, eating out in college canteen, an occasional new dress, some books/CDs and beauty care. My fees and college books get funded by my parents separately. I seriously wish to invest, but does not know how and when I can. Should I borrow some money and start investing?

Do you think Asma can invest now? Write your thoughts in the space below. Look for Mrs. Bharati's explanation at the end of the section.

Saurav says

I am not too good with numbers. And investment seems to be a numbers game. Complex formulae, a lot of numbers, difficult terminology and my hard-earned real money put together scare me. And I do not know whether I will ever understand investing my money. I am a very cautious 25-year-old artist. I simply understand those schemes that say your money would double in so many years. I have put my money in my bank account which offers an auto fixed-deposit of amount in my savings account over Rs.5000. It guarantees that my savings would double in 8 years. I am weary to try anything new in investing. But I also feel that I could be left out of something very life changing.

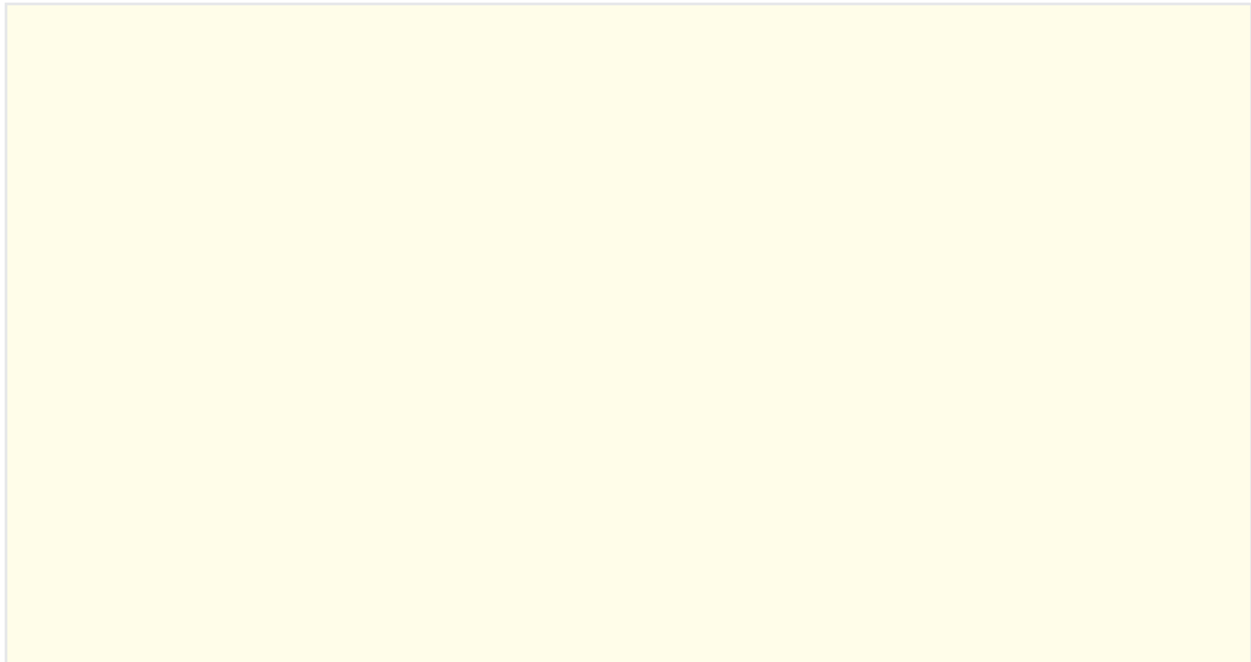
What would be your advice to Saurav? Use the space below. Look for Mrs. Bharati's advice at the end of the section.

Advise Me!!!

Digen asks;

I am 23-year-old mechanical engineer working with a leading automobile company for last 2 months. I earn Rs.20,000 every month and I think I am managing my money well. I have almost Rs.4500 investable money every month. My friend, who and I joined this company together is making huge profits on stock markets since he was a student. Just last week he invested Rs.10,000 in shares of one company and sold them on the same day. And guess what? He made a profit of Rs.5,000 on the same day. WOW! But now that stock is not doing very well. Can you please advise me another profitable stock that I can invest my Rs.9,000 in and make huge profits?

Do you know of any such stock for Digen? Can you advice him so that he can make huge profits? Read Mrs. Bharati's recommendation on the following pages.



Mrs. Bharati's Common Money Sense Answers

Dear Asma,

You are only 19, a student and thinking about investment. Good thinking lady! If you indeed start investing today, you have up to 40 years of productive life on your side to invest. I cannot imagine the amount of wealth you would build by investing for 40 years. Time is on your side. Now get the money too! How?

Firstly, you are above 18 years of age, so you can independently manage all your investments. Consider this, you get Rs.1,000 allowance for your 'wants' (not all that you spend on are your needs). Now if you can find say Rs.500 (to start with) from that money—in a month or two or three, you can get going. Of course you would need a savings bank account to start with. If you do not have one in your name, then open one right away.

Assuming you have a bank account, then your investment options with a starting sum of Rs.500 are listed below:

1. 50 units of a newly launched mutual fund from any reputed asset management company. Through a systematic investment plan (SIP) you can keep investing every month.

2. Demat account and at least 1 share of a well known 'A' list company (Yes you can buy a single share at a time. Then you can build more as you earn more)

3. Recurring deposit account (it earns more interest than a normal savings account) that allows you to invest amount as low as Rs.50 every month.

Should you borrow to invest? The answer is—NO. Never invest money that is not yours and investable. Now the question remains how to find that Rs.500. You will have to figure that out. But if you ask my personal opinion, for a cause as good and great as investment, it makes sense to cut down your expenses from eating out, buying a new dress every month or even beauty care. What say?

Get Set Invest!

Mrs. Bharati

Dear Saurav,

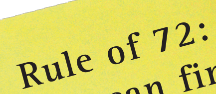
Investment is a science and an art. Since you are an artist, at least the art part of it should not be difficult for you. On a more serious note, I do not know whether to call investing as something life changing (though for some it has proved to be just that). But in general, investing is definitely an empowering process. It enables you to plan for your entire life well ahead in time. Thus, you can maintain your lifestyle (if not steadily improving) during those times of your life also when you would not be earning. It will certainly be helpful in those times also when your income alone proves incapable of supporting you.

Coming to your question, the numbers should not put you off from the process that is so not just about them. Investment, as I keep saying, is mainly about understanding your needs first and finding an external offering (an investment channel) that can help you meet those needs. Numbers and formulae form a small part of this process. Many institutions that sell investment products, these days have their communication simplified for even a less educated to make sense. Or there are those friendly and so-ready-to-help customer service executives at banks who can help you with this. If you can use internet, log onto a search engine and you will find thousands of websites that have calculator programs. These would require you to key in some very basic information but help you with answers to most financial planning problems using math formulae.

You say you understand only doubling the money proposition. Now let me teach you a trick by which you can know when your money would double, if you know the rate of returns on an investment or vice versa. It is called the Rule of 72 (see box). Is not that simple? Many such tricks are also available on the net. Check out the list of resources mentioned in the end of the book

Best wishes,

Mrs. Bharati



Rule of 72:
You can find out how long it will take to double your money through compounding just by dividing 72 by the rate of return on your investment. Or find out what rate of returns you would need on your investment so as to double it in the timeline you desire.

Dear Digen,

Congratulations! You are happy with your money management skills and also have Rs.9000 as investable money within just 2 months of your employment.

If you seriously want my advice on investing in stock market, it would be that you should not invest in stocks right now. And the reason to this has nothing to do with the state of stock markets right now. But it has got to do with you and your ignorance of stock market investing.

My explanation to this curt advice to you would be in 2 parts:

1. You seem to be so dazzled by your friend's 'huge profits' that you are not using your mind. If you put your money, while in such bewilderment, it would be injurious not just to your financial health but also to your mental peace.

   Just use your conscience and think. If making huge profits on stock market was as simple as I knowing and recommending you a stock to invest in, then will I myself (or for that matter any stock market expert) not be minting money?

   Your intent of investing in stock market is good but the premise is wrong. If you read this section and work the worksheets provided sincerely, you would notice that the only premise for investing in any channel (including stocks or shares) should be your investment need. You can be inspired to invest by someone or some thing. But when you take the investment decision—how much should I invest and what should comprise my investment portfolio—that should be based solely on your investment objective.

2. Besides, when you decide to invest your money, you should have a fair amount of knowledge of the channel you are investing in. What are the risks involved and whether the returns are guaranteed or steady? You do not seem to have gathered any such understanding of stock market investing yet.

Firstly, your friend is not 'investing' but he is 'trading' on the stock market.
While trading stocks, he is only relying on price fluctuations on the stock exchange that day, not so much on the quality of the stock or company. Whereas investing in a stock involves longer term intent to hold the shares of the company. You know your friend has recently made profits. It could be interesting for you to know how many percentage times he has lost money while trading.

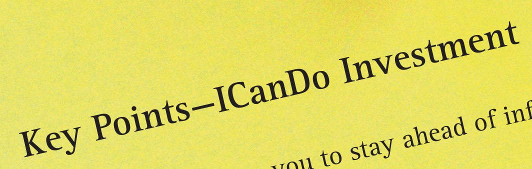
I repeat, never ever lose sight of your investment need/objective. Consider this a rule to wise investing. This is especially true also while picking specific stocks. Ask yourself a few basic questions:

- Is this business I would like to co-own (you would be a shareholder, right?)
- Is this a company/management I can trust?
- How does it treat its shareholders, employees and customers?
- Is it a sustainable profitable business venture? Can it give profits in long term?

(You wouldd need to do some study in understanding this. Refer financial newspapers, the company website and economic news.)

Having said all this Digen, I must add that you have been wise enough not to just jump into investing. Also, that you are not the only one. Many stock market investors invest on wrong premise and assumptions. Then they get their fingers burnt. Hence, most investors are not able to make the best of investing in shares. It has a huge potential to profit its investors in the long run. But it is in the investors' hands to prepare themselves to earn what the investments are ready to offer. Be wise. Read up, understand—stock market investing and your investment needs—and then take measured steps. You will see rewards and expertise coming in with right moves.

