Catalog

BEGINNER'S HANDBOOK FOR FINANCIAL FITNESS IN INDIA

ZEBRA LEARN

MONEY SMART

IN YOUR

20s AND 30s

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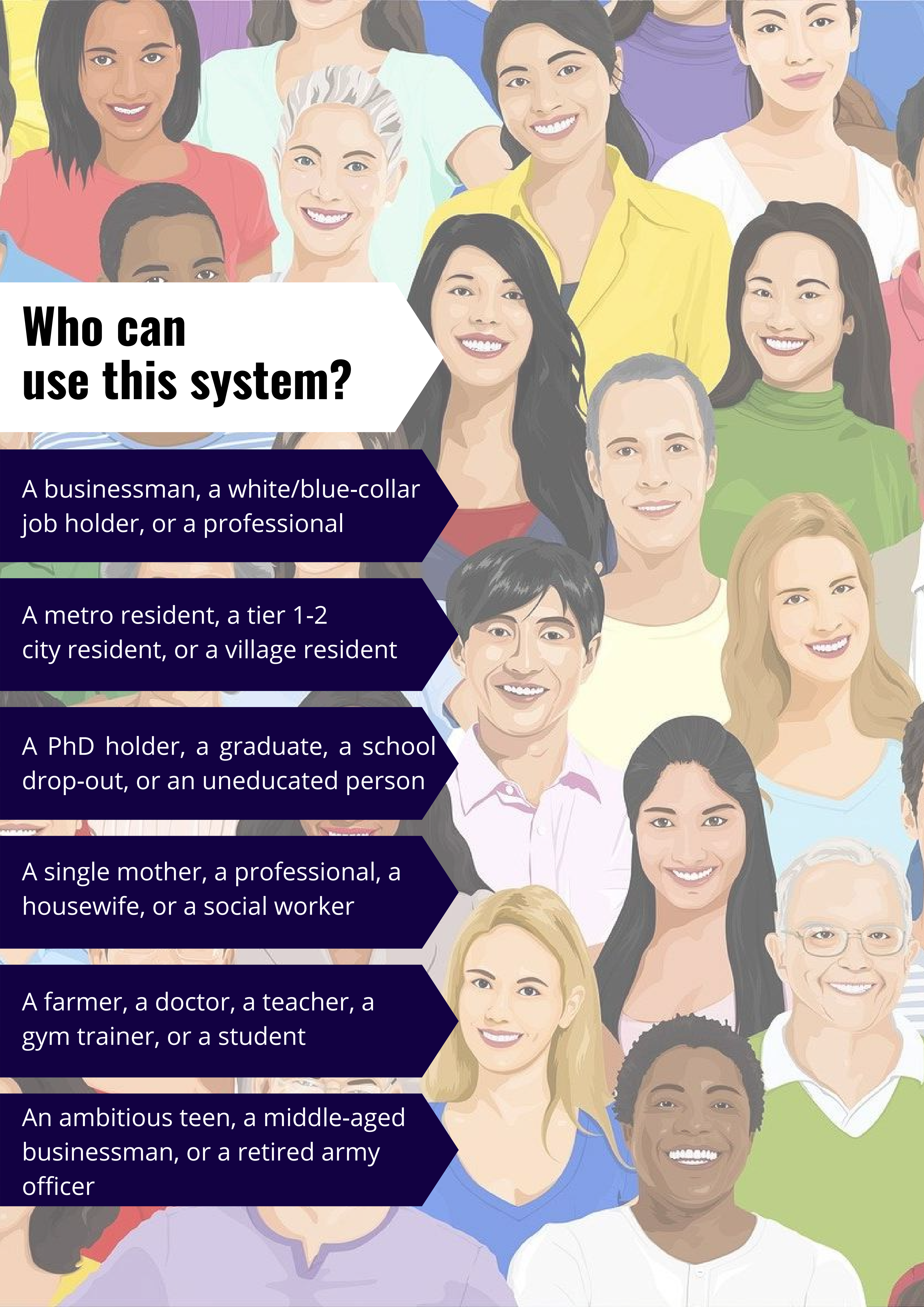
LET'S BEGIN

Hi Zebra Learners! Welcome to the book that presents the most complete and comprehensive structure, developed to handle personal finance. This book has been written down with a keen focus on objectifying personal finance and its processes to the utmost. Our objective has been to make personal finance a 'black and white' matter and leave nothing in the grey and the very name 'Zebra' is indicative of that.

To be honest, it is a rather challenging task. After all, we have to create a system, which works in all the given situations and is relevant for people coming from different backgrounds (refer to the next page). Imagine creating a system that effectively applies and works for all these people, almost like a thread that binds them together to meet their financial objectives. Well, we do believe that we have perfected the system.

This book illustrates a step-by-step process of how anyone, irrespective of age, profession, location, background, etc. can effectively create a financial plan and manage their money within the Indian context. Our team has spent over a year coming up with the concepts and tools discussed in the book. After completing this book, every reader will undoubtedly be capable of coming up with a 'Lazy Financial Plan'.



Who can use this system?

- A businessman, a white/blue-collar job holder, or a professional
- A metro resident, a tier 1-2 city resident, or a village resident
- A PhD holder, a graduate, a school drop-out, or an uneducated person
- A single mother, a professional, a housewife, or a social worker
- A farmer, a doctor, a teacher, a gym trainer, or a student
- An ambitious teen, a middle-aged businessman, or a retired army officer

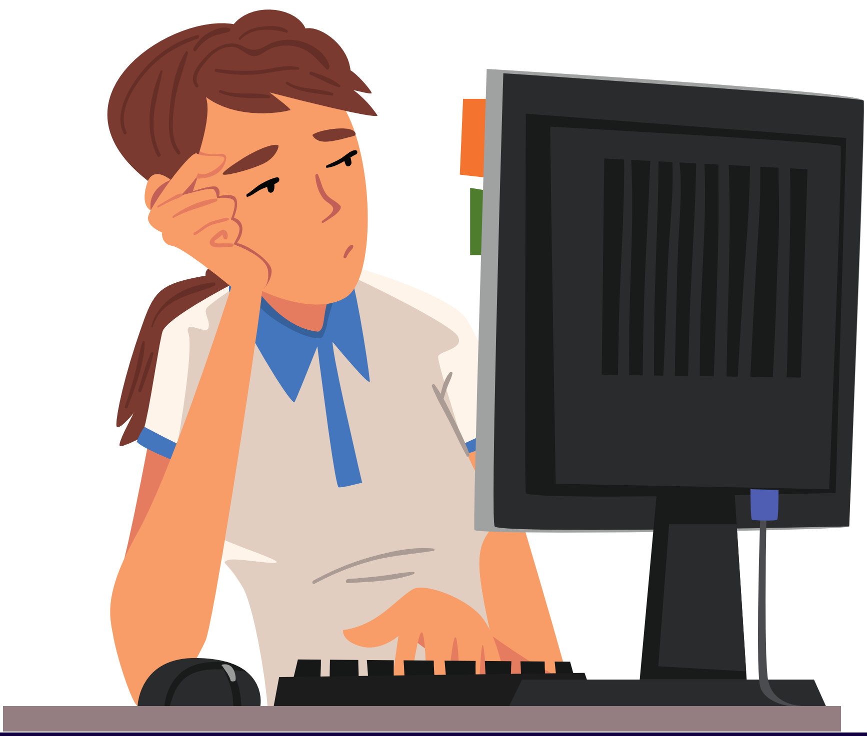
WHY DO WE CALL IT A LAZY FINANCIAL PLAN?

The first thing to understand is that a good financial plan is always a lazy plan. Why do we say lazy? We are aware that all of us have jobs to do, businesses to run and a family to take care of and neither do we need nor want to add one more layer of work to our already busy schedule by continuously working on a financial plan.

We often come across people who are highly enthusiastic about the subject, are constantly tracking the same, and are willing to give this matter a lot of time, effort, and thought. But honestly, this is not a one-time thing. Our financial plan is a lifestyle item, that should be constantly active and in practice. So believe us when we say that a good financial plan is one that is for the lazy. A couple of hours each month should suffice. We could use the rest of the time to focus on our cash inflow – salary, profits, commissions, etc.

An average plan that is executed well is much better than an excellent plan that has been subjected to poor execution. So, while on it, sit back, relax and build a plan that is simple and easy to follow through. Just stick to the basics and there is no need to complicate things.

However, having said that, being lazy does not mean not doing our share of research properly, and by no chance, does it mean being ignorant of our portfolio. We need to track our portfolio constantly. Being lazy simply means making a plan and devising an execution strategy that is more sustainable and doable in the long term.



WHAT IS IN THIS BOOK

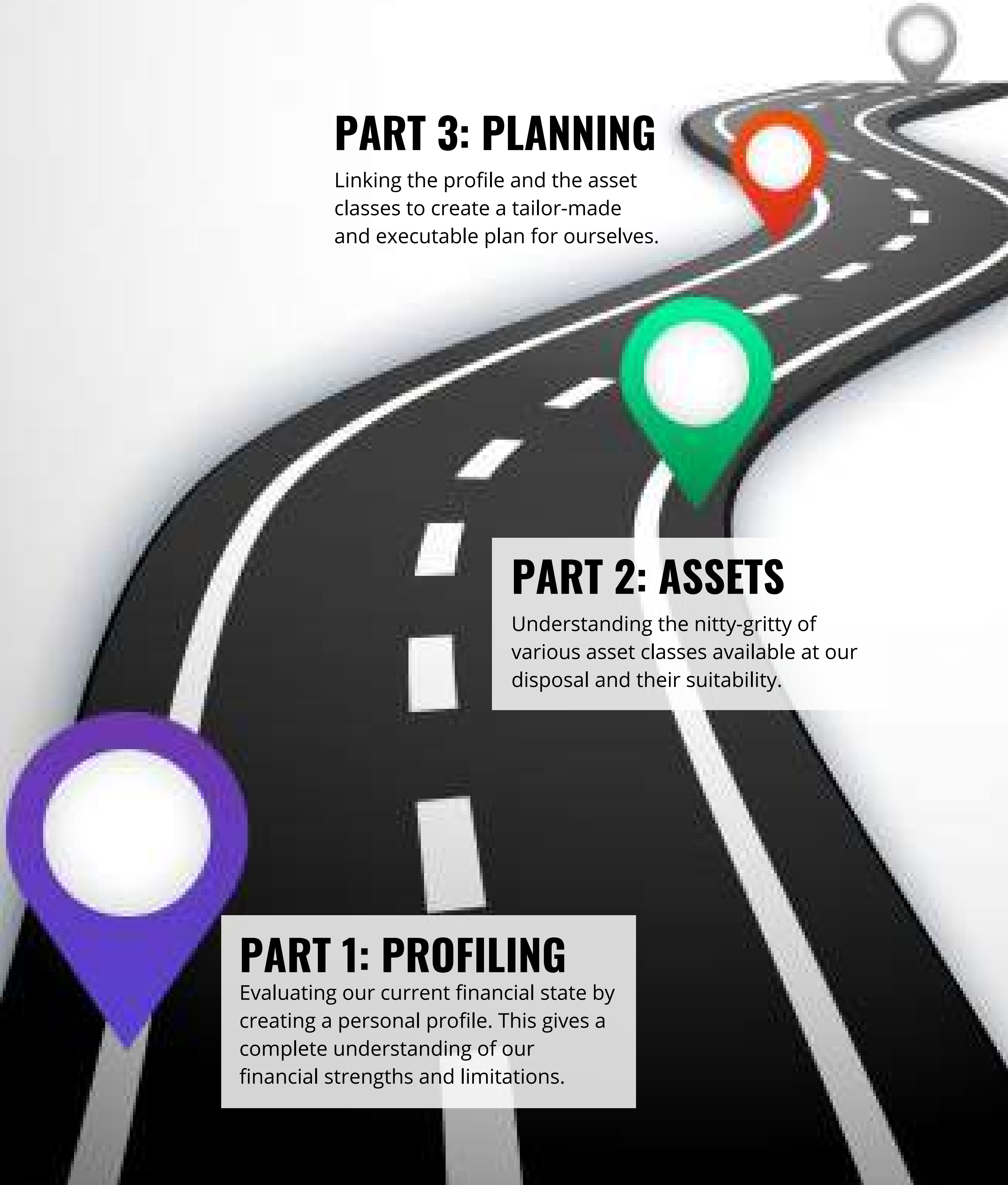
In Part 1 of this book, we will talk about 'profiling'. Taking a hard look at our current financial profile, we will understand how we can create a profile i.e. a personal balance sheet, a personal income statement and keep it separate from our business. We will then comprehend our borrowing position and life-cycle stage. Going forward, we will evaluate ourselves based on the different parameters that affect our financial profile i.e. risk, returns, taxes, time horizon, legal factors, liquidity needs, and unique circumstances. On its completion, we would receive a true picture of our financial situation.

We will also learn about the GETAI principle that helps us determine our risk-taking ability and this is what makes this book special. To date, the risk-taking ability was left for people to evaluate subjectively. We have carefully devised a set of 10 'Yes/No' questions that objectively judge our risk-taking ability.

In Part 2, we will understand the different asset classes available to us as an individual and the suitability of each asset class. We will also learn how we can pick the most suitable instrument within each asset class i.e. picking the right mutual fund scheme, insurance policy, and so on.

Coming to Part 3, we will use our financial profile and asset options to create a financial plan for ourselves. This is where Part 1 (profile) and Part 2 (asset classes) will be linked together. We understand that it is often overwhelming for readers to process and understand so many asset classes in one go and deal with each of them while creating a profile. Thus, we have tried to make this process as objective as possible.

After studying this book and some practice, we will not need any other book or course for personal finance. So, we have to make sure that we keep things simple and not overburden ourselves with too many things.



PRACTICE
PRACTICE
PRACTICE

PART 3: PLANNING

Linking the profile and the asset classes to create a tailor-made and executable plan for ourselves.

PART 2: ASSETS

Understanding the nitty-gritty of various asset classes available at our disposal and their suitability.

PART 1: PROFILING

Evaluating our current financial state by creating a personal profile. This gives a complete understanding of our financial strengths and limitations.

We have to accept and be prepared for the journey we have signed up for with this book. The first part might come off as slightly boring and the second part might confuse us. But finally, in the third part, we will find all the things falling perfectly in place and thus, completing the puzzle. It will all start making sense to us and by then we will be in a position to make a call for ourselves and create our personal Lazy Financial Plan.

WHAT IS NOT IN THIS BOOK?

Firstly, this book is not a career guide. Our personal career decisions are a result of our skills and preferences. Our financial situation might play a role in determining what we can and cannot do, but only to a certain extent. This book will come in handy to absolutely anyone, irrespective of what they do, what age group they fall into, and so on.

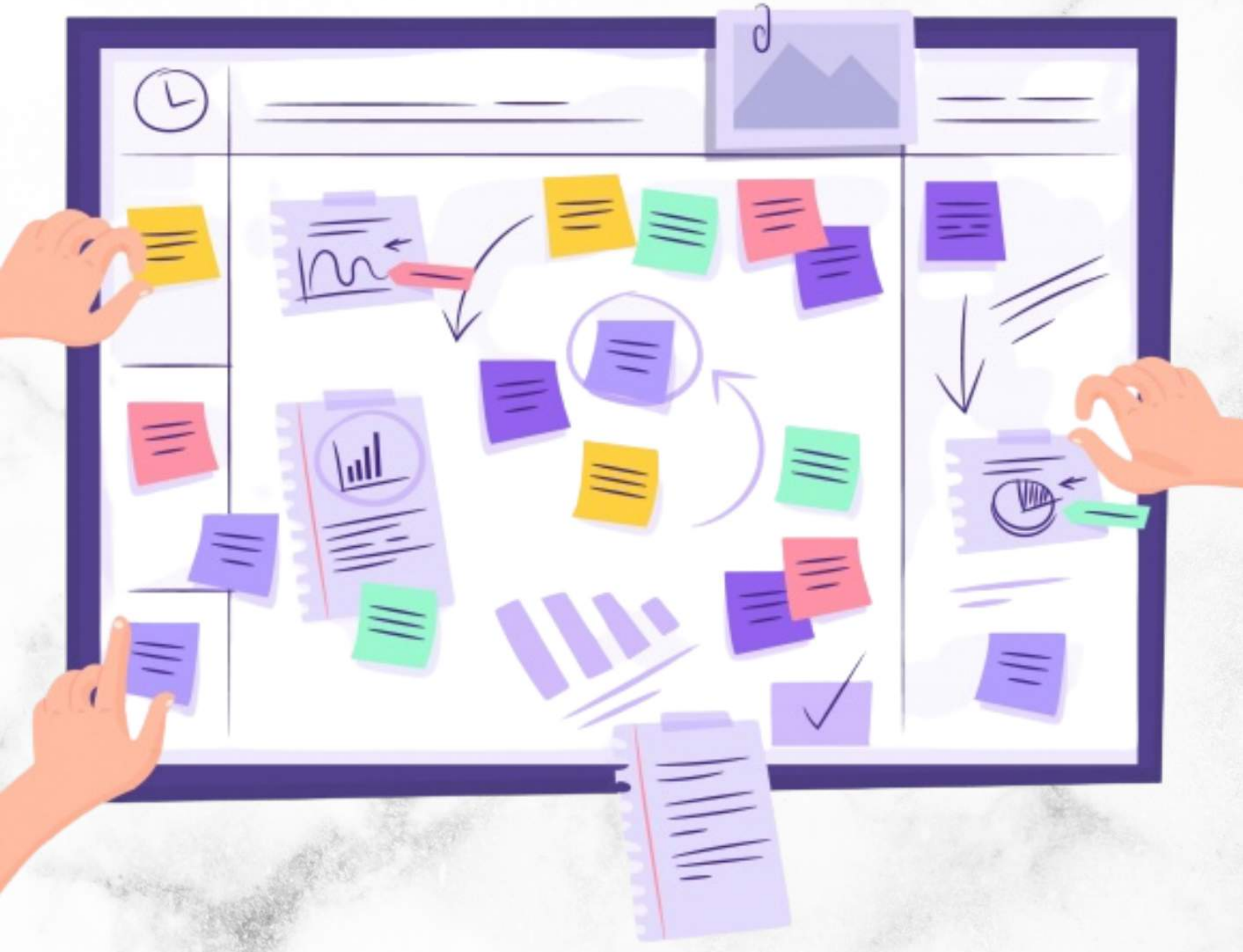
This book is not a book on how we can expand our earnings. People often confuse or assume personal finance books to be texts on 'How to earn more?' To be very honest, there can be no such book. It is with our skill and effort that we can earn more. This is a book which comes to use after our cash flow (earnings) is in order, whether as our salary, fees, or profits.

This book is a reminder that there is no shortcut to EFFORT. As a result, we need to realize and understand that cash flow problems cannot be solved with investing solutions. It is already tough to earn money, but once we have done that, the Lazy Financial Plan should enable us to create a system that allows our finances to take care of themselves. Our money and investments should work for themselves.

We ensure that this is not a motivational book. A lot of personal finance books are simply motivational i.e. increase savings, spend after saving, diversify, and what not... but let us be real, that is pure motivation with no systematic approach. It does not work. Personal finance is 80% science and 20% art. If we stick to the basics, chances are things will work out the way they are supposed to. Everything is linked to one another and we need to understand how each and everything is interlinked. We do not believe in 'Gyaan' – there is an abundance of it already on the internet for free.

LAZY FINANCIAL CANVAS

TRIED AND TESTED CHEAT-SHEET FOR A FINANCIAL PLAN



ONE
PAGE PROFILING
CANVAS

ZEBRA LEARN

WHAT IS A PROFILE?

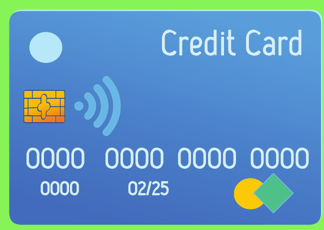
The most primary thing to learn is, "What is a profile?" A profile is a list of facts about us. Anything and everything about us related to the said topic is called a profile.

In this context, when we talk about creating a financial profile, we include everything about our finances. It includes how much we earn, from what sources, the stability of our income, our expenditure, assets we own, our liabilities, and so on. We also include other detailed factors such as the impact of taxes, the impact of social pressures, legal issues, etc. We take into account our preferences with different asset classes, comfort and so much more.

So, while creating a financial profile, it is very important to list down each and everything that impacts our finances. Shortly, we will learn how we can do so in a structured procedure. Our profile acts as a base for us to create a 'Lazy Financial Plan' and hence, how well we profile ourselves will determine how well we can plan. We have made it a point to make the process as easy and objective as possible.

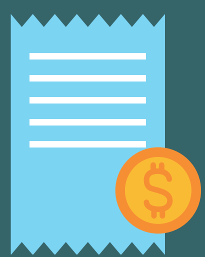
We should keep in mind that our personal finance profile should be very specific to our needs and requirements. It should be a complete reflection of our financial habits. It cannot be generic. Financial profiles are different for a father and his son, a husband and his wife, a brother and his sister, and so on. So, we are to always create a profile that suits each of us exclusively.

ASSETS



LIABILITIES

INCOME



LIABILITIES

WHY IS PROFILING IMPORTANT

Let us think of a time when we pay a visit to the doctor. Let's say we spend 20 minutes in his chamber. For the first 15 minutes, what does the doctor do? He will ask questions about us, our symptoms and discomfort, our habits, and so on. Once he reaches an understanding of the same he will very quickly in the remaining 5 minutes prescribe us the required medication. So, what did the doctor just do? In the first 15 minutes, he created our medical profile upon completion of which, he decided to move forth with his prescription for us based on the same profile.

Similarly, if we go to a nutritionist, they spend time understanding our food habits, preferences, body type, metabolism, sleeping habits, and so on. They too create a nutritional profile for us before suggesting a diet plan. Any lawyer, before picking up any case, spends time understanding the case and its history and thus creates the client's legal profile.

We see that in almost every profession, the professional first creates a profile for the client or customer, based on which they come up with an effective plan. Then why should financial profiling be any different? So, we will first evaluate our current situation with a profile that represents our true financial position. Then we will construct a plan.

We will take a look at the following examples that illustrate how people with similar backgrounds will have extremely different profiles based on their financial circumstances. Hence, upon taking this initiative independently, our plan will be an 80% reflection of how well we profile ourselves.

HIMESH & RICHA

They are siblings living together. Himesh is starting a new business, while Richa is looking to take a student loan

KABIR & ROHAN

Childhood best friends. Rohan is a budding entrepreneur, while Kabir has a stable job

RIYA & SIMRAN

Two lawyers working together. Riya has a family of 3 to support, while Simran lives alone

AJAY & AAYUSHI

Father & daughter, Ajay is planning for his retirement, while Aayushi just started her new job

LAZY FINANCIAL CANVAS

Balance Sheet

Liabilities

Assets

Networth

Income Statement

Income

Expenses

Return Objectives

Risk

Risk Taking Ability

Risk Taking Willingness

Time Horizon

Taxes

Liquidity

Legal & Regulatory Constraints

Unique Circumstances

Insurance Needs

Barriers

LAZY FINANCIAL CANVAS

In the first part of the set, we will focus on profiling ourselves. We have already seen what a profile is and learnt about its significance.

We will use the 'Lazy Financial Canvas' to profile ourselves from a financial perspective. Here, we will first identify all the elements of the canvas in a detailed manner. Then we will learn how to fill up the canvas and also take a look at the questions that are to be answered.

In reality, while filling up the canvas, the devil is in the detail. How detailed we are while filling this canvas will determine how well we can plan for ourselves. Once the canvas is filled up, it will give us a holistic view of our finances with every significant bit covered. So, to fill the canvas, we will divide the entire process into four steps.

CANVAS OVERVIEW

Before we go over the specifics of every element of the Lazy Financial Canvas, let us first take a look at what each element stands for and the objective of each of the blocks in the canvas.

BALANCE SHEET

A balance sheet in common language means a list of all that we own and all that we owe. So, in a balance sheet, we create a list of assets that we own and a list of liabilities that we have to repay. This gives a clear picture of how much we have left as of today after paying all the liabilities. Therefore, first and foremost, we will commit ourselves to create a personal balance sheet.

NET WORTH

Net Worth is a part of the balance sheet that defines the net difference between our assets and liabilities. It means how much we are likely to have left if we repay all our liabilities today. It is our true worth as of today.

INCOME STATEMENT

An income statement is a list that comprises all the different sources that serve as your income and different avenues for expenditure. The difference between income and expenses is a surplus or deficit that is your savings or drawings. We will see how to create a personal income statement in great detail going forward.

RETURN GOALS

The next element of the canvas is the return goals. We will list down all the goals that we intend to achieve financially. Then we quantify them in terms of time and money i.e. how much we will need and in what period. After that, they are prioritized through a rating system. This gives us an understanding of what we are trying to achieve.

RISK TAKING ABILITY

The risk-taking ability is how much risk we will be able to take in our investments based on our goals, time horizon, income, and assets. Risk-taking ability is not only based on our preferences but also on our circumstances. This is where we use the GETAI principle to evaluate our risk-taking ability objectively.

RISK TAKING WILLINGNESS

Risk-taking willingness is the second half of our risk profile. Once we have understood, how much risk we are capable of taking, the next thing that we will do is evaluate, how much risk we are willing to take. This is not based on the circumstances at hand but on our preferences. It is very subjective and we will learn how to deal with the same depending on our past experiences and the kind of financial investor we are.

TIME HORIZON

The next element is the time horizon. In this, we assess the time horizon for each goal that we are investing in. Also, we try and create a financial timeline for our major goals and personal milestones. This acts as a guide for us in the planning stage.

TAXES

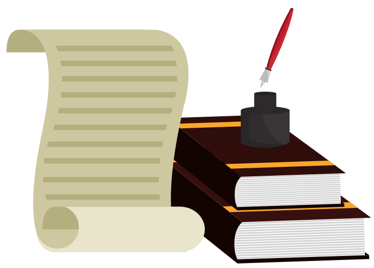
This is a simple yet relatively confusing concept. We focus on tax implications on our investments and also various tax deductions that we can benefit from. These tax implications affect the financial decisions we make. We do not have to be worried about the correct answer since there is no correct answer. The answer is relative to every individual's circumstances.

LIQUIDITY NEEDS

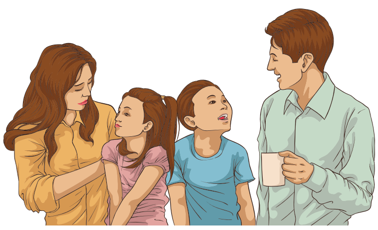
The liquidity needs focus on estimating the appropriate amount of liquid assets and estimating the forms of these assets. Here, we will evaluate our transactional and emergency needs. After that, we will learn about the different kinds of liquid assets that can be used for these needs.

LEGAL AND REGULATORY CONSTRAINTS

For most people, this would be pretty simple. There are legal and regulatory conditions that need to be followed within our plan. Most financial products take care of the general rules. If there is any specific restriction on us, we need to be considerate of it.



UNIQUE CIRCUMSTANCES



Unique circumstances reflect any factor unique or particular to us that has not been accounted for in the above profile. For instance, we may be attached to an asset emotionally, our parents won't get along on our plan, we see some asset class in an inferior manner, etc. all such unique circumstances are reflected over in this section.

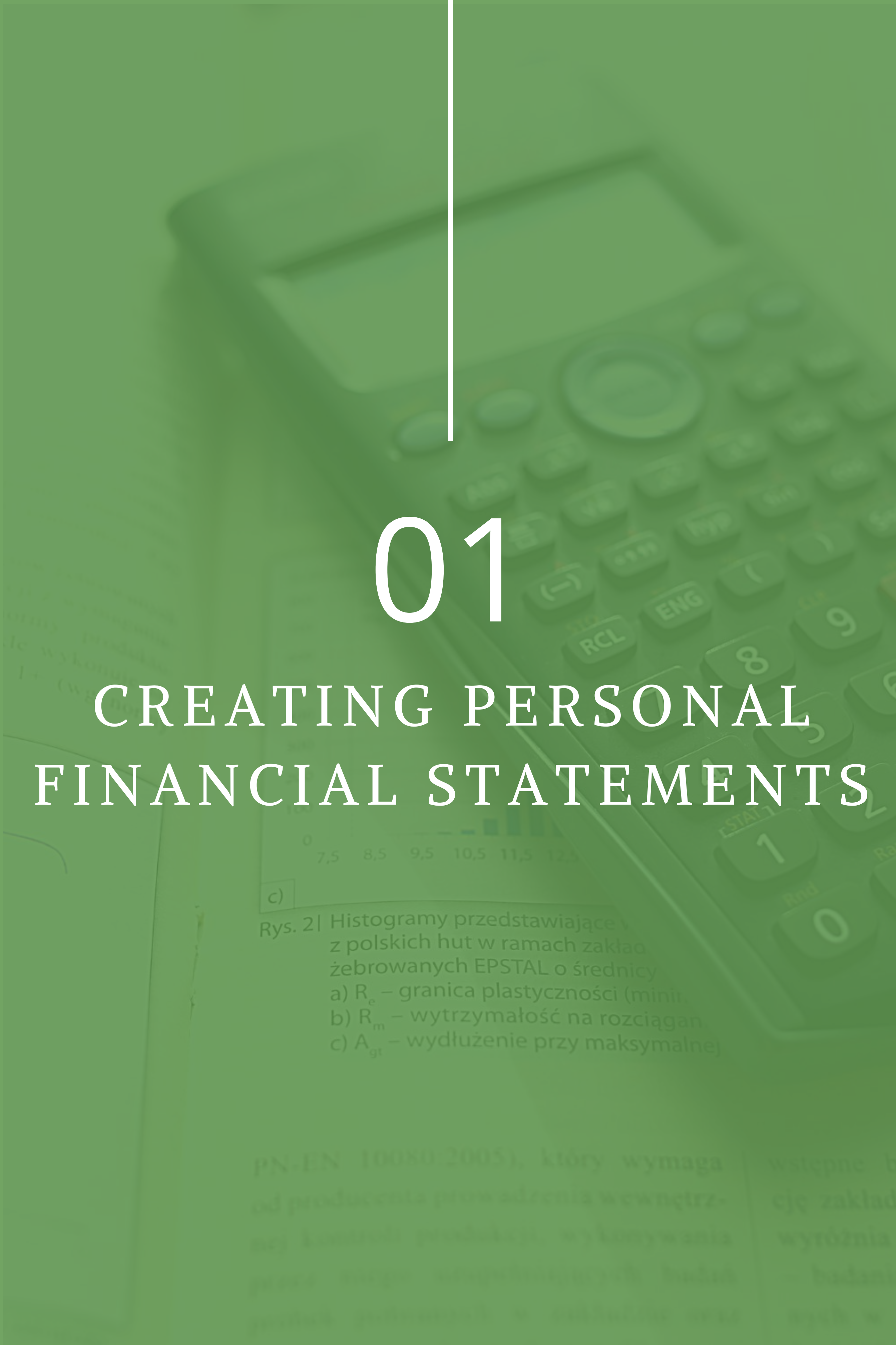
INSURANCE NEEDS

This section will identify the various risks faced by us or our assets and the ones that are significant enough to hamper our financial position and plan. On this basis, we will evaluate the different insurances that we would need and determine the amount of insurance coverage.

BARRIERS

The last block in the canvas focuses on understanding the different barriers that act as obstructions while following the plan. We have identified six barriers and we will learn to deal with them.

In this manner, we will go about filling every component of the Lazy Financial Canvas. In the following segments, we will learn to profile ourselves and fill this up meticulously. Once we do this, we would be in a strong position to create a plan for ourselves. Also remember, this profile is something that needs to be updated every six months or so.



01

CREATING PERSONAL FINANCIAL STATEMENTS

BALANCE SHEET

Let us begin by creating a personal balance sheet. A balance sheet is a list of all the assets that we own and all the liabilities that we have to pay. For example, all that is in our possession like a car, a house, stocks, jewellery, investments, business, etc. are our assets. On the other hand, all that we owe such as personal loans, car loans, home loans, credit cards, unpaid bills, etc. are all our liabilities. While creating a balance sheet, we will list down all our assets on one side and all the liabilities on the other side and then check the net difference. These will be the net assets that we own after paying all the liabilities. It would be considered our net worth.

Liabilities

All that an individual owes to others

STUDENT LOAN

HOME LOAN

CREDIT CARD

OUTSTANDING BILLS

Networth

The true worth of an individual
(Networth = Assets - Liabilities)

Assets

All that an individual owns

HOUSE

GOLD

CAR

BUSINESS PROPERTY

INVESTMENTS

CASH

Keep it simple. Refrain from using Excel, and stick to the good old pen-paper for this. Don't make complex company balance sheets. Keep it informal, avoid jargons and remember to preserve this piece of paper.

NITTY-GRITTIES OF CREATING BALANCE SHEET

1 FOCUS ON NETWORTH, NOT ASSETS

While creating a balance sheet, we must always focus on increasing the net worth. It is not the increase in assets that counts, but the increase in net assets after paying all the liabilities. If both our assets and liabilities increase by Rs. 20 lac, then there is no change in the net-worth. However, if the assets increase by Rs. 2 lac with no change in liabilities, then our net worth increases. Paying off our liabilities also has the same impact on the balance sheet. The net worth is our true monetary value.

2 ASSETS BACKED BY LOANS

Here we will learn to treat an asset bought on loan. On the asset side, we will write down the entire amount of the asset, irrespective of how we bought it. Then, we will proceed to write down the total loan amount on the liabilities side. So, if we bought a car worth Rs.5 lac and borrowed Rs. 3 lac for the same, we will write down Rs. 5 lac on the asset side and Rs. 3 lac on the liabilities side. People often omit this and simply write Rs. 2 on the asset side because they only paid Rs. 2 lac out of their pocket. But this would lead to wrong conclusions and decisions going forward. So, treat the loan and the asset as two different items and write it down in the balance sheet.

Liabilities

CAR LOAN = 3,00,000

Networth

5,00,000 - 3,00,000 = **2,00,000**

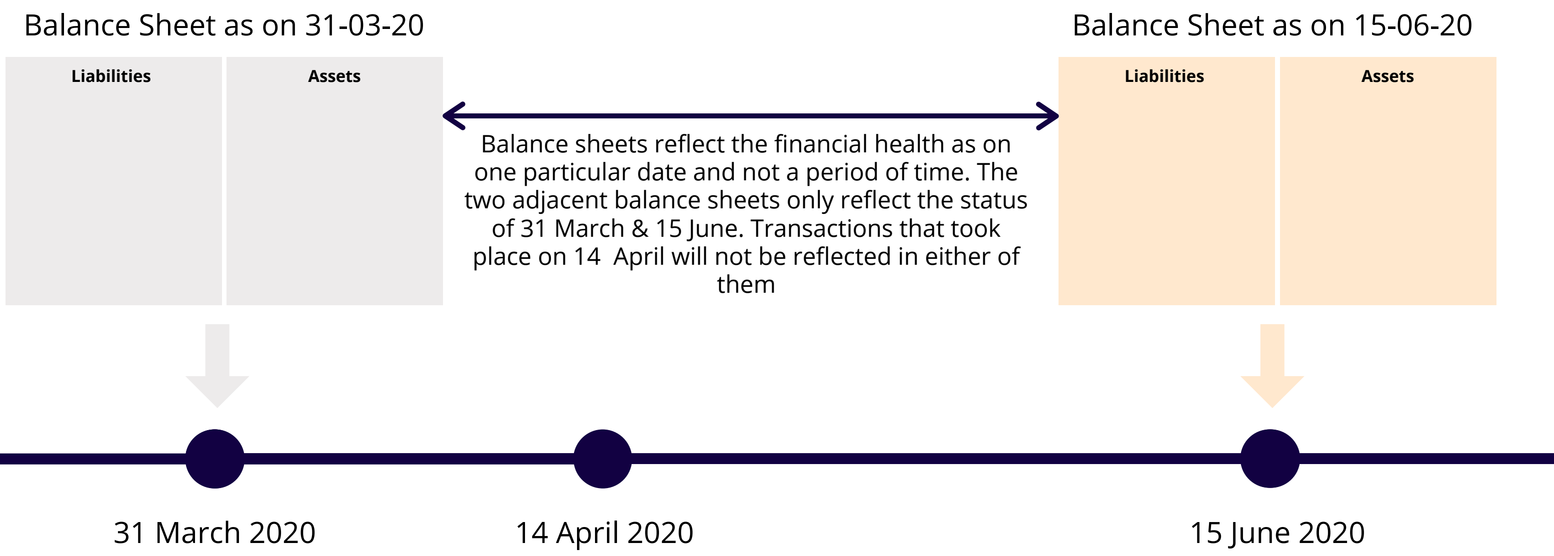
Assets

CAR VALUE = 5,00,000

3 CREATED 'AS ON DATE'

Whenever creating balance sheets, we need to know that it is created as per the 'as-on' date. This means if we are creating a balance sheet on 31st March, we will write down all the assets and liabilities that we have on that very day. If we sell an asset on 1st April, that will in no manner impact the balance sheet created on 31st March.

So, we can create a balance sheet on any particular day i.e. 31st March, 6th May, 18th December and it will be based on what we own and owe on that particular day. Ideally, we will be creating and updating our balance sheet every 6 months and comparing it to the previous ones.



4 CONTINGENT ITEMS

Contingent items are those assets and liabilities that materialize based on the occurrence of a future event i.e. it is conditional or reliant on a future event. So, currently, we are not sure whether we have the asset/liability or not. In such a situation, while listing the balance sheet items, we need to question whether it should be counted or not.

We have two categories under contingent items i.e. contingent assets and contingent liabilities. Let us decode these, one at a time.

ASSETS

Contingent assets are those assets whose possession we are unsure of. Some external factors are likely to influence this. For instance, many families have inheritance disputes, or we could also have a dispute with the government for a land piece or a dispute with a business partner. All these disputed assets, where ownership is not sure, are called contingent assets. We will assume that we are not going to get the contingent asset and list them below the balance sheet. If we do get it in the future, it will be treated as a surplus.

Liabilities	Assets

Contingent Assets

(a) ____________________

(b) ____________________

(c) ____________________

LIABILITIES

Contingent liabilities are those liabilities that we might or might not have to pay. These are again not in our control. Contingent liabilities are treated differently from assets. Here, we go ahead assuming that we will have to pay the liability. If the contingency works in our favor and we do not have to pay the liability, then that will be considered a surplus. So, we will list down the contingent liabilities within the balance sheet and not outside the balance sheet.

Liabilities	Assets
Contingent Liabilities (a) ________________ (b) ________________ (c) ________________	

We treat contingent assets and liabilities in this manner, due to an accounting concept called 'Conservatism'. We hope for the best but we prepare for the worst. We do not want our Lazy Financial Canvas to be ruined by a factor that is beyond our control. Hence, we assume we will not get any contingent assets and have to pay all liabilities. In reality, that is hardly ever the case, and our plan will be in better shape than we anticipated.

An important point to be kept in mind while determining the amount for contingency is to include only the disputed amount. Do not take the entire value of the asset/liability. Let's say, we have a property worth Rs. 50 lac under dispute and the net result will only value up to Rs.10 lac. Then we include Rs. 10 lac as contingent assets, while the rest can be counted as general assets. Consulting an expert will help us be more specific in this regard.

SEGMENTING ASSETS

Now that we have created our balance sheet, the next step is to segregate the assets in our balance sheet into 'Investible Portfolio' and 'Support Assets'. Let us first understand what they mean.

INVESTIBLE PORTFOLIO

Investible portfolio refers to the portion of the assets from the total that we are willing to sell off and relocate to other asset classes, as required by our Lazy Financial Plan to meet our financial goals. Assets held over here are from a returns perspective rather than their utility. For example, we own a house and we live there with no intention to sell it off even for meeting our financial goal; hence, this does not go under our investible portfolio. On the other hand, if we own some gold, we are willing to sell it off to meet our financial goals, then it will come under our investible portfolio. Or maybe, we own a second house that we have rented out. We are willing to sell off this particular property to meet our goals. That house goes in the investible portfolio.

SUPPORT ASSETS

All other assets that do not fall under the investible portfolio category, will automatically be categorized under the 'Support Assets'. These are assets that we are not willing to sell and relocate for our financial planning. These are the assets that serve a utility and we are not willing to look at them as a potential source of financial gain. For instance, we do not want to sell the house that you live in, to plan for finances, and as a result, it will fall under support assets. The assets occupied in our business will form support assets. (Moving forward, we will learn to deal with business assets)


Are you willing to sell off your asset to meet your financial goal?
Yes
No
Investible portfolio
Support assets

All assets compulsorily have to be listed under either ‘Investible Portfolio’ or ‘Support Assets’. Also, it is up to us to choose where we would want to place the assets and what would be the purpose of owning each of our assets. The assets that we are using or assets with emotional value will go under support assets and those that are from a financial return perspective will come under the ‘Investible Assets’ category. We will only use our ‘Investible Portfolio’ to create a financial plan. No matter how inefficient their financial return is, we will leave our support assets untouched. Our scheme is to meet all our goals using the investible portfolio exclusively.

‘Support Assets’ are called so as they act as our ‘support’ in case our financial plan fails and we have trouble achieving our financial goals with them. This segregation of assets is where most traditional books go wrong. They simply count all assets that we own to be the same. This segregation allows us to differentiate between assets that we own to get a financial return from those that we own for consumption.

RATIO OF INVESTIBLE PORTFOLIO TO SUPPORT ASSETS

The last thing to calculate in a personal balance sheet is the ratio of the investible portfolio to support assets. If the proportion of assets in the investible portfolio is very high, it indicates that we are placing a significant portion of what we own under investments and we have a very slim support asset base. However, the upside to this is that more assets will be put to the financially best asset class.
On the other end, if the ratio is too low, it shows that we have put very little under 'Investible Portfolio'. It reflects that a majority of our assets are put to use inefficiently and the chances of meeting all our goals have gone down to as little as invested.

Thus, it is very critical to find a ratio where we are not only comfortable with the 'Support Assets' that we have but also put enough in the investible portfolio to meet our goals. Balance is the key here.

Remember, no financial plan can ever be followed if we are not comfortable with the asset bifurcation. If it keeps us awake at night, the plan is not effective and will not last long. Moreover, we should be doing this bifurcation alone and within 10 minutes. The more time we give ourselves, the messier the thoughts are likely to become. And with this, we have finally created our personal balance sheet. Hurray! It's a great start. Next, we will learn to create a personal income statement.

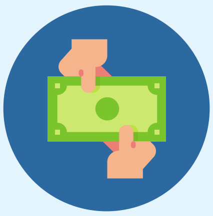
$$\textbf{RATIO} = \frac{\textbf{INVESTIBLE PORTFOLIO}}{\textbf{SUPPORT ASSETS}}$$

INCOME STATEMENT

Now that we understand a personal Balance Sheet and have created one, next we move on to creating a personal Income Statement. Just like our balance sheet, it is a list of all our assets and liabilities, Our income statement is a list of our earning sources and expenses.

To create an income statement, we begin with a list of all the sources of income that we have. Next, we will list down all our expenses. The balance figure that we have is the surplus or deficit. So, if the total of our earnings is greater than expenses, as it should be, we have a surplus and if our total of earnings is less than expenses, we are running a deficit. This surplus/deficit directly impacts our balance sheet. Soon we will also find out how the income statement and the balance sheet are interlinked with each other. The overall health of income statements over many years determines the health of our balance sheet as of today.

Income



SALARY INCOME

BUSINESS PROFITS

RENTAL INCOME

CAPITAL GAINS

DIVIDEND & INTEREST

Expenses

GROCERY BILL

UTILITY BILLS

RENT PAID

HEALTH & EDUCATION

ENTERTAINMENT

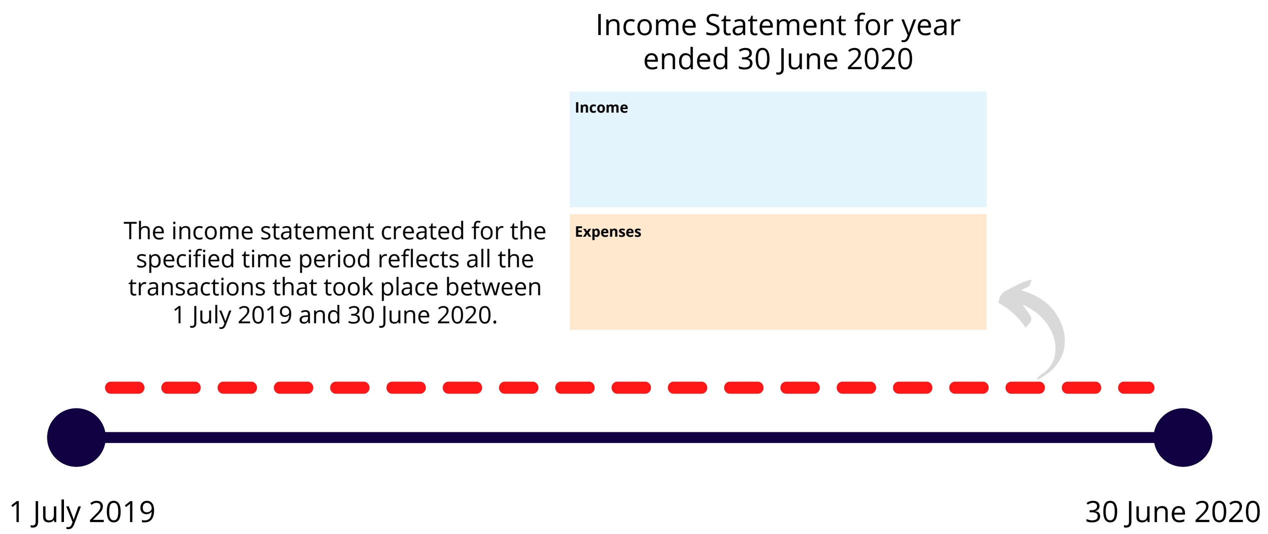
Surplus / Deficit

NITTY-GRITTIES OF CREATING INCOME STATEMENT

1

CREATED FOR A 'PERIOD OF TIME'

The income statement is created for a definite period of time. This means that when we come up with an annual income statement on say, the 30th of June 2020, every income or expense between 1st July 2019 and 30th June 2020 will affect the income statement. Remember, this is different from a balance sheet, as it is created for a 'point in time'. When creating a balance sheet, we only care about what we own and owe today. That's it. However, for an income statement, we care about all the transactions in a given time frame– whether it is annual, monthly or quarterly, or any number of days.



2

POST TAX ITEMS

Whenever we enter any income or expense in the income statement, we have to make sure to use the post-tax numbers. To calculate post-tax numbers, incomes should be taken after deducting the taxes and expenses, after adding taxes that are to paid. Notice the different signs used for post-tax income and expense.

POST TAX INCOME	POST TAX EXPENSE
= INCOME - TAX PAID	= EXPENSE + TAX PAID

3

DIFFERENCE BETWEEN INCOME & ASSETS; EXPENSES & LIABILITIES

When people are asked to create an income statement and a balance sheet, they confuse income for assets and expenses for liabilities. So, we need to be careful with our markings. Go through the definitions again and if the confusion still remains, feel free to drop us an email with the item y ou are struggling with.

ASSETS	LIABILITIES
Assets are what you own and can be sold to someone else in future.	Liabilities are what you owe and benefit is payable by you in the future.
INCOME	**EXPENSES**
Income is inflow that you get for the work you have done or asset that you own.	Expenses are what you pay or to be paid for benefits that you have already enjoyed.

4

MONTHLY OR ANNUAL INCOME STATEMENT

The last thing to consider is whether we should create an annual or monthly income statement. This decision depends on the flow of our income. If our income or salary is steady throughout the year, it is better to go for monthly income statement, as the human mind thinks best in monthly terms However, if our income and expenses are not regular but seasonal in nature, e.g. people who are engaged in businesses like textile , event management, or such other seasonal business, creating an annual income statement should be preferred. Creating a monthly plan would be very inefficient in such scenarios. Make a call on time horizon based on your comfort and circumstances.

5

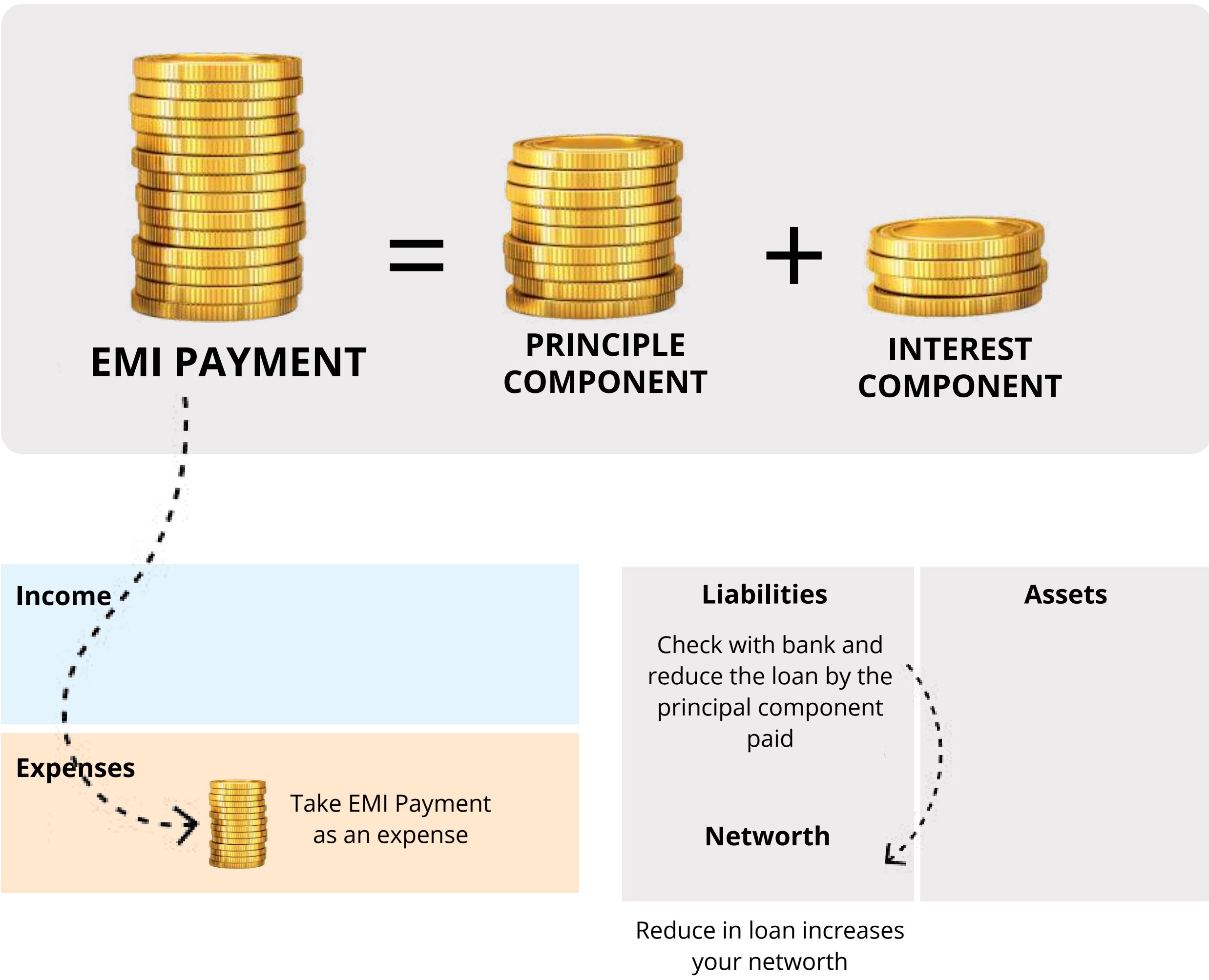
DEALING WITH EMI

To understand the concept of EMI, it is important to break it down. Every instalment paid in the form of an EMI comprises of two components – Principal Component and Interest Component.

The principal component is directed towards the loan repayment. The interest component is the amount that is the expense paid for borrowing the amount. With time, for every loan that we have taken, the proportion of the principal component in the EMI keeps increasing, while the interest component keeps decreasing. This complex math is created in a Loan Amortization Table. But we need not sweat our brains over it or worry since, that is to be done by the bankers and not us.

Technically, the interest component should come under the income statement and the principal component should reduce liabilities in the balance sheet. But we may not be able to estimate the amount of each component every month without a Loan Amortization Table as, it is a time consuming and technical process.

Let us try a simpler method. The entire EMI amount will be recorded as expense in the income statement for the entire year. At the end of the year, we will check the principal amount that we have repaid during the year with our bank, following which the liabilities will be reduced by that much amount. This will increase the networth. We follow this approach for its simplicity and an accounting expert will probably kill us for the same. But it can be surely said that the net result will be exactly same.



MERGING BUSINESS WITH PERSONAL PROFILE

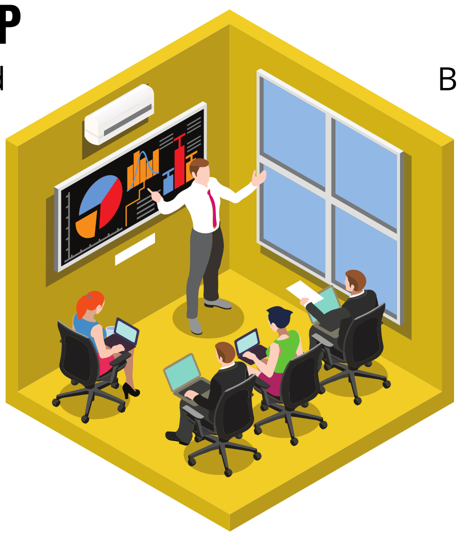
Now that we know how to create a balance sheet and an income statement, there is one special case, concerning business owners, that is to be considered. How should the business owners deal with their business assets while creating their profile? Businesses fall under either of the three categories – Sole Proprietorship, Partnership and Company. NGOs and all other institutions can also be treated as companies.

SOLE PROPRIETORSHIP

100% business is owned and operated an individual

PARTNERSHIP

Business is owned and operated by 2 or more partners



COMPANY

The business has various shareholders. One may hold a percentage of shares in the company

SOLE PROPRIETORSHIP

Here, we own 100% of the firm and all the firm's assets and liabilities are our responsibility. In such scenarios, we include all assets and liabilities in our personal balance sheet. However, know that these should all be categorized under 'Support Assets' and not 'Investible Portfolio'. For the income statement, we will include the business net profit after taxes as income in our personal income statement. Sales and expenses are not to be treated individually.

BUSINESS BALANCE SHEET

Liabilities	Assets
Loans of INR 20,000	Assets of INR 80,000

PERSONAL BALANCE SHEET

Liabilities	Assets
Loans of INR 20,000	Assets of INR 80,000

BUSINESS INCOME STATEMENT

Income	
Expenses	
Profit / Loss	INR 50,000

PERSONAL INCOME STATEMENT

Income	Business Profits of INR 50,000
Expenses	
Profit / Loss	

PARTNERSHIP

In a partnership firm, we own a particular percentage of the business, say 25%, 33%, 50% and so on. The treatment is same as that of sole-proprietorship, except the fact that we need to multiply the numbers by our percentage of partnership. If we are a 50% partner, we will add 50% of business assets in our personal balance sheet, 50% of liabilities and 50% of net profits in our balance sheet and income statement respectively. Even if the firm does not distribute the entire profit and re-invests, we will still count our entire share of net profits in the personal income statement.

BUSINESS BALANCE SHEET

50% PARTNER-SHIP

Liabilities	Assets
Loans of INR 20,000	Assets of INR 80,000

PERSONAL BALANCE SHEET

Liabilities	Assets
Loans of INR 10,000	Assets of INR 40,000

BUSINESS INCOME STATEMENT

50% PARTNER-SHIP

Income

Expenses

Profit / Loss INR 50,000

PERSONAL INCOME STATEMENT

Income

Business Profits of INR 25,000

Expenses

Profit / Loss

(BUSINESS ITEM) × PARTNERSHIP % = (PERSONAL ITEM)

COMPANY

Dealing with a company is fairly simple. We would be getting a salary and might be getting some dividends. We are to add those two in the income statement. The profit or loss of the entire company does not matter. The stock ownership or ESOP ownership that we have, will be shown under assets in the personal Balance sheet. We can revalue them every six months or every year. Again, these would not be part of investible portfolio if we are not willing to sell them.

PERSONAL INCOME STATEMENT

Income

Salary from Company

Dividends from Company

Expenses

PERSONAL BALANCE SHEET

Liabilities	Assets
	Shares of Company

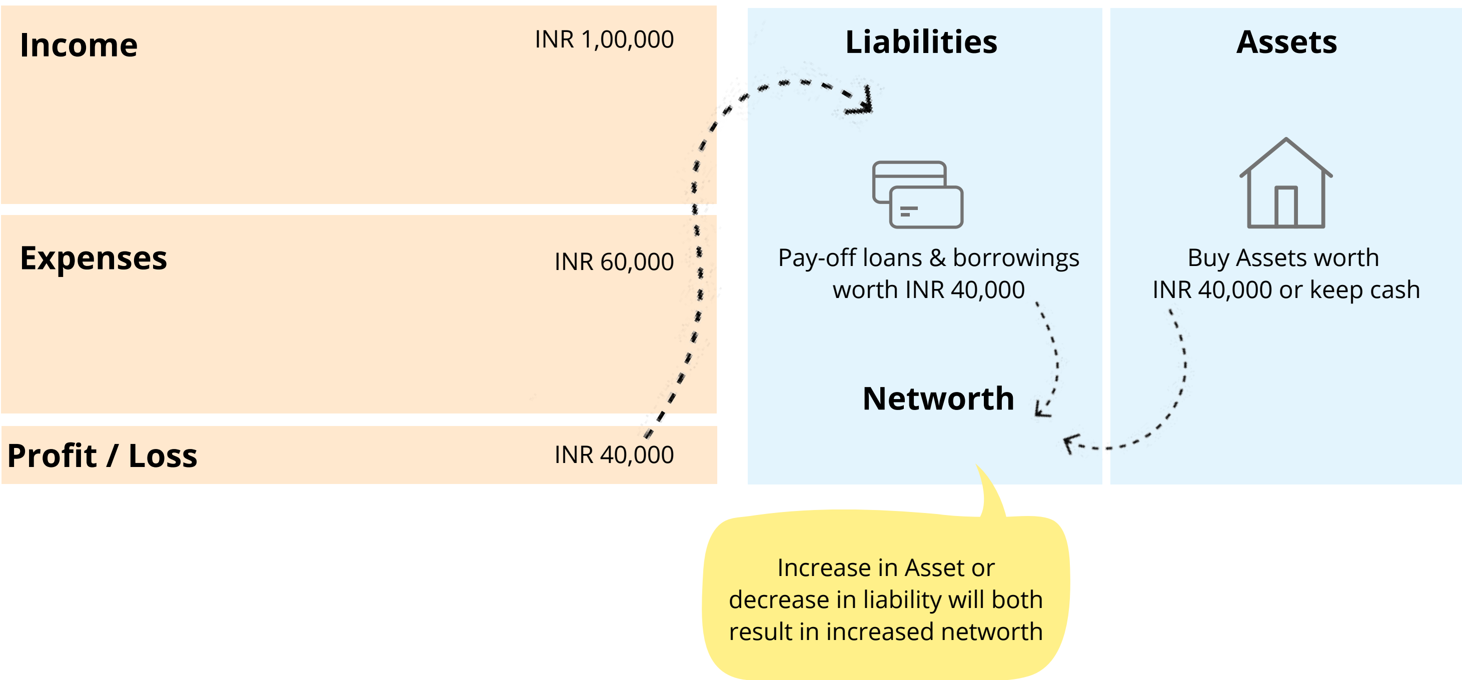
We now know how to create a personal income statement and balance sheet and also to deal with business assets and business liabilities. We can now go ahead and create it for ourselves. This will provide us with a very strong foundation for our lazy financial canvas. When the profile will be completed, the Lazy Plan will follow on its own.

CONNECTING INCOME STATEMENT & BALANCE SHEET

The next thing we need to acknowledge is the effect of changes in the income statement on the balance sheet. Let us say, we have earned Rs.1,00,000 in a month and spent Rs.60,000 out of it. That means we have a surplus of Rs. 40,000. What will we do with this money? We will possibly use it to either buy some asset, pay off a liability or else retain the same as cash which is again an asset. In all of the cases, either our assets go up or our liabilities go down. Both increase our net worth. So, greater the surplus, greater the net worth.

PERSONAL INCOME STATEMENT

PERSONAL BALANCE SHEET



Now let us assume we are in a deficit. We have spent more than our earnings. We will either sell off an asset to fund that or take an additional liability. In either case, our net worth goes down. This is how the income statement and balance sheet are related to each other. The fate of our income statement over many years ultimately will decide the structure of our personal balance sheet. Unravelling this link is crucial to know how our earnings and expenses affect our assets and liabilities.

SOLVENCY CHECK

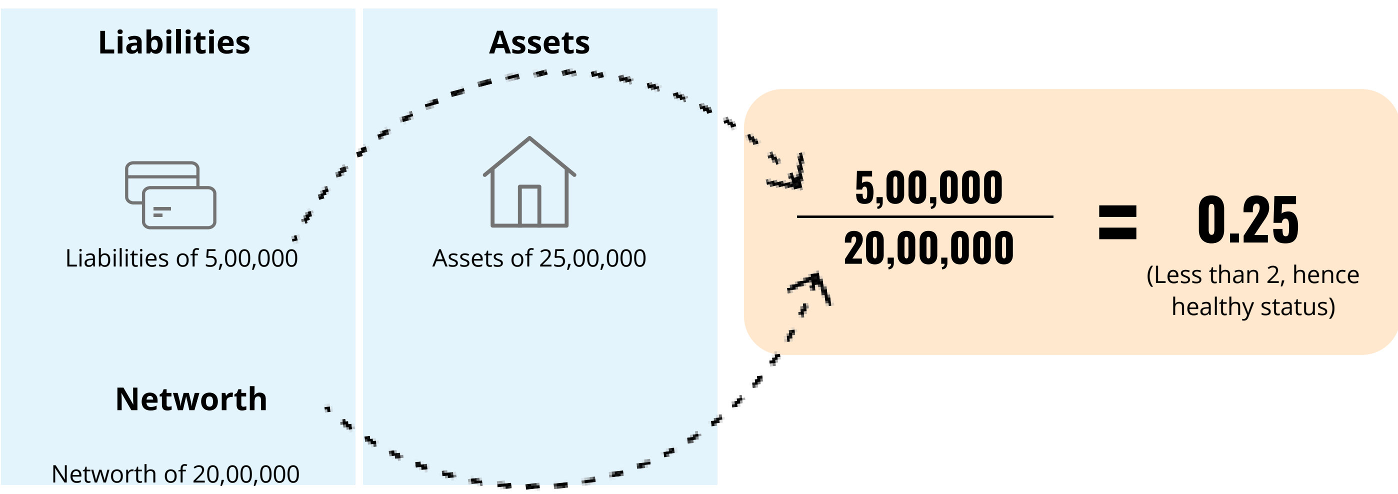
Before moving on to the lazy financial canvas, we need to quickly evaluate our financial position and analyze if we will be facing any risk of insolvency. This will not be the case for more than 95% of Zebra-learners but the rest must seek expert counsel right away, if they are facing any risk of insolvency. We will check two basic ratios for this.

LIABILITIES TO NET WORTH RATIO

Here, we divide the liabilities from our balance sheet by our net worth (assets – liabilities). This ratio explains which part of our assets is owned & which part is borrowed. For instance, if we have liabilities worth Rs. 5 lac, assets worth Rs. 25 lac and net worth equivalent to Rs. 20 lac, the liabilities to net worth ratio is 5 lac / 20 lac = 0.25. If this number is above 2, that means our balance sheet is not healthy and if it is more than 3, we should stop reading this immediately and visit an expert to help us get our finances in order.

$$\text{LIABILITY TO NET WORTH RATIO} = \frac{\text{TOTAL LIABILITIES}}{\text{NET WORTH}}$$

PERSONAL BALANCE SHEET



EMI COVERAGE RATIO

EMI Coverage Ratio= Surplus before EMI / EMI. 'Surplus before EMI' is the surplus/deficit from our income statement before paying any EMI. That means we need to add back the EMI to the surplus/deficit to get 'Surplus before EMI'. Divide this by EMI. This will give us our EMI coverage ratio which refers to the amount of extra cushion we have after paying our EMI. If this ratio is anything less than 1.25, we need to visit a financial expert right away.

$$\text{EMI COVERAGE RATIO} = \frac{\text{SURPLUS BEFORE EMI}}{\text{EMI}}$$

PERSONAL INCOME STATEMENT

Income	INR 10,00,000
Expenses	INR 5,00,000
EMI	INR 1,00,000
Surplus	INR 4,00,000

Denotes the surplus amount before paying any EMI

$$\text{EMI + SURPLUS} = \text{SURPLUS BEFORE EMI}$$

$$1{,}00{,}000 + 4{,}00{,}000 = 5{,}00{,}000$$

EMI Coverage Ratio

$$\frac{5{,}00{,}000}{1{,}00{,}000} = 5$$

(More than 1.25, hence healthy status)

STAGES OF LIFE

In terms of finance, every person's life can be divided into 7 stages. Each stage features different financial characteristics and a different approach to handling it. We need to recognize where we fall currently and create the lazy canvas accordingly. These stages and cycle is discussed by the CFA Institute as well and is followed by experts across the globe.

EDUCATION

Education is the phase of our life where our focus is on learning rather than earning. We are financially dependent on either our family or borrowed money. The objective at this stage is to build a solid base on which we can build our career. This phase lasts till we start working at our first full-time job. For some, it can end at age 15, while for others it may go on till the age of 25. In most cases, we will not even know our financial goals.

EARLY CAREER

This phase constitutes the first 3-4 years of work life. Here again, we are just getting started and perhaps getting paid very low, maybe just enough to pay off our bills. It is during this time that our family starts expecting some sense of financial performance from us. However, we are just getting started and primarily focused on investing in anything that can make us more valuable and can increase our cash inflow.

CAREER ADVANCEMENT

Our career has just begun to take off in this stage of life and our pay is increasing, we are getting promotions, we are buying big properties like a house, maybe a car, etc. By this stage, we would also have increased responsibilities, our parents are approaching retirement, we have a family of our own, we have bills to pay off and we have to start saving to meet our financial goals. Our financial goals have started to gain more clarity. We have enough surplus to start investing as well.

PEAK ACCUMULATION

By now, we have established ourselves in the concerned industry and we are at the peak of our earnings. We are now a seasoned professional, have the energy to do things and we have acquired the senior positions in our field of work. By now, our parents have retired, our family expenses are increasing and we would have major expenses approaching. We earn enough to save money even after paying all our bills. In this stage, contributions to our savings are the greatest.

PRE-RETIREMENT

The next phase of our life is just before our retirement and we are gearing up for the same. Age has started to take a toll on us, we are not taking on new projects and our home loans have been repaid. Our children have grown up and probably started working. By now, we have met most of your financial goals and are looking forward to being prepared for life after retirement.

EARLY RETIREMENT

This stage starts just as we retire. We find ourselves with a lot of time and energy. Our salary has stopped coming in, but our retirement plan or pension pays for our expenses. Few people also depend on their children for their expenses. Our expenses have also gone down and most of our financial goals have been met.

LATE RETIREMENT

This is the last phase of financial lifecycle. Now, we have been retired for a few years and have started using up the money saved for retirement. Our medical bills are increasing at a fast pace and our health falters for the majority of the year.

So,

this is how a typical financial life cycle for a person goes like. We need to identify which stage of life we are at and approach our finances accordingly. For instance, initially, we will focus on learning and investing in ourselves. Going forward, we will invest from a financial goal perspective. Later in life, we will focus on retirement planning and also our family's well being.

We need to keep in mind that there is no well-defined or fixed template based on age. Some people may end education at 28, some at 21, some might never go to school and start working at 14 itself. For others, they might switch career and go back in their early career stage in the mid-30s. Also, the transition from one stage to another may take few years. So this is a subjective and individual activity with no right answers.

METHODS OF SAVING

01
RANDOM METHOD

This method refers to randomly made investments with no fixed patterns. Whenever we find ourselves with extra money, we will buy some assets. This is the method used by most people and this is a very inefficient method to plan our finances.

02
ABSOLUTE METHOD

Here, we decide a particular amount that we will save/invest every month (say Rs. 20,000 per month). Even if our salary increases, we are stuck at investing that amount per month. We do not increase or decrease the amount based on activities.

METHODS OF SAVINGS

03
PERCENTAGE OF SALARY METHOD

We save a percentage of our income (say 20% of income). If the income increases, the savings will increase in the same proportion. This method does not bother to consider financial goals and the desired outcomes. Hence, it exposes us to a risk of shortfall.

04
GOAL ORIENTED METHOD

We have to identify our financial goals, asset classes and expected returns and reverse engineer to decide our saving pattern to meet the goals. This method is used by the least number of people.

The goal-oriented approach is the most effective of all saving techniques as it takes into consideration the end goals that need to be achieved. It also builds a sense of discipline and consistency. As of now, we are to identify which method to use. Going forward, with the Lazy Financial Plan, we will use the goal-oriented method. We might take some time to get comfortable with it, but once we have done that, it will give the maximum results. With this, we end our first phase of profiling.

02

'RRTTLLU' MODEL

RRTTLLU principle is something that is covered extensively by the CFA Institute in their exams. They use the system to create an IPS – Invesntment Policy Statement which is an individual's profile of financial circumstances. It is used by experts across the globe and is used to understand an individual's financial situation in leading investment firms such as Vanguard Assets managers (Manages 30 million investors globally), Seeking Alpha (Largest Investing community in the world), Peak Capital and many more. It is an established model, tried and tested over multiple years and produces tailor made investment plans. RRTTLLU principle is nothing but a fancy acronym for a list of factors using which a person's financial profile. We will evaluate ourselves on these factors.

RETURN GOALS

Let us talk about our future financial goals and the return that we intend to achieve to meet those goals. So we can contemplate over the reason for learning personal financial planning, for investing money and for profiling ourselves. The answer remains the same and that being, we all have some goals that we want to achieve in our lives. By goals, we are here referring to financial goals. For instance, we might want a good education, which is a personal goal. But being able to pay for that education is a financial goal that we intend to achieve.

RETURN GOALS

In the first element of RRTTLU, return goals, we deal with all the financial goals that we intend to achieve with the Lazy Financial Plan. So, all we need to do is list down every single of our financial goals over here, no matter big or small, high or low on priority, short term, long term, urgent or not.

We have to stop ourselves from getting all aspirational here and list down matters that we are serious about. We might dream to own the biggest home in South Mumbai and that is great but we must be realistic with what we are most likely to do. If we outperform our requirements and we have spare resources, we can go ahead with all our dreams. But while identifying financial goals, be specific and realistic.

Our goals should have nothing to do with our age. We might be 19 and the sole earning member of our family and our goals are to be listed down accordingly.

Lastly, it has come to our notice that young people, especially below the age of 25 years lack the clarity of their financial goals and it is completely okay for the majority. They are still in their youth and have a lot of years to plan their finances. Therefore, refrain from trying to create dreams randomly and out of the blue. They have the high risk-taking ability and for now, 'growth' is to be considered as their goal; to invest in themselves and focus on the growth of whatever capital they have. Few years down the line, their financial goals will become much clearer and they will have the time to plan for them. At this stage, do not stress a lot about financial goals.

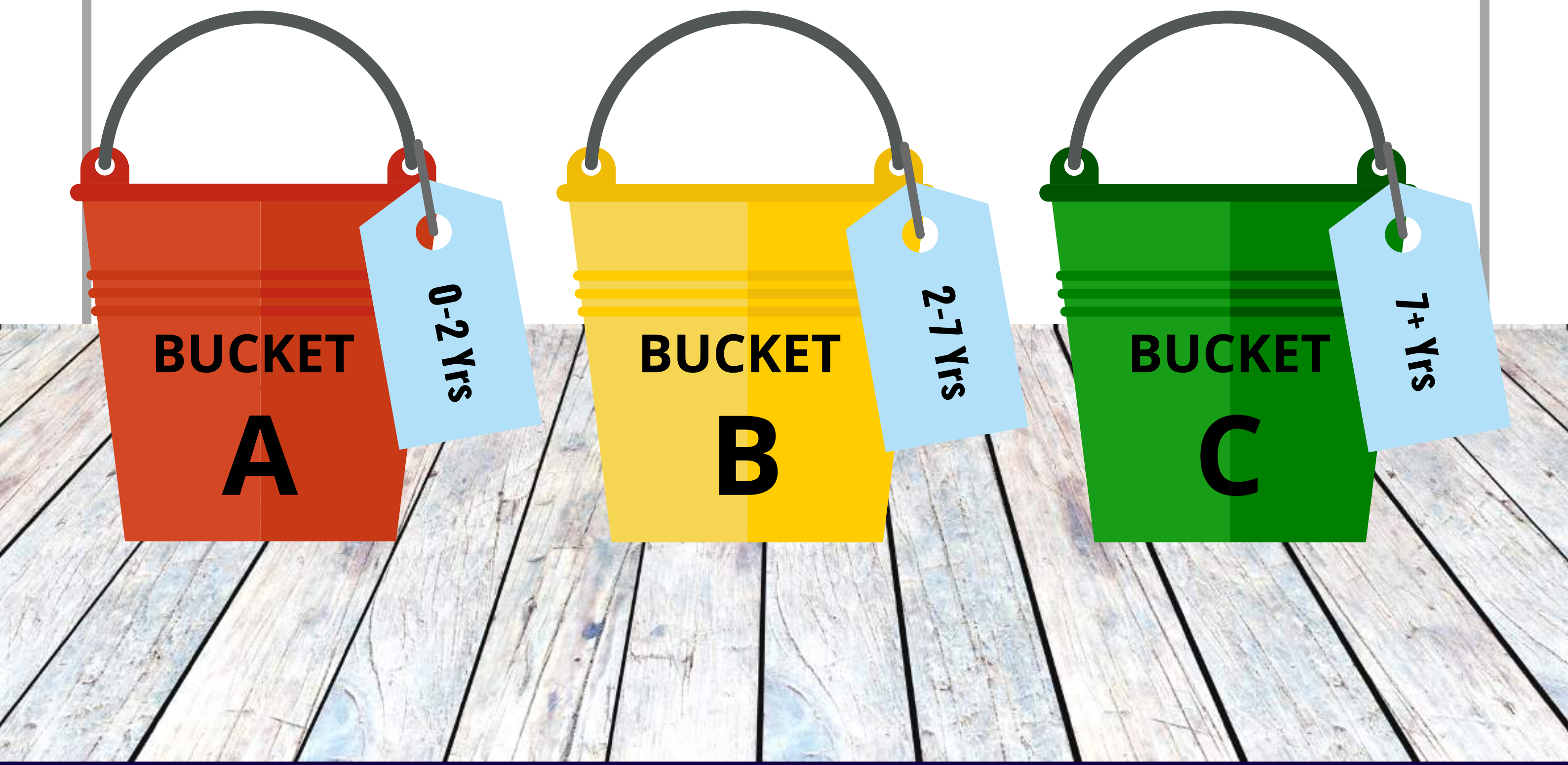
QUANTIFYING GOALS

Once we have all our financial goals, both short term as well as long term, listed in one place, we are to now quantify each of them. We do so in terms of time and money and ask the following questions:

- How much money do we need to meet the goal?
- How many years do we have to meet the goal?

We will try to make the best estimate that we can. Once we have done so, we will divide the goals into three buckets –

- **Bucket A** – Goals to be met in less than 2 years from today.
- **Bucket B** – Goals to be met in 2-7 years from today.
- **Bucket C** – Goals to be met in more than 7 years from today.

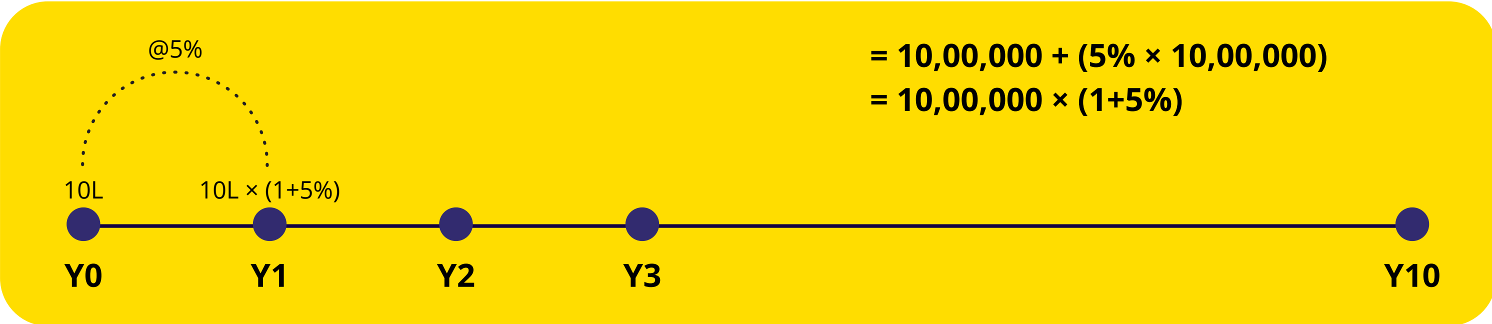


Let us now identify the amount that we would need for our goals. Goals in bucket A & B are relatively near term and therefore we will take the best estimate of the amount of money we will need for the same. We need to conduct preliminary tests of the market of the current prices and take the best estimate for the range of amount we might need. We will learn how to deal with ranges when we do not have a fixed answer, very shortly.

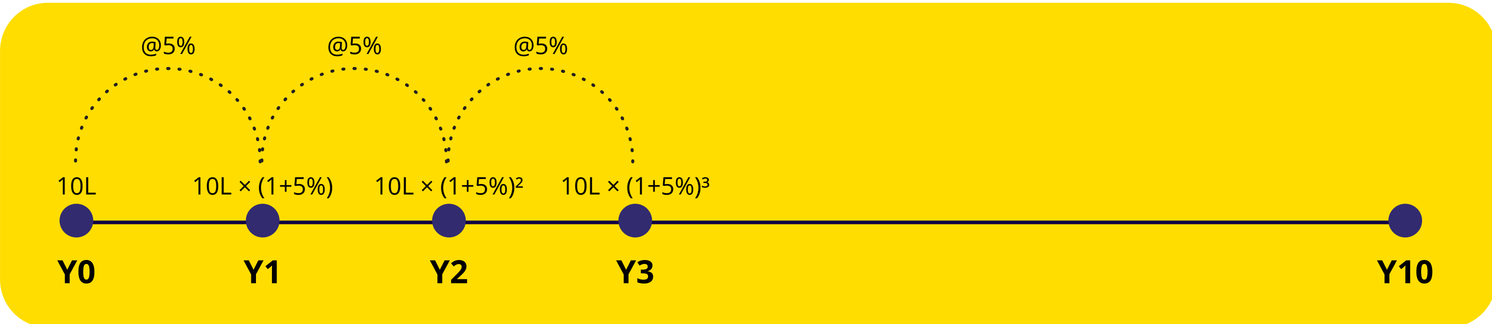
Calculating the amount for goals to be met in bucket C is not limited to a simple best estimate. In this scenario, we use a different method. For starters, we identify the current cost of our goal. We estimate the amount we would need if we were to meet the goal today. For instance, if we had to buy a house in 10 years from today, then how much would it cost now in real-time. Next, we take this and increase it at the current inflation rate. A simple Google search, ‘Current CPI Inflation in India’, will give us the number to be used as the inflation rate. Then use the formula:

Amount Needed in 'n' years = Current Value × (1+ CPI Inflation %)^n

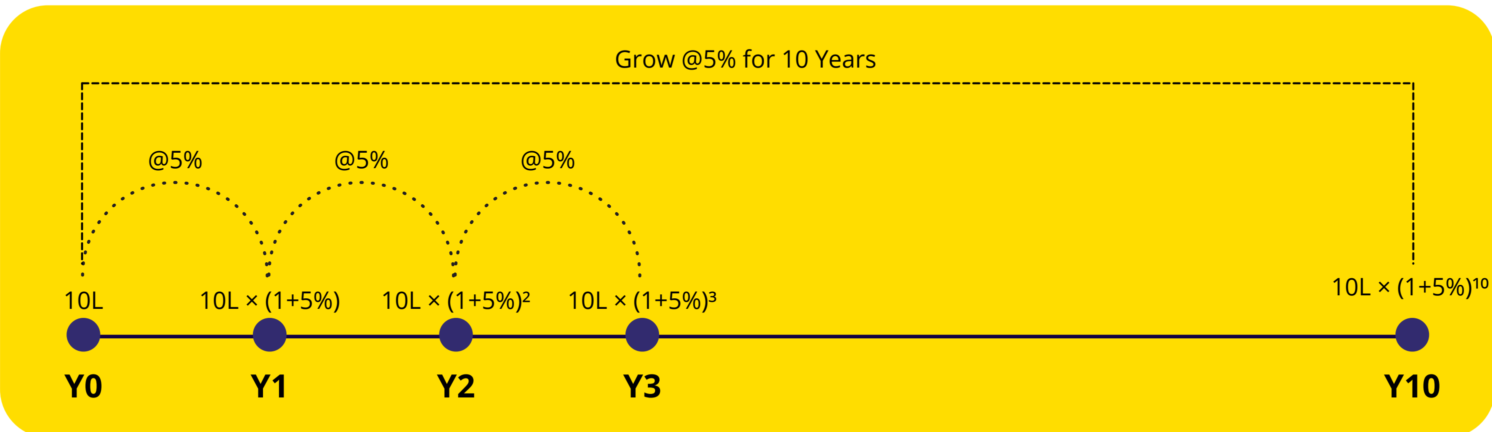
Let us take a quick detour and understand the above formula. It represents compounding. Let us assume we want to buy an asset after 10 years. The price today is Rs. 10 Lac. The inflation is 5%, so we need to grow this 10 Lac at the given rate for 10 years to find its value after 10 years. So at Year 0, the value is Rs 10 Lac. Now, at Year 1, we will grow the amount at 5%. That means we need to add 5% of Rs 10 Lac to the original amount.



We see that we multiplied the amount by 1+5% to grow it. Now, at Year 2, we need to grow it by 5% again. Hence, we will multiply the year 1 value with 1+5%. That gives us 10,00,000 × (1+5%) × (1+5%). This can also be represented as $10{,}00{,}000 \times (1+5\%)^2$. At Year 3, we will again multiply this with 1+5%. Then the value will become $10{,}00{,}000 \times (1+5\%)^3$.



We will continue this until we reach Year 10. There, the value will become $10{,}00{,}000 \times (1+5\%)^{10}$. We use a calculator to solve this, and we get 16,28,894 i.e. Rs 16 Lac. Here, we were growing an amount with the inflation rate. If we are investing in an asset, there we need to grow the amount by the rate of return. When we grow our salary, we will use the salary growth rate. So, the formula remains the same, the growth rate will take different forms.



FLEXIBILITY OF GOALS

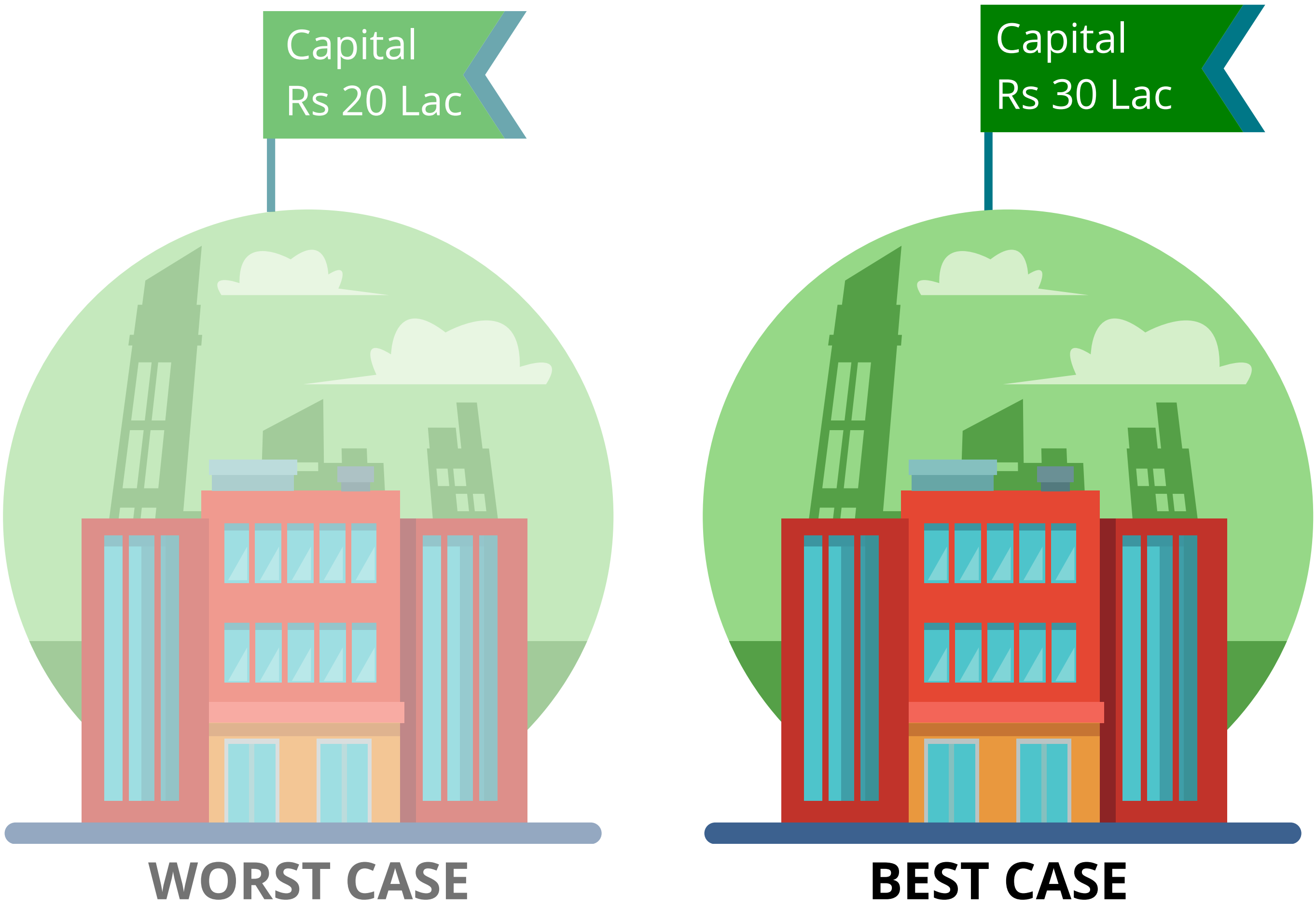
When we quantify the goals, we might face a situation where we cannot exactly determine the amount we will need or the time we have before we want to meet those goals or, we could just be flexible in terms of the amount or the time for our goal. It reflects that we are probably looking to buy a house in the next 5-7 years and we would need somewhere between Rs.50 lac and Rs. 65 lac to purchase it. The ranges used here show flexibility in terms of amount and time.

Using ranges is a solution to the lack of predictability and flexibility. The range has to be realistic and will swing from the worst-case scenario to the best-case scenario and everything in between.

TO BUY A HOUSE

For Rs. 50-65 Lac
In 5-7 Yrs

For example, we want to start a business and will need Rs. 30 lac in 2 years. But, worst comes to worst, we can even get started with Rs.20 lac. Now that we are flexible, we can use a range of Rs.20 lac to Rs. 30 lac when quantifying the goal. On the other hand, had we wanted to start a business, with the exact desired money, Rs. 30 lac, then the goal would not be a flexible one.



In either case, business can commence because the amount required to reach the goal is flexible

A question comes up – Why is judging flexibility even important? Flexibility is important to evaluate how flexible we are with our goals as rigid goals reduce our risk-taking ability whereas flexible goals allow us more freedom to take higher risks.

