The Complete Financial Planning Guide

What is Financial Planning?

Financial planning is a critical exercise in ensuring long-term financial security. A financial plan is a road map to help you achieve your life's financial goals.

Here are three basic questions that you will answer during financial planning:

- Where are you today? What is your current financial situation?
- Where do you want to get to? What is your vision of your future financial situation?
- Will you be able to get there? How do you plan to achieve your vision?

During the financial planning process you analyze what your financial needs and goals are. Then, you quantify in money terms what resources you need to meet those goals, and quantify the time period during which you want to achieve these goals. Finally, you write an action plan on what you need to fulfill your plan in terms of what products to buy and what types of savings to make.

Can you do Financial Planning yourself?

Of course you can, but just like you won't repair your own watch or car on your own, you need to come to an expert for financial planning. Otherwise, without the right financial skills and tools for financial planning, your finances can end up as a disaster.

If you feel you can do financial planning on your own, you might want to answer the following questions:

- Is your family going to be financially secure, whatever happens to you?
- Are your finances tax efficient? Do you know how to legally save taxes?
- Are you confident that investments give you the best return in a rising or a falling stock market?
- Do you have enough money to pay for your son or daughter's education? How about for their wedding?
- Do you wish to retire in the mountains or next to the beach? Is this just a wish, or have you enough money to turn this wish into reality?
- If you don't have a Will, do you know what will happen to your hard earned assets upon your death?

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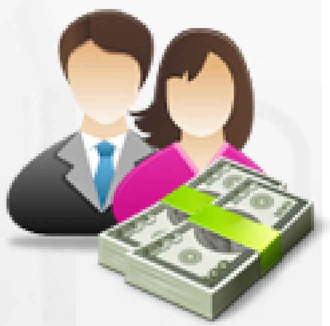

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Someone in their 20s will have different needs as they enter their 30s. Also, over this time period your risk profile might have also changed (age-based financial planning). Someone who is married with no children will have to update their plan when their child is born. As a start, if the person did not have any insurance, he or she must buy protection because the family size has increased. Also, this would be a good time to start thinking about writing a will to identify who your beneficiaries will be (life-stage based financial planning).

Go through stages of life:

First job, marriage, buying a house, children, promotion, education/marriage, grandchildren / retirement

You and Your Financial Plan

Financial planning is one of the things that not many people think about. However, financial planning in India is important to do because it can make your life easier.

While you cannot predict the future, you can certainly be better prepared for it. A written financial plan is designed to make sure that you are financially prepared to deal with whatever happens in your life. And this is not just dealing with the unexpected events, but basic things like buying a car or taking a home loan, funding your children's education or marriage, or taking care of your loved ones.

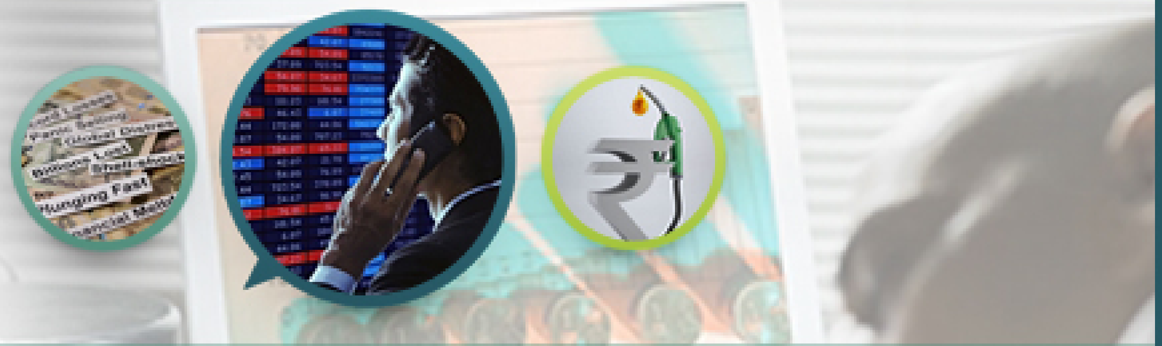
You don't have to be mega rich to have a financial plan. Neither do you have to be very old and approaching retirement. It does not matter how much you earn or what your age is. All of us have something to plan for. In fact, our financial situation influences almost every aspect of your lives....from the type of house we live in, to the type of car we drive, to how many vacations we can take. Regular financial planning can help give you peace of mind.