Take Care,
Mrs. Bharati

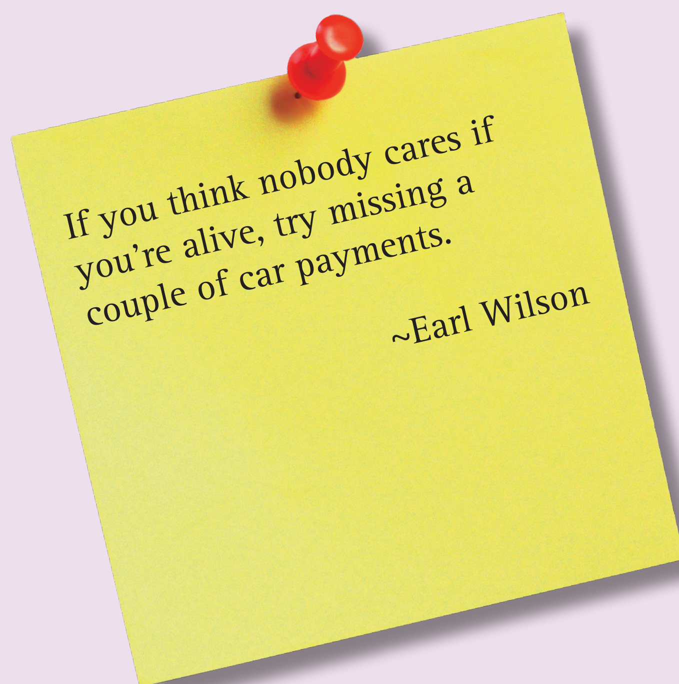


Key Points—ICanDo Investment

1. Investing allows you to stay ahead of inflation and to meet your financial goals.
2. Investment decisions should always be based on your investment needs.
3. The key to any good investment strategy is to balance the risks and returns —minimize the risks and maximize the returns, to an extent possible.
4. Once invested, it is important to maintain your investment portfolio in line with your target asset allocation.
5. A periodic review of your investment strategy and portfolio will allow you to stay in line with your changing needs and risk profile.

Part IV

Planning and Managing Debt



I Can—Mrs. Bharati's Common Money Sense

The one area in personal finance that our generation of young people managed the best was loans or debt. I cannot recall anyone in my generation having any debt related problem in youth. The credit for this, I must admit, did not go to us as much as to the regulations and policies regarding sanctioning loans. The only problem with debt we had then was that it was so inaccessible.

My brother had applied for a loan to buy a piece of land. The loan was not more than a lakh of rupees. But he had to go through a very lengthy process of application. Banks required him to provide a bunch of documents as proofs—of his identity, address, employment, income, even expenses, savings and investments. Some lending agencies also demanded a declaration of why this need (land purchase) was so important to him and how he was justified in asking for this loan. And to make it more difficult, the loan application, in order to be processed further, needed him to present a guarantor. (A guarantor was generally a well-placed individual earning more than the loan applicant who could guarantee the bank the applicant's income-generating ability and also take the responsibility of loan repayment if the applicant failed to.) I thought it was ridiculous—so much of red tape! My brother and I (young blood) also had a heated discussion on how a young person can dream big in this country? Why don't they (the lending agencies) trust us? Why do we have to justify our need? And are we not wise enough to make the decision (about our need and ability to repay the loan) ourselves? Both of us laugh at it, when we talk of it now.

Today's loan market is exactly what my brother and I wished for the wise and ambitious young people. Loans are widely accessible. The application process is simple. In fact, the lending agencies are queuing up to lend you some money. (I often get a crossed cheque in my mail box from my bank as a personal loan! And I had never asked for it!) You can take as much loan as possible, and the next lender you go to will not blink an eyelid before sanctioning you yet another loan.

So, are my brother and I happy for the youth today? Yes and No!

Yes, because there are limitless opportunities to dream and act to achieve the dream. No matter how much you earn now, if you are confident of your potential, you can borrow your future income today. And you do not have to spend days and months collecting documents for applying for a loan. Neither do you need to wait for months to hear from your bank about your loan application. That is really great!

What is depressing though, is to see that various other debt related problems (and of humungous scale) have emerged due to this one convenience of wide accessibility of loans.

The recent economic downturn has showed us all what damage debt has caused all around the world. Debts are not just pulling down individuals, they are crashing on big international companies as well, leaving thousands unemployed and without any financial support.

My brother today owns a call center. And guess what business he is into? Debt collection! On behalf of their clients (credit card companies), they call up people with credit card debt to remind them of their debt repayment schedules and 'advise' them of the consequences if they do not pay on time. The stories he has to tell about loans and debts today are of different kinds. Read these:

1. Credit card debt is emerging as the single largest cause of financial problems across the world.

2. Many credit card users do not know how much interest they are charged on their credit card debt.

3. Debt is the single largest reason for break-ups in relationships, especially in the developed countries.

4. Identity theft is the biggest new-age personal finance fraud.

My experience with people I have come across reveals some interesting differences in attitude towards debt of people in different age groups.

1. Most seniors (45 years and beyond), who have been used to the 'loans on ration and regulation' are careful about raising debt even today and particular about paying it back. This is the group that uses credit cards prudently—not letting a lot of debt mount up on the card.

2. Majority of the youth (25 –35 years of age) have home loans, vehicle loans, multiple credit cards, durables like TV, PC and even holidays and travel bought on EMIs (equated monthly installments).

3. Some younger people (below 25 years of age) have access to credit cards and many have an education loan to repay before even they start earning.

4. Young persons generally have more number of credit cards. Seniors have more credit limit on a single card.

5. Youth are quite liberal in using credit cards for online payments, seniors are skeptical.

Banks and lending agencies have loosened the strings. Credit cards have put the money we do not have now, in our pockets, although temporarily. The deregulation has put the onus of judging our loan repayment capacity and validating the need to seek loans, on us. It is almost like we have every power, everything financially working for us, but ourselves.

It is wiser to learn from those who have made mistakes, than making mistakes ourselves and paying a heavy price for learning a lesson. External controls, whether in the form of parents or bankers' strict policies, always leave no choice but to follow the rules and good practices. It is time we get our internal controls—our own financial wisdom in place while using debt. Effectively, we can get the best of both the worlds—the open world full of choices and opportunities and the regulated world that ensures good repayment practices.

I Know – About Credit, Loans and Debt

The three different words—loans, credit and debt, all point to the same thing.

A **loan** is an arrangement with a bank or other lending agency. In this arrangement, you get a lump sum of money from the lending agency on a promise to pay it back with interest within a given time. The repayment could either be in several installments, or in one payment at the end, depending on the design of the loan.

By taking a loan, you create a **debt.** Debt is that which is owed. But many times in personal finance, the words 'consumer loans' and 'debt' are used interchangeably.

Credit is a lending agency's belief or confidence in your repayment abilities and intent. Based on this, a lending agency—be it a bank or any other, will decide whether to sanction you a loan and how much.

Good Credit is an Asset

A good credit is a lifelong asset that may be used for convenience, investments and in case of emergencies. Loans can allow you to buy or invest in things you need but cannot afford to pay for it upfront like a car, house or education. Hence, instead of wiping out your savings or selling off your investments to buy an important asset, credit allows you to borrow from your future income and repay it in affordable installments, at a small fee.

A good credit can be established by maintaining good savings and investments. And also through a good loan repayment practice i.e., taking loans for productive purposes and repaying them on time and in full.

Credit, if used appropriately, can be a valuable tool. It is convenient, provides the means to start/ expand a business, to acquire valuable assets, and is available for emergencies.

There are many specific kinds of loans; the most common being taken for housing (purchase, construction or repairs), purchase of a vehicle, education, farming or entrepreneurial schemes.

You may also find loans that can get you out of a personal emergency, unforeseen medical expense, or can help you fund a big purchase or wedding/festival celebrations. If this is the case, however, make sure you have a plan to pay it back, as these expenses will not grow your money and you will need to make arrangements to repay them from your other sources of income.

I Know – About Debt Cycles

In financial planning, debt is as significant as savings and investment. Debt, if planned for and managed wisely, can prove to be a good way to access your future income today. But if unplanned and accessed on incomplete information or in haste, can lead to a cycle of instability and subsequently vulnerability.

Use debt so that it stabilizes

Borrowing money for business or asset creation (like house) or borrowing now when you are clearly seeing an assured and healthy future income, is a good money management tactic. It can be thought of as investing your future income. In fact, such a debt is also considered as good debt. In case of an emergency, when all else fails, debt can stabilize your finances.