IMPORTANCE AND PRIORITY

The next step is to prioritize the goals. While listing down financial goals, we will list down a few that are the most important and absolutely 'must be met' as well as others that are 'good to meet' and we would like it if they are met. But the hard truth is, with limited resources, we must first allocate the resources to the most important ones and then use the rest to meet goals that are relatively low on priority.

This step will require us to judge the importance of each goal using a rating system in the range of 1 to 5. This is a very subjective exercise. Importance of one goal can be the same as another as well. So, two financial goals can both have a rating of 4.5.
There are no right or wrong answers to this. Note that the priority of goals keeps on changing with time.

For example, in the given case, if Aisha is unable to meet all goals, she will take away resources from her family vacation and invest it in the high priority items. We need to have this done for all our goals and we will be done with setting up our financial goals. We have identified them, quantified them, judged their flexibility and also their importance.

Aisha is a 27-year-old interior designer working with an MNC. She lives with her parents and sister (21-yrs-old). Alongside is a list of her goals and the ratings assigned to each goal.

- Open design studio in 4 yrs — 3
- Save for father's healthcare — 5
- Buy a house after 8 years — 3
- Save for Euro-trip in 2-5 yrs — 1
- Save for sister's MBA — 4

For Aisha, saving for her father's healthcare expenses is the most important goal and is her highest priority. After planning for this, her next priority is to save for her sister's MBA. Thereafter, she gives equal priority to opening her design studio and buying a house. At the very end, she intends to plan a trip to Europe. This is the priority series based on which Aisha plans her finances. Now, if she is unable to meet all her goals, she will first focus on the high priority goals instead of saving for the Europe trip.

RETIREMENT PLANNING

A SPECIAL CASE

A special case that we will need to attend to while setting up goals is retirement planning. It is something that is present on everyone's list and is a little bit complicated to deal with due to multiple uncertainties and assumptions. People often prepare complicated models for retirement planning and also end up paying heavy commissions to experts to plan for their retirement. So, here we have a simplified approach for you.

Who should be concerned about retirement planning? Retirement planning starts hitting people first around the age of 40 when they are mid-way through their careers. For some, it can be earlier or even a little later. People below the age of 32-33, do not need to worry about it. They are supposed to focus on learning and career growth and not a lot about retirement planning and all such things. This is probably their parents' time to retire and they have a lot of time.

When dealing with retirement planning, the difficult part is about quantifying the goals in terms of time and money. This is quite challenging since the number of years involved is very high. We will assume that we intend to retire at the age of 60. If we work longer, that only improves the efficiency of the plan. So, even if we intend to retire at 70, we begin with planning initially as If we will retire at 60. This is however the age for the majority to retire. So, the time horizon can be calculated as years left to reach the age of 60.

To answer this question, we observed that there are numerous models on the internet and by financial planning experts that are present and most of them over-simplify or over-complicate Retirement Plans. Few of them are effective whereas others are not. However, the most efficient structure has been discussed by Mrs. Monika Halan in her book – Lets Talk Money. She has used three methods and these are among the best methods for most of us to follow. We will use either of the three methods and we shall do great. We do not want to involve ourselves in complicated models. The three methods are disccussed as followings

It is time we ask ourselves, “How much do we need?” To calculate this, we use either of the three methods, instead of getting caught up in complicated models.

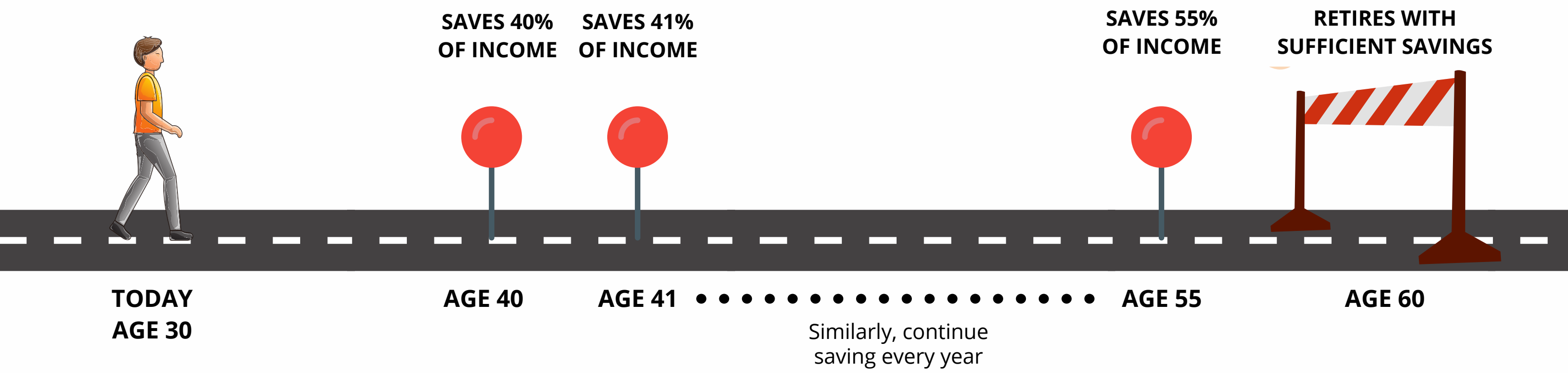
PERCENTAGE SAVINGS METHOD

RULE OF THUMB METHOD

SAVING SUFFICIENCY METHOD

PERCENTAGE SAVINGS METHOD

This is suitable for people around the age of 40 who have just started saving for retirement. We save the age % of our salary till the time we are 60. This means when we are 40, we save 40% of post-tax income towards retirement. Similarly, at 41, save 41% of income, at 42, save 42% of income and so on. We need to keep doing this till we are 60 and we will have a corpus big enough to sustain our lifestyle post-retirement. The math behind this is not within the scope of our discussion, but it works fine to meet our retirement needs.



RULE OF THUMB METHOD

Rule of thumb helps us calculate the sum of money we need at retirement. It comprises of two methods: income multiplier and expense multiplier. According to the income multiplier rule, 10 times of our final year post-tax salary shall be the amount needed. The expense multiplier rule states that 24-30 times of our final year expense shall be the required amount. These are extremely conservative numbers which will assure us that our retirement needs are met on time.

INCOME MULTIPLIER

$= 10 \times$ Last working year salary

$= 10 \times$ [current salary $\times$ (1+annual % increase in salary)^n]

where, n = number of years to retirement

EXPENSE MULTIPLIER

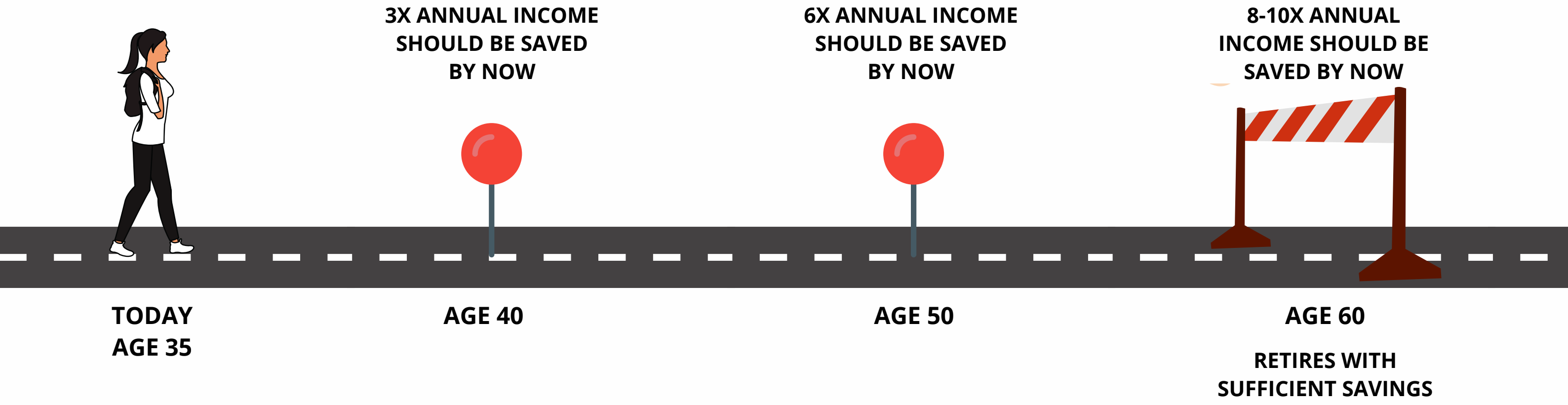
$= 24 \times$ Last working year expense

$= 24 \times$ [Current annual expense $\times$ (1+ CPI Inflation %)^n]

where, n = number of years to retirement

SAVING SUFFICIENCY METHOD

In this method, we do not estimate the amount that we will need. Once again, we use a litmus test to evaluate if our current savings towards retirement planning is enough to meet our goal of retirement or not. So, the objective here is– at 40 we should have 3 times our annual income saved towards retirement, at 50, we should have 6 times our then annual income and at 60, 8-10 times. Notice that our income will also increase over the years, so we should have the multiple of the salary then which means, 3 times of salary at 40, then, 6 times of salary at 50 and so on. This is a relatively simple method, suitable for people who have started planning for retirement quite early in life. This can mostly be the case for stable job owners. This is very difficult for those running their businesses.



Now that we have discussed the 3 methods that can be used to evaluate retirement needs, we can use any of them, whichever makes us comfortable. Please note that each of the methods can give varying numbers. So, what we can do is, select any method and whichever gives us the lowest number, we can follow that. The bottom line is- all three methods work.

Mr. Kishore, 40 years old, is a factory head at Just Eat Ltd, a large cake brand. He has been working here for the last 15 years. His current salary is Rs. 7 lac p.a. However after paying taxes, he gets Rs.6 lac. He expects an annual increase in salary by 5%. He plans to retire at the age of 60 and wants to plan for the same. Let us see how he can plan using the 3 methods we have discussed.

1.PERCENTAGE SAVINGS METHOD

In the given case, Mr Kishore has an annual salary of Rs. 6 lac at the age of 40. As per the percentage savings method, he will save 40 % of his income i.e, Rs. 2,40,000. He will invest this amount for 20 years. Let us assume that the rate of return is 12% p.a. So this amount will grow to Rs. 23,15,110. To get this, we will simply use the compounding formula and grow Rs. 2,40,000 at 12% for 20 years.

At the age of 41, his salary will be Rs. 6,30,000 due to the annual increment @ 5%. As per the method, he will save 41% of Rs. 6,30,000 i.e. Rs. 2,58,300. He will invest this amount @ 12% p.a for 19 years to grow the amount to Rs. 22,24,676. This process will continue annually until he reaches 60 years of age. Ultimately, all the amounts invested for all these 20 years will accumulate to give a sum equal to Rs.3,27,83,871 at the age of 60. Given below is the calculation for each year.

Mr kishore starts investing at age 40 until age of 60 to accumulate his retirement corpus

This column represents the absolute amount of savings made at that particular age

Age	Salary	Savings %	Savings	Invst. at Age 60
40	6,00,000	40%	2,40,000	23,15,110
41	6,30,000	41%	2,58,300	22,24,676
42	6,61,500	42%	2,77,830	21,36,503
43	6,94,575	43%	2,98,667	20,50,662
44	7,29,304	44%	3,20,894	19,67,204
45	7,65,769	45%	3,44,596	18,86,169
46	8,04,057	46%	3,69,866	18,07,579
47	8,44,260	47%	3,96,802	17,31,444
48	8,86,473	48%	4,25,507	16,57,766
49	9,30,797	49%	4,56,090	15,86,534
50	9,77,337	50%	4,88,668	15,17,730
51	10,26,204	51%	5,23,364	14,51,329
52	10,77,514	52%	5,60,307	13,87,300
53	11,31,389	53%	5,99,636	13,25,605
54	11,87,959	54%	6,41,498	12,66,203
55	12,47,357	55%	6,86,046	12,09,048
56	13,09,725	56%	7,33,446	11,54,091
57	13,75,211	57%	7,83,870	11,01,281
58	14,43,972	58%	8,37,503	10,50,564
59	15,16,170	59%	8,94,540	10,01,885
60	15,91,979	60%	9,55,187	9,55,187
TOTAL			1,10,92,620	3,27,83,871

Salary increases at 5% every years!

Savings percentage corresponds to the age. Eg. At age 45, he saves 45% of his earnings

This column represents the final investment amount he has at age 60, from each year's investment. Assume that savings were invested at 12%.

For example, at age 50, he invested Rs. 4.9 Lac in various assets. This amount will keep growing for 10 years, until he turns 60. So the total amount that he has at age 60, will be much more than 4.9 lakh.

Age	Salary	Savings %	Savings	Invst. at Age 60
40	6,00,000	40%	2,40,000	23,15,110
41	6,30,000	41%	2,58,300	22,24,676
42	6,61,500	42%	2,77,830	21,36,503
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TOTAL			1,10,92,620	3,27,83,871

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60	15,91,979	60%	9,55,187	9,55,187
TOTAL			1,10,92,620	3,27,83,871

He invested Rs.4.9 lac for 10 years, until he turns 60. At age 60, that amount would have grown to become Rs. 15.2 lac. Use the compounding formula to calculate this amount. Rs. 4.9 lac compounded at 12% for 10 years (60-50)

=> $4{,}88{,}668 \times (1+12\%)^{10} = 15{,}17{,}730$

Age	Salary	Savings %	Savings	Invst. at Age 60
40	6,00,000	40%	2,40,000	23,15,110
41	6,30,000	41%	2,58,300	22,24,676
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59	15,16,170	59%	8,94,540	10,01,885
60	15,91,979	60%	9,55,187	9,55,187
TOTAL			1,10,92,620	3,27,83,871

Similarly, at age 55, he invested Rs 6.9 lac out of his salary. This amount grows to become Rs 12 Lac by the end of 5 years, i.e. at age 60. Use the same method. Rs 6.9 Lakh compounded for 5 years at 12%.

=> $6,86,046 \times (1+12\%)^5 = 12,09,048$

Age	Salary	Savings %	Savings	Invst. at Age 60
40	6,00,000	40%	2,40,000	23,15,110
41	6,30,000	41%	2,58,300	22,24,676
42	6,61,500	42%	2,77,830	21,36,503
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60	15,91,979	60%	9,55,187	9,55,187
TOTAL			1,10,92,620	3,27,83,871

Continuing this saving method, at age 60, he would have accumulated a total of Rs. 3.3 Crore

2. RULE OF THUMB METHOD

Age	Salary
40	6,00,000
41	6,30,000
42	6,61,500
43	6,94,575
44	7,29,304
45	7,65,769
46	8,04,057
47	8,44,260
48	8,86,473
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54	11,87,959
55	12,47,357
56	13,09,725
57	13,75,211
58	14,43,972
59	15,16,170
60	15,91,979
TOTAL	

This is from the previous calculation
You can also use compounding formula.
Compound Rs. 6 Lac at 5% for 20 years
=> $6,00,000 \times (1+5\%)^{20} = 15,91,979$

INCOME MULTIPLIER

Taking the case of Mr. Kishore and applying the rule of thumb method, under income multiplier approach, the last working year salary as shown in the table, after considering the annual increment for 20 years, is Rs. 15,91,979 rounded off to Rs. 16 lac. Multiplying this amount with the income multiplier 10, we get the amount required at retirement i.e. Rs.1 crore 60 lac (1,60,00,000).

= 10 × Last working year salary
= 10 × [current salary × (1+ % salary increase)^n]
where, n = number of years to retirement
= 10 × 16,00,000
= 1,60,00,000

EXPENSE MULTIPLIER

Under this approach, let us assume that Mr Kishore spends 60% of his income annually for meeting his expenses. So, his current year expense is Rs. 3,60,000 {60% of 6,00,000}. To find the last working year expense, we will multiply the CPI inflation rate @ 5% for 20 years, which will give us a sum of Rs. 9,55,187 rounded off to 10,00,000. Once we have the last working year expense, we will multiply it by the expense multiplier 24, i.e. Rs. 2 crore 40 lac (2,40,00,000). This is the amount required at the time.

= 24 × Last working year expense
= 24 × [Current expense × (1+ Inflation %)^n]
where, n = number of years to retirement
= 24 × [3,60,000 × (1+ 5%)^{20}]
= 24 × [10,00,000]
= 2,40,00,000

3.SAVING SUFFICIENCY METHOD

Under this method, Mr. Kishore should have saved 3 times his annual income by the age of 40. At the age of 50, he should have saved an amount equal to 6 times his annual income and by 60 years of age, he should have saved 8-10 times of his annual income. For simplicity of calculation, the amounts of annual income are rounded off. Given beside is the amount required at the time of retirement.`

Age	Salary
40	6,00,000
41	6,30,000
42	6,61,500
43	6,94,575
44	7,29,304
45	7,65,769
46	8,04,057
47	8,44,260
48	8,86,473
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52	10,77,514
53	11,31,389
54	11,87,959
55	12,47,357
56	13,09,725
57	13,75,211
58	14,43,972
59	15,16,170
60	15,91,979
TOTAL	

3 × 6,00,000 = 18,00,000

6 × 10,00,000 = 60,00,000

10 × 16,00,000 =1, 60,00,000

TIME HORIZON

The time element is relatively simple and can be created based on return goals that we have identified. We will use the quantified goals that we had listed earlier to create a timeline for ourselves the goal we would want to focus on financially and the time for the same. This will give us a comprehensive understanding of the Financial Timeline. We will develop a timeline accounting for all the major financial milestones and also personal milestones.

But first, why is time horizon so important? When we calculate the final output of our investments, three factors play a role i.e. the initial amount invested (Principal Amount), the rate of return and the number of years. Time horizon is one of the most important factors when it comes to judging the result of our investments.

$$\underbrace{A}_{\text{Amount}} = \underbrace{P}_{\text{Principal}}\,(1+\underbrace{r}_{\text{Interest Rate}})^{\overbrace{t}^{\text{Time}}}$$

Let us get started with a couple of exercises. First, we need to estimate the time to achieve each goal and their flexibility in terms of time. Well, we have learnt a lot about this in goal settings. We would have quantified each goal and estimated its flexibility. We see how each stage in profiling is inter-related with others and together they create the lazy canvas.

The time we have before we need to meet a particular and the degree of risk that we can take together determine what asset class we should invest in.

TODAY

We will understand taxes as a constraint when creating our Lazy Financial Plan. We will focus on making investments or creating a financial plan while keeping in mind the tax implications of our decisions. Hence, an asset that might be much more attractive than other assets might become less attractive after considering tax implications.

We will be looking into the various types of taxes, the way they are calculated, the important terms related to taxes and lastly, the exemptions and deductions in India that we can benefit from. We will also take into account the differences between the new tax regime (introduced in Budget 2020) and the old tax regime. Putting all these together shall help us with everything relevant to our lazy profile and Lazy Financial Plan.

WHAT ARE TAXES?

Taxes are what we pay to the government as rent for our citizenship. We use multiple government benefits, all public infrastructure and so on. Taxes are a means for the government to get the money to provide for such benefits.

DIRECT TAXES

It refers to that tax which is directly charged from your income or assets. This means whatever you earn in an year or whatever assets you have, the government charges a portion of it as taxes. Since it is directly charged from your income or assets, irrespective of how you intend to spend it, it is called direct taxes. Income Tax and Wealth tax are two examples of direct taxes.

INDIRECT TAXES

Indirect taxes are a bit different. They are charged at the time of consumption and not income. Whenever we buy a product or service, it has a tax component in it. In India, it has now been consolidated under GST (Goods and Services Tax). This tax is levied whenever we consume anything, irrespective of how much we earn or own.

Now let us review direct and indirect taxes from a financial planning perspective. There is not a lot that we can do about indirect taxes. However, direct taxes offer a lot of deductions and exemptions that we can take advantage of. So, going forward, we will only talk about direct taxes in our lazy financial canvas

INCOME TAX

Coming back to direct taxes, we saw that direct taxes are mainly of two types – Income Tax and Wealth Tax. In India, wealth taxes have been abolished. So our majority discussion will be about income taxes going forward. Lets get started with Income Taxes. Firstly, we need to understand two key terms and the difference between the two i.e. earned income and taxable income.

EARNED INCOME

Earned Income is the sum total of all the incomes that you have from all the sources combined. You got something from rental income, something from dividends, salary, interest income etc. All that we have earned in the year, irrespective of their tax treatments. Here, some income may be taxed, some may not be.

TAXABLE INCOME

Taxable Income refers to that part of earned income that is identified as income in the government's eyes. Income tax is calculated based on taxable income. Earned income after adjusting all the tax benefits (i.e. exemptions and deductions) is the taxable income.

EARNED INCOME	-	TAX BENEFITS	=	TAXABLE INCOME
All income that you have earned		Exemptions & Deductions i.e. generally reduce taxable income and tax burden		Amount at which tax rate is levied

For instance, dividends were not taxed in India till 2020. That meant, if you received dividends, it will be included in Earned Income but not included in Taxable Income. So, you do not need to pay taxes on dividends because it is not a part of the taxable income i.e. it is not an income in the government's eyes.

When dealing with financial plan relating to taxes, the net effect on Taxable Income is what we will focus on going forward. Also, note that currently in India, every individual has a choice to opt for either one of two tax regimes. The old tax regime that existed for years or the newer one that has been introduced in the budget for FY21. Know that these tax rates may change with each budget. A simple Google search on"Current Tax Slabs in India" will inform us regarding the same.

OLD TAX REGIME

GENERAL PUBLIC
(Below 60 Yrs of Age)

INCOME TAX SLAB	TAX
Upto INR 2.5 Lac	Nil
INR 2.5 - 5 Lac	5%
INR 5 - 10 Lac	20%
Above INR 10 Lac	30%

SENIOR CITIZENS
(60 to 80 Yrs of Age)

INCOME TAX SLAB	TAX
Upto INR 3 Lac	Nil
INR 3 - 5 Lac	5%
INR 5 - 10 Lac	20%
Above INR 10 Lac	30%

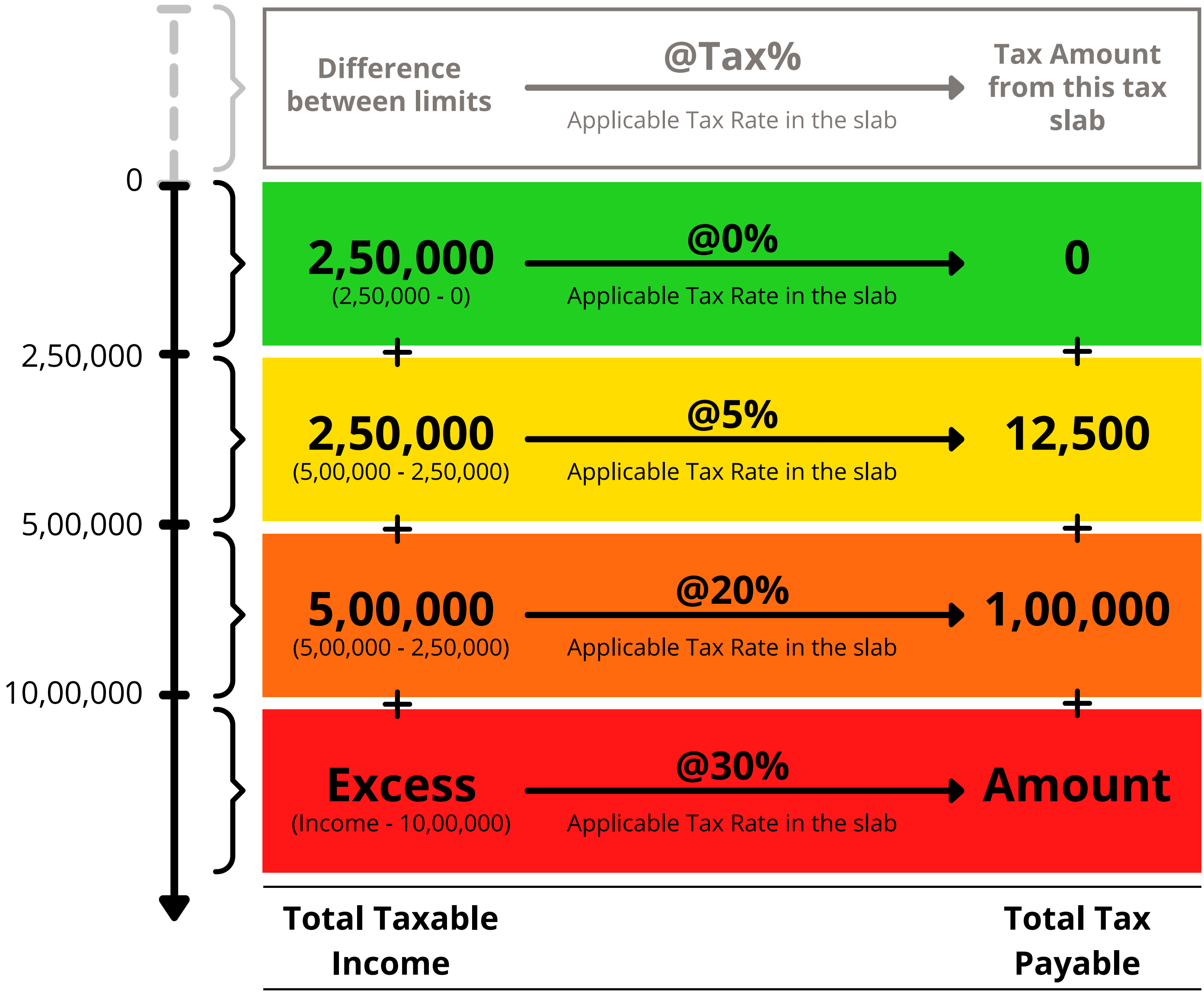
SURCHARGE

- 10% of the Income Tax, where taxable income is more than INR 50 Lacs but upto INR 1 Cr
- 15% of the Income Tax, where taxable income is more than INR 1 Cr

EDUCATION CESS

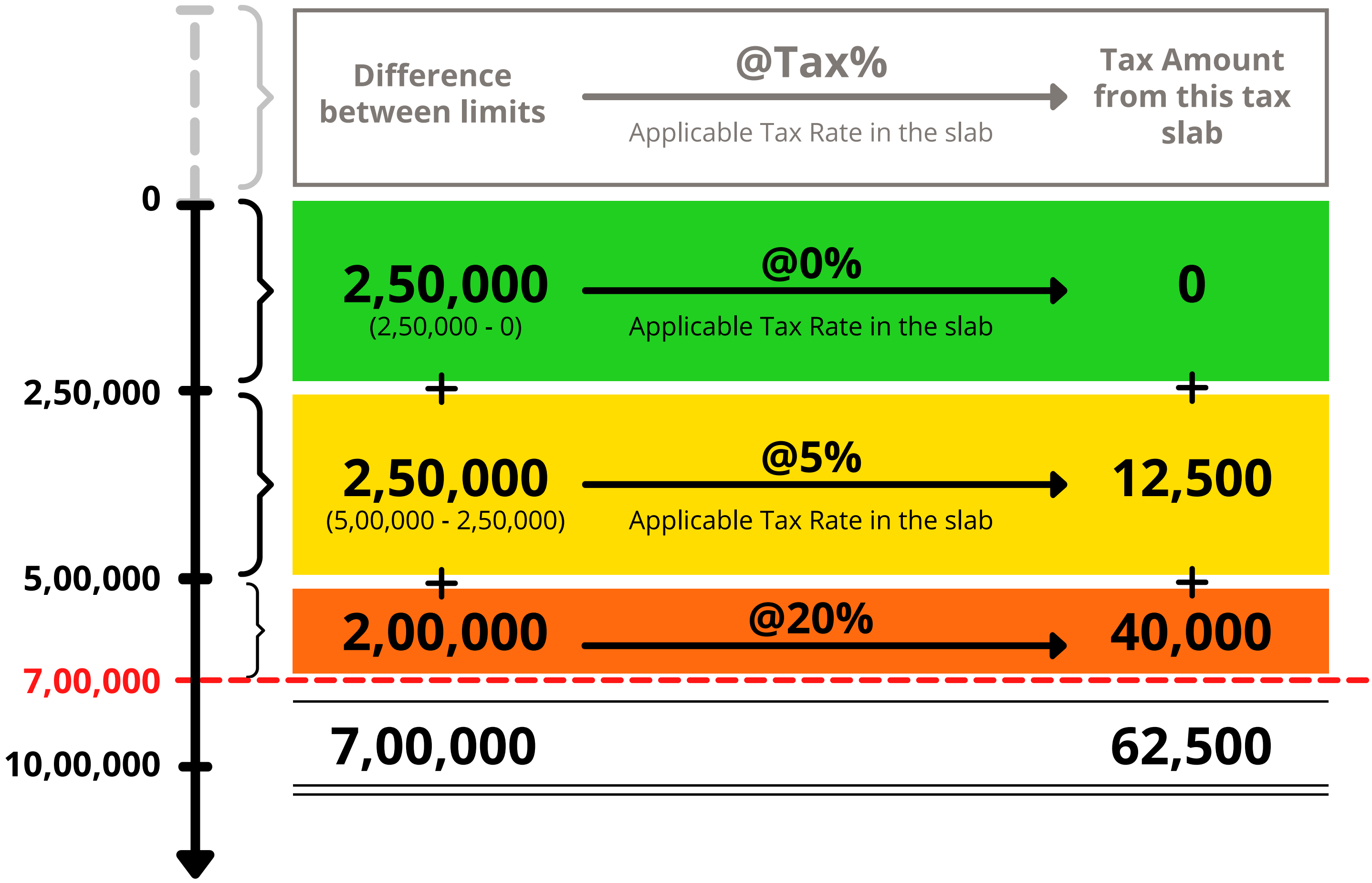
- 4% Health & Education Cess is applicable on income tax and applicable surcharge

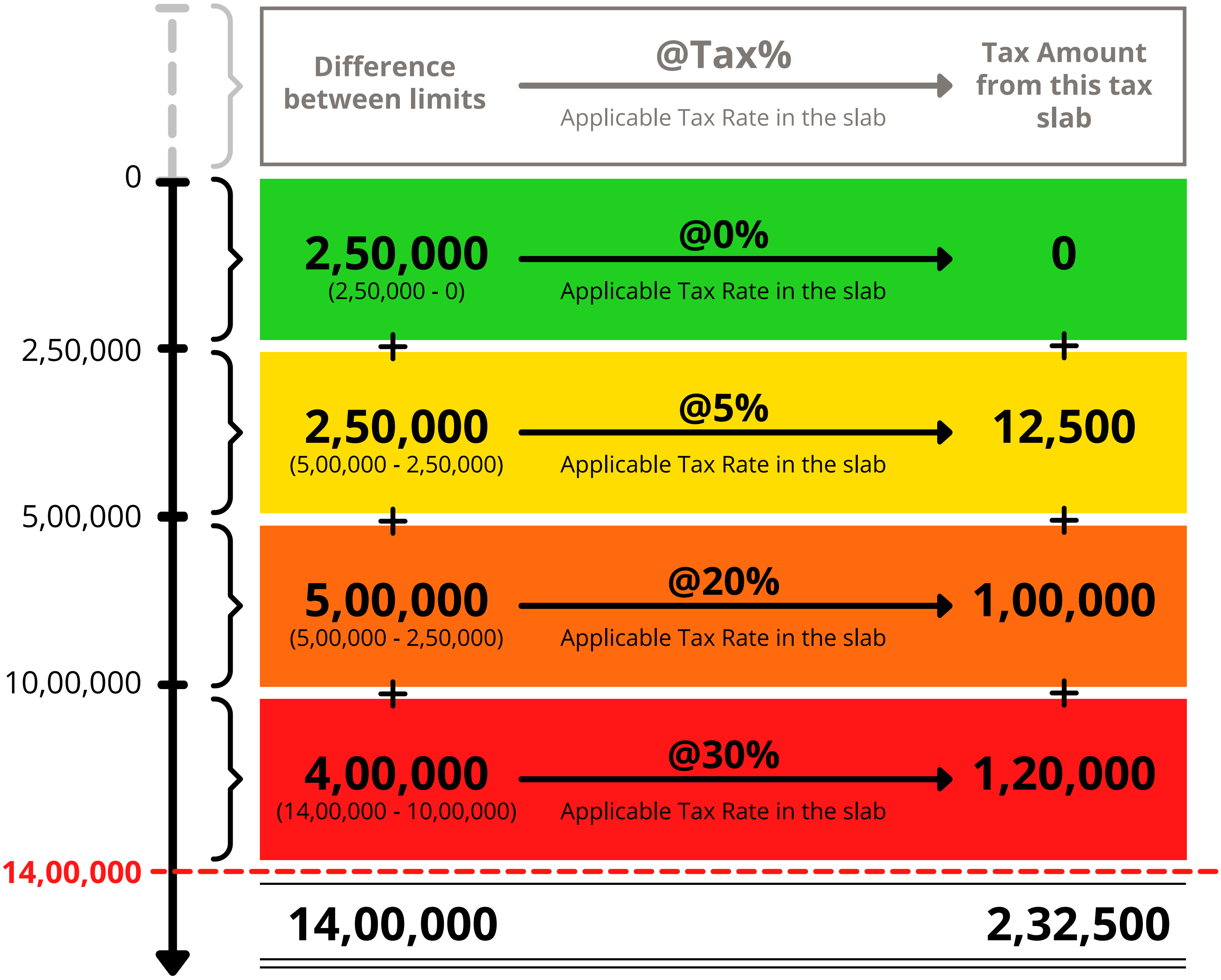
The rate at which we will be charged is based on the category under which our current taxable income falls (after all the deductions and exemptions). For the first Rs. 2.5 lac(first slab), we will pay 'nil' tax. Then, for the next Rs. 2.5 lac (2nd slab, Rs. 2.5 - 5 lac), we will pay tax at 5%. For the next Rs. 5 lac (3rd slab, Rs. 5 - 10 lac), we will pay tax at 20% and similarly, for anything exceeding Rs. 10 lac (4th slab), the tax will be paid at 30%.



So now, let us assume that our taxable income is Rs. 7 lac. We would think that we fall under the 3rd slab and have to pay tax at 20% on the entire Rs. 7 lac i.e. Rs. 1.4 lac. However, that is not how it works. In the sum of Rs. 7 lac, first Rs. 2.5 lac fall in the first slab, another Rs. 2.5 lac all in the second slab, and the rest of the Rs. 2 lac fall in the 3rd slab. Now the tax will be levied on this basis.

We have to pay 'nil' tax for the first slab; 5% of Rs. 2.5 lac i.e. Rs.12,500 in the second slab; and 20% for the rest Rs. 2 laci.e. Rs. 40,000. So, the total tax comes out to be (2,50,000 × 0%) + (2,50,000 × 5%) + (2,00,000 × 20%) = 0 + 12,500 + 40,000 = 62,500. Notice that, in a flat tax system, we were to pay Rs. 1.4 lac as taxes. While in the progressive tax system, we have to pay only Rs. 62,500. We need to add a cess of 4% after this.





Let us take another example. Let us assume that your taxable income is INR 14 Lacs. With a flat taxation system, you will fall in the 4th slab and you would have to pay 30% on the entire INR 14 Lac which comes out to be INR 4.2 Lacs.

However,under the progressive tax system, on the first Rs. 2.5 lac, we pay tax at 0%; on the second Rs. 2.5 lac, we pay tax at 5% i.e. Rs. 12,500; on the next Rs. 5 lac, we pay tax at 20% i.e. Rs. 1 lac; and finally on the last Rs. 4 lac we pay tax at 30% i.e. Rs. 1.2 lac. So now, the total tax comes out to be (2,50,000 × 0%) + (2,50,000 × 5%) + (5,00,000 × 20%) + (4,00,000 × 30%) = 0 + 12,500 + 1,00,000 + 1,20,000 = 2,32,500. Notice the difference between Rs. 4.2 lac and Rs. 2.3 lacs. Add cess after this.

Also, those with taxable income above a certain limit, have to pay additional surcharge and cess as shown above. This is how your income taxes are calculated based on what slab you fall into. The rates in the table are as per the older regime and focus shall be on taxable income and not earned income.

NEW TAX REGIME

FOR ALL INDIVIDUALS

INCOME TAX SLAB	TAX
Upto INR 2.5 Lac	Nil
INR 2.5 - 5 Lac	5%
INR 5 - 7.5 Lac	10%
INR 7.5 - 10 Lac	15%
INR 10 - 12.5 Lac	20%
INR 12.5 - 15 Lac	25%
Above INR 15 Lac	30%

SURCHARGE

- 10% of the Income Tax, where taxable income is more than INR 50 Lacs but upto INR 1 Cr
- 15% of the Income Tax, where taxable income is more than INR 1 Cr

EDUCATION CESS

- 4% Health & Education Cess is applicable on income tax and applicable surcharge

NEW TAX REGIME

The alternate tax slabs offered by the government as per the New Regime introduced in 2020 are in the below table. Government gives an option to each choose between the two tax regimes. You will observe in the newer regime that the rates are lower than the older regime. But why so? Rates are lower as the new tax regimes do not allow a person to take advantage of any of the deductions and exemptions offered under the old tax regime. Because of this, even though tax rates go down, the taxable income remains higher and therefore you end up in a higher tax bracket.

The calculation of taxes payable remains the same under both the methods. Only the rates change for the same.We will discuss the suitability of the old and new regime in a while and how it affects your Lazy Financial Plan. Both these are suitable in different kinds of circumstances. We will discuss the required aspects of it going forward. Before we discuss selection of tax regimes and its implications on taxes and Financial Plan, we will first understand the various exemptions and deductions. These are offered to us only as per the older regime and newer regime does not allow for any of it.

TAX BENEFITS

As discussed earlier, our earned income and the taxable income are different. The differences arise due to the tax benefits that we get. These tax benefits are extended to us by the Government. They reduce the tax liability of the person. Now, tax benefits can be given in two forms i.e. exmeptions and deductions. Let us understand the technical terms first.

EARNED INCOME	-	TAX BENEFITS	=	TAXABLE INCOME
All income that you have earned		Exemptions & Deductions i.e. generally reduce taxable income and tax burden		Amount at which tax rate is levied

EXEMPTIONS

Exemptions are those income sources which are exempted or not counted as part of our income. Certain asset classes have returns that are free from tax liability. For instance, up until FY20, the government did not tax dividends received in India. These are income sources that are included in the earned income but are, however, excluded from the taxable income. Another example would be, the interest received on PPF in India. It is not counted in our taxable income. This means PPF interest is tax-exempt.

Dividend income before 2020 was tax exempt

Interest earned on PPF (Public Provident Fund) is tax exmept

DEDUCTIONS

According to income tax rules, we are allowed to invest up to a certain amount which will be deducted from our earnings to avoid income tax. In deductions, however, the amount can only be deducted if we invest in certain kinds of assets or we spend the money in a certain manner. For example, education fees, insurance expenses, grants etc. are deductible from our income. That means if we pay Rs. 26,000 in a year on child’s education fees and our income is Rs. 5,60,000, then we can claim a Rs. 26,000 deduction and reduce our taxable income to Rs. 5,34,000.

Similarly, we can also invest in certain assets and get that amount deducted from the overall taxable income. Remember, lower the taxable income, lower is the tax liability. Here, the government is only concerned about the way we spend the money, the way we earn it is not relevant. Also, the deductions come with a fixed limit, generally about the maximum deduction of a particular type that we can claim.

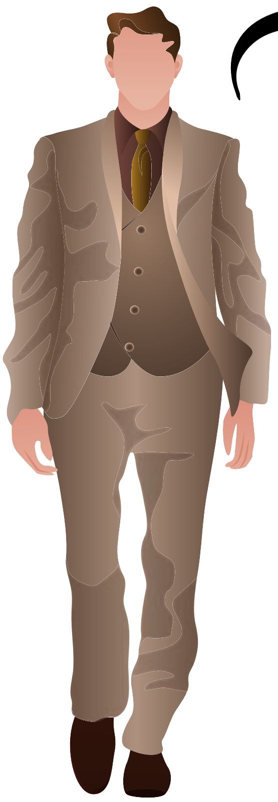
Education fees is
tax-deductible up to
a certain limit

EXEMPTIONS & DEDUCTIONS

Lets us begin with the various sections of the Income Tax Act that offers deductions to the citizens currently. Numerous tax benefits are offered by the government. However, for simplicity, we have listed down the most useful exemptions and deductions. We have categorized them in groups. These tax benefits may have more technicalities so you might need a tax expert's help at some places. However, this section will educate about the various tax benefits that you can use and hence, make a plan keeping in mind such benefits.

1 STANDARD DEDUCTION

Standard deduction is one of the most commonly used tax benefits. As of writing (FY21), the standard deduction in India is Rs. 50,000. This is a standard benefit provided exclusively to anyone who is a salaried person or is a pensioner, and the government does not bother with the avenue on which the money has been spent. Naturally, self-employed individuals are not allowed to benefit from this. Those who qualify for this benefit can seek a deduction in their taxable income of up to Rs. 50,000. This money reduces their taxable income and also tax liability. The amount for the same keeps on changing so we need to keep a constant track of the same.



TAX WITH TAX BENEFIT

Earned Income	10,30,000
Less: Standard Deduction	50,000
Taxable Income	**9,80,000**
Tax Based on Slabs	1,08,500
Add: Cess	4,340
Total Tax Liability	**1,12,840**

TAX WITHOUT TAX BENEFIT

Earned Income	10,30,000
Tax Based on Slabs	1,21,500
Add: Cess	4,860
Total Tax Liability	**1,26,360**

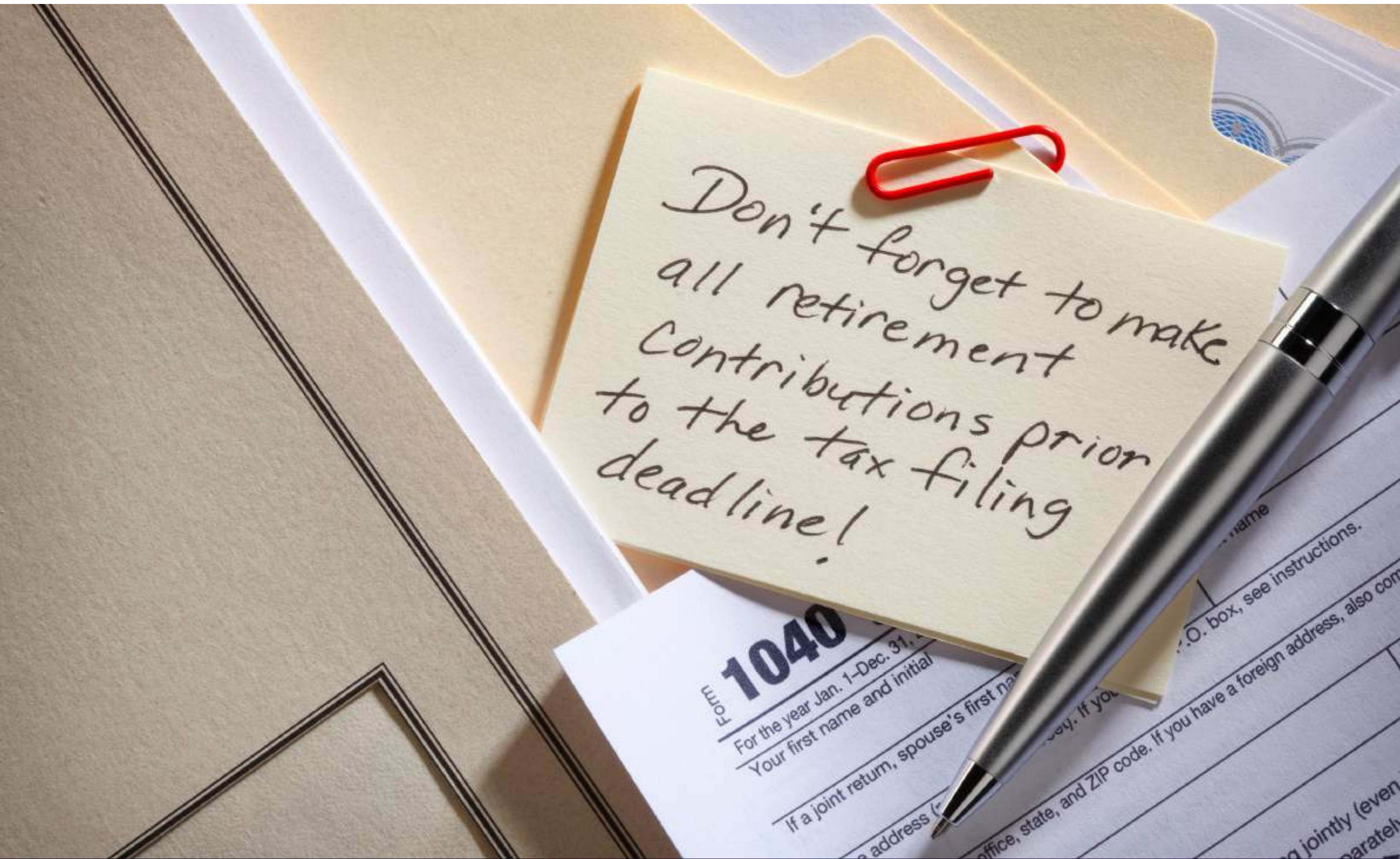
2

SECTION 80C & RELATED

The broadest category of deductions is Section 80C /80CCC/ 80CCD. These mainly relate to investments and certain special kinds of expenditures. In the corresponding image, it lists down the various investment avenues and expenses that are allowed by the section.

The three sections combined, offer an advantage of up to Rs.1.5 lac (1,50,000). So, if we invest up to the prescribed limit in any single or a combination of asset classes or spend it on the expenses mentioned like the education of up to 2 children, principal repayment on home loan etc. we can claim a deduction and our taxable income will go down by the amount that we have spent or invested in them. There is no qualification requirement for these sections and anyone who files an IT return in India can benefit from the same.

From a financial planning perspective, we will try to select assets that can allow us to meet our Financial Goals at the same time allow us to benefit from these deductions as well. However, if required, we will let go of these deductions in case they are contrary to out requirement of fulfilling the Financial Goals.We will understand these asset types in great detail in the next phase where talk about all the different asset classes and their behavior.



Options Available under Section 80C / 80CCC / 80CCD

Total deduction allowed for all investments and expenses combined is Rs. 1,50,000

DEBT INVESTMENTS

- NSC - National Saving Certificates
- SCSS - Senior Citizen's Saving Scheme
- Tax Saving Fixed Deposit (for 5 yrs)
- Tax Saving Post Office Deposit (for 5 yrs)
- PPF - Public Provident Fund
- EPF - Employee Provident Fund
- SSY - Sukanya Samriddhi Yojana

EQUITY INVESTMENTS

- ULIP - Unit Linked Insurance Plan
- Pension Plans from Mutual Funds
- Pension Plans from Insurance Funds
- Central Govt Pension Schemes
- NPS - National Pension Scheme
- Tax Saving Mutual Funds (ELSS)
- Life Insurance Premium

EXPENSES

- Principal Payment of Home Loan
- Stamp Duty & Registration Cost of House
- Tuition Fees for 2 Children

Section 80CCD-1B

Offers an additional deduction of Rs 50,000 over and above Rs. 1,50,000

- National Pension Scheme

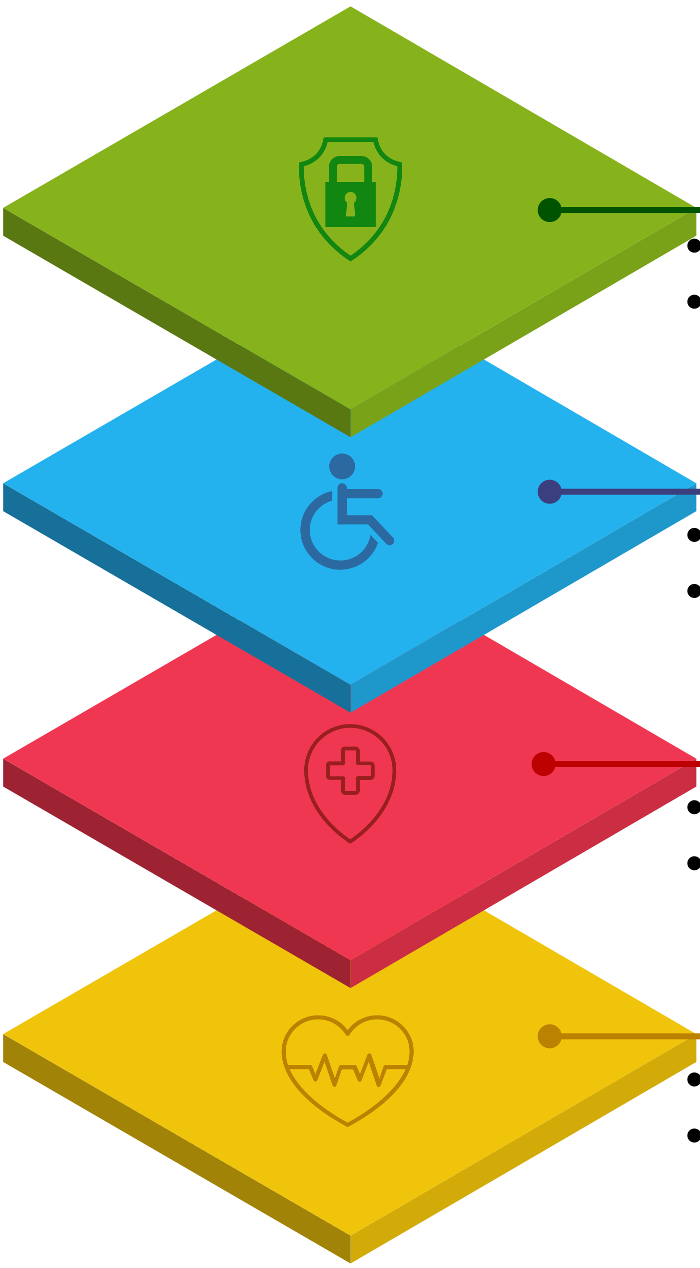
SECTION 80CCD-1B
NATIONAL PENSION SCHEME (NPS)

Section 80CCD-1B – A special section under section 80C that gives an additional deduction of Rs. 50,000 that relates to the National Pensions Scheme (NPS). This section offers an additional deduction of Rs. 50,000 over and above the Rs. 1.5 lac offered by Section 80C. National Pension Scheme is a retirement planning product offered by the government. NPS also offers an additional Rs. 50,000 as deductions which make the total potential under Section 80C including NPS to be Rs. 2,00,000.

3 HEALTH & WELLNESS RELATED

The next set of deductions offered is for expenses relating to our and our families' well-being and health. The corresponding image represents the different deductions offered under this section and its subsections. The limits here are completely independent and if we spend that amount in the specific categories, then we will be eligible for deduction.

At the profiling stage, we just need to list down categories where we currently spend money to understand what deductions we are eligible for. In most cases, we would already be taking benefit of these deductions. These expenses are mostly not determined by us but by our circumstances. The only issue that could be controlled by us is health insurance. We will read more on insurance in the parts to come.



SECTION 80D

- Medical Insurance for Family
- Deduction: 25,000 - 1,00,000

SECTION 80DD

- Health exp. of Disabled Dependent
- Deduction: upto 1,25,000

SECTION 80DDB

- Treatment of certain disease/ ailment
- Deduction: upto 1,25,000

SECTION 80U

- Physically Disabled Tax-payer
- Deduction: upto 1,25,000

4 LOANS

Education Loan

IT Act allows a deduction for loans mainly under two sections. Section 80E and Section 24. Under Section 80E, we can claim a deduction for all interest on our educational loan. Here, no limit has been defined and the entire interest component can be deducted. The interest is the only component that can be deducted and not the principal component of the EMIs that we will be paying. So, currently in our profile, we simply need to identify if we have any education loan or the intention to take one in the foreseeable future. If that is not the case, then this deduction can be ignored.

Section 80E
Interest Component of Education Loan
No Limit for Deduction

Housing Loan or Home Improvement Loan

Next under section 24, similarly, only the interest component of home loan is deducted. The principal component is covered in Section 80C. Here, a limit is identified for up to Rs. 2,00,000 worth deduction on home loan and if it is home improvement loan, then a limit of Rs. 30,000 is fixed.

Section 24
Interest component is deductible here
Home Loan - limit of Rs 2 Lac
Home Improvement Loan - limit of Rs 30,000

Section 80C
The principle component is deductible here, total limit of Rs 1.5 Lac

Section 80G
Donations to charitable funds and institutions

Section 80GGA
Donations for scientific research or rural development

Section 80GGC
Donations to political parties

5 DONATIONS

The next set of deductions deal with donations to different kinds of organizations. The limit has not been fixed over here, however, there are many detailed technicalities about the kind of donations that can be considered to get an Income Tax deduction. You should meet a tax expert to understand the same in greater detail. In most cases, this section is irrelevant. Here, you need to profile if you donate significantly each year and if you do, you should identify the same in your Lazy profile canvas and meet a tax expert or CA about the same.

OTHER TAX DEDUCTIONS 6

Certain other tax deductions are popular and relevant to individuals. These are all independent deductions irrespective of other deductions that we claim. So, we need to identify in our lazy canvas if we qualify for any of the conditions mentioned in the chart. Section 80TTA is a universal deduction for all asset classes whereas Section 80TTB is exclusively for senior citizens only.

Section 80GG
Paying rent in case of no HRA Deduction upto Rs 60,000

Section 80TTA
Interest received in savings account upto Rs 10,000

Section 80TTB
Interest Income for senior citizens (fixed deposit or savings account) upto Rs 50,000

NOTE : The amount of deduction under section 80D/ 80DD/ 80DDB / 80U varies from person to person depending on the circumstances of the case of every individual. The purpose of giving these amounts is to give the reader an idea regarding the availability of deductions in these areas. Readers are advised to approach a tax consultant regarding their individual deduction amount eligibility.

OLD REGIME V/S NEW REGIME

Now we need to choose between the old regime and the new regime. This decision mainly depends on the level of difficulty for us to switch and the binding assets we have. So, up until today, we were following the old tax regime. We will have home loans and education loans going on. We will have assets tied up in PPF investments that we need to continue. We will have ongoing insurance plans and so on. These commitments from our end are binding and they will continue with us for years to come irrespective of the tax regime that we follow. These commitments that bind us for years to come are called binding instruments.

If we have a very high amount in binding instruments, we will have to stick to the older regime. If the number of binding instruments is not very high, we can go ahead with the newer regime. In most cases, the older regime is the one that we will have to stick to.

The newer regime only makes sense for those with fresh slates and just starting on their careers. It would be in our best interest to consult an expert about old regime vs new regime. For most people, the old regime will make more sense due to the backlog of binding instruments that they are carrying.

If we plan to go ahead with the newer regime, we can skip the entire tax deductions part in the Lazy Plan stage as the new regime offers none of those benefits. It simplifies the process as no tax implications are to be understood. Only completely exempt assets can be used for benefit in the newer regime. However, when creating a Lazy Plan, always and always focus on meeting the financial goals properly rather than trying to squeeze out every ounce of the tax benefit by investing accordingly. Our primary goal is not to save maximum taxes, but to meet our financial goals.

CAPITAL GAINS TAX

The last topic that we need to understand with taxed before we move forward is a special type of tax – Capital Gains Tax. Capital Gains tax is applicable at the time of selling any asset. Capital Gains tax refers to the one-time tax corresponding to the capital appreciation of any asset from the time it was purchased.

So, an asset was bought for Rs. 20 lacs and sold for Rs. 25 lacs, the capital appreciation in this case is Rs. 5 lacs. So, a capital gains tax is applicable on the Capital Gain i.e. Rs. 5 lacs in this case. The rate of taxation depends on the asset class and the period for which it was held. Short term capital gains rate and long term capital gains often vary. Also, the tenure that is considered as short term varies for different asset classes. Irrespective of tax slab that you fall into, the tax treatment of capital gains remains the same. It has been shown in the table below-

Asset Classes	Equity & Equity Based Mutual Funds	Debt & Debt Based Mutual Funds	Real Estate
Short Term CST	15%	Part of Taxable Income	Part of Taxable Income
Long Term CST	10% of Cap Gains (above Rs. 1 Lac)	10%	20%
Tenure for Short Term	Less than 1 year	Less than 3 years	Less than 2 years

Capital Gains tax is a major consideration while we are making an asset sales decision. We might postpone or prepone the decision to sell based on tax implications. So, it is important to understand the tax implications whenever we sell an asset. Their tax liability when we earn dividends and interest from assets as well. We will learn their tax treatment in the asset stage.

With this we end our discussion of taxes in the RRTTLLU principle. We have understood how taxes work and what are the relevant sections for us. This is will play a huge role when we create a Lazy Financial Plan for ourselves going further.

LIQUIDITY NEEDS

The fifth element in the RRTTLLU is Liquidity Requirements. We will understand how much liquid assets do you have and how much do you actually need? Before we get into this, let us first understand, what exactly do we mean by liquidity. Liquidity of an asset is our ability to sell the asset and get it converted to cash, at a short notice, and at full price.

CONDITIONS FOR AN ASSET TO BE TRULY LIQUID

CASH CONVERSION
One should receive cash on sale that can be used elsewhere

SHORT NOTICE
One should be able to sell asset at a short notice to a willing buyer

FULL PRICE
One shouldn't have to offer any discount for quick cash conversion

ILLIQUID ASSETS

HOUSE

CAR

LIQUID ASSETS

FIXED DEPOSIT

GOLD

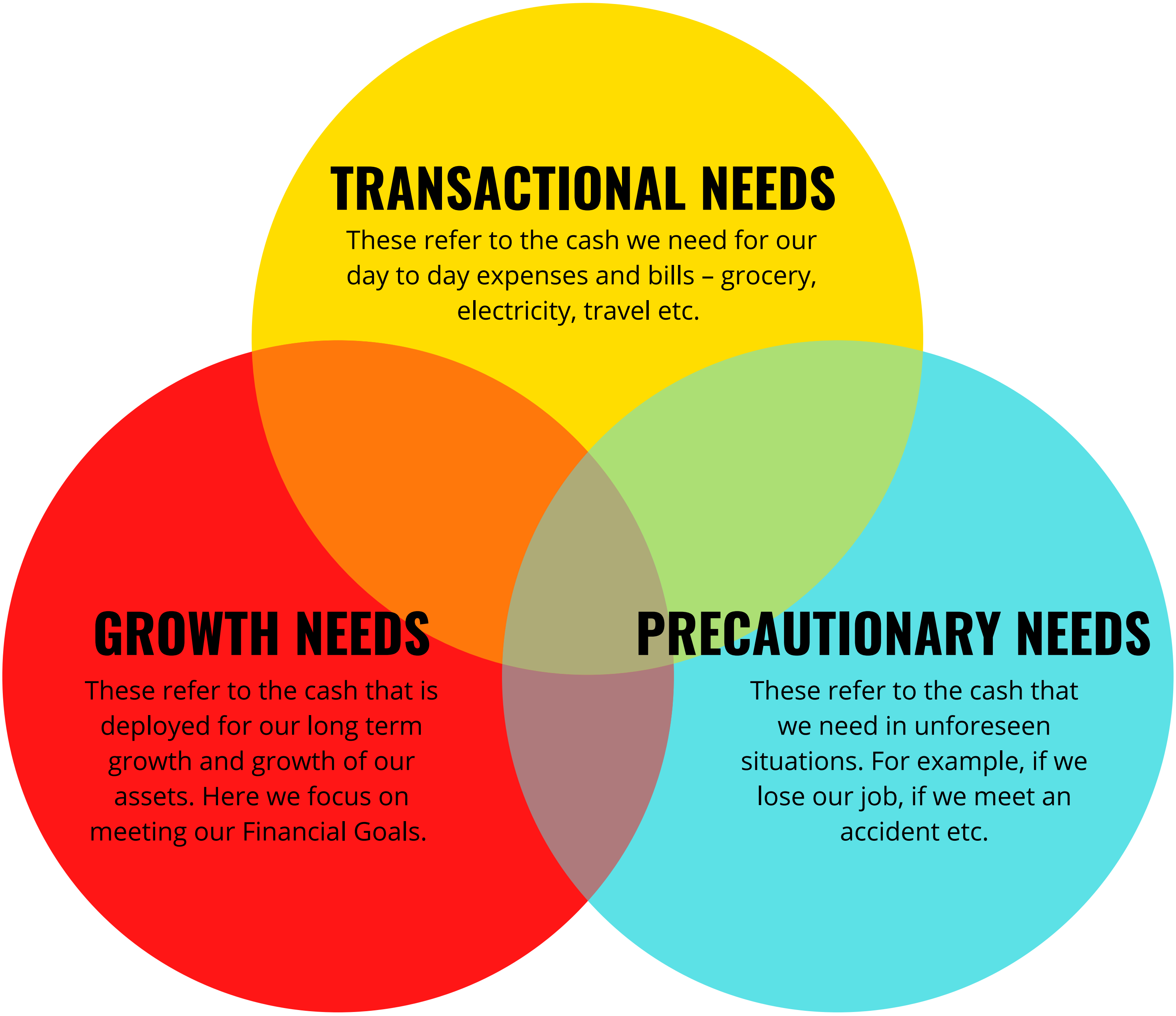
SHARES

Now we come to the importance of liquidity of assets. Cash is required to pay for all our expenses and most liabilities, meet a majority of our financial goals, and also deal with spontaneous emergencies. Hence, we must be able to convert our assets into cash at a short notice. Assets need to be liquid enough to meet our liquidity needs. Sadly though, assets that are more liquid, generally generate lower returns. As a result, the entire asset base cannot be liquid. There has to be a balance wherein the assets are liquid enough to meet our needs and simultaneously not too much to get us lower returns.

In the lazy canvas, we will first look into our current asset liquidity status and then hop onto estimate how much of the liquid assets we would need for ourselves. We will provide for these in the Lazy Financial Plan based on the needs mentioned.

We will begin by determining our current liquidity status. We will go back to our balance sheet, take a look at the asset side and identify how liquid each asset is. For this, we will estimate the time needed to sell the asset at its full price. Assets that can be sold faster are liquid and others are illiquid assets.

Moving on to estimate our actual liquidity needs; we have already discussed that the higher the liquidity, the lower is the return from the asset class. Therefore, we need to maintain a good-enough level of liquidity in our assets rather than flooding them with liquid assets. To do that, we will start by deciphering our liquidity needs. Let us get back to elementary economics, where we studied the role of money. We know that money comes in to meet the three kinds of needs listed below.



TRANSACTIONAL NEEDS

The liquidity requirements for your transactional need should be ideally met by your salary, business profits, interest, rent etc. In most cases, transactional amount is not used from assets but from income and as income is received in cash, we do not need to manage liquidity for transactional amount separately.

PRECAUTIONARY NEEDS

The precautionary amount is the money that we do not necessarily need instantly but we would want it liquid enough to be cashed out at very short notice, maybe even instantly. This is also called emergency money. Here, we will keep the money in highly liquid assets. These will include bank saving deposits, fixed deposits that can be en-cashed before maturity or jewellery.

Ideally, we should save up 8-9x of our average monthly income for this. Thus, if we earn Rs. 1 lac per month, a liquid asset base of Rs. 8-9 lac is sufficient to sustain our requirements.

GROWTH NEEDS

This will mainly include the amount that is to be invested in our general growth and meeting our financial goals. If a major goal is to be achieved in the following year, the liquidity needs will go up substantially. On the other hand, if the next major financial goal is 5 years away, we can invest in less liquid assets. Thus, liquidity needs depend on flexibility and time horizon of various financial goals.

We now understand that the liquidity requirement mainly pertains to the precautionary amount that we need. Liquidity for financial goals will be taken care of automatically when selecting assets to achieve them. We have also seen how liquidity affects our life. It so often happens that people, irrespective of having the assets, are unable to produce cash when needed. This is where liquidity management comes into the picture. For now, we will fill up the lazy profile canvas with our liquidity requirements. With this, we come to the end of our discussion about the fifth element of RRTTLLU principle.

With this we end our discussion of the fifth element of RRTTLLU principle. The last two elements are pretty simple and straightforward. Let us move forward and understand them one by one.

LEGAL & REGULATORY CONSTRAINTS

LEGAL CONSTRAINTS

Legal constraints relate to laws made by government or government agencies. These laws act as constraints that limit us from freely buying and selling assets. For instance, India introduced the Land Acquisition Bill, which allowed the government to buy land for development purposes. This law forced many people to sell off their land which they otherwise might not have. This is one of the many examples of legal constraint. Many such laws might affect us.

REGULATORY CONSTRAINTS

Regulatory constraints are similar to legal factors. However, they mainly relate to regulatory bodies rather than the Government and its agencies. Regulatory bodies, like the Reserve Bank of India (RBI) for the Banking sector, the Securities Exchange Board of India (SEBI) for the capital markets and so on create rules to regulate the markets.

All these constraints have to be considered while creating our Financial Plan. However, a large number of laws and regulations that apply to the open market, are taken care of by the financial companies itself that create financial products. So, an individual need not be concerned with the general laws and regulations. What needs special emphasis are the laws and regulations that specifically apply to us as individuals or a small section of people who are under conditions similar to us. If any such laws or regulations are present, we will list them in the canvas.

UNIQUE CIRCUMSTANCES

Time to pat our backs as we have made it to the last element of the RRTTLLU principle. 'U' stands for 'Unique Circumstance's which refers to factors that are unique or specific to us such as emotional attachment to certain assets, differences in opinion between family members regarding certain asset types, dependency on certain assets etc. These factors will affect our financial plan exclusively. List down any such factor in the canvas.

Refer to the following page to look at a few examples. In this manner, people have different circumstances that they need to take into consideration while creating a financial plan. Since it is impossible to list them all at one go, we will go on adding them as we realize more and more circumstances proceeding with the planning stage.

With this, we end the RRTTLLU stage of profiling. So far, we have created a personal income statement, balance sheet and understood our profile. We are done with a major chunk of our lazy canvas. The two steps that remain are to support our plan so that we can follow them up effectively. This is the part where we understand our insurance needs.

Sumit joined his family business that was being run by his father in the city of Nagpur. Till date, his father was managing his family's finances. Recently, Sumit attended a seminar on Financial Planning and wants to explore equity as an asset class. However, his father is only comfortable with gold and fixed deposits. Now, Sumit is faced with a unique situation where his family is uncooperative. Going forward, his planning will have to be adjusted to reflect his unique circumstance and therefore it is important to include it in the lazy financial canvas.

Shikha is a single mother and a teacher at a primary school. She has low interest in understanding and managing finances. So, she asked her brother to manage her finances. Now, this dependence is a unique circumstance for her and she will have to incorporate the same in the personal financial canvas.

Rajat is an engineer working with Amazon. Rajat and his father had saved and bought a small piece of land in their hometown. They had planned to meet the educational needs of Rajat's 2 children with the land. However, few days back, the previous owner from whom they had purchased the land, came back with a lawsuit that Rajat and his family had not cleared all the dues. Because of this, Rajat's entire financial plan is in jeopardy. Also, he has to travel to his hometown a lot and this affects his current job at Amazon as well.

03 RISKS AND INSURANCES

RISK & INSURANCE

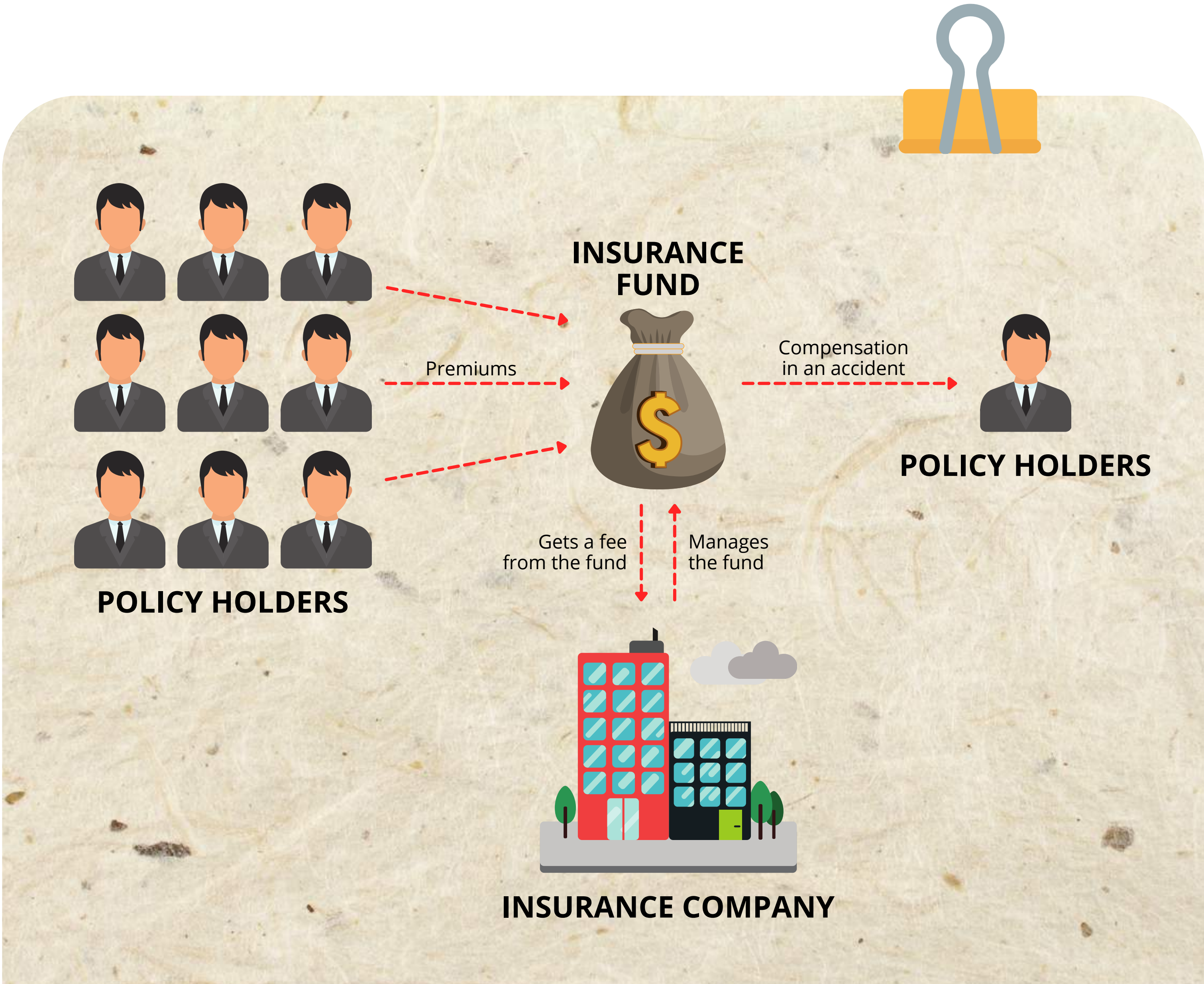
We have now completed two major steps of creating a lazy profile canvas. Our income sheet, balance sheet and RRTTLLU will form the backbone of our entire plan. Let us say, we have profiled ourselves perfectly and come up with a perfect plan for ourselves. According to our plan, all major goals will be met in the next 12 years. Everything was going well till the 5th year but then something untoward happened. Perhaps, we met with an accident and our salary was cut off or discontinued. We also have to pay hospital bills. Our financial plan would be completely derailed and we won't be able to meet most of our crucial financial goals

We see that our Financial Plan has a leakage. Leakage refers to a situation beyond our control that might put our plan completely off track. Even the best financial plans are prone to such risks. So, we need to address these risks and control them with what we call 'insurance'. With insurance, we can pay a small premium and if something happens, the insurer will pay for the expenses. Insurance makes our plan bulletproof.

Insurance is selling our risks to someone else for a premium (fee). For instance, let us say we own a house and the house has risks like property damage, fire, etc. and in all these cases we will have to suffer significant losses.

We do not know if the mishap will happen or not and the chances of it happening are slim. But, if it happens, it can have serious consequences. With an insurance cover, we transfer the risk to the insurer. The insurer profits from the insurance premium if the year passes smoothly without any bumps and if a claim comes along, he will pay for damages. For instance, the insurer insures 100 houses and only 1 of them has a loss on average. So, the premium from 80 homes will be paid to that claimant and the remaining 20 premiums will become his profit.

What are we getting from insurance? We are protecting ourselves from a large loss that is worth years of our income by paying a small portion of our current income.

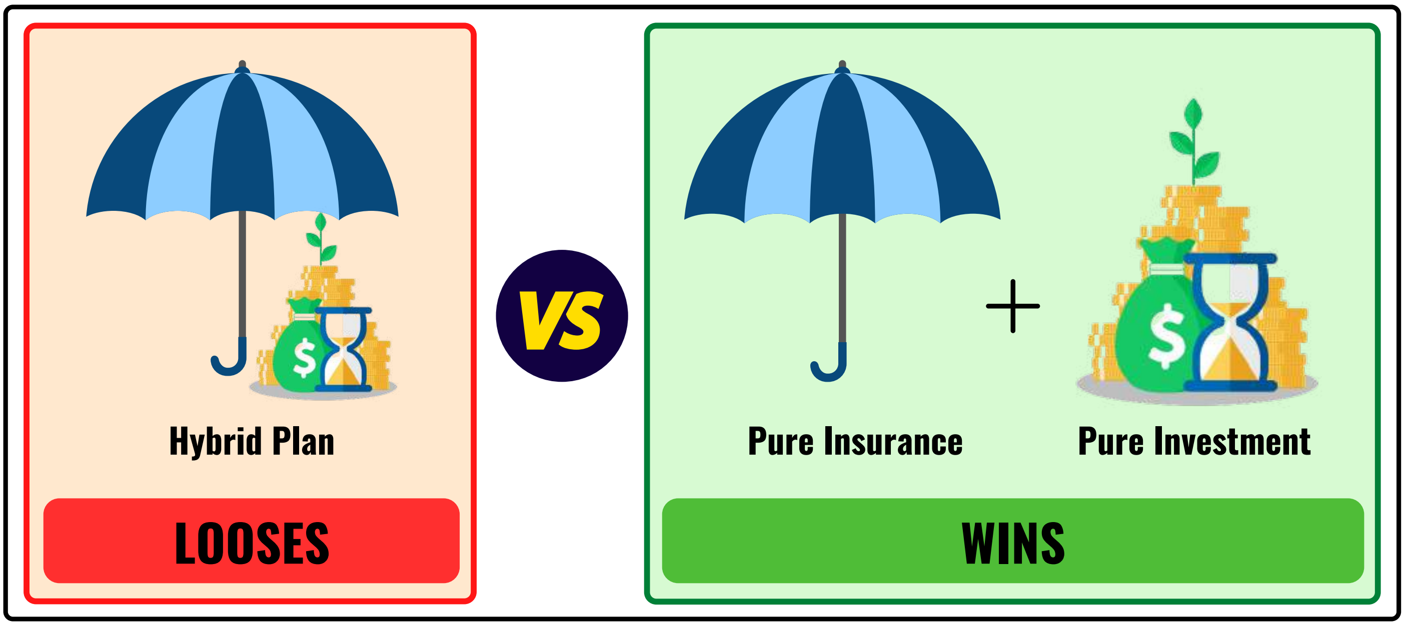


Now that we know what insurances, let us understand what insurances are not. Insurances are often advertised and promoted as Investments products as well. Insurances are not Investments.

Currently, Insurance companies sell products that have investment value attached to them as well. For instance, you pay life insurance premium for 20 years and you will get a fixed amount at the end of 20 years. What are the companies effectively doing? They are protecting you, but also mixing the same with an investment product. That means, a part of your premium goes for your protection, whereas another part goes as EMIs for the payback at the end.

With such policies, you are not just getting yourself insured, but are also paying for Investment Returns. However, the problem with such policies is that the math of it is just too complex for a common person to understand and if we break it down, the returns that we get are often lower than fixed deposit returns as well. That means we are investing in a relatively asset class and getting less than lowest of the market returns. And the math of it is so complicated, that it is impossible for a common person to do it.

Whenever, we talk about insurance needs going forward, we will always discuss about Pure Insurance Products and not those that have investment value attached to it.



A better way to look at pure insurance away from investment features added to the same is that, for a hybrid product, whatever coverage you are getting, get that coverage for a policy that does not pay back at the end, and whatever premium you are saving, invest that in an Investment product. You will see that at the coverage is also in place and the exit return is also higher.

The reason behind this happening is, if people pay premium for many years and the risk does not materialize, they start seeing the premiums as waste of money, not realizing what the insurance is doing by covering their risks of huge losses. However, with true insurance our money does get wasted if the risk does not materialize.

What kind of insurance do we need?

What should be the coverage of insurance?

A very small percentage of Indians currently buy insurance adequately. Those who do not, they leave their Financial Plan open to leakages. They are leaving their financial plan up to the mercy of luck which is hardly ever a good idea.

We want to protect ourselves from these events that might occur once in a while or perhaps once in many years, but when they happen, they send us back many years financially. This is why we will protect our Lazy Plan with insurances in a way such that we are neither underinsured with unwanted risks nor over-insured with money wastage.

Now that we know how insurance works and we have established we need them, in the next part we will figure out the type of insurance we require. There are various types of insurances such as health insurance, life insurance, property insurance etc. Then, we will estimate the amount of insurance coverage needed.

So, let’s get started…
We need to first understand the risks that we face. Risk is any uncertainty that can go wrong and by the term ‘Financial Risks’, we refer to the risks relating to our Financial Plan. We will consider all the factors or events that are beyond our control and can jeopardize our financial plan. We will create a list of all the risks that we face, our income and our assets face and then use a model to evaluate which of these risks need to be insured and which ones can be safely ignored.

To create a list of the potential risks, we will begin by going back to our balance sheet, pulling out every asset and liability, and anticipating what can go wrong with them.

LIABILITIES

Liability insurances refer to the protection against the risks that some unforeseen liability might present to us. So, with insurance, we intend to shift the risk of an unforeseen liability to the insurer and with the appearance of an unforeseen liability, the insurer will meet the liability on our behalf. A significant liability coming up can derail our financial plan.

For example, if we own a factory that sets on fire one day due to which a workmen liability arises suddenly. Or, your company is accused of Intellectual Property (IP) infringement and liability has arisen. So, we seek insurance to keep ourselves protected against such risks. The list of possible risks will be created based on the profession and the kind of liabilities people from similar fields of work have faced in the past. We understand that it is not possible to create an exhaustive list of all risks or liabilities that we face.

ASSETS

We own a house, what could go wrong with it? It can catch fire or an earthquake can damage it and so on. Practically anything can go wrong with the asset and it is undoubtedly a risk. Next, let us say, jewellery. What can go wrong? The jewellery might get stolen. Similarly, we have to create a list of risks for all the assets that we could face and make the list as exhaustive as possible. We will use a system going further that will evaluate which risks need to be insured and which ones can be ignored.

One common mistake is to include market-related risks in this list. For instance, in the case of jewellery, the market price of gold may go down. We cannot ensure such risks that are market-related, or related to our skills, risks built-in asset classes and so on. We can only ensure risks that are a potential threat to the asset or completely exhaust the asset.

Income

FROM ASSETS

These will be insured when we insure the assets i.e. rental income, interest income, dividend etc.

FROM EFFORT

Insure these income sources i.e. salary, business profits, commission fees and so on

Expenses

Small expenses can be met by emergency fund; large expenses will be covered under liability insurances, hence no insurance needed.

Once we have finished listing down the risks relating to our personal balance sheet, we will add the risks relating to our income and expenses. On the income side, we see there are 2 sources – from our assets such as interest, dividends and rental income and those that come from our efforts such as salary and business profits. So, the first category will be taken care of on its own when we insure our assets.

We need to insure ourselves against events that can deteriorate our effort based incomes like salary. What happens if our salary stops coming in and we no longer can earn the same? In cases where we perhaps lose our jobs or worse comes to worst, due to some accident we end up with some temporary or permanent disability and can no longer continue working.

Such uncontrollable risks that affect our ability to work or perform are the risks we must jot down in the list of risks. Here again, we will not include market-related factors such as not getting our desired jobs, not getting paid as much as we would like and so on.

Lastly, we move to expenses. We will not be including any risk relating to expenses. Why so? This is because if the amount of expenses is small, those will be taken care of from our emergency fund and if the amount is large, it will be treated as an upcoming liability.

By now, we will have an exhaustive list of risks we might face. With our list of risks, if we try and get each one of them insured, we will end up paying a large portion of our income as premiums and end up being over-insured unnecessarily. We will selectively insure the risks. Let us see how we will evaluate these risks. To select the risks that need to be insured, we will answer the following two questions for every item on our list.

1

HOW FREQUENTLY DOES A RISK OCCUR?

We mean, does the risk occur every year, once in every 2-3 years, every decade, or perhaps, once or twice in a lifetime. We have to understand the frequency of the risk-based on our specific circumstances. For instance, if we live in a flood-prone zone, flood losses and related perils would be a frequent risk, occurring almost every year. However, for those living in areas where floods rarely happen, we can say that it is infrequent. Frequent risks occur once every 2-3 years while infrequent risks once in every 4-5 years.

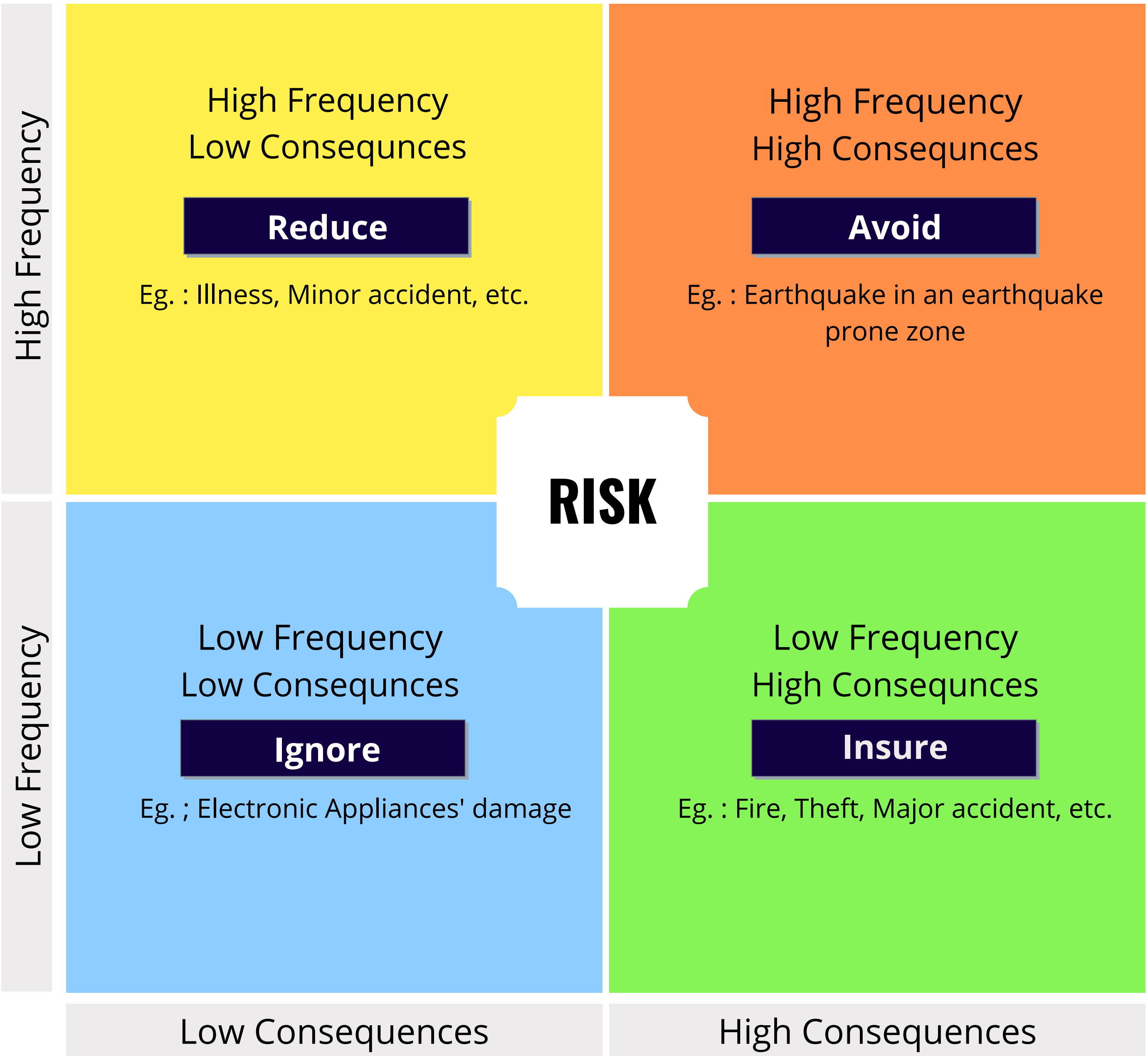
2

WHAT ARE THE CONSEQUENCES IF THE RISK OCCURS?

We mean, does the risk occur every year, once in every 2-3 years, every decade, or perhaps, once or twice in a lifetime. We have to understand the frequency of the risk-based on our specific circumstances. For instance, if we live in a flood-prone zone, flood losses and related perils would be a frequent risk, occurring almost every year. However, for those living in areas where floods rarely happen, we can say that it is infrequent. Frequent risks occur once every 2-3 years while infrequent risks once in every 4-5 years.

Based on these two questions, we will plot each risk in one of the quadrants as shown on the next page. We will stop for a while and do this for all the risks. We will decide the appropriate treatment of the risk based on the quadrant it falls into.

We will place each risk in one of the quadrants in the above framework and based on which quadrant they lie, we will learn how to deal with each of them.



By now we have created a long list of all the risks that we face and then also evaluated each of them using our framework. We have also narrowed down our list to risks that need to be insured i.e. those that are infrequent but have high consequences. The next concern in the profiling stage is to look into the kind of insurances we would need and lastly, the pocket pinch for the same.

So, let us study the four major categories of insurance that almost everyone needs. These will cover most of the risks that fall into the insure quadrant. After this, our profiling for insurance needs would be complete. We will be discussing the process to select insurance schemes in the lazy planning stage.

RISKS COVERED BY INSURANCES

HEALTH INSURANCE

It comes into the picture when we or someone from our family falls ill and are hospitalized. The insurance company covers all the expenses of the medical expenses during this period. In India, medical expenses are rising at a rate faster than 10-15% p.a. Illness comes with emotional and physical stress and we do not want to add another layer of stress to it i.e. financial stress. Having to pay off the hospital bills has put numerous families' finances out of shape because in most cases, it comes unannounced. That is why we need health insurance in place.

1

WHO ALL ARE DEPENDENT ON US FOR THEIR MEDICAL EXPENSES?

The first question that we will answer to evaluate our requirement for health insurance needs is to determine who and how many people are dependent on us for their medical expenses. These are people that we will have to pay for, in case they fall ill and have medical expenses. These can be our spouse, parents, children, uncle, aunty, grandparents, friends, etc.

So, when we talk about health insurance and its need, we will discuss it keeping these people in mind. These are the same set of people that we will look to get insured as we go ahead. If we have too many dependents, we definitely will need an insurance plan in place. The reason being an increased probability of people falling ill.

2

DO WE NEED A HEALTH INSURANCE ?

We have already created a list of risks that are infrequent but have significant consequences. Health risks are a common phenomenon and apply to almost anyone doing this exercise. However, not everyone needs Health Insurance. So, to decide if we need health insurance or not, we will check if we have spare assets, which are not tied to any financial goal so that we are ready to let go of them in case, any health-related financial need arises.

If yes, we can decide to not have medical insurance. However, another catch is that the asset should be liquid. Only then our asset qualifies to meet health-related financial needs. However, we would still advocate that every person should have health insurance. The reason being, health emergencies often come unannounced and bring with them a lot of emotional pain. You do not want to add to that with financial pain. Also, it has been observed that insured patients opt for better treatment than uninsured patients. It is not as infrequent as other risks.

IF WE NEED HEALTH INSURANCE, HOW MUCH COVERAGE DO WE NEED?