If you have dreams, you need a financial plan!

So, what do you need to know about yourself when thinking about a Financial Plan?

Your financial plan entirely depends upon how much effort you are willing to put in. This means not just having a good handle on the details of your income and expenses, assets and liabilities, but more importantly on the following items:

- *Time Horizon and Goals*
- *Risk Tolerance*
- *Liquidity Needs*
- *Inflation*
- *Need for Growth or Income*



No doubt there are other factors that are important as well, but we believe that the above five require a more detailed study on your part.

Time Horizon and Goals:

It is important to understand what your goals are, and over what time period you want to achieve your goals. Some goals are short term goals those that you want to achieve within the year. For such goals its important to be conservative in one's approach and not take on too much risk. For long term goals, however, one can afford to take on more risk and use time to one's advantage.

Risk Tolerance:

Every individual should know what their capacity to take risk is. Some investments can be more risky than others. These will not be suitable for someone of a low risk profile, or for goals that require you to be conservative. Crucially, one's risk profile will change across life's stages. As a young person with no dependents or financial liabilities, one might be able to take on lots of risk. However, if this young person gets married and has a child, he/she will have dependents and higher fiscal responsibilities. His/her approach to risk and finances cannot be the same as it was when he/she was single.

Liquidity Needs:

When do you need the money to meet your goal and how quickly can you access this money. If you invest in an asset to and expect to sell the asset to supply you funds to meet a goal, then please understand how easily you can sell the asset. Usually, money market and stock market related assets are easy to liquidate. On the other hand, something like real estate might take you a long time to sell.

Inflation:

Inflation is a fact of our economic life in India. The bottle of cold drink that you buy today is almost double the price of what you

paid for ten years ago. At inflation or slightly above 4% per annum, a packet of biscuits that costs you Rs 20 today will cost you Rs. 30 in ten years time. Just imagine what the cost of buying a car or buying a home might be in ten years time! The purchasing power of your money is going down every year. Therefore, the cost of achieving your goals need to be seen in what the inflated price will be in the future.

Need for Growth or Income:

As you make investments, think about whether you are looking for capital appreciation or income. Not all investments satisfy both requirements. Many people are buying apartments, but are not renting them out even after they take possession. So, this asset is generating no income for them and they are probably expecting only capital appreciation from this. A young person should usually consider investing for capital appreciation to take advantage of their young age. An older person however might be more interested in generating income for themselves.

Your Life - Your Goals

What financial goals should you be thinking about?

Anything you want to do in your life can usually be quantified in terms of the money that you will need to spend on it. All goals have a monetary value attached to them. Financial Goals that you should think about can basically be categorized into Foundation Goals (or basic needs) versus Lifestyle Goals (or good to have).

Foundation goals should be given first priority when creating a financial plan. These are common to most people. Foundation goals include:

- *Housing need for shelter*
- *Basic life insurance and health insurance for protection*
- *Having enough savings to pay for your children's school and college expenses*
- *Having enough savings to pay for your children's marriage expenses*

- Maintaining an emergency fund to be able to meet any unexpected expenditure

Depending on your means you have to prioritize as to which goals are most important for you and start saving and investing to meet those goals. Just like a building is constructed on a stable foundation, your financial condition should also be built on a stable foundation.

Once your basic needs are met you can start to think about your lifestyle goals. These goals are somewhat discretionary and could differ greatly from person to person depending upon the type of lifestyle you want for yourself and family. Lifestyle goals are highly personal and are often dependent upon what dreams you have. Examples of lifestyle goals include:

- *Owning a vacation home in a hill station*
- *Buying the latest digital camera*
- *Taking a cruise in Europe as opposed to holidaying in India*

How can you know how much to save or borrow to meet your goals and what to invest in?