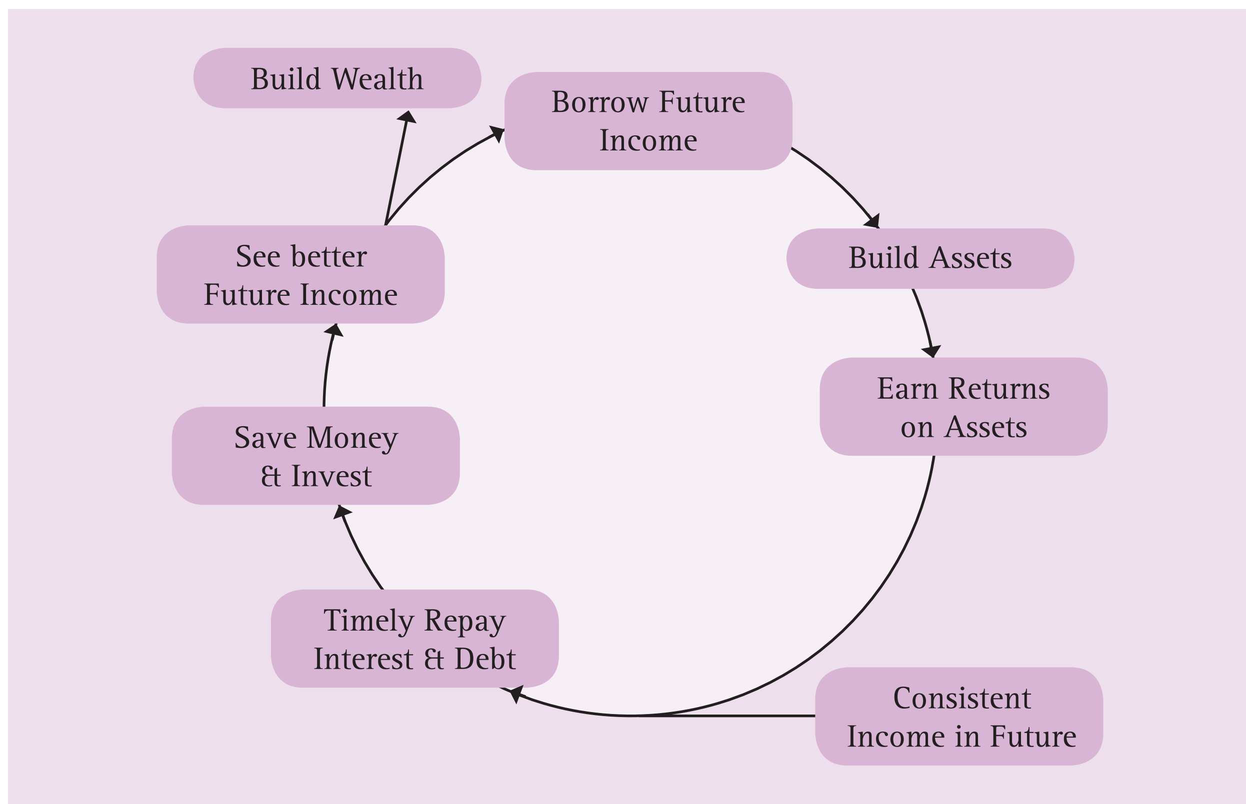


Fig 4.1 Positive debt Cycle

Do not allow debt to control your life

Many, unfortunately approach borrowing in a very haphazard manner, mostly to manage some emergency— not planned for earlier or to manage big expenses that may be unnecessary. Such a debt is obviously bad debt. If proper thought is not given to how the interest rate would impact the amount you borrow or how you would repay the debt and the interest, then in all possibilities you may be left 'managing' everyday trying to repay. This may, at times, force you to exhaust your savings, sell off some or all of your assets and worse, borrow further at a higher interest rate. Avoid unplanned/thoughtless borrowing as it may push you into a vicious cycle of debt which could take control of your life.

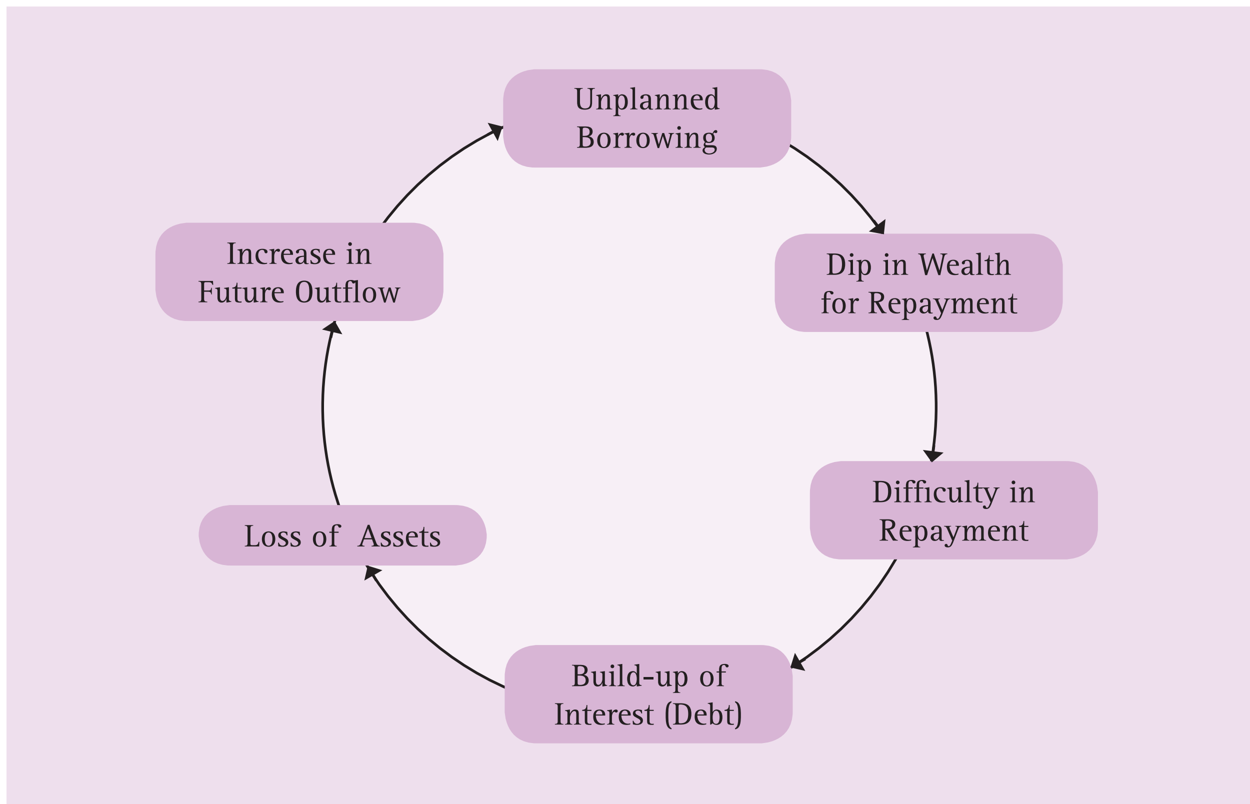


Fig 4.2 Vicious Debt Cycle

Remember: A clear plan for repayment, even in an emergency borrowing situation, is vital for profitable usage of debt.

I Do – Planning and Managing Debt: Step 1

Step 1– Do you really need a loan?

Debt is costly and should not be the first thing you resort to as a funding source. Take the following quiz to know whether you really need to get the loan. This is an important question you would need to answer in order to stay out of bad debt and a vicious debt cycle. Take the quiz every time you think of a loan to fund something.

Place a tick alongside the statement/s that is/are true about you.

1. **What do I need the loan for?**

   ☐ Housing ☐ Starting a business ☐ Investing for better returns

   ☐ Education ☐ Buying a computer ☐ Buying a vehicle

   ☐ Clearing debt ☐ For consumption ☐ Managing emergency

   ☐ Other ___________________________

2. **Can it (what I need to fund) generate income/save me money from other expense in order to payback the debt installments in full, on time and on a sustained basis, until the debt is cleared?**

   ☐ Yes ☐ No

   If the answer to the above question is yes, then with a clear debt repayment plan, Go to Question 5.

   If the answer is No, then proceed to Question 3.

3. **Do I really NEED this now?**

   ☐ Yes ☐ No

   Ask yourself if it is a need or a want. If it's a want, delay the purchase until you have enough money to fund it. Save for it. Do not take the loan.

   If it indeed is a need, proceed to Question 4.

4. **Is it possible to delay the need until I build up savings?**

   ☐ Yes ☐ No

   If there is a possibility to fund the need through saving, try to either increase your income or budget to cut down expenses or both, to maximize your savings and fund the need. Do not take the loan.

   If there is no way you can fund it through saving, move to the next question.

5. **Do I have enough balance in my emergency fund?**

☐ Yes ☐ No

If the answer is No, first build the emergency fund before moving further. Once there is enough balance in the emergency fund, move to the next question.

6. **How much is the amount I would need to borrow?**

Rs.____________

7. **Have I surveyed the lending agencies well for their reputation, interest rates, installments and the charges/penalties in case of a default?**

☐ Yes ☐ No

If you have not done the survey, do it and fill up the following table before moving to the next question.

Name of the Lending Agency	Interest Rate	Individual Installment Amount	Installment Interval Month/Quarter etc	Installment Period	Charges/Penalties

8. **What is the best (lowest) available interest rate on the loan?** ________

9. **How much would be the loan installment I would need to payback, how frequently (monthly/ quarterly etc) and for what period?**

____

10. **Effectively how much interest will I be paying to the lending agency on the loan amount?**

Rs.______________

11. **Will it be profitable to fund this need through any other source then?**

Compare the cost of liquidating some investments against the interest amount you would be paying on the loans.

☐ Yes ☐ No

If your answer is yes, Do not take the loan. Consider liquidating your investments and build it up regularly with the money you would have otherwise paid to repay the loan.

If you do not have any investments or if taking the loan looks more money wise than selling off assets, then move to the next question.

12. **Do I have an assured income source at present that is most likely to last for the loan period so as to repay the loan installments on time and in full?**

☐ Yes ☐ No

If your answer is No, Do not take the loan unless you figure out a way for the timely repayment of the loans. Otherwise, the consequences could be dangerous to your financial health in future.

If you currently see a consistent income source for the loan period, move to the next question.

13. **What options do I have to repay the loan, in case I lose my income source?**

____

____

14. **Who are the people who can repay my loan installments in case, for some reason, I am unable to pay it back?**

(Inform people on this list about your intent of taking the loan, for what purpose and the loan amount. Specifically ask them if they would bail you out in case of your inability to repay the loans)

____

____

15. **I am convinced that:**

☐ - I **need** the loan, right now.

☐ - I have done a proper survey of lending agencies and have found one with terms that suit my needs and profile the most.

☐ - I am okay with the cost of taking loans.

☐ - I have a strong repayment plan in place and will not have any problem repaying the loan on time and in full.

After taking the quiz, agree with all the four statements above, then you seem to be ready for the loan.

You may go ahead and apply for the loan.

I Know – Things to consider before taking loans

1. **Interest Rate:**

   Interest is the fee paid to the lender on borrowed money.

   For loans, the interest rate will tell you how much more than the original loan amount you will have to pay back. In general, interest rates are fixed for a length of time (the life of a loan, for example). But as the markets change, so do the interest rates. It is important to understand if the interest rates that apply to your accounts are fixed (one rate throughout the loan tenure) or floating (variable interest rate that changes according to market changes). Usually, even the fixed rate loans have a re-set clause to be applied after some years.

2. **Loan tenure/Repayment pattern and Instalment amount:**

   Knowledge of all the three will give you an idea of

   i) The number of months/years you will take to repay the loan in full.

   ii) What amount you would be required to pay at a time, and

   iii) Whether you need to pay it on a monthly/quarterly/half-yearly/yearly basis.

   This information will help you plan your finances better and also to check whether you are borrowing as per your expected future income or are going beyond it.

3. **Other charges and penalties:**

   Banks and other lending institutions generally charge a nominal one time processing fee and a service tax. Also, if you fail to pay any installment on time they may charge you a penalty for late payment. It would be wise to know these and other charges (if any) before hand, to avoid any shocks or surprises later.

4. **Foreclosure or pre-closure charges:**

   You may wish to resort to foreclosure to avail loans at lower interest rate from some other bank. Lending agencies generally penalize pre-closure of loans or ending the loan agreement before its earlier agreed term. Foreclosure charges are generally applicable on your outstanding loan amount and may be around 2-3%.