Let us begin estimating the extent of insurance coverage we could need. To do so we will look at the treatment facilities and options in our home city and then contemplate over the city we would like to get treated at in case of health emergencies. Sometimes, people coming from a relatively small town, village, or in some cases even tier 1 or 2, travel to metro cities to seek treatment.

Let's say, someone who gets treated in Delhi, will expect a room rent between Rs. 6,000-8,000 per day in the hospital. As per the rules, we would need at least 100x cover of the room rent that we will be treated in realistically. This is only the minimum insurance that we need. So, in this case, minimum insurance is 8,000 x 100 = Rs.8 lac. However, the ideal range is between 150x and 200x of the room rent. That means the ideal health insurance ranges from Rs.12 lac to Rs.16 lac. This is the ideal range of coverage he should aim for.

ROOM RENT	×	MULTIPLIER	=	INSURANCE COVERAGE	
8,000	×	100	=	8,00,000	Realistic Amount
8,000	×	150	=	12,00,000	Ideal Range
8,000	×	200	=	16,00,000	

LIFE INSURANCE

Life Insurance is the insurance of ourselves and our responsibilities. If something were to happen to us, who would take care of our responsibilities? Who would look after our families? This is where life insurance comes into play. We pay a premium to the insurer, and if something happens to us, the insurer will pay out a one-time lump-sum to our families so that our financial responsibilities can be taken care of. The ones who are financially dependent on us should not have to bear the brunt of our death. Even though death might be an uncomfortable topic, it should not be ignored and catered to while there is still time. Insurances secure our family's financial future in case something happens to us. Now let us answer these 3 questions based on which we can evaluate if we need life insurance –

HOW MANY PEOPLE ARE DEPENDENT ON US FOR INCOME?

We have already evaluated this while judging our risk-taking ability. Even if a single non-earning person depends on us for their expenses, we need life insurance. In case something happens to us, this person will not be able to meet their expenses. Therefore, we need to create a safety net for them. These people can be our spouse, parents, grandparents, children, relatives etc.

HOW MANY PEOPLE IN THE FAMILY EARN?

If multiple people in our family earn, the responsibility is shared. However, if one is the sole earning member, they burden the whole responsibility single-handedly. If your income goes away, the entire family's source of income goes away. However, if there are other earning members then there is still some source of earning coming in for the family. Hence we have to assess if our family will still be financially stable even if we stop earning suddenly. If the family has other sources, then we do not need life insurance but if our salary is the major income source, then we do need a life insurance cover in place.

DO WE HAVE ASSETS TO MEET LIABILITY?

If our asset ownership is high, we will be getting income from our assets as well which will continue even if something happens to us. Secondly, our family can always sell assets to meet their financial goals and responsibilities. For someone whose investible portfolio is really big, they depend more on their assets in comparison to income. Thus, in this case too, life insurance is not required. But if we do not have enough assets, health insurance is needed.

AMOUNT OF INSURANCE

Now that we have understood if we need life insurance or not, the next step is to figure out the amount of insurance coverage. We will determine it by a pretty simple and straightforward calculation i.e.8-10 times of our current post-tax annual income plus major liabilities that need to be repaid.

LIFE INSURANCE COVERAGE

8-10 TIMES OF YOUR CURRENT POST TAX ANNUAL INCOME

MAJOR LIABILITIES

To cite an example, Hitesh earns Rs.50,000 per month currently after paying all his taxes. He also has a student loan of Rs.20 lac. So, his post-tax income is Rs.50,000 x 12 = Rs.6,00,000. So, based on his income, the life insurance required should be between Rs.48 lac to Rs.60 lac. He also needs to add Rs.20 lac for the liability that he has. In sum, he should get coverage for an amount between Rs.68 lac to Rs.80 lac. Rs.75 lac is the amount of life insurance cover that he should aim for.

INCOME	×	MULTIPLIER	+	LIABILITY	=	INSURANCE COVERAGE
6,00,000	×	8	+	20,00,000	=	68,00,000
6,00,000	×	10	+	20,00,000	=	80,00,000

ACCIDENT COVER

Accident cover is one of the most under-advertised types of insurance because the people who sell it are not incentivized for the same. It is one of the most important forms of insurance.

The medical expenses, in case any inconvenience to a person are met by health insurance. In case of death, it is taken care of by life insurance. But what happens if the person lives on with a temporary or permanent disability? The recovery might take from a few months to a few years based on the event. The person has to bear the increase in expenses relating to his treatment for a very long time and all of it may not be covered by health insurance. Additionally, due to the disability, the person's ability to earn can also take a hit. In this period of increased expenses and reduced income, how would one sustain their financial well-being? The answer is through accident cover insurance.

We go to a general insurer and pay a premium for accident coverage. They protect us from any temporary or permanent disability that arises due to an accident. Insurers divide accident coverage into categories –

TEMPORARY DISABILITY

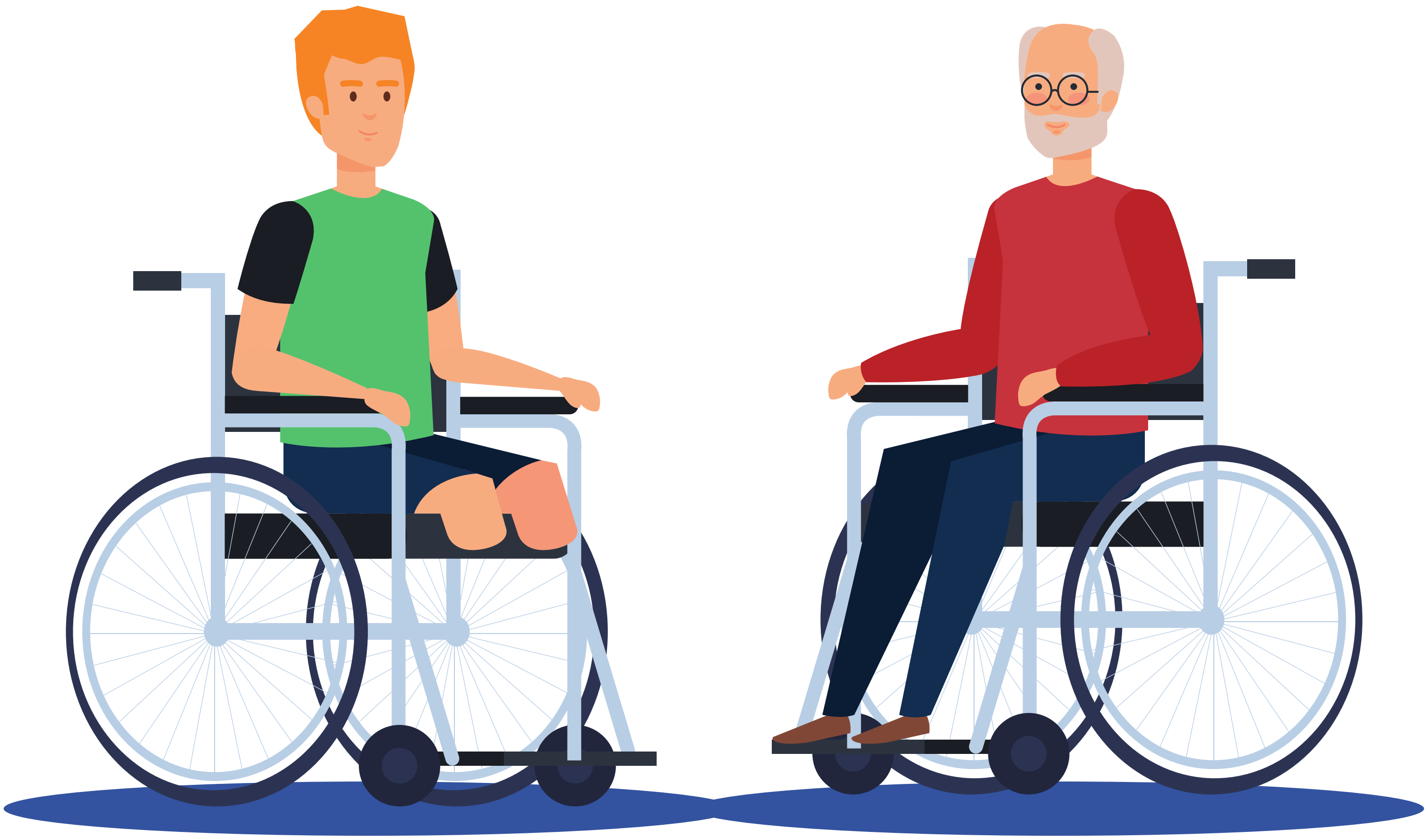
It refers to those categories of accidents where the person cannot work for a particular period, be it for 6 months, 2 years, or 3 years.

For Temporary Disability, a fixed amount is paid every week or every month during the period of disability where the earning ability has been impacted.

PERMANENT DISABILITY

It refers to those accidents where the person cannot return to work. It has an irreversible impact on earning power.

For permanent disability, the calculation is much more complicated. The insurance companies and regulatory bodies have together identified the 'value of each body part.' This has been done based on the impact of losing one body part on people's ability to work productively.



DO WE NEED ACCIDENT COVER?

The answer to this is pretty simple and straight-forward. If we need life insurance, we need accident cover as well. The 3 questions that we used to evaluate our need for life insurance, will also help us evaluate our need for accident cover.

FOR WHAT AMOUNT WOULD WE NEED THE ACCIDENT COVER?

The amount would be 8-10x of the post-tax annual income that we are making currently. This is the same method that we are using to calculate life insurance needs except that for life insurance, we had also added the major liabilities to our coverage amount. Here, we can ignore adding up liabilities to the coverage amount.

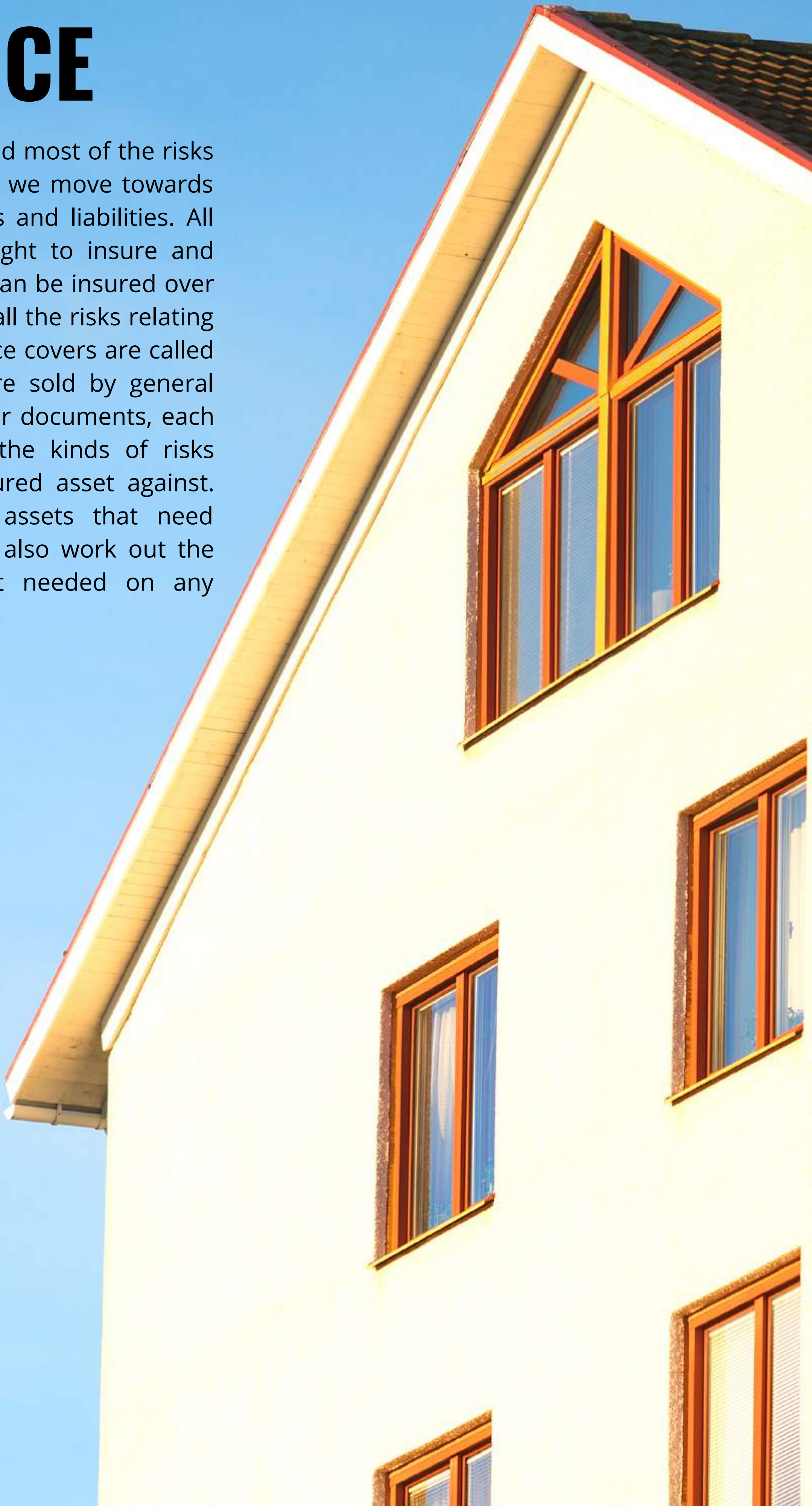
All this may sound a little overwhelming and some may ask why we are getting so pessimistic. And we would say, “We hope for the best, but prepare for the worst”. For the Financial Plan to be effective, we need to take care of the downside, the good stuff can take care of itself. That is why it is so important to expect the worst case and prepare for the same.

The purchase of multiple insurance covers with high premiums might get us complaining about the little left for our investments and consumption. But we are only insuring ourselves in line with our income. Moreover, paying premiums is a planned and systemic outgo. On the other hand, a liability arises out of the blue and usually requires a significant amount. So, smaller premiums out of income are much better than large one-time items that put our financial plan completely out of context. We do not want unpredictable liabilities destroying our financial health.

We build a full-proof insurance system so that we can protect the growth plan that we will be making going forward to meet all our financial goals. Emergency funds and insurance system will help us insure everything else that we achieve financially and to do so, paying a small part of our annual income is a good trade-off.

PROPERTY & GENERAL INSURANCE

Up until now, we have insured most of the risks related to our income. Next, we move towards insurances relating to assets and liabilities. All the risks that we had thought to insure and have not been covered yet, can be insured over here. We will begin insuring all the risks relating to our assets. These insurance covers are called property insurance. They are sold by general insurance companies. In their documents, each insurance policy describes the kinds of risks they would protect the insured asset against. Here, we will assess the assets that need property insurance. We will also work out the property insurance amount needed on any given asset.



For assets that are tied up to any financial goal

For these kinds of assets, we need to get property insurance. If they are financial assets, insurance is not needed. But if they are physical assets, insurance is a must. There are no second thoughts to spare in this regard, we will get all the relevant insurances for the assets tied to financial goals.

For these assets, 100% of the asset's current market value must be insured as only that way we truly protect our Lazy Financial Plan from leakages or risks.

For assets that are not tied up to any financial goal

Here we can decide whether or not we would want insurance for our asset. We would recommend insuring these assets as well because it takes several years to build an asset and one single event to destroy it.

We recommend insuring 100% of market value for the same too. However, here if we intend to save on premiums, we can insure worth less than 100% of the same too. But in no case, will we recommend insuring less than 50% of the asset's market value

WHAT VALUE SHOULD THE ASSETS BE INSURED FOR?

One of the most confusing things people do is get their assets insured but only for a very small value of it. This means, for an asset that is worth Rs. 20 lac, they will get an insurance cover worth only Rs. 5 lac. This makes no sense since the purpose of insurance is not even served. We are risking the entire dollar to save a few cents and that is never a good idea. It is always a good idea to insure 100% of an asset’s worth.

Now, we stop for a while and go to the asset side. We will add the need to insure 100% of the assets tied to financial goals to the Lazy Canvas. For those that are not tied to any financial goal, we need to insure the same for a minimum of 50% of market value, preferably higher.

Going back to our list of risks, we will take a look at the assets that need insurance, and whether or not they are being covered for all the possible risks. For instance, a building should be insured for both fires as well as earthquakes. So, we will check if the assets are covered for all the risks or not and then add them to the profile accordingly.

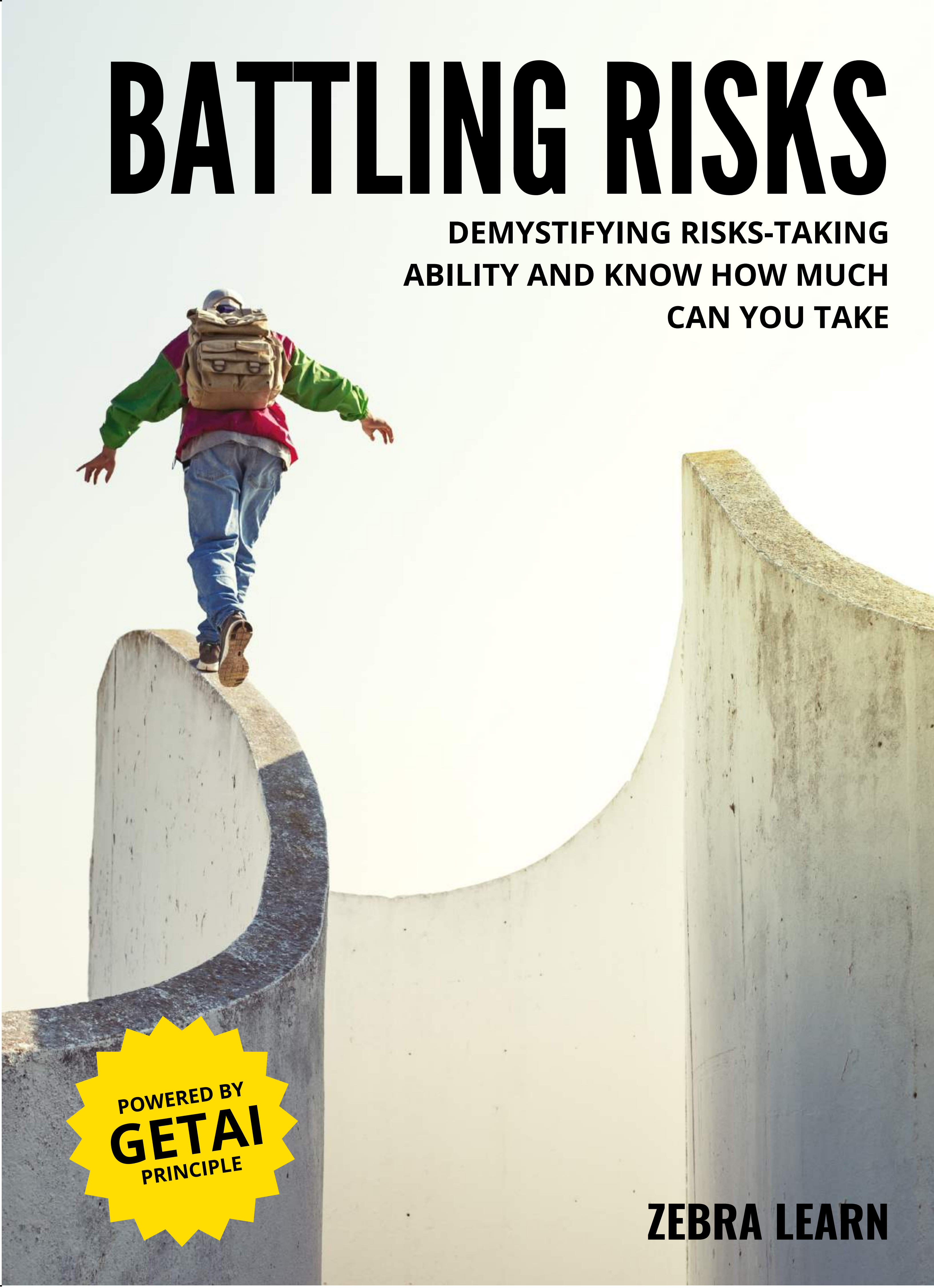
By now we have covered most of the major risks associated with –our health, life, accidents and major accidents. However, if we go back to the list of risks, we will see that many smaller risks remain unsolved. We will strike out the major risks that we have looked at from the list and focus on the risks that are left. All these risks would be insured by general insurance providers.

There is a wide variety of insurance covers currently being offered. These include vehicle insurance, trade credit insurance, jewellery insurance, liability insurance, etc. So, any risk that meets our criteria, there will be someone insuring the same. Add these insurance requirements in the lazy canvas. We are done profiling ourselves for our insurance needs. We will see how to select different types of insurances going forward in the planning stage. Here, we have clarity about what insurances we need and for what amount.

Before we wrap up the insurance needs, we would again like to emphasize two points. Numerous people have fallen for these psychological traps and have had their finances ruined. We will not get ahead of ourselves and consider ourselves to be above all risks and accidents. In all probability, 99 out of 100 people are not the unlucky ones. But what if, we are that one person? It is better to be safe than sorry. The financial circumstances are so significant that it is way better to consistently be insured.

Secondly, being covered for risks is psychologically so peaceful. It gives so much mental strength that god-forbid if something happens, our assets and families will be taken care of. Many people start with insurance, they pay the premiums year in and year out, but the risk does not materialize for years and slowly they start thinking of insurance as money down the drain. But one day, out of the blue something might happen and destroy the financial well-being of our family. A single event can take us 5-7 years back.

With this, we are almost done with our lazy profile canvas. We have filled almost all the blocks and understood the guiding profile of our Financial Plan. We see that the profile is very personal and therefore the plan that we will create will be specifically tailored for us. However, we often see that people behave differently even after knowing the right choices that are to be made. The reason for this is reality influences. Let us understand these in detail.



BATTLING RISKS

DEMYSTIFYING RISKS-TAKING ABILITY AND KNOW HOW MUCH CAN YOU TAKE

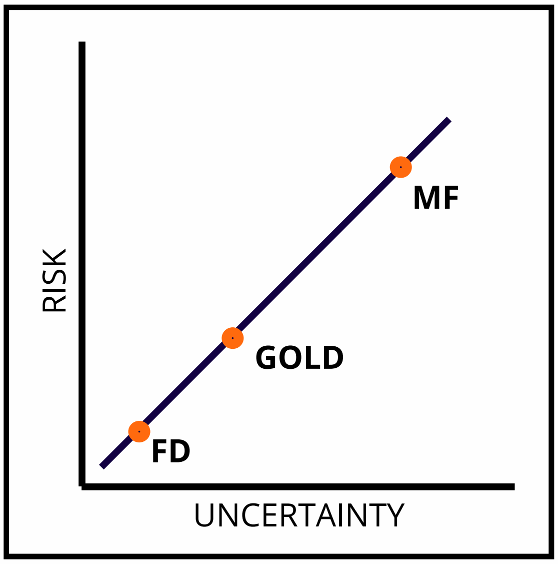
POWERED BY
GETAI
PRINCIPLE

ZEBRA LEARN

RISK

INTRODUCTION

The next element of RRTTLLU principle is risk. Return goals and risk are the two most important components of the RRTTLLU principle and the entire lazy financial canvas. First, let us understand what we mean by risk? Risk is simply the degree of uncertainty based on our decisions. Here, we are talking about risks from the financial point of view and it talks about the degree of uncertainty of the outcome. Higher the uncertainty, higher is the risk. It refers to the times we cannot predict the outcome.



FIXED DEPOSIT

Low Uncertainty
Low Risk

GOLD

Moderate Uncertainty
Moderate Risk

MUTUAL FUNDS

High Uncertainty
High Risk

Moreover, risk is relative. This means that one asset is more or less risky in relation to other assets. In itself, we can't judge riskiness. We evaluate risk in comparison with other asset classes.

HOW TO THINK ABOUT RISK?

Risks need not always have a negative outcome or impact. Without taking risks, we cannot get meaningful returns. Assets that give higher returns have higher risks attached to them. We cannot play it too safe and expect to meet all our financial goals. The very definition of investing is – "Reward for Risk Undertaken". Hence, higher the risk, higher is the reward. This does not imply that we start making rash decisions or baseless risks to earn higher returns as that will blow up our entire Lazy Financial Plan.

The critical thing to do here is balance risk and return. We evaluate how much risk we can take based on our profile and secondly, how much risk we are willing to take. Remember, too much risk and our plan may not survive long term. And too little risk, we may not end up meeting our financial goals, which is an even bigger risk.

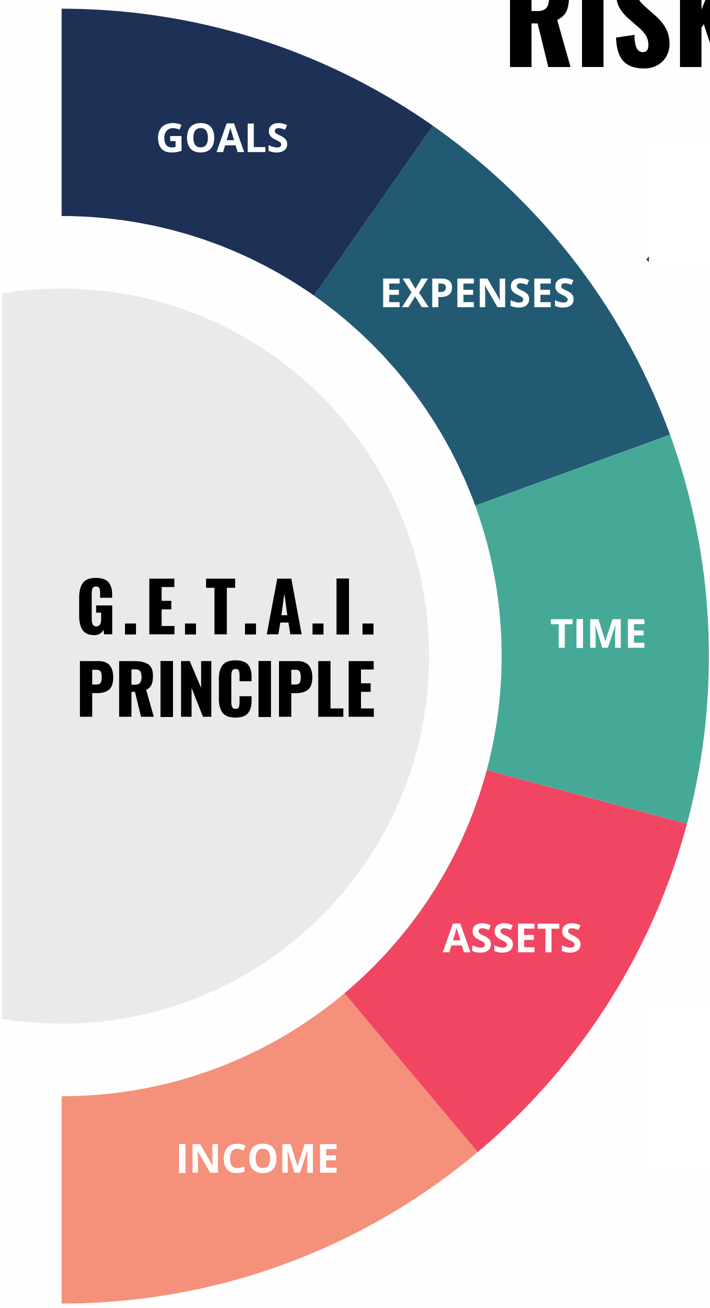
RISK TAKING ABILITY

it is the degree of risk that one can take based on their current financial circumstances i.e. assests, income, expenses, etc.

RISK TAKING WILLINGNESS

the degree of risk that one is actually comfortable with irrespective of the financial circumstances.

RISK TAKING ABILITY



Our risk-taking ability, willingness and return goals will together help us achieve the risk-return balance that is needed. We already are aware of our return goals. We will now evaluate and profile ourselves based on our risk-taking ability and willingness one by one.

Evaluating risk-taking ability is a very subjective process. Most people evaluate it based on their biases. However, using the G.E.T.A.I. principle, we will try to make it as objective as possible. It is a set of factors that together evaluates our risk-taking ability. GETAI stands for Goals, Expenses, Time, Assets and Income.

GOALS

It stands for the financial goals that we discussed a little while ago. We had listed down all the goals, prioritized them, quantified them and judged its flexibility. Now we will use two factors – flexibility and importance of the goal to evaluate risk-taking ability.

HOW FLEXIBLE IS YOUR GOAL?

The more flexible our goal is in terms of amount and time, the higher is our risk-taking ability. If we have high flexibility, we still have room to meet our flexible goals even if things do not go as per the plan. We can either do it with a lower amount or else by delaying the requirement for a while.

HOW IMPORTANT IS THAT GOAL?

The more important the goal is to us, lesser are the chances we would want to take and therefore lower will be our risk-taking ability. When the goals are less important, we can take risks and try to earn higher returns that will compensate for less flexible and more important goals.

EXPENSES

We will go back to our income statement that we had created and get our expenses from there. Following are the questions we need to answer.

WHAT IS INCOME CUSHION YOU HAVE?

We will check from the personal income statement and estimate what percentage of our income do we spend. If we have to spend 80-90% of our income that means our income cushion is very thin and our risk-taking ability is very low. As our income increases or expenses are reduced and our income cushion widens, our risk-taking ability goes up.

HOW MANY PEOPLE DEPEND ON YOU?

Evaluate the number of people who depend on us for their expenses. This is important because when we take risks, we also take risks for them. So, the higher the number of dependents, the lesser is our risk-taking ability. If we are the sole earning member in the family, our risk-taking ability goes down.

TIME

Time is where we talk about the period we have for each of our goals and how flexible they are. The questions to be looked into are:

HOW MUCH TIME DO WE HAVE TO MEET EACH GOAL?

Some goals are to be met in 2-3 years, others in 5 years and the rest in 15 years. Longer the time horizon to meet goals, greater is our ability to take risks. As our timeline increases, our ability to deal with uncertainty increases. If a goal is to be met in 1 year, we have to approach it safely as we do not have time to deal with uncertainty. However, if a goal is to be met in 10 years, even if things do not go as per the plan for 2 years, we would still have time to recover.

HOW FLEXIBLE ARE YOUR GOALS IN TERMS OF TIME?

We have already seen, higher the flexibility of our goals, higher is our risk-taking ability. It assures us that we can shift the timeline by a few years if need be.

ASSETS

Here, we do not focus on how much we own, but on the liquidity of our assets and how thick our support system is using assets. The questions to be answered are:

ARE YOUR ASSETS LIQUID?

Liquidity of assets refers to the time taken to convert our asset into cash (if we want to). Gold or FD can be converted to cash overnight. However, an ancestral land will take 1-2 years if we wanted to sell it. Easily convertible assets are liquid assets and those that take time are illiquid assets. Higher the liquidity, higher is the risk-taking ability.

HOW MUCH OF YOUR TOTAL ASSETS IS SUPPORT ASSETS?

Refer the personal balance sheet and see what percentage of total assets is under support assets. Higher the support assets ratio, greater is our risk-taking ability. However, we must balance it with the size of the investible portfolio too. If it is too small in absolute terms, we might not end up meeting our financial goals.

INCOME

Using this parameter, we establish the stability of our income and also whether we are more dependent on income or assets. The questions to be dealt with are:

HOW STABLE IS YOUR INCOME?

Some people have stable government jobs, some have startup jobs, some have commission-based income and others may run a business. We need to evaluate if our income is stable i.e. predictable or variable where some years we earn exceptionally well and others, not so much. Stable income increases our risk-taking ability whereas unstable income reduces risk-taking ability.

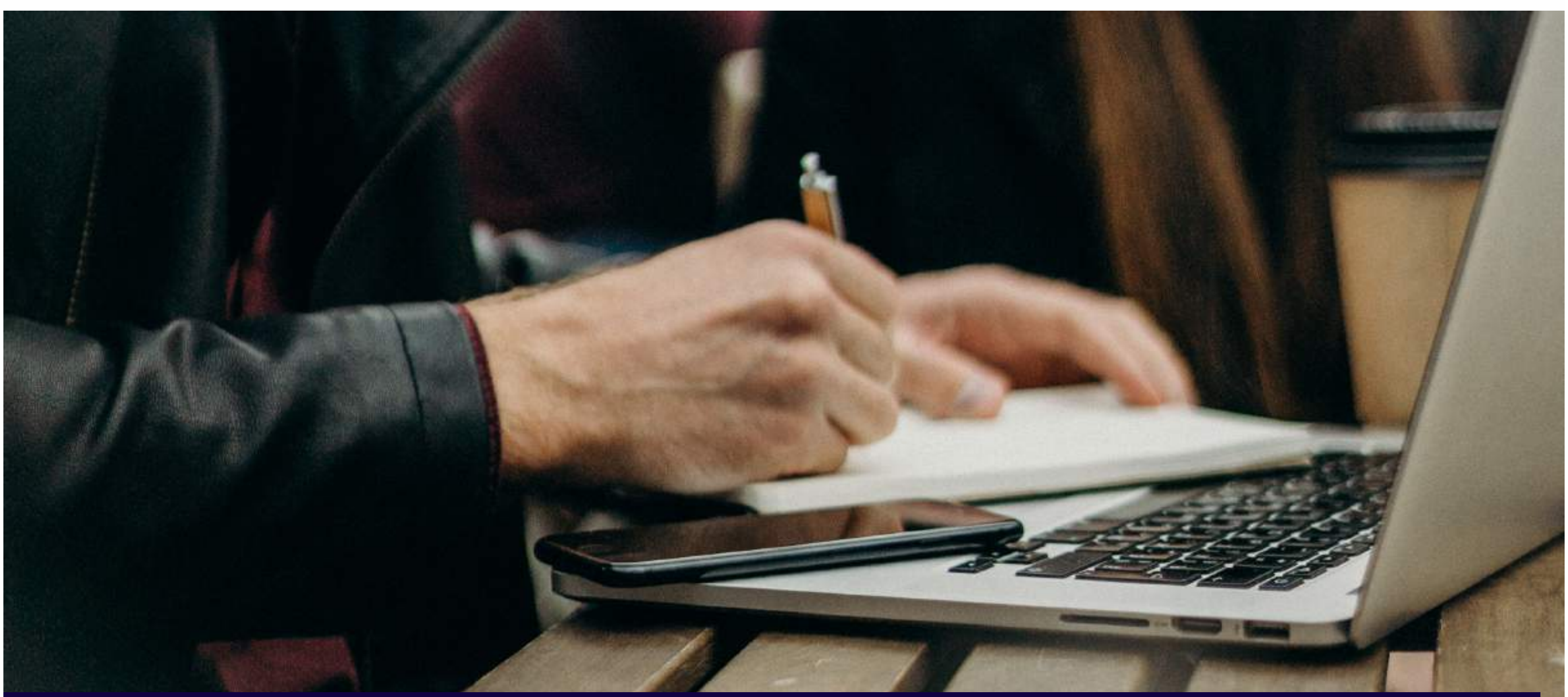
WHAT IS SIZE OF YOUR INCOME WITH RESPECT TO TOTAL ASSETS

Find out the percentage of our total income to our total assets. If we earn Rs.10 lac annually, and own assets worth Rs.1 crore i.e. 10% income ratio, then we have enough assets for our survival. At the same time if we only had assets worth Rs. 20 lac i.e. 50% income ratio, then we depend more on income. Higher the income ratio, higher is the dependence on income, and lower is the risk-taking ability.

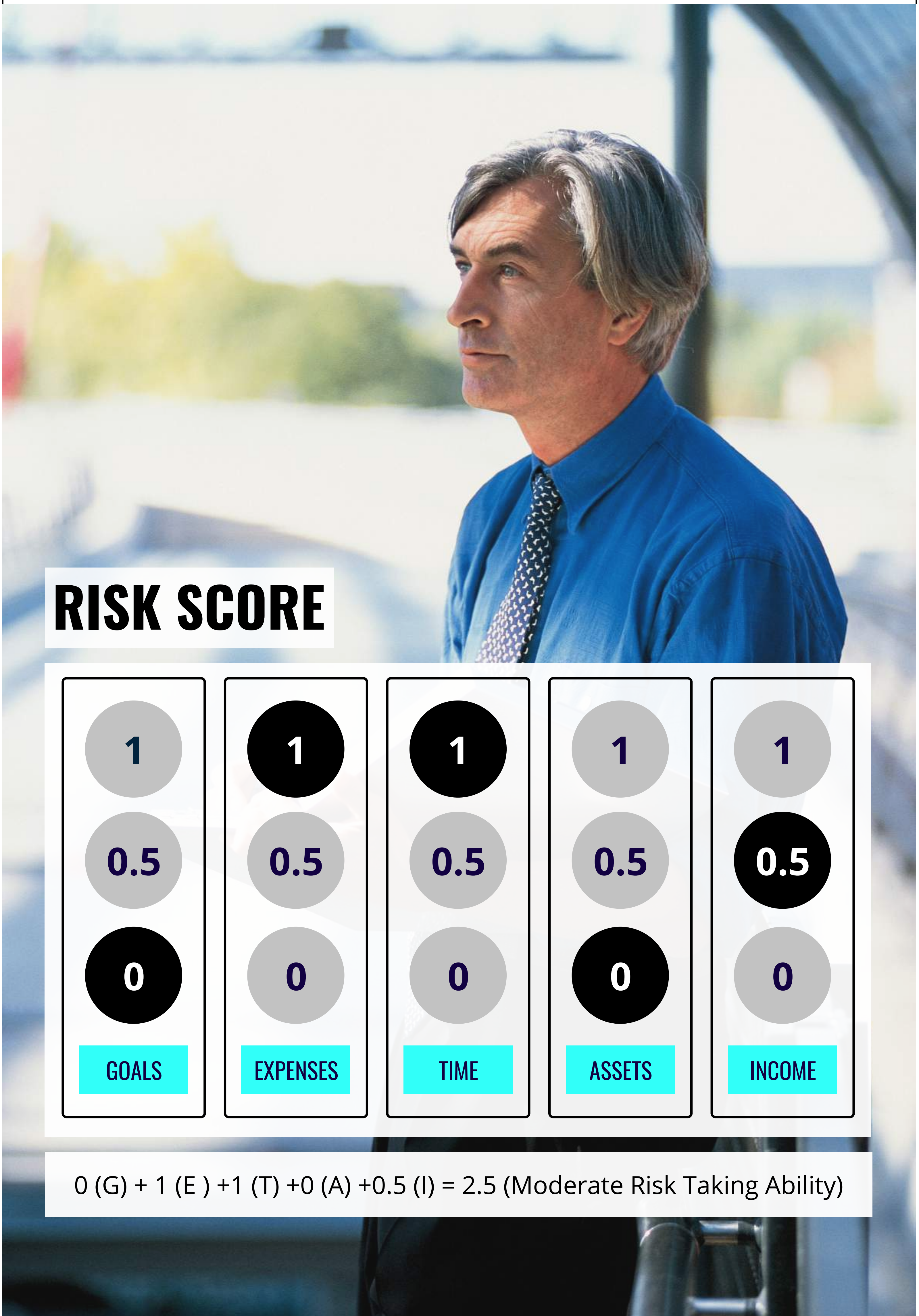
We have covered all the five elements of the G.E.T.A.I. principle. We saw that each of these elements has 2 questions that need to be evaluated. Putting all these together, we can judge our risk-taking ability in a much more objective manner. It is natural to get conflicting answers while evaluating each element. Some factors will say we have high risk-taking ability whereas others will suggest otherwise. The cumulative is what counts the most.

HIGH RISK TAKING ABILITY	**1**
MODERATE RISK TAKING ABILITY	**0.5**
LOW RISK TAKING ABILITY	**0**

We will assign a score of – 0,0.5 or 1 for each of the 5 elements, add them up and the total score out of 5 will determine our Risk Score. For each element, we will check if risk taking ability is low, we will assign 0, if moderate than 0.5 and if high then 1. On adding each 5 elements, if you get a total score of less than 2, you have very low Risk Taking ability, between 2 to 3.5, you get relatively moderate Risk Taking Ability, between 3.5 to 5, we get high risk ability. We will learn in the Planning phase, how to use this Risk Taking Ability Score to decide on assets. In the Lazy Financial Plan, estimate your risk taking ability and leave it at that. This entire exercise should not take more than 15 minutes and do not update Risk Taking Ability very regularly. Do it only once every year or so. Let us look at an example to understand this better before we move forward.



...37 years old, Mahesh Singhvi is the Head of Operations at a Chemical Company. He lives with his wife and son. Let us estimate his risk-taking ability. Most of his goals are important and not very flexible. So he gets a 0 for goals. Next, his expenses are 40% of income and his wife also earns, so he has less financial dependants. So, he gets a 1 based on expenses. Then, the majority of his goals need to be met in 15-20 years and are pretty flexible at the moment. So, we assign 1 based on time. After that, the majority of his assets are not very liquid and only 10% of his assets are in support assets. So, he gets a 0 based on assets. Lastly, his income is pretty stable but his income is 20% of assets currently. So we assign 0.5 based on income. In total we get, 0 (G) + 1 (E) +1 (T) +0 (A) +0.5 (I) = 2.5. Using the GETAI principle, we get a risk score of 2.5 which means moderate risk-taking ability...



RISK SCORE

GOALS	EXPENSES	TIME	ASSETS	INCOME
1	**1**	**1**	1	1
0.5	0.5	0.5	0.5	**0.5**
0	0	0	**0**	0

0 (G) + 1 (E) +1 (T) +0 (A) +0.5 (I) = 2.5 (Moderate Risk Taking Ability)

RISK TAKING WILLINGNESS

Now that we can evaluate our risk-taking ability, the next thing we can focus on is, our 'willingness' to take risks. First, let us differentiate between 'ability' and 'willingness'. Ability to take risk depends on our circumstances and goals. However, willingness to take risks is much more of a 'psychological' factor. It depends more on our preferences and past experiences with different assets, rather than circumstances.

For people in the same circumstances, the risk-taking ability might be the same, but the willingness may vary. It is very subjective and the degree of risk people are willing to take depending on their past experiences with different asset classes varies from person to person. Thus, here we need to assess whether people are willing to take the risk that is proposed by the GETAI principle and the plan even if they do have the risk-taking ability. We will then make changes to the Lazy Financial Plan based on the person's willingness.

As part of identifying our risk-taking willingness, we need to understand the kind of person we are financially. So, before we move forward, answer the given questions.

What kind of a person are you in terms of decision making?

Emotional | Logical

What kind of an attitude do you have towards investing?

Aggressive | Defensive

When we use the term ‘emotional’, we mean that our financial decisions are based on our intuition and opinions of friends and family. Logical decision making means that we evaluate every situation, consider the pros and cons, visit an expert and then take a call. If we do a little bit of both, we need to stop and decide which one is the more prominent method.

Risk-seeking behavior is where a person is open to the idea of taking more risks in anticipation of higher returns. He has comfort for higher-risk situations. On the contrary, risk-averse is where the person is not open to taking higher risks.

	Emotional	Logical
Aggressive	• High Risk Taking Ability • Easily influenced by others	• High Risk Taking Willingness • Not influenced by others
Defensive	• Low Risk Taking Ability • Easily influenced by others	• Low Risk Taking Willingness • Not influenced by others

We need to identify which quadrant we fall into. This will help us in the planning stage i.e. Part 3. Also, know that there is nothing good or bad about any quadrant. Just be honest, people in any quadrant can manage their plan very well.

Our risk-taking ability & willingness may not be the same. In most cases, one is more than others. This is what we do in such situations.

ABILITY < WILLINGNESS

We want to take more risks but our circumstances do not allow us to do so. In this case, we will always follow the lower of the two– our ability to take risks and take fewer risks. Why? We have responsibilities and goals to meet. We will follow the lower risk profile until our circumstances improve.

ABILITY > WILLINGNESS

In such circumstances, we will be allowed to take high risks. Contradictorily, we generally prefer lower risks as we are only comfortable with such investments. We will spend time understanding the higher risk asset classes and start by trying them with small amounts. If even after all this, we are not comfortable with higher risk assets, we will stick to lower risks that we are willing to take. This is because when we are following a financial plan, it has to be followed for years and if we are not comfortable with an asset class that we are invested in and if anything goes downhill, it will just add to our discomfort and the entire lazy financial canvas will not work.

The bottom line is, whenever our ability and willingness are different, always follow the lower of the two. Now we know the optimum risk level that we can take. The risk profile will help us choose assets in the planning stage. With this, we conclude the evaluation of risk.

ROAD BLOCKS

FACTORS THAT STOP YOU FROM FOLLOWING FINANCIAL PLAN AND HOW TO DEAL WITH THEM

6
COMMON ROADBLOCKS DISCUSSED

ZEBRA LEARN

BARRIERS TO PLAN

Using the canvas that we have created for ourselves, we might have created the most perfect plan. Yet, some of us might end up not following it. The entire exercise goes for a toss and despite being aware of the correct decisions to be made, we end up doing other things.

Six major factors are acting as 'barriers', a combination of which is responsible for such behaviour. Let us identify the factors that affect us.

1 ARE YOU IGNORANT OR AGGRESSIVE WHEN IT COMES TO FINANCES?

There is one category of people who are curious, actively learning, and following their financial plan. They spend time and effort to organize their finances. They follow their plan proactively.

The second category of people includes those who are ignorant about their finances, don't follow their financial plan actively, and don't invest time and effort in creating a financial plan.

This is a huge barrier and the most common one that we cross paths with. Those who fall in the second category, find it difficult to plan for this. This is particularly the case with younger people, especially those below the age of 25 who do not have any real responsibility and therefore fail to take their finances seriously. They grow ignorant about their finances. Anyone who is reading this book, will probably not fall under this category.

However, it is very difficult to get this category of people to create a lazy plan for themselves and then make them follow it along. These people then give up their financial planning and with whatever financial resources they have, they start investing the way their parents did or friends do without questioning or understanding if it is suitable for them or not. We see that lack of intent and follow up of the financial plan can make a huge difference in acquiring the financial goals.

THE WAY OUT FOR IGNORANTS

- ACCEPT THE EXISTENCE OF IGNORANCE , IF ANY
- CONSULT FINANCIAL EXPERT
- PUT TIME & EFFORT TOWARDS MANAGING PROFILE AND MONEY

These people should first accept that they are ignorant of their finances. Secondly, they should meet a financial expert instead of following a family member's or friend's way of managing money. However, there is a risk of the plan being subjected to influence by the incentives that the financial expert is getting. Selecting the appropriate expert could be quite a challenging task but with the right selection, then the financial expert will guide them and take care of the more important decisions on their behalf.

It is recommended for them to put more time and effort into deciphering their financial profile and managing their money. Do not leave your financial management to luck, take active responsibility and start managing finances.

When creating a Lazy Plan, we should identify and take into account if we are an ignorant person. Also, it would be best to conduct this entire exercise under the guidance of a financial expert. We cannot change ourselves overnight but we can systematically handle the same. This is how someone ignorant about finances can best prepare themselves to handle the issue systematically.

Remember, creating a little less perfect plan that is followed is better than creating a perfect plan that is not followed at all.

HOW SUPPORTIVE YOUR FAMILY IS IN YOUR INVESTING DECISIONS ?

2

The next barrier that arises in following a financial plan is an uncooperative and unaccommodating family that is disregarding our Financial Plans. This is particularly a problem that young people face. Someone who has just taken up a job for the very first time formulated a customized plan and is now trying to execute it might face resistance from the family.

It takes a person several years to get comfortable with an asset-based on their experience. For instance, some are very comfortable with the idea of investing in stock markets whereas others are not. This is because stocks worked out well for some whereas not so well for others.

Some are more comfortable with stocks, others with real estate, yet others with fixed deposits and some only with gold. So, when a young person comes in with their new ideas they are often met with resistance if the elders in the family have not had a good experience with that kind of assets in the past or simply negative comments and stories about the same.

The problem is much bigger in joint families where decision-making is vested with different people and the lines of communication are generally not very open. At other times, resistance can come from others in the family such as wife, parents, children, etc.

Let us see how we can handle this. First and foremost, acknowledge it. If our family does not support our financial plans, we must accept it and discuss the same with family members.

Secondly, it would be smart to get them on-board and win their support through education, consulting, and experimentation. It would be wise to show them the back-calculation or logic of the plan, its expected fruitfulness, the assumptions that we have made, and how they have turned out in the past.

We could get them books, courses, and educative courses to understand different asset classes. However, this does not work with everyone as the family members might not be willing to spend time on the same. However, if we constantly expose them to books and courses, they might consume some parts of it. This opens up their minds about new asset classes.

Thirdly, get them to talk to consultants. Sometimes, people turn a blind eye to something being suggested by a family member but believe in it when proposed by an expert. Hence, a 2-hour consulting session with an expert should help open their minds towards our financial goals. However, to act on it, they might need 3-4 consulting sessions.

All these will open up their mind for experimentation. Experimentation means investing in an asset class as an experiment rather than an investment. So, we begin by investing Rs. 1,000 in the equities. This will not be anything meaningful from an investment perspective but it will be a start. Over time, we can increase our investment in the asset class as comfort and support from family increases. Win their support by logic and not by emotions. It takes around a few months to a year but in most cases, it works.

3

HOW SIGNIFICANT IS THE IMPACT OF SOCIAL PRESSURE ON YOU?

The third common barrier that stands in the way of people following their financial profiles is the impact of social pressures. Society and the people around us influence the financial decisions that we make. We are often bothered by 'what will people say' while making a financial decision. It forces us to buy cars bigger than we can afford, houses bigger than we need, and throw parties more lavish than we can afford.

Let us face it. There is not a lot that we can do about social pressures. Human beings are social creatures and we live in a social world. People want to be liked and accepted, they need a sense of belonging and therefore maximizes the chances of succumbing to social pressures. We can't live in ignorance.

Also, another school of thought portrays the ability to ignore social pressures as a symbol of strength. This is completely irrelevant. Social pressure is something very natural and it should not be perceived as a means to determine strength or weakness.

The very first thing that we will do is accept that we are influenced by social pressures. And because we intend to plan for a realistic world, our plan will take into consideration all the social pressures.

To include the impact of social pressures, we will go back to our list of goals and increase the amount of each goal such that it helps us meet social obligations as well. Each goal doesn't need to have a social pressure component. For instance, a child's wedding-related expense will have a social pressure element but a child's education will not have any social pressure element. We will do this right away.

One pitfall is that people fail to draw a line at the right place. We often stretch ourselves far too much in the name of social pressures which is a terrible idea. For instance, if we can buy a car worth Rs. 5 lac, we might stretch the same to a car worth Rs. 8 lac to cope with social pressure. However, if we start stretching ourselves for a car worth Rs. 20 lac then that won't be acceptable. This way, we will never be in a position to meet our financial goals. So, we have to be realistic and build a plan that can be implemented.

Rs. 5 LACS

Rs. 8 LACS

Rs. 20 LACS

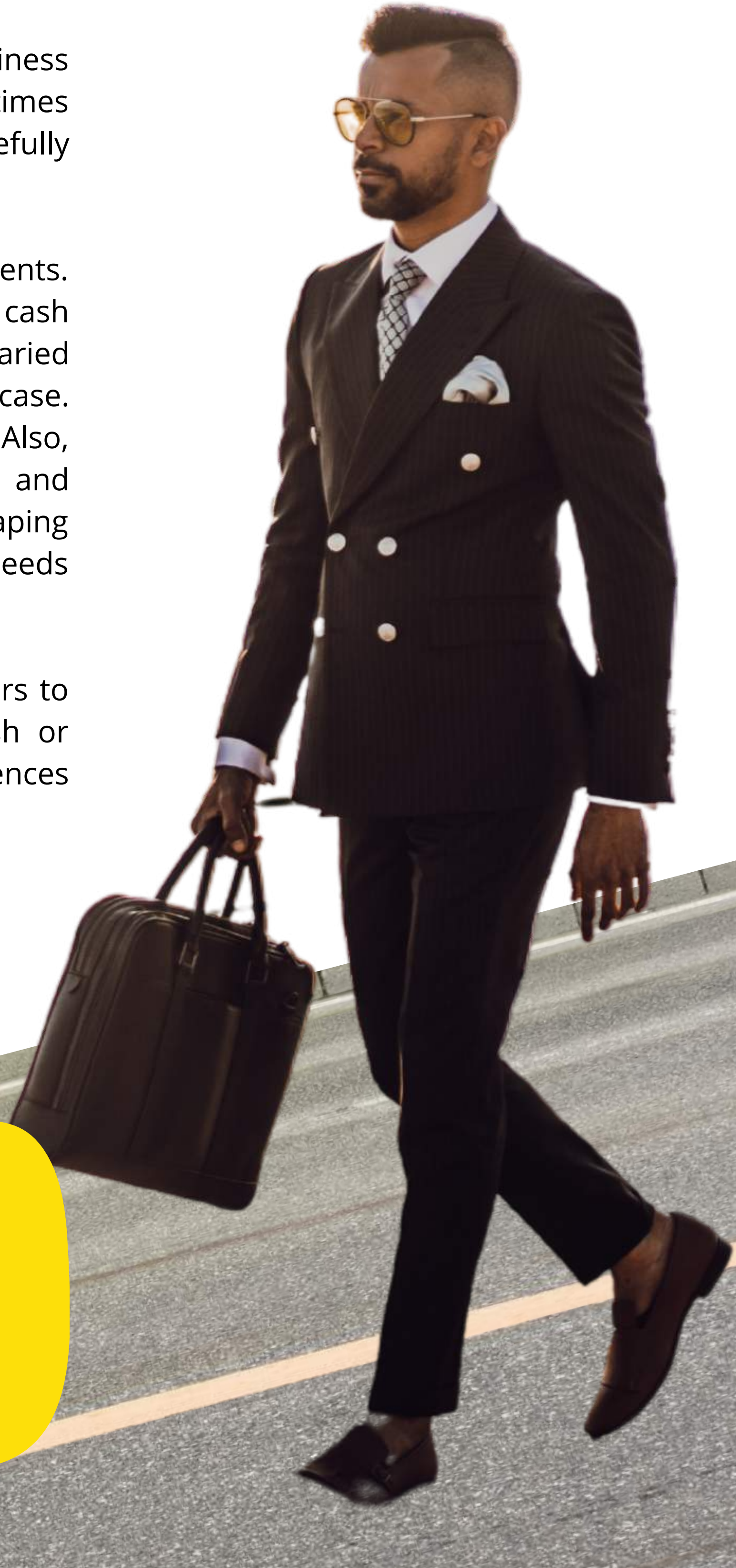
We can systematically deal with social pressures and their impact. Not with aggression but with careful acceptance and profiling and careful planning. Social pressures should be built in the lazy financial profile and Lazy Plan itself.

4 WHAT IMPACT DOES OWNING A BUSINESS HAVE ON YOUR PERSONAL FINANCE?

Business owners have to keep up with the business needs as well as personal finance needs. Also, at times they use their business as an excuse to not carefully plan their finances.

Business owners have different financial requirements. First, most financial models assume constant cash inflow throughout the year. This suits the salaried people but for most businessmen, this is not the case. In businesses, some years are better than others. Also, different businesses are at different stages, and accordingly, they play an instrumental role in shaping our financial profile. Hence, personal financial needs should be balanced with business financial needs.

We will evaluate our business on a few parameters to understand whether the business produces cash or consumes cash. This will have significant consequences on our cash flow.



EXCUSES

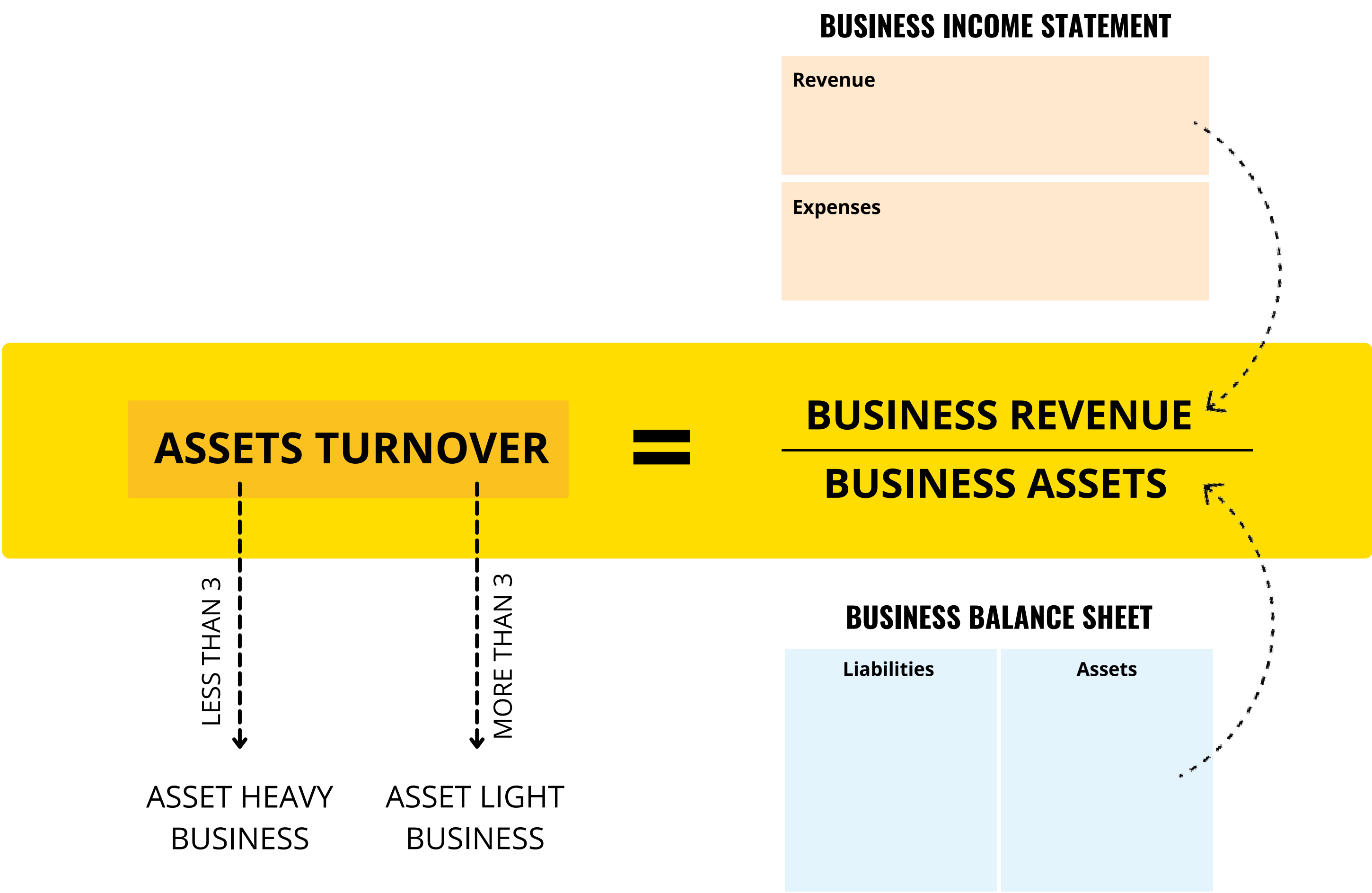
- Business was not good this year
- Earnings re-invested into the business
- No need for personal finance plan as business will fund us when required.

EVALUATION OF BUSINESS

IS THE BUSINESS ASSET HEAVY OR ASSET LIGHT?

To understand its capital requirements, the very first question to ask a business is whether it is asset-heavy or asset-light. Asset-heavy businesses are those that need a lot of assets like machines, land, building, etc. to conduct operations. For example, cement manufacturing plant, textile knitting unit, truck logistics business, etc. These businesses need a lot of assets to operate and thus require a lot of capital to be functional.

At the same time, some businesses do not require that many assets like in the case of marketing firms, legal firms, software companies, etc. So, the first thing that we will do is decide whether our business is asset-heavy or asset-light. We do so using a ratio called the 'asset turnover ratio'. This is calculated by dividing business sales by total business assets. If the business has assets worth Rs. 50 lac in business and can sell products worth Rs. 1 crore in the year, then the asset turnover ratio is = 1 crore / 50 lac = 2x. If the asset turnover ratio is less than 3, we will categorize our business as an asset-heavy business and if it is more than 3, we will categorize it as an asset-light business. This will help us identify how much capital does the business need going forward.



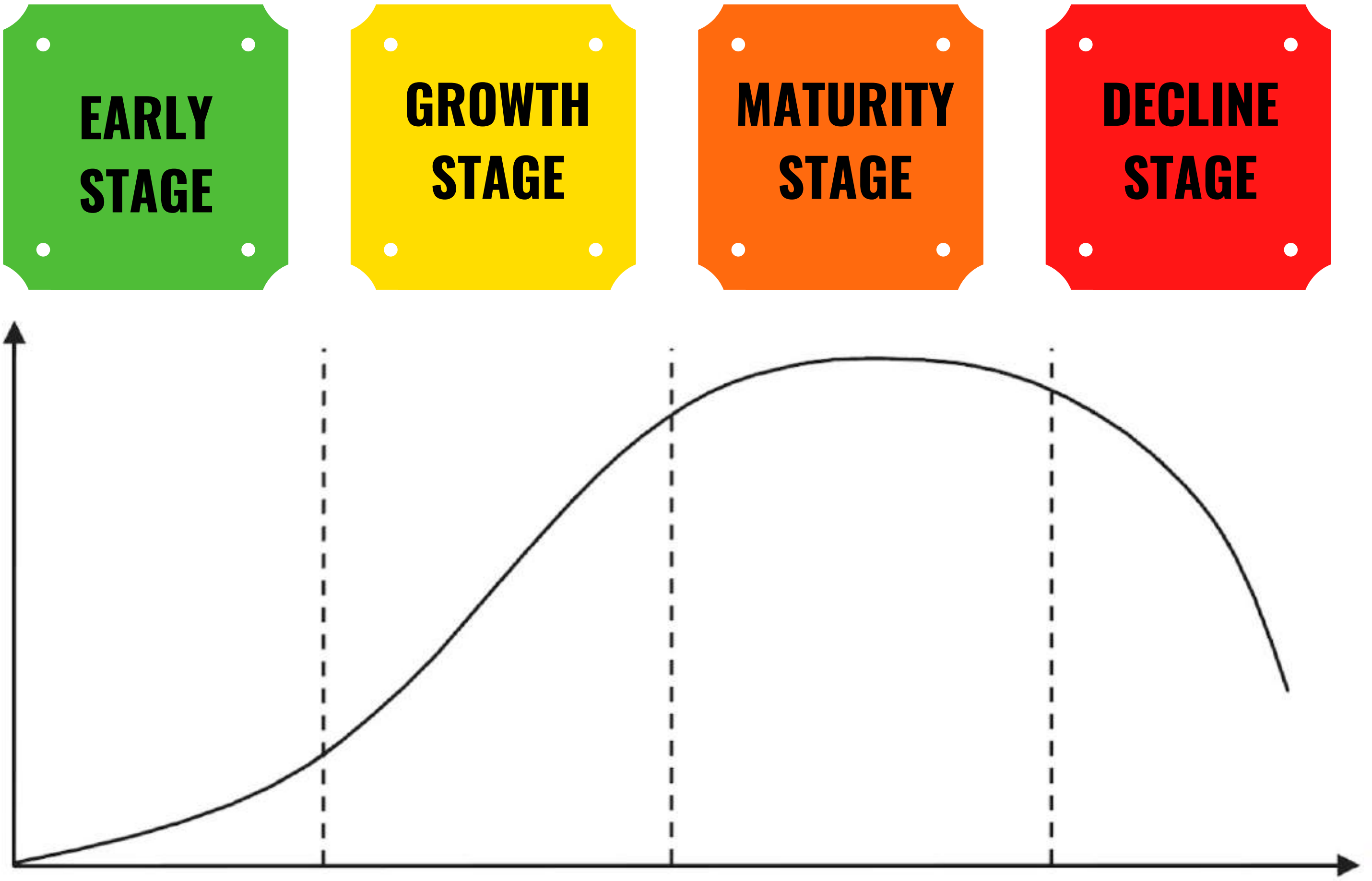
IS THE BUSINESS SEASONAL OR NON SEASONAL?

Some businesses conduct a majority of their sales in certain months of the year. For instance, travel and event businesses carry out intensive and maximum business over a few months. At the same time, essential products, schools, hospitals, etc. are in business throughout the year. We need to identify if our business is seasonal or constant throughout the year.

During the months of peak work, seasonal businesses, require additional capital investment whereas, in the dull months, capital gets free and sits idle for a few months. This has significant implications on our lazy finance profile.

WHAT STAGE IS OUR BUSINESS CURRENTLY IN?

Typically, a business passes through 4 stages -Early stage, growth stage, mature stage and lastly, decline stage. We need to understand which stage is the business currently in.



Early-stage refers to the very early days of any business, primarily when the business has just taken off and the product has just been launched. At this stage, we are making investments from our pockets and the business is not making any money. We will draw on our assets or savings to sustain us during this period if we have already quit our jobs.

The second stage is – growth stage. In growth stage, we are still putting in money from our end. The business has started earning money and the business is growing rapidly. The money made by the business is being re-invested in the business. At this stage, we can also consider an outside to fund our business. Till this point, the business consumes money and is not in a stage to release money.

The next stage is – mature stage. Now the business has grown and has captured good market. All the functions of the business are well funded. There is not much room for the business to grow in the same space. If our business is at a mature stage, we can expect that the business does not need any further investment from us. The business would be giving us steady cash outflow. Here, we can depend on the business to fulfil our financial needs.

The last stage is the decline stage where the businesses start failing. This could be because some other product, competitor, or business model is gaining prominence. We try to make changes to the business so that it can survive longer. Here again, the business is in a position to provide for profits and a lot of assets tied up with the business get free at this stage.

We can see that businesses in the early-stage and the growth-stage will not be able to support us financially. They will need investments from us directly. In the mature stage and decline, the company will pay out a lot of profits. Also, it is during this stage that a lot of capital tied to the business is freed at this stage.

For any business owner, we first profile their current business to understand their cash flow consequences and the capital requirement of their business. We study to realize the time for which the business will need money from our end and the time after which can we start expecting returns. We saw how capital-intensive businesses require more money to grow, seasonal businesses have seasonal swings in the capital and lastly, the stage of business determines how the cash flow of the business is expected to behave. All these factors have severe consequences on our business. Considering these factors, a person should profile as per their business.

5 HOW STRONG IS YOUR FEAR FACTOR?

The next barrier that comes in the way of people following their financial profiles is the fear factor. The fear factor is the psychological discomfort that we have about things not working according to plan. We might have had a bad experience with a particular asset class in the past and because of that, we fear the asset class for the rest of our lives going forward. We fear that someone might cheat on us with the financial investments we make. We fear that someone might run away with our money. All such fears that we have in our minds often lead to uncertainty.

This is the fear of the unknown. This, once again, we will solve with education, consultation, and experimentation. Education is going through as many blogs, books, courses, seminars, etc. about the subject as possible. Consultation means talking to experts about the subject. Our fear will not go away overnight. However, if we are not rigid about the process and engage ourselves in this repeatedly, our mind will start becoming more open to change. If we understand the backend calculation for different asset classes, we will start getting more and more comfortable with them.

The next step is experimentation. Start experimenting with the asset class with Rs. 1000 or Rs. 500 or whatever amount that does not bother us. Think of this money as already lost and track for a few days.

As and when we get more comfortable with the asset class, we can start to increase the amount of money being invested in the asset class. We will start small and then increase investments as our comfort increases and fear reduces.

This is how we systematically deal with the fear factor. At this point in the profile, we need to write down asset classes that we are strongly biased against for whatever reason. Fear often pushes us towards inactivity. The key is to get up and get started. Getting started, even if it is small, makes the difference as with time the comfort only grows.

HOW SIGNIFICANT IS THE ROLE OF 'BLACK MONEY?

6

The last barrier that comes in the way is black money. Every financial planner, course, and book completely ignores black money and its impact on the personal financial plan as if it does not exist. According to them, black money is not an ethical way to make money, which is correct. However, this does not make it any less real. To make the Lazy Financial Plan effective, we will have to discuss some key facts about black money and see its benefits and limitations.

LIMITATIONS OF BLACK MONEY

BLACK MONEY LIMITS INVESTMENT OPTIONS

The first and biggest limitation from a Lazy Financial Plan perspective is that it limits investment options. We cannot invest a sizeable amount in equities, mutual funds, bank fixed deposits, etc.

On looking around, we noticed that there are only three asset classes, where sizeable black money is being invested–real estate, gold, and lastly personal loans to the people we know and trust. Now, each of these asset classes has specific problems. First, the government introduced RERA for real estate and compulsory PAN registration to buy gold. So, these regulations make it difficult to invest black money in these asset classes. Lastly, personal loans which include black money cannot have attached paperwork to them and therefore offer no legal way to get the money back if the borrower refuses to pay it back. So, this is the first and biggest limitation of black money from a personal finance perspective.

BLACK MONEY IS UNPREDICTABLE

Whenever we plan for a future goal, we invest for a long time knowing that we will meet the goal with some predictability. However, with black money that is not the case. We might save for many years, but something untoward can take away the entire effort and we might not have the resources to meet our goals despite planning for it. The government can change rules and norms that make it difficult to invest or spend black money, they can carry out exercises like demonetization, or even events like IT raids can take away our money. Thus, we can say black money is highly unpredictable and there is a real risk that it might come across as futile to meet our goals.

SPENDING OF BLACK MONEY IS A CHALLENGE

Spending black money could be pretty challenging at times. Let us say a major expense is coming up; we need to pay for our child's education and the amount is significant. We might have the amount in the form of black money, however, we will not be able to pay the same. It is difficult because the amount is big and will show in our bank account which will bring us under the radar of Income Tax (IT)authorities.

Also, we are only talking about these limitations from a financial perspective. We have not even spoken about the legal and ethical downsides of black money. If it does not make sense financially, there is no point to discuss legal and ethical problems.

BENEFITS OF BLACLK MONEY

The first and biggest benefit of black money is that we can avoid paying taxes to the government and hence save the amount. The saved amount can be used to pay off expenses and liability in the near term. For instance, if a major expense is coming up in 1 year or less, we are effectively only taking the risk for one year that we will not come on the radar for IT companies. However, if we get caught, there are huge legal and ethical implications attached to the same. There are a great dilemma and financial stress attached to it. Thus it is now up to us if we want to risk jail, penalties, and not meeting our financial goals to save some taxes and create a loophole in our financial plan. Also, if we see, the biggest of the big investors have not expanded their wealth using black money. They have grown by keeping their asset options wide open. We call black money 'a train without an engine'. It might be the longest and biggest train, but without the engine, it will take us nowhere. It looks good in the short term as we save on taxes, however, the money does not grow at a fast pace going forward and therefore the result of the return is lower than the legitimate money.

Mr. Paul had Rs 1 lac. He did not pay taxes and had invested in gold where the return was 3-4 % p.a. At the end of 10 years, his amount had increased to Rs. 1.34 lacs.

Mr. D'souza had Rs. 1 lac.He had paid 30% taxes and therefore had Rs.70,000 left. He had invested this amount in mutual funds with an average return of 12% p.a. At the end of 10 years, he had Rs. 2.17 lacs.

Why this difference? Mr.D'souza had multiple asset options left where he could invest, which was not the case with Mr.Paul. He only had 3 asset classes where he could invest. In the short term Mr.Paul was happier as he saw that he saved Rs. 30,000 in taxes. However, as we saw, it is a train without an engine and therefore got him nowhere whereas Mr.D'souza had higher amount despite paying taxes as he kept his options open. Legitimate money can grow at a really fast pace and in a scalable manner. Black money has financial limitations, ethical and legal implications and all of that with a risk of Financial Plan being ruined completely and even potentially attracting heavy fines and penalties. Our stand about Black Money is pretty clear, it is for each individual to decide where they want to stand.

We do realize that 2-3 pages on black money will not miraculously make people change their behaviour and it is a very secretive subject for most people. However, it is important to know the financial, legal, and ethical implications of the same and then take a call. We do not encourage black money. Those who decide to continue with it are opting to commit major blunders. Those who decide to switch might consider a voluntary disclosure. That is beyond the scope of this book, and they will have to consult an expert that they trust to help them with it.

We have understood the 6 reality influences or 'barriers' that comes in the way of people following their lazy financial plan. We have seen how to deal with them systematically and make them a part of our Lazy Plan. These barriers take time to overcome but this is the hard part which once overcome, makes it easier to follow through the rest of the Lazy Financial Plan.

CONCLUSION

With this, we come to the end of our profiling stage. We have successfully filled out the lazy financial canvas for ourselves and created a tailor-made profile for ourselves. This is as good and elaborate as any professional does. Now going forward, we will understand the different asset classes and then create a Lazy Financial Plan for ourselves. If so far, there is any confusion, do not worry. When we create a plan, we will see everything falls in place perfectly. So, let's hop onto the next section.

ZEBRA LEARN

EQUITY, FD, BONDS, MUTUAL FUNDS, PPF, EPF, AND MANY MORE DISCUSSED

THE ASSET MAZE

WHICH ASSETS TO BUY, WHEN AND F0R HOW MUCH?

TABLE OF CONTENT

LET'S BEGIN

Congratulations! We have finished the heavy lifting upon readying our lazy personal profile. It was indeed the most tricky segment due to its ambiguity. Once done, we will understand the asset classes, and lastly, we will put everything together with a lazy financial plan.

When we say asset classes, we mean the different types of assets like gold, stocks, bonds, fixed deposits, real estate, etc. Each asset class behaves in a certain way, suits different people, has a different risk profile, and so on. We will understand their working, risks, and returns that can be expected, basic terms relating to the same, suitability, tax treatment, etc.

If we do the first part well i.e. profile ourselves well and understand the asset options that we have, the planning stage will play out simply. We will cover multiple asset classes as well as insurance types in this section. Let us get started.

01

FIXED DEPOSITS

FIXED DEPOSITS

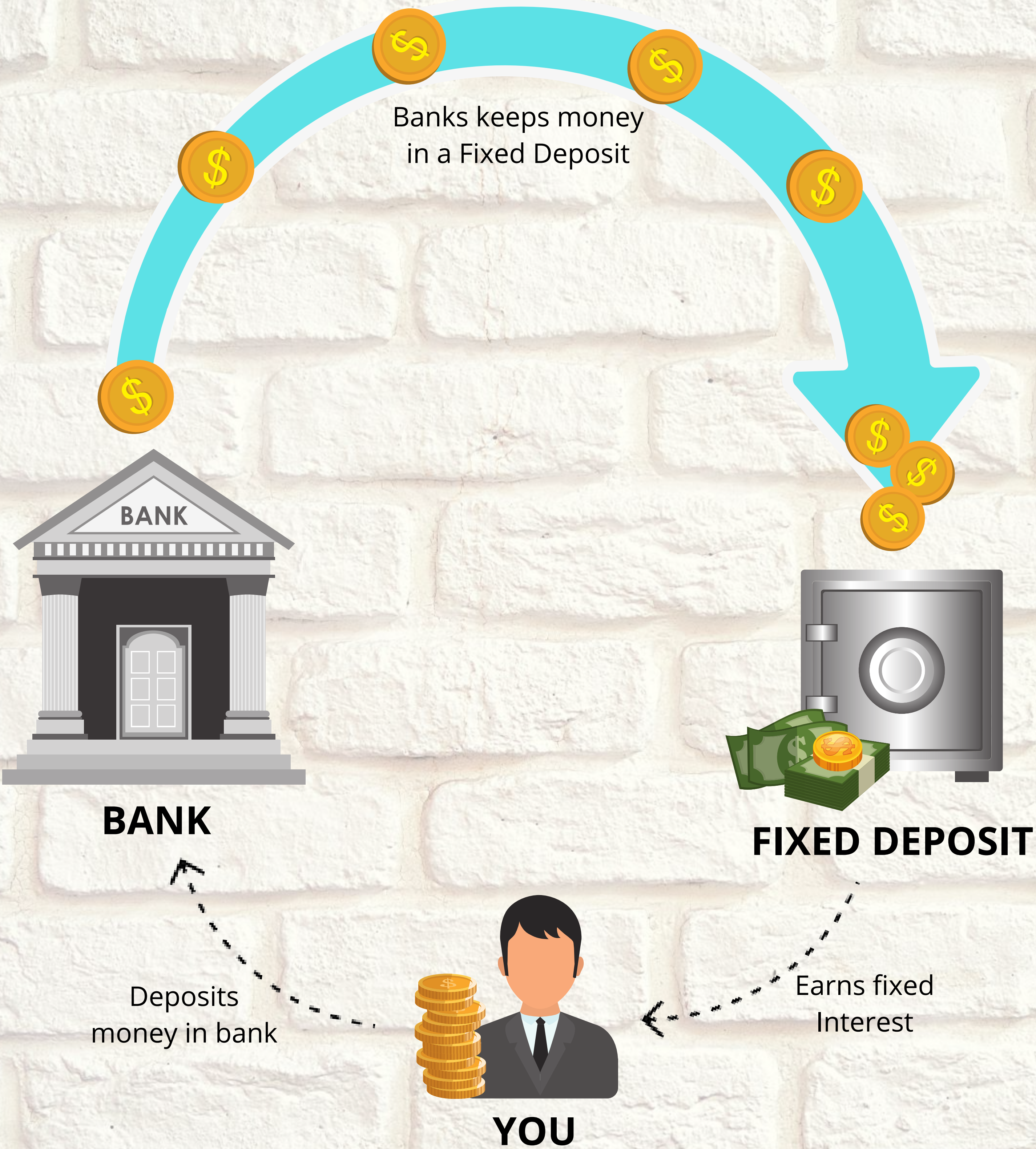
Fixed Deposits is one of the most standard and commonly understood asset classes. When money is deposited for a fixed period with a bank or a company at a fixed interest rate, it is referred to as a fixed deposit.

The time and the rate of interest are fixed and hence, the name 'fixed deposits'. Fixed deposit is one of the simplest investment options where everything can be pre-determined. It is like giving away the money as a loan to a company i.e. in this case, lending to the bank.

*Tenure: 12 - 60 months

Banks	General citizens' FD Interest Rates*	Senior Citizens' FD Interest Rate*
BAJAJ FINSERV	6.10% - 6.60%	6.35% - 6.85%
pnb Housing Finance Limited	6.00% - 6.50%	6.15% - 6.95%
HDFC BANK	5.85% - 6.25%	6.10% - 6.50%
SBI	2.90% - 5.40%	3.40% - 6.20%
IDFC FIRST Bank	2.75% - 6.00%	3.25% - 6.50%
AXIS BANK	2.50% - 5.50%	2.50% - 6.05%

Source: https://www.myloancare.in/fixed-deposit/fd-interest-rates/


Banks keeps money
in a Fixed Deposit
BANK
BANK
FIXED DEPOSIT
Deposits
money in bank
Earns fixed
Interest
YOU

HOW DOES IT WORKS?

We select the time horizon that we are looking to invest for. Then we see different banks and companies that are offering fixed deposits for that time frame and then the one that offers the most attractive return is the one where we invest. However, an important factor to consider is the health of the bank/company with whom we are making the deposit.

CAN THE MONEY BE WITHDRAWN BEFORE MATURITY?

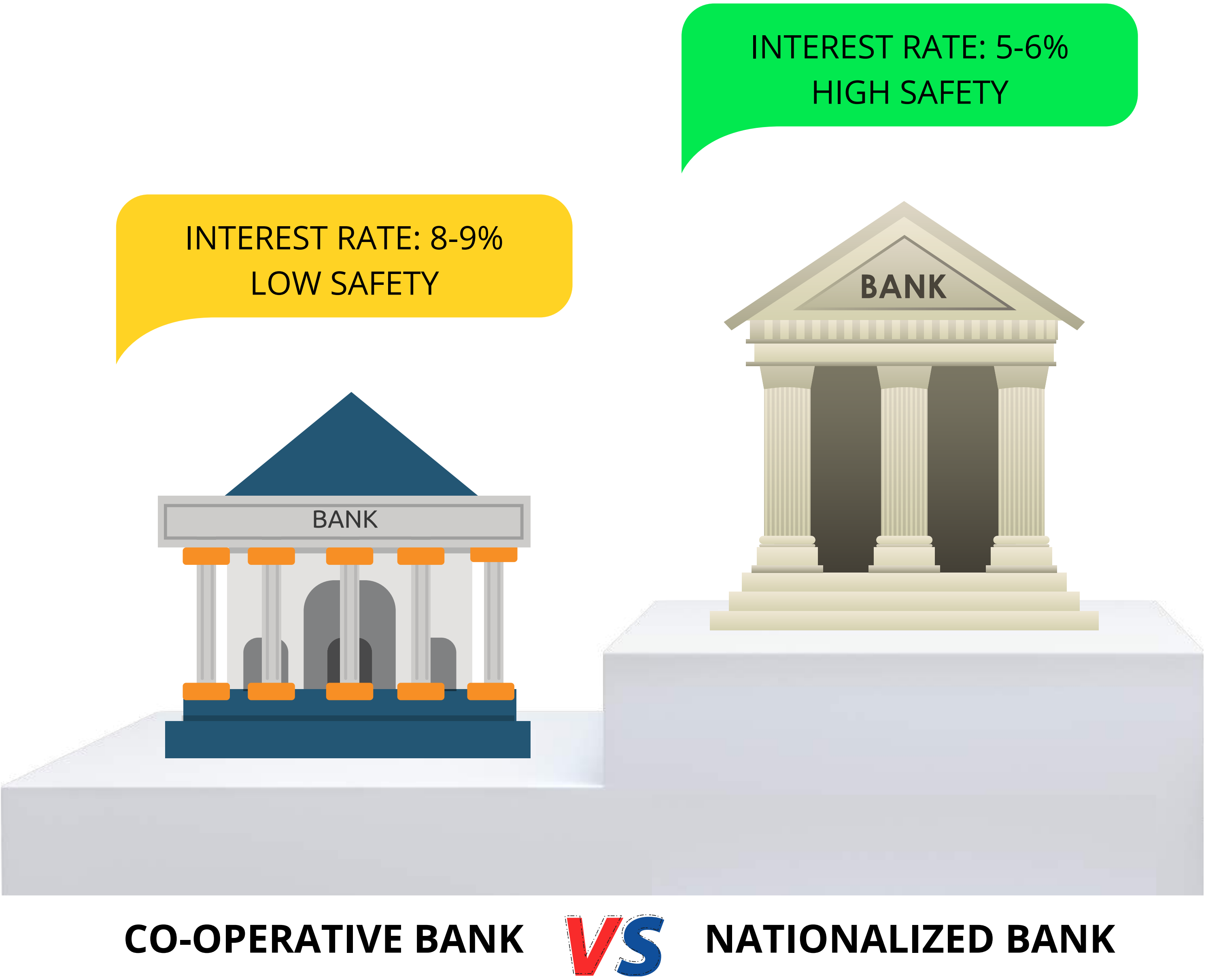
In most fixed deposits, money can be withdrawn before maturity. This is called premature withdrawal. Some companies charge a small penalty for this whereas others do not. So, fixed deposits are one of the most liquid forms of investments that can be converted to cash at very short notice.

WHO IS SUITABLE FOR THIS?

The primary purpose of fixed deposits is to maintain the purchasing power of money. This means that in the long term we can expect fixed deposit returns to be in line with the inflation rate (CPI Index). Secondly, it is a very liquid form of investment. So, a fixed deposit is a good asset class for emergency funds, short-term cash needs, or any major expense that is coming up within a time frame of less than one year. Fixed deposits are mainly for the stability and safety of capital and not the growth of capital. When investing with a time horizon of more than 5 years, fixed deposits is a complete NO since it does not grow capital. Also, for those who have high risk-taking ability, fixed deposits do not make a lot of sense.

As we saw earlier that fixed deposits are like lending money to the bank. Therefore, it is important to check the health of the bank or company before we give/lend them the money. The nationalized banks and larger established companies would be accepting deposits at 5-6%. At the same time, small banks, co-operative banks, private players like Big Bazaar would be offering 8-9% for the same deposit. In all these cases, we will opt for a nationalized bank with lower returns.

Co-operative banks, regional banks, rural banks are all unsafe and there have been many cases of these banks shutting down in the past. Those who offer a higher rate of interest do so to attract depositors. We do not want to keep our money with banks that face the risk of shutting down even if they offer higher interest rates. Remember, the objective of fixed deposits is the safety of capital rather than its growth. Also, with fixed deposits, we are dealing with short time horizons. So, a 2% difference for 2 years would not impact our ability to meet a goal.



RBI cancels licence of Karad Janata Sahakari Bank

PTI | Dec 8, 2020, 23:41 IST

A- A+

MUMBAI: The RBI on Tuesday said it has cancelled the licence of The Karad Janata Sahakari Bank Ltd, Karad, Maharashtra, as it does not have adequate capital and earning prospects.

BusinessLine

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Money & Banking

13 co-op banks turned insolvent last fiscal

PTI New Delhi | Updated on May 27, 2013 | Published on May 27, 2013

As many as 13 cooperative banks failed in 2012-13, resulting in credit insurance company DICGC paying nearly Rs 160 crore to depositors.

Among the 13 cooperative banks, which failed to repay deposits to customers, nine are from Maharashtra, two

mint

A view of closed CKP Co-operative Bank after RBI cancelled its licence, during the nationwide lockdown to curb the spread of coronavirus, in Mumbai (Photo: PTI)

Over 1,100 customers to lose out in CKP Co-operative Bank's liquidation

3 min read . Updated: 04 May 2020, 07:18 PM IST

Shayan Ghosh

- These customers are those who have deposited more than ₹5 lakh in their accounts
- RBI cancelled the bank's licence citing its highly adverse financial position

RBI cancels Mapusa urban bank's licence

Newton Sequeira | TNN | Updated: Apr 17, 2020, 15:21 IST

Goa tourism's marketing has big budgets but due to lack of vision, it is not result-oriented, say tourism stak... Read More

PANAJI: Pulling the p one of Goa's oldest cooperative banks, th Reserve Bank of India Thursday cancelled M Urban Co-operative B (MUCB) banking licen paving the way for its liquidation since mult attempts at the merg have failed.

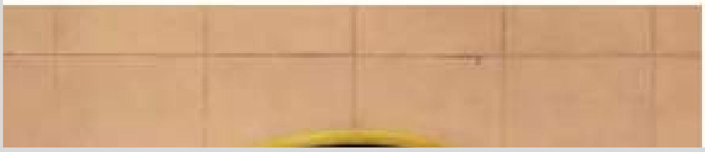
According to sources can appeal against th

RBI bars People's Co-operative Bank from granting fresh loans, accepting deposits for six months

PTI

MUMBAI, JUNE 12, 2020 10:31 IST
UPDATED: JUNE 12, 2020 10:38 IST

SHARE ARTICLE | 1 | PRINT | A | A | A



These directions will remain in force for six months from the close of business on June 10 and are subject to review, the RBI said

In 2020, RBI has put 44 co-operative banks under watch. How deep is the rot?

In April alone, the RBI acted on nine co-operative banks. This included the cancellation of licence of Mapusa. The RBI found that the bank did not have adequate capital and earning prospects and its continuance would be prejudicial to the interests of its depositors.

INTEREST RATE

Check the interest rate to match the time horizon

PREMATURE WITHDRAWAL

If the premature withdrawal restrictions are too rigid, we will ignore those deposits

SAFETY OF THE CAPITAL

We will only go ahead with Nationalized banks or established private banks instead of co-operative banks

TYPES OF FIXED DEPOSIT

CUMULATIVE DEPOSIT

Interest is added to the amount and the entire amount including the interest is paid at maturity.

PAYOUT DEPOSIT

Interest is paid into the corresponding bank account every month or every quarter based on the mandate.