First, it is important to quantify your goals. You must estimate how much it is going to cost to achieve your goals. For example, a buying a home in India could cost Rs. 30 lakhs or Rs. 50 lakhs or more depending on what you want.

Second, it is important to know at what point in the future do you want to achieve your goals. Your goals could be short-term in nature (within less than 12 months from now), e.g., buying a TV, prepaying your car loan or creating a contingency fund for an emergency. On the other hand, your goals could be medium term to long term,e.g., like buying a bigger home three years from now, providing for your daughter's college education twelve years from today and having a retirement corpus 25 years hence.

Once you have quantified your goals and know their time horizon, then based on your risk profile, you can select the appropriate savings and investment instruments and assess your borrowing needs.

The following are the THREE arrangements which need to be ensured before venturing out to retire early:

1. Accumulated corpus and wealth created

The sufficiency of the corpus for an enjoyable post-retirement depends on the length of such expected period and the extent of monthly expenses. Also crucial are the expected inflation, including lifestyle inflation, and the commensurate return expected from investing corpus. The emphasis is on striking a critical balance between the withdrawal rate from the corpus and an adequate rate of return on the corpus.

2. Management of corpus

There should be a robust and diversified asset base. A second house ensures a good market-linked income stream and a healthy appreciation in the asset along with tax benefits, if a loan is availed to buy the second house. A prolonged retirement period of around 35 years requires financial assets which provide an inflation-beating return.

An optimum asset allocation and an effective monitoring of the same in consultation with experts, usually Certified Financial Planner(CM) professionals who are trained in this aspect, ensures the protection of a sustained desired income stream.

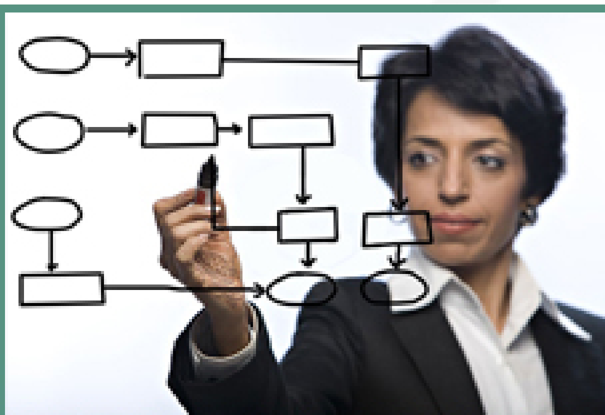
3. Commencement of a new career

After taking an early retirement one can pursue an alternate career of choice. The time engagement, social networking and pecuniary aspects along with an image and reputation in society are other benefits. Managing a proprietorship firm or a partnership firm is the most effective way of such engagements. Taking up consultancy and advisory services or freelancing can also be explored on fee and commission basis.

One aspect that comes forth as a result of the above observation is the importance of health insurance. If health insurance is taken at an early age it will serve the purpose as well as the employer benefits would cease to be available earlier than normal retirement. Some other types of insurance such as accident, disability and critical illness cover must be taken to protect the retirement kitty.

Life gets more difficult as one gets older, thus it become imperative that if one is going to live longer s/he must start planning for it right away. Retirement planning is a relatively simple exercise which requires investing discipline and regular monitoring.

However there are some important points which should be considered while planning for retirement.



1. Start early

If one wants to retire early, one has to start planning for it early. It is most practical to start at a young age, as soon as a person gets in to employment. A person has higher risk bearing capacity to enable her/him earn suitably higher returns. The effect of compounding does wonders to accumulate a sizable retirement kitty with the small streams of savings invested.

2. Set clear retirement goals

One should be clear about one's expenses in relation to the income earned. The expenditure post-retirement and the lifestyle that one would like to maintain will give an idea on how much money is required as corpus on retirement and what quantum to be invested periodically at an expected rate of return.

3. Be disciplined

Since retirement is the most distant goal, the other short-term goals might take precedence and one has the tendency to dip into retirement savings for fulfilling other goals.

If one is able to follow all the steps mentioned here in a disciplined manner over the desired working time with the help of a financial planner then one can sit down and relax enjoying the sunset years.

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