   Similarly, some lenders may have pre-payment charges that are applicable if you decide to prepay the loan's entire amount at any time during the term.

I Do – Planning and Managing Debt Step 2

Step 2 – Debt up-to-date Record

If you already have raised debts, then to keep them manageable, you would need to keep track of them. Record all your current debt details in the table given below for a ready reference of your debt status.

Debt record for the month: ________________

No. of loans	1	2	3	4
Loan type, and lending agency				
Original loan amount				
Current balance to be repaid				
Interest rate on the debt				
Installment amount				
Next installment due date				
Final pay-off date				

No.	Credit cards	Current balance due	Minimum amount due	Actual payment	Interest rate per year
1					
2					
3					

I Know – About Debt repayment

Debt is often referred to as a double edged sword, which can help as well as harm. Therefore, while using this tool, it is best to understand how you can use it smartly and effectively to your advantage. Given below is a list of practices that can help you stay out of debt trap and use debt as an enabling tool in financial planning.

Do's

1. Do a thorough check on whether you really need a loan. Refer Step 1 worksheet.
2. Spend time in surveying for best rates and repayment patterns that suit you.
3. Check your financial position and your ability to repay the debt on time.
4. Have a clear loan repayment plan before applying for the loan.
5. Take care to repay all installments on time.
6. Use 'budget' as a tool to find money to repay on time.
7. Limit the number of credit cards in your wallet (ideally to 2, just 1 is the best).
8. Pay your credit card bills on time and in full.
9. Maintain a record of repayment schedules and documents.
10. Maintain an emergency fund at all times.

Don'ts

1. Do not spend more than what you earn.
2. Do not spend money you do not have—overspending on credit.
3. Do not only pay the minimum amount on your credit card.
4. Do not use debt to pay off debt

How do I manage debt?

Rahul says

Hi, I am 29 years old, practising lawyer. I have been working with a law firm for last 7 years. I am married and we are expecting our first child in 3 months. I feel we are deep in debt. My wife (a secretary) and I had both taken housing loans from our companies 3 years back. With my wife on a maternity break from work, I am the single earner now. Most of my salary goes in repaying our 2 credit card bills, a housing loan and a vehicle loan. I am thinking of taking a personal loan to be able to manage our increasing expenses with a baby coming.

If Rahul had approached you, what would be your advice to him? Write your thoughts in the space below. Look further for Mrs. Bharati's advice.

Jassi says

I am a 25-year-old HR professional. I take home a net salary of Rs.35,000 every month. I have been using 3 credit cards since I was in business school. Now I have a total credit card debt of about Rs.75,000. I also am yet to repay a part of educational loan, which comes to Rs.6,000 per month. My home loan installment gets deducted from my salary before I get it. I had borrowed Rs. 3 lakhs from my father to fund the initial payment. I have also borrowed Rs.25000 from a friend to pay my credit card bill last month. I am finding it increasingly difficult to find money to pay my debts and manage my expenses. How can I get out of this?

Do you have advice for Jassi? Write your thoughts in the space below. Look for Mrs. Bharati's explanation at the end of the section.

Mrs. Bharati's Common Money Sense
Answers to the cases

Dear Rahul,

It is good to know that you are foreseeing change in your financial life with the change in your family. There are indeed a lot of changes occurring in your financial life and it is wise to note them. Your household expenses are only expected to increase from here and your family income has come down (may be temporarily) with your wife not earning anymore. What is possibly not changing right now is on the debt side. And believe me, if you at all want to change this side too, it better be by lowering that obligation and NOT increasing it further.

I will advice you not to take any personal loans now. You do not want to put yourself and your family at this stage in any further debt. By doing so, you would be making your family vulnerable to financial risks. Besides that, personal loans are high interest loans.

Taking a loan now, would help you in the immediate short term. But it would add to your regular monthly outflows over a long term. And mind you, your expenses are only going to increase in future—child birth, education, health care. You do not want to be restricted by your debt obligations in future.

You will have to manage your money well. You will have to find money to meet your future expenses. And you have 3 months to do just that.

My advice for these 3 months, considering your current situation would be to build up your savings.

The steps to build up your savings are given below;

1. **Do away with your credit cards—you do not need them now.**
   Credit cards often make you spend the money you do not have now. But you do have to pay the bills later. If you use cash instead of credit cards, you would always question the need of the expense before actually spending your money.
2. **Make a budget and stick to it. (Refer to Section 1 for details.)**
   Reduce your expenses as much as you can and start saving.
3. **Manage your debt well.**
   See if you can get a lower interest rate or a smaller installment amount on your loans. Talk to your bank about this. Check other options available in the market. By doing so you would be reducing your monthly installment and spreading it over more number of years. You can thus find some more money to build your savings every month.
4. **Keep saving with increased income.**
   Continue to build your savings with every increase in income—your increment, wife contributing to income, your investments yielding returns—or reducing expenses.

This way you would be able to give a debt free and stable financial future to your child.

Best wishes,
Mrs. Bharati

Dear Jassi,

I am glad that you know how much debt you currently owe. It's indeed good that you have been able to put specific figures to all your debt obligations. Though the debt itself does not speak well of your current financial state.

But understanding your financial position in itself is a big step in financial planning.

Now let me get down to answering your question one thing at a time.
Firstly, you do not need 3 credit cards. In fact you do not need any credit card right now. So stop using them first.

Next, repay the Rs.75,000 due on the credit cards. That is the first debt you should pay off as it is a very costly one. Check with the bank that gave you the educational loan if you can defer the payment installments for 5-6 months. Now, going by your salary and by minimizing your expenses, you should be able to pay off the credit card debt in 5-6 month's time.

Meanwhile, talk to your friend who lent you money to repay your credit card bills and your dad about your intent to pay their debt, although you are at present getting out of your other debts first. I am of course assuming that these loans to you were more of goodwill, and were interest free.

Once you are out of the credit card mess, start repaying your student loan.
Maintain your expenses to the minimum and pay your friend who saved you in need, may be with a small gift.

And keep following this until you have given your dad his money back. Only after this last commitment can you call the money you have your own.
And of course, do not resort to any further debt during this whole process.

Even in future, if you wish to take a loan, follow the planning and managing debt questionnaire to be in the positive debt cycle.

Best wishes,
Mrs. Bharati

Key Points—ICanDo Planning and Managing Debt

1. Debt, loans and credit—point to the same thing. Your credit with a lending agency allows you to take loans from them and by doing so you raise debt.

2. Use debt to stabilize your finances.

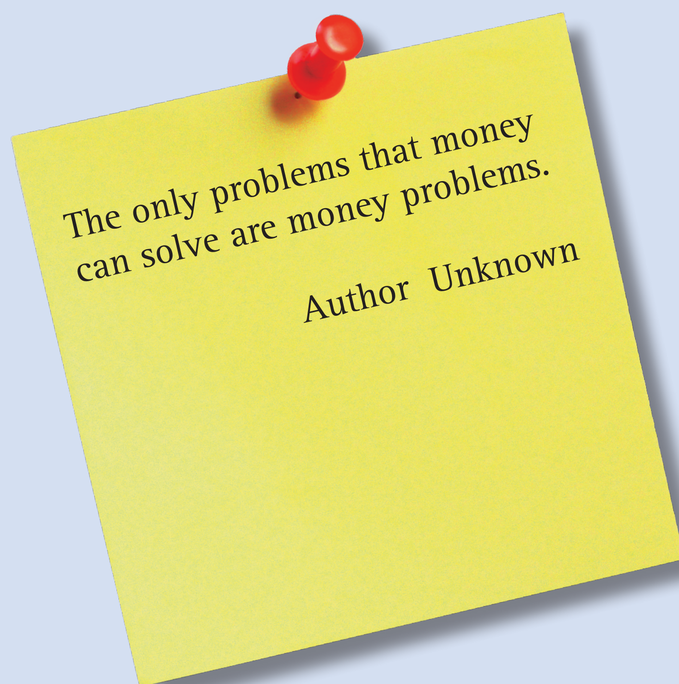
3. Never go unplanned or unprepared for loans.

4. Track debt and repayment schedules and stick to them, even for credit card debts.

5. Debt, if not managed well, leads to vulnerability to financial risks.

Part V

Financial Risk Management



I Can—Mrs. Bharati's Common Money Sense

Have you ever been caught in rains, without an umbrella? That too while on way to a job interview?

It did not seem like it would rain that day. I had my final interview with the Production Head of a TV Channel at 11 a.m. I was all set to reach at least half an hour early, but suddenly it started raining cats and dogs and there was utter chaos on the road. By the time our bus had reached my stop, it was already 10:45 and it was still raining, though not that heavily.

I did not have an umbrella, the office was a good 10 minutes walk (something that had seemed to be a 'just' 10 minutes walk earlier), it was still drizzling, there was no taxi or rickshaw visible and I had just 15 minutes to get into the interview room from where I was.

There was nothing that I could do but pray. And had this been some film situation, I am sure my prayers would have been answered. The rains would have stopped and a bright sun would have been out in a moment as if it was always there. Or a good-looking hero, with an umbrella and a kind heart would have bailed me out. If nothing else a superman could have surely come to my rescue.

But it was not to be. And that was the reality of 'life', at least my life then. All the odds that moment seemed against me and I was left in a totally confused state of mind. What do I do next? Will I make it on time and in a presentable situation? How do I not get wet in this rain and still reach the office on time? Why did I not carry an umbrella? Why did I not have a back-up plan? How could I let such an important interview go by, without giving my best shot?

There were just two options in front of me:

a. wait, either for a rickshaw/taxi or for the rain to stop and reach late with an apology, or
b. start walking, overlook the rains, reach on time, though wet.

Both seemed equally scary. Why did I not carry a simple umbrella? Or at least why did I not take a taxi right from my home till the office? These were the two questions that kept haunting me. I knew I had goofed up big time. It was me and not the rains to blame. Rains or no rains, I could have avoided this happening to me. There were so many other interviewees who reached well ahead of time and in their most well-groomed way. Why not me?

The answer is simple, as I look at it now—25 years and a million experiences later; I was not prepared for surprises. I had believed that everything will be just how I expected it to be — normal.

I had overlooked the probable risks on the way to such an important event and hence, had no plan to manage them.