POST MATURITY INSTRUCTION

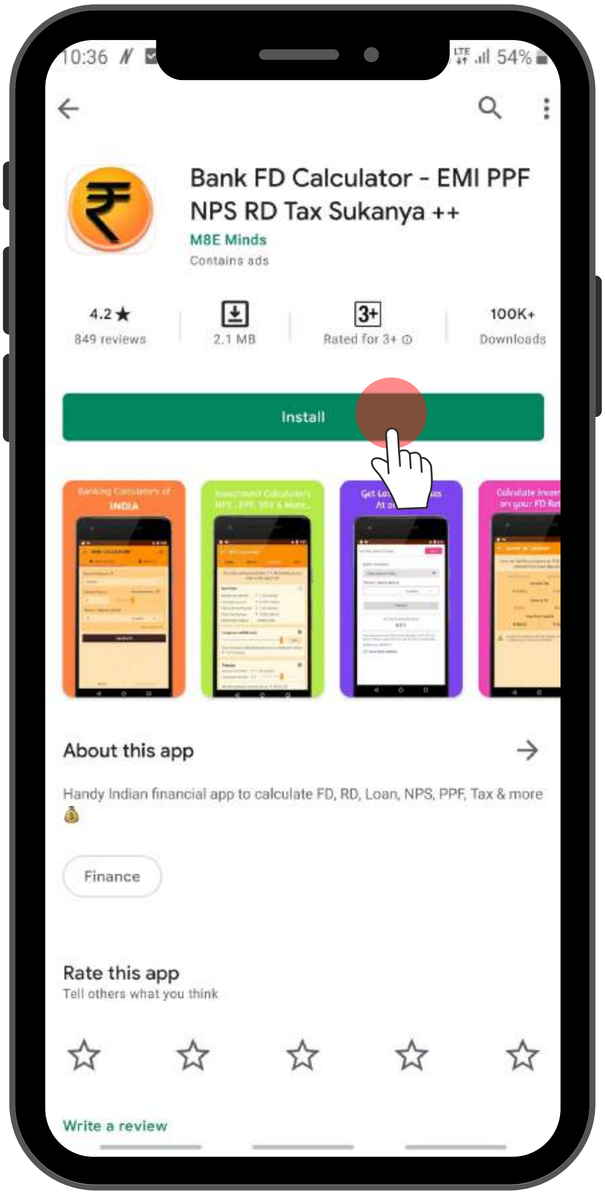
RENEW PRINCIPAL

It converts the maturing Fixed deposit into a new deposit on the day of maturity.

REDEEM PRINCIPAL

It release the money in the registered bank account with the bank.

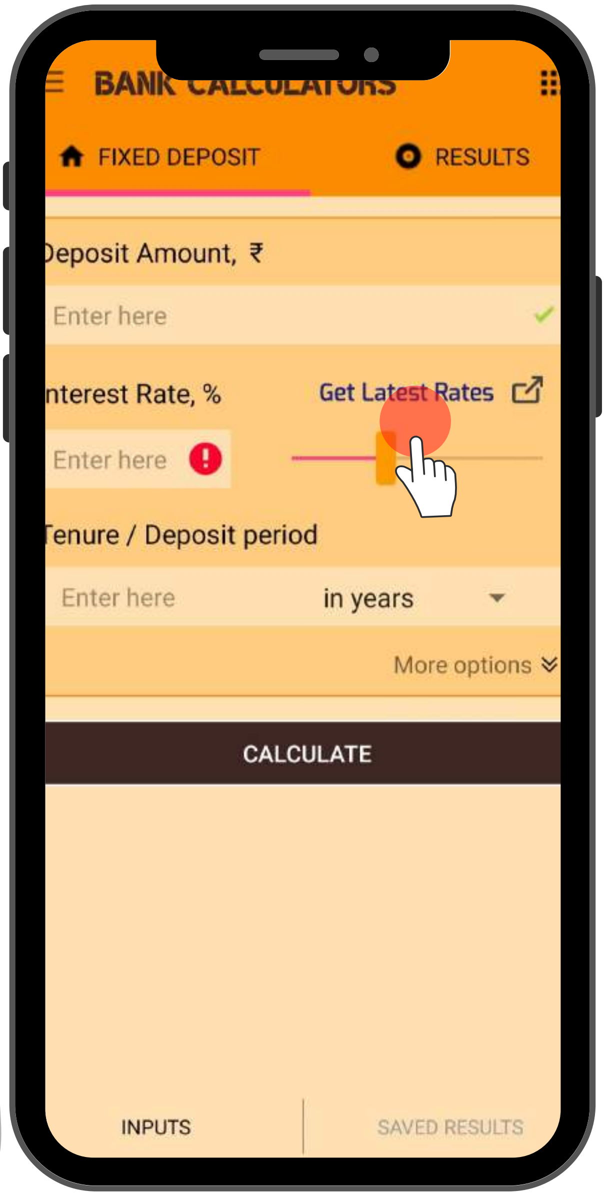
HOW TO SELECT A FIXED DEPOSIT?



1

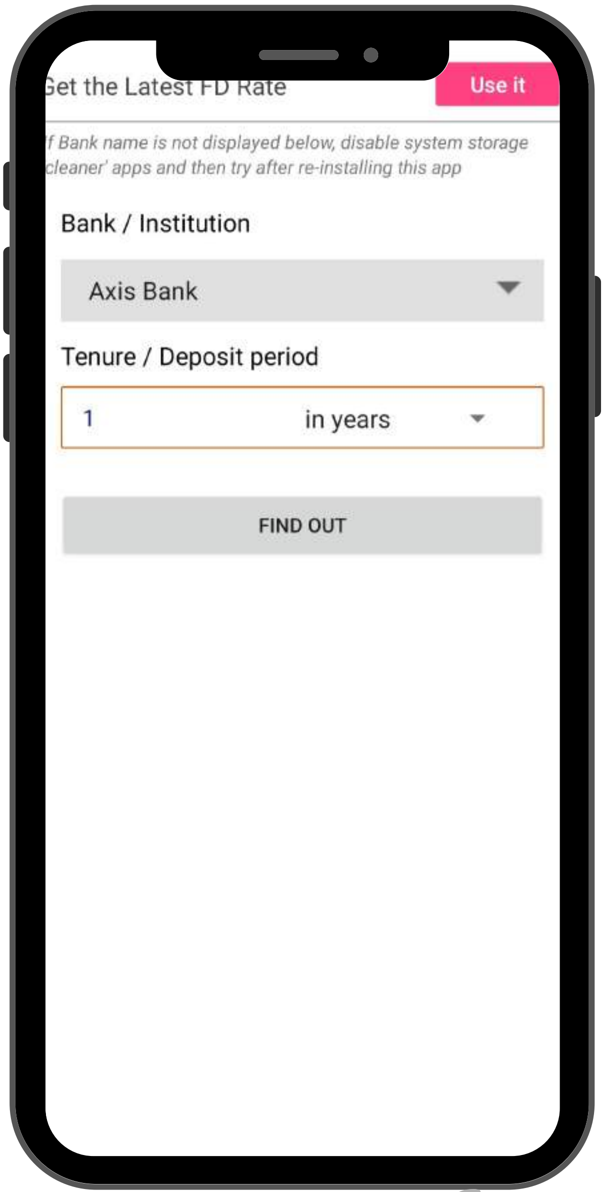
DOWNLOAD AN FD CALCULATOR APP

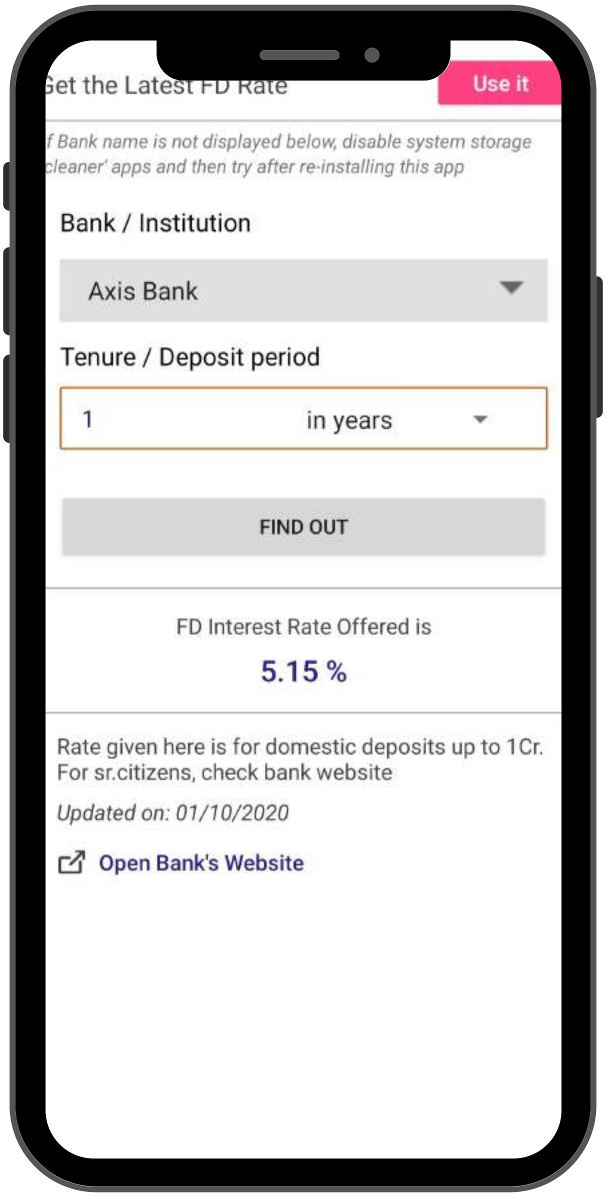
Download an FD calculator App: The one we will use currently, only for fixed deposits, is –'Bank FD Calculator' by M8E Minds.



GO TO 'GET LATEST RATES' OPTION ON THE HOME PAGE.

2





SELECT AN APPROPRIATE BANK SELECT THE TENURE

3

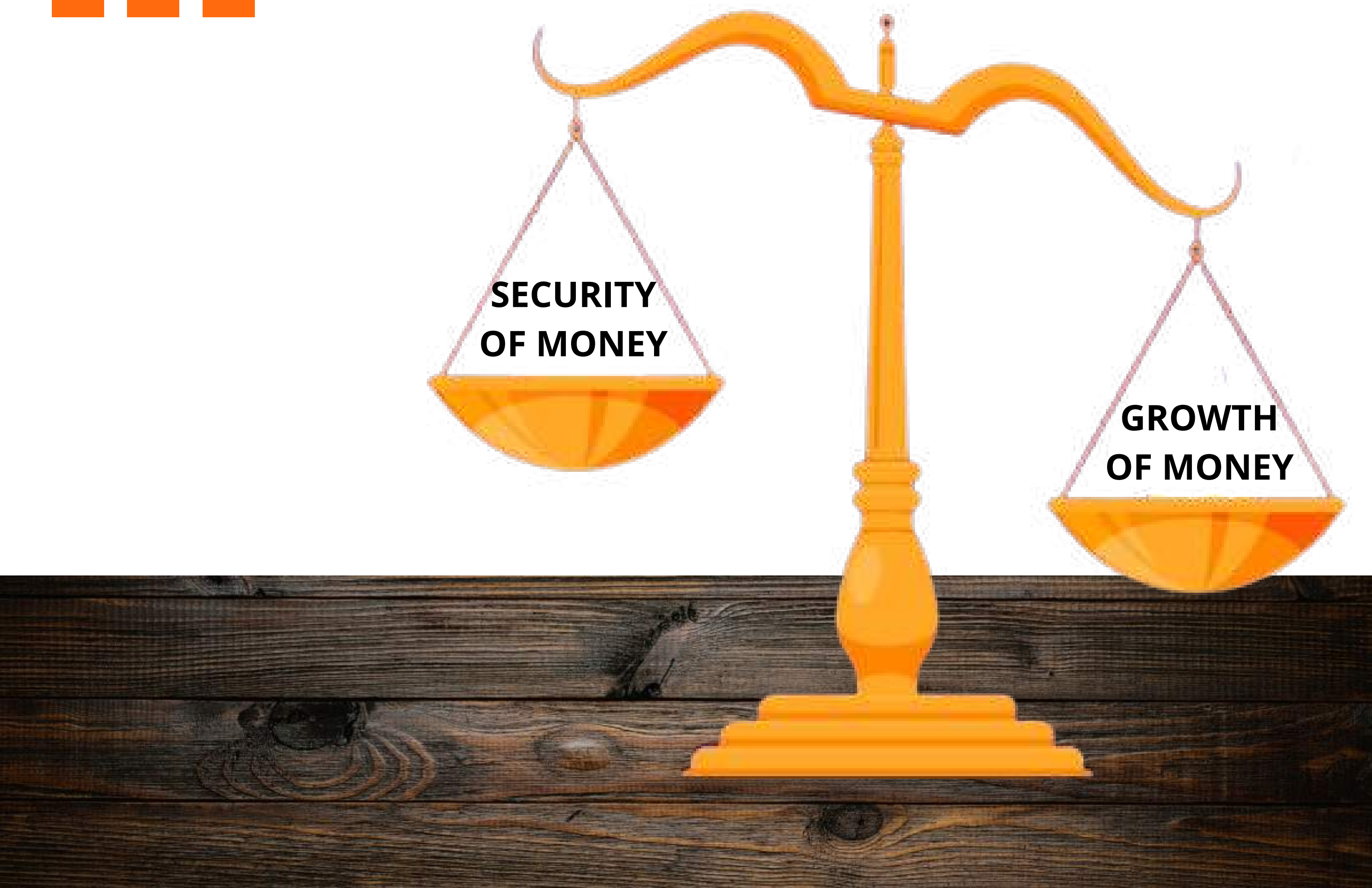
For instance, we have checked Axis Bank's 1 year FD rate which turns out to be 5.15%. Similarly, we will do the same exercise to find out the FD rates offered by different banks. We should check out the FD rates of those banks that are located near your home.

Some banks offer these services via third-party apps as well. However, mainly these are done by visiting bank branches or via bank app on the phone.

For taxes, interest on fixed deposits is added to regular income and taxed based on tax slabs that we fall into. There are some provisions for senior citizens as we saw in the tax profiling stage.

Interest from FD → Forms a part of Taxable Income → Taxed as per Tax slabs

With this, we end our discussion on fixed deposits. We need to remember, fixed deposits are more from a security perspective rather than a growth perspective and should be used to meet short term financial requirements. Also, we should not focus on interest rates here as much as we should with whom we are making a deposit.



02

EQUITY

EQUITY

What is equity? Equity is like buying a partnership in a business. This can be in the form of investing in a private business or buying shares for a publicly listed company. Here, when we talk about personal finance, we will mainly talk about publicly-listed companies and shares that we can invest in. This includes all the companies that are traded on the stock exchanges i.e. BSE, NSE, etc. So, buying equity can be done in two ways – Direct as well as Indirect.

DIRECT EQUITY

It refers to buying shares directly. Here, we get part ownership of the company. This means if we buy one share of a company that has 10,000 shares in sum, we become 1/10,000th partner of the company. So, as we have more and more shares, our ownership of the company increases.

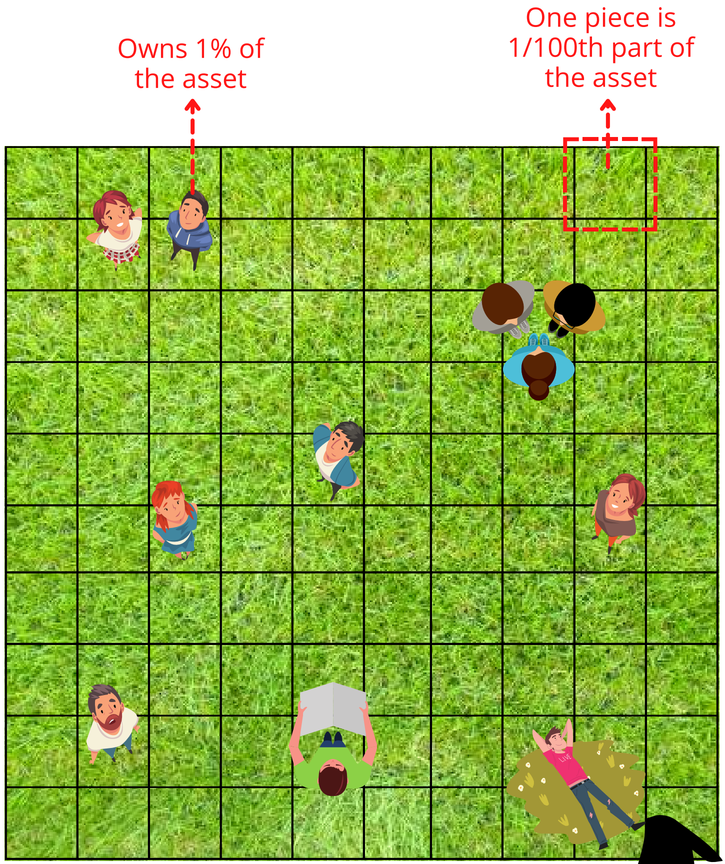
INDIRECT EQUITY

Indirect equity investing refers to buying direct shares but through a portfolio management service or a mutual fund. So, we give our money to these asset management companies and they buy equity on our behalf using the skill and expertise that they have. In return, they charge a small fee.

DIRECT EQUITY

For now, we will focus on direct equity investing. Buying direct equity in a company is like buying a small percentage in that business and how well that business performs going forward, will determine our returns.

Buying a company's shares is same as buying a small piece of land. Assume that this piece of land is a company.



The landowner breaks into 100 small parts and sells these to different people. Each buyer is the owner of 1% of the land. Similarly, a company is broken down into smaller pieces i.e. share, and it is sold to different people.

Every shareholder becomes the owner of the proportion of the company. The Company ownership can be divided into 100 parts or 1 Lac parts. To buy one share, we need to pay the price of one share, to buy 1,000 shares, we will have to pay the price of 1,000 shares

SHORT TERM EQUITY V/S LONG TERM EQUITY

Direct equity can be bought for a day, 10 days, 3 months, 5 years, or whatever the time horizon maybe. So, when investing in direct equity, the time horizon is not pre-decided and can vary. Based on the time horizon, the process of research changes and so does our expectation of return.

SHORT TERM EQUITY

Short term equity activities are called stock trading and include intraday (same-day trade), buy today and sell tomorrow, etc.

NOT PREFERABLE

VS

LONG TERM EQUITY

Long term equity activities are what we call investment activities. Here, we are mainly talking from a perspective of investing for a time horizon of at least 3 years

PREFERABLE

We do not count stock trading to be a part of the Personal Finance Plan. Stocks have spoilt their reputation as an asset class because of the losses that general people have made trading the stocks. It is advised to stay away from trading unless and until someone is a professional trader. We will focus on the long term behaviour of stocks in this entire section.

WHAT CAN BE
EXPECTED IN TERMS OF RETURNS?

Unlike fixed deposits, equity investments do not guarantee any return. In fact, in equity, we can even get less than what we had invested. The return that we will get depends on how the business performs and how the market perceives the investment. Equities have high volatility; if done properly, equity investments can give the highest returns and at the same time can give the worst return as well. Over the short term, equities give the most unpredictable returns. But over the long term, if invested effectively, it can give very attractive returns.

INVESTING SYSTEM

DEMAT ACCOUNT

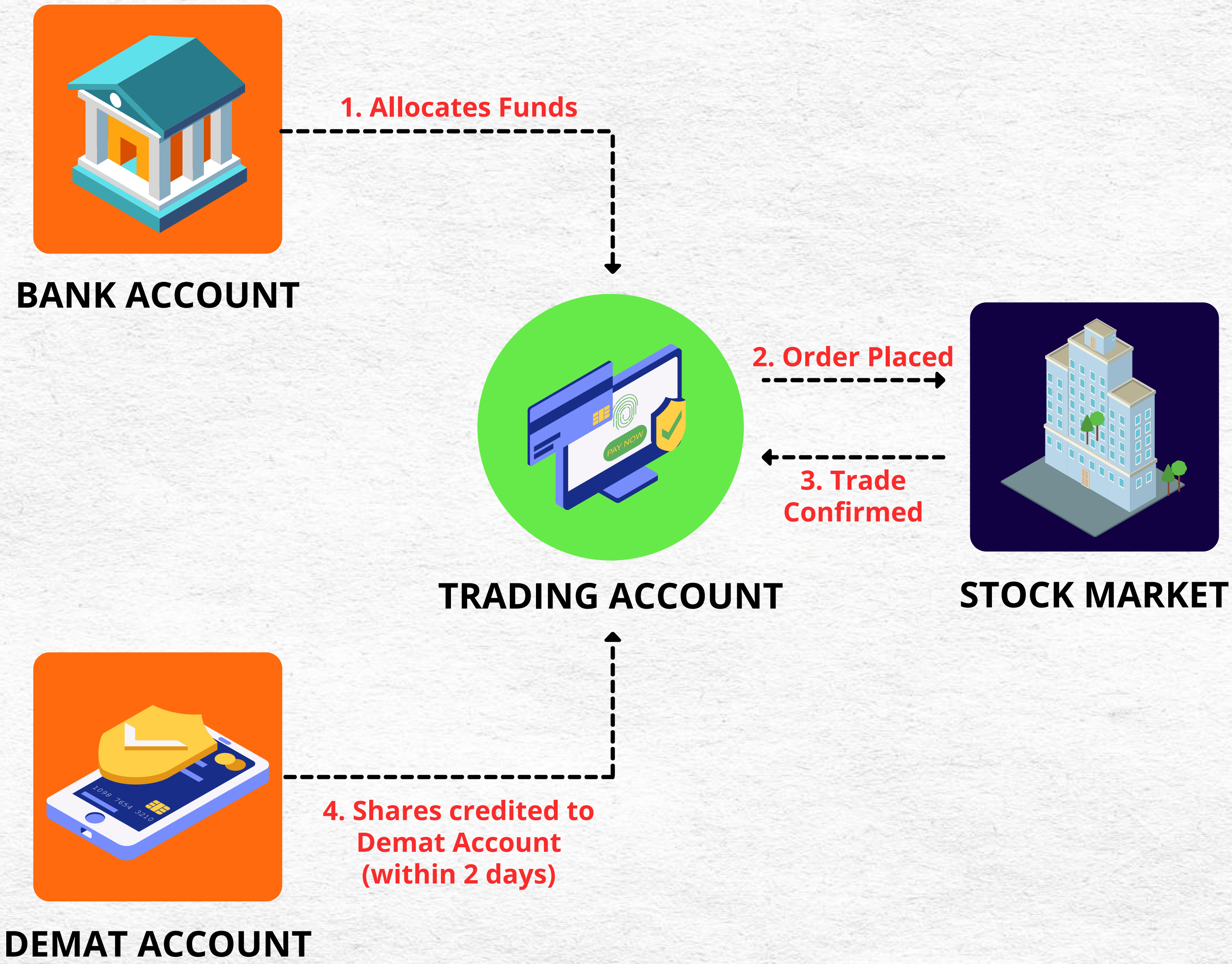
To start investing in shares directly, one needs to open two kinds of accounts. These are called Demat Account, and Trading Account. Demat account is the account that holds our shares. Let us say, we own 1,000 shares of Reliance Ltd, so these shares will be deposited in the said account. A Demat account is like a bank account where the currency is in shares. In India, it is maintained by CDSL and NSDL.

TRADING ACCOUNT

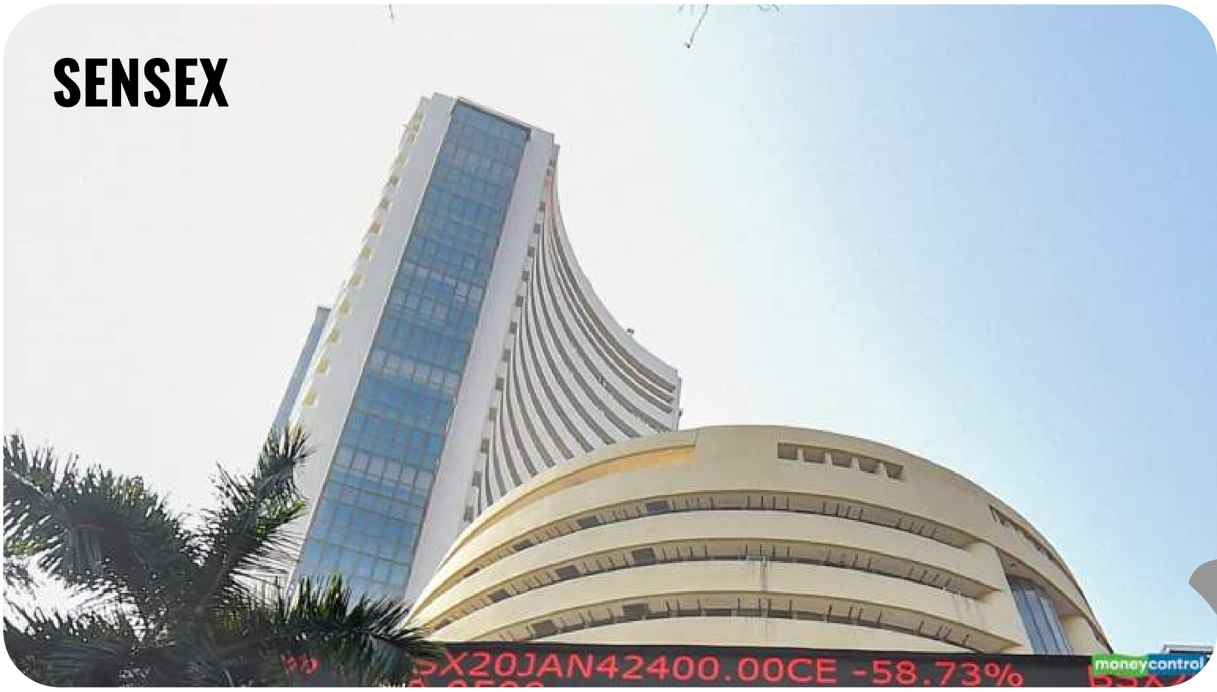
A trading account is opened with a broker. A trading account is needed to trade i.e. buy/sell any share. When we buy a share, we pay cash from our general bank account to the trading account. The money will be transferred between the trading accounts of the buyer and the seller, following which the shares are deposited in the attached Demat account. Only by using a trading account, we can convert cash to shares and vice versa.

SETTLEMENT (T+2 DAYS)

Settlement period refers to the time between the actual sale of a share and the cash transfer. In India, a T+2 settlement exists. This means when we buy shares, we have to pay cash for the same within 2 days of making the purchase and if we sell, we get a cash payout in 2 working days of making the sale.


1. Allocates Funds
BANK ACCOUNT
2. Order Placed
3. Trade Confirmed
TRADING ACCOUNT
STOCK MARKET
4. Shares credited to Demat Account (within 2 days)
DEMAT ACCOUNT

SENSEX



Sensex is an index of the top 30 listed companies in India. Sensex is managed by the Bombay Stock Exchange (BSE). Each company is given a weight and together they form what is called Sensex. The companies keep changing and so does the weight of each one.

Nifty works in a manner exactly similar to Sensex, however, instead of covering the top 30 companies in India, they cover the top 50 companies. However, Nifty is managed by the National Stock Exchange (NSE).

NIFTY

EXAMPLE WEIGHTS IN SENSEX AS ON 30 JUNE 2020

BSE Scrip Code	Company	Weight in Sensex (%)
500209	INFY	7.30
532540	TCS	5.81
500325	RELIANCE	14.57
532174	ICICIBANK	6.05
500180	HDFCBANK	11.63
532281	HCLTECH	1.62
532454	BHARTIARTL	3.59
532187	INDUSINDBK	0.79
500112	SBIN	1.86
500510	LT	3.07
532755	TECHM	0.93

Reliance has 14..57% weightage in SENSEX.

1% increase in Reliance share price will increase the SENSEX by 0.1457% i.e. (1% × 14.57%)

Source: https://www.samco.in/knowledge-center/articles/sensex-companies/

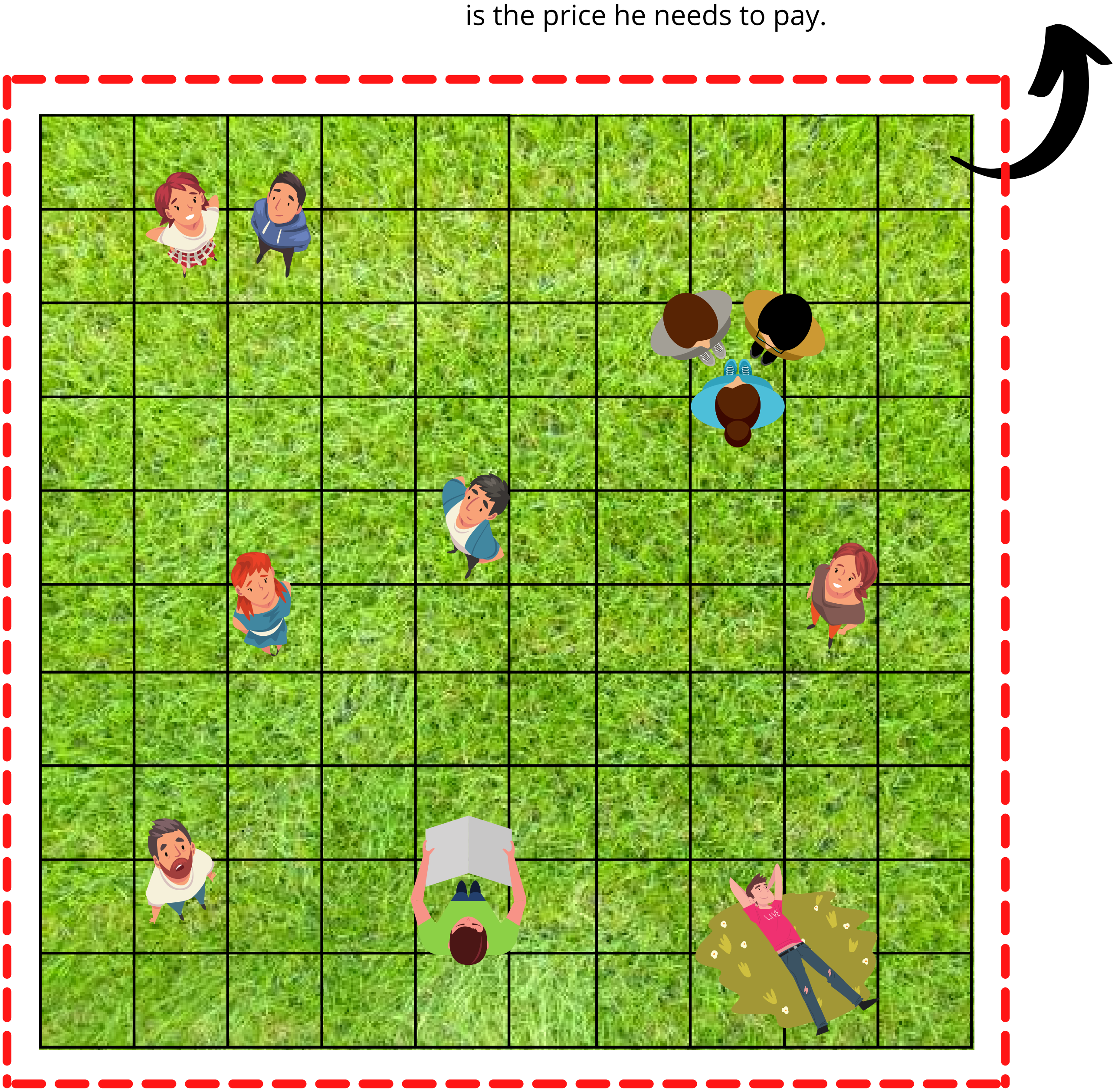
We see that each stock has a weight and a 1% change in that stock affects the Sensex by 1% x weight in Sensex. The sum of these changes for all 30 companies, decide the change in Sensex for the day.

MARKET CAPITALIZATION

Market capitalization is the total value of the company. It is based on the profits they make and the current circumstances. So if a company has 20,000 shares and the share price is Rs. 100, then the entire company can be bought for Rs 20 lac (20,000 x 100). This is the market capitalization of the company. Higher the market capitalization, larger is the size of the company.

MARKET CAPITALIZATION = PRICE PER SHARE × NUMBER OF SHARES ISSUED

The combined market price of all these small pieces is the market capitalization of the asset. So if one wants to own the entire asset, market capitalization is the price he needs to pay.



SMALL CAP | MID CAP | LARGE CAP

The terms- large-cap, mid-cap and small-cap relate to the capitalization of the company. Large caps refer to the companies that are relatively larger in terms of value. There are no fixed rules for the threshold to be a large-cap. In India, there exists an unsaid rule which implies that large-cap companies have a market cap larger than Rs. 10,000 crore. Mid-cap stocks refer to stocks with a market cap between Rs. 1,000 to Rs. 10,000 crore. Small-cap stocks refer to stocks with a market cap of less than Rs. 1,000 crore. Companies in different market cap range exhibit different behaviour and have different risk-reward characteristics.

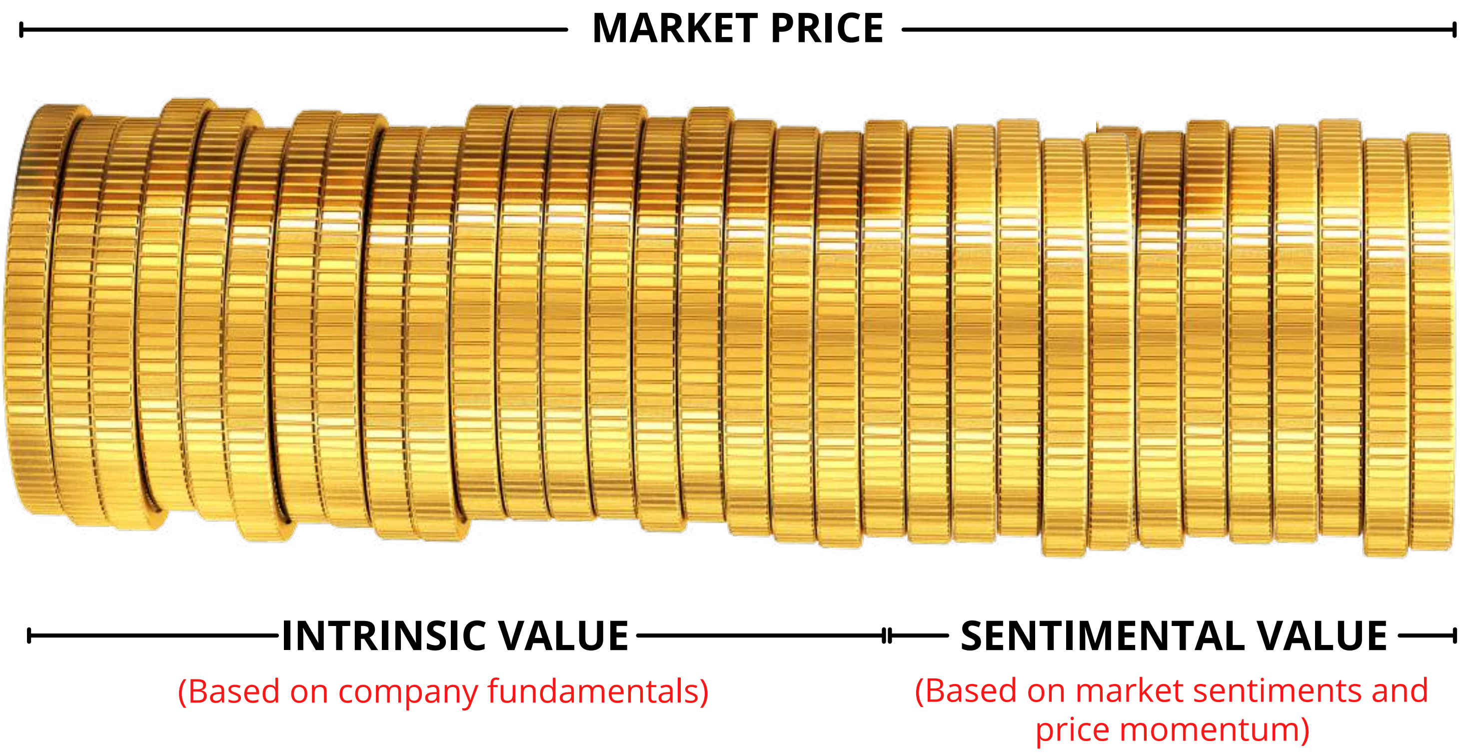
	INR 1,000 CR	INR 10,000 CR
SMALL CAP	**MID CAP**	**LARGE CAP**
Small-cap stocks do not have strong industry leadership and are quite young. Due to lack of resources they might not be able to absorb shocks or completely fail in execution. However, on the brighter side, they have a huge room to grow. They can be multi-baggers. So, small caps offer high risk and attached with high return potential.	Mid-cap companies are relatively bigger than small-cap companies. They have some foot stand in the industry and are capable to absorb risks. They also have growth potential. However, they might not be multi-baggers like small-cap companies. Hence, these have moderate risk and return.	Large-cap companies are generally well-established market leaders that are performing strongly. They have enough resources to absorb all kinds of problems. So, the risk is low. However, they have less room to grow and as a result, the reward is also limited.

Understanding market cap is very important. This is because each capitalization category exhibits very different risk-reward behaviour. It helps investors understand the kind of return and risk that can be expected from them. This understanding will play a critical role in allocating our assets based on our risk-taking ability.

HOW STOCK PRICES MOVE AND HOW A RETURN IS MADE?

We see in equities, there are two factors related to any given share- its value and its market price. For this, let us understand the composition of a share price. The share price is affected by two things. One is the intrinsic value of the share or the true worth of the share price. It is based on the company's performance, its strength, its weaknesses, its pricing power, and other fundamental factors. In a nutshell, it is determined based on company-related factors.

The second component is the market sentiments. It is determined by the speculators in the stock market. It is based on the emotions and perception of the company in the market; what the investors feel irrespective of the company's inherent factors.

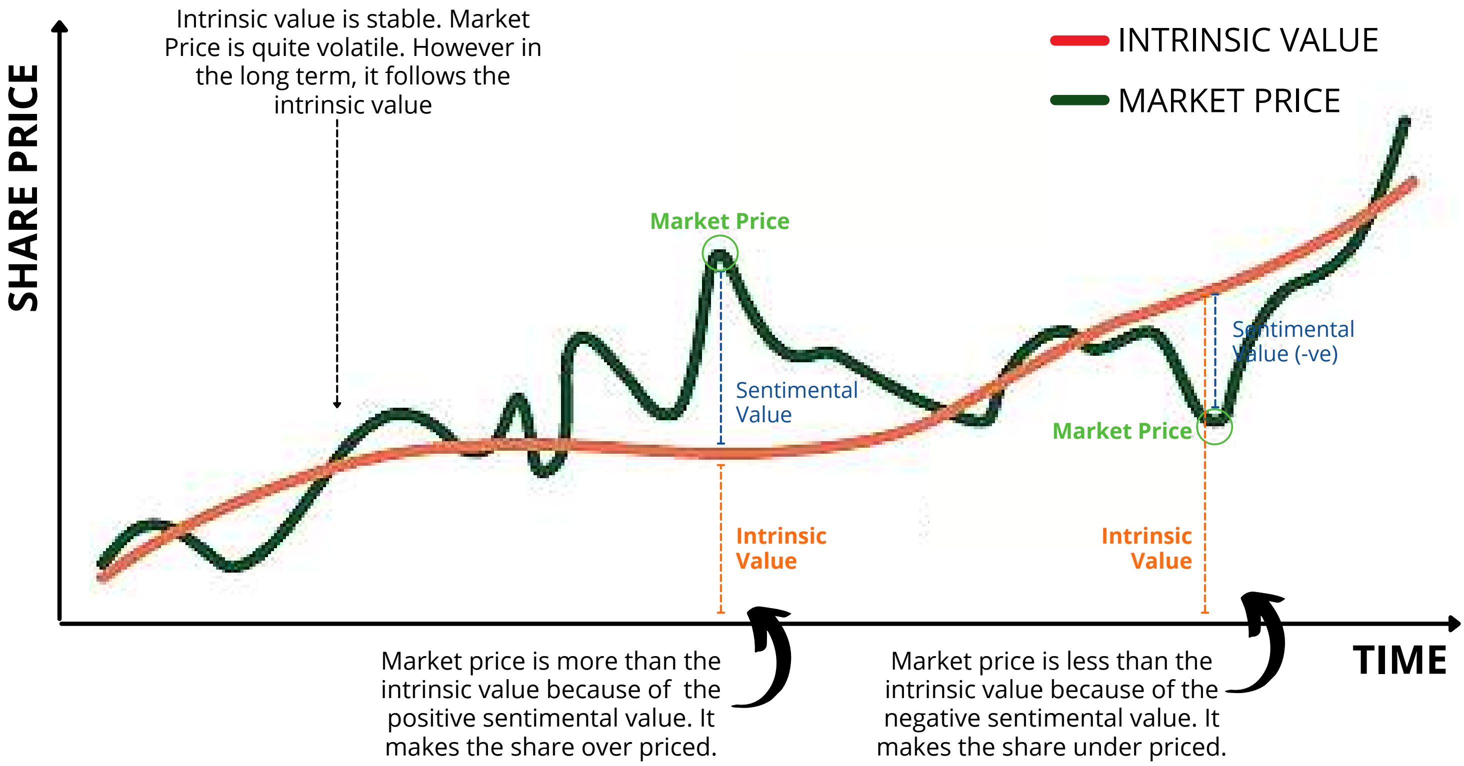


When we say that a share is priced at Rs 100, Rs 60 would be its intrinsic value and Rs 40 would be market sentiments. In other cases, market sentiments can also reduce the price. Let us assume another share priced at Rs 110. Now, its intrinsic value may be Rs 150, but because of negative market sentiments i.e. Rs 40 (negative), it is trading at Rs 110. So we see that market 'price' is a combination of intrinsic 'value' and market sentiments.

Now, value or intrinsic value is the true value of the company. It is more stable. It will move upwards if the company performs well and move downwards if the company underperforms.

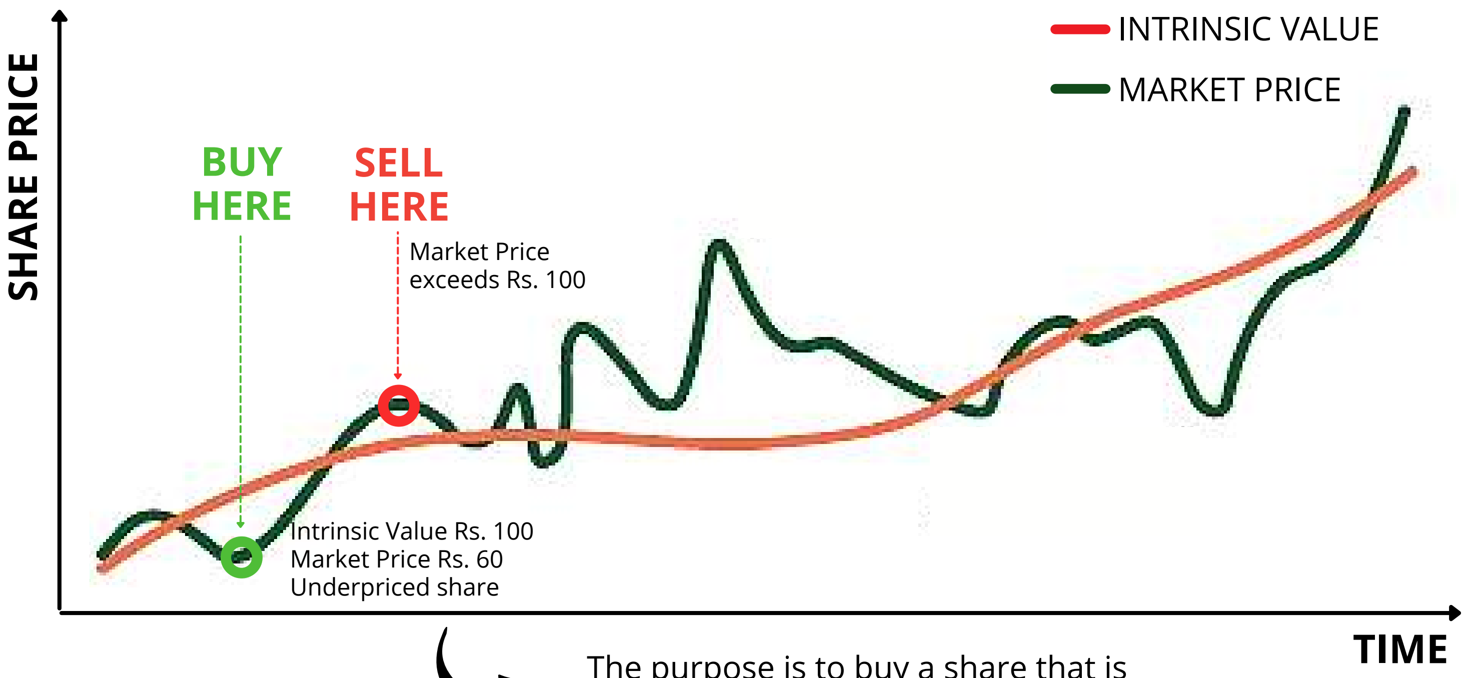
On the other hand, market sentiments are only speculative. They can't be trusted. It can change with a small piece of news and may take any direction.

The price of the stock is a combination of both value and market sentiments. But no one knows the exact intrinsic value of the company and all numbers are mere speculations. So the proportion of intrinsic value and the market sentiment is unknown. Price is significantly affected by the sentiments. As perceptions and sentiments can change very quickly, market prices can move quickly in any direction. However, in the long run, the price will always follow the true value.



To make money in direct equity, we want to buy an asset and then sell it at a price much higher than the buying price. With this, we make a profit on the sale. This is similar to how people invest in real estate. For equity, this can be done in two ways.

First, one must buy shares of companies that have a market price lower than the estimated intrinsic value. For example, pick a company that is selling for Rs. 60 per share (price), whereas, the intrinsic value of the share is around Rs. 100 (value) according to our research and analysis. Then, we will wait for the price to catch up with the value. This might take a few years. Once the market price crosses Rs. 100, then we can sell to book our profits. By this time, the value might increase even more and so we can wait longer. This is called value investing.



The purpose is to buy a share that is underpriced and sell it once the price exceeds the estimated value.

The second way is to buy companies whose actual value is rising very rapidly and the price will catch up. So if the price is Rs. 100 and the estimated value is Rs.60 currently, it might not make sense to buy an over-priced company. However, if we are very sure that in a few years the value of this company will increase to Rs 150-200 due to the company's expansion or other factors, then we can buy the stock. The price is bound to follow the value. Once the value and the price increase, we can sell the stock. This is called growth investing.

Buy a share whose intrinsic value is bound to increase. Even if the share is currently over-priced. Increase in intrinsic value will ultimately increase the market price also

It takes a lot of time and effort to do the background research. We can see that analyzing individual stocks is a time-consuming job and requires complete education and training for the same, which is beyond the scope of what we are doing right now.

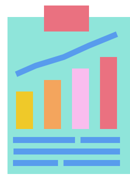
Value is steadier whereas price keeps on changing based on the market. It can take any direction. In short term(less than 2 years), the price can take almost any direction. However, in the longer term, price follows the direction of the true value of the company. This is how returns are made in direct equity investing.

EQUITY – RESEARCH METHOD

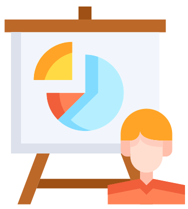
The last page introduced us to the entire math of direct equity investing. Let us see how analysts estimate the intrinsic value of the company. They do things like:

Study Annual Reports of Last 5-7 Years

Conference Calls

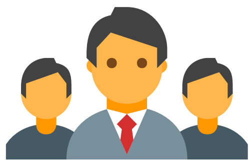


Tracking Quarterly Results



Financial Analysis

On-ground Research

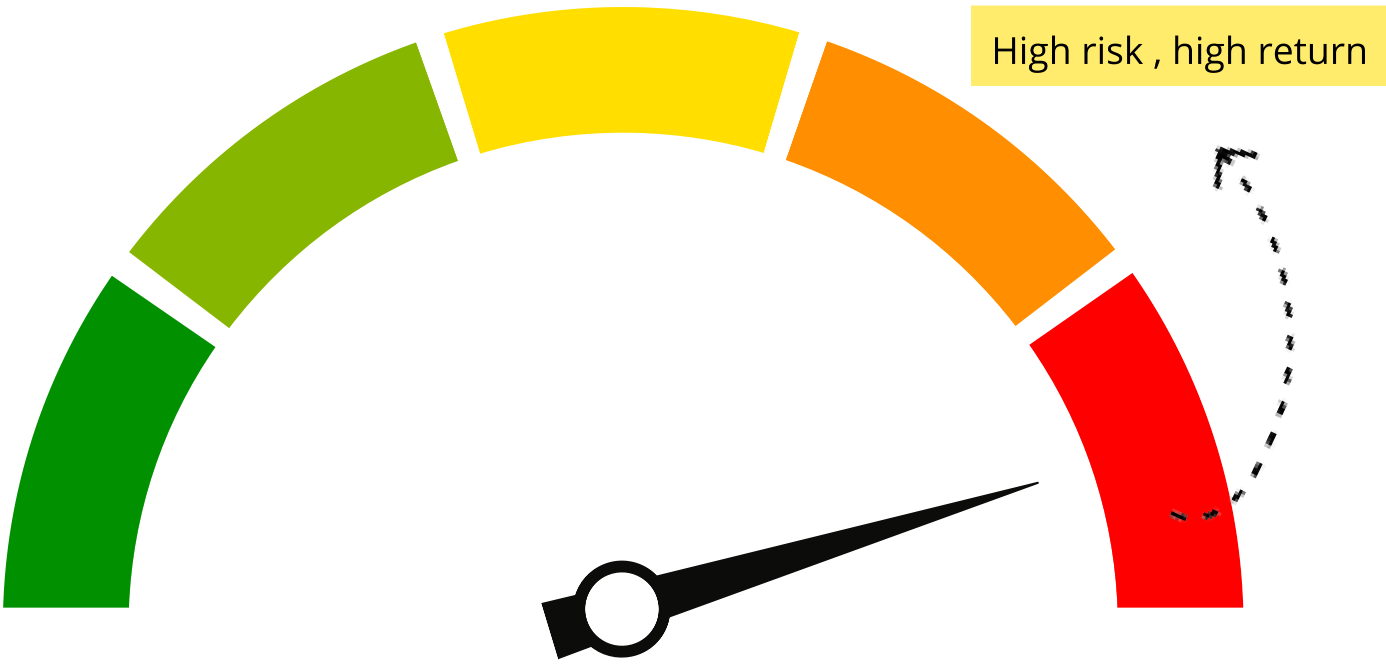


Management Meets

However, most do not have the skill or the time to invest in equities directly and move towards indirect equity. Secondly, we should stay away from 'tips'. Tips are not backed by adequate research and because they have so many incentives behind them. The number one reason why people lose money in stocks is that they think they know it all and invest with inadequate skill and research.

Therefore, we can safely conclude that direct equity investing is full-time work. Knowing a company in and out is a lot of effort. We need to have the skill as well the time to go through the same. If we have the skill and time to go through the above process, direct equity investment is suitable for us. If we do not have the skill or time, we must let go of direct equities and move towards indirect equities.

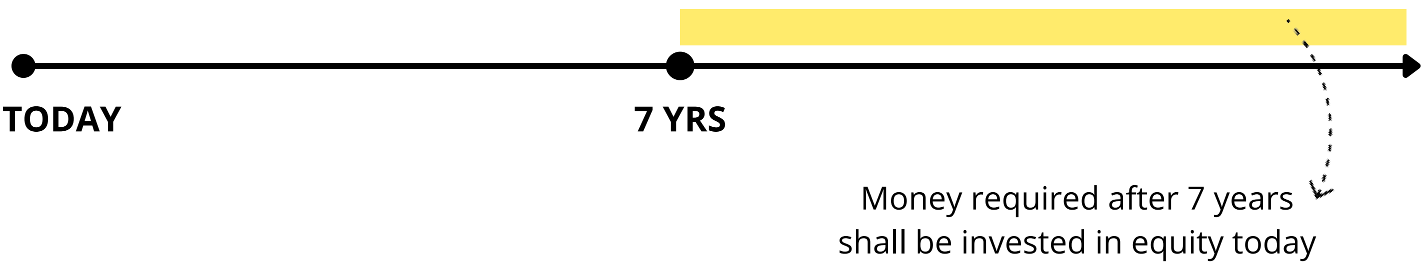
WHO IS IT SUITABLE FOR?



RISK METER

Direct equity is capable of giving the highest returns in contrast to other asset classes. However, it also comes paired with high risks possibility if done improperly. In the short term, equity prices can take any direction and the returns are completely unpredictable. We might do everything correctly from our end, but the returns of the short term might still be very poor. In the long term, equity prices follow the fundamental strength of the business and the true value.

Equity is suitable to meet all long terms goals. The prices may go up and down, but in the long run, if the company is performing well, the prices will go up. Any money that we do not need for more than 7 years, a major chunk of that must go into equity. If long term money goes into debt or fixed deposits, we will lose out on returns for no reason.



However, another aspect is the availability of skill and time. Estimating the true value of stocks and understanding their businesses requires skill. If we do not have the skill, we cannot carry out direct equity investing. Same is the case with time. We might have the skill but we might not have the time to carry out thorough research. If we do not put in the required time, we will never be able to estimate the true worth of the companies.

Upon the absence of either, we will invest in equities via indirect method or the alternate methods to direct equity. Let us get familiar with the common alternatives to direct equity investing, applicable to those who lack skill, time, or both.

ALTERNATE OPTIONS TO DIRECT EQUITY

If we do not have the skill or time to buy individual stocks, we need not worry as there are alternate ways to invest in shares as well. These include Mutual Funds and Portfolio Management Services.

MUTUAL FUNDS

A mutual fund is an asset management company that takes money from a large number of individuals and invests it together based on the fund's mandate. Let us say we want to invest Rs. 1 lac in equities. We do not have the skill or time to invest and no expert would lend their time to manage Rs. 1 lac. This is where mutual funds come to our rescue. They club together, say, 1,000 such people with Rs. 1 lac each. They have to now manage a total of Rs. 10 crores.

They will appoint an expert team to manage the money on behalf of the 1,000 investors. So, an individual with almost any amount can get the expert to manage their investment as well by contributing to the mutual fund. This is how mutual funds work and they are the central part of the Lazy Personal Finance Plan.

PORTFOLIO MANAGEMENT SERVICES

Portfolio management service is when we give our decent-sized portfolio to an expert to manage on our behalf and charge a fee for the same. They manage the portfolio exclusively based on our needs and circumstances. In a mutual fund, the total amounting from all the investments is carried out in the manner as stated by the fund's mandate. In a PMS, the investments are tailored to our requirements. Also, mutual funds have no minimum amount requirement whereas PMS has a minimum asset size requirement.

MUTUAL FUNDS		PORTFOLIO MANAGEMENT SERVICES
Amount invested in thousands & above	INVESTMENT SIZE	Amount invested in lacs & above
Minimal managing cost	COST	Relatively high managing cost
Anyone can invest	WHO CAN INVEST	Generally, HNIs (High Net Worth Individuals) invest
Relatively high tax benefits	TAX BENEFITS	Relatively low tax benefits

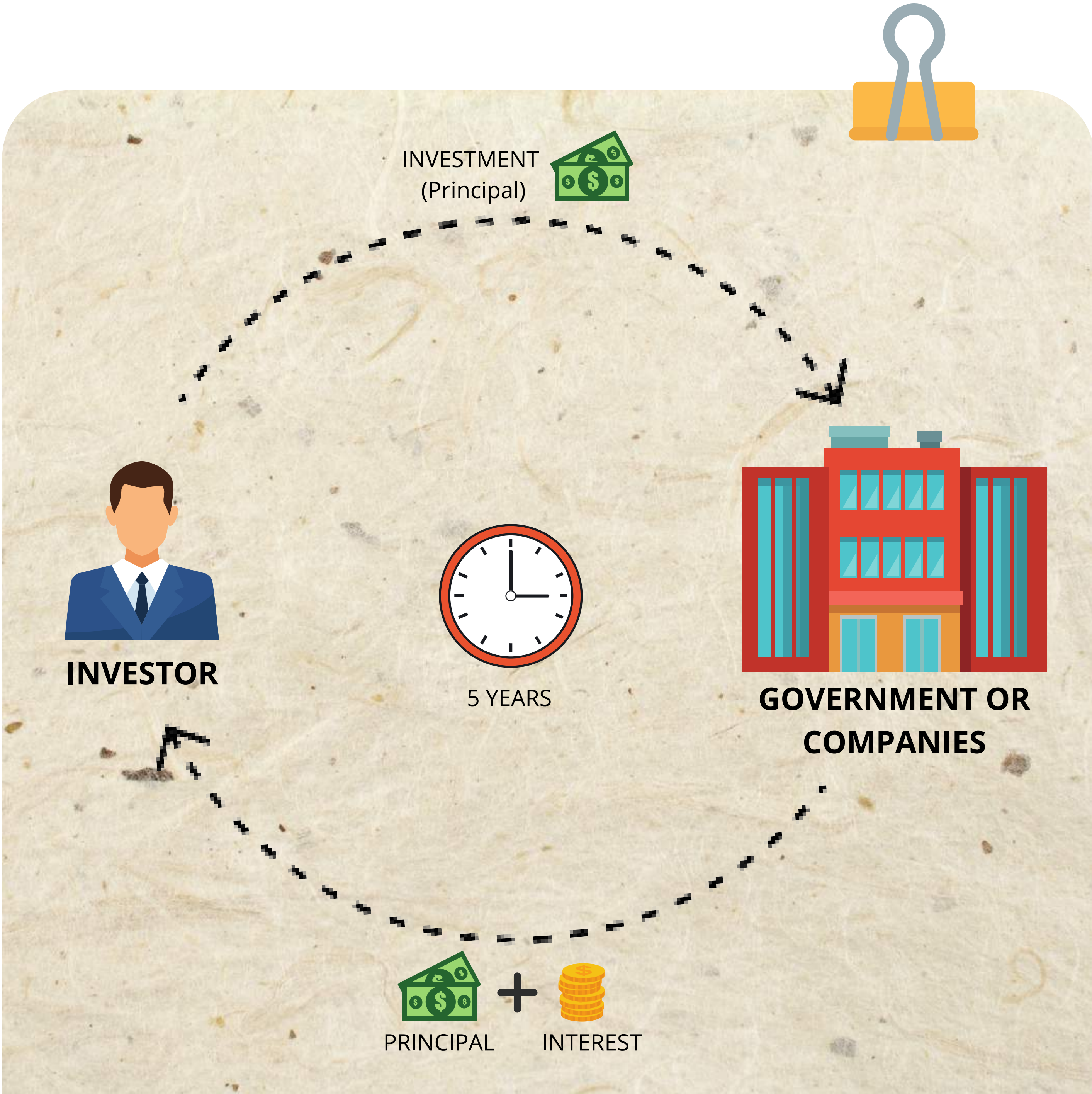
With this, we end our discussion on direct equity on the listed side. We have concluded that it is suitable for long term goals and has a high risk-return attached to it.

03

FIXED INCOME

FIXED INCOME

All items exhibiting debt-like characteristics such as bonds, commercial papers, debentures, are called fixed-income assets. These are similar to giving a loan to a company. Unlike equity, here we lend a fixed amount, for a fixed time, for a fixed interest rate. It is called fixed income as all the elements and our income (interest) are fixed beforehand. All interest-bearing assets fall under the fixed income asset class. Fixed deposit is also a type of fixed income asset. Like equity, we can invest in fixed income assets directly as well as indirectly (via Mutual Funds).



TYPES OF FIXED INCOME

COMMERCIAL PAPER

When we buy commercial paper, we are effectively lending the amount to the company that has issued the paper for a short-term basis. On maturity, the company is liable to pay us a maturity amount as mentioned on the commercial paper.

BONDS

Bonds are similar to commercial paper but are issued for a longer-term. Bonds can take years to mature. For instance, we buy bonds worth Rs.10,000 issued by Asian Paints that pays 7% p.a. interest and matures in 5 years. So the company will pay Rs. 700 as interest every year and at the end of 5 years, it will repay the principal amount of Rs.10,000.

TREASURY NOTES

Just like companies raise money in the form of debt from the public, similarly, RBI also borrows money from the public. They do so by issuing treasury notes. These are similar to bonds, have long maturity periods, and pay interest rates. The only difference is, they are backed by the government whereas bonds are backed by companies. They are the safest form of bonds and offer the lowest interest rate because of safety.

TERMS TO KNOW

MATURITY

Maturity is the time from today, in which the bond matures i.e. is due for redemption. So, a 7% 10-year Ultra Tech Cement Bond, has a maturity of 10 years if issued today. If the same bond was issued 3 years back, the maturity from today would be 7 years. The maturity of the fixed income asset will be determined by the time left for the bond to mature starting today. Maturity can range anywhere between a few months to 100 years. Some bonds do not have a maturity date i.e. perpetual bonds.

ISSUER

The issuer is the company/entity that has issued the fixed income bond. It is the entity that is borrowing the money and is liable to repay it on maturity. The financial health of the issuer determines the price and performance of fixed-income assets

COUPON RATE

Every bond that we buy has a fixed interest payment by the company. This interest can be paid every year or cumulatively at the end as well. The interest rate quoted in the name of the instrument is the coupon rate. For instance, a 7% 10 years Torrent Pharma Bond has a coupon rate of 7% i.e. the company is liable to pay an interest rate of 7% p.a.

YIELD TO MATURITY

When we buy a bond for less than Rs. 100 (original principal) i.e. at a discount, we get a slightly higher return than the coupon rate as we invested less than the original principal i.e. Rs. 100. When we buy bonds for more than Rs. 100 (original principal) i.e. at a premium, we get a return less than the coupon rate as we overpaid for the bond. This return, after adding or deducting return based on premium or discount at the time of purchase to the coupon, is called the yield to maturity. It depicts the actual returns from our investment.

The market price at which the last transaction (buy/sell) of a bond was executed

'QUOTED' interest rate. This rate will be used to calculate the amount of interest that the investor receives

Security Code	ISIN No	Issuer Name	Coupon (%)	Maturity Date	LTP	Weighted Average	
						Price	Yield
790MRHFL30	INE950O08196	MAHINDRA RURAL HOUSING FINANCE LIMITED	7.90	16/12/2030	100.4375	100.4400	7.8300
1125TATAMFL99	INE909H08113	TATA MOTORS FINANCE LTD	11.25	28/06/2099	103.6085	103.6100	8.5000
703NHAI40	INE906B07IH3	NATIONAL HIGHWAYS AUTHORITY OF INDIA	7.03	15/12/2040	100.5000	100.7800	6.9500
875NHAI2029	INE906B07DF8	NATIONAL HIGHWAYS AUTHORITY OF INDIA	8.75	05/02/2029	126.0427	126.0400	4.5800
975AJMERVVN31	INE888F08030	AJMER VIDYUT VITRAN NIGAM LIMITED	9.75	30/03/2031	104.1900	104.1900	8.9500
980JAIPURVVN31	INE887F08040	JAIPUR VIDYUT VITRAN NIGAM LIMITED	9.80	30/03/2031	104.4000	104.4000	8.9500
970JODHPURVVN31	INE886F08034	JODHPUR VIDYUT VITRAN NIGAM LIMITED	9.70	30/03/2031	103.9800	103.9800	8.9500
ABFL17JAN21	INE860H07GN1	ADITYA BIRLA FINANCE LIMITED	0.00	15/01/2021	117.4327	117.4300	8.6500
775TATAC30	INE857Q08032	TATA CLEANTECH CAPITAL LIMITED	7.75	26/07/2030	102.2200	102.2200	7.4100
985APPFCL2022	INE847E08DL4	ANDHRA PRADESH POWER FINANCE CORPORATION LTD	9.85	30/01/2022	100.9500	100.9500	9.1200
719THDCIL30	INE812V07039	THDC INDIA LIMITED	7.19	24/07/2030	100.4900	100.4900	7.1100
866IIFCL34B	INE787H07347	INDIA INFRASTRUCTURE FINANCE COMPANY LIMITED	8.66	22/01/2034	140.4082	140.4100	4.5000
848IIFCL28	INE787H07255	INDIA INFRASTRUCTURE FINANCE COMPANY LIMITED	8.48	05/09/2028	125.8054	125.8100	4.4400
905HDBFS28	INE756I08140	HDB FINANCIAL SERVICES LIMITED	9.05	27/07/2028	109.5000	109.5000	7.3500

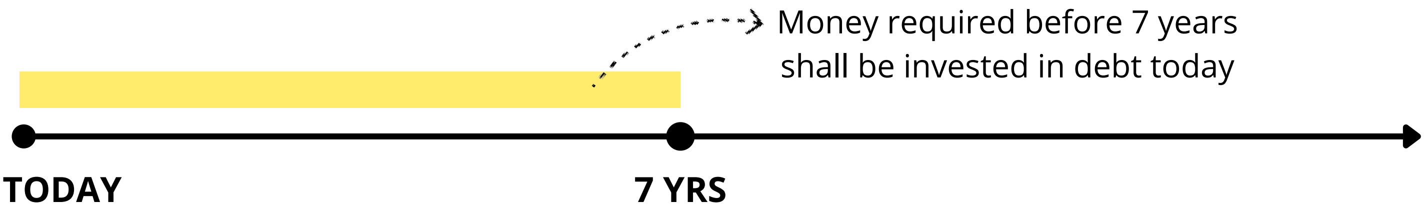
Company that issues the bond

Date of redemption

Effective interest rate of the investment. Due to the premium (discount) purchase, the effective return may go down (up). This rate depicts the actual return that the investor marks.

SOURCE: https://www.bseindia.com/markets/debt/CorporateBonds.aspx?Flag=1

WHO IS IT SUITABLE FOR?

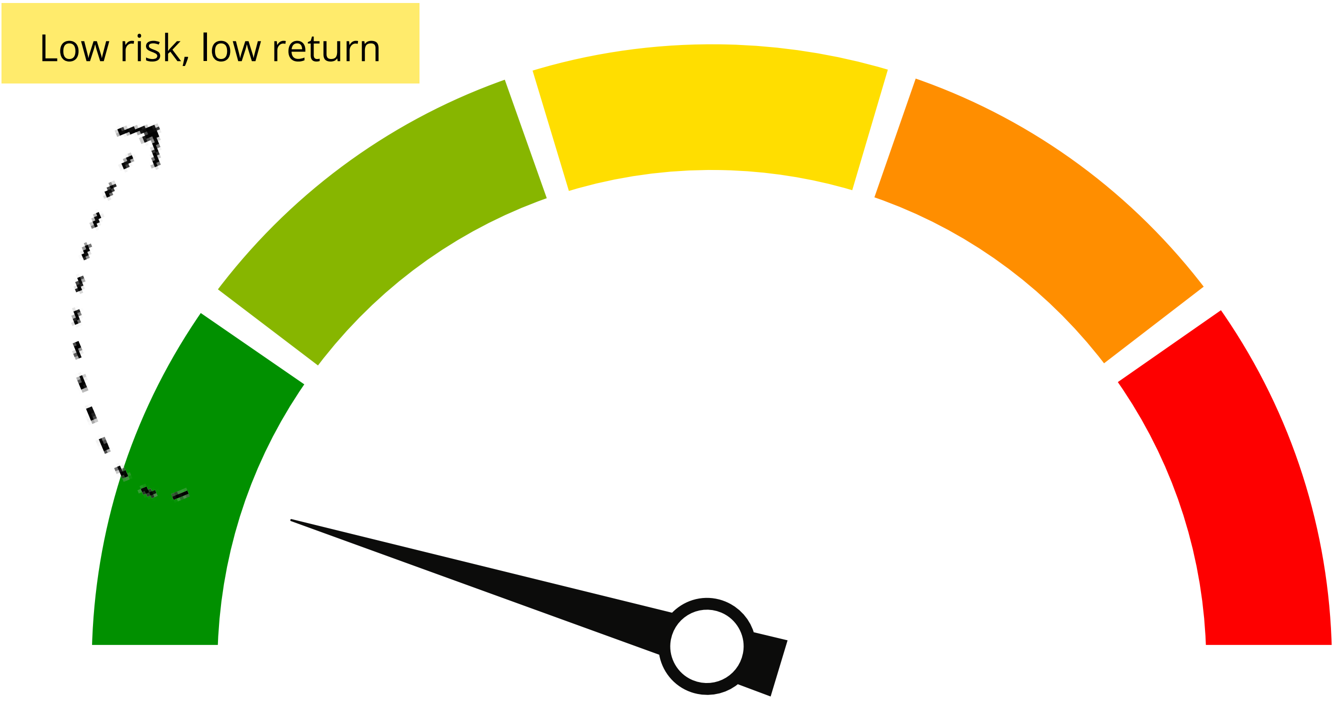


BASED ON TIME HORIZON

Debt funds are suitable to cater to goals that are to be met in less than 7 years from today. For, financial goals to be met in less than 2 years i.e. bucket A, should use debt investments only, whereas goals to be met in 3-7 years i.e. bucket B, you can use a mix of equity and debt. As the time horizon keeps on reducing, the share of debt in investment keeps on increasing.

BASED ON RISK

Debt is suitable for all those having a low risk-taking ability. For short-term goals, our risk-taking ability is low and hence, suitable. It can also be used for meeting long term goals if the risk-taking ability of the person is very low. However, planning for very long term goals using debt is a trap that people fall into. Debt generally comes with lower risks and therefore lower returns. The purpose of accepting a lower return using debt is to reduce the volatility of prices. But this is not required in the long term since we can bear the risk of uncertainty with the neutralization of the volatility of equity. Debt gives a comparatively steady but lower return. So, a volatile higher return is better than a steady but slow return in the long term. This is why we try and plan for long term assets using equity rather than debt.

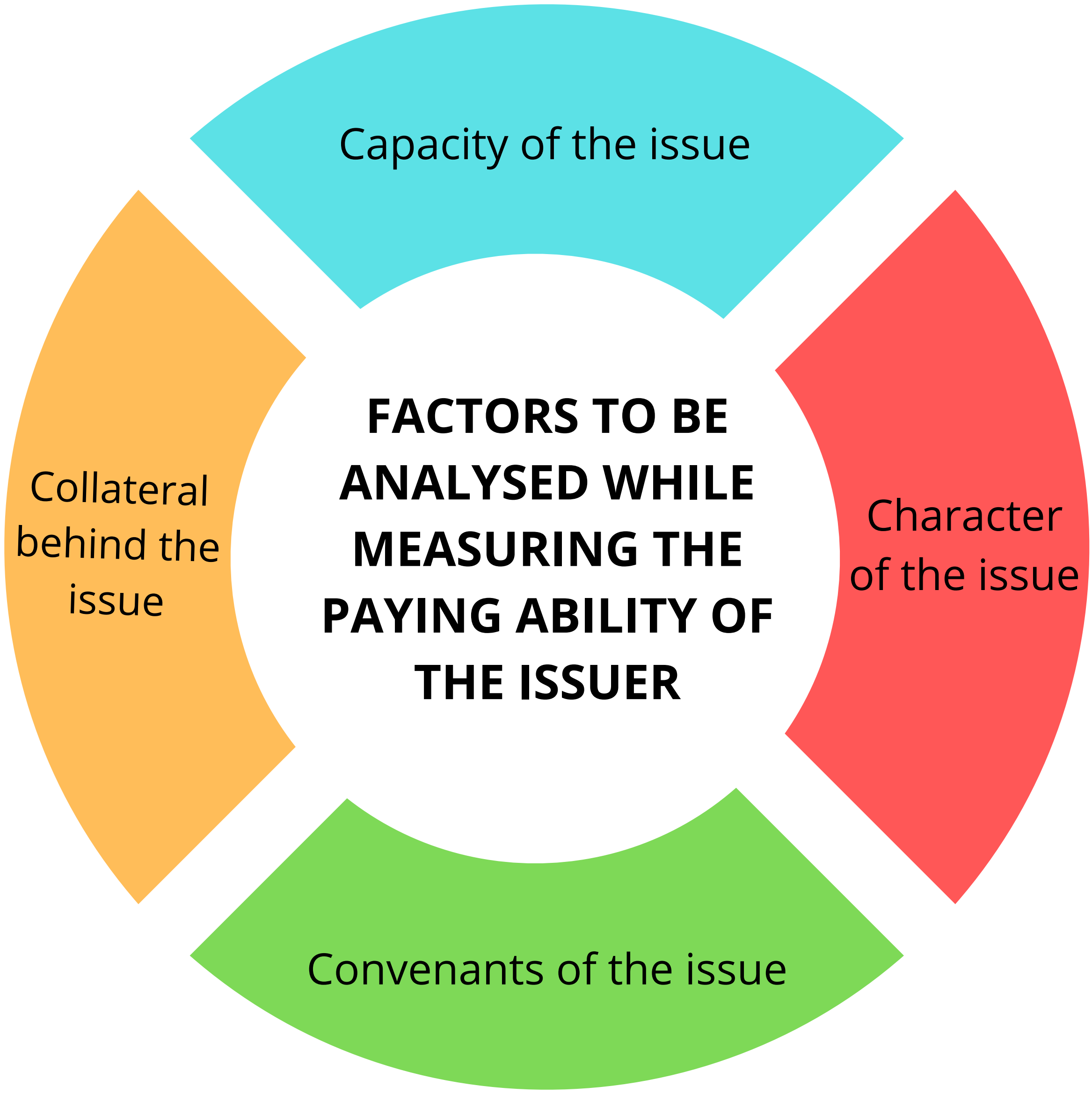


BASED ON TIME AND SKILL

Should the investments be made using debt instruments directly or via indirect methods? Again we have to evaluate if we have the skill and time to analyze debt instruments. Understanding fixed-income assets and their analysis too require the same time and same rigour as with direct equity investments. Upon the lack of either, we should invest in fixed income assets via an indirect route only.

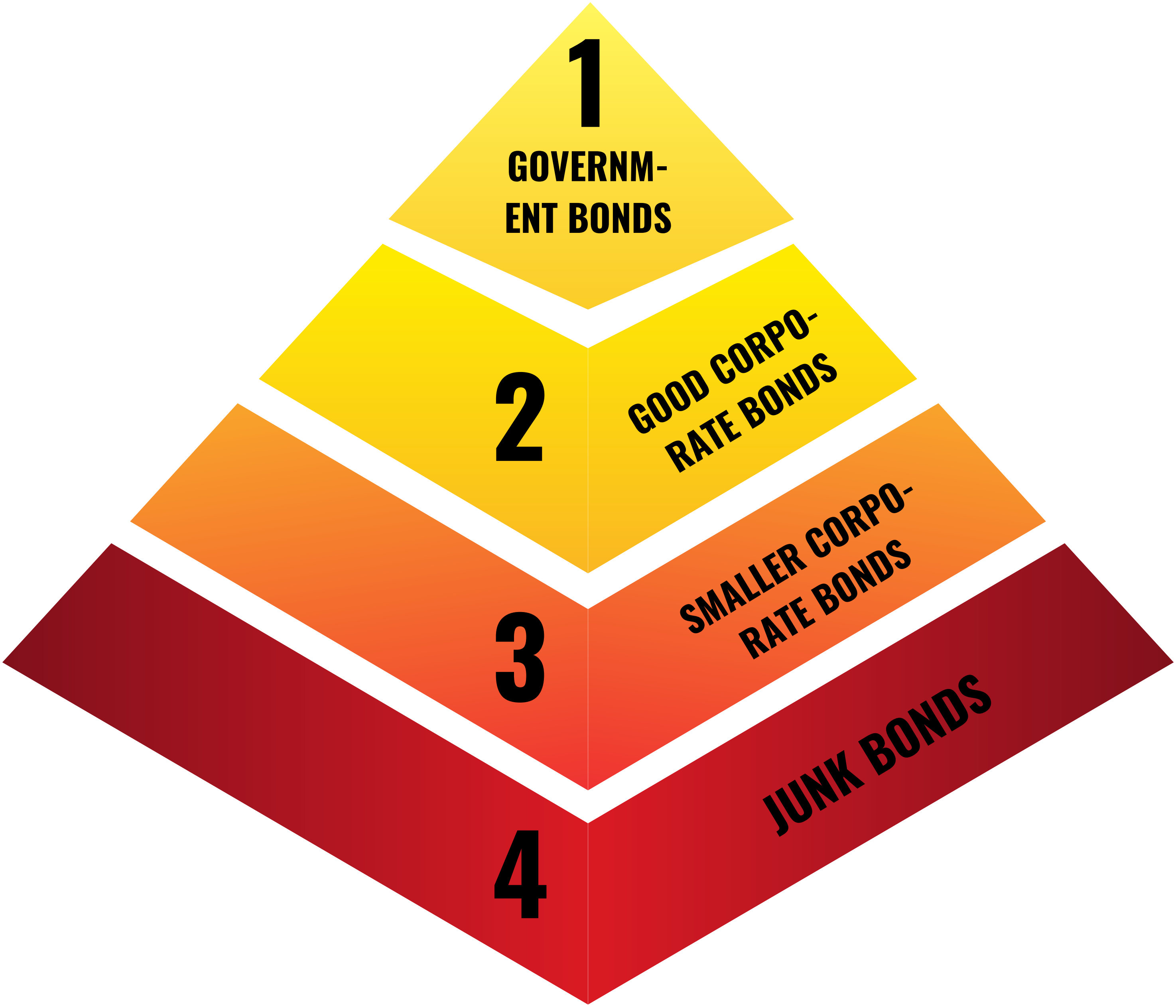
EXPECTATIONS

The general rule of fixed income assets claims that the higher the risk in the asset, the higher will be the yield offered. When evaluating fixed income assets, the issuer and their ability to repay the liability is understood, and based on that, a return is expected. Lower the ability of the issuer to pay back, riskier is the bond, and therefore higher is the expected return. To understand the paying ability of the issuer, multiple factors are analyzed which include the capacity of the issuer, the character of the issuer, covenants or conditions in the bond issue, and the collateral behind the issue. Based on these factors the ability is determined and that is why we say that investing directly in fixed income assets requires time and skill.



So coming back to expectations, the safest bonds are those issued by the government and they offer the lowest returns of all fixed-income assets. These offer a return that is in line with the standard fixed deposit rates. Second, good corporate bonds are slightly riskier than the former. Hence, the return is also slightly higher than government bonds. Lastly, bonds issued by smaller corporates are riskier and therefore offer higher returns.

As the quality of the issuer keeps going down, the rate of return keeps going up. At the end of the spectrum is junk bonds or bonds of companies with a very poor financial position. Their bonds are bought due to the high returns they promise and require close monitoring and are beyond the scope of this book. We can opt for each of these kinds via the indirect route i.e., via mutual funds.



To begin understanding any fixed-income asset, we start by reading the credit analysis report. Credit rating reports are issued by independent credit rating companies like ICRA, CRISIL, and CARE in India. These are independent companies that analyze the company and release a rating report based on various parameters and they grade each company based on its worthiness.

So, each credit rating agency follows its rating scale and give a rating to each bond in the market. From this, we can get an idea of the credit quality of the issuer. For instance, an AAA rating means the highest security whereas B, C or D means very high risk and low safety in the asset. This is the rating system used by CRISIL. ICRA and CARE also have a similar rating system.

Each bond compulsorily needs to be rated. We can hence go through the credit rating report that gives a score and also lists down the strengths and weaknesses of the issuer. Having said that, credit rating reports have two problems:

- one, credit rating agencies are paid by the company (issuer) and therefore the company can influence the report,
- second, they can be incorrect at times.

However, as an individual, we can rely on credit rating reports to be correct in general and can be relied upon.

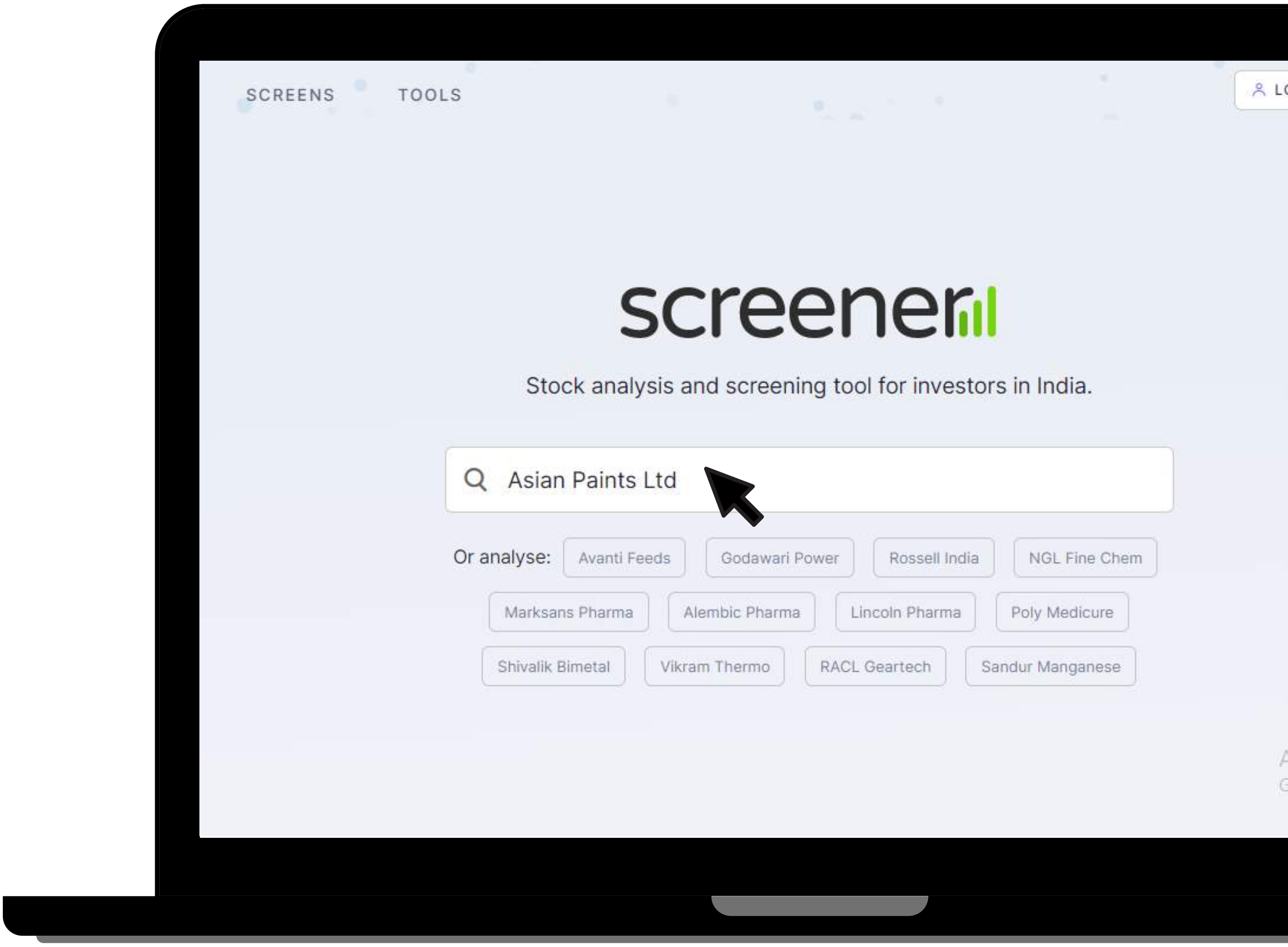
AAA	Highest Safety
AA	High Safety
A	Adequate Safety
BBB	Moderate Safety
BB	Moderate Risk
B	High Risk
AAA	Very High Risk
AAA	Default

HOW TO SELECT?

1

GO TO 'SCREENER.IN' SEARCH THE COMPANY WHOSE REPORT IS NEEDED

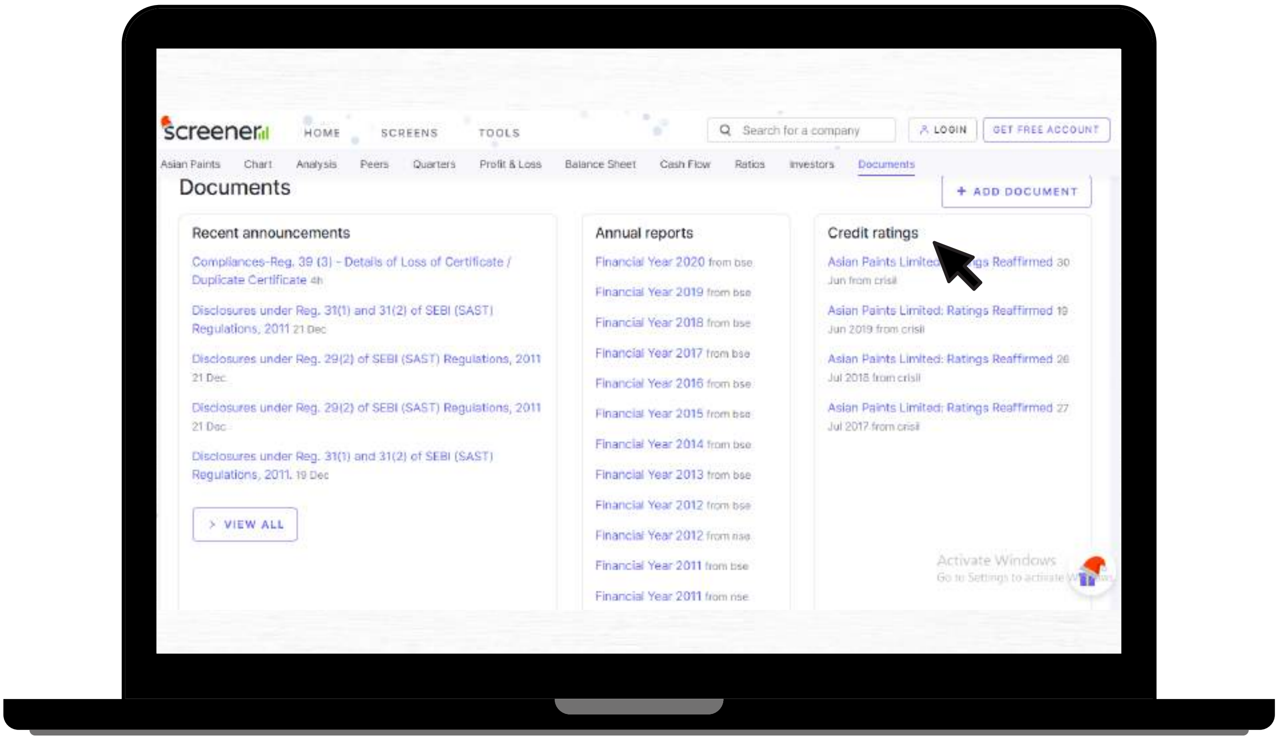
For instance, here we have searched for 'Asian Paints Ltd"

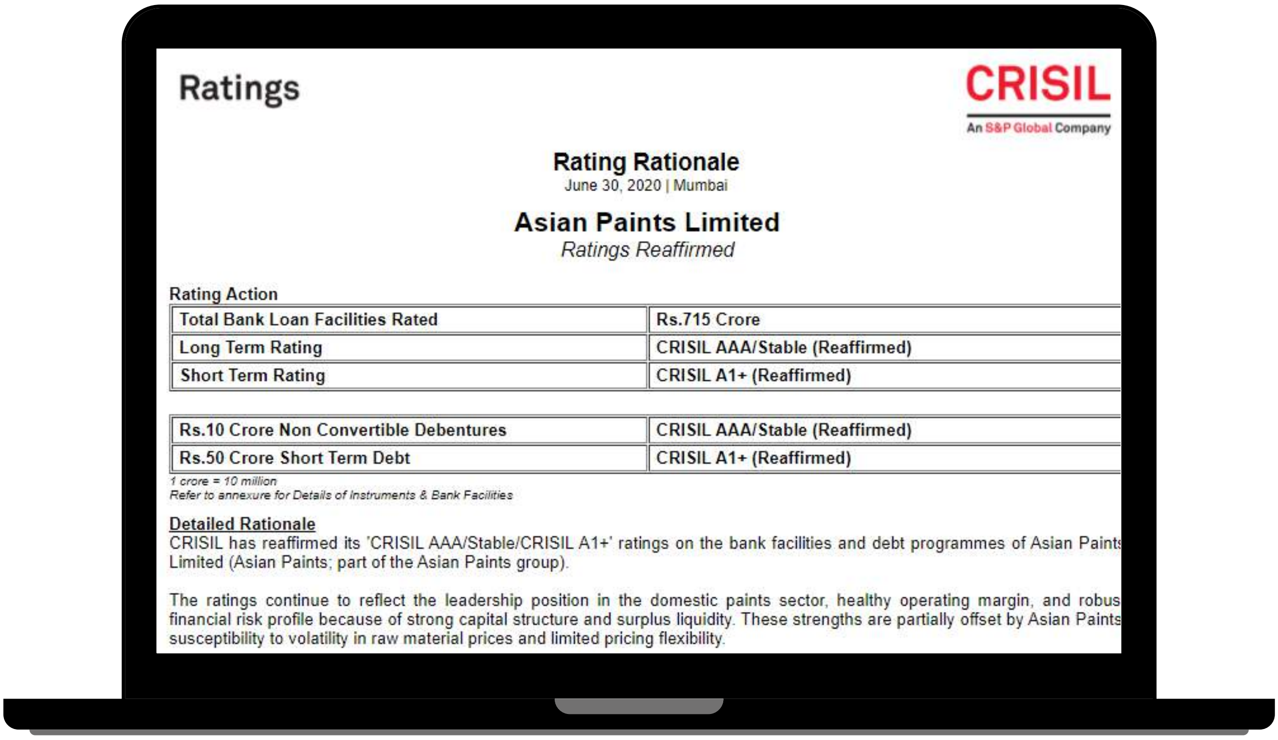


2

SCROLL TO THE END OF THE PAGE. WE WILL SEE 'CREDIT RATINGS' SECTION.

We can select on any of the options given in the section





Ratings

CRISIL
An S&P Global Company

Rating Rationale
June 30, 2020 | Mumbai

Asian Paints Limited
Ratings Reaffirmed

Rating Action

Total Bank Loan Facilities Rated	Rs.715 Crore
Long Term Rating	CRISIL AAA/Stable (Reaffirmed)
Short Term Rating	CRISIL A1+ (Reaffirmed)

Rs.10 Crore Non Convertible Debentures	CRISIL AAA/Stable (Reaffirmed)
Rs.50 Crore Short Term Debt	CRISIL A1+ (Reaffirmed)

1 crore = 10 million
Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale
CRISIL has reaffirmed its 'CRISIL AAA/Stable/CRISIL A1+' ratings on the bank facilities and debt programmes of Asian Paints Limited (Asian Paints; part of the Asian Paints group).

The ratings continue to reflect the leadership position in the domestic paints sector, healthy operating margin, and robus financial risk profile because of strong capital structure and surplus liquidity. These strengths are partially offset by Asian Paints susceptibility to volatility in raw material prices and limited pricing flexibility.

The credit rating report is a good place to begin at but they have to be combined with a lot of in-depth research and analysis of the company's finances and business. This requires both skill and time significantly. A detailed description of this is beyond the scope of this book set. Hence, it is prescribed for the majority to go with investing in fixed income assets via Mutual Funds and Portfolio Management Services.

Also, fixed income assets require an understanding of forwarding rates and spot rates and how they are moving. All these are financial concepts best left to financial experts and much beyond the scope of our Lazy Plan. So, we will focus on what a lazy would have done – Indirect Fixed Income Ownership.

Let us now discuss the last topic relating to fixed income assets i.e. How to buy them in India". People who do not intend to buy directly, can skip this part if they want and move to the next section about mutual funds.

HOW TO BUY?

In India, buying bonds directly is still a complicated task and comes with multiple obstructions. There are primarily a couple of ways in which bonds can be bought and sold. These are as follows-

OVER THE EXCHANGE

It refers to buying and selling in a manner that is similar to shares. NSE and BSE allow buyers and sellers to meet on the platform and transact. Similar to shares, demand, and supply on the platform decide the price of the share. However, in India, only a small fraction of bonds are traded over the exchange. Most others engage in trading over the counter.

OVER THE COUNTER

It refers to manually looking for buyers or sellers of the asset, getting in touch with them, and then negotiating a deal one-on-one. It is difficult for individuals to trade these bonds because they may not have the required connections to find the other party. Moreover, it requires minimum lot sizes. So, a person buying must buy at least 1 lot of a particular asset which will be worth a few lacs. A majority of the readers with only a few thousand to spend will never be able to invest in the securities.

To buy government bonds, we can use NSE or BID app. Today, new-age companies have been working on making the transaction of bonds relatively simpler. Zerodha has a few products on its platform and Capitalmind runs a website by the name of buybonds.in in India. However, these are not very well developed yet, and buying bonds and fixed income securities remains a difficult task and not within the ability of most individuals.

With this, we end our discussion on fixed income assets. In the next section, we will understand more about mutual funds and how it allows us to access the different asset classes and get help from experts in the field.

05

REAL ESTATE

GETTING STARTED

Real estate is one of the most popular asset classes. because it is a physical asset. Stocks and bonds at the same time are financial assets or, paper assets. As a result, people have become more comfortable holding physical assets than paper assets, as physical assets have utility value attached to them. Also, real estate is something that everyone has been directly or indirectly related to, unlike the case with financial assets.

Another reason why real estate is really popular in India is because of its power to consume black money. The government is taking significant steps continuously to reduce black money circulation in the economy. However, historically, it has been one of the parking spots of black money. Let us now understand the major drawbacks and benefits of real estate as an asset class.

STABLE INCOME SOURCE

Real estate provides a stable source of income in the form of rental yield. The tenants are generally sticky on an annual basis and as a result, they provide a stable source of rental income to the owner.

ALLOWS USE OF LEVERAGE

Real estate is the only asset class where debt or loans can be used to buy the assets and hence, increase our returns. No other asset class can be bought using loans.

ENTERTAINS BLACK MONEY

Real Estate is one of the key asset classes when it comes to parking black money. Despite its unethical and risky nature, if someone is still bent on using black money, real estate has always been one of the most prominent avenues to entertain the same.

PSYCHOLOGICALLY EASY TO HOLD

We already saw on the previous page that real estate is a physical asset and along with investment value, it also has a utility value attached to it. As a result, it is psychologically easier to buy and hold real estate than other asset classes.

REAL ESTATE IS A BULKY PURCHASE

Each asset is a bulky purchase. A person with Rs. 10,000 can buy mutual funds, and invest in fixed deposits but cannot buy a piece of real estate. Hence, a SIP sort of arrangement is not functional in real estate.

REAL ESTATE IS ILLIQUID

It takes a few months to a few years to sell a piece of real estate. The process of finding a buyer who likes the property takes a lot of time. Thus, we cannot meet short term goals using real estate investments.

REAL ESTATE NEEDS MAINTENANCE

We have to take care of repairs, incur electricity charges, society charges, housekeeper charges, and so on. Thus, real estate maintenance takes time and a lot of effort. This is not the case with other asset types.

TERMS TO KNOW

RERA ACT (REAL ESTATE REGULATORY AUTHORITY ACT)

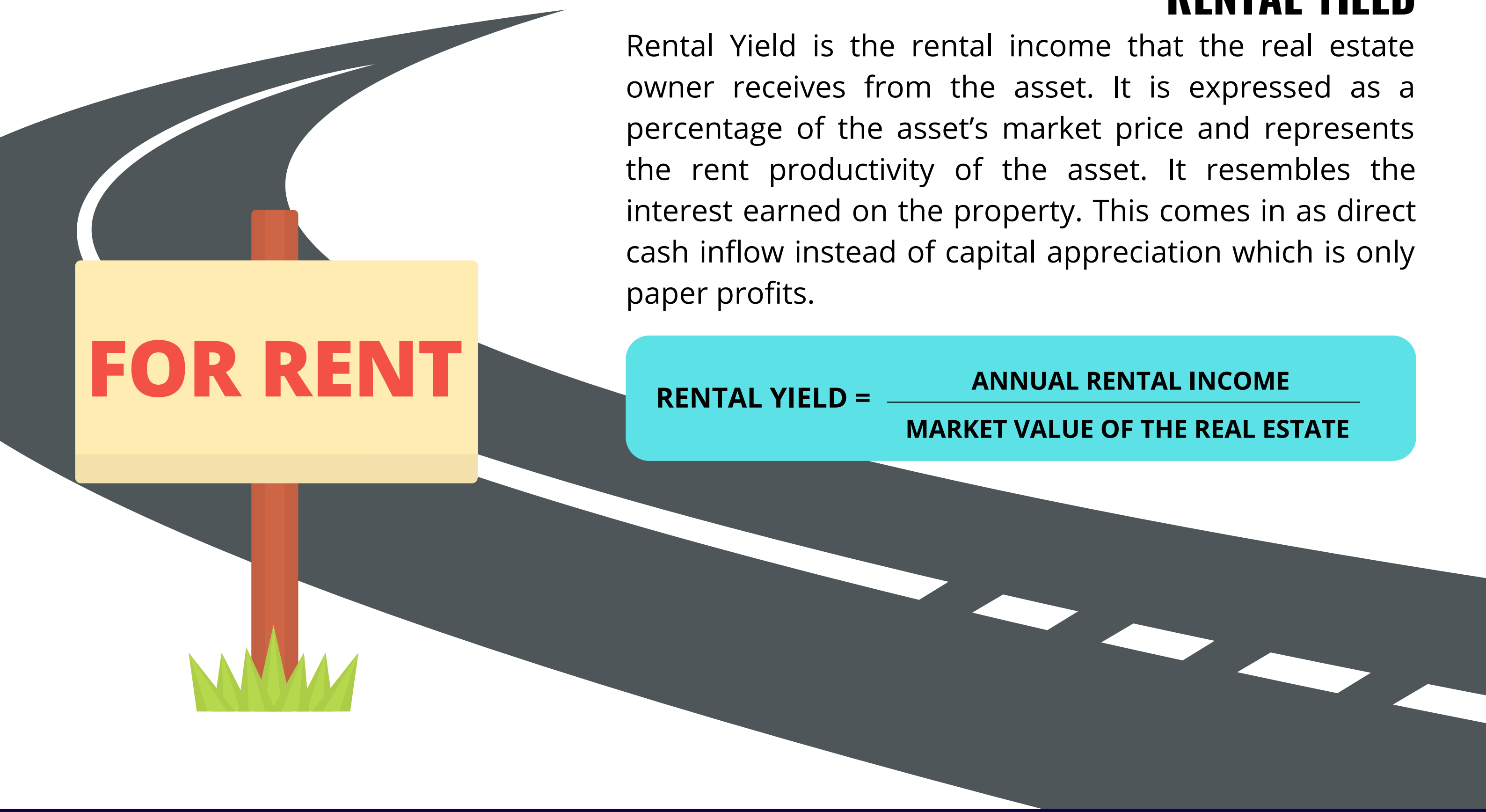
The Government of India introduced the RERA bill intending to safeguard the interests of homebuyers across the country and to prevent them from being exploited by builders. So, RERA Act created authority in each state that will have to grant permission to every project. Each project comes with a specified time limit and if the project is not completed before the deadline, the builder will be liable to pay interest to the homebuyers. Also, builders will not be able not to misuse the money given to them to construct their properties.

RERA is one of the most important Acts related to real estate development. It brings transparency to space and safeguards the interests of buyers.

RENTAL YIELD

Rental Yield is the rental income that the real estate owner receives from the asset. It is expressed as a percentage of the asset's market price and represents the rent productivity of the asset. It resembles the interest earned on the property. This comes in as direct cash inflow instead of capital appreciation which is only paper profits.

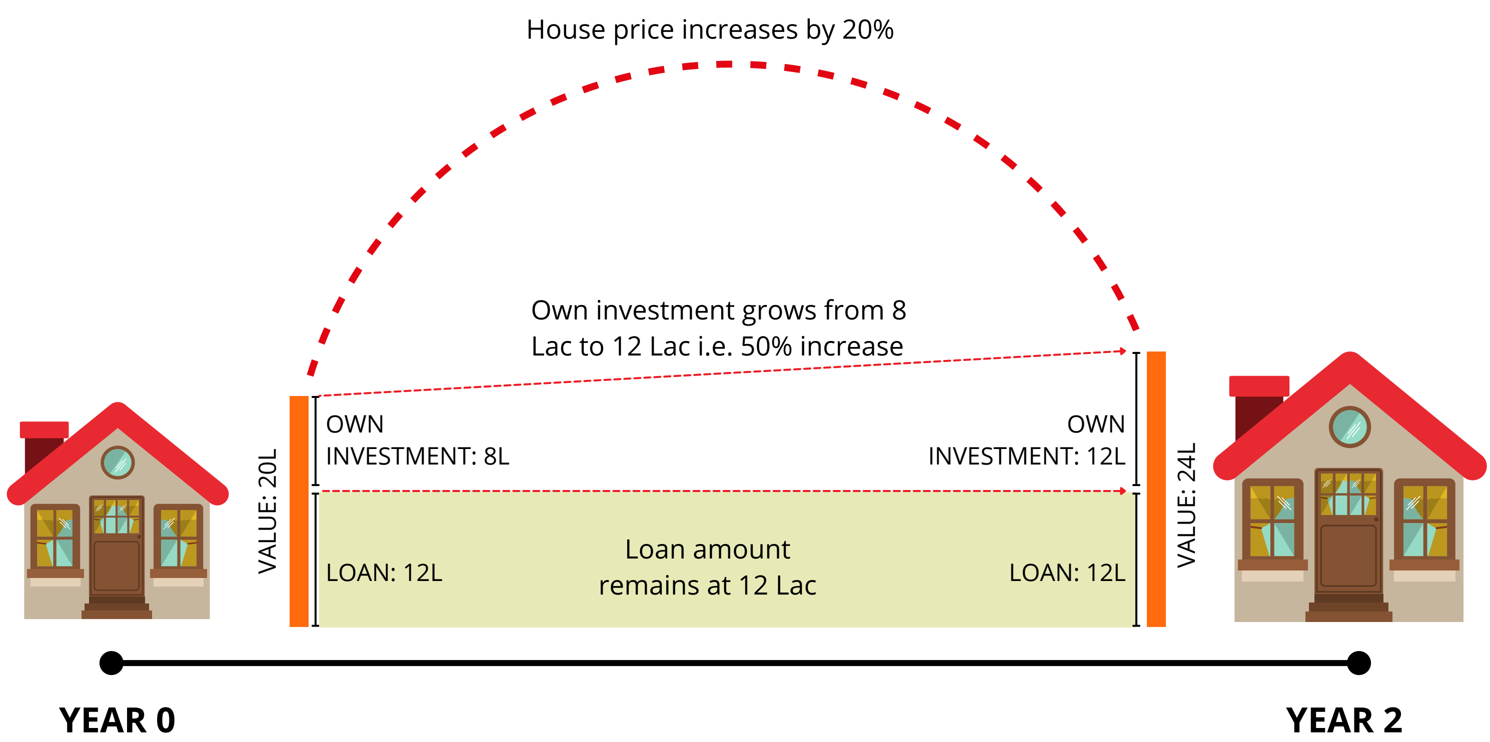
$$\text{RENTAL YIELD} = \frac{\text{ANNUAL RENTAL INCOME}}{\text{MARKET VALUE OF THE REAL ESTATE}}$$



EXPECTATIONS

You can earn in real estate only when you have an understanding of micro markets or the immediate area of the property. Real estate returns are determined by the surroundings of the property– schools, residential facilities, neighborhood, transportation, etc. It is very difficult to generalize real estate returns. The returns and risks all depend on the micro-markets i.e. the immediate surroundings of the property.

However, in general, as an asset class, real estate beats inflation by a fair margin. Also, it allows us to use leverage and increase our returns. Let us see how this works. For instance, let us say, we intend to buy an asset worth Rs. 20 lac. We put Rs. 8 lac in equity and borrow the remaining Rs. 12 lac. The price of the property goes up by 20% in the next 2 years i.e. to Rs. 24 lac. With this increase, our equity increased from Rs. 8 lac to Rs. 12 lac. Thus, a 20% increase in prices led to a 50% increase in our equity. This is due to the use of leverage or debt. Using leverage increases our returns manifold. However, debt is a double-edged sword i.e. the opposite is also possible. If the asset price goes down by 20%, our investment amount will reduce by more than 20%. If managed well, real estate portfolios can give excellent returns. However, this requires a lot of time, attention, and skill.



SUITABILITY

Real estate is suitable for people who are generally scared of mutual funds, equity, and debt. It is for those, who are not comfortable with the financial assets and would prefer physical assets.

Secondly, real estate is suitable for someone who is buying the asset not only for its investment value but also for its utility value. For instance, a person buying a house is also looking for a place to stay. It is not merely an asset. Similarly, a person buying land might consider farming or building a factory on the same.

Other than this, real estate may be suitable for anyone who has inherited a lot of ancestral property. As so much property is inherited, it is difficult to liquidate it and invest it efficiently in other asset classes and as a result, real estate is suitable.

Long term and experienced real estate investors can buy real estate and make a great return out of it, making judicious use of debt. However, this too is a skill that needs to be learned over time. In most cases, it does not make sense to buy real estate with 100% equity unless prices are volatile.

HOW TO SELECT

The selection process of Real estate investments is unstructured and there is no fixed method. Let us understand the common aspects of the evaluation process.

Firstly, we know that real estate returns depend on the location and surroundings. The economic growth in the surroundings– people coming to stay, roads and infrastructure developing, businesses growing, etc. are the factors that lead to an increase in demand for real estate in any given area. The process cannot be generalized as each micro-market is different and also, within each micro-market, individual properties are different. It depends on one's understanding of micro-markets, the demand and supply forces.

Even firms that invest in real estate, employ a large workforce to understand each micro-market. It is very difficult for individuals to evaluate all properties. Instead, individuals operate on an 'Availability' basis.

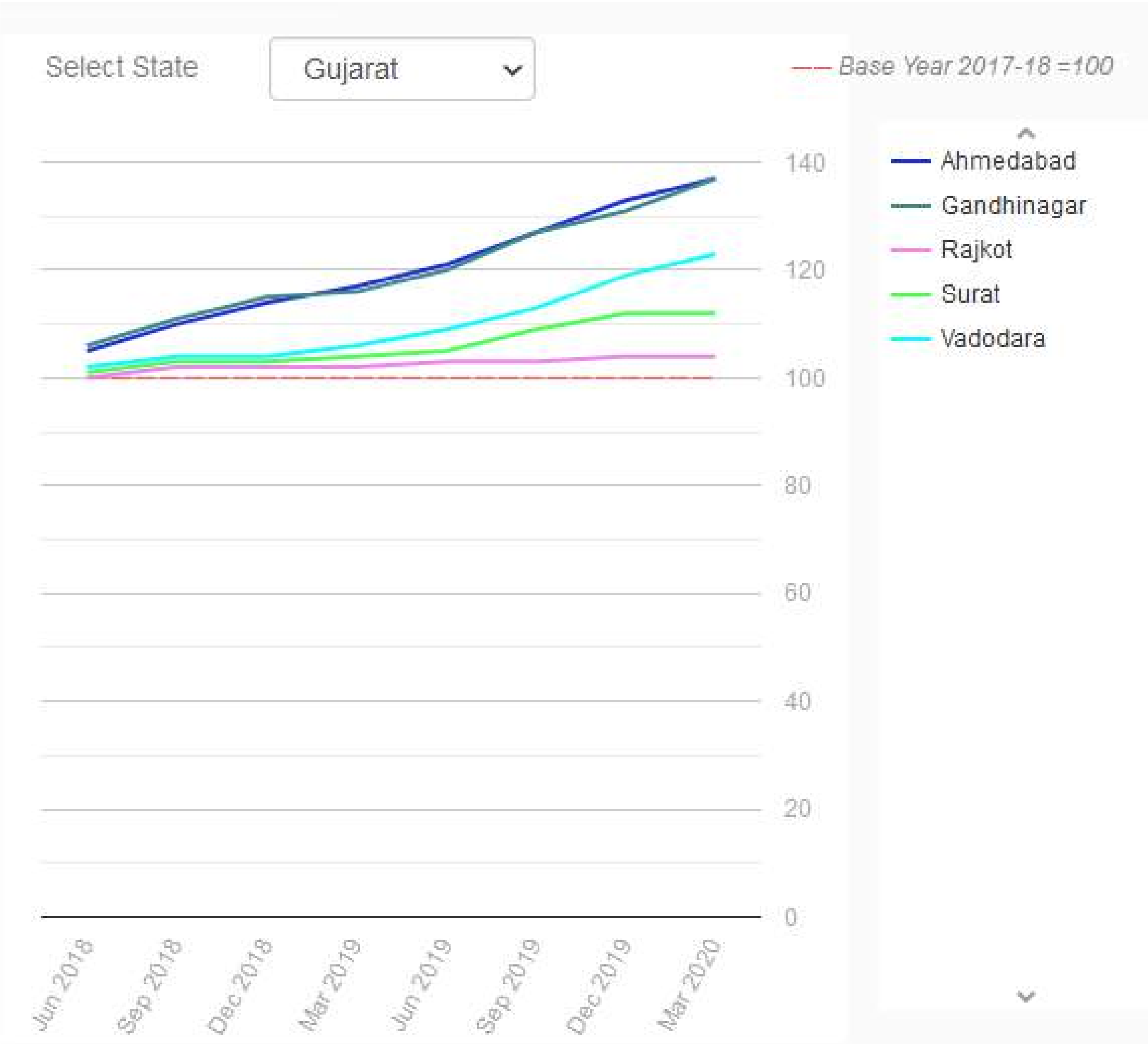
HERE WE LIST DOWN BASIC CHECKS THAT ARE TO BE CONDUCTED TO UNDERSTAND AND BUY REAL ESTATE INVESTMENTS –

- MICRO-MARKET IN WHICH THE REAL ESTATE FALLS IN.
- CLEAN HISTORY OF THE REAL ESTATE
- RERA CERTIFICATION
- CLEAR LAND USE TITLE
- LOCATION OF THE REAL ESTATE ASSET
- STATE OF INDUSTRY THAT EMPLOYS MOST OF THE PEOPLE USING THAT REAL ESTATE.

BASED ON THIS, A PERSON CAN FINALIZE HIS REAL ESTATE INVESTMENT. MANY OTHER FACTORS GO INTO IT AS WELL. REAL ESTATE INVESTMENTS ARE A RATHER LONG PROCESS AND BEYOND THE SCOPE OF THIS BOOK. HOWEVER, THE ABOVE MENTIONED REAL ESTATE FACTORS CAN HELP US EVALUATE A LARGE PART OF THE INVESTMENT

RESIDEX

Earlier, real estate prices all over India and within different cities could not be tracked and understood as each had a different trajectory. So, the National Housing Board, a subsidiary of RBI, launched RESIDEX – an index for housing prices across the cities. It depicts the changes in real estate prices in different states and cities over the years (2013 and onwards). It gives us a sense of direction and speed about each city and its residential real estate market. It can be found on the website - https://residex.nhbonline.org.in.



Source : https://residex.nhbonline.org.in

REITS - REAL ESTATE INVESTMENT TRUSTS

Investing in real estate is a very cumbersome process and often overwhelming for many. Additionally, it requires a large amount to invest in real estate. However, if done well, the rewards are commendable. A solution to overcome the previously mentioned problems for those who wish to invest in real estate without considerable effort would be to invest in Real Estate Investment Trusts (REITs). REITs are similar to mutual funds but are for real estate. REITs can be bought like ordinary shares in the market. In India, there is only three REITs at the time of this writing – Embassy Office Parks. However, we hope to see more shortly.

Just like mutual funds, in REITs too, a large number of individuals pool their money and fund managers invest the same in income-generating real estate. Securities Exchange Board of India (SEBI) mandates that REITs need to distribute at least 90% of their yield to investors as dividends. The capital appreciation of the real estate is reflected in the stock price of REITs. Currently, Rs. 50,000 is the minimum amount that needs to be invested in REITs. Also, illiquidity is a major factor when it comes to real estate. REITs are much more liquid than a typical real estate property.

With this, we end our discussion on real estate, its characteristics, RESIDEX, and REITs. Real estate is psychologically very easy to hold and if done well, can be very rewarding. However, on the darker side of the moon, it requires a lot of time, effort, and skill. All portfolios don't need to have real estate. Purely from an investment perspective, real estate has more substitutes. It depends a lot on an individual’s personal biases and the Lazy Profile that we had created earlier. In the next section, we will see where exactly in our Lazy Plan does real estate fit.

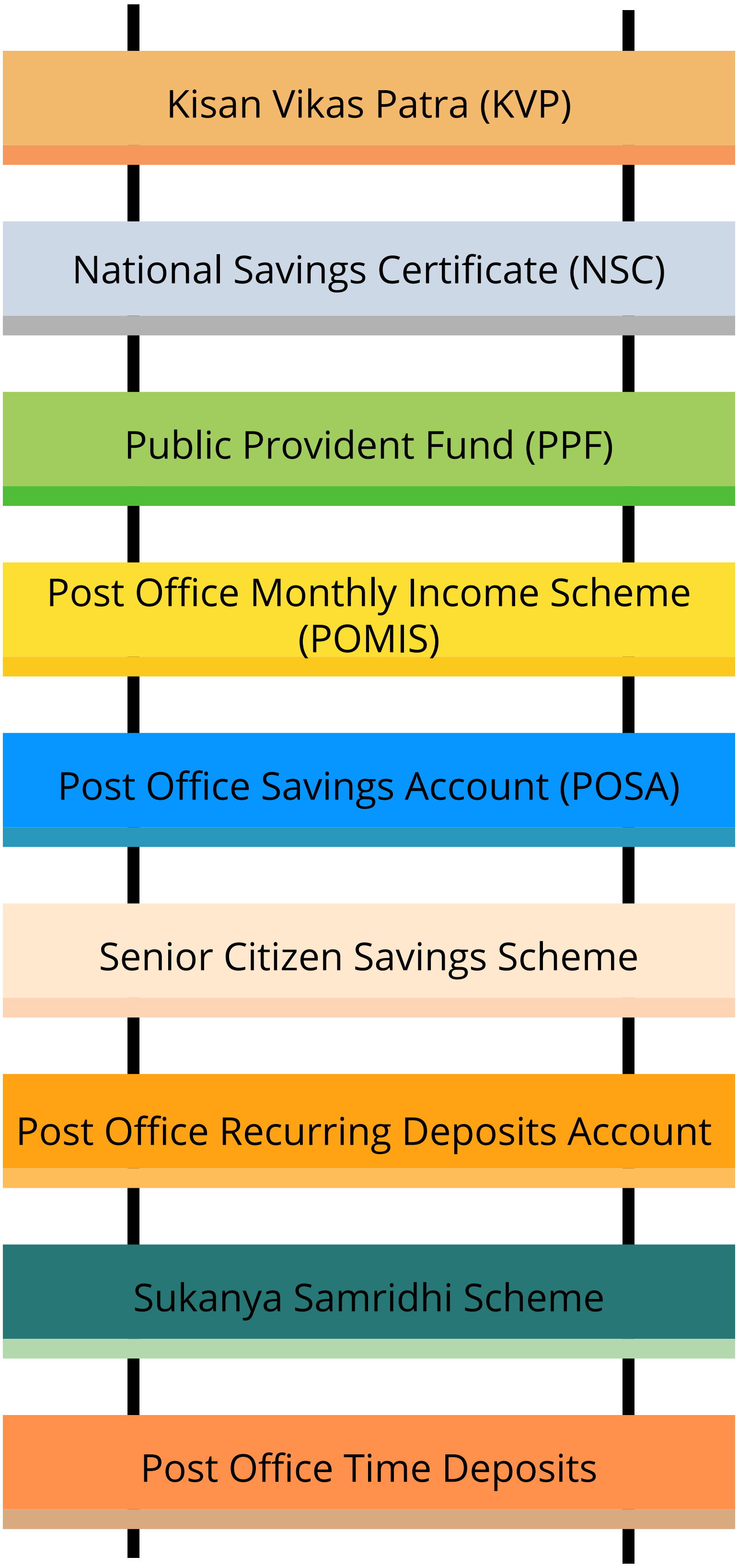
06

SMALL SAVINGS

GETTING STARTED

The next asset class that we will talk about is small saving schemes. The Government of India along with its institutions runs various small saving schemes. These small saving schemes are created keeping in mind the needs of the individual saver. The objective of all these schemes is to encourage financial inclusion and inculcate savings and financial planning as a habit in various sections of society. Some of these offer lucrative returns, some offer tax benefits and some are designed to achieve a particular goal.

Small saving schemes will form a central part of the Lazy Financial Plan for various segments of the society. We will learn about various small savings schemes, the reason for their establishment, their return and tax implications, their suitability, and much more.



KISAN VIKAS PATRA

Kisan Vikas Patra is a small saving scheme that was launched by the government to encourage long-term financial discipline in people, particularly in farmers. The objective was to offer a savings tool for those in rural parts of the country with no bank account. So, they could save for themselves using this instrument which is managed by the Indian Postal Department.

INTEREST	As of May 2020, KVP offers 7.7% p.a. However, one needs to check before investing about the latest interest rate. Principal doubles every 118 months (9 years and 10 months)
TENURE	KVP matures in 118 months. It returns double the amount invested in this time frame.
TAX TREATMENT	The returns generated by investing in KVP is completely taxable under ordinary income each year.
SUITABILITY	KVP is suitable for people who do not have access to the proper banking system and live in distant places where access to financial instruments is difficult. For most ZebraLearners, KVP will have better substitutes in Fixed Deposits and Debt Mutual Funds.
PURPOSE	Good for risk-averse individuals, who have surplus money and do not need it for a few years to come. However, there are much better alternates than KVP currently. KVP makes sense only when access to the banking system and banks is difficult. Otherwise, much better instruments exist. It can also be used as collateral to get loans.
PREMATURE WITHDRAWAL	Premature withdrawal of cash is allowed after 2.5 years from the day it is bought. The entire principal and the interest can be withdrawn. However, an interest rate that is slightly lower than agreed interest is paid out on premature withdrawal.
HOW TO BUY	We can visit banks or even select banks that can help us buy the same.

NATIONAL SAVINGS CERTIFICATE

National Saving Scheme was introduced to encourage small and mid-income investors with a low-risk appetite to invest while saving taxes. This is again managed by the Indian Postal Department and operates on lines similar to fixed income security. This also has a provision of tax savings. Let us understand the important features of the same:

INTEREST	As of May 2020, NSC offers an interest return of 7.9% p.a. compounded annually, which is all paid at maturity.
TENURE	NSC matures in 5 years and then the money can either be withdrawn or can be re-invested into NSCs along with the entire principal and interest.
TAX TREATMENT	The returns are taxed under ordinary income. However, while making the investment, the amount invested can be claimed for a deduction under Section 80C of the old regime of tax law. The limit here is Rs. 1.5 lacs across categories that we can invest in.
SUITABILITY	NSC is suitable for people who do not have access to the proper banking system and live in distant places where access to financial instruments is difficult. NSC is also suitable for low risk-taking ability individuals and those who are looking for investments under section 80C.
PURPOSE	It is mainly to promote savings in small and mid-income individuals and those who do not have complete access to the banking system. NSC incentivizes savings by allowing tax deductions when the money is being invested.
PREMATURE WITHDRAWAL	Premature Withdrawal of NSC is restricted. It can only be withdrawn if the policyholder passes away, or by court order, or a Government Officer forfeits the account. In case of time less than 1 year, no interest is paid and in case of withdrawal after 1 year, the entire amount and interest are paid.
HOW TO BUY	We can visit select banks that can help us buy the same.

PUBLIC PROVIDENT FUND

Public provident fund is an instrument that was started to help individuals save for old age along with earning interest and saving taxes on the same. PPF is a combination of tax benefits, retirement planning, and interest return that effectively creates a popular asset category. It allows both salaried and non-salaried classes to save for their future.PPF is again on the lines of fixed income security and is maintained by National Savings Institute. Let us understand the important features of the same:

INTEREST	As of May 2020, PPF offered 8.0% compounded annually. The interest rate keeps on changing and we need to check the latest PPF interest rates. A simple Google search will give the answer.
TENURE	PPF matures in 15 years and the maturity can be further extended by 5 years at a time when the maturity date is approaching. Due to the long maturity, PPF becomes a useful tool for low-risk individuals looking to plan for long term goals.
TAX TREATMENT	The most attractive part of a PPF investment is its Exempt –Exempt - Exempt category. The amount invested in PPF can be claimed for deduction at the time of investment under section 80C. The interest earned and the return accumulated are all tax-exempt. Thus, no taxes are to be paid on PPF throughout the holding process.
SUITABILITY	PPF is a very suitable form of investment for those planning for Long Term Goals with Debt-like securities. It is suitable for low and moderate risk-taking individuals. However, the key here is that long-term goals can only be met by these as it comes in with strict Pre-Mature withdrawal restrictions. For high risk-taking ability, equity mutual funds will still be more lucrative. Also, PPF restricts the amount that can be invested by one individual to a maximum of Rs. 1.5 lacs per annum.
PURPOSE	The main purpose as said earlier is to have an investment tool to plan for long-term financial goals, at the same time taking advantage of tax savings and an attractive interest return. It helps individuals to plan for long term goals.
PREMATURE WITHDRAWAL	Premature withdrawal of PPF is restricted. It allows a withdrawal of 50% of the corpus at the end of 4 years and part pre-mature withdrawal after 6 years. The withdrawals are restricted. Post 5 years, pre-mature closure of account is permitted under special circumstances.
HOW TO BUY	PPF account has to be opened with post offices or banks. It can be opened online as well as offline.

SENIOR CITIZEN SAVINGS SCHEME

Senior Citizen Savings Scheme is a financial scheme that was created particularly to serve the needs of senior citizens. The scheme offers preferential interest rates to senior citizens who have retired from their jobs and are living off their savings. It is backed by the government to offer additional layers of security for citizens above 60 years of age. Let us understand the important features of the same:

INTEREST	As of May 2020, SCSS offers an interest return of 7.4% p.a. compounded quarterly. The interest rate is revised every quarter and one needs to check for the latest interest rate.
TENURE	SCSS matures in 5 years from the day Investment is made and also, can be extended for an additional 3 years on maturity. Currently, the extension option for one deposit is only available once.
TAX TREATMENT	Investments made in Senior Citizen Saving Schemes do qualify for a deduction in Section 80C. However, interest and return on SCSS are fully taxable under ordinary income tax bracket.
SUITABILITY	SCSS is suitable for Senior Citizens who have very low risk-taking ability and cannot afford to lose money. The security by the government makes this a safe investment. For those with Higher Risk taking ability, they can combine SCSS with other higher-risk asset classes as well.
PURPOSE	The purpose is to have an instrument that specifically meets the needs and requirements of Senior Citizens. The instrument scheme is backed by the Government, which provides an additional layer of security to senior citizens for whom ordinary income source has stopped
PREMATURE WITHDRAWAL	No Premature Withdrawal is allowed in the first year of investment. For premature withdrawals made between years 1 and 2, a penalty of 1.5% is imposed on the interest and for premature withdrawals after 2 years, a penalty of 1% is levied.
HOW TO BUY	We can visit post offices or even select banks that can help us buy the same. A nominee has to be appointed when opening such an account.

SUKANYA SAMRIDDHI YOJANA

Sukanya Samriddhi Yojana was a special financial scheme initiated by the Government of India that encourages investment towards girl child's marriage and education. The scheme is managed by the banks. The scheme aims at promoting education for girls and their welfare in the country while paying unwavering attention to their needs. Let us understand the important features of the same –

INTEREST	As of May 2020, Sukanya Samriddhi Scheme offers an interest return of 7.6% p.a. compounded annually, which is all paid at maturity.
TENURE	Sukanya Samridhi Scheme matures in 21 years or when a girl turns 21, whichever is sooner. Partial maturity occurs when the girl turns 18 as well. The entire principal and interest is paid at maturity.
TAX TREATMENT	The returns are taxed under ordinary income. However, while making the investment, the amount invested can be claimed for a deduction under Section 80C of the old regime of tax law. The limit here is Rs. 1.5 lacs across categories that we can invest in.
SUITABILITY	Sukanya Samriddhi Scheme Account can be opened by the guardian of a girl child under the age of 10. The account can be closed after the completion of 21 years. So, this is suitable for anyone who has lower risk-taking ability or willingness and needs to plan for their girl child's future. Alternate asset classes to plan for the same is suitable for those with relatively higher risk-taking ability.
PURPOSE	Sukanya Samriddhi Scheme was introduced to plan for Education and Welfare of Girl Child in the country by providing a reliable financial program for the same.
PREMATURE WITHDRAWAL	Premature Withdrawal of the Sukanya Samridhdhi Scheme is restricted. 50% of the previous year's balance can be withdrawn once the girl turns 18. Full withdrawal can be done under specific circumstances – the medical treatment of girl child under life-threatening disease or death of the guardian. Otherwise, premature withdrawal is very restricted.
HOW TO BUY	We can visit post office or select banks that can help us buy the same. This cannot be opened online.

POST OFFICE MONTHLY INCOME SCHEME

Post Office Monthly Income Scheme is a special scheme managed by the Post Office to support those who need a stable source of income. We deposit our money under this scheme, and interest is paid out each month. The principal can be redeemed at the end of the tenure. We can also, opt for the distribution of the principal. This means, interest and principal will be distributed as monthly payments and the corpus will exhaust at maturity. The monthly payments can be used to meet expenses. Let us understand the important features of the same –

INTEREST	As of May 2020, POMIS offers an interest return of 6.6% p.a., payable monthly. We can also opt for a payout for Principal in an amortized manner.
TENURE	POMIS comes in with a maturity of 5 years.
TAX TREATMENT	POMIS offers no favorable tax treatment. It is not deductible under Section 80C and also interest is taxable under ordinary income tax bracket.
SUITABILITY	POMIS is suitable for those who rely on assets more than income. This includes mainly senior citizens who have retired. There are private mutual funds as well that offer Monthly Income Schemes. So, for lower risk-taking ability, POMIS is the way to go and for those with high risk-taking ability, they can evaluate other schemes as well. Monthly Income Scheme comes in very handy when regular income has stopped- For instance, for retired senior citizens. These can be combined with SCSS to meet post-retirement goals exceptionally well.
PURPOSE	POMIS is mainly run with an incentive to provide a tool to promote the Protection of Capital. It also helps those who rely on assets to meet their expenses rather than their active income. It provides a constant monthly inflow of cash.
PREMATURE WITHDRAWAL	Within 1 year, premature withdrawal is impossible. Between 1 year and 3 years, the entire corpus can be returned with a penalty of 2%. Between 3 years and 5 years, the entire corpus can be returned with a penalty of 1%.
HOW TO BUY	They can only be opened with a post office by visiting the same offline.

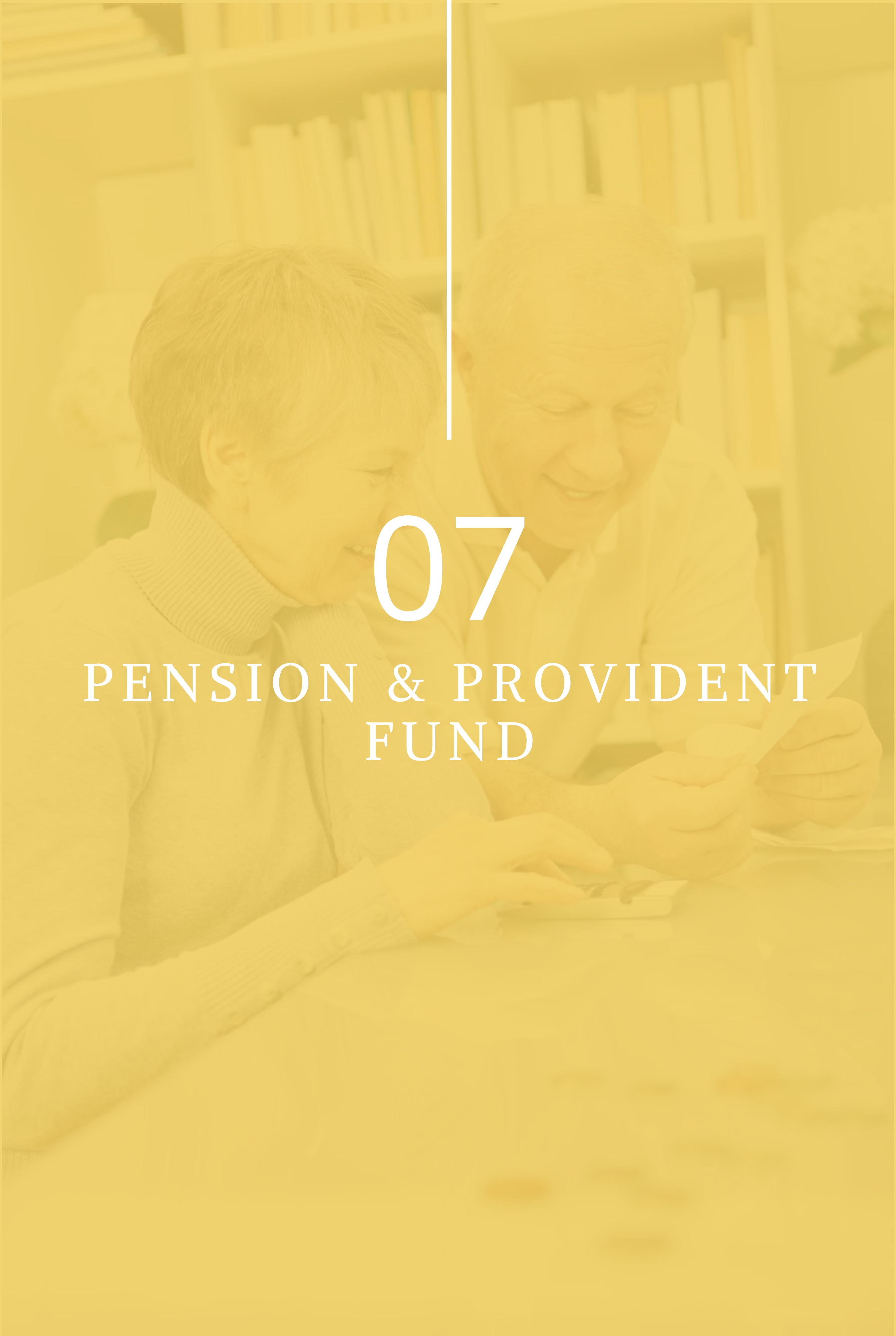
POST OFFICE SAVINGS ACCOUNT/ FIXED DEPOSITS/ RECURRING DEPOSITS

Earlier, the Indian Post Office was much more wide-spread than the bank branches. Hence the Government of India decided to offer banking services through Post Offices. This was done to improve financial inclusion. The banking facilities include a savings account, fixed deposit account, and recurring deposit account. These are exactly the same as the ones offered by banks. The products, risk-return, and suitability are identical to those of banks. Let us understand the important features of the same.

INTEREST	In line with Public Sector Banks
TENURE	As per the scheme and product selected
TAX TREATMENT	No preferential treatment is given in terms of tax.
SUITABILITY	For those who can access banking, banks are always advisable as they have a larger variety of offerings. Post Office Schemes are suitable for those who cannot access banks or it is too far from their place. However, with digital banking gaining prominence, this will reduce

PURPOSE	The purpose is to promote Financial Inclusion and take banking products to distant parts of the country as well where banking cannot reach.
PREMATURE WITHDRAWAL	Restrictions depend on the product selected.
HOW TO BUY	They can only be opened with a post office by visiting the same offline.

With this, we end our discussion on small saving schemes. These are the common schemes that are offered in India and when creating a Lazy Financial Plan, these will play a critical role. We must check the suitability of each of them to decide which ones are suitable for us and our financial goals. The interest rates for these keep on changing and we need to verify the same before we go ahead with them.



07

PENSION & PROVIDENT FUND

PENSIONS & PROVIDENT FUNDS

The next asset class that we will discuss is the National Pension Policy and the different provident funds. All these are offered by the government with a primary objective of long term financial planning and mainly retirement planning. We will learn more about them, their use, their functioning, and their role in the entire financial plan. Let us first begin with the pension. Till the age of 60, a person is working and is getting a salary to support their day to day expenses. However, once they retire, the salary stops coming in. Here, a pension comes in handy and allows them to meet their expenses. During their working years, people save a small part of their income for their retirement. Then they get this as a regular monthly inflow in the form of a pension. We have already been introduced to 3 methods of retirement planning.

We can follow any of the three methods and do it in 2 ways- one, manage our retirement corpus on our own by selecting mutual funds and assets by self and second, give the money to the government and let them take responsibility for our pension.

The government schemes offer relatively lower returns but higher stability and security. More importantly, they come in with a lock-in feature that helps those who lack financial self-discipline. At the same time, managing on our own allows us to manage as per our needs and invest in assets with higher returns. So, we will suggest a balance between the two– the stability and security of the government and combined with higher returns by self-management. The government runs a National Pension Scheme for pensions.

NATIONAL PENSION SCHEME

NPS is a Government-run scheme that focuses on retirement planning of professionals and the self-employed. Under NPS, the amount can be invested in select asset classes as identified by the scheme. The person keeps depositing money every year in his account which keeps on compounding. On retirement, the corpus is distributed as a pension to the beneficiaries.

HOW IT WORKS?

A person opens a pension account which is managed by the Pension Fund Regulatory and Development Authority (PFRDA). They keep depositing the money in the same account with strict withdrawal restrictions. They can select the asset class where they want their money to be invested and based on the asset class selection, returns are generated. Once they start approaching their retirement age, they start receiving cash payments in the form of a pension to support their expenses.

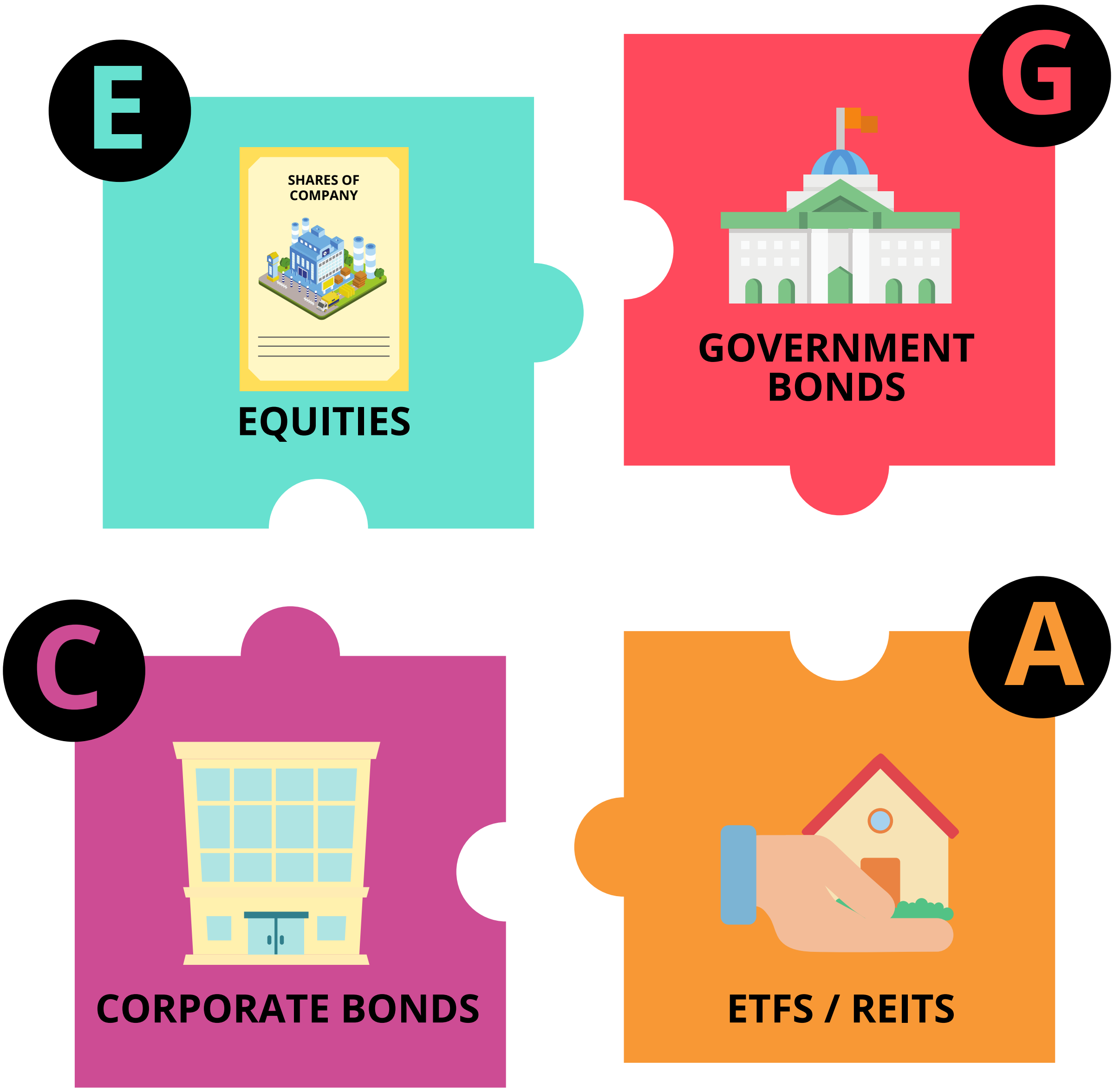
A person below the age of 60 can only withdraw up to 20% of the entire corpus and the rest converts automatically to an annuity (i.e. financial instrument that pays out a regular and fixed dividend). A person above the age of 60, can withdraw a maximum of 60% as a lump-sum and the rest 40% will be converted to an annuity. Payments from the annuity help meet an individual's expenses. Such restrictions on withdrawal enforce discipline from the individual's end.

Below 60 years	Above 60 years
Withdraw Maximum 20% of Entire corpus lump sum	Withdraw Maximum 60 % of Entire corpus lump sum
Rest - annuity	Rest - annuity

NPS ASSET CLASSES

When investing under NPS Scheme, NPS does not promise a fixed rate of return. Instead, it gives a choice to invest in different asset classes and our money is tied to these asset classes. The risk and return of these classes are then reflected in our investments.

Let us thoroughly understand each of these classes. First is the E-class i.e. equity class where our money is invested in equities. Next, the C-class is where the money is invested in corporate bonds. Then, G-class, where the money is invested in Gilt-funds or government bonds. After that, A-class is an open class that allows investments in ETFs and REITs. Lastly, there is an auto-mix format that invests automatically in these classes based on our age. We can opt for anyone or a combination of more than one asset class. Note that there is a 50% cap limit on E-class. Irrespective of our age and circumstances, we cannot invest more than 50% of our corpus in E-class.



NPS investments can be used for deduction under Section 80C that has a limit of Rs. 1.5 lac. Additionally, there is an additional deduction of Rs. 50,000 that can be claimed over and above Rs. 1.5 lac under Section 80CCD-1B. This additional deduction is only for our contribution to NPS. This tax saving is a big incentive for most when it comes to pension planning.

NPS falls in the EET category i.e. Exempt-Exempt-Taxable Category. We can claim deductions when we are making the investments, and the income is exempt when we are accumulating the same. However, when we withdraw the money or get an annuity, the amount is taxable as ordinary income.

TAX TREATMENT

SUITABILITY

NPS is suitable for anyone who is planning for retirement and has a low risk-taking ability. This gives a lot of stability and security as it is backed by the government. Besides, we also saw that NPS gives an additional deduction of up to Rs. 50,000 under NPS.

Individuals should opt for a mix of NPS and managing retirement benefits on their own. So what one can do is, invest up to Rs. 50,000 under NPS to take full benefit from the above scheme. Once the amount exceeds Rs. 50,000 and tax benefits are no longer available, they can go ahead with mutual funds and other asset classes to manage the rest of the portfolio on their own. This gives a good balance of safety, stability, and growth. Also, all those who are below the age of 55, should take advantage of the 50% exposure in E-class.

This is how we can systematically plan for our retirement using various asset classes and combining them with the government schemes. With this, we end our discussion of the National Pension Scheme. Let us now move ahead and understand another class for long term financial planning– Provident Funds.

PROVIDENT FUNDS

Provident funds are arrangements where employees and employers contribute to a pool, throughout the employment tenure of an individual, out of which a lump-sum is given to the individual upon their retirement. There are three types of provident funds – Employees' Provident Funds (EPF), Voluntary Provident Funds (VPF), and Public Provident Funds (PPF). Let us understand this one by one.

EMPLOYEE PROVIDENT FUNDS (EPF)

Employee Provident Fund is a type of provident fund where the employees contribute 12% of their basic salary and dearness allowance towards the EPF during their working years and the same amount is matched by the employer. All this money goes to the Employees' Provident Fund Organisation (EPFO), which is an organization run by the government to manage EPF for individuals.

EPF offers fixed interest and works like typical fixed-income security. EPF offers 8.5% p.a. as of November 2020. However, the rate keeps on changing and one needs to check the updated interest rates before investing. Whenever one changes employment, the EPF must be shifted to the new employer. There are various restrictions on the withdrawal of EPF. Only after the age of 54, can a person withdraw 90% of their EPF savings. Also, there are provisions when one can withdraw in case of unemployment, marriage, medical emergency, etc. if they meet specific criteria.

SUITABILITY

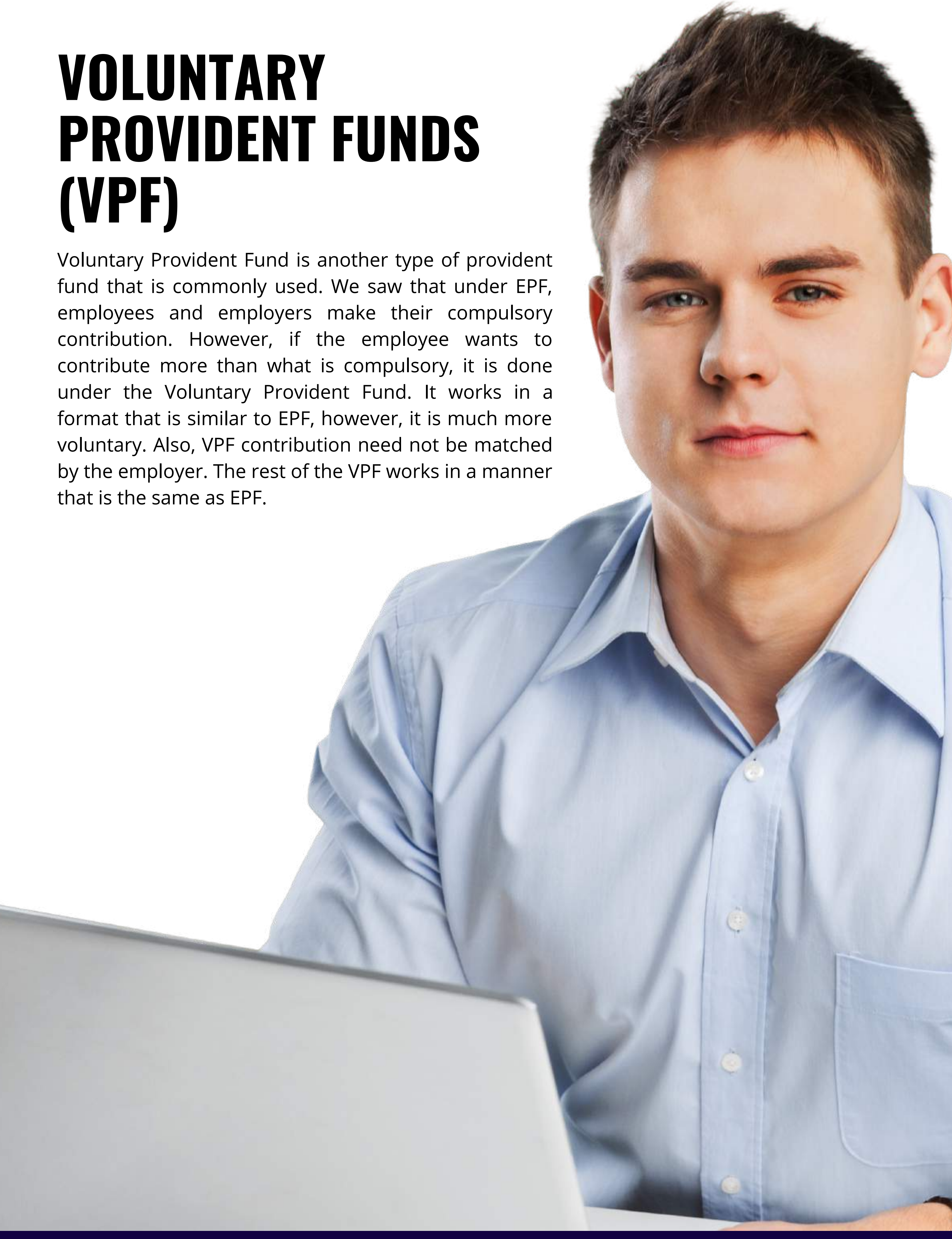
EPF is specifically suited for salaried people and those working in the organized space. It is compulsory for the government employees to have an EPF enrolment, i.e. to have EPF contributions.

TAX TREATMENT

EPF can be withdrawn tax-free after 5 years of service at the same company. Also, EPF contributions are deductible under Section 80C within the limit of Rs. 1.5 lac.

VOLUNTARY PROVIDENT FUNDS (VPF)

Voluntary Provident Fund is another type of provident fund that is commonly used. We saw that under EPF, employees and employers make their compulsory contribution. However, if the employee wants to contribute more than what is compulsory, it is done under the Voluntary Provident Fund. It works in a format that is similar to EPF, however, it is much more voluntary. Also, VPF contribution need not be matched by the employer. The rest of the VPF works in a manner that is the same as EPF.



PUBLIC PROVIDENT FUNDS (PPF)

We see that EPF and VPF are two provident funds under which the salaried class can invest their money. However, for the self-employed, there was no such provident fund. As a result, the Government introduced the public provident fund. We have already discussed PPF in detail in the small saving schemes section. It works similarly. An individual contributes to the fund every year and then gets a lump-sum on maturity. The interest rate for PPF also keeps on changing.PPF comes with a 15-year lock-in which is relatively stricter than EPF restrictions. Also, through PPF we can claim tax benefits under Section 80C up to Rs. 1.5 lac per year.

With this, we end our discussion on provident funds. It is suggested that one must have a combination of these provident funds and assets such as mutual funds when planning for long term finances and particularly those relating to retirement. It provides stability and security as well as higher returns. At the same time, it also forces us to be disciplined as it comes in with lock-ins and restrictions on withdrawals.

08

GOLD

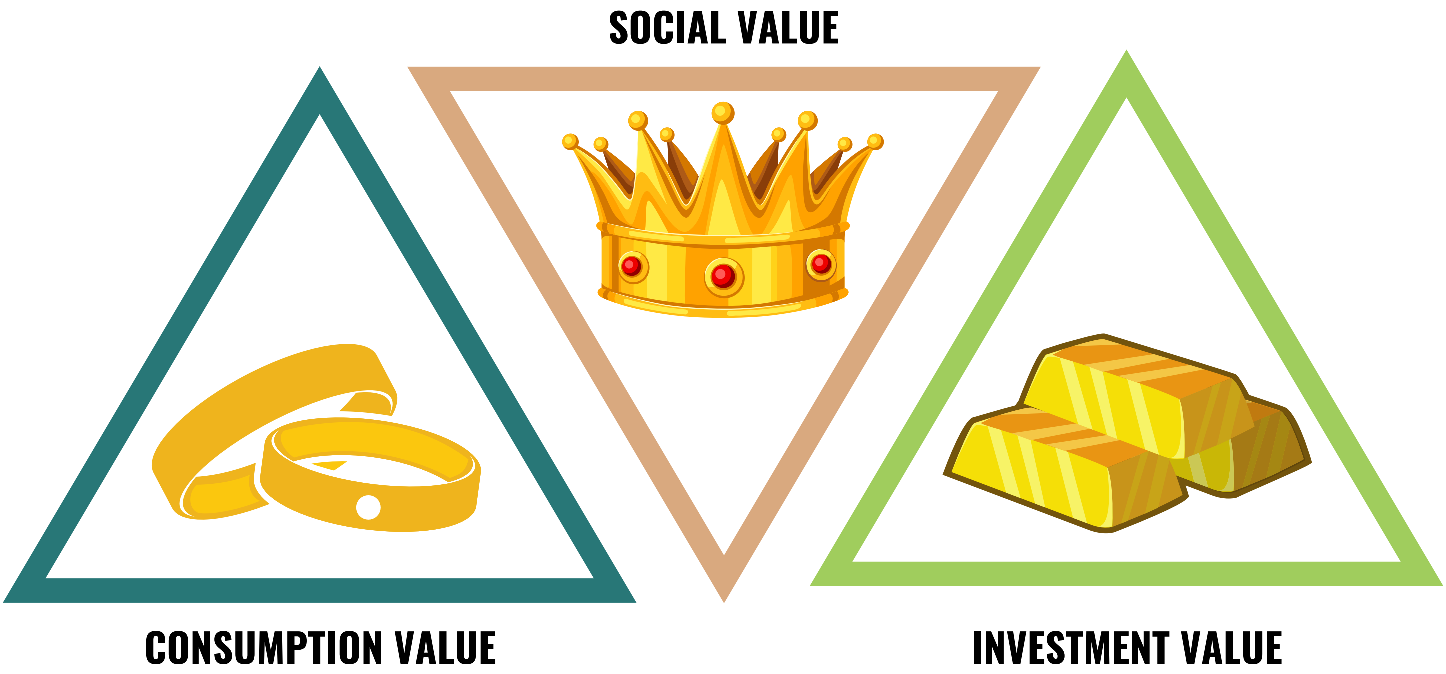
GETTING STARTED

Gold is one of India's favorite asset classes. Nowhere in the world do people buy gold as much as they do in India. This is because gold has multiple usages, unlike most other Investment classes. Gold is bought for its Consumption Value, Social Value and Investment Value. Particularly in Southern states, gold is one of the most common methods to accumulate or store value.

People feel safe with gold as it is a physical asset and has multiple utility points, particularly in Indian society and culture. Let us first spend a moment understanding the three kinds of value gold offers. Firstly, gold has a consumption value. People buy gold for consumption i.e. to use it as jewelry or to gift it to friends and family on important life events.

Next comes Social Value. People with hefty gold reserves are seen as socially more powerful or more influential in India. People wearing expensive gold jewelry are perceived to be well-off and it satisfies an individual's willingness to be a part of the influential segment of the society. So we see that gold comes in with a lot of social value.

Lastly, gold also has investment value. When people buy gold, they buy it assuming that gold will appreciate at price and later it can be sold at a higher price. Very few asset classes have the potential to provide all these three. The closest is real estate. Mutual funds only provide investment value. It is very well justified why gold is such an integral part of the Indian lifestyle.



CHARACTERISTICS

Let us move ahead and understand some characteristics of gold. We will understand these from an investment perspective. We are only evaluating gold as an investment asset, and see where it fits in our Lazy Financial Plan.

SAFETY HAVEN

1

Across the globe, gold is considered a safe haven investment class. What are safe-haven investments? There are certain asset classes that people find psychologically safer and when all other assets go down, fear is at its peak and all that people want is the safety of money, they park their money in such asset classes. They sell other assets i.e.equity, mutual funds, fixed income, etc., and shift the money to such assets. Gold is the most common safety haven asset. Because of its safety haven perception, when prices of equity, bonds, real estate, etc fall and fear grips the market, demand for gold goes up. As a result, the prices of gold go up when everything goes down. Hence, gold becomes a great hedge on the portfolio of various investors.

2

GOLD RETURNS

Over the short term, gold moves freely and short-term fluctuations can give highly negative or positive returns. However, whenever we are talking about the Lazy Financial Plan, we want to focus on the long-term return expectations of the asset. We will not participate in short term fluctuations to meet our goals. Over the long term, gold returns substantially underperform other asset classes. Gold gives returns that match inflation and at times even lower.

In difficult times, gold significantly outperforms all other asset classes. We see that gold does not increase purchasing power, it preserves it at its best performance. However, it compensates for the lost investment value through consumption value and social value.

Source: https://goldprice.org/gold-price-charts/10-year-gold-price-history-in-indian-rupees-per-kilogram

3 HOLDING COSTS

Gold comes with heavy holding costs. When we buy physical gold, there is a cost associated with the storage and insurance of the same. Besides, we continuously carry the risk of theft. All these put together comes down to about 1% of the gold's value per year i.e. cost incurred to hold the physical gold. So, gold becomes one of the worst-performing long term assets when we deduct the holding costs from the long term returns of gold, and. In the long run, it underperforms debt, equity, and even fixed deposits.

Despite the above statements, gold is not necessarily a terrible asset. After all, it is one of the most common asset classes in the country. We will understand the suitability of gold in the coming sections.

HOW TO BUY GOLD

PHYSICAL GOLD

The most common form of buying gold is in the form of physical gold. We buy this from jewelers around us. Gold is bought in the physical form when the person wants to benefit from social and consumption value and not just investment value. Historically, the physical form of gold was the only way to buy it. The physical form of gold carries all the holding costs associated with gold– insurance, storage costs, loss due to theft, etc.

GOLD ETF

We saw that ETFs are mutual fund-like instruments that have an underlying asset to them and the price of ETF moves exactly in line with the underlying asset. A Gold ETFfollows the gold indices and the prices of ETF move exactly in line with gold prices.

Also, instead of physical gold, ETFs are deposited in our Demat account in the form of a certificate. This reduces the storage costs, insurance costs and there is no risk of theft as we do not receive physical assets. Gold ETFs are a better way to buy gold when we do not need it for its consumption value. A lot of hassle in handling and buying physical gold goes away and the process of buying and selling becomes much easier.

SOVEREIGN GOLD BONDS

The third form to buy gold is via the Sovereign Gold Bonds (SGBs). These are similar to lending the bank or government our money, only here instead of money we lend gold and we earn interest in terms of gold itself. Let us say, we lent the bank 100 grams of gold at a 2.5% interest rate. This means that our principal is 100 grams gold and our interest is 2.5 grams of gold. So, at the end of one year, we will receive 102.5 grams of gold instead of 100 grams.

The gold prices may go up or down, and that does not affect our return in terms of quantity. So, our net return will be a combination of the gold price changes and the interest earned in form of gold. This is one of the best ways to invest in gold. Moreover, there are no holding costs. This was initiated in India in 2015 under the Gold Monetization Scheme. This is suitable when consumption value is not the priority.

So, the above mentioned are the three forms in which we can buy gold. Each form has its pros and cons and depending on what we need, we will then select the form in which we will buy gold.

SUITABILITY

Firstly, gold is suitable for those who are looking at it for its social and consumption value rather than investment value. Gold is an integral part of Indian culture with it being the primary gift in major life events. We need to know that we are forgoing investment value, in return for social value.

The trouble begins when people start accumulating gold in physical format for these occasions for 7-8 years. We already saw that, when dealing with long term goals, we can afford higher risk assets as well and then later convert them to gold. Even if we wish to keep the money invested in gold, ETFs or SGBs are a better way to do so. With SGBs and a 2.5% return on the gold for 7 years, 100 grams of gold will increase to 130-140 grams and we will not have to incur any storage costs as well. We can always convert the SGB to physical gold when it is needed.

The second instance when gold is suitable is again from an everyday jewelry perspective. However, most of this will be added to support assets and not an investable portfolio. A lot of gold buying is also done under social pressure.
Buying gold is a way to exhaust black money. The government is getting stricter day by day and reducing gold's ability to absorb black money. Black money is a personal choice and there is not a lot that we can explain here. We call it a train without an engine.

For investment purposes, a large portion of the portfolio should not be put in gold. Even though gold can hedge the portfolio, all those valuations are complicated for common people to understand and they should avoid the hedging math. From an investment perspective, not more than 5-10% of the investible portfolio should be in gold under any circumstances. For those who have a very high preference for this asset class, they need to mention this in the unique circumstances section in their lazy profile and build the plan accordingly.

With this, we end our discussion of gold. We have learned its characteristics, forms to buy gold and lastly its suitability.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09

CURRENCY

GETTING STARTED

Currency is a very important instrument in the lives of all those who have an earning member in other countries and they earn or spend in a different currency. All these families are significantly impacted by currency fluctuations.

A common mistake is to see the currency as an asset class rather than an instrument. Currency is not an asset class, it is an instrument. Remember, cash is an asset, and all different currencies are just a form of cash. If you hold Indian National Rupee or US Dollar, they are all types of cash. So, it is unfair to see INR and USD as two different assets.

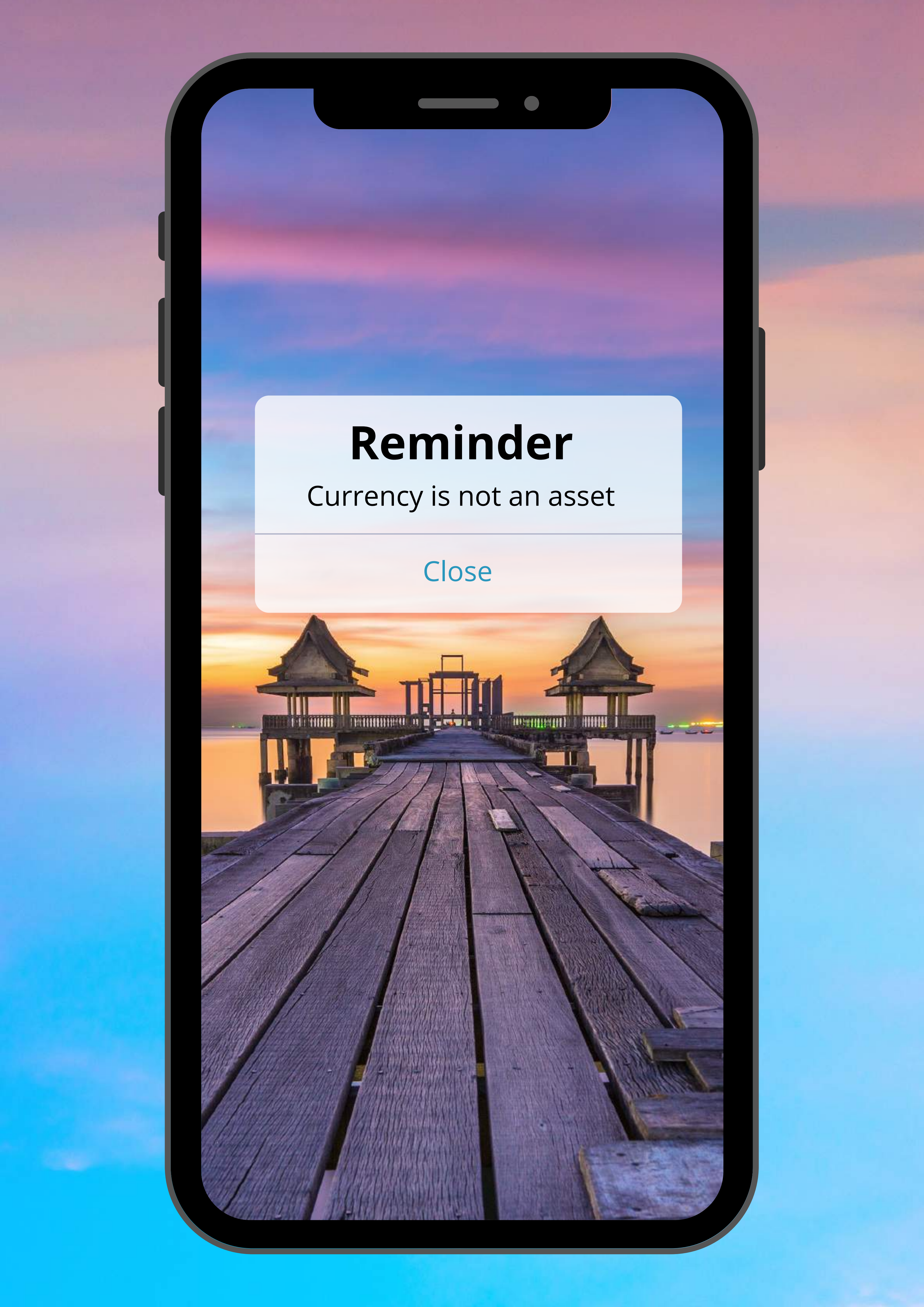
Currency fluctuations are a matter of supply and demand and these depend on macro-economic factors that are beyond anyone's control. It largely depends on different interest rates and inflation rates of the two countries. Understanding these calculations and currency valuations is beyond the scope of this book.

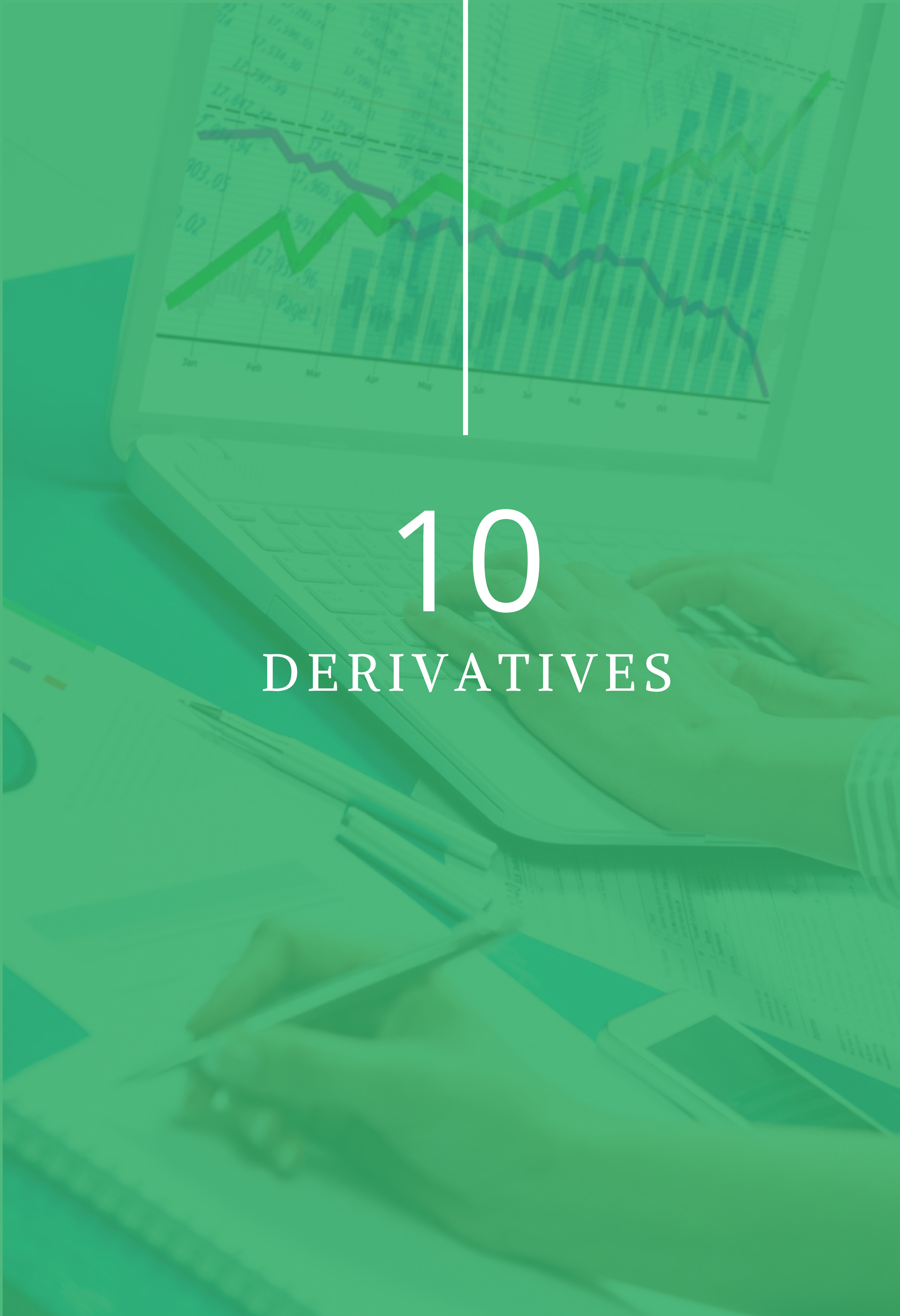
As a result, we will deal with currencies using the Systematic Transfer Plan. We will have a systematic plan for currencies where we transfer currencies over an extended period. This way, neither do we buy it at a really expensive price and nor at a cheap price. We switch between the currencies at the average valuation.

We will avoid bulk exchange between currencies unless and until it becomes a compulsion. We will transfer equal amounts every month or every quarter via STP so that we make the exchange at average valuations.

Lastly, a new form of currency is picking up and gaining traction in the last 2-3 years i.e. crypto-currency. It has been making all kinds of news across the globe and has enticed a lot of people to invest in it due to the fast price appreciation that it had. Should crypto-currency be a part of the Financial Plan? The answer to this is NO. This is because whenever we invest in assets, we want them to store value for a long time so that we can use them to meet our financial goals in the future. Digital currencies have not established themselves as a store of value yet and neither are they regulated. They might become the currency of the future, who knows? However, we do not want to risk having them at the core of our investible portfolio and jeopardizing our Plan.

Those with extremely high risk-taking ability, greater than 4, can have an exposure of a maximum of 2-5% of their investible portfolio. However, they should already know that this is speculative and the chances of losing their capital in this class are significant. We will not invest money that is tied up to our goals in such asset classes. If they get more established in the future, we will review it again as an asset option. However, right now they are not well established, and rather than choosing the popular investment, we will select the suitable one.


Reminder
Currency is not an asset
Close

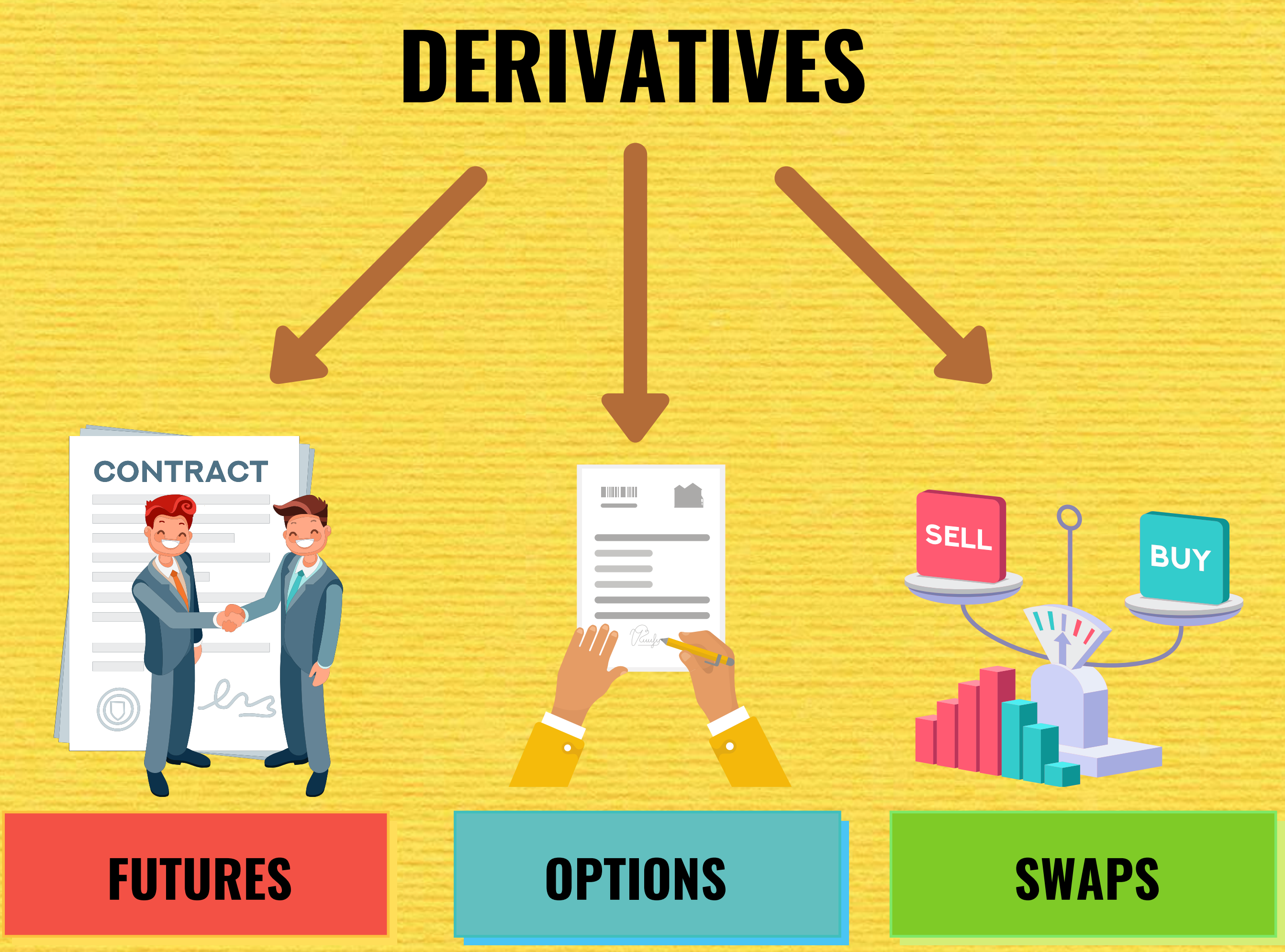


10

DERIVATIVES

GETTING STARTED

The instrument up next is derivatives. Notice, that we are not calling them asset class but instruments. Derivatives are financial instruments that derive their values from an underlying asset. This might appear to be a little overwhelming for most readers. Common types of derivatives include forwards, futures, options, swaps, etc. These are very high risk and very high return instruments. They are capable of churning out both very high profits and losses in a very short time horizon.



HOW IT WORKS

Coming to derivative contracts, let us say there is a stock that is worth Rs. 1,000 currently as per market. We think the stock will go up and our friend thinks it will go down from here. One way is to buy the stock and try to benefit from the same. Or, both of us enter an agreement according to which if the stock goes up, they will pay us and if it goes below Rs. 1000, we will pay for them. It is like a 'bet' that we both are making. We decide on a cut-off date when the result will be decided. This kind of contract allows us to take a position and benefit from a price increase without actually buying the asset. Now, the nitty-gritty of this contract can be changed and different kinds of derivative contracts can be made.

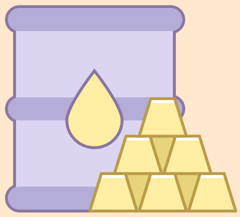
In every contract, there are two parties i.e. one that thinks that the price of the underlying asset will go up and the other that thinks that the price of the asset will go down in the future. The former is the long investor and the latter is the short investor.

UNDERLYING ASSETS

In the above example, we were betting on the stock price of a company. The derivative was dependent on the share price of that company. However, there can be other alternatives that you can bet on. For example, the price of real estate, current market interest rates, bond prices, currency exchange rates, and so on. Any form of bet is a derivative contract because the two parties are not buying/selling the asset, they are just entering into a contract that is dependent on the asset

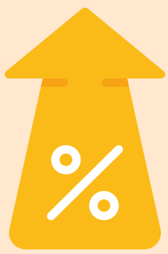
STOCKS

BONDS

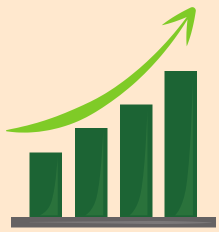


COMMODITIES

CURRENCIES



INTEREST RATES



MARKET INDICES

WHY NOT AN ASSET CLASS?

Why are they called instruments rather than asset classes? Return potential is very high in all derivative instruments. However, these come with a very high degree of risk attached to it. As a result, we cannot park or invest long term money here because it is critical for our financial goals. We do not want our long term money that is tied to financial goals to have so much volatility and instability. We want more 'Staying Power' in our assets and because derivatives lack 'Staying Power' and 'Store of Value' functions, they cannot be considered as an asset class.

RISK OF BANKRUPTCY

While investing in derivatives, we may have to pay a small amount such as Rs 100 to get an exposure of an asset of, say, Rs. 1000. That Rs. 100 is the margin. Now in such cases, we may have invested only a small amount of money, but our portfolio is exposed to the risk of much more than that. If the deal does not work out in our favor, we will have to pay anything up to Rs 1000. In this situation, the amounts are very low, but a majority of such contracts have a risk exposure in lacs and crores. Due to this, we may go bankrupt overnight. We do not want to expose your portfolio to such risks unless you have the time and skills to invest in such instruments. Hence, we should stay away from these instruments completely.

WHY WERE THEY CREATED?

Derivatives were created as a risk management instrument for banks and for large investors who have large exposures to different assets. So, they use derivatives as a hedging instrument i.e. to increase or decrease exposure in short term without actually buying or selling an asset. So, derivatives are a risk management instrument rather than an investment instrument.

Trouble begins when financial instruments are used for purposes other than the ones they were created for. As a result, most individuals are better off away from derivative instruments. Legendary investor, Warren Buffet says that derivatives are 'Weapons of Mass Destruction.' Years of effort can be lost in a few hours using derivatives.

With this, we end our discussion on derivatives, an instrument and not an asset class. These are best avoided by most and those who wish to participate must take formal training about systems, concepts, and risk management and be prepared for a full-time involvement.

We have now understood major asset classes. Combining these, we can create a Lazy Financial Plan for ourselves. We will now move on to know more about insurance. We understood the risks that we face and the insurances that we need in the lazy financial profile stage. Let us now understand more about the terms and the selection process related to the different types of insurances that we discussed.

THE JOURNAL OF MUTUAL FUNDS

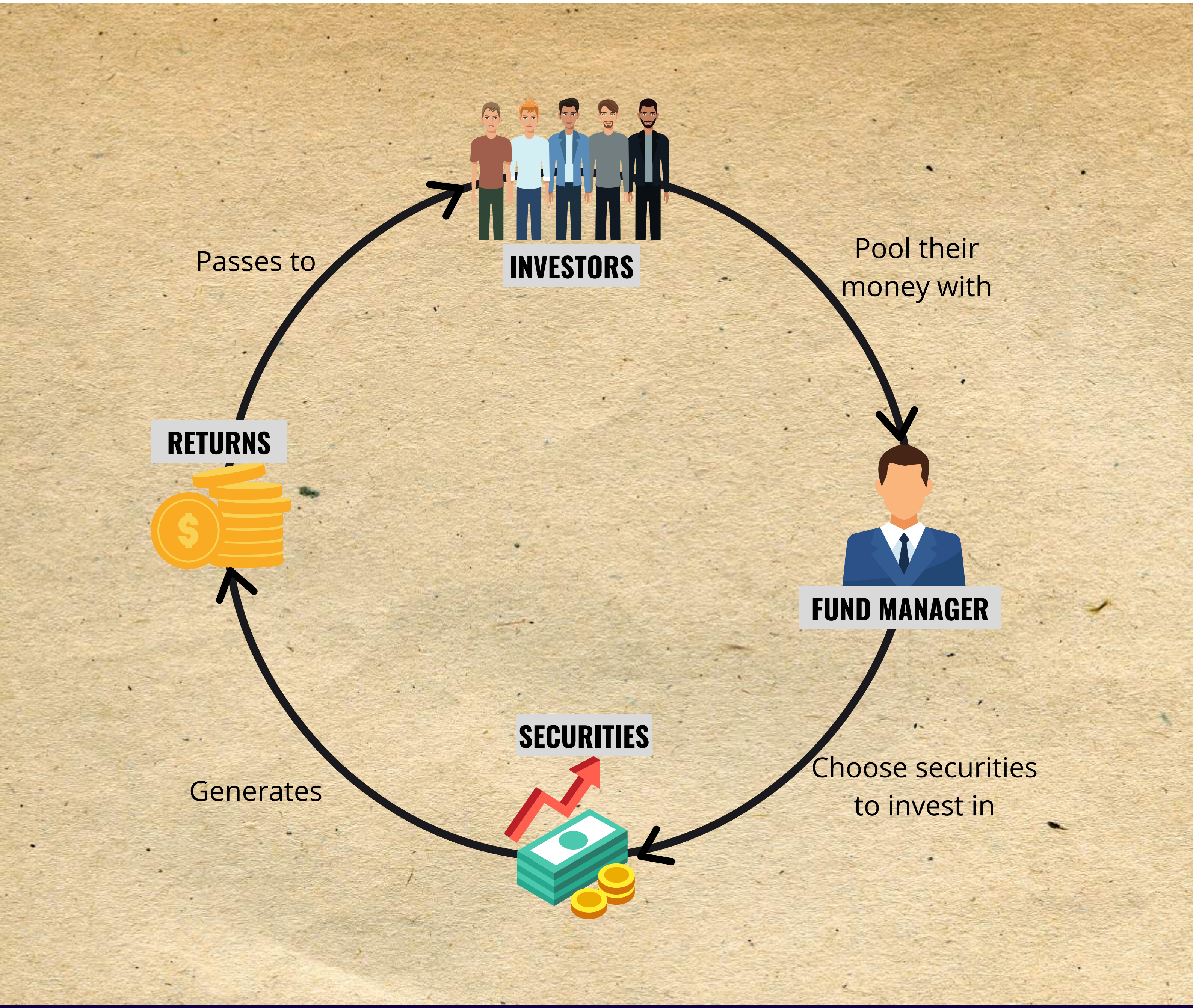
HOW TO SELECT WINNING MUTUAL FUNDS

LEARN MORNINGSTAR MUTUAL FUND SCREENER

ZEBRA LEARN

For those without the skill or time to invest directly in an asset class, they can invest in the same via an indirect method, which involves using expert help, also known as mutual funds. As we have already discussed earlier, mutual funds are like a collection of small individual investors who pool in their resources and get an expert to manage the same. For instance, 100 investors together pool Rs. 10,000 each to a mutual fund which now has Rs. 10 lac. The fund now appoints an expert to manage their money. Independently, none of these individuals would have been able to afford an expert. But together, their money is being managed effectively by an expert. This is the underlying math behind the functioning of mutual funds. It is built on the power of collective investing i.e.mutual investments.