I failed the interview, even before I appeared for it. Call it my negligence or my overconfidence, but a seemingly insignificant risk cost me a big opportunity. I learnt a valuable lesson though; 'it is better to be safe than sorry.' Carrying an umbrella did seem an 'uncool' idea, but it would have been better than reaching wet for an interview. Taking a taxi would have cost me more money, but that cost would have been far lower than the cost I finally paid—a lost chance.

Though I was 'taught' this lesson many-a-time earlier, I really 'learnt' it the first time from my own experience, as all wise young people do from their failures and mistakes. And I see its relevance and effectiveness

everywhere in life, even in financial planning. Seemingly small financial risks can cause a huge damage.

I was practising financial risk management from the beginning of my financial planning exercise. After all I had learnt the 'be safe' lesson in life the hard way. I would always keep an envelope with some cash in my locker, you know 'just in case'. I had a savings account in my son's name which had some money that was not to be touched, until an emergency struck. Though, I learned about the formal practice of maintaining an emergency fund many years later.

Of course, insurance just happened. Vehicles came with a compulsory insurance in tow. And my husband's aunt was a life insurance agent. So thanks to social obligation, both my husband and I had to draw an insurance policy from her, for an amount she suggested. It was only much later did I know that a life insurance cover for me is okay but not necessary, since I am not the main earner for the family. Or that there is a guideline to know how much insurance cover you need.

But if I were to point one financial risk management strategy that is a star in my kitty of strategies, then it has to be 'the umbrella and the taxi' strategy.

I mean, it may not be cool to have just one credit card and still at times pay by cash. But it still is much cooler than running from friends to family to manage to pay the mounting credit card bills.

It might not be cool to spend time on managing your money—the income and expenses and to live within means, especially in this world of plastic money. But it is coolest to know that your financial practices today are going to get your family a better life with every passing year and not make it vulnerable to financial risks. An insurance premium might cost some money, but it is certainly worth it, considering that it gets us peace of mind thinking that in case something happens, there is a partner who can share the financial burden.

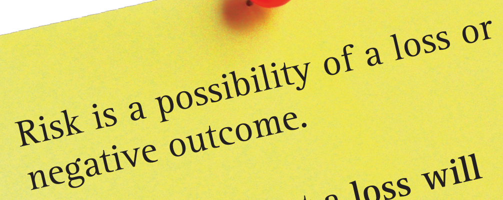
The umbrella and taxi strategy also keeps me grounded and reminds me of the biggest risks to your financial plans—negligence and overconfidence.

I Know – About Risks

Risks are everywhere and in every situation. Just consider this. During rainy season, there is always a risk of getting wet on your way to office. So you carry an umbrella to avoid that risk. But in this case too there is a risk of losing your umbrella or forgetting it somewhere or even theft.

The degree of risk will differ from individual to individual and from situation to situation. Take again the example of rains and umbrella. The risk of getting wet might not be that big if you are going to a friend's place or heading home. Also if you have that 'devil may care' attitude, you may take getting wet in your stride and still present yourself smartly for a formal meeting or an interview.

Like in all aspects of life, there are many risks in our financial lives as well.



Risk is a possibility of a loss or negative outcome.

I. the chance that a **loss will realize**, and
II. the degree or **magnitude of loss**
together decide if a risk is high or low.

Vulnerability to risks
Risks do not necessarily affect everyone the same way. While some households manage big expenses like child's marriage fairly effortlessly, there are examples of some other households that are thrown in lifetime of debt and poverty cycles because of this one expense.

Vulnerability defines how weak or susceptible you are to risks. It is your ability (or inability) to cope with risks, to prepare for and protect against or recover from losses.

Poor households with uncertain, irregular income are more vulnerable to risks. But vulnerability is also determined by your money management practices and actions. Some practices increase vulnerability, while some help reduce vulnerability.

Whether with uncertain/irregular income or not, it makes sense to be aware of these practices, so that you can reduce your vulnerability to risks as much as possible through wise financial practices. This would be your first step in risk management.

I Do – Check and reduce your vulnerability to financial risks

(Given below is a checklist of financial practices that reduce vulnerability to risks. Place a tick ☑ alongside the statement you find applicable to you to check your vulnerability.)

A. Wise Money Management

1. My savings account always has a balance of at least my 3 month's living expenses, to help me manage emergencies. ☐
2. I spend my money judiciously. ☐
3. I am particular about small things like paying bills, insurance premiums, depositing savings on time. ☐

B. Consumer Awareness

1. I always check my bank account statements, credit card statements, investment statements and other bills for correctness. ☐
2. I always ask for a proper bill and warranty/guarantee card of any big ticket item I am buying. ☐
3. I always keep my bank cheque book, ATM/debit card/credit card/PIN, online trading login IDs and passwords safe and secret. ☐
4. While at ATM, I always check if I have collected my card from the machine before leaving it. ☐
5. I never sign a blank cheque. ☐
6. I cross a cheque before putting it in a drop box or sending it by post. ☐
7. I am careful about my financial transactions on the internet. ☐
8. While phone banking, I key in my PIN/the 3-digit CVV number on Credit card and do not speak them out. ☐
9. I never sign a document without reading and understanding it. ☐

C. Financial Planning

1. I plan (save/invest/carefully borrow) for my bigger financial goals. ☐
2. I have started investing my money to meet my financial goals. ☐
3. My investments are in line with my goals and risk appetite. ☐
4. I do not invest in the 'get-rich-quick' schemes. ☐
5. I invest my money only after a careful understanding of the investment channel. ☐
6. I avoid unplanned borrowing of money. ☐
7. I avoid taking a personal loan, as far as possible, by saving for goals. ☐
8. I always pay all my credit card debts in full and on time. ☐
9. I have no more than two loans to be repaid at a time. ☐
10. I have no debt or I have a robust plan to repay my current debt. ☐
11. I have informed at least one person in my family about my financial plans, investments and debts (if any). ☐
12. I keep myself updated with the developments and financial opportunities open to me. ☐

If any of the above statements is not true of your current practices, you may want to revisit the respective section to see how you can correct it. If you have been able to check in all the boxes, then you are doing well with your current financial practices to reduce your vulnerability to risks. This section of ICanDo Financial Planning will guide you on the final part risk management.

I Know – About Financial Risks

We face various kinds of financial risks, which may or may not realize during our life cycle. But this does not mean we can overlook them. The first step to managing a risk is being aware of it. Some common financial risks are mentioned below.

1. Risk to Income:

A dependable source of income can be considered to be the first step towards a secured financial living. A risk of income loss, if realized, can throw all your financial planning off gear.

2. Risk to Expenses:

Expenses, if managed properly, leave scope for saving and wealth building through investments. But expenses going beyond the means, lead to a highly unstable financial state that could lead to risks to assets and debt.

3. Risks to Assets:

Cash assets like savings help deal with expenses and emergencies. Investment assets help money grow and store the value of money by beating inflation. Vehicles, equipments, computers etc., are assets that, besides having monetary value, are worth more for their function. Life cycle needs if not planned for and managed properly tend to eat into these assets. Hence, the risk to expenses, if not managed, will soon aggravate the risk to assets. With assets depleting, it would reduce the cushion that guards your finances, making you vulnerable to further financial risks.

4. Risks to Debt:

Income generating or asset-creating loans (business, buying home/vehicle) get repaid from the income generated through the asset or savings made possible due to the asset. But credit card debt and personal loans need to be repaid through some other sources of income.

Life cycle needs and emergencies if not planned for may force you into rushing unprepared and unplanned for debts on any terms. With such debts come pressures to pay them back, along with the high interest amounts. Choice of the source of loans can also pose a risk to debt. If the lender is not a legal, authorized entity then you are most likely to be at a risk of costlier loans—higher rate of interest, fixed interest or more frequent interest and even frauds/cheating.

I Do – Understand the financial risks you face

(Given below is a table of common financial risks. Tick alongside the risk you feel you may face during your life cycle. Tick in the appropriate columns (Low/High) based on your judgment of the possibility that the risk may realize and that of the magnitude of loss, should the risk occur. Refer to next pages to find out how you can manage these risks.)

No.	Type of Risk	Do I face this risk?	Possibility of occurrence		Magnitude of loss	
			Low	High	Low	High
I. Risk to Income:						
1.	Temporary/uncertain employment					
2.	Loss of a stable job					
3.	Severe loss in business/agriculture					
4.	Disability of the main/only earning member of the family					
5.	Loss of the main/only earning member of the family					
6.	External factors - natural disasters, economic recession affecting income source					
II. Risk to Expenses						
7.	Life cycle events—marriage, childbirth, family responsibilities, retirement					
8.	Personal emergencies—sudden illnesses, accidents, death in the family					
9.	External factors like inflation, natural disasters, riots					
III. Risks to Assets						
10.	Damage due to accidents, theft or fraud					
11.	Liquidating assets due to huge expenses					
IV. Risks to Debt						
12.	Seeking loans to manage big spendings/emergencies					
13.	Default, inability to repay debts on time					

I Know – About Managing Risks

Although there is not much we can do about an event occurring, we can manage the risk of financial loss. In other words, steps can be taken to maintain/restore financial security even when a loss itself cannot be prevented.

Possibility or chance of a risk realizing and the magnitude of loss it can cause, determine if a risk is high or low. Hence, the risk management approaches can be best determined by these two aspects of a risk as shown below in Fig. 5.1

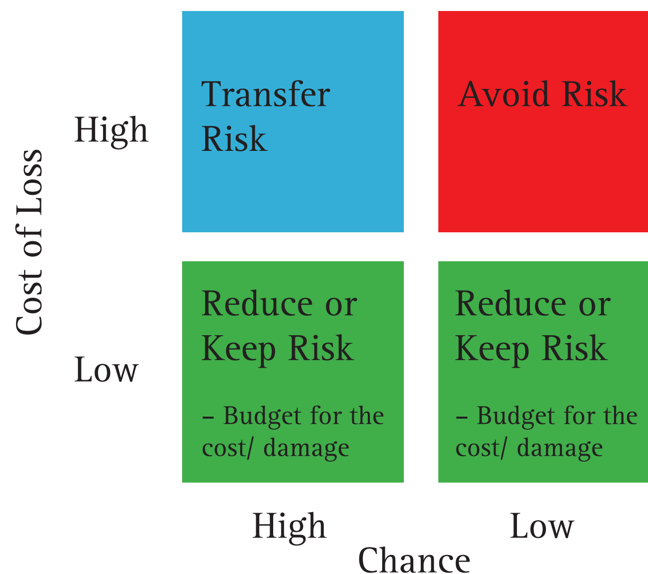


Fig.5.1 Risk management approach

I Know – How to manage risks?