In reality, thousands of people contribute lacs of rupees into mutual funds. Mutual funds today have thousands of crores to manage. The funds can very effectively manage such large amounts by having a team to carry out extensive research and investment activities.

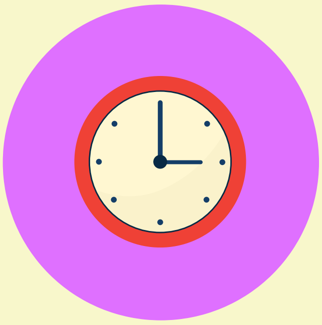


Well, can mutual fund managers do whatever they like with our money? Each mutual fund scheme has a 'Mandate' attached to it. It is a guide to what can or cannot be done with the money, for instance, the kind of assets and the sub-categories they can invest in and the restraints they might have. For instance, some mutual funds can only invest in equities, some only in debt, some in a mixture, some can only invest in mid-cap equities, others only in banking stocks, and so on.

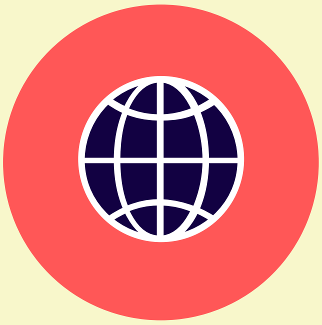
MANDATE

A mutual fund mandate is a document that acts as a guideline for the scheme. Following are a few factors that it consists of. It is compulsory for the fund to make decisions based on the mandate

ASSET CLASS
Eg: Equity, debt, etc.



TENURE OF INVESTMENT
Short-term, Mid-term, Long-term



SECTORS OF INVESTMENT
Eg: Technology, Banking, etc.

INVESTMENT LIMIT
Max & Min

ACCEPTABLE LEVELS OF RISK

BENCHMARK RETURNS

TERMS TO KNOW

1 NET ASSET VALUE (NAV)

Similar to buying 'Shares' of a company, we buy 'Units' while investing in mutual funds. If 'Share Price' is the price at which we can buy a company's share, the 'NAV' denotes the price at which we can buy one 'unit' of a mutual fund.

NAV × **TOTAL UNITS ISSUED BY MUTUAL FUNDS** = **ASSETS UNDER MANAGEMENT**

SHARE PRICE × **TOTAL SHARES ISSUED** = **MARKET CAPITALIZATION**

SCHEME SIZE 2

The size of a scheme is the total assets that are being managed under the scheme. This is also called an asset under management (AUM) by certain companies. The total number of units multiplied by the NAV would give us the AUM. Think of this as market capitalization as learned in the equity section.

Too small a scheme size increases the cost of managing the scheme and too large a scheme size limits the places that the company can effectively invest in.

3

CAGR

The compounded annual growth rate is the average compounded return that we receive on our investment. If we earn a CAGR of 18%, that means our asset is compounded at 18% annually for N number of years. CAGR is calculated based on compound interest and not simple interest.

EXPENSE RATIO

4

It is the percentage of scheme size/AUM that is being spent to run the mutual fund. A mutual fund has a lot of expenses such as costs related to asset research, office expenses, distribution and marketing expenses, and so on. These costs are denoted as a percentage of scheme size. So, if a mutual fund scheme incurs a cost of Rs. 5 crore to manage Rs. 300 crore, we can say that the expense ratio is 1.66% (5Cr / 300Cr). Lower the expense ratio, more efficient is the fund in its operations. This forms a key decision factor when selecting mutual funds. The expense ratio can range between 0.5% and 2.5%.

5

SECTORS

This refers to the different business sectors that the fund is allowed to invest in as per its mandate. For example, sectors may include pharmaceuticals, telecom and infrastructure, financial services, consumer durables, food and beverages, and so on. Some mutual funds are sector agnostic i.e. they can invest in all sectors and others may be sector-specific i.e. they invest in select sectors.

TOP 10 STOCKS (%)

6

Each mutual fund has a majority of its investments distributed in a few key holding. The rest are a small percentage of multiple stocks. So, typically we will see 60% of assets in the top 10 stocks and the rest 40% distributed in the next 25 companies. This has a positive side as well as a negative side. So, the top 10 stocks (%) refer to the percentage of holding in the top 10 stocks. It shows how concentrated the fund is.

7 CATEGORY

Mutual Funds have a lot of categories based on asset classes and subclasses that they invest in. These include mid-cap fund, small-cap fund, high-duration bond fund, gilt funds, BFSI sector fund, an international fund, etc. Mutual fund schemes in the same category have similar behavior and risk-reward characteristics. We will use categories defined by Morningstar. Getting the category right is 80% of the mutual fund selection process.

PORTFOLIO P/E 8

P/E or Price to Earnings ratio is one of the most commonly used valuation metrics. It illustrates how much the company is being valued for each rupee of earnings that it makes. In a P/E multiple, P stands for the price of the company and E stands for the earnings (profits) of the company. So if a company has a P/E of 20 and its earning is Rs. 1 crore, then the company will be priced at Rs. 20 crore. If we have an identical company, but its P/E is 15, then it would be priced at Rs. 15 crore. P/E depends on the strength of the business and market sentiments.

The higher the P/E multiple, the higher is the valuation of the company, and the higher are the chances that the price is currently above the company's true value. Portfolio P/E is the weighted average of the P/Es of all the companies owned by the scheme. Portfolio P/E is one of the indicators of valuation used.

OPEN-END MUTUAL FUND

It allows us to invest & redeem at any given time based on our convenience. Mutual funds where we can enter and exit at any given point in time are called open-end mutual funds

CLOSE-END MUTUAL FUND

We are allowed to invest in closed-end mutual funds exclusively upon their announcement or when the fund manager specifically opens the fund for new investments. Funds, where entry & exit is restricted, are called closed-end mutual funds.

GROWTH MUTUAL FUND

In a growth fund, the profits of the fund are reinvested in the fund instead of distributing it to the investors. Due to this, the wealth compounds. The objective is to increase the amount so that we can sell off the mutual fund at a high price.

DIVIDEND MUTUAL FUND

In dividend mutual funds, the profits of the fund are regularly distributed among the investors in the form of dividends. It is not reinvested and hence the growth of the originally invested amount is slower. It is suitable for those who want a steady source of income.

FRONT LOAD

Mutual funds at times charge the investors when they invest money in the scheme. It is charged upfront at the time of investing and is called the front load.

EXIT LOAD

Mutual funds at times charge the investors when they withdraw money from the scheme. It is charged at the time of withdrawal and is called exit load.

EXPECTATIONS

The return expectations from mutual funds are based on the underlying assets owned by the scheme. If the mutual fund owns equity, we can expect a return that matches equity. If the fund only owns debt, we can expect a return that matches debt.
Because the fund expectations in terms of risk and return depend on what assets they own, getting the category right becomes very critical in our lazy Financial Plan. The category determines the assets that the fund can invest in and will therefore determine the risk-return characteristics. For instance, small-cap mutual funds shall give relatively higher but more volatile returns than large-cap funds.

Mutual funds can be used to substitute direct investments in almost any asset class.

e can create a personal finance plan only using different types of mutual funds. Instead of buying any asset directly. we pool in the same with mutual funds and get an expert to manage the same. It is just an alternate way of owning assets.

With mutual funds, we pay a small portion of the return as an expense that was incurred in running the mutual fund operations and getting the expert team to manage the money. So, if we earn 16% CAGR with a fund and it has a 1.5% expense ratio, then the NAV will only reflect an increase of 14.5% (16% - 1.5%). However, paying out the expense ratio makes sense because if we were to manage the money ourselves, we might not get such high returns. Even after paying the expense ratio, our portfolio is still doing good for itself by earning 14.5% every year.

EFFECTIVE RETURN = CAGR − EXPENSE RATIO

SUITABILITY

Most people do not have the skill or time to identify and invest in individual securities. As a result, irrespective of what assets we want to invest in, mutual funds are suitable for most people as most assets like equities, fixed income assets, commodities, etc . can be bought via a mutual fund ownership scheme. Real estate mutual funds called REITs are also picking up now.

We need to be realistic about our skill and time and decide if we want to pick individual investments or go via mutual funds. In reality, it does not matter, both can be used to meet financial goals. For simplicity, anyone who does not have a bare minimum of 6 hours a week to invest in understanding their investments have should opt for mutual funds. Now we know if mutual funds will be appropriate for us or not. For most people, it will. There are multiple categories of mutual funds. Different categories are suitable for different people. There is no one size fits all. Now we will find out the type of mutual funds perfectly suited for us.

HOW TO SELECT?

1) SELECT THE FUND CATEGORY → 2) SELECTING THE FUND WITHIN THE CATEGORY

As discussed earlier, mutual funds are divided into multiple categories. These categories are determined based on the underlying asset classes they invest in. Each category has different risk-reward behavior. A suitable category has to be selected based on the return objectives. For instance, equity mutual funds are suitable for long term goals and debt-related mutual funds for relatively short term goals.

CATEGORIES OF MUTUAL FUND UNDER EQUITY BASED ON

SIZE OF THE CO.	PURPOSE	SECTOR	THEME
• Small-cap • Mid-cap • Large-cap	• Retirement • Savings • Tax-savings	• Energy • Consumer • BFSI	• Rural Development • Consumption • ESG

CATEGORIES OF MUTUAL FUND UNDER DEBT BASED ON

ISSUER	DURATION	CREDIT QUALITY
• Government Bonds • Corporate Bonds	• Low Duration • High Duration	• Safest • Safe • Risky • Junk

Then there are hybrid mutual funds as well. Thus, as a result, mutual funds are very diverse and have many categories. We follow categories by Morningstar. In the next few pages we have listed down the different categories by Morningstar and what do they mean and where are they suitable

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
HYBRID FUNDS		
Dynamic Asset Allocation	The fund manager chooses between bonds and equities and can make re-adjustments based on market conditions. It can have any proportion of debt and equity based on the market.	• High flexibility in goals
Retirement Funds	Fund managers can invest anywhere they deem fit to meet the goals of retirement. These generally come with a lock-In period.	• About to retire. • 50+ in age
Aggressive Allocation	This is a mutual fund that is more aggressive in risk-taking and seeks long term wealth generation. Here, a larger share goes towards equity.	• Long term goals • Risk-taking ability: Moderate to high • Time Horizon: 7+ years
Children Funds	These are managed specifically for long term goals of children – education and marriage. These have varying levels of debt and equity.	• Children related goals • Risk-taking ability: Moderate to high

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
Conservative Allocation	These are conservative mutual funds that are risk-averse and ready to let go of returns for lower risks. They invest a larger share in bonds.	• Risk-taking ability: Low
Fund of funds	Fund of funds is a mutual fund that further invests in multiple funds, so as to give diversification benefits. This is a single fund that invests in multiple other funds.	• Too Expensive • Can be diversified on our own by owning multiple funds
Equity Saving Funds	They invest in debt, equity, and arbitrage. Arbitrage are situations where opportunities unrelated to the general market arise.	• Complicated • Best if ignored
Multi-asset Allocation Funds	These funds invest in a suit of assets – equities, bonds, gold, other mutual funds, Government Securities, etc. These give diversification benefits across asset classes.	• Expense ratio: Relatively high • Automatic diversification • Better to buy these assets individually

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
EQUITY MUTUAL FUNDS		
Arbitrage Fund	They try to take advantage of the differences in equity and derivatives prices. Also, they participate in event-based arbitrage. Here, the expense ratio is generally high.	• Complicated • Better if avoided.
Contra Funds	Contrarian Investing refers to an 'Against the Wind' style of investing. It includes taking investment decisions against the common perception to buy assets for cheap. This is a well-established approach.	• Difficult to understand • Better & simpler solutions available
Dividend Yield Fund	These funds mainly invest based on dividend yield. They invest in high dividend-paying companies.	• Regular income from assets • Old age/Retired people • Regular cash-flow
Equity-others	These are specific types of funds based on a theme or approach. E.g. MNCs, PSU Fund, New Energy, etc. These mainly invest based on a theme or concept.	• Exposure to theme • Simpler options available

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
Focused Funds	Focused Funds are those that focus on a particular sector or a few companies. They limit their diversification. This limits opportunities but increases the depth.	• Better if avoided by individuals • Rather go with Sector funds
Capitalization	They invest in companies of a certain capitalization range i.e. size. Large caps are the least risky and produce stable but lower returns as compared to small caps.	• Everyone - irrespective of their risk-taking ability
Sector Funds	They only invest in stocks in a particular sector. So, performance is tied to the sector and not the general economy. Here, we are taking a sector-specific bet.	• Who work in a particular sector • Having insights of that sector • Best if ignored
Value	Value means strong companies at cheap valuations even if growth is low. Here, the focus is on downside minimization.	• Goals: Long-term • Time horizon: 7+ years • Risk-taking ability: Low to moderate

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
Equity Linked Saving Schemes (ELSS)	ELSS is a special kind of tax saving mutual fund where investments can be claimed for deduction under Section 80C. It produces good returns due to the presence of the 3-year lock-in.	• Claiming 80C deductions • Tax-saving Goals: Long-term
Index Funds	They mainly focus on a predetermined index and trade based on that. They can follow Nifty50, Nifty100, or anything else too. ETFs are also a category of this. We will discuss this in great detail soon	• Low expense ratio • Low liquidity
Global Funds	Funds that invest outside India too. The foreign currency also becomes a factor here.	• Risk-taking ability: High • Best if avoided by individuals
Multi-cap Funds	These invest in a mix of large cap, mid cap, and small cap stocks in a proportion seen fit by the fund manager and those in the fund's mandate.	• Time horizon: 7+ years • Risk-taking ability: moderate to high

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
COMMODITIES		
Precious Metals	These invest in Gold and Silver only.	• Better than owning goal directly
BONDS		
10years Government Security	These invest in 10 year Government Bonds and are the safest investments as the government can always print money and payback.	• Long-term safe assets • Safety of capital • Risk-taking ability: Low
Banking & PSU	They constantly need money to lend to others. As a result, they have a lot of bonds in the market. These mutual funds only invest in these Banking and PSU organization securities.	• Returns: slightly high
Dynamic bonds	They can invest in any bond category, based on the market situation. The fund manager makes the decisions	• Risk-taking ability: between 2 & 4 • Returns: Higher • Goals: Medium-term

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
Government Bonds	The Government issues bonds of various tenures. Also, different government companies issue bonds. These bonds are backed by the government and therefore are very safe. However, they give relatively lower returns.	• Time Horizon: Less than 2 years
Duration	Duration of bond is how much its price changes when the interest rate in the economy changes. In simple words, it measures the risk for bonds.	• Ultra-short: 3-6 months Short : 1-3 years Medium: 3-10 years Long: 10+ years • Diversified fund
Corporate Bond Funds	Invests in corporates and companies. These have a higher risk and return	• Risk-taking ability: 2.5+ • Returns: Higher
Credit Risk Funds	Such funds take higher credit risk and expect to earn higher returns. They invest in lower-priced bonds for higher returns.	• Risk-taking ability: 4+ • Best if avoided

CATEGORY	MEANING	SUITABLE FOR THOSE WITH
Floating Rate Funds	These are bond funds that do not give fixed returns but invest in assets with floating return instruments. The instrument returns keeps on changing as per the market.	• Emergency Fund
SHORT-TERM FUNDS		
Money market funds	These invest in bonds and commercial papers, that mature in less than 1 year. They keep on re-investing assets that mature.	• Time Horizon: Less than 2 years • Emergency funds
Liquid Funds	They invest in bonds and commercial papers that mature in less than 91 days.	• Short-term investment • Better than FDs
Overnight Funds	They invest in bonds and securities that invest each day. For instance, banks borrow money to meet overnight fund needs. These have the lowest returns.	• Complicated • Better if ignored by individuals

1) SELECT THE FUND CATEGORY

2) SELECTING THE FUND WITHIN THE CATEGORY

In the previous pages, we saw the different mutual fund categories that exist, the assets they invest in, and their suitability. Deciding upon the category is significant as all funds in the category produce returns on similar lines in the long run. If our category selection is wrong, we might not be able to meet our financial goals even if we get the fund within the category right.

If our category selection is right, we can even skip the fund selection part by dividing our money into several funds in the category. However, there is no way to skip the proper category selection. We can learn more about the category behavior by understanding past returns of various schemes under the category.

We have attached an instructional video on our website i.e. how to check the category's past returns. However, remember that past returns do not guarantee future performance. In the past, we have seen the best performers of the last 5 years become the worst performers of the following 5 years. We will only use category returns over the last 5 years or longer. We will completely ignore the last 2-3 year return. It is not relevant to us.

Multiple tools can be used to make our decisions about mutual fund and category selection. These include Morningstar, Valueresearchonline, Moneycontrol, etc. We will use Morningstar throughout the book as they provide the most relevant mutual fund screener for Indian markets at the moment

So, check the list in the previous pages and the video on the website to understand how to select mutual funds. Once we have selected the category, we will select the fund within the category. We will use the Morningstar mutual fund screener for the same.

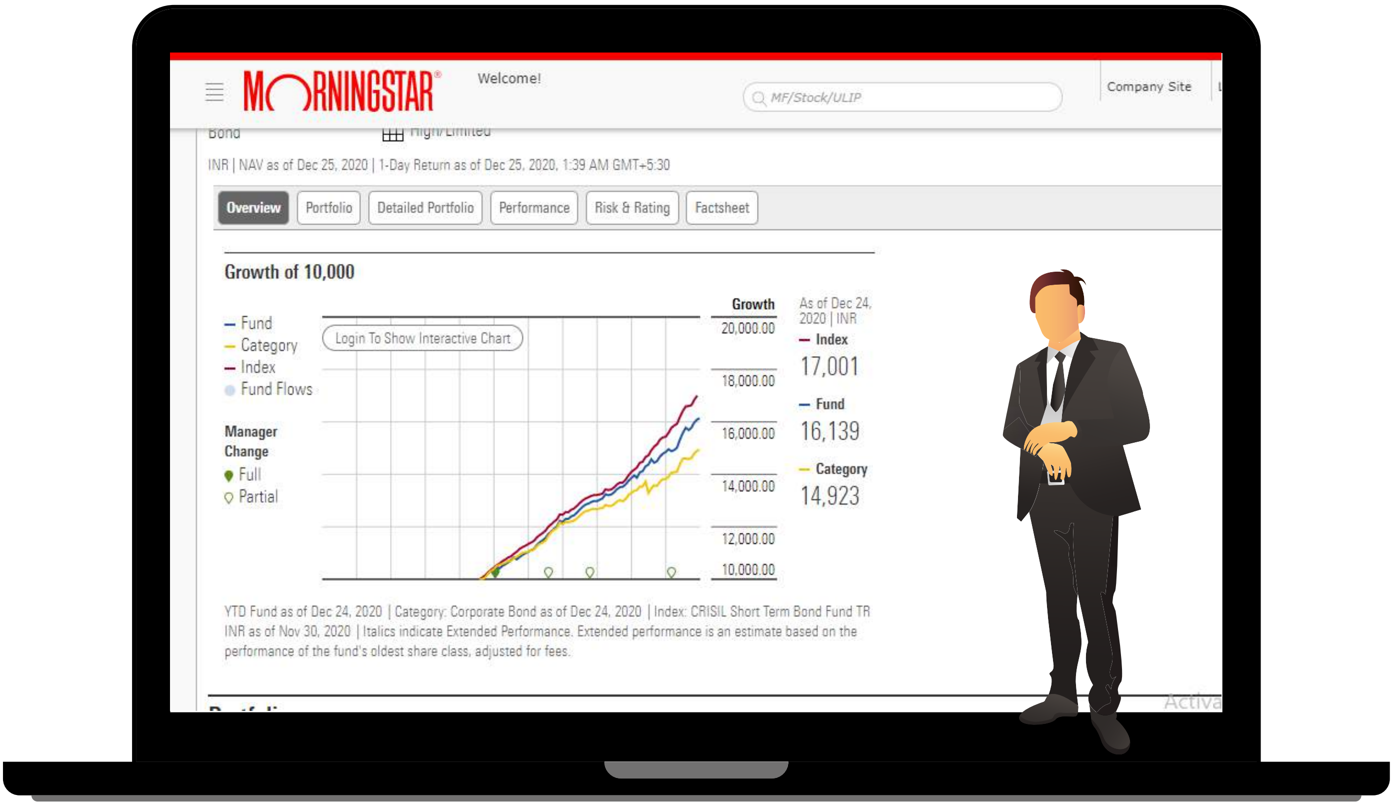
FACTORS TO CONSIDER

Once we have used the Morningstar screener, we will have a few mutual funds shortlisted in the category that we are interested in. The next step is to individually review each one of them and then select the most relevant one. To do this, we need to understand the parameters on which each mutual fund should be evaluated.

MANAGEMENT

The most important aspect of selecting a mutual fund is perhaps keeping at par with its management. The fund manager's skill will determine our results. Morningstar will give us the name of the manager. We will search for the manager on LinkedIn to get his past track record of employment. We want to make sure that the fund manager has at least seen 2 complete market cycles. This typically implies that the fund manager has been active in the markets for 15 years and it does not matter if it has been at another company or in a junior role. Do not invest if the management has not spent 15 years in the capital markets.

Second, we will see, for how long the fund manager has been in charge of the fund. Morningstar gives major management changes in its description of its fund. So, this is relatively simple. It wouldn't be a wise decision to invest with somebody who has not been in charge for at least 3 years. Lastly, we are to consider if the fund outperformed the category at this time. Even though past performance is not at all indicative of future performance, yet consistent outperformance of category is a positive sign.

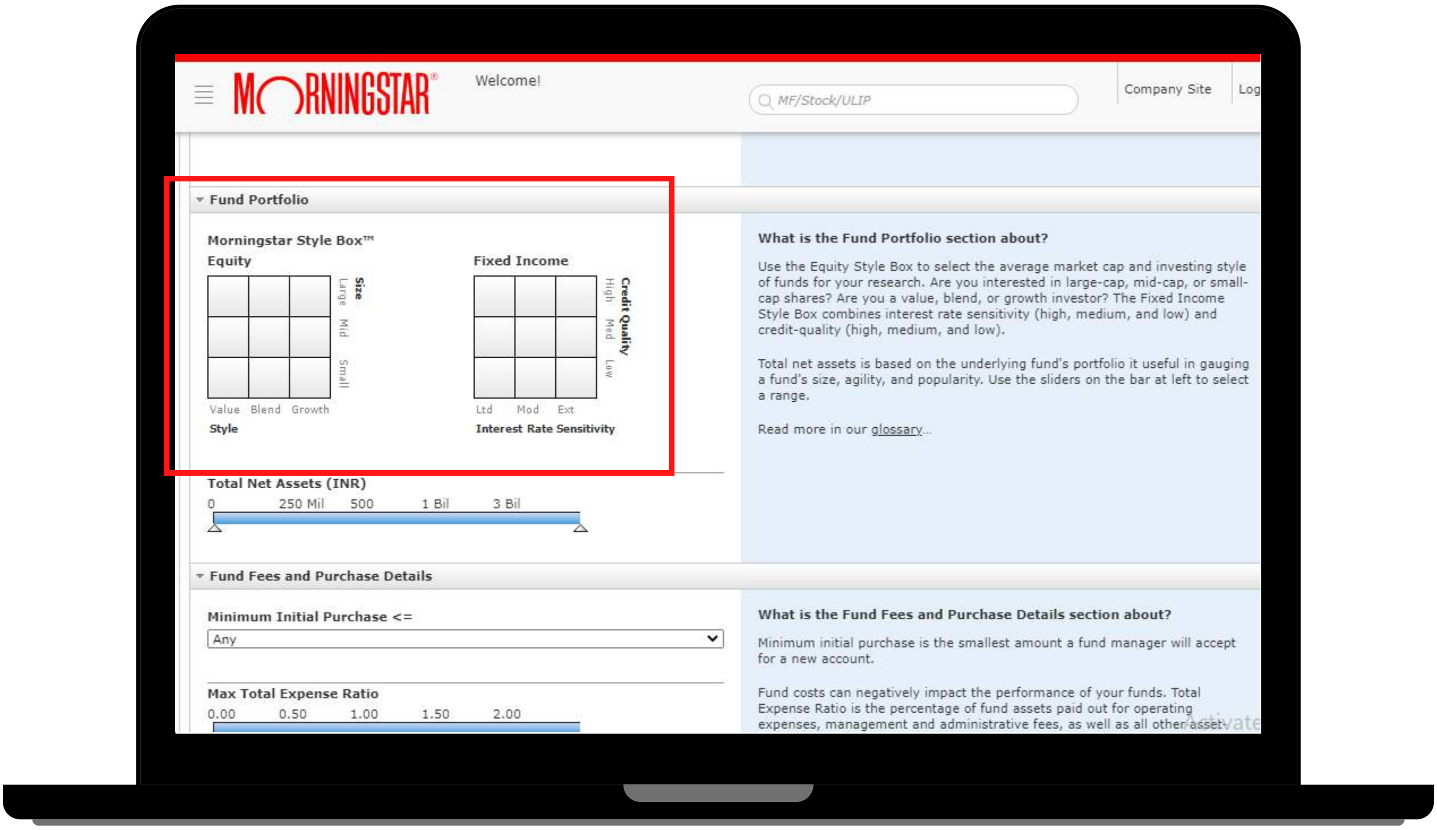


SOURCE: Morningstar.in

FUND STYLE

We see that Morningstar uses 3x3 metrics to evaluate different equity and debt mutual funds. For equity, they use small-cap, mid-cap, and large-cap on one axis and value, hybrid, or growth approach on the other. We already are aware of small-cap, mid-cap, and large-cap. The value approach is when mutual funds try to buy assets below their value whereas the growth approach is when the managers are ready to pay more than the true value if they think the company's true value will increase in coming years. We saw this when we were learning about equity shares. Both approaches have their merits and demerits and there is no correct answer.

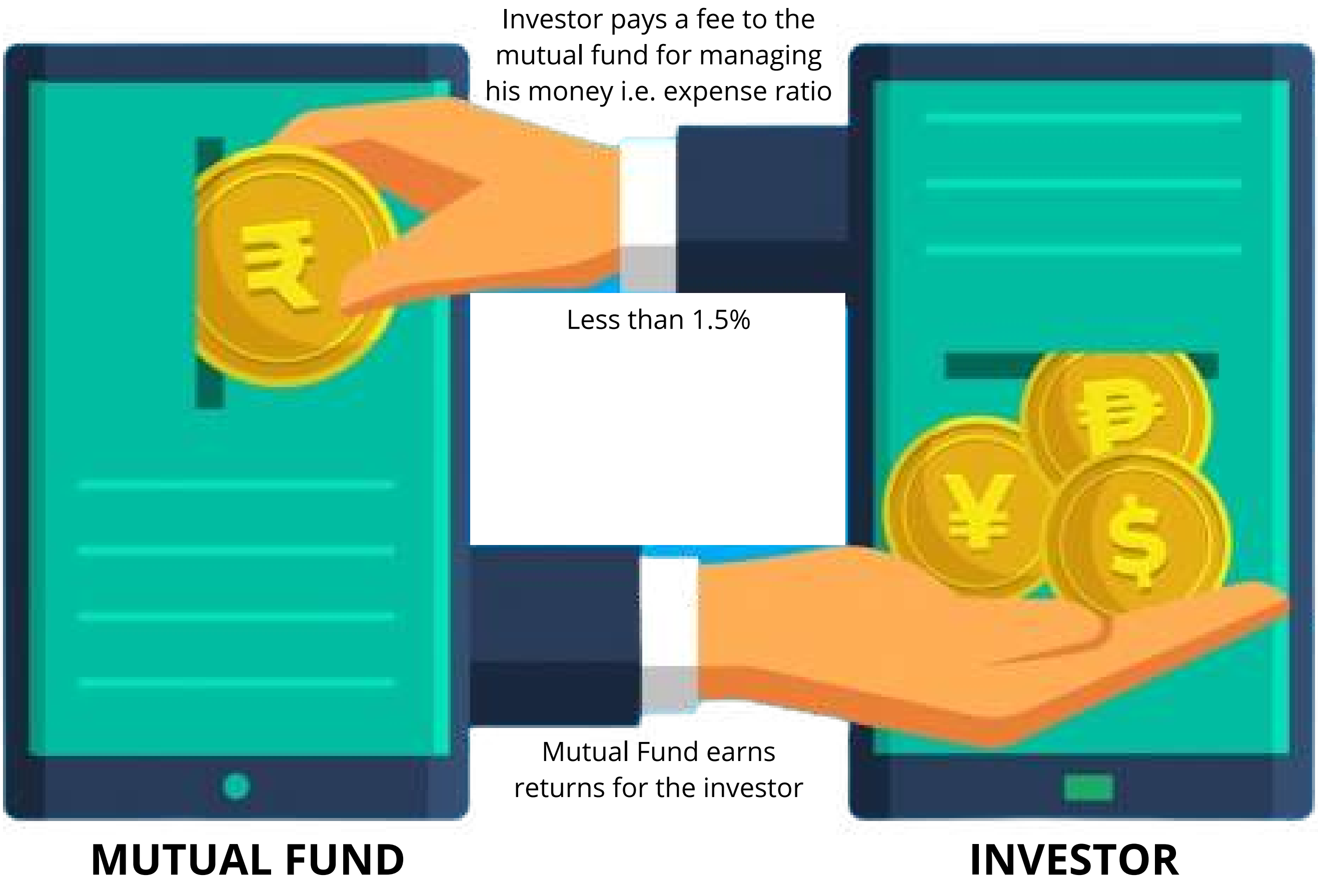
Fixed-income assets too use a similar 3x3 metrics box. Here, one axis depicts credit quality as determined by credit rating companies. The second axis represents interest rate sensitivity. Market Interest rate keeps on changing with changes in the market price of mutual funds. Prices of long term bonds change more frequently than that of short term bonds. Credit quality and interest rate sensitivity together decide the fund style for fixed income securities.



SOURCE: Morningstar.in

EXPENSE RATIO

We will not invest in any fund that has an expense ratio of more than 1.5% in equity and 1% in debt. Most of this will, however, be taken care of by applying a filter for expense ratio in the Morningstar Mutual Fund Screener.

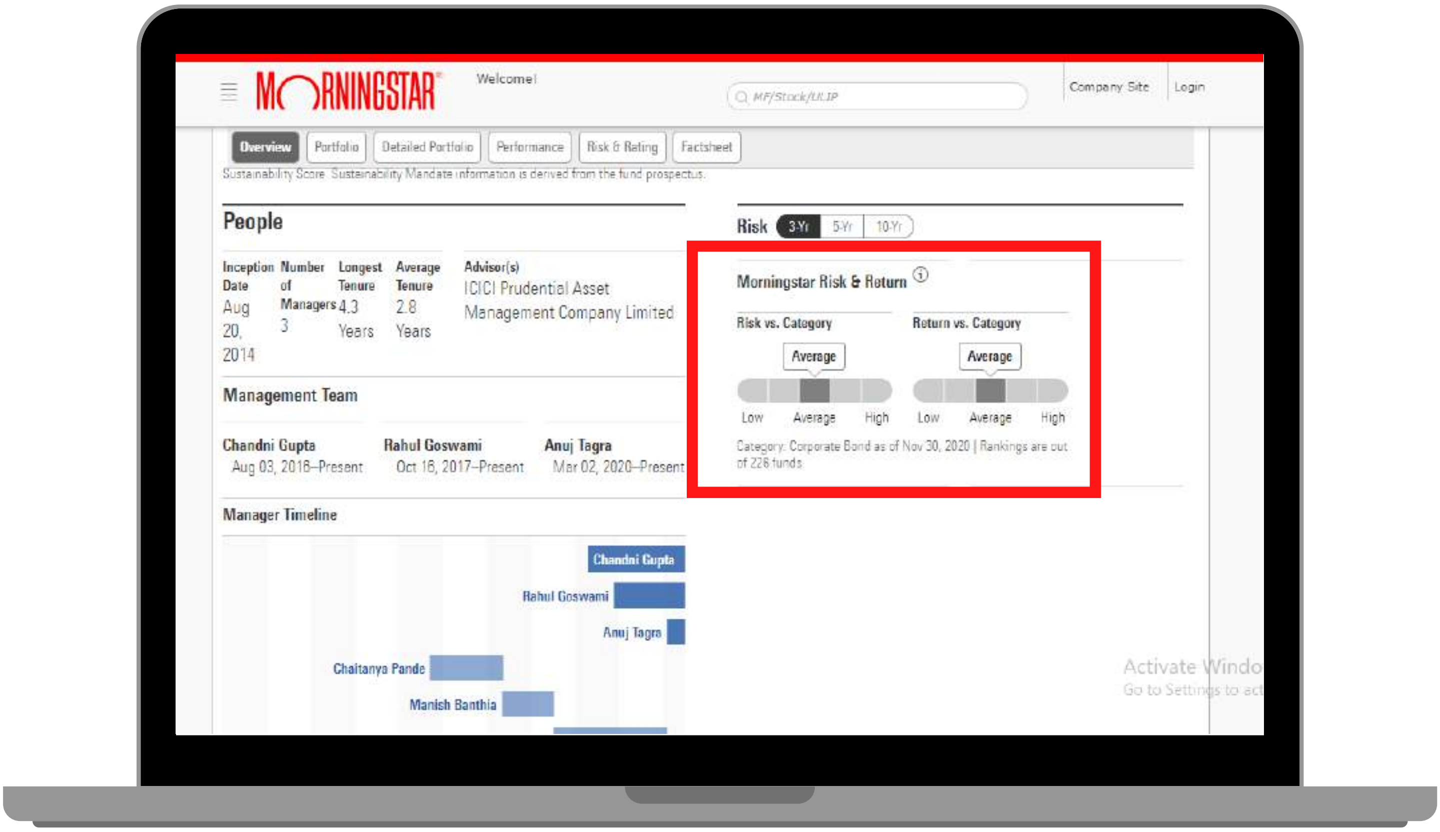


PERFORMANCE IN THE PAST

Next, we will check is if the fund has exceeded its category's performance in the last 5 years. If the category has produced a CAGR of 3% p.a. in the last 5 years and the fund has performed 5% p.a., we can say that the fund has performed exceptionally well. Instead of focusing on absolute performance, we must focus on relative performance.

RISK

By risk, Morningstar mainly refers to the standard deviation in the fund returns. Standard deviation is a statistical concept used to evaluate the variability or volatility of a particular element i.e. NAV in this case. Let us understand this with an example. Let us say, two mutual funds, A and B, have NAV of Rs.100 each on 1st January. On 31st December, both have a NAV of Rs.120 each. However, during the year, NAV of A has mainly been in the range of Rs. 90-130. At the same time, NAV of B has been between Rs.60- 150. So, we see that B has been much more volatile as compared to A. Thus, the standard deviation of B will be more than A. We mainly use variability as a measure of risk here. For our purpose, risk should be average or less than the category average. Morningstar shows risk against category for each mutual fund offering.



SOURCE: Morningstar.in

% ASSETS IN TOP 10

This shows how concentrated the mutual fund is. Unless it is a sector-specific fund, the percentage (%)of assets in the top 10 should not be more than 60%. The percentage of assets in the top 10 investments is easily available on almost all mutual fund websites. We can find the same on Morningstar Fund details as well for each fund.

ASSET UNDER MANAGEMENT

Too small AUM or scheme size would mean that the fund has a higher expense ratio as the expense would be distributed over a small size of unitholders. At the same time, a significantly large AUM will limit the number of investment options and will therefore lead to underperformance of the fund. So, we will follow the ideal AUM size as specified in the table's range. This should remain valid for the next 4 years i.e. until 2024 after which we will have to expand these ranges. When evaluating the ideal AUM size, we should stick in the range provided here.

CATEGORY	AUM SIZE
Small Cap	500-2000
Mid Cap	2000-5000
Large Cap	5000-10000
Debt	Min. 500

FUND STYLE OF BOND FUNDS

We saw that Morningstar uses a 3x3 matrix to evaluate debt as well as equity funds. For debt, they use credit quality vs. interest rate sensitivity matrix. For individual investors, they must always prefer to invest in high-quality funds. Individual investors should stay away from low credit quality bonds. Next, if we are buying for the short term (less than 2 years), we should go for low-interest rate sensitivity, for medium-term (3-7 years), opt for moderate sensitivity and lastly, for the long term (more than 7 years), go for high-interest rate sensitivity in bond fund style.

TOP 10% ASSETS

In bonds, we must be as diversified as possible. So, the top 10 holdings should be less than 40%. In case we want even higher safety, we must buy government bonds instead of corporate/individual bonds.

Besides that, everything remains the same. The same applies to hybrid mutual funds as well. For most individuals, it makes more sense to buy debt-related assets via mutual funds only. With this, we are equipped to make our decision of selecting the most suitable mutual fund category and then also the best funds in them.

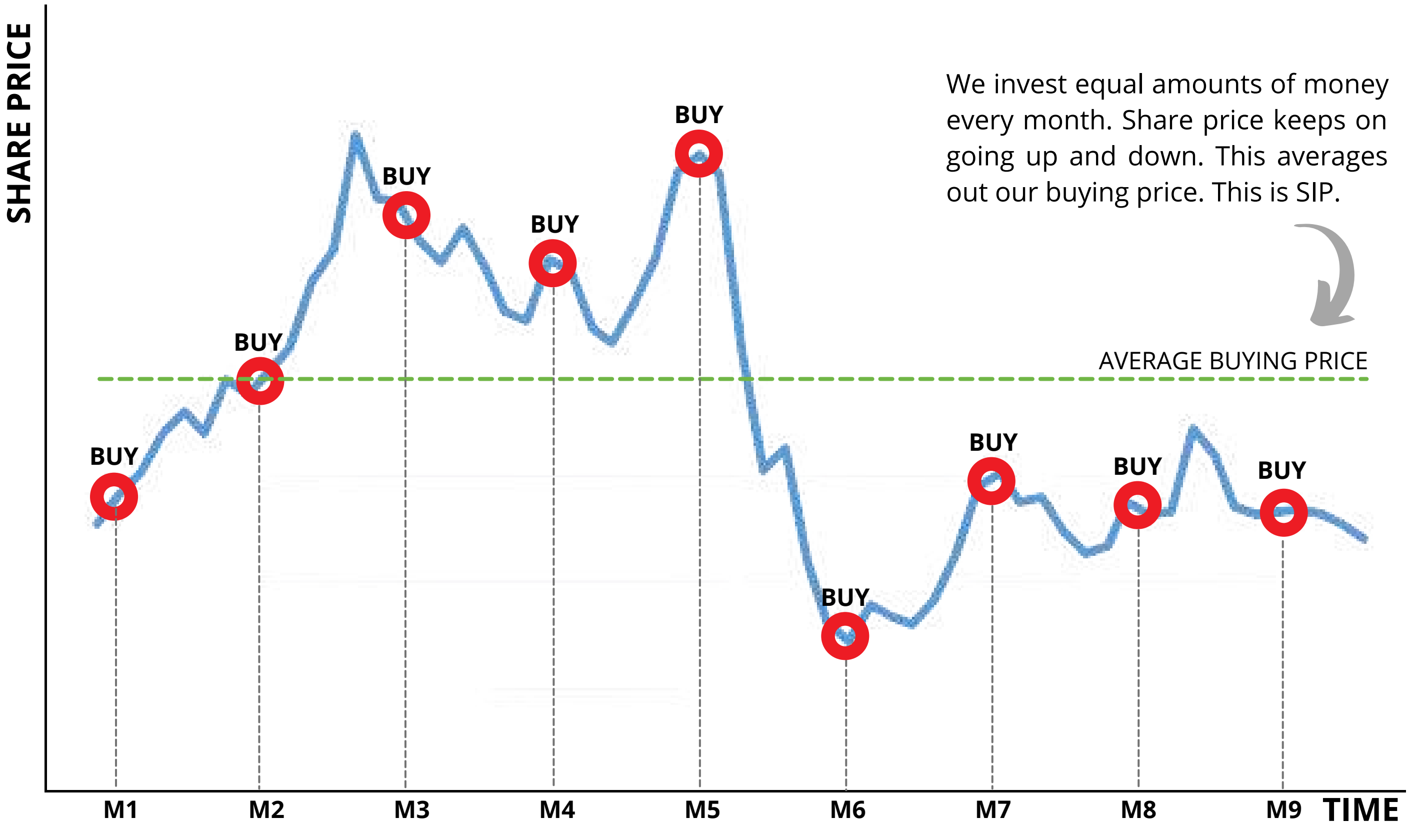
Till now, we have only talked about what it is that we should buy. We have not concentrated on when we should buy. That is solely because coming to terms with market valuations takes years of practice and experience. Even the experts do not understand it completely. We will deal with valuations more systematically. Deciding what to buy is 80% of the effort. Once we have decided that, how to buy and when to buy are relatively simpler decisions.

WHEN TO BUY?

Before we decide upon the time to make a buy, we will take into account if we are investing small amounts regularly or a lump-sum amount at once.

REGULAR SMALL INSTALLMENTS

In most cases, we will be making small and regular investments. The way to do this is through a Systematic Investment Plan, also known as SIP. SIP route invests in mutual funds a certain amount each month or each quarter. The notion behind SIP is that because we are buying the same mutual fund at high, low, and all different prices, over years, we end up buying the mutual funds at average valuations. This way, we systematically ignore the risk of market valuations using SIP.



However, the trouble begins if we stop our SIP plans when the market begins to fall. We had invested when the price was high and stopped investing when the market started falling. Now, we are unable to average out our purchasing price and we end up buying at high prices only. If we do not interrupt our SIP investment plan, we buy the average prices of the market and this works fine to meet our financial goals.

LUMP SUM INVESTMENTS

When we have a lump-sum amount to invest, we have to deal with the impact of valuations. It is a tricky bit and most individuals cannot get this right. Again, we try and deal with the same systematically. The way to do this is as follows:

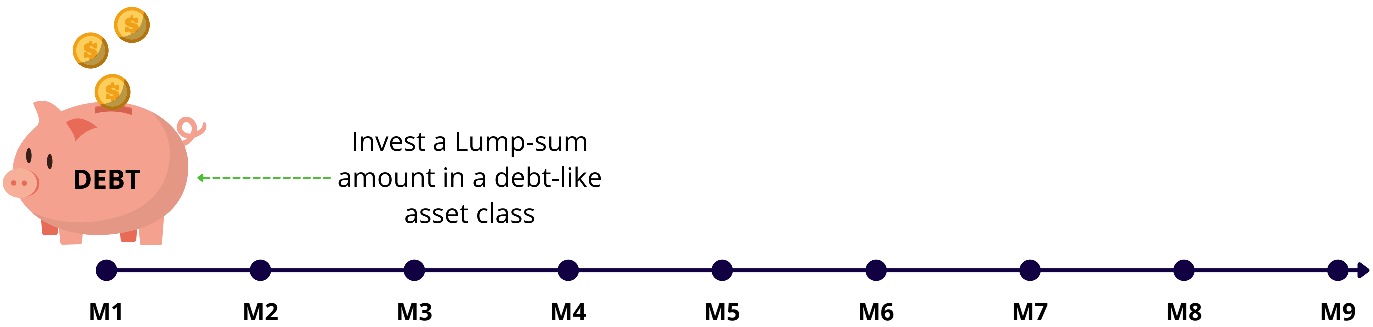
PORTFOLIO MANAGEMENT SERVICE

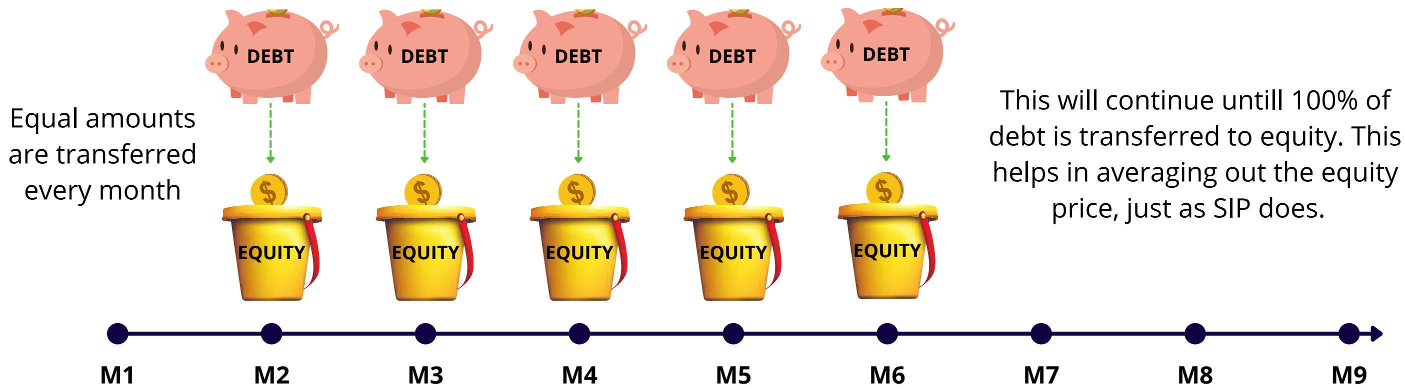
SEBI gives PMS license to companies that can manage our lump-sum investments based on our specific needs. They will charge a fee or a share in profit in exchange for their services. In a mutual fund, our money is invested based on the fund's mandate, irrespective of our needs. When investing in a mutual fund, we need to decide 'when' to give money. However, PMS will invest specifically for us. They will understand our needs and create a customized portfolio after looking at the current market. They will manage valuations better and not lose money as their incentives are also tied to the returns. PMS lacks regulation in comparison to mutual funds. Hence, PMS can churn out equally good or bad performances.

PMS data is submitted each month on the SEBI website. A simple Google search, 'PMS Data SEBI website' will take us to the website. Here, we need to take a look at different PMS companies and their data. We will generally avoid investing in companies with less than Rs. 100 crore under management. We will then go through their website, schedule a meeting with them and repeat this process with a few PMSes. Then, we will select the one that suits us the most and whose ideology matches ours. We will use the same guidelines as a mutual fund but leave out the AUM size. PMS size is generally much smaller than a mutual fund.

SYSTEMATIC TRANSFER PLAN (STP)

The second way of systematically dealing with a lump-sum amount is through a systematic transfer plan (STP). Initially, we deposit the lump-sum in a debt fund or a fixed deposit. Then we initiate a systematic transfer from the debt fund to an equity fund in equal installments spread out over 24 or 36 months. This way, we end up reducing the impact of valuation extremes on our finance. It is a combination of SIP and lump sum.

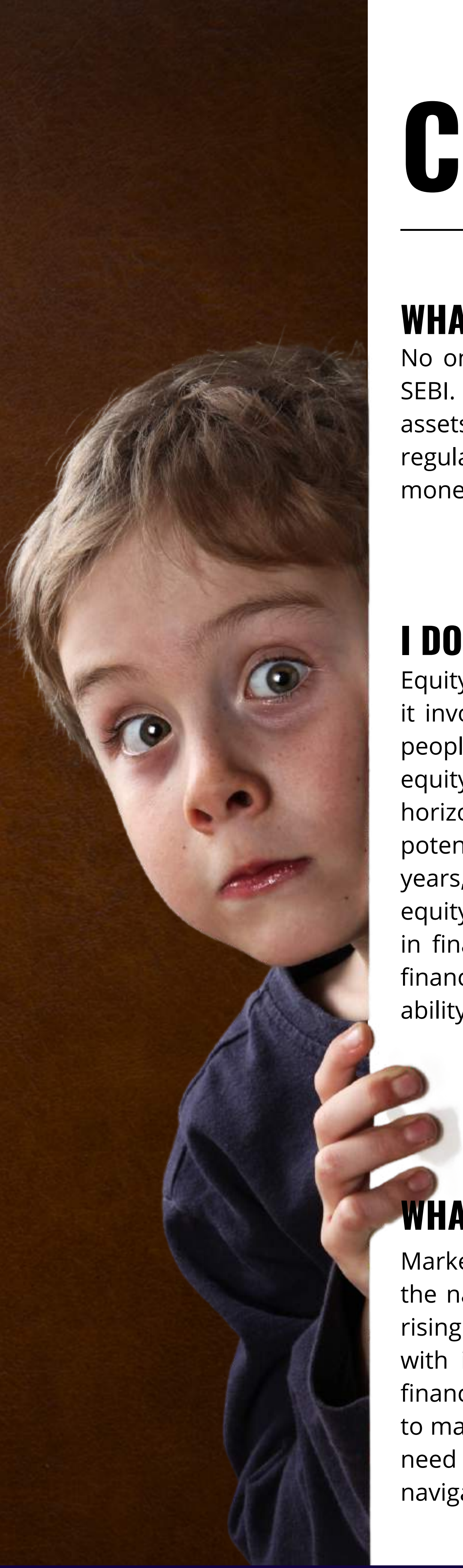




These are the two ways of dealing with lump-sum money to invest and reduce the risk of valuation extreme. We will never try to and judge valuations. It is an art that takes years to develop and an individual investor is better off dodging valuation systematically rather than trying to guess the same.

It is very much possible that we might end up buying when the markets are too expensive and then lose money. This will lead us to lose trust in the asset class and we will leave the principal to recover for years. Imagine what would have happened if we invested 50% of our life savings in equity at the peak of 2008. Our capital would have been eroded by 50-60% in the following 6 months and we would have lost trust in equities for life. This is what can happen if we get the wrong valuations. So, as an individual, we will always deal with valuations systematically rather than judging it by ourselves. We will use SIP, STP, or PMS to cater to it.

So, as an individual, we will always deal with valuations systematically rather than take the risk of objectively judging the same. We will deal with the same either via SIP, STP or PMS. We need to be careful that excitement to invest is highest when markets are at its peak and many people invest heavy lump-sum in the same. However, we must resist the temptation and must go through a PMS at the least. It is generally in such markets that we end up buying expensive and then when the market corrects, we end up with poor experience with the asset class for life.



COMMON FEARS

WHAT IF SOMEONE RUNS AWAY WITH MY MONEY?

No one can run away with our money. It is well regulated by SEBI. So, they appoint a third-party custodian that holds the assets and the entire structure is very formal and well regulated. No individual or company can run away with our money.

I DONT UNDERSTAND EQUITY AT ALL!

Equity is relatively more complex than other asset classes since it involves a lot of uncertainty and it is very natural for many people to get overwhelmed with it. However, on the other side, equity gives the best returns. If we have a long investment horizon, very few asset classes will be able to match the potential of equity. For instance, if we need money after 20 years, FD will only increase our money to 5 times whereas equity can multiply it 12-16 times or even higher. The difference in final value is huge. That is why equity is required in most financial plans. Long term plans with moderate risk-taking ability need to be planned with equity.

WHAT IF MARKET FALLS?

Market falls are inevitable but they will get back up too. That is the nature of the markets. We cannot be afraid of the market rising and falling when investing in mutual funds. If we deal with it systematically, by not trying to time the market, our financial goals will be met and we will perform well. If we give in to market enthusiasm, only then will investments take a hit. We need to have a disciplined approach and we will be able to navigate through a volatile market.

EQUITY INVESTING

DIRECT	INDIRECT	
	ACTIVE	PASSIVE

In mutual funds, we saw that the fund has skilled experts and they carry out research, and based on their skill and asset selection, the fund's returns are determined. It is expected that the fund manager and the team will outperform the category by picking out stocks or bonds that are better than others and to do so, they incur costs in the form of the expense ratio discussed above. Here, the fund manager actively picks stocks and the weight is assigned to each stock in the portfolio. This is called active management.

The second way to manage money is passive. Here, fund managers do not research or actively study companies. They do not make the decisions of the stocks or bonds to be picked and the weight to be assigned to each one of them. Rather, they pick an index and invest in the same stocks and the same weight as the index.

For instance, if they follow Nifty, which has 11% weightage to Reliance, 10% to HDFC Bank, so they will invest 11% of their entire AUM in Reliance and 10% in HDFC Bank and so on. They will replicate the returns obtained by Nifty as it is. The objective is to minimize the costs incurred to make active investment decisions. There are a variety of indices and they can follow any one of them. They can also follow commodities. They can invest the entire amount in Gold and a buyer can buy a gold ETF instead of gold without any fear of theft. They can invest as per Nifty50, Nifty100, FMCG Index, BSE Small-Cap, and so on. So, whatever the index returns will be our return as well.

PASSIVE INVESTING

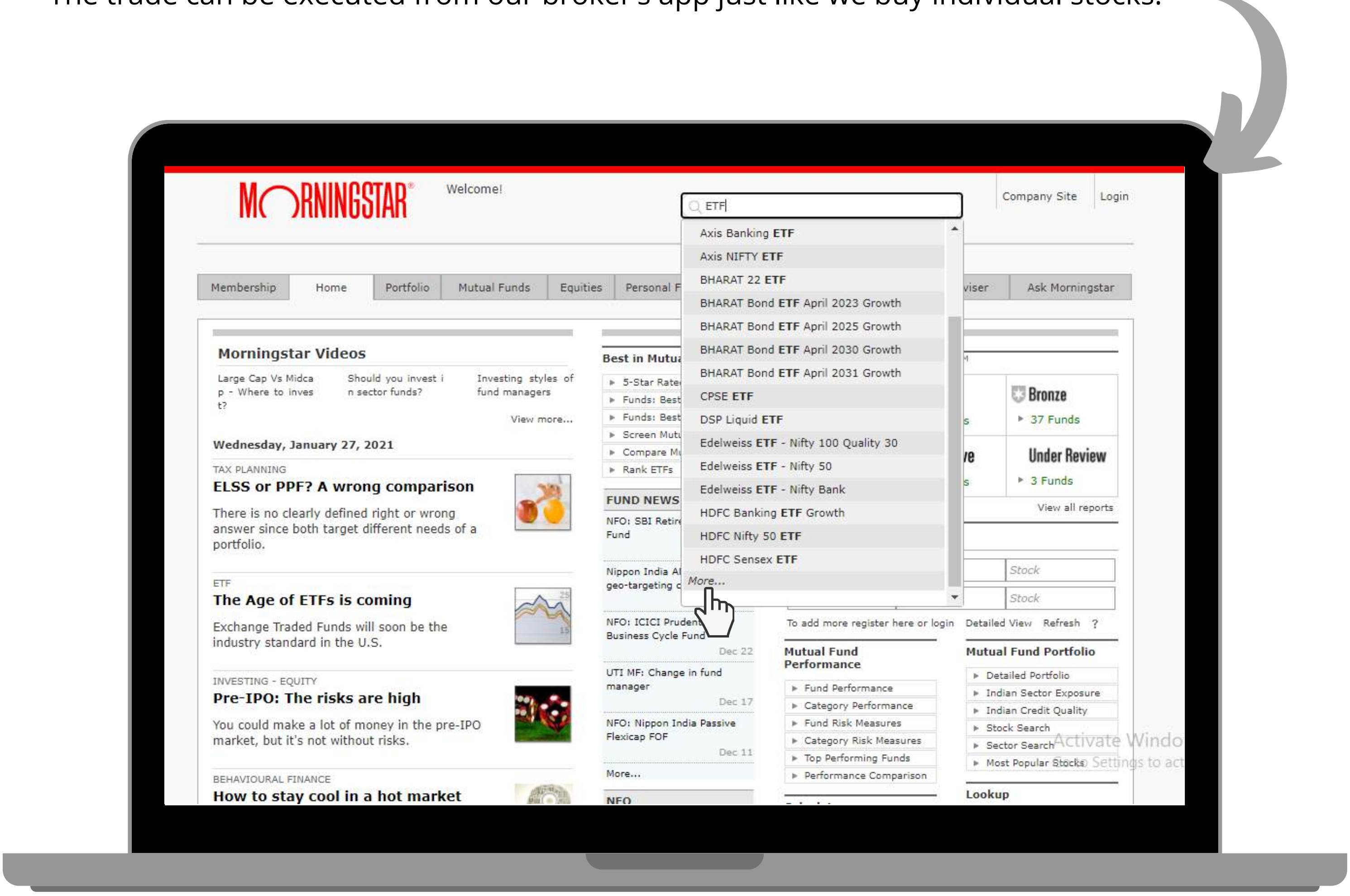
Index funds and ETFs are two ways of passive investing. ETFs are traded over the exchange and can be bought and sold like ordinary shares. At the same time, index funds are bought and sold like mutual funds.

ETFs generally have a lower expense ratio than index funds. When selecting ETFs and index funds, the key metric to be used to evaluate the best fund is the expense ratio as everything else is pretty much standard. The idea is that both ETF and index funds track the index or asset class for returns and as a result, those who can do it for a lower price should be bought. As a result, ETFs are recommended over Index Funds.

EXCHANGE TRADED FUNDS (ETF)
Traded on the stock market like equity shares

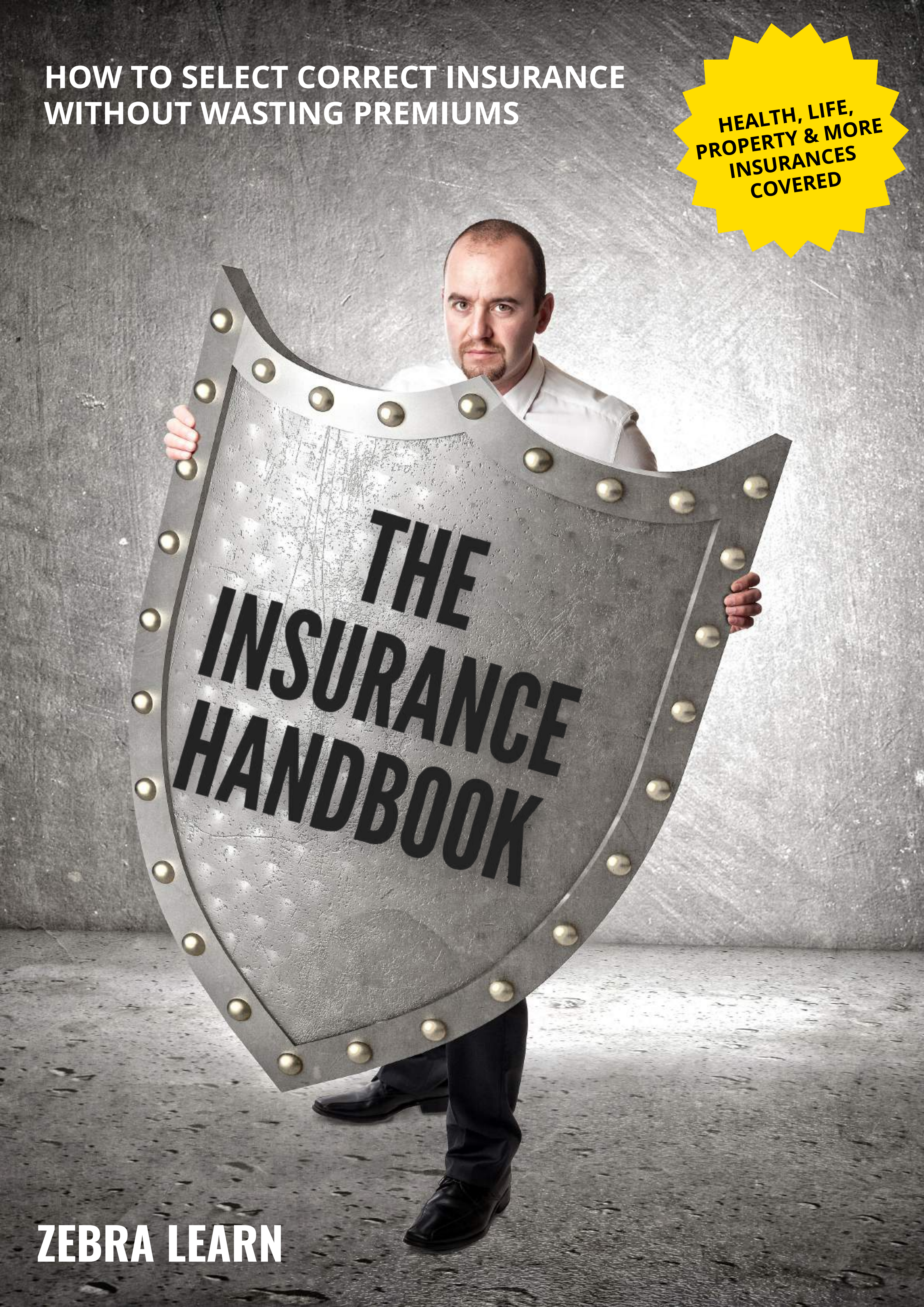
INDEX FUNDS
Available in the market like Mutual Fund Units.

To select ETF in India, go to www.morningstar.in. In the search bar, type, 'ETF' and a dropdown menu will appear. Here, click on 'more' and it will take us to a list of ETFs available in India. In the ETF list, we can see the various indices or asset classes that we can invest in. The trade can be executed from our broker's app just like we buy individual stocks.



The indices are average performance in the category. BSE and NSE create indices that show average performance i.e. the average of all active investors. So, in the long run, getting a return that is in line with the category average works out well for wealth generation. Also, with active investment, we are allowing the manager to incur an expense ratio and then expect them to outperform the category or at least be at par with the category average. For instance, the fund manager incurs 1.5% expense and the category returns 16%. So, they need to achieve 17.5% just to be on par with the average. This is a relatively difficult task to do. As a result, ETF is used which has a very low expense ratio and gives us category average performance consistently. However, the return shall be enough to meet our goals.

In ETF and Index Fund, buying the correct category index is the key. The index represents a category and the return will be based on the same. So, either mutual funds or ETFs, both work fine to meet our financial goals, if done well.


HOW TO SELECT CORRECT INSURANCE
WITHOUT WASTING PREMIUMS
HEALTH, LIFE, PROPERTY & MORE INSURANCES COVERED
THE INSURANCE HANDBOOK
ZEBRA LEARN

We already saw how insurances protect our Lazy Financial Plans from leakages and any one-time event that might ruin our years' worth of effort. As we have learnt earlier, for insurance we pay a premium to a company and they cover the risk for us and in case there is an event or loss, the insurance company pays the loss. It is not an asset class but is needed to keep other class assets and the plan safe. Let us get started with common insurance policies.

HEALTH INSURANCE

Health insurance is needed to protect our financial interests when we or someone from our family falls sick and a sudden health bill comes up. In such situations, the insurance company pays for our healthcare expenses. First, we need to understand a few important terms that relate to insurance products in general and health insurance in particular.

TERMS TO KNOW

1 PREMIUM

Premium is the up-front fee paid to the insurance company for covering our risks. If any liability arises, the insurance company pays the same and if nothing arises, the premium remains with the insurance company. Premium is the price that we pay to transfer our risk to the insurance company.

2 PRE-EXISTING INCLUSION & EXCLUSION

Pre-existing inclusions and exclusions refer to the pre-existing medical conditions that will be included or excluded from the insurance cover. So, any liability arising from such conditions will not be borne by the insurance company, if mentioned. Usually, the health insurance companies specify a time-frame of 2-4 years, after which the pre-existing illnesses are covered.

3 SUM INSURED

The sum insured is the amount up to which the insurance company will cover the risk. It is the maximum payment that we can receive from the insurer. The premium is dependent on the sum insured. Thus, an adequate amount of sum insured is critical and we do not wish to be under-insured or over-insured

4 SUB-LIMITS

Insurance policies impose sub-limits so that they can control the expenses incurred by the patient. For example, they set limits for the room category or the room rent. This ensures that the insured person does not spend unnecessarily. We will generally go ahead with a policy that has not such sub-limits in their policy.

NO CLAIM BONUS 5

It is a financial benefit given to us by insurance companies if we do not ask for a claim in any given year. No-claim bonus operates in two ways. They either offer us a higher sum insured at the same premium next year, or they offer the same sum insured at a lower premium. A No-claim bonus is an insurance company's way of rewarding users who make fewer claims. We want the policies that have the highest no-claim bonus.

6 CO-PAY CLAUSE

Co-pay clause refers to a policy condition according to which the insurance company does not pay 100% of the expenses, instead, it requires the insured to bear a percentage of the expenses. They may have a 10% or 20% co-pay clause, which will require us to pay the same percentage of the entire claim. So, if we claim Rs. 10 lac with a 20% co-pay, we will only be reimbursed with Rs. 8 lac. The Co-pay clause is the insurance company's way that forces us to spend wisely. We will avoid insurance policies that have a co-pay clause.

RIDERS 7

Riders are add-ons to the basic insurance policy which offer additional benefits or risk protection for an additional premium payment. For instance, health insurance policies come with accident cover riders combined. So, if we pay the additional amount specified, we will be covered for these additional risks to the extent mentioned.

8 CLAIM COMPLAINTS

Insurance companies often reject claims that do not make sense to them or seem suspicious. It is a routine part of their business. So, the number of complaints against an insurance company per 10,000 claims made is an important metric that depicts the company's tendency to honour claims and not reject them. So, we will go ahead with companies that have low complaints per 10,000 claims.

9 TOP-UP PLANS

They are insurance plans that are added over the base plan to increase the cover at a relatively lower cost. For instance, a person might have a base plan of Rs. 2 lac as the sum insured. He may take an add-on of Rs. 8 lac. In case of a health-related expense, the first Rs. 2 lac will be paid by the base insurance company and any amount over Rs. 2 lac, will be paid by the top-up insurance company. Top-up plans increase the coverage at a significantly lower premium price.

10 RESTORATION OF COVER

Health insurance policies offer a restoration of the cover in the same period if the liability arises due to an unrelated illness in the same year. For instance, if we have a cover of Rs. 10 lac that we have exhausted due to disease A and have another liability of Rs. 8 lac due to disease B, the insurance policy will cover both these liabilities if it has restoration benefits. The catch is that the two diseases should be unrelated.

11 FLOATERS V/S INDIVIDUAL

Individual plans refer to those policies where only an individual is being covered by the policy. At the same time, floater plans are those where all members in the policy (generally a family) are covered to the combined extent of the sum insured. This means that the insurance company covers costs relating to the illness of any of these members. If insuring for the entire family, we will go for the Family Floater policy, and if only for ourselves, we will opt for an individual policy.

FACTORS FOR HEALTH INSURANCE

Let us understand the features of ideal health insurance and the factors to be considered while selecting a policy. The features of an ideal policy are as follows –

95% CLAIM SETTLEMENT RATIO

RESTORATION COVER

POST HOSPITALIZATION COVER

NO CLAIM BONUS

CO-PAY CLAUSE

SUB-LIMITS

CASHLESS SETTLEMENT

PRICE

FAMILY FLOATER PLAN

LESS THAN 30 CLAIM COMPLAINTS

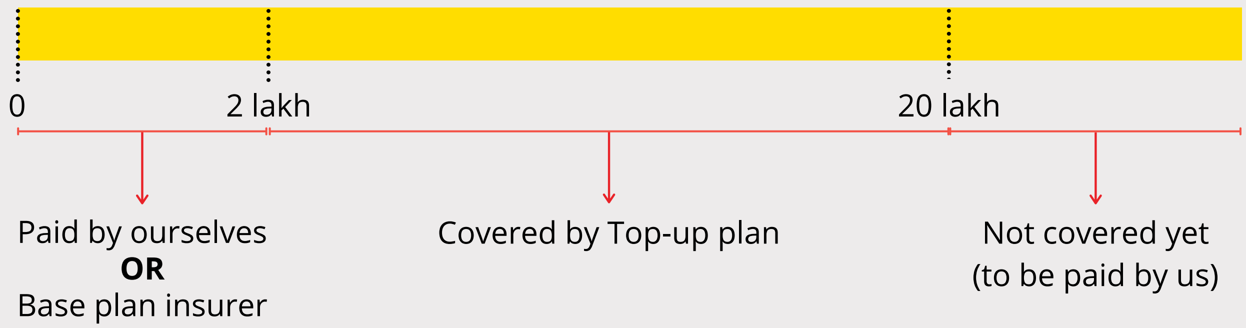
HOW TO SELECT?

Now, we understand the factors that are relevant to health insurance. We will now go through a video that explains two tools– HTSecureNow Mediclaim Ratings and PolicyBazaar. In the video, we will discuss the process to select policies, the factors to be considered, the insuring procedure for large amounts using Top-ups, and the selection of top-ups.

INSURING FOR LARGE AMOUNT

The video taught us to insure for larger amounts using top-up plans and base plans together rather than buying one large base plan. This reduces the up-front fee significantly for the same sum insured. Some people only buy a top-up plan, they let go of the base plan. For example, let us assume that they buy a top-up plan that covers all the expenses over and above Rs. 2 lac, up to Rs. 20 lac. In case a health-related liability arises, they will pay Rs. 2 lac out of their pocket and anything over that will be paid by the insurance company.

COVERAGE OF HEALTH EXPENSES



Remember that even if we have a bill of less than the base cover, we must file the same with an insurance company. This is because if there is any subsequent claim in the year, the first amount will be deducted. For instance, in the previous example, let's say we have an expense of Rs.1.5 lac and a subsequent expense of Rs.4 lac in the same year. So, if we report the first one to the top-up insurer, we will get back Rs.3.5 lac when we claim the second expense. The insurance company deducted Rs. 1.5 lac from the first claim and Rs. 50,000 from the second one. However, had we not reported the first claim, then the company would have deducted Rs. 2 lac from the second one when we would claim it. In that case, we would only receive the remaining Rs. 2 lac.

For people with sufficient liquidity and 12 months' worth of emergency fund (we will learn more on this in the planning phase), it is fine to have only a top-up plan. They can pay the base coverage from their savings and if this expense is significant, they can always get a claim from the insurance company. People with liquidity crunch and limited savings must buy both the base plan as well as the top-up plan.

Not having a top-up plan at least is a disaster. Any major illness, disease, or accident can ruin the Financial Plan. Smaller bills can still be handled without insurance, as they do not have that high financial implication. But countless families have seen their wealth being destroyed due to one member's critical illness. Top-up plans protect us against this.

HOW TO BUY?

COMPANY'S WEBSITE

The best way to buy insurance is to do so from the company website directly. Call them up directly or try to find a ‘Buy Now’ or ‘Contact Us’ on their website. This way, no intermediary will be involved and the company can offer us the best price. This is because intermediaries are paid high commissions in the insurance industry which we can skip by contacting the company directly.

INTERMRDIARY WEBSITE

The next best alternative is to buy from digital platforms like Policybazaar.com and ETMoney. These online providers are better than individual insurance agents on the price front because they want to capture a higher share of the market. However, they do not provide a lot of support services as an agent does. However, if these companies extend support services like getting our claim through, etc. then we should go for these online portals.

INDEPENDENT AGENT

The last way is through independent agents. They help us stay connected with insurance companies whenever we face any difficulty or want to ask for a claim. However, for this, they exclusively operate at commissions which are generally very expensive. As a result, health insurance is best bought from the company directly or else from digital platforms.

LIFE INSURANCE

We have already understood our need for life insurance in the profiling stage. Not everyone needs life insurance. But those who do, suffer significantly if they do not have a proper insurance system in place. Their entire family's survival depends on life insurance in case of death. We also know the insurance coverage we need.

TERMS TO KNOW

1

COVER UPTO THIS AGE

It is the maximum age up to which the insurer will cover the insured person and will pay life insurance benefits. This can be 75, 80, or 90 and varies from insurer to insurer, policy to policy. The insurer will not allow the insured person to renew their risk coverage beyond this age because after that it becomes a case of natural death rather than a risk.

2

SUM INSURED

Sum insured is the coverage amount of the life insurance that has been purchased. It is the amount that the insurance company will be liable to pay in case the risk materializes. Also, the insurance premium is decided based on the sum insured and a few other factors.

3

PREMIUM

Premium is the upfront fee paid to the insurance company for covering our risks. If any liability arises, the insurance company pays us a lump sum and if nothing happens, the premium remains with the insurance company. Premium is the price that we pay to transfer our risk to the insurance company.

CLAIM SETTLEMNT RATIO

4

Claim Settlement Ratio depicts the percentage of people whose claims were settled (the amount was paid) by the insurer as compared to the total number of people who have made claims. A claim settlement ratio of 97% means that out of 100 claims made, the company rejected 3 of them. We wish to get ourselves insured with a company that rejects fewer claims than others.

LIMITED PAY

5

It is a special kind of term insurance where a person pays higher premiums for the first few years and then no premiums going forward and gets covered for a fixed maturity that is relatively longer. For instance, a person may buy 20-year term insurance and pay the higher premium for the first 8 years and then no premium for the next 12 years to stay insured for 20 years.

RETURN OF PREMIUM PLANS

6

Return of Premium Plans is those that return premiums at the end of the entire duration of the Insurance Plan. These are only valid for multi-year Insurance schemes and the Insurance company returns premium under these plans with or without any additional interest. These are marketing gimmicks by Insurance companies. We will keep Insurance and Investment separate which we will discuss very shortly.

SOLVENCY RATIO

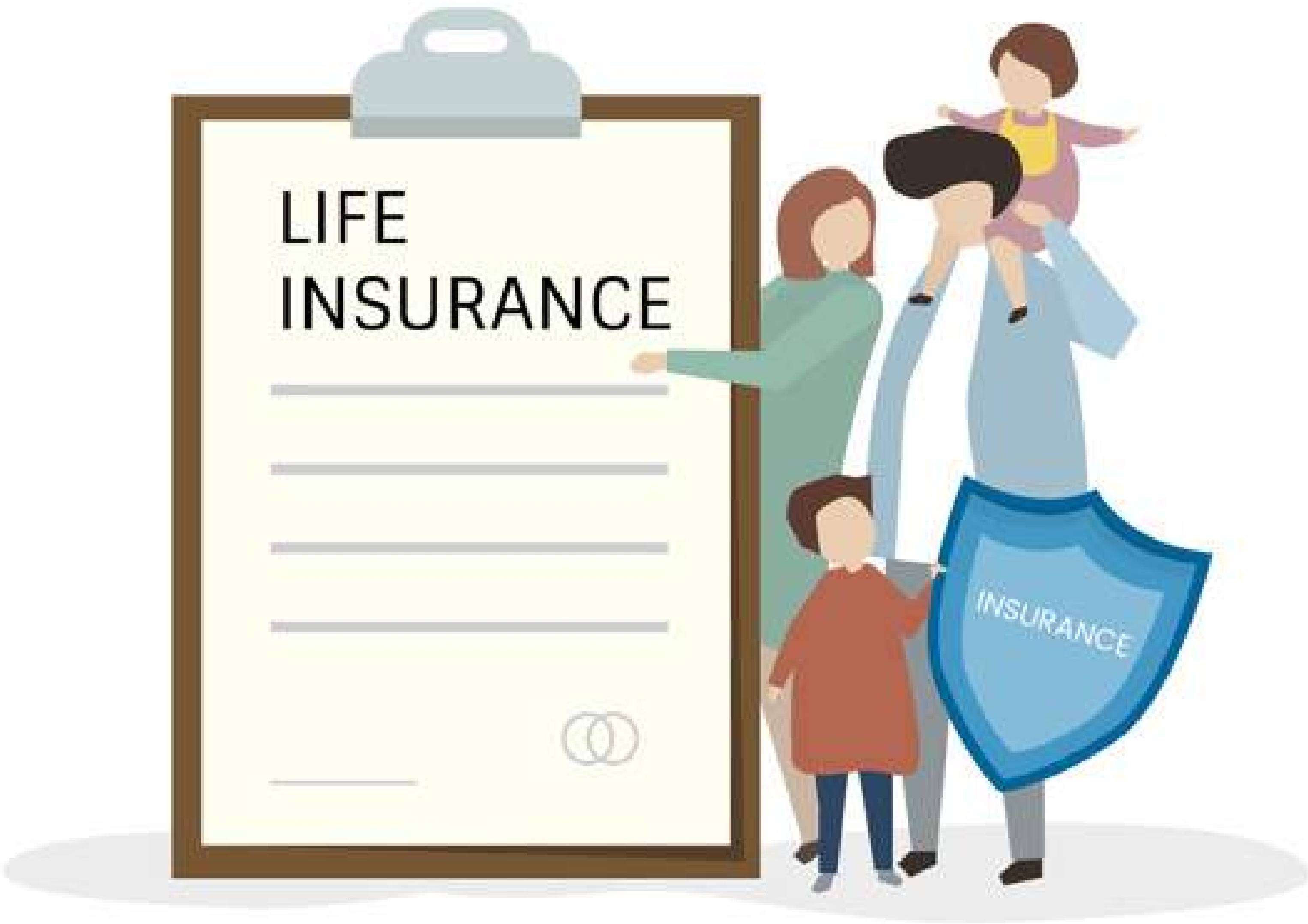
7

Solvency Ratio of a company is its ability to meet its liabilities and financial commitments with its cash flow and assets. So, with insurance companies, the solvency ratio represents their financial ability to meet the liabilities that they have on their books. In India, insurance companies have to maintain the solvency of 15 as per IRDA. Higher the Solvency Ratio, the better it is.

CLAIMS COMPLAINT RATIO

8

Insurance companies often reject claims if they seem ingenuine or suspicious. Of those they reject, many users also complain to the insurance company in consumer courts. It is a routine part of their business. So, the number of complaints against an insurance company per 10,000 claims made is an important metric. It shows the company's tendency to honor claims and not reject them. So, we will go ahead with companies that have low complaints per 10,000 claims.



TYPES OF LIFE INSURANCE

There are three major life insurance types that we will talk about over here - ULIPs, Endowment Plans and Term Plans. Let us understand each one of these, how they are different and which one is most suitable for us.

ULIPs

In a ULIP plan where the premium is divided into two parts-insurance and investment. Here, a part of the premium is used as a premium for life insurance, and another part is used as an investment. The investment component is put to investment products like equity, bonds, mutual funds, etc. The policyholder can choose the asset classes. It promises to pay a guaranteed lump sum to the family/policyholder on the death of the policyholder or maturity of the policy, whichever is earlier.

ENDOWMENT PLAN

Any life insurance policy that has an investment component is an endowment plan. Like ULIPs, you get a lump-sum on the death of the policyholder or maturity of the policy, whichever is earlier. Unlike ULIP, we cannot decide where the investment component will be invested. It is decided by the insurance company. Like we discussed earlier, we should never mix investment and insurance.

TERM PLAN

This is pure insurance and there is no investment component. We pay only the premium for the insurance component and if there is no claim, the money gets wasted and we do not get paid back anything in return. Term plans offer higher coverage than all other plans. This is the one that we need to buy. We want our life insurance money to be wasted.

We will observe two things with endowment plans and ULIPs. First, whenever they advertise, they will use large numbers. Rs.10,000 each month becomes Rs. 1,00,00,000 in 20 years, Rs.65 a day, will become Rs.30,00,000 in 15 years and so on. However, if we inquire about the rate of return, most will return sub6% for the same which is pretty much in line with fixed deposits. If we invested the investment component separately, we could have made much better returns. The companies try to use big numbers as a marketing technique to get us all overwhelmed and not use too much logic against it. As a result, whenever we see big numbers, we need to be very careful and always ask for the rate of return.

Second, the sum insured in this case is generally low. The reason for this is they need a sizeable component to go in the investment component. As a result, we would either be inadequately insured or we would need to pay sky-high annual premiums. The latter can become psychologically exhausting. Additionally, we might even have to let go of one month's worth of our salary as an annual premium for insurance. It is impossible to expect someone to pay so much for an insurance cover and thus, most will remain under-insured.

If we are lured by money-back on maturity, we can do something interesting here. Check the premium of the endowment plan for a particular coverage amount. Now, we could buy a term plan (at a much cheaper rate) of the same sum insured and invest the balance in an equity mutual fund. If this is done over multiple years, at maturity, we will have 2-3x of what the endowment fund returns us. So, we will always be buying a term plan and investing the rest as per our financial goals.

HOW TO SELECT?

By now, we are aware of what to buy and for how much. We also know the terms and types of life insurance. The next big question that crops up is concerned with the one that we are supposed to be buying. We can see a very detailed explanation of the same in the next video. It will help us identify the most suitable life insurance policy for us. Also, the policy that we select, must meet the following criterion to be effective.

A policy that meets all these criteria, must then be selected based on the price for the same. Go through the detailed PDF of the policy that is selected to achieve a greater and detailed understanding of the same.

CLAIM SETTLEMENT RATIO: 95%+

SOLVENCY RATIO: 1.8+

FIRM'S AGE: 15YEARS+

WHERE TO BUY?

1) Company's website
2) Intermediary website
3) Agents

ACCIDENT COVER

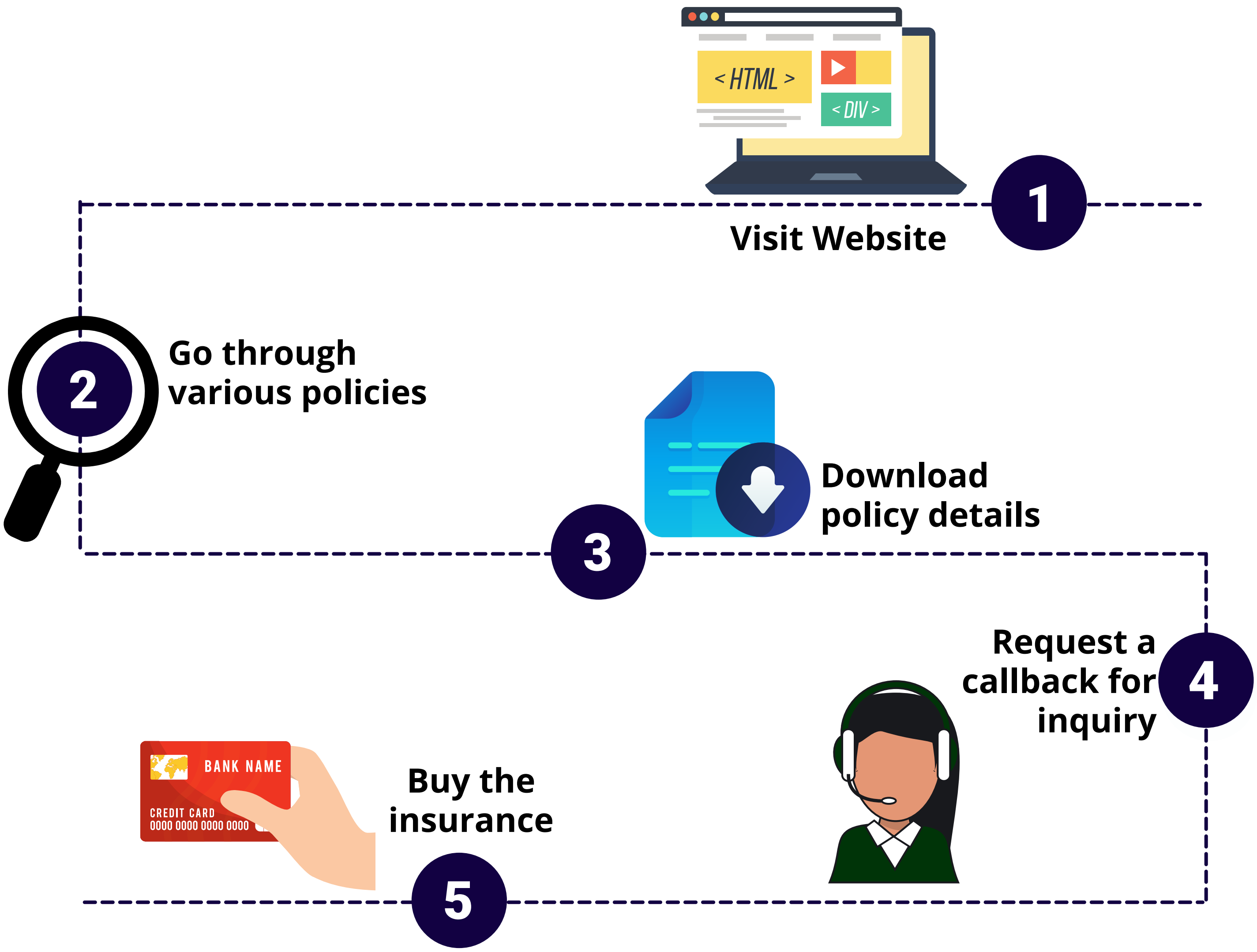
It has already been explained that health insurance covers our treatment expenses in case we meet with an accident or we fall ill. The term plans cover our family's expenses in case the accident is too severe and something untoward happens. But in most cases, we would probably make it out alive with a temporary or permanent disability. We might not be able to go to work for a few years. In such cases, we need an accident cover.

If we need life insurance, we also need an accident cover. They pay us a certain amount if we are disabled. If the disability is permanent, they pay a lump-sum amount. If the disability is temporary, they pay out every month to help us sustain our expenses during the period. These come in very handy at a time when we are unable to work because of an accident.

HOW TO SELECT?

Our agents and online portals do not push accident cover so much because these are relatively small and they do not earn much from these covers. We could not find a platform that allows us to compare and sell plain accident covers. Few of them try to sell it as riders on the health insurance policy. However, we do not want to buy riders, we will buy them separately. That way they will be cheaper and would serve the purpose as well. Going through multiple websites, we found the following companies to be offering accident cover policies:

BAJAJ Allianz General Insurance Co. Ltd. | HDFC ERGO GENERAL INSURANCE | ICICI Lombard GENERAL INSURANCE | MAX Bupa HEALTH INSURANCE



HOW TO SELECT?

For instance, we did go through one of the accident covers. Going through the brochure, we came across the following benefits of the policy–

DEATH -
100% of Sum Insured

PERMANENT TOTAL DISABILITY -
125% of Sum Insured

PERMANENT PARTIAL DISABILITY -
As per the table

TEMPORARY TOTAL DISABILITY -
Rs.5000 or 1% of Sum Insured

MEDICAL EXPENSES

We have already covered medical insurance and death-related expenses in health insurance and life insurance. So, here we can remove these benefits over the call and get our premium reduced significantly. This is how we select accident cover.

It is relatively one of the simpler forms of insurance. We must make sure that our accident insurance is in place if our family depends on our income. To buy the same, we will have to buy it via the company's website only. There is no marketplace for it and the agents are hardly interested in selling this.

The last category of insurance that we talked about is general insurance. All other forms of insurance, other than the ones we discussed earlier, are a part of general insurance. We need to get our car insured, we need to get our property insured, and so on. We have already profiled that whether or not, we need these insurances

GENERAL INSURANCE

MOTOR INSURANCE

The first and most common category of insurance is motor insurance. We insure our vehicles from any damages and accident-related losses.

TERMS TO KNOW

INSURED DECLARED VALUE (IDV)

Insured Declared Value is a concept for general insurance where the value of the asset being insured is declared. It is equal to or less than the fair value of the asset. IDV is similar to the 'sum insured' and in case a liability arises, IDV will be used as a base for all calculations of settlements.

THIRD PARTY COVER

Third-party insurance is a concept related to motor insurance that protects us against any liability that arises due to a loss to a third party (to their car or physical), resulting from an accident that involves our vehicle. So, in case our car is involved in an accident, the losses to the counter-party are insured by the Third-Party Insurance.

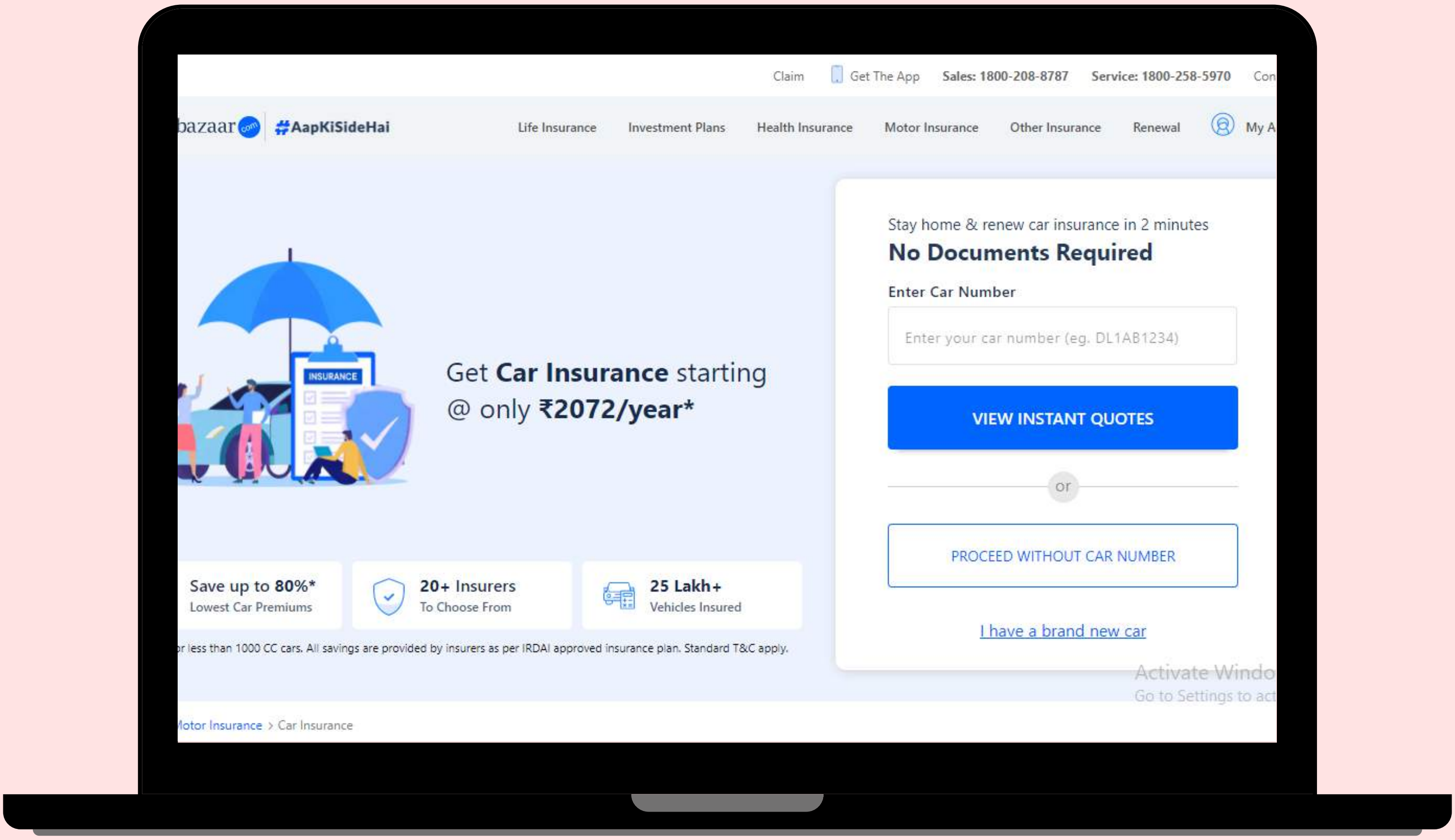
COMPREHENSIVE PLAN

Comprehensive plans are those which insure us against third-party liabilities but also insure us to cover any losses that our car might have. Law requires that every motor on road must have at least third party insurance cover, comprehensive cover is optional.

HOW TO SELECT?

Selecting motor insurance is pretty simple and straightforward. Generally, the higher the IDV, the higher would be the premium. So we need to identify which company gives us the highest IDV for the lowest premium. The policy should be straight-forward and should not include other complications.

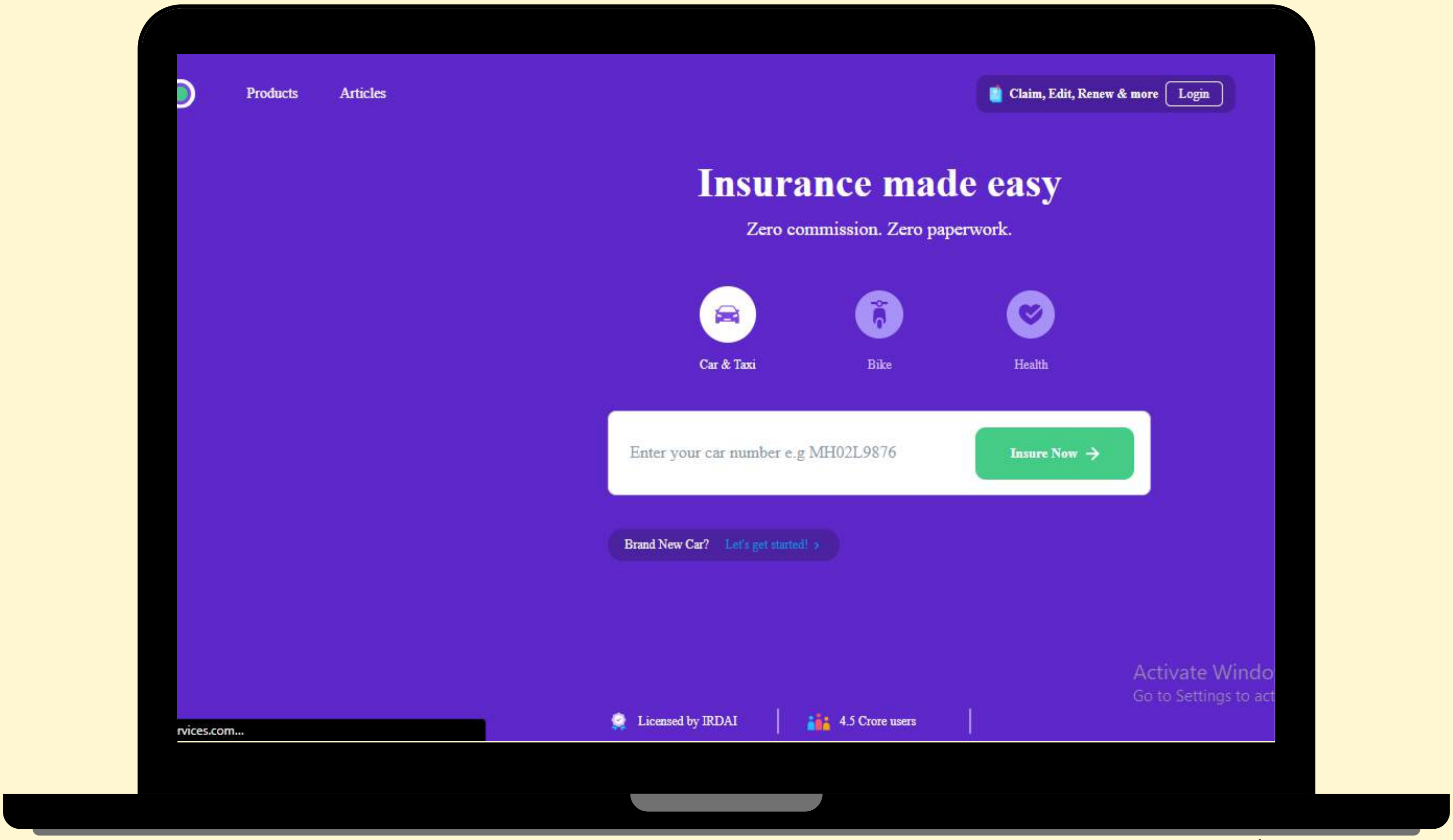
Go to Policbazaar.com and fill in car details. We will get a list of options to select from. We also need to decide if we want a third-party cover or a comprehensive cover. We will suggest going ahead with a comprehensive plan. However, either does not make a world of difference to our financial health in the long term. Our emergency fund also comes to rescue us in such situations. Remember that third party insurance is a must for each motor owner in India.



SOURCE: Policybazaar.com

WHERE TO BUY?

The motor policy can again be bought from online portals like PolicyBazaar.com. These provide multiple options and if we intend to, we can buy it then and there itself. Another place that we can suggest is Acko.com that specializes in car and 2-wheeler insurance. They do not appoint any third party agents or commissions and only sell it through their website and as a result, can sell cheaper. It will be a relatively cheaper alternative to traditional methods.

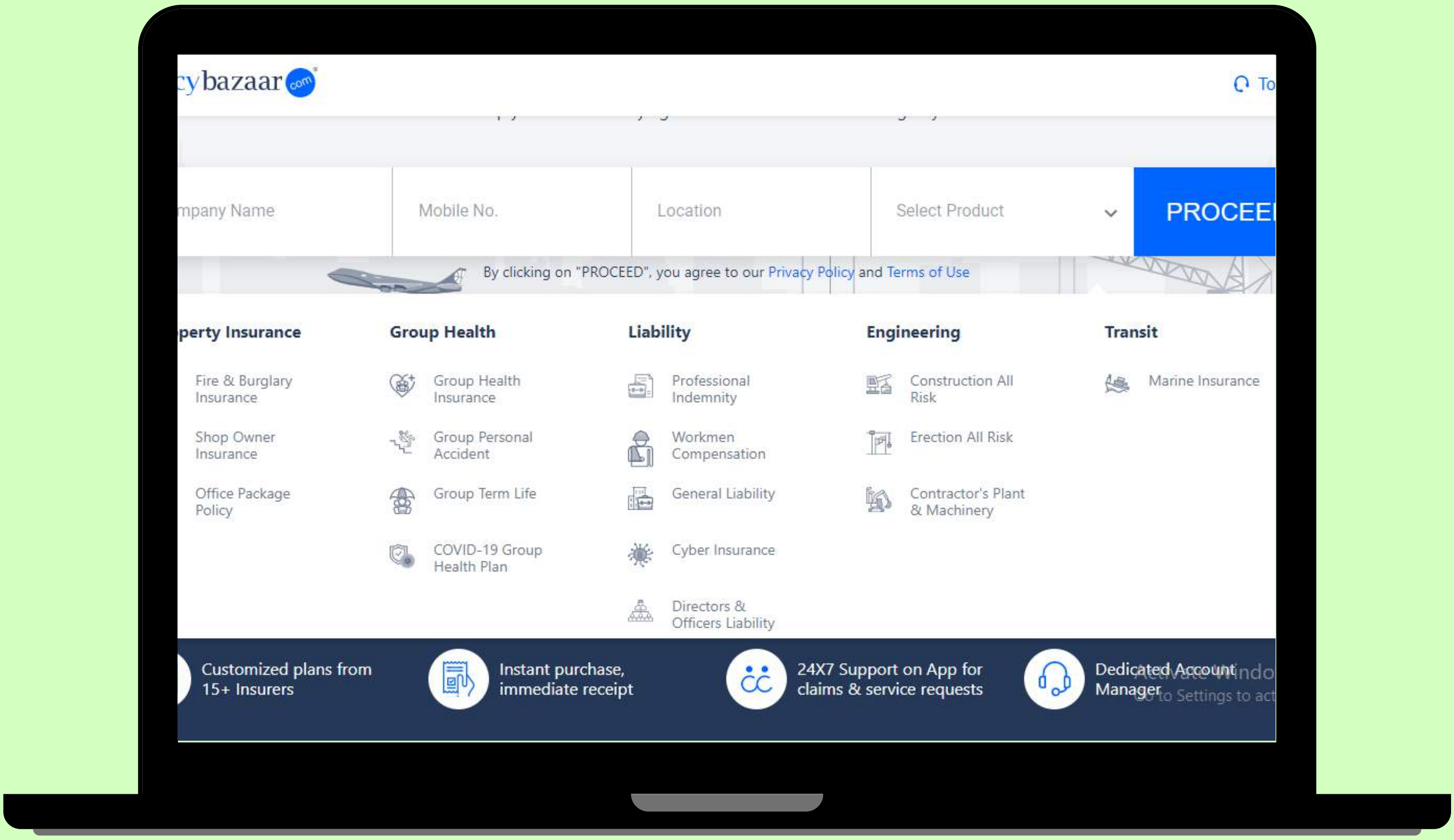


SOURCE: Acko.com

BUSINESS INSURANCE

By now, we have insured ourselves for most of the individual risks. Next, we need to buy insurance for our property, business, and other assets. As we already saw in the profile stage that we face a very large variety of risks and we also created a list of those that we need to get insured. These are very diverse kinds of risks. Not all these risks can be explained individually as they are beyond the scope.

We here present a list of common insurance policies and schemes that individuals and businesses need. We will visit the website– www.sme.policybazaar.com to understand these in greater detail. When we go to the website, we will see a list of common insurances needed. These are listed here.



SOURCE: https://sme.policybazaar.com/

Businesses have different kinds of risks as compared to Individuals. These products can together serve their needs to transfer risk. Each insurance fits a specific business environment. So, we need to select the ones that are relevant to us.

The most common insurances are fire & burglary insurance. Shop owners' insurance helps ensure the business against loss to physical property or the shop.

Individually, we can also ensure our assets and other properties. The best way to get the specific product is to request a ‘CallBack’from online insurance portals like Policybazaar.com or else to go on the company website directly and talk to their representatives. This way, we get a complete and customized explanation of each product.

TERMS TO KNOW

ASSET-WISE SUM INSURED

Sum insured is the maximum amount up to which the insurance company will cover the risk. For instance, in case of property insurance, a sum insured of Rs. 80 lac means that all liability up to Rs. 80 lac will be paid by the insurance company and any liability above Rs. 80 lac will have to be borne by us. The sum insured decides how much premium we have to pay. We need to estimate the sum insured for each asset that we own.

PREMIUM

Premium is the upfront fee paid to the insurance company for covering our risks and if some liability arises, the insurance company pays the same and if nothing arises, the premium belongs to the insurance company. Premium is the price that we pay to transfer our risk to the insurance company.

RISK COVERED

Risk covered refers to the list of risks that have been covered by the insurance policy. For instance, some property insurance might cover the earthquake, whereas others might not. Thus, we need to understand the risks that are being covered for each type of insurance that we discussed earlier.

CLAIM COVENANTS

For each insurance policy, some covenants or details are in-built in the policy. These are conditions and restrictions to be followed by the policyholder. Claim covenants vary based on the type of insurance scheme and risks covered. One needs to understand claim covenants for each type of insurance that they are getting for themselves.

By now, we have understood all the major asset classes available. We have understood the characteristics, working, math, positives, and negatives, tax treatment, selection process, and suitability of each of them. Now, we will use our Lazy financial profile and the asset options to create a customized Lazy Financial Plan for ourselves. We know where exactly we stand today, we know our future goals, the asset options to meet them, and the factors that are influencing the same. We will link them together so that everything falls in place and a working plan is created which is tailor-made to suit our needs.

Remember, the plan is to be executed by us. It has to be simple. As long as our goals are being met, it is okay to pick options that we are comfortable with even if they don't give us higher returns. We need to remember that a great plan not followed is no match for a good plan that is followed. So, our focus should be entirely on creating a financial plan that can be followed by us.

As mentioned in the beginning, we may have been a little bored while talking about profiling and confused about asset classes and options. However, everything will fall into place and seem to connect wonderfully in the third phase where we will talk about the Lazy Financial Plan. In the next section, we will understand more about Lazy Plan and create one for ourselves. The more we practice, the better plans will we create.

LAZY FINANCIAL MASTERPLAN

PUTTING ALL THE PIECES TOGETHER AND MEETING EACH GOAL

INSANELY SIMPLE PLAN THAT ANYONE CAN FOLLOW

ZEBRA LEARN

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LET'S BEGIN

Congratulations to us, we have made it this far! So far, we have gone through the creation of a lazy personal canvas, where we filled it as per our circumstances. We have then understood the different assets and insurances. Now, we are heading towards the third section of the set, where we will create a Lazy Financial Plan, exactly tailor-made to suit our situation and preferences.

Using the lazy canvas as a guide, we will match our decisions with the asset classes. to best create a financial plan that meets all our needs.

The Lazy Plan is for everybody. Once we have profiled ourselves properly, the Lazy Plan is relatively simple to create. All we have to do is not give up and follow it through. Lazy Plan is not a 6 month or 1-year exercise, but a lifelong journey. Consequently, we want it to be as simple as possible. Again, having a good plan that is followed consistently is in many ways better than having a great plan that is not followed.

It is important to recognize our objectives and at the same time understand the features of our Lazy Financial Plan, their functions and limitations.

THINGS TO KNOW

IT SHOULD BE LAZY

We will create our plan in a manner that will not need our constant attention and concern. We should be in a position to follow the same with minimum effort and a maximum of 2-3 hours per week. This is the primary objective of Lazy Financial Plan. We all have full-time jobs and are anyway always occupied, working super hard for the same. We do not want money management to become another task that demands 7-8 hours a week.

1

IT SHOULD BE SIMPLE

We will not complicate the Lazy Plan by adding too many assets or by buying assets that we do not understand. Simplicity is the key and it will help us stay in sync with our plan. The moment we make it complicated, it will no longer be lazy and as a result, sooner or later we will give up following the same.

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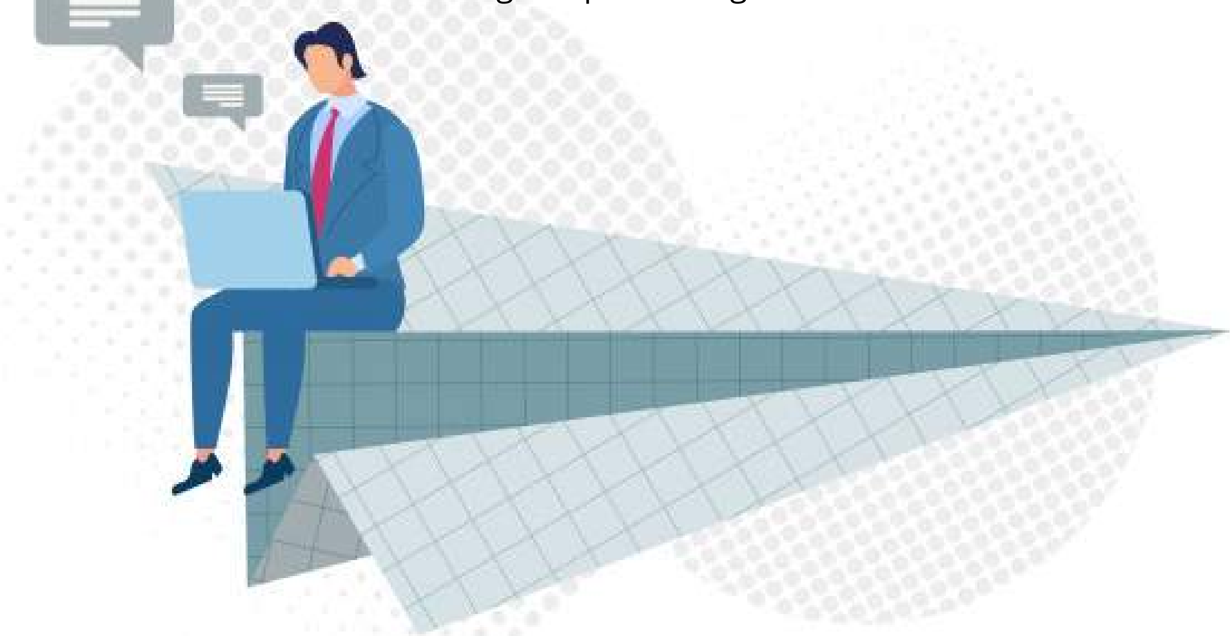


3 NO SHORT TERM TRADING

For our financial plan, we will not get involved in any short-term buying and selling of assets i.e. for benefit. We will not talk about buying shares today and selling them in 2-3 days, to expect a profit. This is because these short term activities cannot be relied upon to meet our goals. In case, we need assets for short term investments, we will deal with fixed deposits and money market mutual funds. We need to understand that such short term trading requires time and skill.

4 PRIMARY FOCUS IS MEETING GOALS

Whenever we are creating a Lazy Financial Plan, our primary focus will always be to meet our goals. It is not to have the lowest risk investment or to earn the highest return. In many cases, we will settle for a lower return asset class, if it helps us meet our goals more reliably.

5

ULTIMATE RISK IS NOT MEETING GOALS

Most people believe that the major risks they face relate to their assets and earning sources. This is what they need to control majorly. However, the ultimate risk is of not meeting the financial goals. During our financial journey, we may often see some risks materializing. For example, a theft at home or a fire at the factory. Despite all these, if we can meet the financial goals, then these risks just become similar to a stepping stone. The purpose is to meet financial goals. Failing to meet these goals is the ultimate risk. Do not get lost in managing the microelements (i.e. asset or income risks etc.) and lose the sight of the macro picture (i.e. financial goals).

IT WILL BE DYNAMIC

Understand that when we are creating a Financial Plan, we are not creating a 'still' plan but a 'dynamic' one which keeps on evolving with new information. At times, the plan could get drastically updated over events. We will always begin with the last version of our plan and make changes to it as per the new information.

6

7 WE WILL NEVER HAVE COMPLETE INFORMATION

We will never have all the information when we start creating our Financial Plan. Quantification of goals in terms of time and amount, risk-taking ability etc. is all guess-work. We will create a plan based on speculations and with time as things will become clearer, we will keep on updating the 'Dynamic' Lazy Financial Plan. If we wait for all information to be clear, we might end up being late.

This is a limitation of finance in general i.e. the art of taking decisions with limited information. As information becomes clear, the time to act on it is mostly gone. It is human nature to want things to be crystal clear and information to be right in front of us before we start anything since it makes us comfortable.

FOCUS ON VEHICLE & NOT DISTANCE

When we have limited information, we become handicapped in terms of exact speed and distance. Thus, our Lazy Plan will focus on direction and vehicle. It implies that our plan will allocate our resources to the suitable asset classes i.e. focus on the direction of the plan.

Speed refers to the rate of return. Distance refers to the profits in absolute term. If the direction is right and the asset classes are suitably selected, the speed and distance will take care of themselves.

8

9

SPEED NOT IN OUR HANDS

As we just discussed, the rate of return i.e. speed is not in our control. Market forces and a lot of external factors influence the same. So, we need to focus on vehicle and direction and the rest should take care of itself on its own.

10

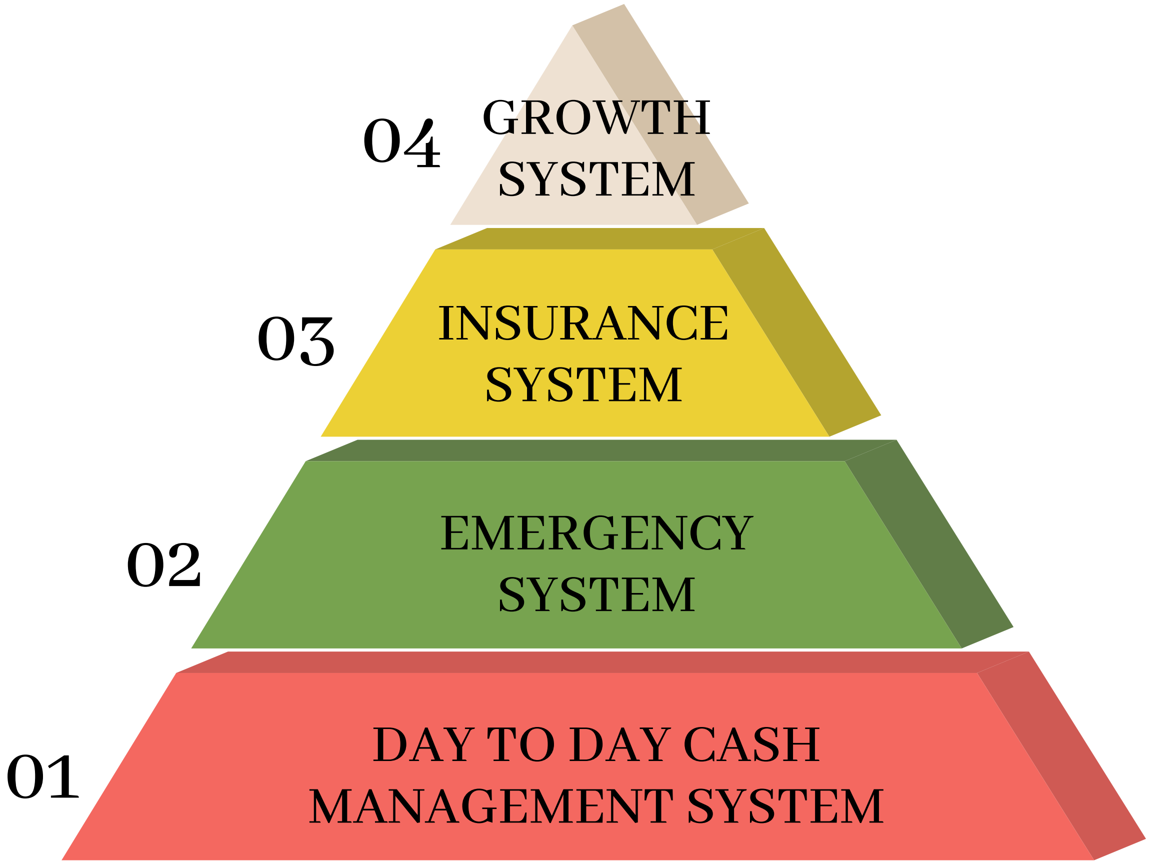
NO RIGHT ANSWERS

When creating Lazy Financial Plan, there are no right answers. This is simply because the information is limited and a lot of individual psychology and comfort is involved in creating the plan. Multiple assets and different combinations can be used to achieve the same objective. Until the goals are being met, one can follow any path.

11

DIFFERENT PEOPLE BEHAVE DIFFERENTLY & THAT'S OKAY

As we just saw, a lot of individual psychology, comfort and past experiences play a major role in the process. Not everybody will agree with the decisions we take or suggested by professionals and that is completely okay. Different people behave differently financially and till the time they are meeting their financial goals, it is all good.



BEGIN PLANNING

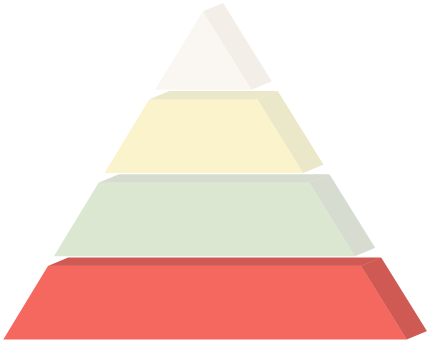
We learnt about the limitations and characteristics of the Lazy Financial Plan. Now we move on to see how it works.

The Lazy Financial Plan is structured in a way such that it can be divided into four tiers. Only after taking care of the lower tier, will we move to the next tier. This will ensure that we build a reliable system that is easy to follow through and is 'Lazy'. With all these tiers and systems in place, all different financial needs will be fulfilled. However, it is essential to plan for each of these tiers systematically.

We observed that several different financial need hierarchy pyramids are used in the personal money management industry. However, there is too much noise around them and at times it gets difficult for an individual to understand which part of the pyramid they are dealing with.

The Lazy Plan is a simplified version of such financial pyramids. A pyramid based approach works best as they are more intuitive and we can have a better understanding of the rolling out of our plan.

Let us take a look at various financial pyramids that are currently used in the money management industry.

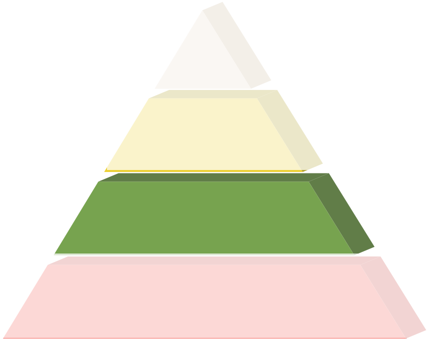


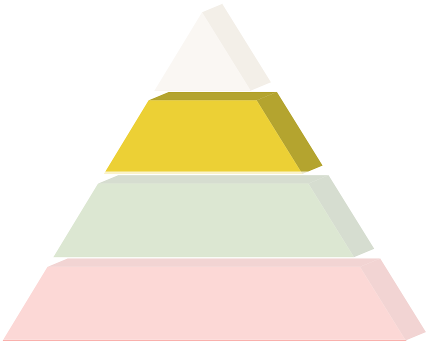
1) DAY TO DAY MANAGEMENT

This is the first step. We will have adequate accounts to make sure that the day to day cash is well managed and efficiently used to meet our daily financial needs and at the same time, have a working system that directs money towards our investments.

2) EMERGENCY SYSTEM

In the second tier, focus on setting up an emergency system that will take care to meet the emergency expenses. We will focus on the efficiency of our Lazy Plan to absorb emergencies and financial requirements that come up un-anticipated.



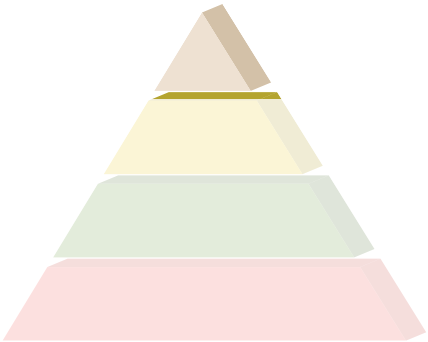


3) INSURANCE SYSTEM

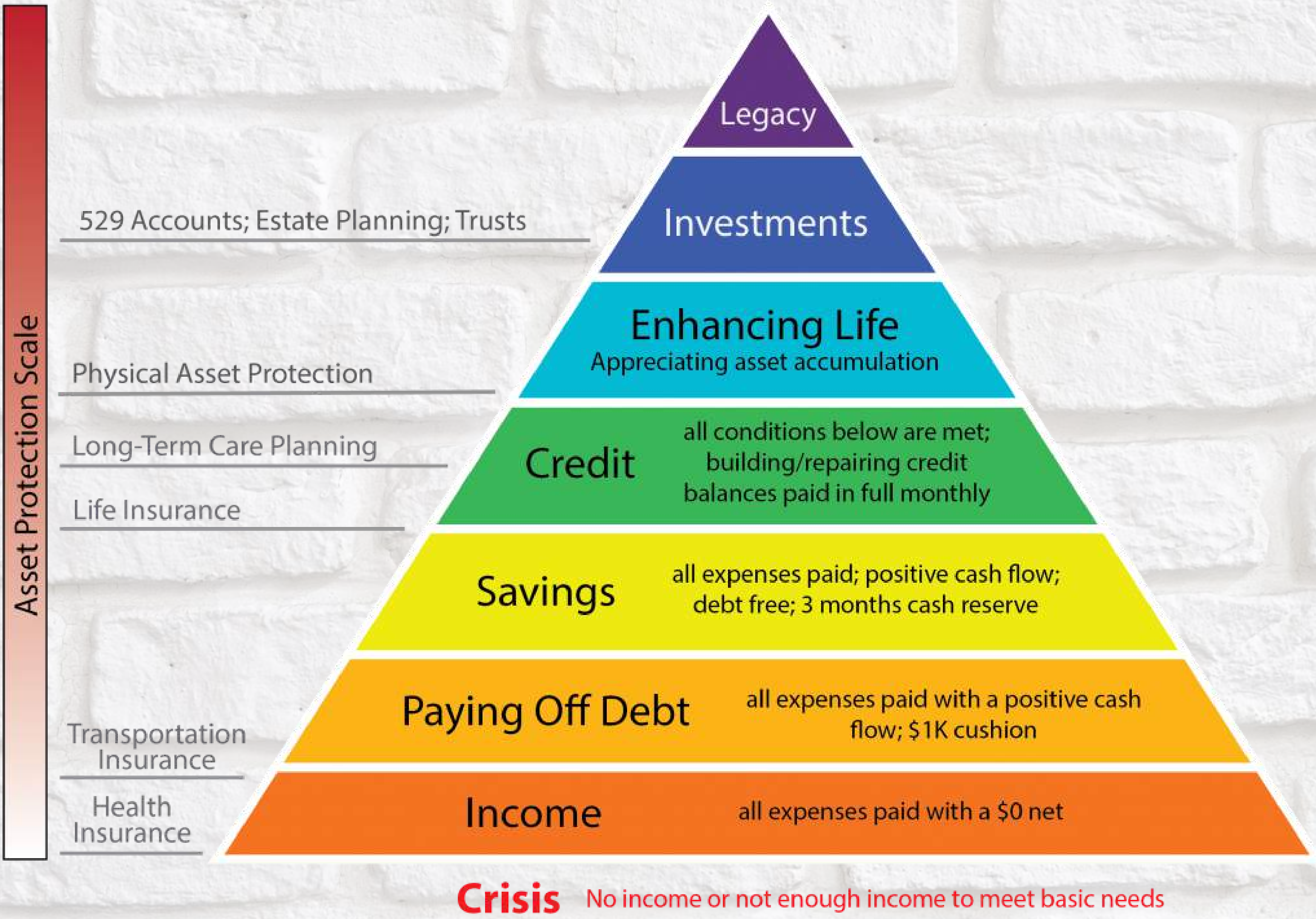
The third tier focuses on the insurance system if the plan is leakage proof, and it's an emergency system. We will manage all those risks that have a low possibility but high impact on occurrence.

4) GROWTH SYSTEM

This is the last tier that we will move on to once all other tiers have been taken care of. Here, we focus on reducing our liabilities and increasing our assets. All of this will help us meet our financial goals. The general growth of the portfolio is also a part of this stage.



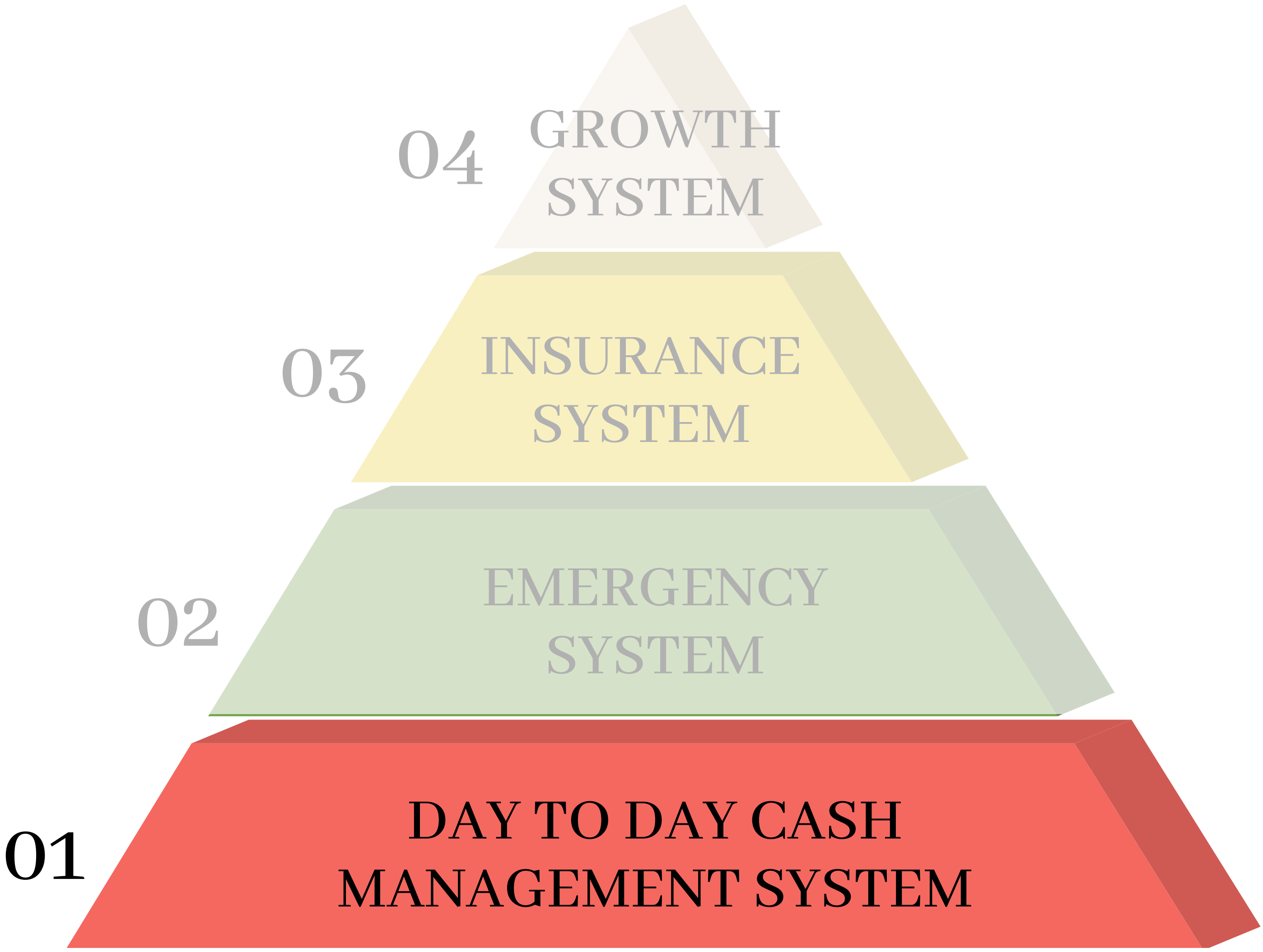
So we see that each tier has a specific role in the Lazy Financial Plan. When we have a working system after planning for each tier, we will end up with a robust financial plan where all our financial needs are automatically managed. We will try to reduce the active effort required for each paycheck. We will make it an automatic process where the money is invested systematically and not in an ad-hoc manner.



Source – Anonymous

Source – www.financialhighway.com

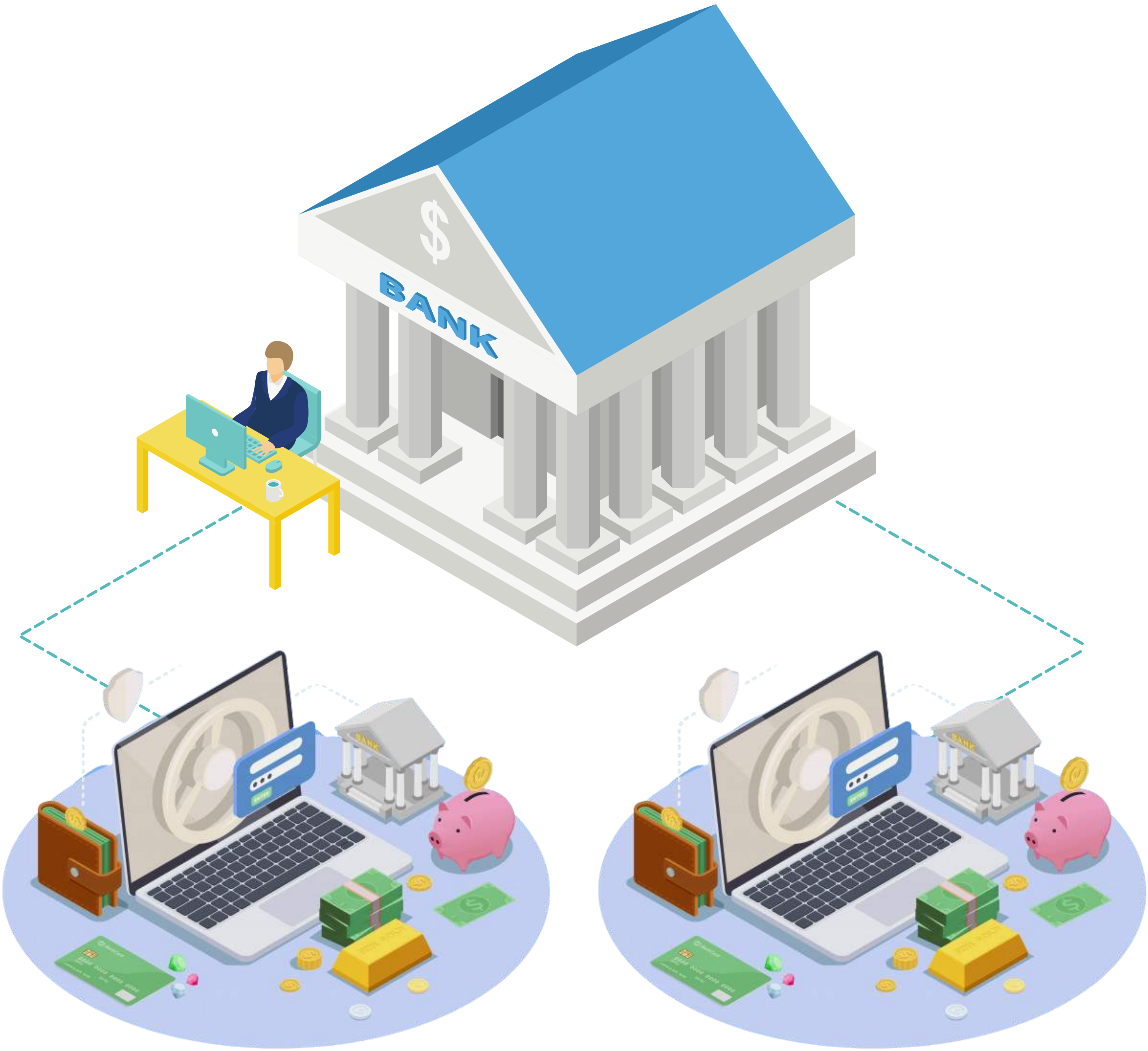
Source – www.moneyunder30.com



Let us begin with the first tier i.e. to have a cash flow management system in place. A healthy cashflow practice is the key to a healthy financial plan. This is because the cash flow system is the only way through which new money comes into the financial plan. So, how it is channelized, spent or invested, plays a very critical role in the long term health of the financial plan. Cash flow management system includes receiving income and allocating it to expense and investment purposes.

All our expenses like grocery, education, healthcare, utilities, maintenance, EMI payments, leisure, travel etc. will be taken care of here. It is a systematic approach through which all our expenses and short term liabilities are met.

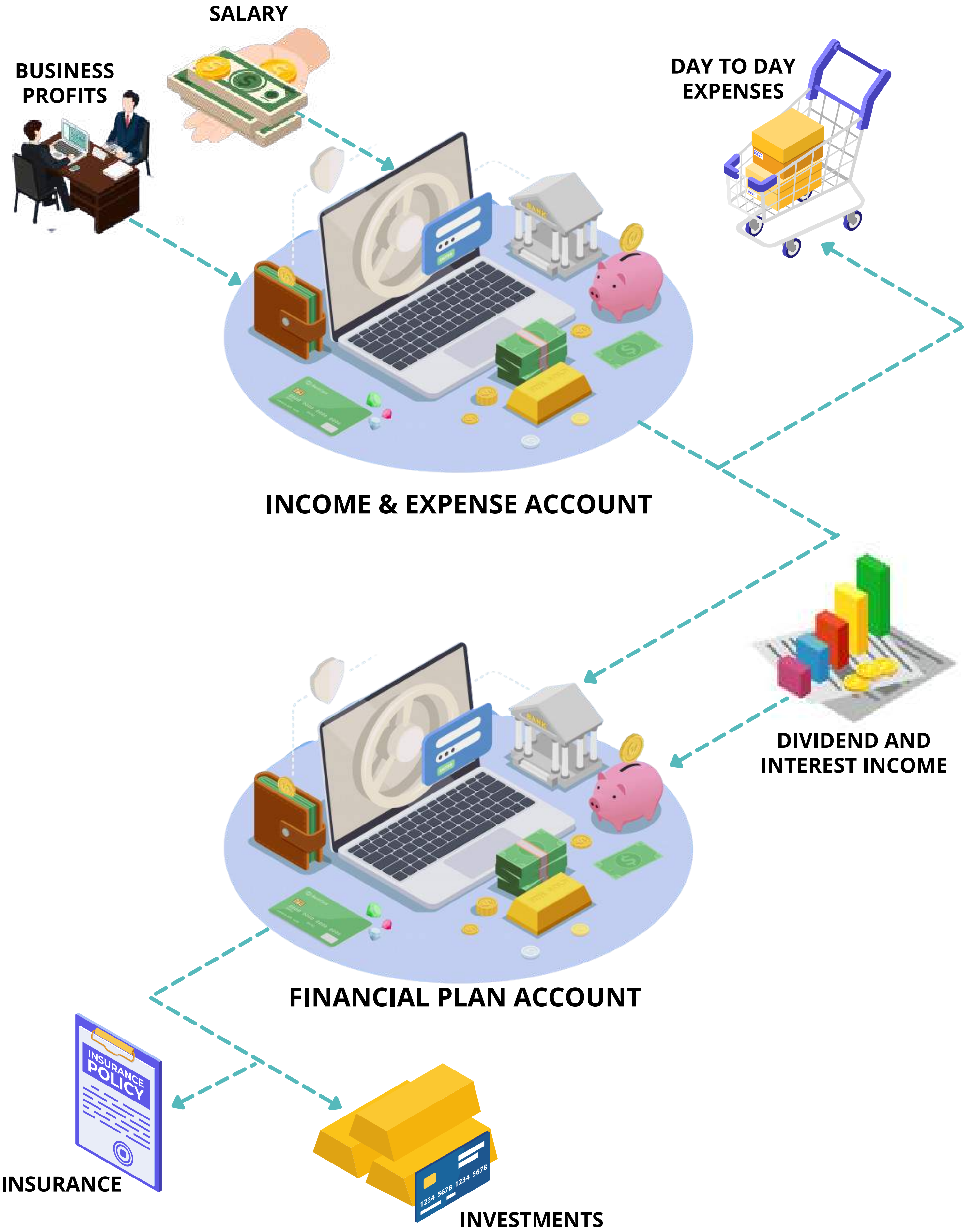
First, we need to have two bank accounts to carry out our transactions. People generally carry out all their transactions from one bank account. We will receive our incomes and pay our bills through the first account. We will call it 'Income and Expense Account'. The second account will manage our investments and insurances for our Financial Plan. We will call the second one 'Financial Plan Account'.



INCOME & EXPENSE ACCOUNT **FINANCIAL PLAN ACCOUNT**

This is how it will work: we will first receive all the money i.e. salary, profits etc. in our ‘Income and Expense Account’. Then we will segregate it between expenses and investments. The expenses piece will remain in the account, and everything else will be moved to the ‘Financial Plan Account’.

The shift should be automatic i.e. we must set on a fixed part of our salary that will be required for regular day to day expenses and the rest will be shifted towards the financial plan. We will not allow ourselves to change the amount every month at our convenience.


SALARY
BUSINESS PROFITS
DAY TO DAY EXPENSES
INCOME & EXPENSE ACCOUNT
DIVIDEND AND INTEREST INCOME
FINANCIAL PLAN ACCOUNT
INSURANCE POLICY
INSURANCE
INVESTMENTS

The first account is the one with the debit card and all other banking facilities. This account will typically hold large amounts only when we receive income. It will have one large transaction every month (when money is shifted to the other account)and various small transactions (relating to expenses). On the other hand, the financial plan account will only have one major income and a few investment transactions.

We will have to be wary of missing the two accounts as this will create a lot of confusion and reduce the differentiation between expenses and investments. The financial plan account should be clean and only have transactions related to insurance and investments. This account will always hold larger balances, will be linked to our trading and broker accounts and therefore, we will not share the details of this account with anyone, not link this account to digital wallets, smart cards, and other unnecessary services, thus reducing its exposure to cybercrimes.

All the dividends and interest should be received in the financial plan account. Also, note that the flow of money from income and expenses account to financial plan will be a one-way flow i.e. money will not come back to income and expenses account, unless and until we have a major financial goal coming up or we live off our assets, i.e. during retirement. All other accounts that we might have i.e. business accounts, family member accounts etc. are all other than these two accounts.

This process might sound simple, but it requires people to get organized and change their financial habits. It will take us a few months to adopt this, but it is completely worth it.

INCOME AND EXPENSE ACCOUNT

FINANCIAL PLAN ACCOUNT

The most demanding part is determining the amount of money that will be retained in the income and spending account and the amount that will move towards financial plan account. In the income and spending account, we will retain an amount that will last us till the next paycheck or inflow of capital. If we are a seasonal business, we will retain 6 months worth of expenses in this and shift the rest to financial plan account. We will refrain from retaining surplus money in the income and spending account and spend the entire amount retained. . What we won’t need expenses currently will be dealt with in the financial plan account so that it can be put to best use as per the lazy financial canvas.

We will not go on a strict saving diet when it comes to day to day expenses. Many people fall into this trap to move more money towards long term investments. It is a very mis-advertised concept and after some time it becomes unsustainable. We work hard and we have to maintain a basic lifestyle. We want to buy a few expensive things and more than that enjoy our lives. We do not want to kill every small happiness in life due to a financial plan.

However, this does not imply that we become irrational about our expenses and start spending on things that ruin the entire Lazy Financial Plan. We need to strike a balance between the two so that our goals are met while keeping it sustainable.

STRIKE A BALANCE BETWEEN FULFILLING CURRENT LIFESTYLE NEEDS & ACHIEVEING FUTURE FINANCIAL GOALS

We will always open these accounts with a public bank or a large private bank i.e. Kotak bank, HDFC Bank, ICICI Bank etc. We will avoid smaller private banks, co-operative banks, regional banks etc. This is because smaller private banks and co-operative banks come with a lot of credit risk and there are distant chances that something untoward may happen to them over the years. The government would not let the large private banks or public banks fail even if they face problems.

Secondly, we will attempt to get a zero balance account since we do not want our money to be stuck in the bank account to maintain the basic requirements of the banks and it is much less a hassle. This will take away some of the benefits that the bank offers.

When we have all these systems in place, most of our day to day activities will become automatic. Money comes in, automatically a part of it is retained and the rest is transferred to the financial plan account.

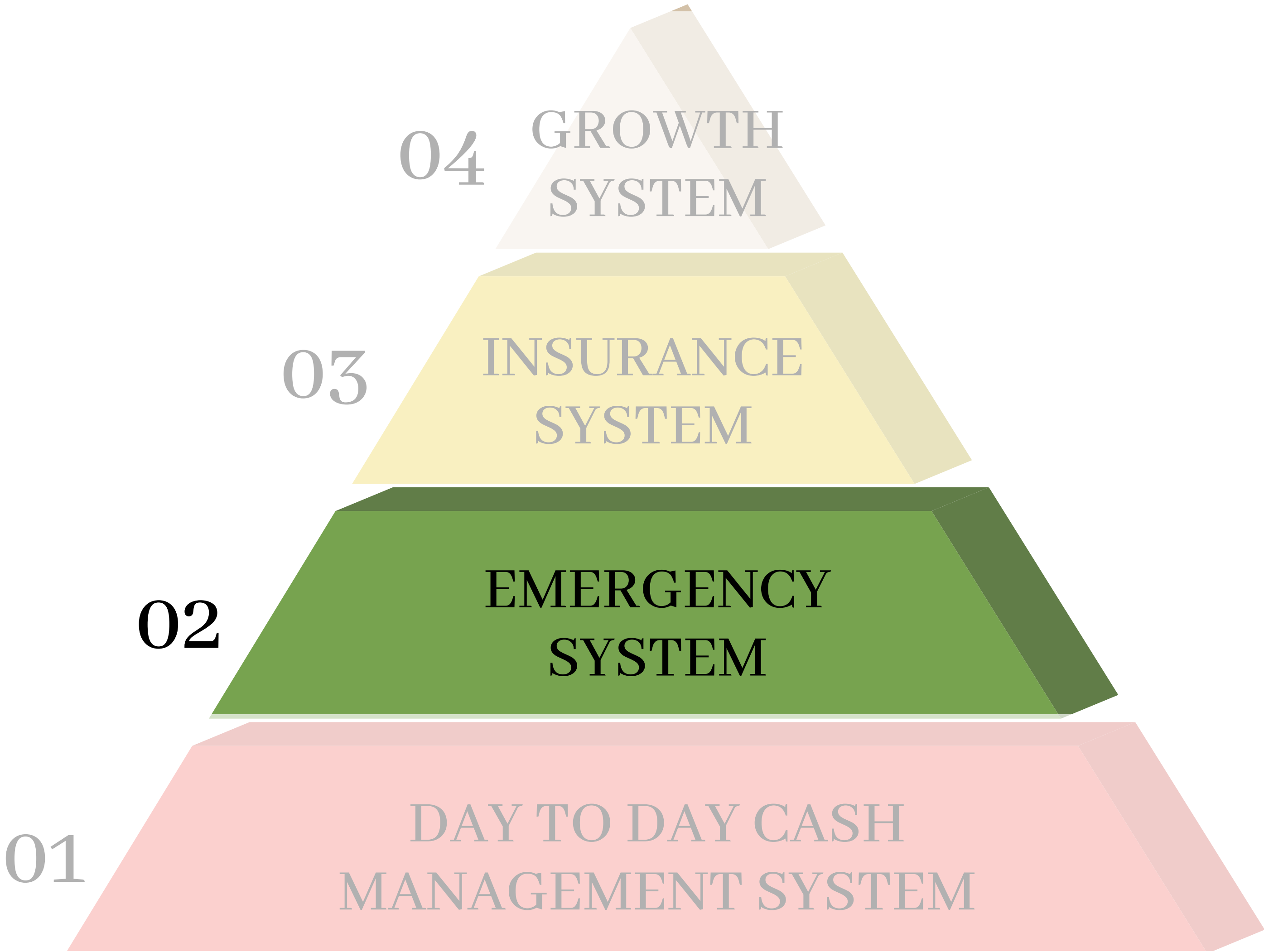
For those who majorly depend on assets, they can transfer money back from financial plan account to the income and spending account. They will shift a month's worth of expenses every month to the income and spending account and the rest remains the same.

For those who earn and spend in cash majorly, should have two different cash bags to monitor the plan. One bag is the income and spending bag where all the new money comes in and the second one is the financial plan bag. The two work the same as the bank accounts.

Without two banks accounts, keeping a track of bank transactions mentally leads to errors. People often end up spending more than they should. It becomes difficult to stay disciplined when we have a debit card linked to the account. Moreover, it becomes hard to keep the investments and expenses separate. Having two accounts is a sustainable idea.

With this, we have created a fully functioning cash flow system that effectively manages the day to day expenses and have a systematic inflow to investments as well. We have created two separate bank accounts, segregated spending money with investing money. We have fixated on an amount that will be retained in the income and spending account and the amount to be shifted to the financial plan account systematically. This way all our day to day finances, spending and investments will be in check and will be in line to meet our financial goals.

This is the easiest of the four tiers. Creating a system takes no time. However, getting used to the changes and changing financial habits may take up to a few months. Once we have taken care of this tier, we will move to the next tier – emergency system.

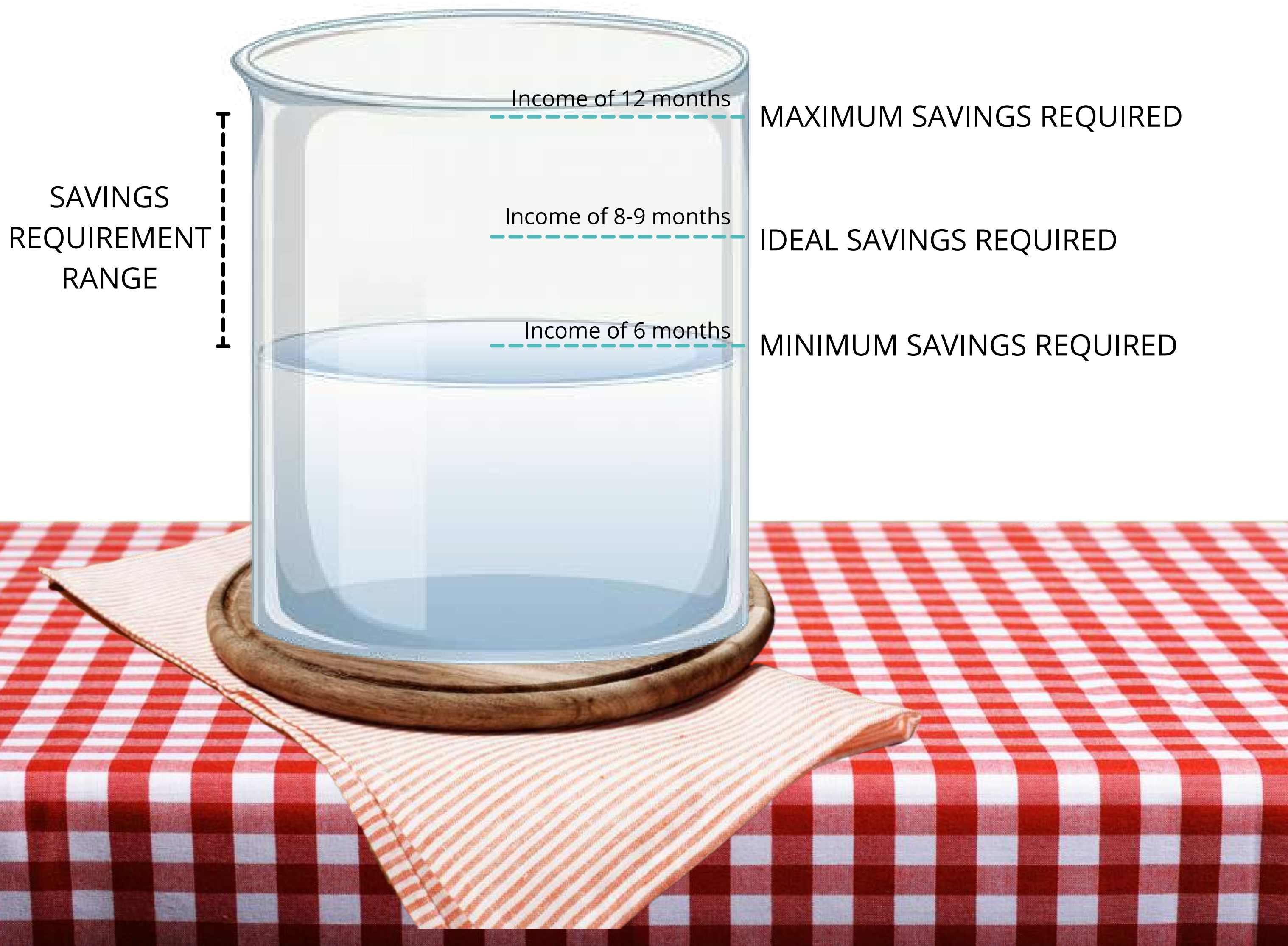


The objective is to be prepared to meet any expense or liability arising due to an emergency and navigating smoothly through such periods of difficulty. This adds buffer space to our Financial Plan that if things do not work well for us for a while, we will be in a position to take care of ourselves financially.

We need 8-9 months' worth of income in our emergency fund. So, if we earn Rs. 20,000 p.m., we will need Rs. 1,60,000 in our emergency fund. At the maximum, we can have up to 12x our monthly earning i.e. a year worth of earning. On the lower end, we need to have at least 6x our monthly earning i.e. half year worth of earning in the emergency fund.

Often people put a lot more in the emergency funds than needed. This gives them a sense of safety. We need to understand that our aim is to be prepared for emergencies and not to raise the money. A year worth of income is more than enough to be prepared for emergencies. Beyond that, we are simply wasting money and not putting it to efficient use.

The importance of emergency funds has been well established in the recent turn of events with the pandemic and poor economic circumstances. The emergency system gives great strength to navigate through hard times. And we can also realize how a year worth of income would have been enough to navigate through the hardest of times where the whole world went upside down. So, there is no point in having anything more than this in the emergency system.



Money in the emergency system needs to be readily available and hence should be in liquid assets. We will not buy real estate or equity with the emergency funds. We will consider floating rate fund category and liquid funds category of mutual funds. Apart from these, we can also opt for regular bank fixed deposits.

FLOATING RATE FUNDS

Floating rate funds are those where the money is invested in fixed income assets, whose interest rate is not fixed i.e. it returns the market interest rate. It is called floating because the interest rate keeps changing as per the market.

LIQUID FUNDS

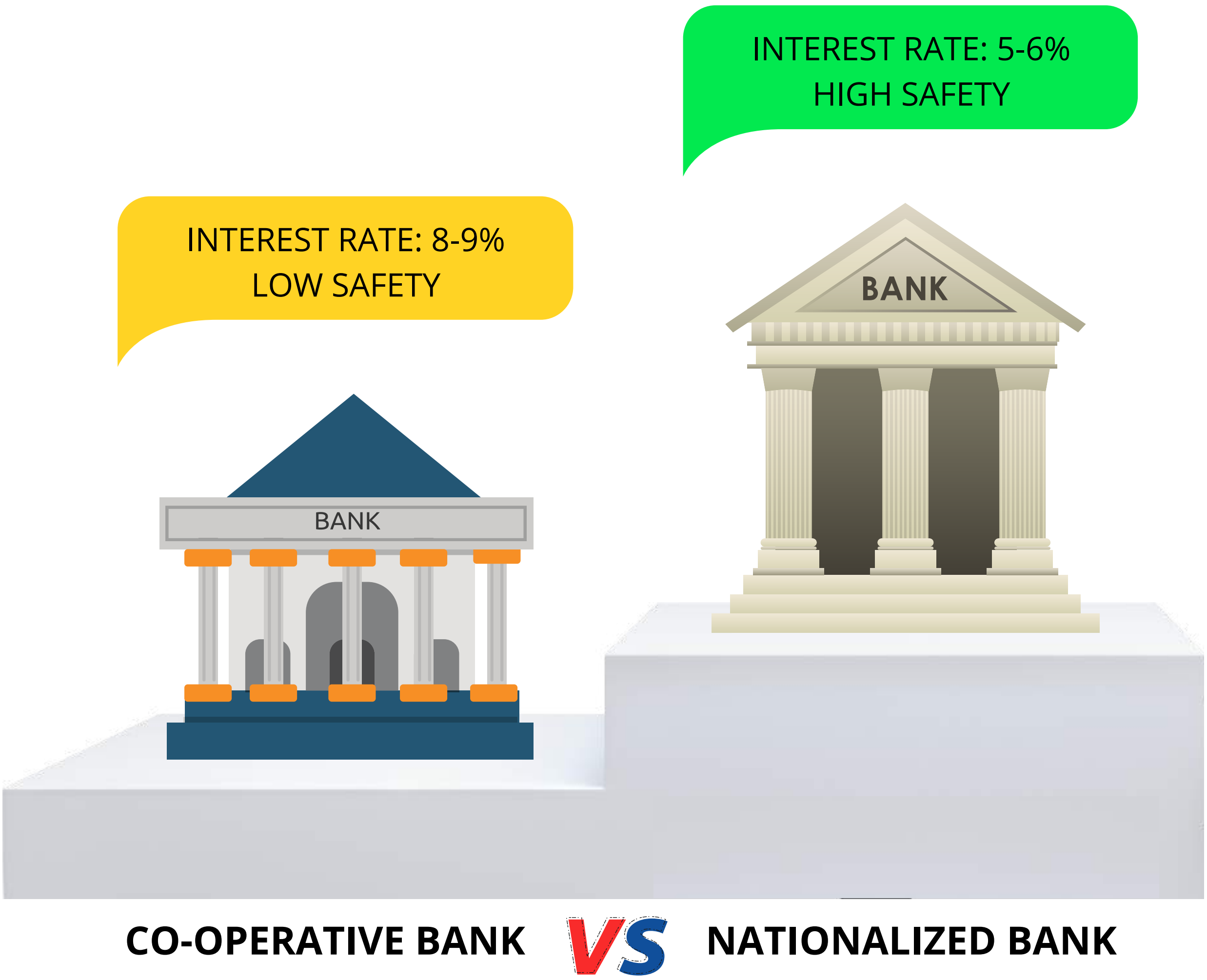
These are those where money is invested for short term and price is not too variable . We can also invest in money market category of mutual funds.

FIXED DEPOSITS

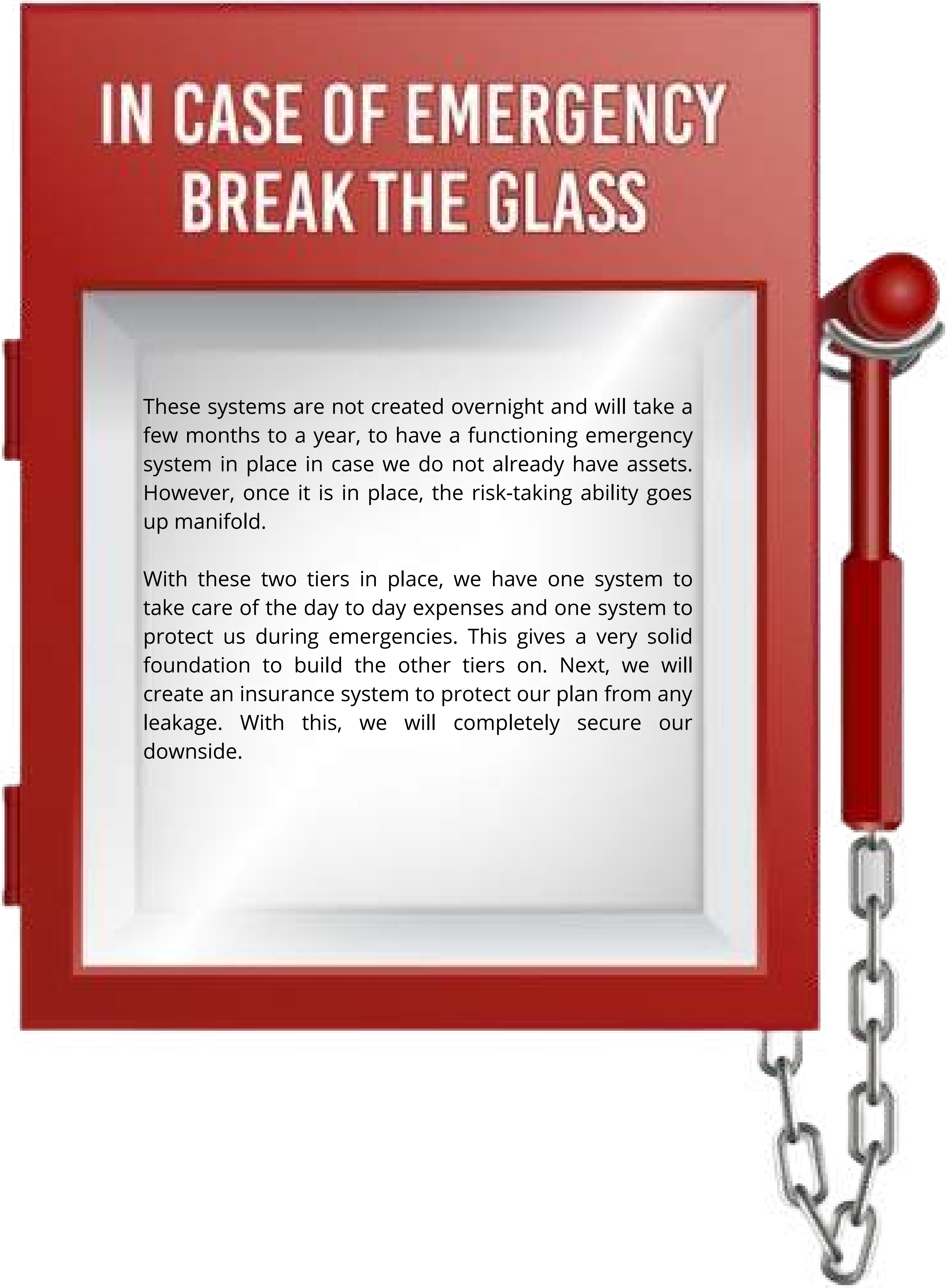
Fixed deposits are maintained with banks. They offer low returns but they are suitable for the purpose. They can also be withdrawn with a penalty.

All of them have similar characteristics and each of them can meet our requirements for the emergency system. So, we can go ahead with either one or a combination of more than one of these assets according to our convenience.

With the emergency fund asset selection, our focus is not on returns. The focus is on the safety of capital and liquidity of the asset. It should be completely risk-free and we should be able to access the same whenever need be. If given two assets, one earning 8% p.a. and another earning 6% p.a., but the latter is more stable, secure and liquid than the former, we will choose the latter.

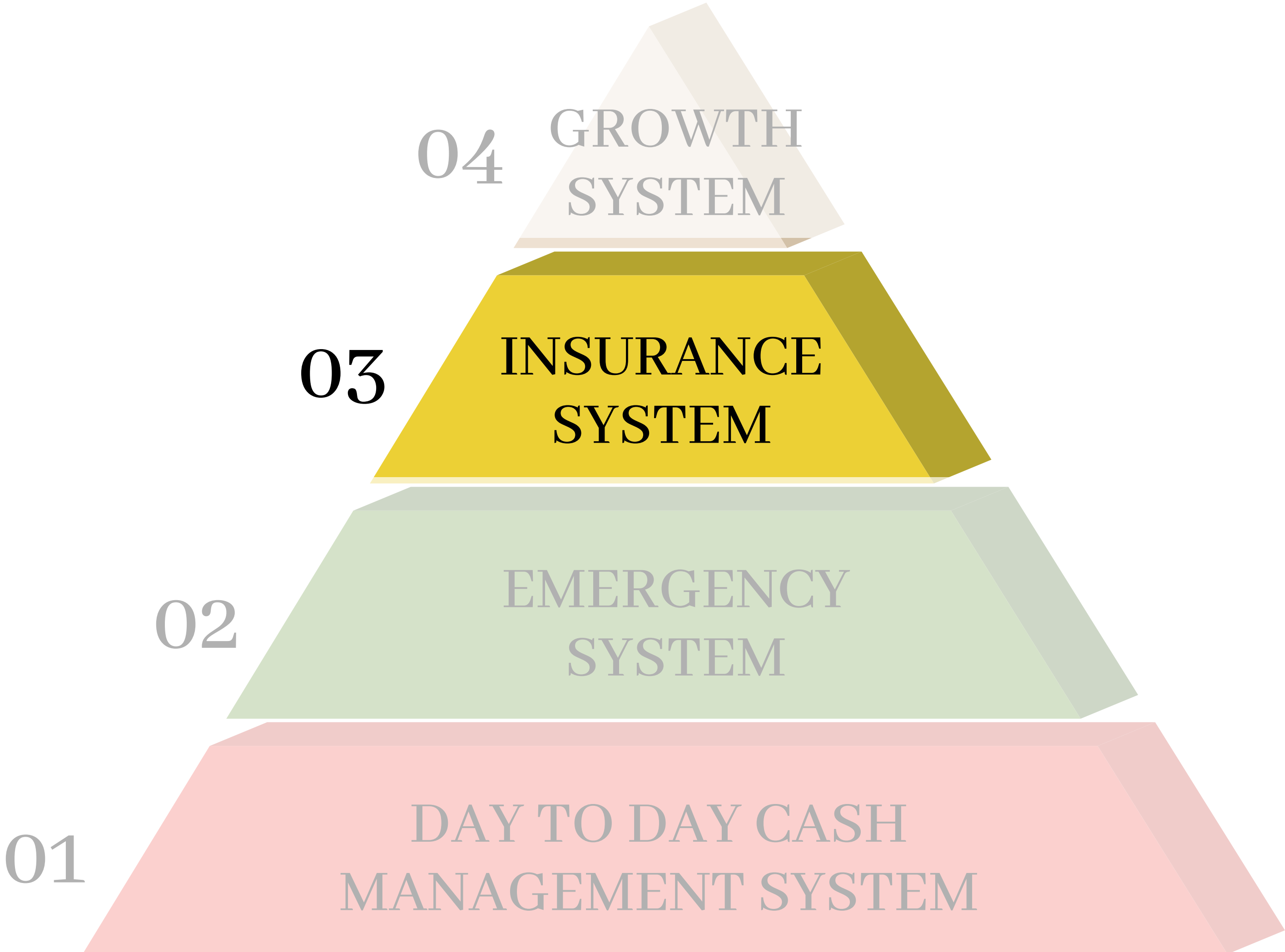


For those who begin with this early on in their career, they will begin with 8-9x times of their income. But as their income increases, the amount required in the emergency system will also keep on increasing and as a result, they will keep making additional contributions to maintain 8-9x of their increased income in emergency funds. 8-9 months of income can sustain us for 12-16 months in terms of expenses. That should be enough time for us to mitigate through the emergency.



These systems are not created overnight and will take a few months to a year, to have a functioning emergency system in place in case we do not already have assets. However, once it is in place, the risk-taking ability goes up manifold.

With these two tiers in place, we have one system to take care of the day to day expenses and one system to protect us during emergencies. This gives a very solid foundation to build the other tiers on. Next, we will create an insurance system to protect our plan from any leakage. With this, we will completely secure our downside.



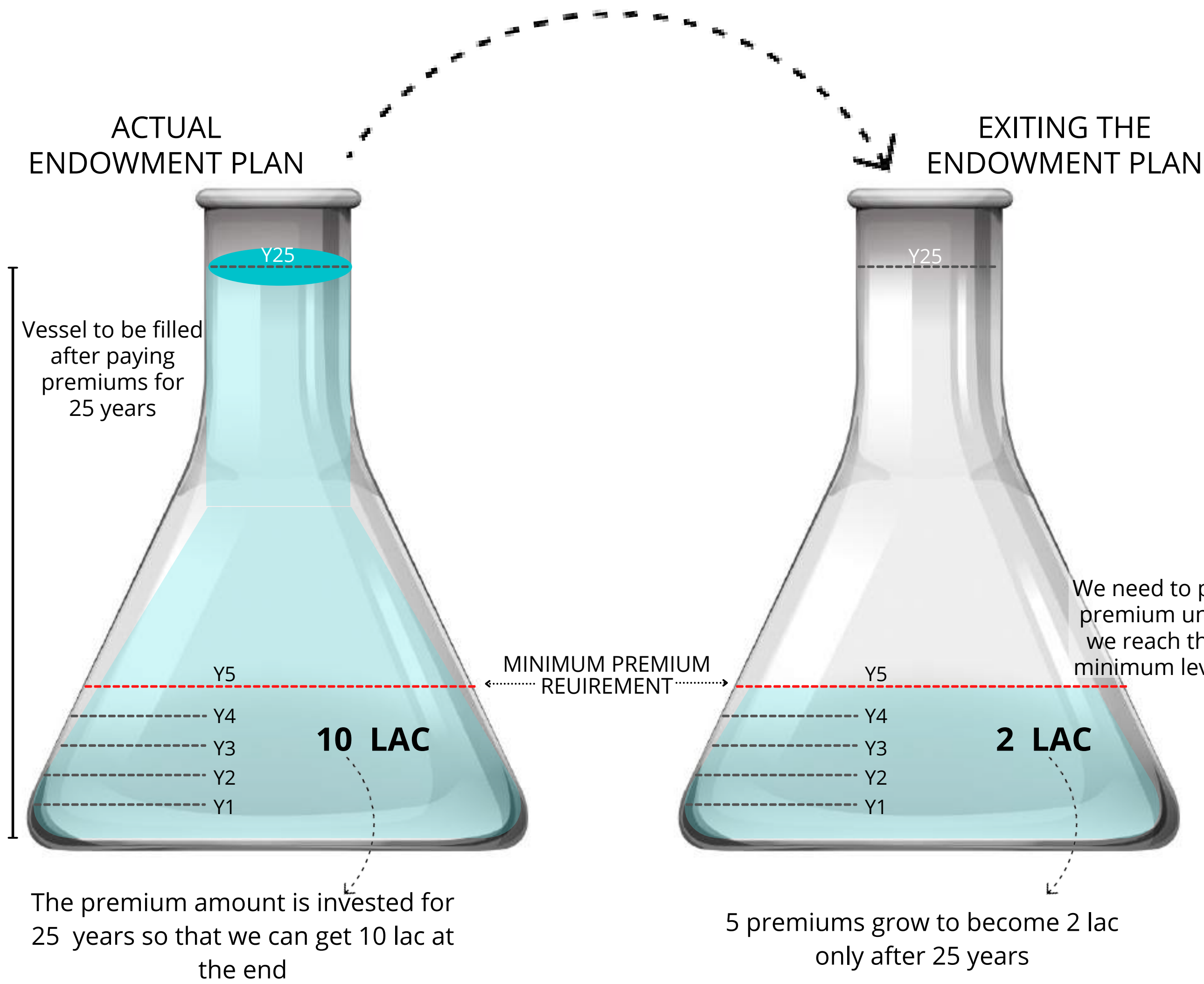
Once we have created the first two tiers, we will move onto the insurance system. This system will safeguard our Financial Plan from leakage i.e. no single event should ruin years of effort and our financial plan. We will create the insurance system from the Financial Plan bank account.

We are already familiar with insurances and their functioning. We will purchase all the required insurances as per our lazy financial canvas and make sure that all these insurances are for an adequate amount. This way we will create a robust system for ourselves that makes sure that there is no leakage in the financial plan. Also, we will be certain to not mix investment and insurance and we already know why this is beneficial.

With the lazy plan, we will get the right kind of insurances and the right amount of coverage as per our requirements. We have already discussed everything that is required to create a robust Insurance System. Put all that we have discussed in the previous sections together and we shall have a robust and functioning Insurance System in place. We will make sure that we do not mix investment and insurance. We will keep the two separate in each kind of insurance. We have already discussed in great detail why this is the case.

We will buy term plans and not endowment plans that have an investment element. Now, what if someone has an ongoing endowment plan. In such scenarios, the person can shift to a term plan going ahead. This will take a little bit of effort, but it sure is worth it. They need to visit the insurance company where the endowment plan is ongoing and understand the redemption policy and the discontinuation policy i.e.under what circumstances can they redeem the endowment plan investments and what happens to their money in case they discontinue the policy and stop paying premiums.

Generally, according to the ' Redemption Policy and the Discontinuation Policy', on paying a minimum number of premiums towards the endowment plan (for example, at least 5-year premiums for a 25-year plan), we do not have to pay the remaining premiums; a pro-rata (proportional) amount of the maturity lump-sum is paid back to us on maturity. For instance, a plan required us to pay Rs. 10,000 per year for 25 years and in return it promises to pay Rs. 10 lac at maturity. If we pay the premium for the first 5 years (1/5th of total premium payments) and then discontinued, we will get Rs. 2 lacs (1/5th of maturity lump-sum i.e. Rs 10 lac) as lump-sum at the end of the 25th year. This means we will get back the investment component of the premiums that we have paid along with the interest earned on it.



After reaching the minimum level, we will discontinue premium payments & start with the Term Plan. At the maturity ie after 25 years, we will get a lump sum payment of 2 lac for the 5 premiums we had paid.

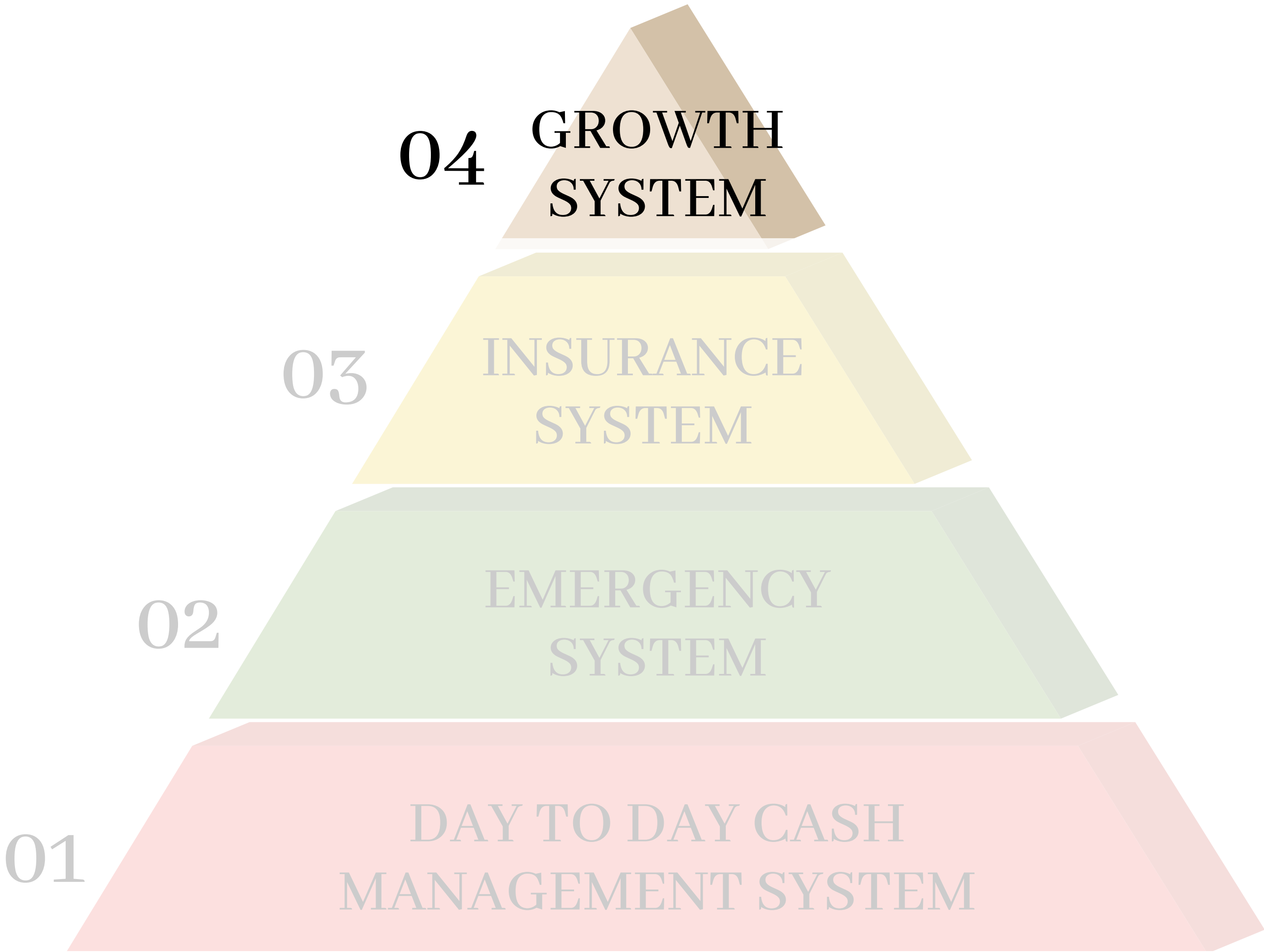
So, we should pay the minimum number of premiums towards endowment plan so that we get our money back on maturity and then buy a term plan going ahead. The premium of an endowment plan is much more than a term plan for the same sum insured. So we will buy a term plan, which will be available for a much lower premium. The rest amount can be invested as per our growth plan. This way we get the best of both worlds, adequate sum insured from the insurance component and better returns from the investment component.

So, this is how someone with an ongoing endowment plan can switch to a term plan. Under all circumstances, people should keep their investments and insurances separate. If we merge them, we get lower protection on the insurance end and lower return on the investment component.

We will make sure that we are neither over-insured nor under-insured and have health insurance, life insurance, accident cover, property insurance and all other forms of insurance required in adequate amount. We will make it a point to never cut on the sum-insured to save some money in premiums. When the risk strikes, these prove to be very costly.

Sometimes people are curious to learn the need for individual health insurance even after having company health insurance and whether the latter covers the entire family too. If it covers all of our dependents, then we can let go of the individual insurance and count on the benefits provided by the company. Else, we will have to get an insurance cover for those not covered. We also need to understand that when we switch jobs or are unemployed for a while, we will not have any insurance Cover: Also, when we retire, we will have to buy health insurance at a more expensive price. We need to acknowledge these two limitations of company-sponsored health insurance, After accepting these two limitations, one can stick to company-sponsored health insurance and change to personal health insurance later on in life.

Putting all the pieces of this system may take up to a couple of years for some. But once such a system is in place, it is really easy to follow up since all the ratios are fixed. We need to automatically contribute to the different systems as our income increases to maintain the ratios. This way we will have created a plan that is automatic and is for the ‘Lazy’ With this, we have created the first three tiers of the Lazy Financial Plan. Now, let us move forward to the last tier where we focus on the growth of the portfolio.



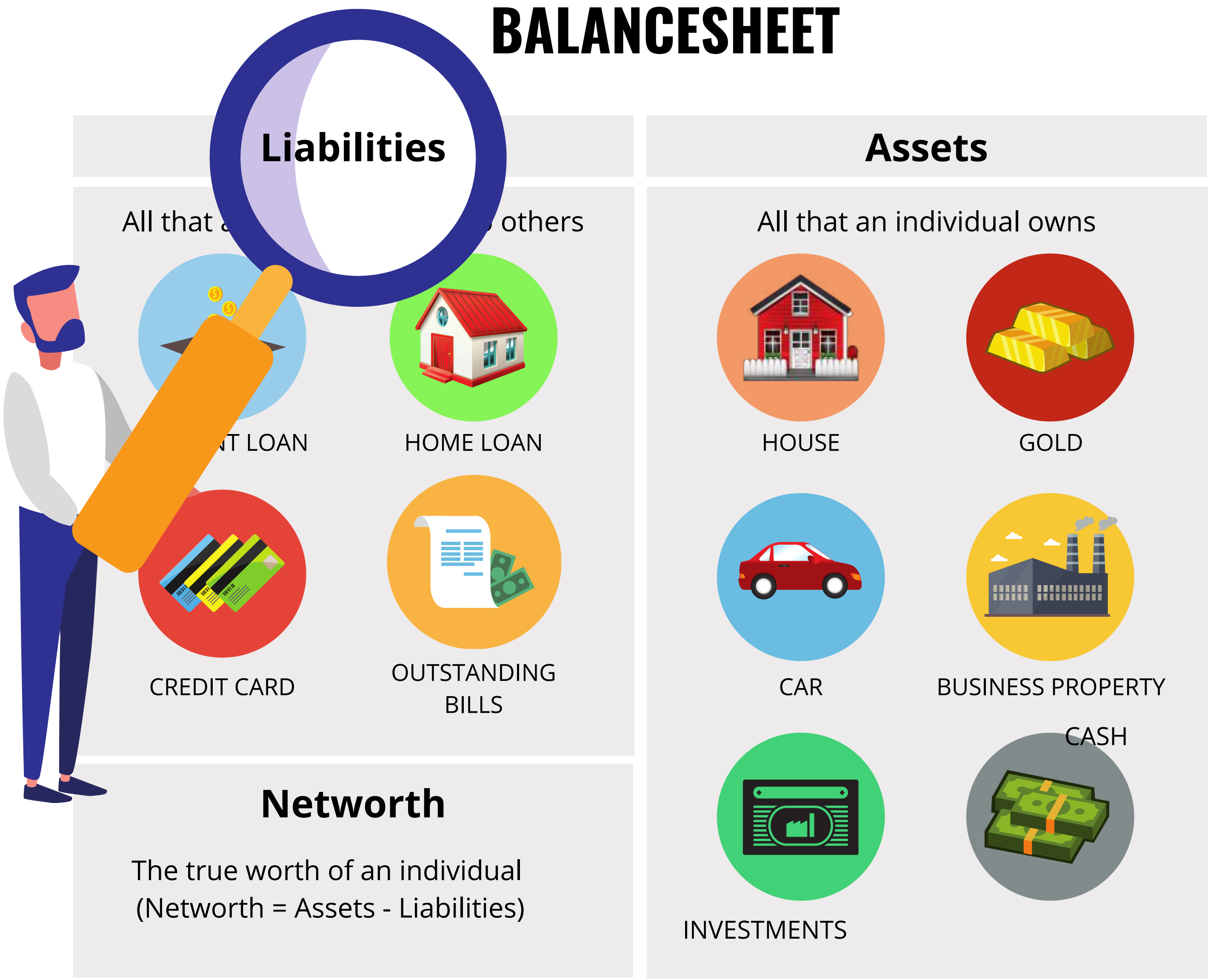
So far we have managed our day to day expenses, emergency needs and lastly, our insurance needs. Going ahead we will learn to manage our assets and liabilities so that they are in the best position to help us meet our financial goals. We have taken care of the short term factors and protected our downside so far. As we move on, we will take care of the long term planning and focus on our upside. We know that getting to this stage may take up to 1-2 years for individuals. If someone has surplus assets, then it can be done faster.