Risk to Income

Temporary, uncertain employments, single earning member in the family, loss of a stable job, severe loss in business, lesser yield from agriculture are some reasons that may pose a risk to your family's income, although temporarily.

Disability or loss of main or only earning member of the family is not just a sudden but could be a major risk to the family's finances. As it may take a long time to recover from such a big loss and may need radical alternatives to restore normalcy.

Avoid Risk

Having multiple sources of income

– a second job, side business, double income/ more earning members

Reduce Risk

By proactively managing your money well and through proper financial planning.

Maintaining an emergency fund* for a 'rainy day'

**read more about emergency fund in further parts of this section*

Transfer Risk

Buying life insurance cover for the earning member

Insuring income sources - shop, vehicle, factory, equipments, crop, warehouse, cattle

Risk to Expenses

Life cycle needs—marriage, childbirth, retirement pose a risk to your household expenses. These, if not planned for, would often take a toll on your finances.

Then there are emergencies, some personal—sudden illnesses, accidents and death in the family—and some external emergencies like natural disasters along with human suffering, can cause major financial disaster in a household.

Avoid Risk

Living within the means – avoiding unnecessary expenses, gifts and celebrations that can be beyond your means

Reduce Risk

By proactive financial planning - Setting specific lifecycle goals and saving/investing to meet them

Transfer Risk

Buying health insurance (usually for everyone in family), accident insurance (for those who use vehicle often) and vehicle and house insurance.

Risk to Assets

Life cycle needs if not planned for and managed properly tend to eat into assets. Hence, the risk to expenses, if not managed, may aggravate the risk to assets.

Wiping out savings or selling of property or liquidating investments, or withdrawing from school—loss of education—are some risks to your household assets that you should avoid as far as possible.

Other likely risk to assets could be from damage to assets due to accidents, fire, other disasters, theft/robbery and frauds.

Avoid Risk

Deal only with legal banks and other financial organizations

Do not sign any document/ blank paper without reading and understanding contents/ terms

Keep assets and records safe (bills, agreements, receipts, passbook/ statements)

Reduce Risk

Understand your rights/ responsibilities as a consumer of financial products/ services.

Practice financial planning to avoid eating into assets in times of needs

Diversify portfolio – do not invest all your money in one type of asset

Transfer Risk

Put your savings in a bank/ Post office savings account

Insure assets – home, vehicle

About Regulators

The financial system of our country is maintained in harmony with the basic intent of ensuring fair practices and safety of the common man – investor, consumer, insurer, borrower or a depositor. **The Reserve Bank of India** (www.rbi.org.in) or **RBI** is the monetary authority of India which regulates and supervises the financial system so as to maintain public confidence in the system.

SEBI or The Securities and Exchange Board of India (www.sebi.gov.in/ investor.sebi.gov.in/) regulates the securities market - stock exchanges, mutual funds, brokers to ensure investor safety.

Like these two main financial regulators, there are also others like those who regulate the insurance market and the pension fund market.

Dealing with legal institutions would lower your risk of cheating or a financial fraud as they are expected to follow the rules and policies laid down by the regulators.

Risk to Debt

Life cycle needs and emergencies if not planned for and managed properly may force you into another, more disastrous act of rushing unplanned for loans on any terms. With such debts come pressures to pay them back, along with the high interest amounts. This generally should ring an alarm bell—a warning signal that your finances are not in control and your financial well being is in danger.

Other likely risk to debt—almost a consequence of unplanned borrowing and/or wrong money management practices—is default or inability to repay debts on time. This leads to a vicious cycle of higher interest rate or loss of collateral, increased debt, loss of assets, no further savings or assets and thus further vulnerability to financial risks.

Choice of source of loans can also pose a risk to debt. If the lender is not a legal, authorized entity, then you are most likely at a risk of costlier loans—higher rate of interest, fixed interest or more frequent interest and frauds/cheating.

Avoiding such a costly risk or reducing it are the only two ways to manage risk to debts.

Avoid Risk

Avoid taking personal loans - for consumption purposes. Instead plan and insure/ save for them

Pay loan installments and credit card bills in full and on time

Deal with only legal lending institutions. Do not sign any document/ blank paper without reading and understanding contents/ terms.

Understand the lending terms before hand and check if they suit your plans.

Reduce Risk

Chalk out a proper repayment plan and include it in your overall financial plan.

Keep loan records safe (initial documents, receipts for collateral, agreements, installment receipts etc.)

Understand your rights/ responsibilities as a consumer of loans take care to follow them regularly

I Know – About Emergency Fund

An emergency fund or a rainy day fund, as the name suggests, is that cash reserve– your savings kept aside for any unprecedented event happening or an emergency. It is a good way to reduce your risk to income; loss in income or a sudden dip.

How much to save for a 'rainy day'?
It is generally recommended to maintain an emergency fund that can cover your living expenses for at least three months. But if your job is less secure or you run a business or are self-employed, then you probably should save to cover your expenses for six months or more.

Where to save?
Money in the emergency fund should be kept in a savings account—separate from your other savings accounts—that is easily accessible. You should ideally fund your emergency account before any of your other savings accounts.

If you do not have the money right now to fund an entire emergency fund, start small but immediately. Save a little bit from each paycheck, until you have built up the required savings. In the meantime, also try to cut back on some other unnecessary spending to help save faster.

I Know – About Insurance

Many a times, the 'downs' of life are small and manageable. A healthy emergency fund can often take care of such shocks. But in case of disasters that strike once in a while—fire, death, accidents, huge commercial losses—financial losses can be much beyond means. These can wipe out wealth and financial plans in a moment and lead to further suffering.

Often when a disaster strikes or any unexpected, unpleasant event occurs, there would always be a few friends you can rely on, who would stand by you in your trying times and help you stand up again. They could be your family, close friends, relatives, neighbors, members of community. One such friend who can help you avoid hardships during an emergency and share your financial burden is **Insurance**.

What is insurance?
Insurance is a channel to transfer risk when the chances of a risk realizing are low, but if the event occurs then the heavy cost of loss can set you back substantially.

Insurance allows you to transfer the risk of a potential loss, from you to the insurance company, in exchange for a fee or premium.

The premium or the fee is a relatively fixed and affordable amount that you pay periodically (generally once a year) to be covered against a highly uncertain and potentially catastrophic loss. By setting this amount aside (in an insurance policy) you are actually reducing the uncertainty of a probable financial disaster. Knowing that should a loss occur, it would be fully or partially covered by insurance, you are actually buying yourself and your family, peace of mind.

No matter how well you manage your finances and build wealth, failure to purchase appropriate and adequate insurance can destabilize everything in a moment. On the other hand, buying insurance you do not need or paying too much for insurance would eat out your allocation for other purposes.

It is thus extremely important to buy insurance products that are appropriate for your needs and that can cover financial losses due to uncertain events adequately.

Some very common types of insurance that can be applicable to many are—- life insurance for the main earner of the family, health insurance, accident covers for those who regularly use vehicles, motor insurance for costly vehicles you possess (2/4 wheelers, tractors, LCV), home insurance, pension/retirement policies (especially for the self-employed).

To take advantage of insurance options, you need to buy an insurance 'policy'.

A policy is nothing but an agreement that lays out the basic rules of your contract with the insurance company. According to the rules of the policy, you pay 'premiums' at regular intervals to keep your policy up-to-date. The amount and frequency of your premium will be determined by the kind of insurance you purchase and the insurance company you take the policy from.

If you keep your insurance payments up-to-date, should something you have insured yourself against happen, the insurance company will help you pay for the financial damage that occurs. The exact amount they pay and under what circumstances are all subject to the initial terms of your policy, so make sure that you understand these things well and always keep your policy up-to-date!

As in case of savings, the motto 'Earlier is better' works with insurance as well. The earlier you buy insurance in your life cycle or that of the assets you wish to insure, the better it will be as the premium payments can be lower. And, if you are insuring yourself against potential future disaster, you need to have the product purchased and paid for before time of need!

Remember—you would not get any money if you let your policy lapse by not paying the premium! So, make sure that you can commit to the regular payment schedule of your policy, or it would not be worth anything!

Insurance Types

Personal	**Commercial**
Life	Agricultural
Health	Industry
Accident	Shop
Property	**Others**
Home	Weather
Auto	Travel
Appliances	Retirement

I Do – Taking Life Insurance—Decision Process

(Given below is a guideline worksheet to take the decision regarding insuring your life. Please note that this is just a simple guideline to initiate you and any decision should be made on proper research and/or professional advice.)

A. Do I need a life insurance cover now?

1. I am the only earning member of my family — Yes/No

2. I have at least one person financially dependent on me — Yes/No

If the answer to any of the above is yes, then you do need a life insurance, work the following sheet. If the answer to both is no, then you do not need a cover just yet.

B. How much cover do I need?

Five times my gross annual income — (amt.1) Rs.____________

Life cycle needs of my dependents — (amt.2) Rs.____________
(e.g., children's education, parents' retirement etc.—write your best estimate)

My emergency fund amount — (amt.3) Rs.____________
(3 to 6 months of living expenses)

My total outstanding debts — (amt.4) Rs.____________

Total estimate of my family's financial needs — (amt.5) Rs. ____________

(amt.1+amt.2+amt.3+amt.4)

Total of my cash assets — (amt.6) Rs. ____________
(e.g., savings accounts)

Estimate of life insurance cover I need — Rs. ____________
(=amt.5—amt. 6)

Help Me!!!

Zach calls for help

Hi! 1 am a 24-year-old estate agent. I am getting married next month, and I think I should get a life insurance cover, also because it will save me some tax. So I went scouting for options, and I am thoroughly confused. First there are so many insurance companies; then there are various plans. I do not know how to get a plan that is correct for me?

Can you suggest Zach some steps he needs to take to make a decision in choosing a life insurance plan. Use the space below. Look for Mrs. Bharati's explanation ahead.

Mrs. Bharati's Common Money Sense Answers

Dear Zach,

Congratulations on your marriage next month. And more compliments for your responsible outlook towards this new phase of your life. Considering life insurance cover for yourself at this stage is indeed a very thoughtful and smart move. For one, the sooner you get a cover, the lower are the premiums and more your family is secured. Secondly, this is indeed a win-win way to ensure your family's financial security and at the same save taxes on your current income. One suggestion, do not determine the policy value based on tax saving. Instead take professional advice and use the guideline given in this section to determine exactly how much cover you would need.

Now coming to your question about specific life insurance plans, you are indeed spoilt for choices these days. Earlier it used to be just one company and just a couple of types of plans for all. So naturally with so many options, there is bound to be confusion about what to choose.

The good news is that these plans, by any insurance company, are designed to meet specific financial need. Following steps might help you in short-listing some options:

A. Look at your financial needs in general and insurance needs in particular.
B. Survey insurance plans from all the companies for their objectives, fees, insurance term, premiums, and other benefits.
C. Match the plans with your needs and short-list the ones you find relevant

Many a times the names of such plans are self explanatory like: Children's Endowment at 18 or Jeevan Saathi. What is more, insurance companies also take special efforts in educating customers about insurance and specific plans.

So go ahead and make the most of these opportunities that are open to you. But do not forget to analyze your own financial needs before that.

Best wishes,
Mrs. Bharati

Key Points—ICanDo Risk Management

1. It is important to be aware of the financial risks you may face.

2. It is best to avoid as many risks as possible through wise money management and proactive financial planning.

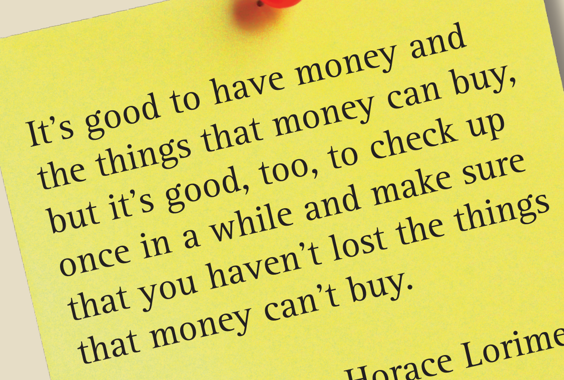
3. An emergency fund is an effective way to manage risks to income.

4. With insurance you can smartly transfer those risks that can cause huge loss if realized.

5. Risks, if not managed well, make your finances vulnerable to further risks and losses.

Last Few Pages

Sample Planning Steps for Common Financial Goals



Financial goals would differ from individual to individual, based on age, income, life cycle stage, values and personality. But a few broad goals may be applicable to a vast majority. Here are a few examples that can give you a brief idea of some steps in financial planning for these goals.

Cash Management

Your first paycheck– what you can do with it?

The Goal—To have a healthy balance through smart spending, saving, budgeting and record-keeping so as to build wealth in the long-term.

What is it?

Whether you earn in hundreds, thousands or millions, how well you manage them will decide how much money you would end up having for your goals. The sooner you start a conscious and prudent cash management program—possibly with your first paycheck (or second or even tenth) —and practice it consistently month after month, the more you will benefit from it by developing a good money habit.

Key steps on the financial plan for cash management
Understanding pay slips—earnings (your salary and perks), deductions (taxes, loan repayment) and contributions (provident fund, ESOP—stock option program).

Smart Spending—prioritizing needs over wants, avoiding wastes, using credit card wisely, funding expenses from savings and not loans, understanding terms of EMI (equated monthly installments) before buying on EMI

Record-keeping—keeping an account of daily money transactions, keeping bank passbooks and investment records updated, keeping organized other important financial records—credit card statements, bank/investment statements, warranty cards, income tax documents, insurance receipts etc.

Budgeting—for having a healthy balance—balancing income and expenses, cutting down on unnecessary expenses, allocating your income (e.g. Spending 50% of the net income, saving (20%), stabilizing finances through emergency fund and insurance (20%), investing for growth (10%)), implementation and review

Saving—planning to save, paying to the savings account first, saving for buying assets, saving for investing

Relevant financial channels—credit card, EMIs, savings account

Tax Planning

The Goal—To plan and manage finances proactively so as to optimize tax benefits and investments.

What is it?

Often mistaken as a last minute, year-end activity, tax planning proactively has much to offer beyond just saving taxes. Rather than making haphazard decisions and putting money in instruments classified for tax deductions, a proper tax planning from the beginning of the year is a good money habit that needs to be inculcated before you acquire the very popular bad tax habits. If you carefully look at the various instruments mentioned under the 80C/D (do not bother about the section numbers), you will understand that this incentive (tax deduction) is to promote long-term savings and retirement planning. Thus, from your side if you spend some time in understanding and planning your taxes, it offers a double benefit—minimizing current taxes and securing financial future.

Key steps on the financial plan for tax planning

Understanding your tax liability—This is calculated based on your taxable income and Finance Ministry's tax provisions for the year, as mentioned in the central budget.

Knowing the various tax saving instruments—National Saving Certificates, EPF (employee provident fund) —deducted and paid by the employer, PPF—with post offices/banks, life insurance, ULIP or unit-linked insurance, equity-linked saving schemes (a type of mutual fund), home loans, infrastructure bonds.

Understanding the terms of each of the instruments— minimum amount that needs to be invested, fees, lock-in period, estimated risks and returns, convenience of investment and withdrawals.

Investing in the instrument/s that suit your profile—rather than 'putting' your money where every tax payer puts it just to save the taxes, 'investing' it as per your risk appetite and investment goals offers all the advantages of tax planning

Filing taxes on time—else any delay calls for a penalty and a continuous pressure.

Record keeping—a stamped copy of the submitted tax application form, a copy of the tax calculations—profit and loss account, balance sheet, other important documents as applicable—bank statements, insurance receipts, PF slips, mutual fund statement, TDS (tax deducted at source) certificate.

This might seem to be a tedious step at first, but this education will last for life. It is worth investing time on understanding this well rather than leaving everything to your CA or tax consultant.

Relevant financial channels—NSC, EPF, PPF, life insurance, ULIP or unit-linked insurance, equity-linked saving schemes (a type of mutual fund), home loans, infrastructure bonds.

A House of Your Own

How to plan for it?

The Goal –To buy/build your own house within a set timeline

What is it?

Besides the excitement and the endless search for an ideal home, buying your own house is also a major financial activity. Whether you wait a while to fund your house from your long term savings and investments, or you decide to go for a home loan in the very first year of employment, your first house is a moment of pride. All you need to do is to plan for it.

Key steps on the financial plan for buying a house

Check if you are ready—a steady (or growing) source of income, future which is looking better and richer, you have a good credit history—you have repaid timely any other loans including credit card debt, you have a good saving for down payment (generally 8% of the cost of house).

Estimate your future income and decide on a limit also considering other costs—tax, fees, brokerages, interest on the home loan—generally your employee or the lending institution would do this for you. But as a rule of thumb you can buy a house (including other costs) that costs up to about two-and-one-half times your annual salary.

Surveying home loans available in the market—Things to consider—lender's reputation, interest rate: what percentage and whether it is fixed (one rate throughout the loan tenure) or floating (variable interest rate that changes according to market changes). The interest rate and other charges will tell you how much more than the original loan amount you will have to pay back. Repayment pattern—monthly, quarterly etc., loan tenure and installment amount will help you plan your finances better.

Deciding the payment option that suits you the best—through your/family's savings, sale of other property/ investments or with a housing loan. How much home loan to take, what type of interest, for what period of time and at what monthly installment?

Purchase – transfer of ownership and related rights in your favour, checking the house for fulfillment of all the commitments by the seller.

Insurance – considering house insurance.

Safe keeping of records—home loan documents, land registration with the corporation, house ownership documents, if it's a housing society then membership documents, house insurance papers.

Relevant financial channels—savings account, home loans, insurance

Your First Asset

The Goal – To buy consumer asset (e.g. vehicle, laptop, other electronic items, jewelry).

What is it?

The big ticket items you would need to enhance the quality of life or as an investment or the ones that you fancy which may not be bought as a regular expense from your month's paycheck. The purchase of such items needs to be planned for in advance for a better financial health. You may in the future go about buying assets like you buy your grocery, yet your first asset—bought out of your own income—is special and would need some smart planning.

Key steps on the financial plan for buying an asset

Setting the goal—what to buy, how much, which brand, when and what is the cost.

Seeking the best deal—survey, look for discounts (store specific, festive etc.).

Ensuring authenticity of the asset—originality of the brand and store (warranty/guarantee, after sales service, easy and efficient process of complaint redressal, holograms and standards).

Evaluating payment options—entire cash payment, credit card (you better have a repayment plan in place, fully understanding the extra cost due to interest if any), saving over few months (recommended approach), EMIs

Deciding the payment option that suits you the best

Purchase – transfer of ownership and related rights in your favor, checking the item for fulfillment of all the commitments by the seller. Ensuring the commitments of guarantee/warrantee and free servicing (if any) are stamped by the dealer/ seller.

Safe keeping of records—bills, warranty card, certificate of authenticity, free service (if any) coupons.

Relevant financial channels—credit card, EMIs, savings account.

Enjoying Your Life

Financial Planning for life cycle stage

The Goal—Planning the finances as per the life stages, in order to maintain financial independence and to build wealth at every stage.

What is it?

Your financial needs, values and priorities will change over time, and so will your financial goals. The key to a financially sound life is to understand your evolving needs and opportunities at every stage and making investment strategies that are appropriate for every stage. Although financial profiles of no two individuals are alike, most of us pass through three primary financial life stages.

Financial plan for life stages

I. Beginning to earn:

Goal—As you just start working and begin to earn, your aim at this stage should be to build a strong financial foundation through good money habits.

Characteristics—Income and expenses are lower compared to other stages, lesser responsibilities, new to financial instruments, learning to manage money, good risk appetite.

Important activities—Budgeting, spending wisely, regular saving, using credit card responsibly, beginning to invest and above all educating yourself on important aspects of personal finance.

Measures:
- You have no debt or debt that can be easily managed through your earnings.
- You have acquired right financial habits.
- You have built a decent cash reserve or saving.
- You have invested, as per your risk profile, for financial security (current and future) and for growth.
- You are contributing regularly to your retirement fund.

II. Peak of earning:

Goal—As your income peaks, so do your expenses and responsibilities. Your aim at this stage should be to build wealth and secure your financial future through investments, insurance and saving for retirement.

Characteristics—Income and expenses are at the peak, responsibilities are at their highest—family, children's education etc. You may have experimented and acquired many financial assets and instruments. Continuing money habits acquired in the earlier stages. Risk appetite may vary from person to person (for the same individual, it may be lower than the first stage)

Important activities—Continuing sound money habits, actively investing, actively planning for family's current and future needs and for retirement.

Measures:
- You have repaid most of your debts (barring possibly home loans).

- You have continued practicing right financial habits and possibly taught them (either consciously or simply through your example) to your children.
- You have an emergency fund and a decent cash reserve or saving.
- You have created a well-diversified portfolio of investments, as per your risk profile, for financial security (current and future) and wealth creation.
- You have built good amount of assets and in all possibilities own a house or two (or many).
- You have built a good retirement fund and are continuing to contribute to it regularly.

III. Retirement (or very close to it):

Goal—Whether you choose to retire (from work) early or late, your aim at this stage should be to enjoy your financial freedom and possibly share your riches.

Characteristics—income and expenses have begun to drop from the earlier levels, income is largely from passive sources—investments, pension fund. Responsibilities and obligations may have dropped significantly, as also the risk appetite.

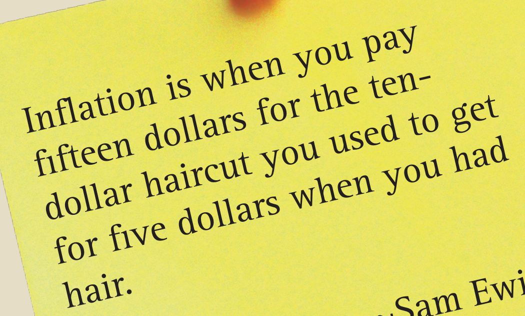
Important activities—Continuing sound money habits, enjoying returns on investments and retirement accounts, sharing your riches.

Measures:
- You have repaid almost all the debts.
- You still maintain an emergency fund and decent cash reserve or saving.
- Your investments are earning you returns—you may have possibly started systematic withdrawal.
- You may have built a legacy of assets to be passed on.
- Your retirement fund is actively supporting you at this stage.

Last Few Pages

ABCs of Financial Planning

Glossary



About Compound Interest—An important concept in financial planning

Compound interest has been called the eighth wonder of the world. Albert Einstein called it one of the greatest mathematical concepts of our time. Compound interest is a concept of adding the interest to the principal back to it for the next term, so that this amount becomes principal for the next term and the whole amount earns interest.

The power of compounding lies in its ability to turn a little bit of money, invested regularly into a whole lot of cash. It works like a snowball; when you save or invest, your money earns interest. The next year, you earn interest on your original money and the interest from the first year and interest on any further saving/ investment during the year. In the third year, you earn interest on your original money, any additional savings in the year (and the previous years) and the interest from the first two years. Thus if you continue to invest/ save every year, your every rupee invested so far earns more money, including the money you would have earned as interest in previous years.

But watch out as compound interest can work against you on your debt/loans. If you have accumulated debt on your credit card, your money owed would keep increasing exponentially due to compounding of interest until you pay your debt fully.

The trick then is to make this great force—compound interest—work for you rather than against you. Here are a few reminders from the book that will help you harness its power.

1. Start saving/investing as early as you can.

2. Keep saving/investing regularly—even if it as a small amount every month.

3. Forget about your savings and investments—as far as possible do not withdraw from your investments and do not bother about how slowly it is growing.

4. Repay debts in full and on time.

Glossary of terms (as used in this book)

Account—A periodical record of individual/household income, expenses, assets and liabilities.

Allocation—Distribution of resources (money) as per plan/budget.

Allowance—Pocket money, a portion of money allotted or granted to someone.

Asset—Something of value, that can be exchanged for cash generally with a profit.

Asset Allocation—It refers to how an investor distributes investments among different asset classes.

Asset Class—Collection of investment channels with similar risk, return potential and regulations.

ATM Card—ATM card or bank card issued by the bank where you hold an account. It allows holder to transact on his/her account through an ATM machine—deposit, withdraw, check balance, get mini statement.

Bond—A debt investment channel, a proof of loan issued by the borrower (generally government or companies) to the lender, with specific terms on interest, loan period.

Borrowing—To receive something from somebody with an intent to return it, generally with interest.

Budget—A plan of how income would be used for spending and saving.

Capital—The original amount invested.

Cost of Living—is the cost to maintain your certain standard of living.

Credit—A system that allows payments for purchase to be made on a later date, either in full or in installments.

Credit card—A plastic card issued by a bank that allows the holder to make purchase on credit through the bank. In this, the credit card company (bank) pays for the purchase and the card holder pays the bank later, collectively for all the purchases made on credit for a month.

Debit card—A plastic card that allows an alternative to cash payment. In this the payment is made upfront through the card holder's bank account.

Debt—Something that is owed.

Deductions—The amount which is subtracted as in from salary or from taxable income based on the provisions.

Deposit slip—A written note accompanying cash/cheque deposit in a bank account.

Diversification—Spreading investments across asset classes to minimize risks and maximize returns

Dividend—Payments made by companies to the shareholders representing their share in the company's profits.

Electronic transactions—Electronic payments by card (credit/debit) not involving physical transfer of currency.

EMI/ Equated Monthly Installments—Loan repayment in equal monthly installments.
ESOP (Employee Stock Option Program)—The program through which an employee is generally given share in the company's capital after a certain length of employment with the company.

Equity—Ownership participation equivalent to one's investment in a company through stock/shares.

Expenses—Outflow of money/cause of spending money.

FD—Fixed deposit is an account with a bank/post office that allows money to be deposited by the account holder and withdrawn at the end of a fixed term along with interest on it.

Fixed Rate of Interest—Interest on home loan that stays at a predetermined rate throughout the loan term.

Floating Rate of Interest—Variable or adjustable rate of interest that can vary through the term of debt—loan/bond depending upon the market conditions.

Income—Inflow of money/money received in the form of salary, profits, fees, dividend/interest.

Inflation—An increase in general level of prices/cost of living.

Installment—Portion of debt payable at certain specified times.

Insurance—A method of transferring financial risk of an uncertain event.

Insurance Policy—A plan/course of action that specifies the insurance terms, premium installments, claim procedure.

Interest—Price paid for borrowing money or that received for lending money.

Interest Rate—The percentage of amount of money charged per year for its use.

Investment—Use of resources/money in expectation of profit/more money from it.

Liability—An obligation/debt or responsibility owed to someone, a disadvantage

Life Cycle Stages—The different stages one passes through from birth to death—childhood, youth, marriage/family, middle age, retirement, old age.

Life Cycle Needs—General needs of different life cycle stages.

Loan—An arrangement with a lending agency to borrow money on certain repayment terms

Maturity—A term indicating date of repayment of principal and interest.

Mutual Fund—A professionally managed investment scheme that pools money from many investors and invests in investment channels as per the fund's investment objective.

Net Worth—A total of assets minus total of liabilities can be considered as an individual's wealth or net worth.

NSC/National Savings Certificate—A long term safe investment and tax saving option issued by Government of India's Department of Post.

PAN (Permanent Account Number) is a national identification number in India, issued by the Income tax department to all taxpayers with a taxable income.

Passbook—A book that keeps track of transactions in individual bank accounts.

Pay in Slip—see deposit slip.

PIN (Personal Identification Number) is a secret numeric password to access accounts through ATM.

RD/Recurring deposit—A systematic monthly investment plan in the form of deposit account, wherein you deposit a certain sum every month to get a lump sum on the maturity of the account.

Reserve—Savings/money reserved or kept aside for future use.

Retirement—An act of withdrawing from active employment.

Retirement Account/Fund—An account/fund that allows long term savings/investments for retirement. E.g., provident fund, pension scheme, etc. These also offer tax advantages.

Returns—Gain (or loss) from investment.

Risks—A possibility of a negative outcome, which has a potential to cause financial loss.

Saving—The practice of storing or putting aside money for future use.

Saving account—A bank or post office account that allows safe keeping of money and also earn interest.

Sharing—The act of helping someone in need by sharing one's riches.

Stabilizing Finances—A proactive measure of managing probable emergencies and risks so as to ensure minimum financial impact and a stable financial future.

Stock/Shares—Part ownership in a company traded in stock markets

Take Home (Net) pay—The pay actually received by an employee after deducting taxes and provident fund contributions and after adding bonuses (if any).

Warranty—An undertaking that the product/service sold would be as per what's promised/ declared by the seller. In the event the product/service fails to live up to the promise, the buyer would be entitled to a free repair/ replacement. Warranties are generally for limited period of time, and some may be limited to certain geographies only.

Wealth—see Net Worth

Withdrawal slip—A written document through which one can withdraw money from one's account.

Last Few Pages

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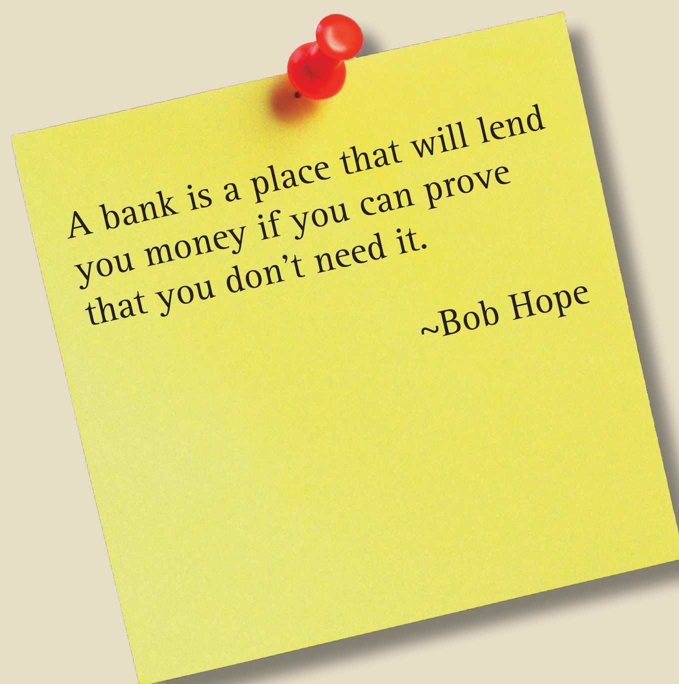

Books

- The Automatic Millionaire by David Bach
- The CashFlow Quadrant by Robert Kiyosaki
- The Complete Idiot's Guide to Managing your Money by Robert K. Heady and Christy Heady
  Learn to Earn: A Beginner's Guide to the Basics of Investing and Business by Peter Lynch and John Rothchild
- The Intelligent Investor by Prof. Benjamin Graham
- Common Stocks Uncommon Profits by Philip Fisher
- The Little Book of Common Sense Investing by John Bogle

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