It will take a few months to get Cashflow Management system and practice in place, followed by time to accumulate Emergency Fund. Once that is done, buying insurances will again take a few months and only then do we reach this stage. So someone starting to follow this today, should be fine if they reach this stage in first 2 years.

In the growth stage, we plan for assets and liabilities over the long term. A common mistake is to begin the growth stage with assets when it should be started with the liability side.

Coming to liability management or debt management, we will not focus on paying off the liability completely, but on guaranteeing the liabilities are in control. We will make it a point to ensure that the liabilities will be paid off systematically.

and we will be in a position to allocate money to our investments so that we can meet our financial goals. We cannot be allocating resources towards building assets if our liabilities are not in control.



MANAGING LIABILITIES

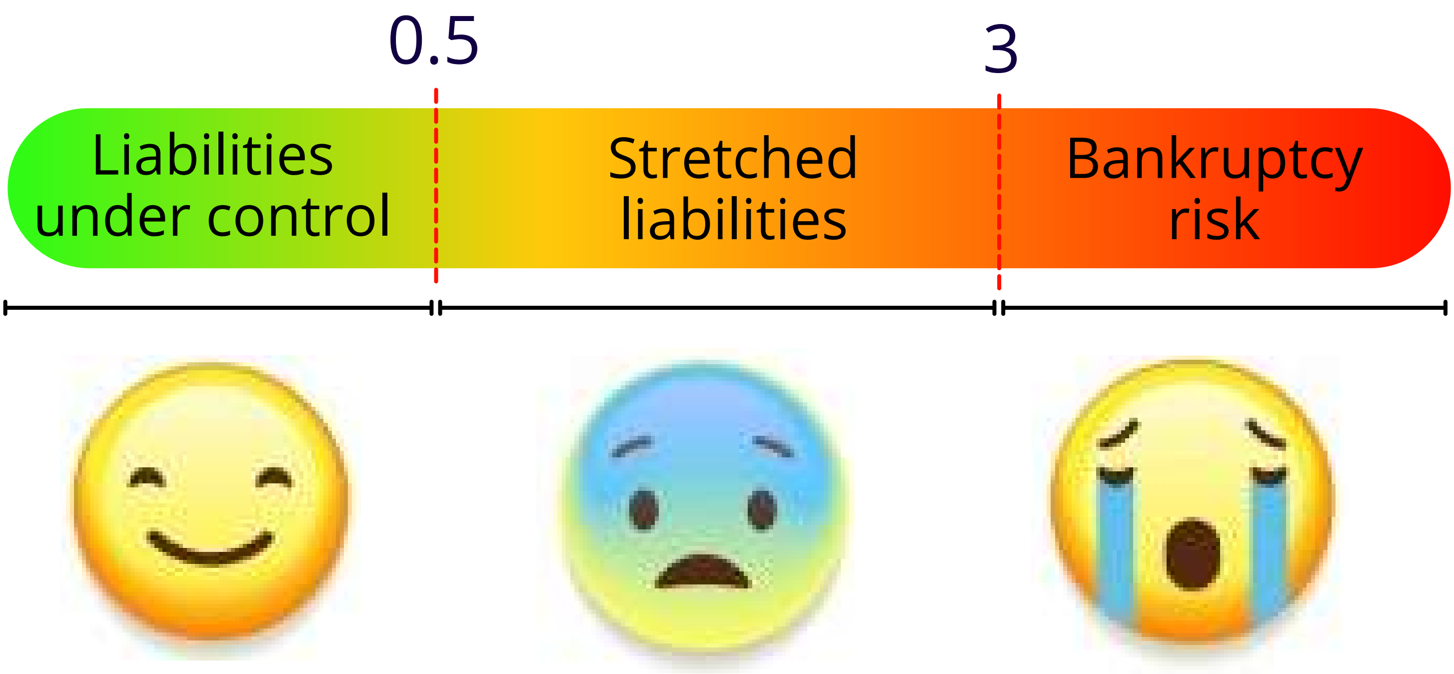
Previously, we had conducted two checks for our solvency. We will assume that our EMI coverage ratio is more than 1.25 and our liabilities to net worth ratio is less than 3. If not, we need to stop moving forward and visit an expert right away, we might be facing a bankruptcy risk. We will only tread on if our debt is in control.

	SHOULD BE
$$\text{EMI COVERAGE RATIO} = \frac{\text{SURPLUS BEFORE EMI}}{\text{EMI}}$$	MORE THAN **1.25**
$$\text{LIABILITY TO NET WORTH RATIO} = \frac{\text{TOTAL LIABILITIES}}{\text{NET WORTH}}$$	LESS THAN **3**

LIABILITIES TO NET WORTH RATIO

However, this does not necessarily mean that our liabilities are in order. Our liabilities could still be stretched even if we are not facing bankruptcy risks. So, we will first get our liabilities under control and keep the liabilities to net worth less than 0.5. However, if it is more than 0.5 but less than 3, we can say that we are not facing any bankruptcy risk but our liabilities are stretched. We will stop to make sure that our liabilities are in order and are getting systematically paid.

Our focus will remain on the liability side till the time we get our liabilities to net worth ratio reduced to 0.5. After that, we can start focusing on the assets. Once the ratio falls to 0, then our full-fledged focus shifts to the asset side. This is when we will start investing aggressively. We will never use debt as an excuse to not have and follow a Lazy Financial Plan. Debt is very much a part of the Lazy Financial Plan.

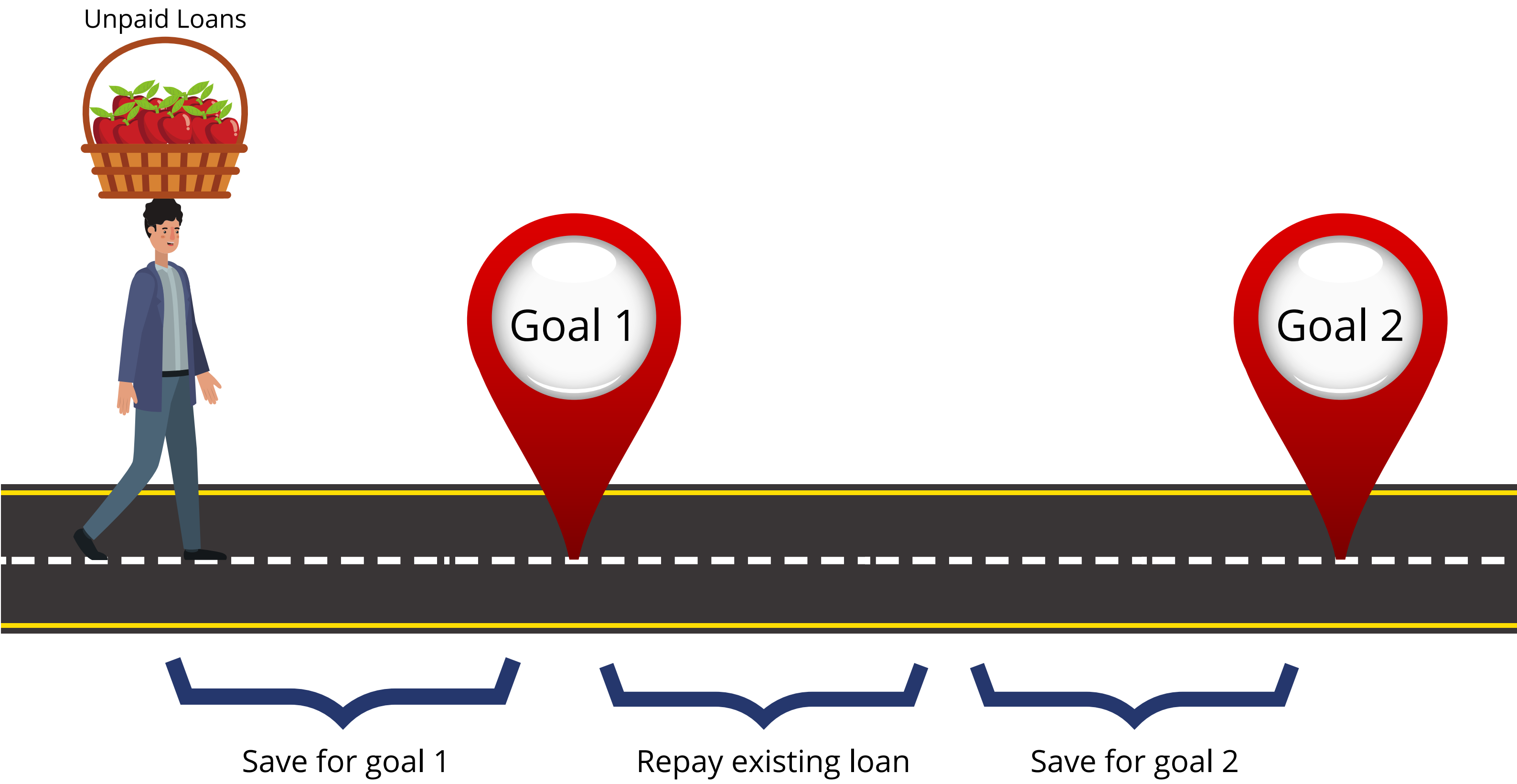


CREATING A TIMELINE FOR LIABILITIES

Often while we are focused on repaying the liabilities exclusively, we might see a major financial goal coming up. In that case, we will not be in a position to meet that goal. Hence, we will go back to the timeline that we had created in the lazy canvas. We will fix slots on the timeline where we want to focus on the goal and the slots where we intend to cut off on the debt. For instance, let us say we have a child's marriage coming up in 2 years and we also need to get our debt in order. So, for the next two years, the marriage becomes our focus financially. Once the goal is met, we start paying off debt aggressively over the following 4-5 years.

An important factor in this is the interest rate that we have to pay on the loans. In case we have to pay high interests for our loan, we will first get that loan off the papers. Then, we can take a new loan to meet the financial goal and repay it over the next few years.

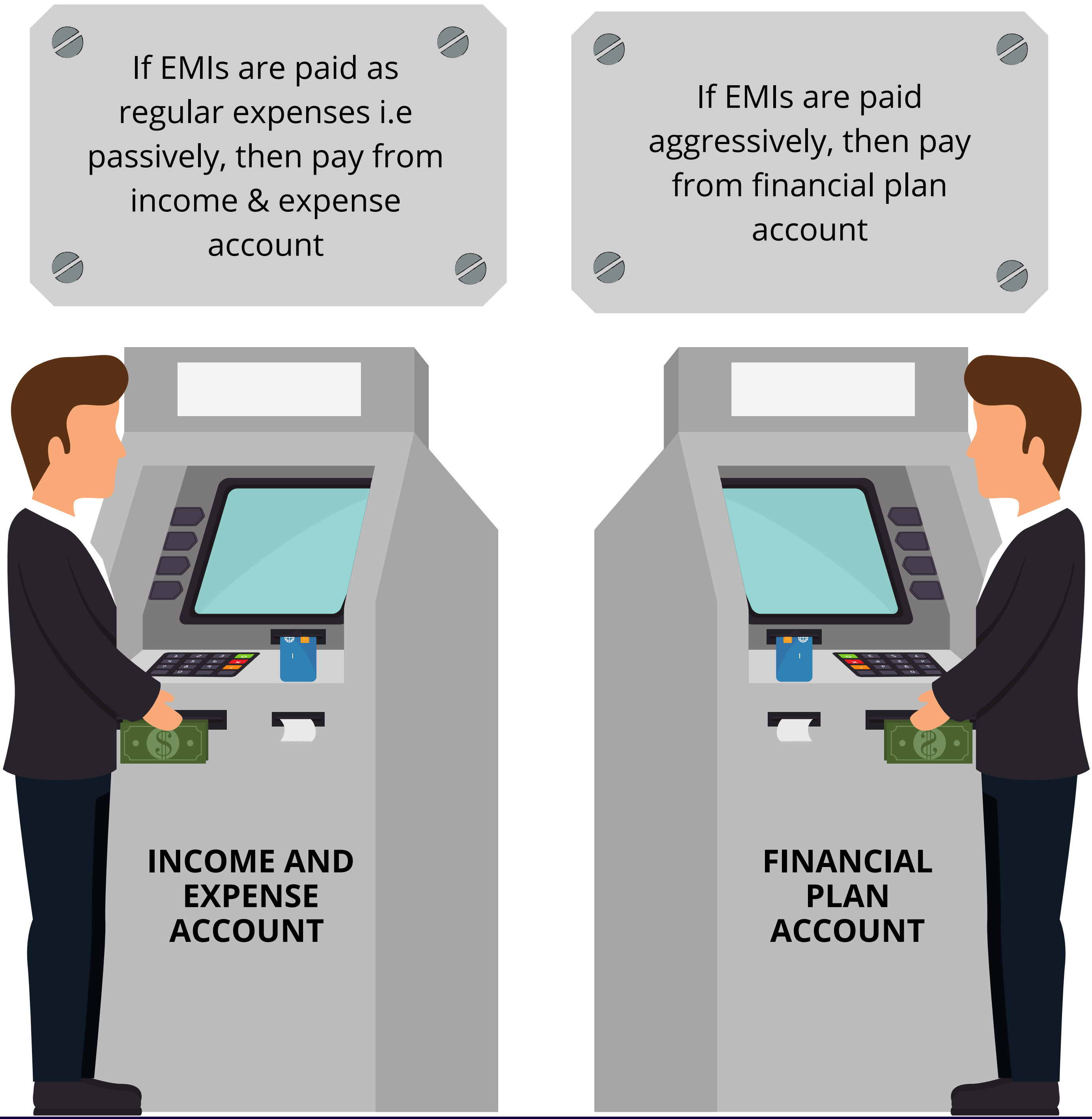
So, this is how we need to keep a balance between paying off any major liabilities and meeting our financial goals. However, this is applicable only when our liabilities are stretched. If they are within comfortable limits, systematic paying off of the same will serve the purpose and we can move to the asset side.



CASH FLOW MANAGEMMENT TO PAY LIABILITIES

We know that EMIs are a part of regular expenses and therefore will be paid from income and expenses account. However, in the phase when we are aggressively paying off the liabilities, we will be paying off the liabilities from the financial plan account.

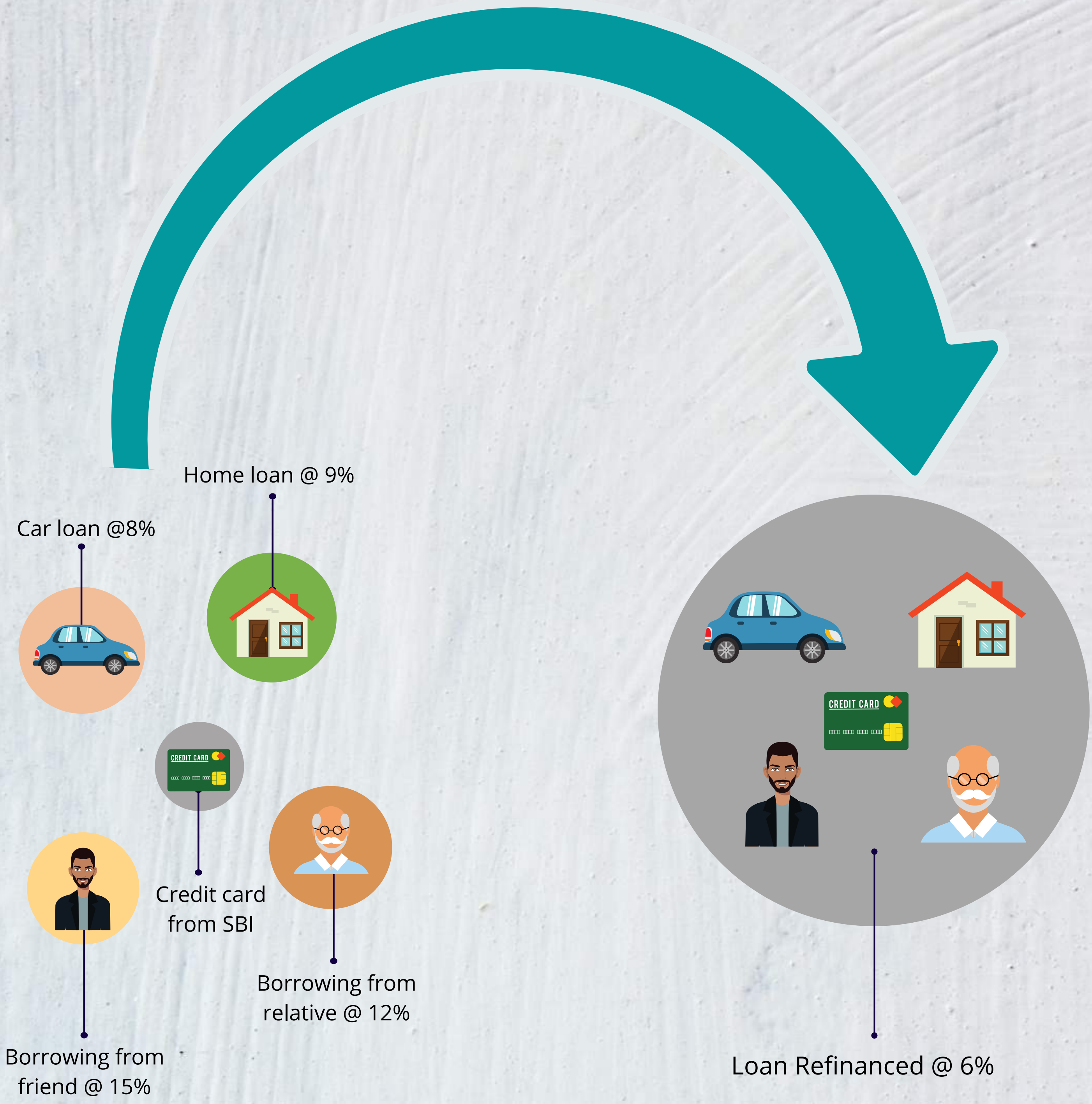
When we are paying off EMIs, we are paying it ‘passively’ in a systematic manner. These are small payments. However, when we are ‘actively paying it off, we won’t be able to focus on investments during that period. We would be sacrificing on building more assets to repay this loan. These will be large payments and hence should go out from the financial plan account because paying off loans aggressively will have a significant impact on our financial plan. Paying off small EMIs will not impact our financial plan.



The first step towards repaying liabilities efficiently, be it actively or passively is to have it structured. We will accumulate all the small loans/liabilities that we may have i.e.credit card bills, personal loans, small mortgages, a loan from a friend etc., combine them and get the same refinanced by a larger lender. We will pay off all these smaller liabilities and in return have a single bigger liability to deal with. We now only have to deal with one lender instead of multiple small lenders.

We can renegotiate a lower interest rate from this lender and then work out a customized paying schedule to repay it aggressively as well as with convenience. Ensure that there is no pre-payment penalty in the new loan. Pre-payment means paying off the loan earlier than expected. We may pay Rs. 1 lac as instead for an EMI of Rs 20,000. This way we will be able to repay it much faster i.e. pre-pay the loan. For those, who already have liabilities to net worth less than 0.5, they can skip this section to move directly to the investments.

REFINANCING OF LOANS



We earlier had smaller loans & were liable to repay the loan to 5 different entities. So, we take a longer loan from a bank & repay all smaller loans. Now, we are liable only to the bank. Also notice that refinancing of loans is done at a lower interest rate.

If we want to repay the loans individually, then we will repay the loans with a higher interest rate first and then go ahead in descending order.

In this manner, we can systematically pay off the debt and get it under control. We are looking to bring our debt to a level so that the liabilities to net worth is less than 0.5. Once we have reached this level, we can keep repaying the leftover passively over the years and focus on planning for our financial goals.

Whatever we have discussed in this section is just plain math. However, it is easier said than done. It requires a great deal of patience and discipline to pay off liabilities. We are not talking a lot about our earning power as that is something beyond the scope of personal finance. But working on income by improving skills and education is always a good idea to improve the health of Lazy Financial Plan and the lazy canvas.

CREDIT CARDS

In general, credit cards are the most expensive form of money and almost all financial experts and books profess against the use of credit cards. Up until a few years back, credit cards would have been a complete no-no for everyone. However, now credit cards can be used by those who are disciplined. This is because credit cards offer a lot of deals and also has a system of reward points that leads to significant savings and advantages. There are apps like CRED which reward people to pay using credit cards through their platform. However, the trick is to be disciplined and pay off the dues regularly. If we are not disciplined and do not pay off credit card bills on time, then the cost of using it would be much more than the discounts.

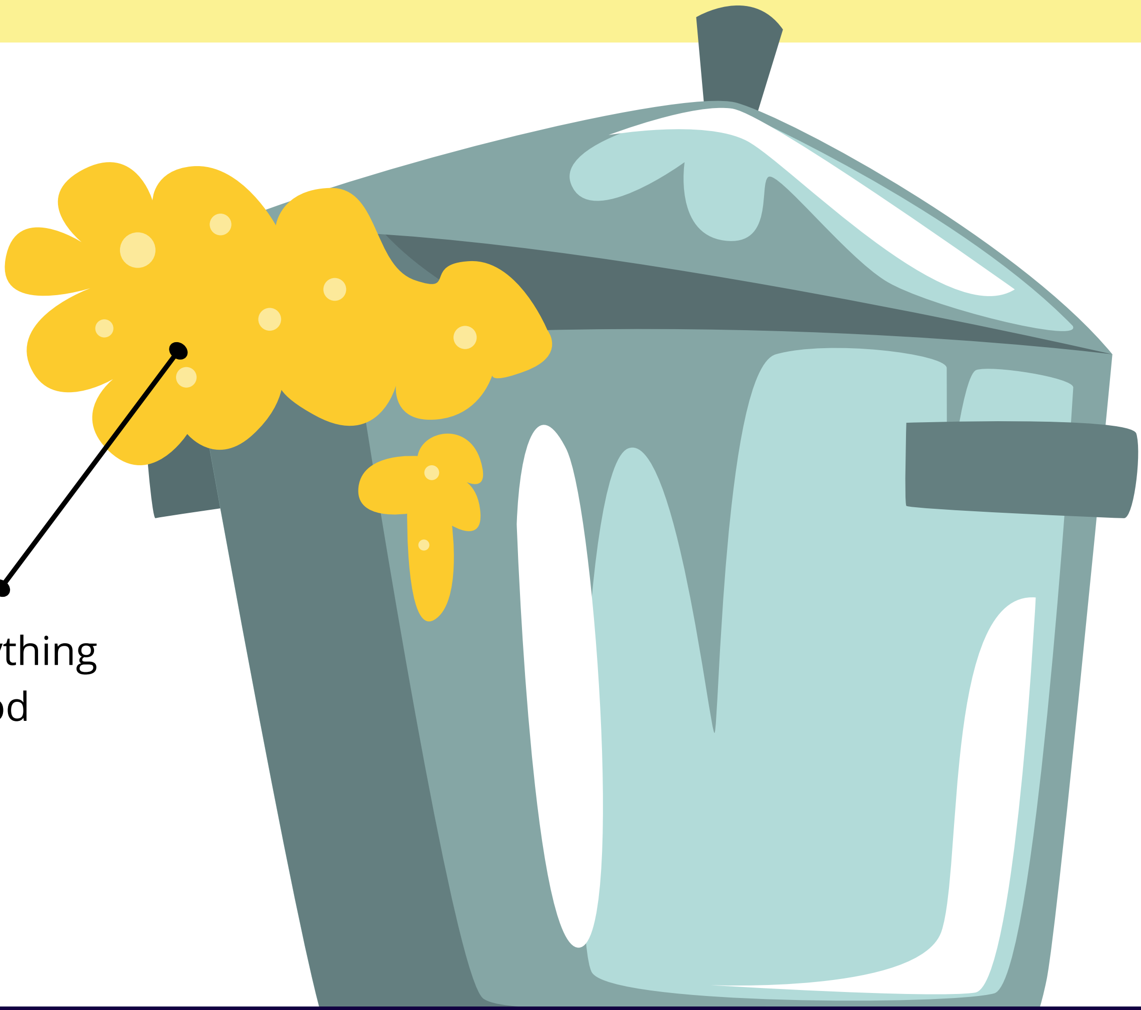
We can now manage our own money and if not, approach an expert to aid us in managing our liabilities. It might be simple ordinary math but it's the execution that is the key challenge. And finally, we come to the end of our discussion on liabilities. When we move to the asset side of the growth system, we have the liabilities under control and are now planning our assets to meet the goals on a very strong foundation.

MANAGING ASSETS

Now, we move ahead with the asset side of the growth system. Before we get started with these, let us revisit two common mistakes people make when dealing with assets.

PUTTING EXCESS MONEY IN EMERGENCY NEEDS

The first mistake is to put many years of their income in emergency-related assets. These assets are generally very liquid and earn a low but stable return. People find these psychologically more peaceful and as a result, but many years worth of income in these assets. We have already seen that 8-9 months of income is more than enough to meet emergency requirements. By putting excess money, we are earning a much lower return for no reason.

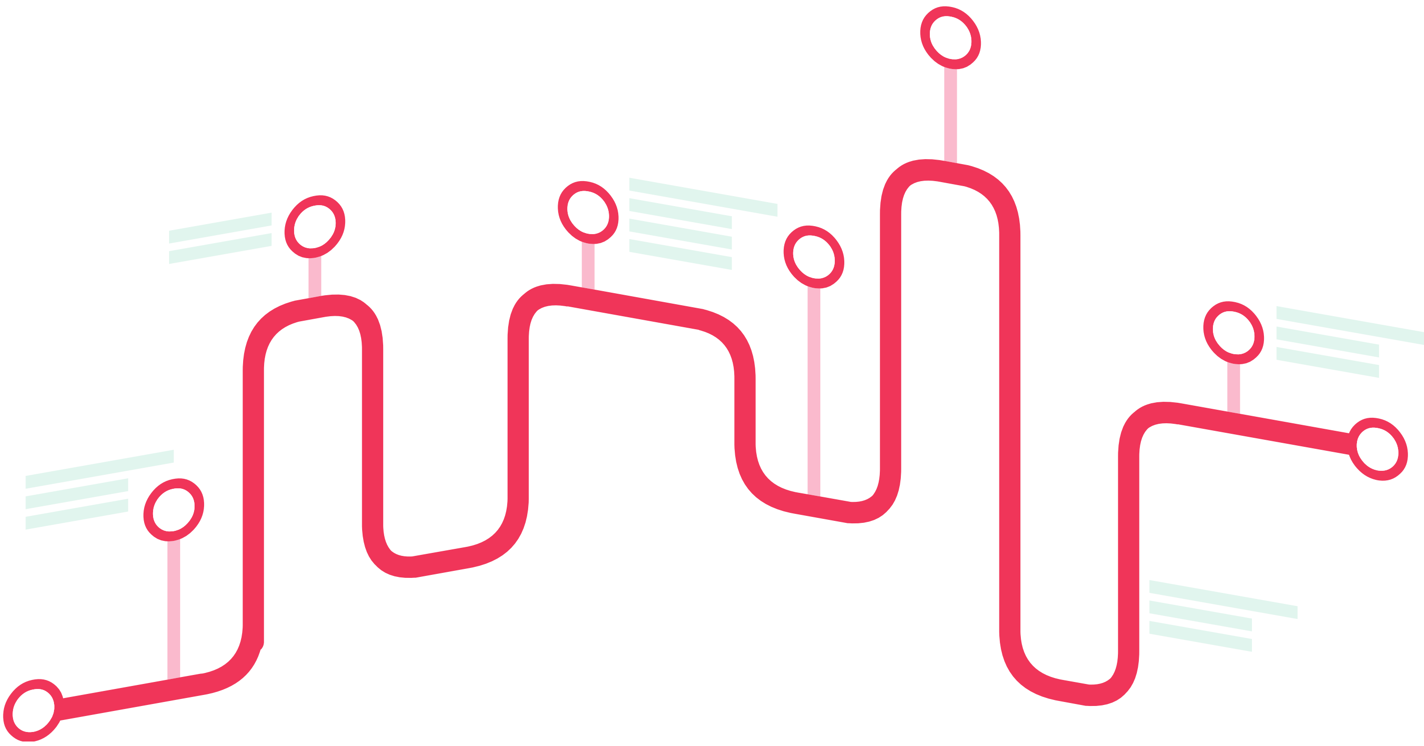


Excess of anything
is not good

VERY STRICT SPENDING DIET

Sometimes people try to save in every single thing and this process of frugality, they kill the small happiness along the journey. Such a strict spending diet is really difficult to follow and becomes impossible to do over multiple years. As a result, the entire Lazy Plan becomes unsustainable. So, it is much better to run a marathon than a sprint. Our financial goals and risk-taking ability and willingness will act as guiding light and direct us towards the next section i.e. to manage the asset side of the Lazy Financial Plan. The rest of the lazy canvas will help us create an effective growth system for ourselves.

Once we have taken care of these two factors, we will move ahead and create the asset side of the Lazy Financial Plan. Our Financial Goals and Risk taking ability and willingness will act as guiding light. The rest of the Lazy Canvas will help us create an effective Growth System for ourselves.



Money comes to our income and spending bank account and we leave the money that is required to meet our expenses and shift the rest to the financial plan bank account. Also, by now we have taken care of emergency needs, insurance system and liabilities. So, money that goes into our Lazy Financial Plan will move towards assets in the growth system.

Coming to the list of financial goals that we had created in the profiling stage, we had quantified them, prioritized them, and marked them on a timeline. We will begin with the goals that are highest on our priority list. Once we invest and plan for high on priority goals, then we will plan for those that are less important and so on.

Also, we had already plotted the timeline with different segments of it focusing on different goals. For instance, if we have to pay for our child's education in the next 3 years, our focus for the next 3 years is child education fees. We might have other more important goals, but because those are further down the line, our short term priority is child's education fees. We need to balance between allocating money towards high priority goals and the high urgency goals.

PLANNING AS PER TAXES

Let us get down to the part we have been waiting for so long, i.e. to begin planning for our assets and complete the Lazy Financial Plan. The very first thing that we will do is plan assets as per taxes. We will understand how we will plan our taxes as per the old tax regime and tie them up to financial goals. Those opting for the new tax regime can skip this step altogether as no tax deductions and exemptions are allowed under the new tax regime introduced in Budget 2020. In the case of the old regime, we will have to follow this step carefully.

Sometimes people make the mistake of investing with the sole objective of saving taxes, irrespective of whether or not it meets their financial goals and suits their financial circumstances. What they should do is focus on meeting the financial goals and thus try and save taxes. However, there also will come circumstances where we let go of tax benefit assets to plan better for our financial goals. Tax saving and financial goals should go hand in hand and tax benefits should only be exercised if they help us meet our financial goals.

First, we will go back to the canvas where we had listed down all the tax benefits that apply to us and we might be in a position to take advantage of. Next, we will create a list of expenses that we are already incurring and are eligible for deduction under Section 80C. For instance, we might be paying child's education fees, home loan principal repayment, or life insurance premium.

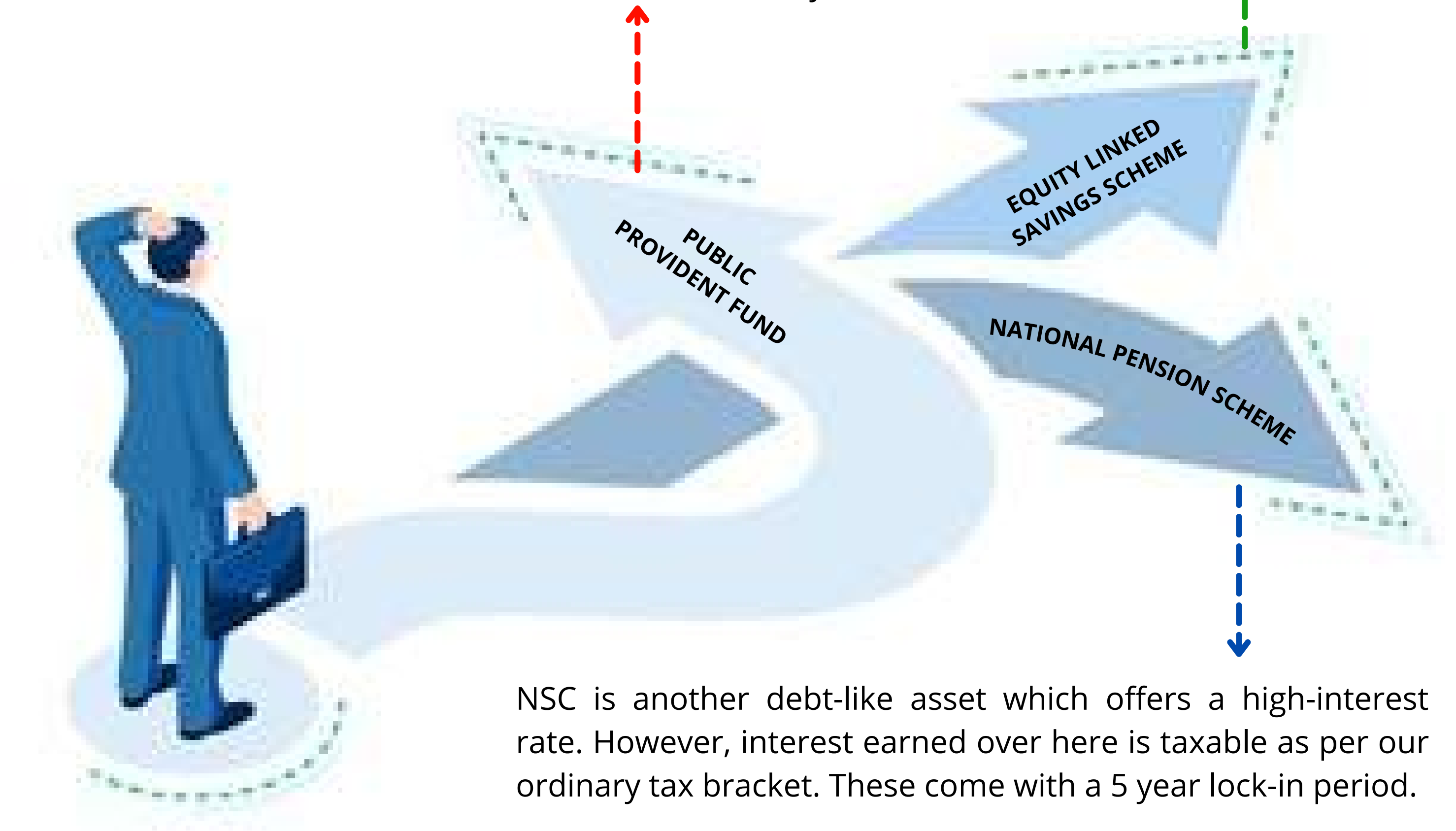
We will claim all these for deduction under Section 80C and will have used a portion of Rs. 1.5 lac deduction that is allowed to us. Let us say, all the above expenses amounted to Rs. 60,000. So, we have Rs. 90,000 left that we need to plan for and seek deduction for. For this, we will invest in different tax saving assets.

Now that we know the amount to be invested in tax-saving assets, the next question is how to invest and where to invest for tax benefits. We saw in the assets section that various assets are eligible for Section 80C deductions. We can invest money in these assets and claim a deduction from our taxable income for the same amount. This reduces our tax bill.

We have identified three main investments that are most beneficial and suitable for almost everyone. This is for simplicity and these three can help plan for any financial goal. These include – ELSS (Equity Linked, Mutual Fund like a scheme with a 3-year lock-in for investments), Public Provident Fund (PPF) and National Savings Certificate (NSC). We will plan for 80C deductions using these assets. Let us understand more about these -

These are special types of mutual fund schemes that are linked to equity. Their risk-return characteristic is in line with equity. They come with a 3-year lock-in of capital. These offer the highest return in tax saving instruments as they are the only way to get equity exposure.

PPF are on lines of debt and offer a fixed rate of interest that is quite attractive for a fixed income asset. Also, they fall in EEE category which means we get tax benefits when we invest when we get interested and when we redeem the investment at maturity. They come with 15-year lock-in. Equity funds are better than PPF because PPF has to be invested for 15 years.



NSC is another debt-like asset which offers a high-interest rate. However, interest earned over here is taxable as per our ordinary tax bracket. These come with a 5 year lock-in period.

SUITABILITY OF ASSETS

Now we know the asset options made available to us. The following list guides us towards allocating money amongst the three and the one that would be the best suited.

For anyone who has moderate or high risk-taking ability (2.5 or greater than 2.5), should put the entire 80C investment component in ELSS. This is because money is anyways locked-in in other assets and over the long term, ELSS would produce the best returns as compared to other assets.

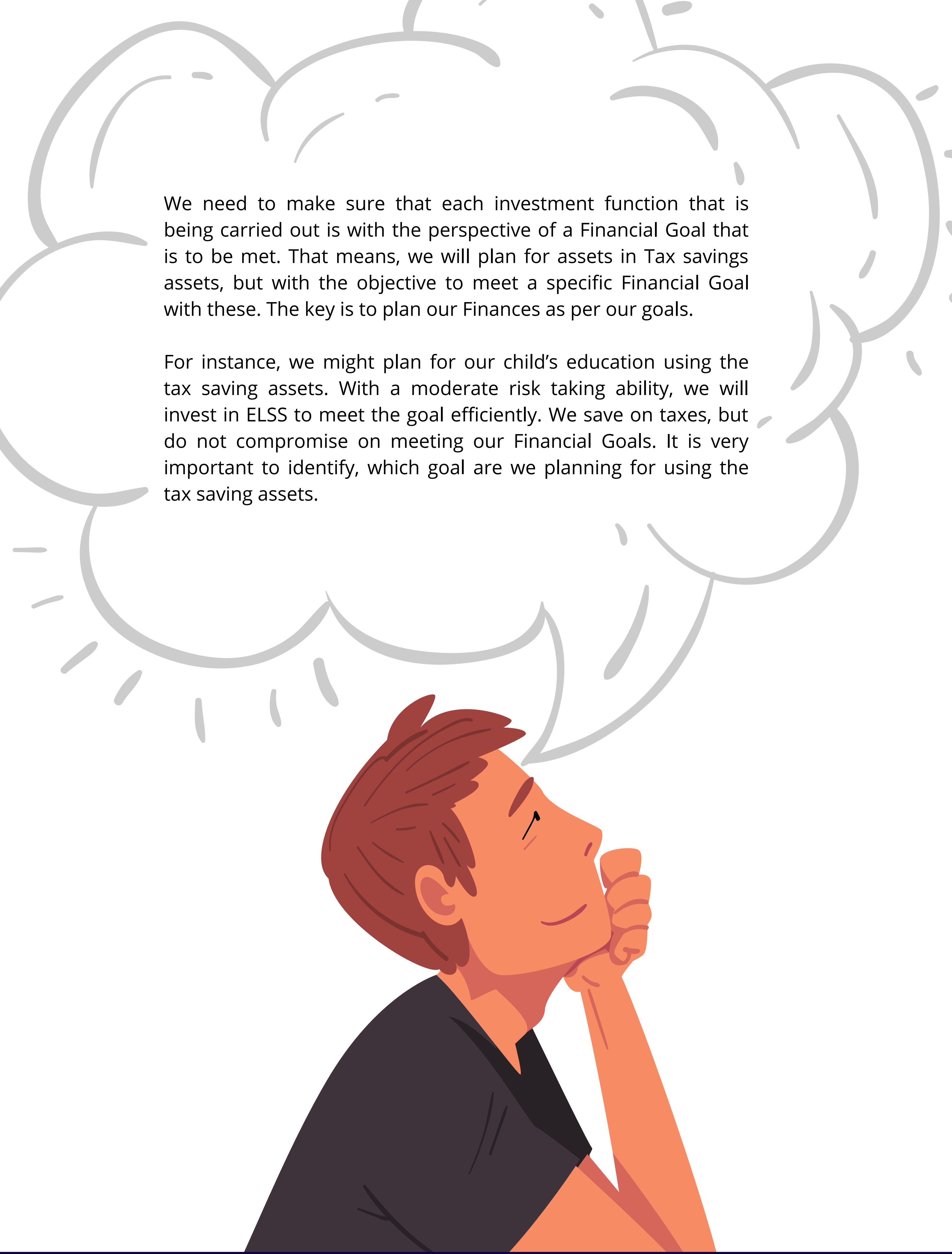
For anyone with a low risk-taking ability (less than 2.5) and having long term goals that they intend to meet with these savings – they are better off with PPF. The higher interest rate allows them to hold money here for longer-term. PPF is the most popular tax saving asset today – mainly because of its debt-like nature and distinctly higher interest rate.
For those who intend to meet medium-term goals (5-7 years) and have a low risk-taking ability (less than 2.5), they shall invest the 80C investment component in National Savings Certificate. For medium-term goals, NSC is better than ELSS because ELSS is linked to equity and cannot always be sold when required.

Note that we should prioritize financial goals and not tax savings. Tax saving can be an added benefit. If we opt for a tax-saving asset class but are unable to reach our goal, then it makes no sense.

GOAL / RISK SCORE	SHORT TERM	MEDIUM TERM	LONG TERM
> 2.5	DO NOT GO FOR ANY TAX BENEFIT	ELSS	ELSS
< 2.5		NSC	PPF

We need to make sure that each investment function that is being carried out is with the perspective of a Financial Goal that is to be met. That means, we will plan for assets in Tax savings assets, but with the objective to meet a specific Financial Goal with these. The key is to plan our Finances as per our goals.

For instance, we might plan for our child's education using the tax saving assets. With a moderate risk taking ability, we will invest in ELSS to meet the goal efficiently. We save on taxes, but do not compromise on meeting our Financial Goals. It is very important to identify, which goal are we planning for using the tax saving assets.



SMALL SAVING SCHEMES

So far, we have generalized all of the tax-saving assets under three broad categories– ELSS, PPF and NSC. However, there are other small saving schemes that we had discussed earlier in the assets section, specifically suitable in certain select situations. If suitable, we can always explore other options.

Small saving schemes are particularly suitable for senior citizens or those approaching retirement i.e. Senior Citizen Saving Scheme, POMIS etc. create a great investment case for the elderly. Senior citizens can plan for tax savings using the above-mentioned assets as well. Although, most of it has substituted in the mutual fund industry, however, if government backing comforts senior citizens more, then they should pursue the same.

NATIONAL PENSION SCHEME

Not everybody is fit to invest with the National Pension Scheme. NPS offers additional Rs. 50,000 as a deduction which is over and above the Rs. 1.5 lac offered by Section 80C. We saw earlier how NPS works, how we can select from various classes and also how NPS has a very restricted withdrawal policy. However, NPS has a restrictive withdrawal policy i.e.we can only withdraw a small portion of our corpus after the age of 55 and the rest is converted to annuities. So, the only purpose of NPS is to plan for pensions and retirement. That is the only goal that NPS can help us meet.

Anyone below the age of 40 should refrain from investing in NPS since the lock-in is significantly high and thus are much better planning for retirement or long term goals using equity and mutual funds. Also, the time horizon is long which means compounding will have a significant role to play and as a result, we want a higher return from our assets.

For anyone above the age of 40 will take advantage of this Rs. 50,000 additional benefit that is being offered as tax savings. We saw that we want to manage a part of retirement funds on our own and another part with the government. The part that we manage will make sure we earn higher returns and the one with the government will ensure safety, stability and discipline. So, we will invest Rs. 50,000 in NPS and anything beyond this will be managed on our own using retirement funds, mutual funds and other assets.

When investing in NPS, we would need to select a class of assets that we want our money to be invested in. So, between age 40 and 50, we will invest the maximum i.e. 50% of our money in E-class and rest in C-class and G-class. Between 50 to 60, we will gradually decrease our share in E-class. By age 55, we will want 80% of our assets in C-class and G-class.

So, this is how we deal with NPS and the deductions the taxing authority has to offer for the same. We have planned for 80C and all its deductions.

AGE / ASSET CLASS	BELOW 40	40-45	50-60
E-CLASS	DO NOT INVEST IN NPS	50%	GRADUALLY DECREASE SHARE IN E- CLASS
C-CLASS & G-CLASS		50%	BY THE AGE OF 55, 80 % OF ASSETS IN C & G CLASS

ONLY RS.50,000 WILL BE INVESTED IN NPS. REST WILL GO TO OTHER ASSETS

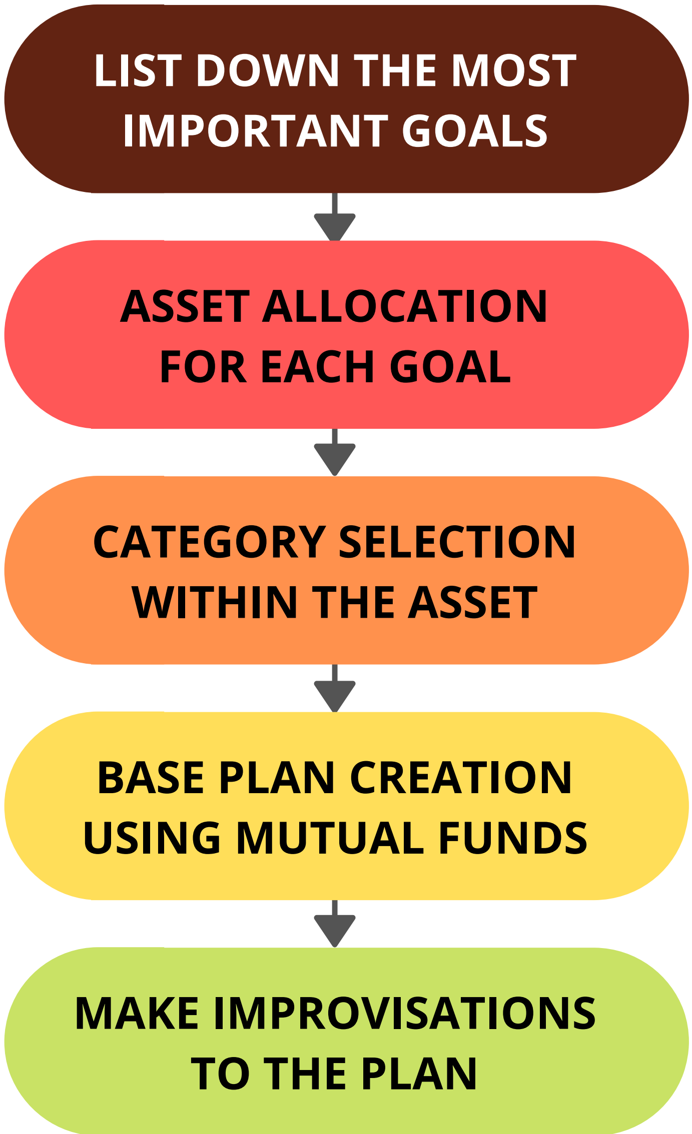
We saw the major deductions offered by the Income Tax Act relating to investments and expenses. However, the Act offers many other deductions that we have already discussed n the lazy canvas stage. Let us understand, how to deal with these.

We had earlier identified deductions under categories like health, loans, donations, saving/fixed deposits and so on. We had already marked all the scenarios that apply to us in the lazy canvas. We will seek deductions for each of these. These do not have any major implication on our growth system and hence there is not a lot to plan over here.

PLANNING FOR GOALS

We will now focus on systematically planning to meet our individual goals. We will emphasize where and how much should be invested for each financial goal. We already have a broad understanding of how we begin with the most important goals and then how we move to other goals after taking care of more important ones.

Here, we will start with the broad allocation of resources into different asset classes for each goal. Then we move forth with selecting the category within the selected asset class which best suits our risk-taking ability. We will create a base plan using debt and equity only i.e. different mutual funds. After that, we will replace some of it with other assets i.e. real estate, gold, direct equity etc. to better suit our willingness and comfort.



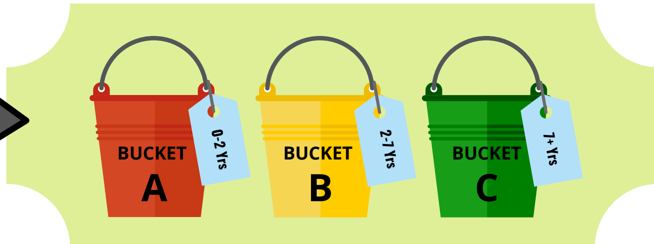
For now, we will go back to the list of Financial Return Goals where we had quantified and prioritized each goal and put them in different baskets based on time horizon. We will use these buckets to decide broad asset allocation between different types of assets. We will then use Risk Taking ability to decide Categories to be selected within each Asset Class.

We already saw that we will create a base plan only using a plain vanilla debt and equity allocation. We will introduce other assets in the mix going further. We will mainly be talking about Mutual Funds as Mutual Funds have substitutes for every asset. Different kinds of Mutual Funds are capable to create a Financial Plan for any situation. As a result, we will create a base plan around them and add other assets to the mix later on depending on comfort with Financial Assets.

LIST DOWN THE MOST IMPORTANT GOALS

ASSET ALLOCATION FOR EACH GOAL

Use these buckets for this step



CATEGORY SELECTION WITHIN THE ASSET

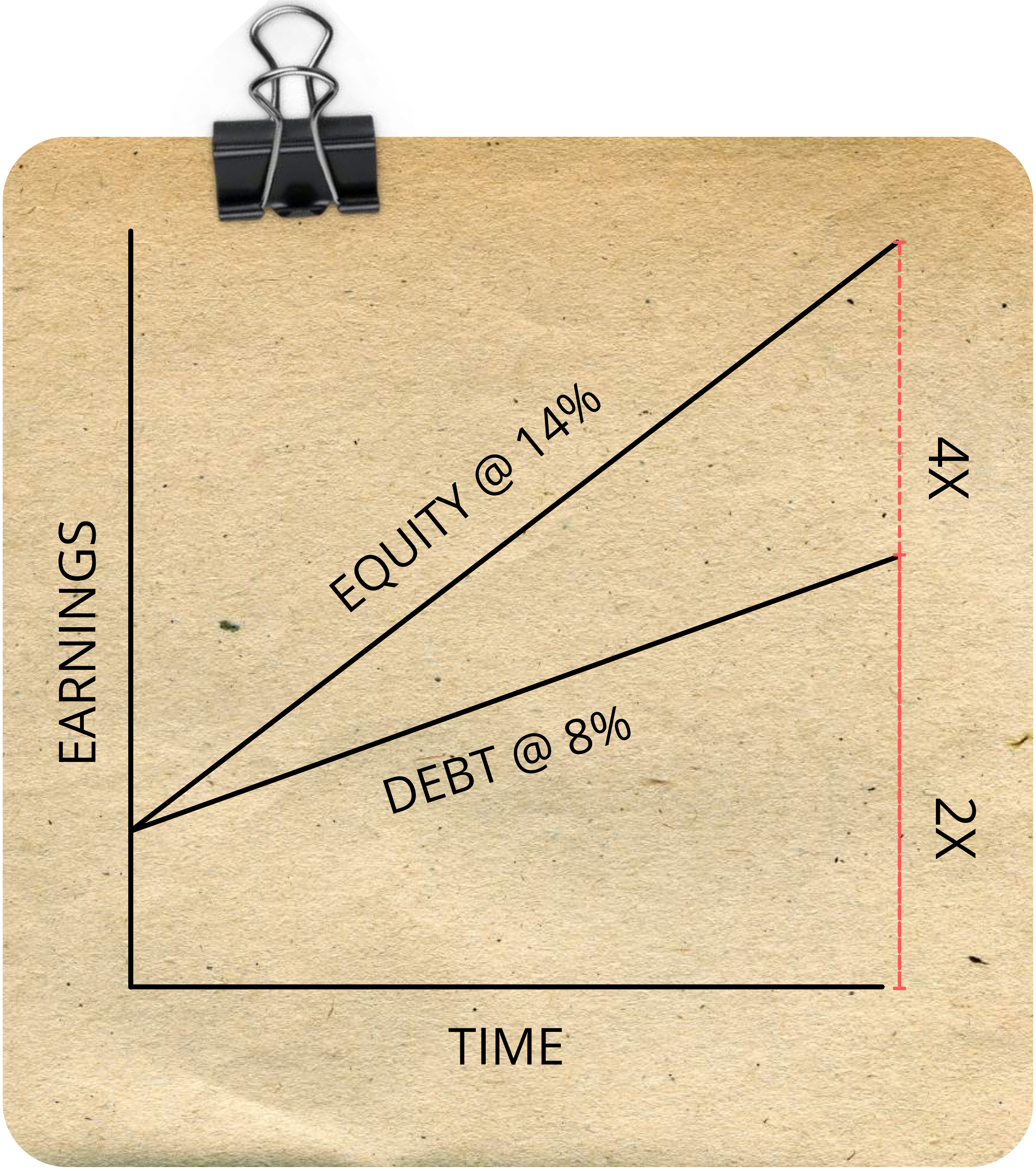
BASE PLAN CREATION USING MUTUAL FUNDS

MAKE IMPROVISATIONS TO THE PLAN

GOALS TO BE MET IN MORE THAN 7 YEARS

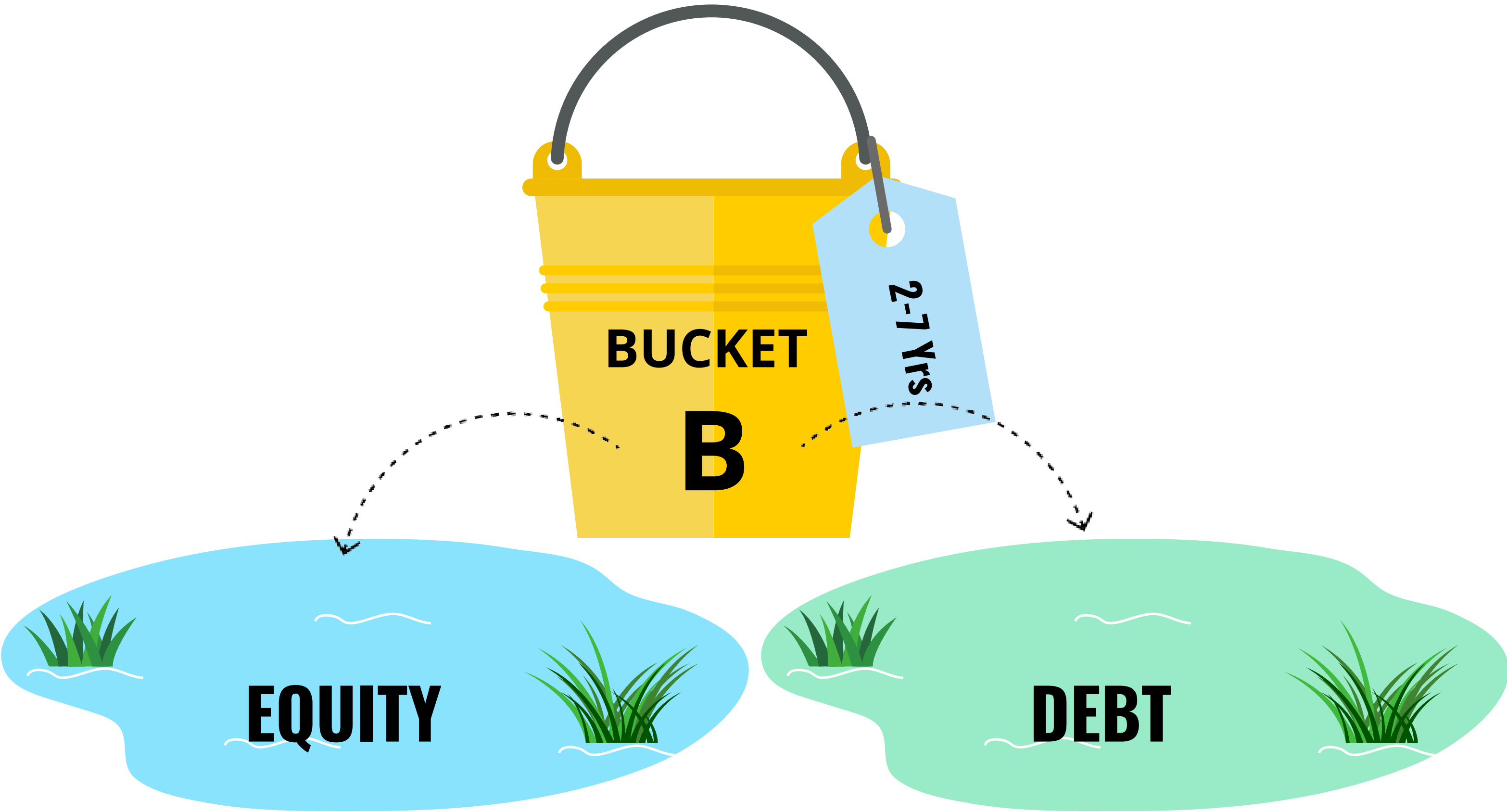
Goals that are to be met in more than 7 years, are long term goals where we can invest up to 100% in equity. Here, we have enough time to deal with the volatility and as we want higher return so that the compounding effect is greater. The allocation within the different categories of equity will depend on our risk-taking willingness.

We know that we can invest in mutual funds either through SIP or in a lump-sum. A lump-sum amount can be invested via Systematic Transfer Plan (STP) or Portfolio Management Service (PMS). STP is better than PMS as it takes care of the valuation risk in a much more systematic manner.



Why do we emphasize on equity for long term goals? In the long term, equity outperforms debt by a huge margin due to the compounding effect. For instance, a fixed deposit with 7% p.a. as the return, doubles the money in every 10years. At the same time, an equity investment earning 14% p.a. grows the money 4x in a similar time frame. So, we have 2x by investing in equities compared to what we would have by investing in fixed deposits. The difference increases as more time passes. Over 20 years, the difference becomes 4-5x. This difference could decide if we are meeting the goals or not. That is why, when we have more than 7 years to reach a goal, we should try and allocate as much as possible to equity.

GOALS TO MET IN 2 TO 7 YEARS



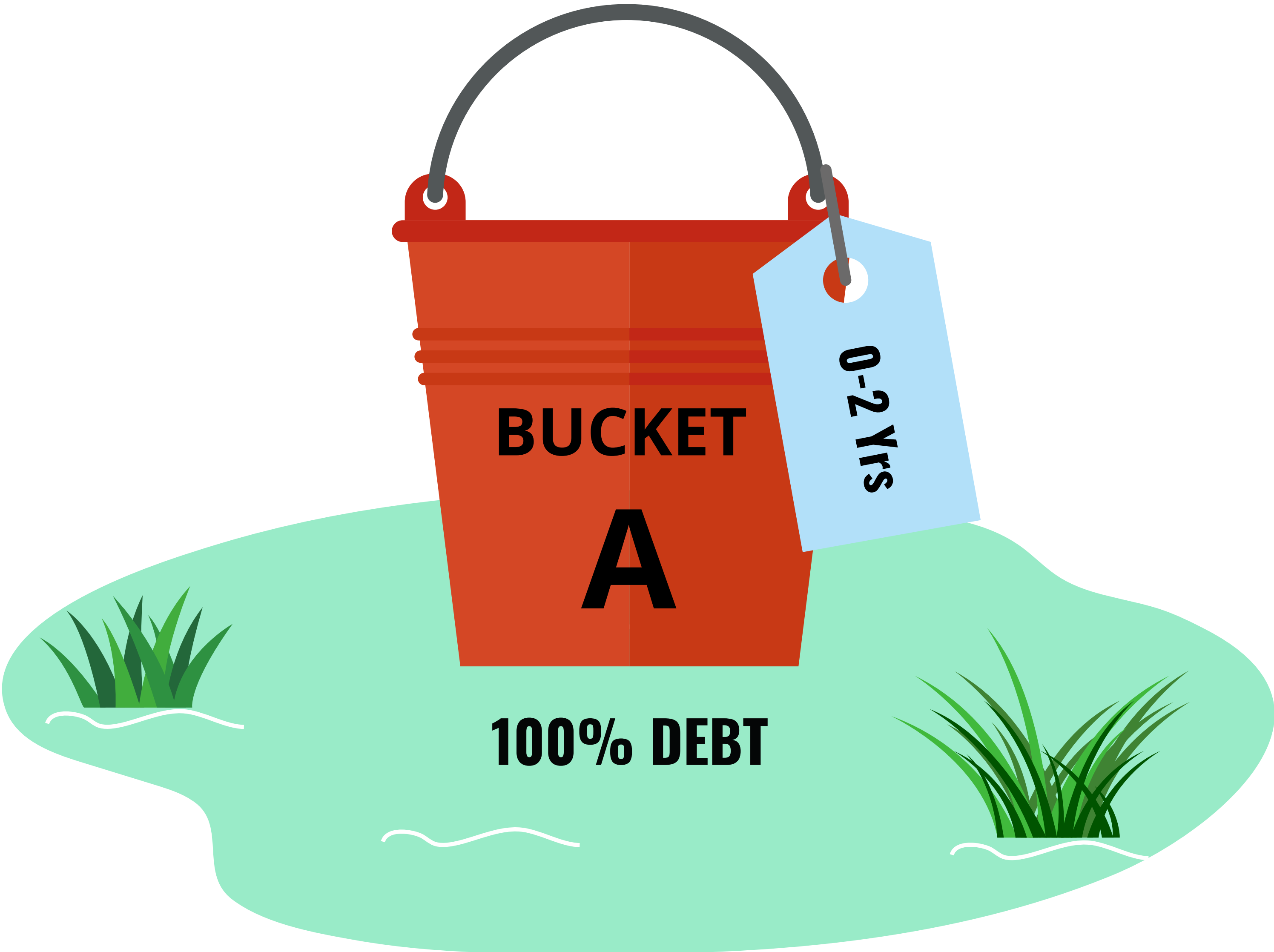
Goals that are to be met in the medium term will have a reducing equity component and increasing debt component. The goals to be met in the span of 2 to 7 years will be sub-grouped as 5-7 years, 3-5 years and 2-3 years depending on the time left starting today.
We started with 100% equity for 7+ years, but as time passes, the effect of compounding reduces and our ability to handle volatility also goes down too. As a result, we will systematically decrease the equity component in the mix.

For goals to be met in 5-7 years from today, we will have 30% of the amount in debt and 70% in equity. This will give us a balance of stability and higher returns. For goals to be met in 3-5 years, we will have 50-50 share of equity and debt. One can always reduce the share of equity in the mix if the risk-taking willingness is low. For goals to be met in 2-3 years, we will have 70% in debt and 30% in equity. As time horizon reduces, we want more of stability and low returns will be fine as compounding is no longer powerful the way it was with long term goals.

YEARS	EQUITY	DEBT
6-7	70%	30%
4-5	50%	50%
2-3	30%	70%

We will have to shift money from equity towards debt systematically. The best way to do that is through a Systematic Transfer Plan (STP).

GOALS TO BE MET IN LESS THAN 2 YEARS



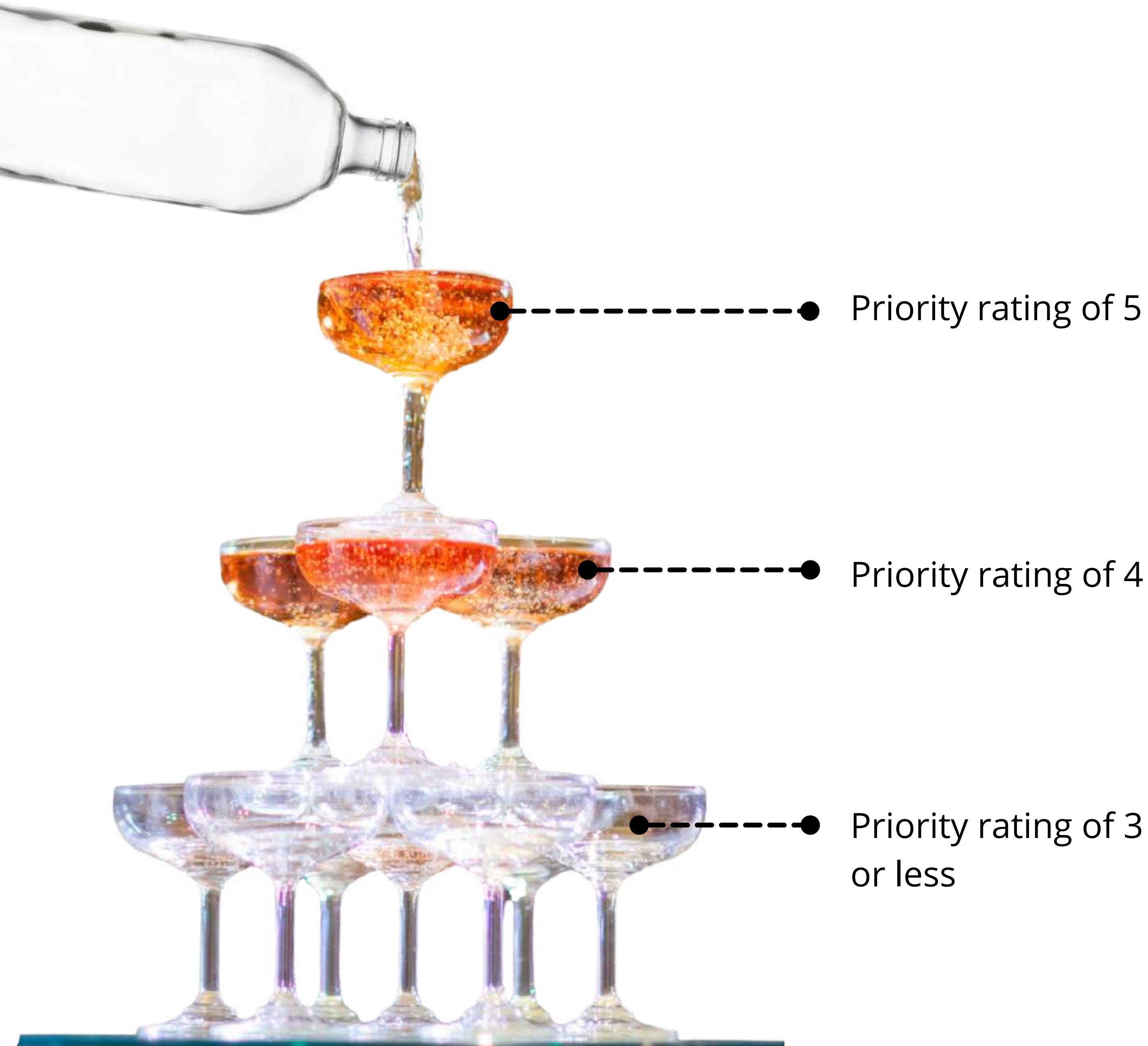
The last bucket contains those goals that are to be met in less than 2 years. Here we do not have time, the risk-taking ability is low and safety is of utmost importance. Few percentage points of return here and there will not make a lot of difference because no effect of compounding will be seen in such a short period. Here, we will invest 100% in debt. We will prefer money market mutual funds, government bond funds with low maturity or fixed deposits.

We see how our investments have evolved. Starting from 100% equity, we have systematically transferred the money to 100% debt and in time to meet our financial goals. We balanced stability and returns all along to plan for the goal efficiently.

PRIORITIZING FINANCIAL GOALS

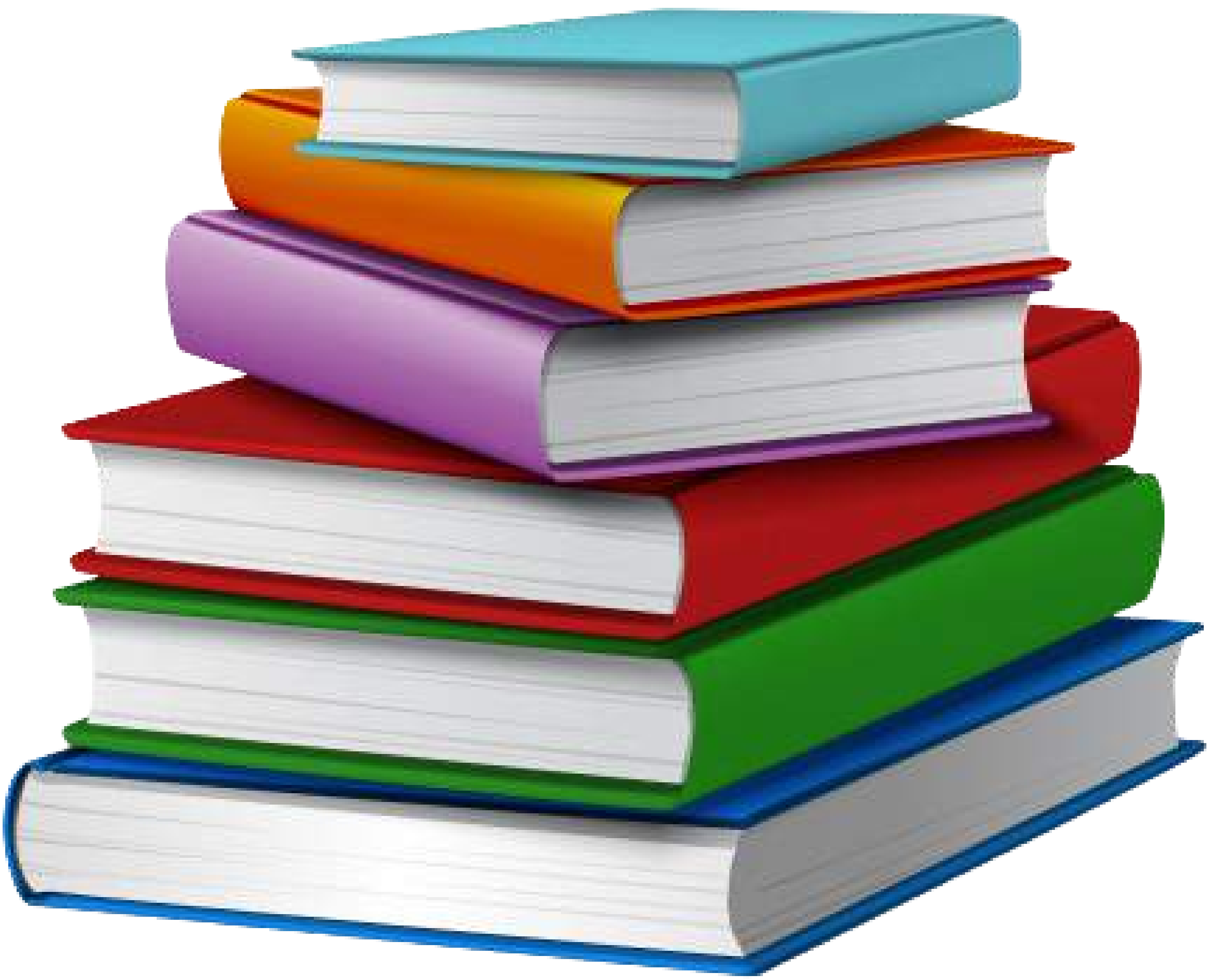
There is a possibility of not being able to meet or fulfil every goal since. we might not be left with enough money l after paying our expenses. This is why we had prioritized the goals initially and we begin with the most important ones and move to the less important ones only if we still have resources.

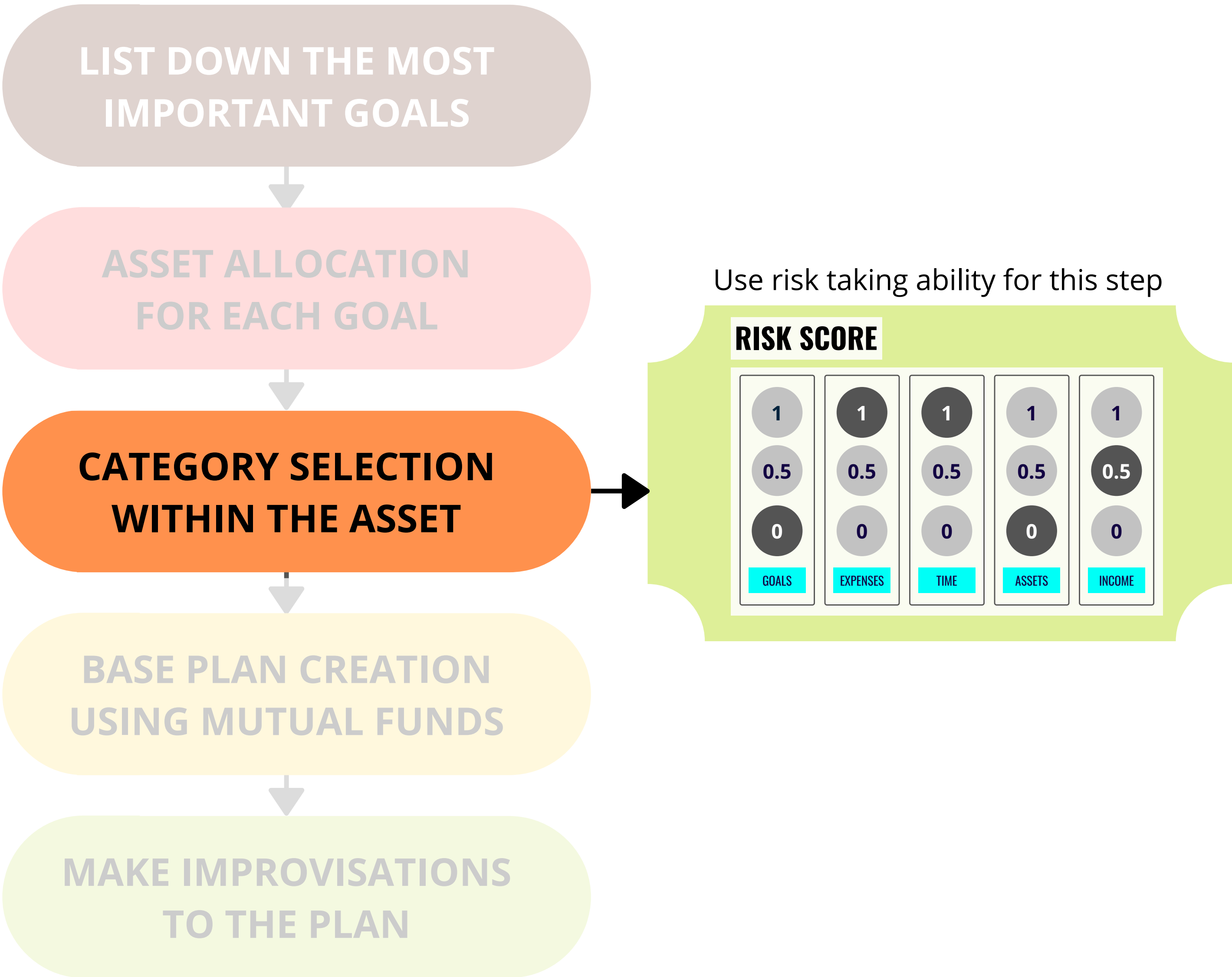
We will begin with the goals that have a priority rating greater than 4. If we have resources left after planning for each of those, then we will move to the goals with a priority rating of 3. If we do not have enough earnings or money to plan for each goal, we will leave the goal for the time being. We will take care of these in the future when income increases or responsibilities decrease. This is how we allocate money for each goal.



OVERSIMPLIFICATION BY FINANCE BOOKS

Many finance books deal with debt and equity by simplifying it way too much. The common rule says that 100 minus our age is the percentage of assets that should go towards equity and the rest towards debt. So if we are 40 years old, 60% should go in equity in 40% in debt. However, this oversimplification does not work when we already know our goals. When we know our goals, we allocate our resources based on the requirements of each goal and in the process, the debt-equity ratio can come out to be anything. As mentioned before, mutual funds form the base of our plan.





We had discussed earlier that we will be creating a base plan using mutual funds. So, once we decide the debt and equity allocation for each goal, we will select the correct categories within debt and equity.

We are not talking about direct equity or fixed income over here because we are aware that these are only for those who have adequate skill and time. However, for most individuals, mutual funds are a better way because it is not very demanding of time and skills.

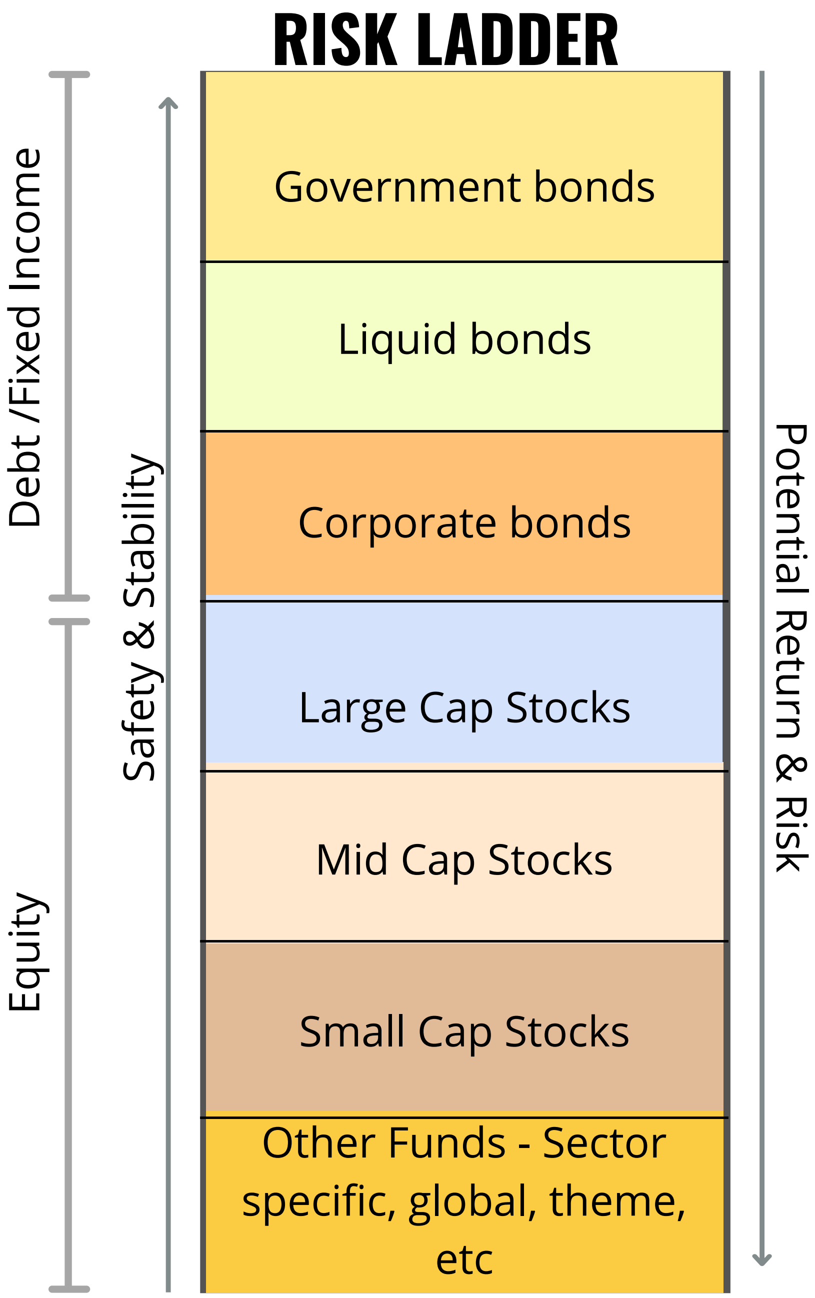
SELECTING THE CATEGORIES WITHIN EQUITY MUTUAL FUNDS

Once we select the mutual fund category, we know how to select the best mutual fund within the category. To keep it simple, we will stick to the basic ones as they work just as well. The selection of category depends on the risk-taking ability. Let us understand the categories for equity-related mutual funds.

CATEGORY / RISK-TAKING ABILITY	SMALL CAP	MID CAP	LARGE CAP/ VALUE FUNDS	EXPERIMENTAL/ HIGH RISK*
HIGH ABILITY > 2.5	20%**	30%	40%	10%
MODERATE ABILITY 2 - 3.5	—	40%	50%	10%
LOW ABILITY < 2	—	20%	80%	—

*Experimental or higher risk categories – Focused funds/ real estate/ Global funds/ sector specific funds etc.

**Here, 20% means 20% of the equity portion. We can invest using Mutual Fund as well as ETF, both work great.



We just saw the adequate category wise distribution of the equity component based on Risk Taking Ability. However, it often happens that when the amount to be invested on a per month basis is small, categorizing it in the above categories becomes really cumbersome. Also, often people want have low risk taking willingness. They are not comfortable with higher risks as discussed. In all these cases, one can move up the risk ladder and select assets that are above what is ideal based on risk taking ability. so, if someone needs 50% mid cap and 50% large cap, they can move up the ladder and have 100% in large caps.

They can even move up to debt part. We will understand debt categories very shorty. The key is always to move up the ladder. Never will we move lower in the ladder. The objective for this movement can be lower risk taking willingness or simplification of allocation as mentioned. However, we will avoid moving too many steps up on the ladder. It leads to inefficiency and lower potential returns for no reason. We will try to limit the movement to one step in general.

SELECTING THE CATEGORIES WITHIN DEBT MUTUAL FUNDS

CATEGORY / RISK-TAKING ABILITY	GOVERNMENT BOND FUNDS (Security & Safety)	SHORT TERM BOND FUNDS (Low Risk & Low Return)	CORPORATE BOND FUNDS (Relatively more risky than government but higher return)	MEDIUM DURATION BOND FUNDS (Medium Risk & Medium Return)	SEE BELOW FOR NOTES
HIGH (ABILITY > 3.5)	—	—	✓	✓	1
MODERATE (ABILITY 2-3.5)	✓	—	—	✓	2
LOW (ABILITY <2)	✓	✓	—	—	3

1 We can select either of the above or distribute between the two in any ratio. Both of these can help us meet our objective at this stage. We will avoid credit risk bonds and long duration bonds despite high risk taking ability because that is beyond the scope of most individuals to understand and monitor. As a result, we will ignore these high risk bonds completely.

2 We will distribute between the two categories based on our willingness to take risks. Ideally, a 50-50 distribution should serve a good balance.

3 These give both stability as well as safety. They have relatively low return, however, match our risk profile.

GOALS TO BE MET IN LESS THAN 2 YEARS

For goals that are to be met in less than 2 years, the risk-taking ability does not play a role in the Debt selection process. The time left is so less that we cannot afford volatility. Here, we will invest in very safe assets.

FIXED DEPOSIT

LIQUID BOND FUNDS

MONEY MARKET FUNDS

LIST DOWN THE MOST IMPORTANT GOALS

ASSET ALLOCATION FOR EACH GOAL

CATEGORY SELECTION WITHIN THE ASSET

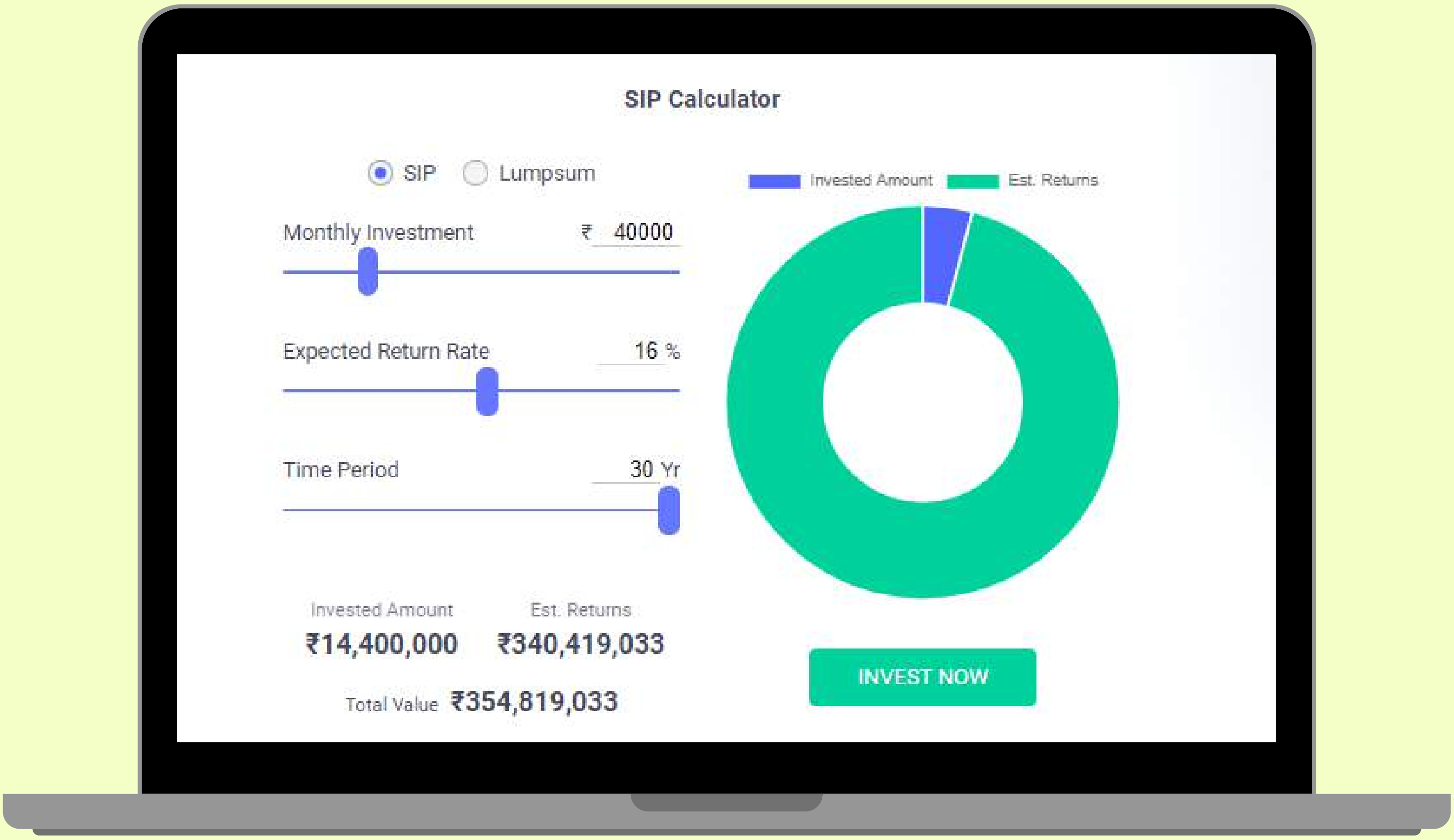
BASE PLAN CREATION USING MUTUAL FUNDS

MAKE IMPROVISATIONS TO THE PLAN

HOW MUCH TO INVEST TO MEET THE GOAL?

So far we have covered the broad asset allocation and understood the categorization based on risk-taking ability. We have also seen how we begin with the highest priority goal and then move ahead to less important goals. We have also seen how timeline and focus on shorter-term goals also have implications on how we route our finances. Lastly, we need to determine the amount of money that we need to invest today so that we have the required funds when the time comes.

Determining the amount of money revolves around the concept of 'Time Value of Money'. Let us understand the implications of the same. We will use the SIP calculator available on the Groww website to calculate the number of investments we need to make today. We can use other SIP calculators also. We can access this calculator here - https://groww.in/calculators/sip-calculator/

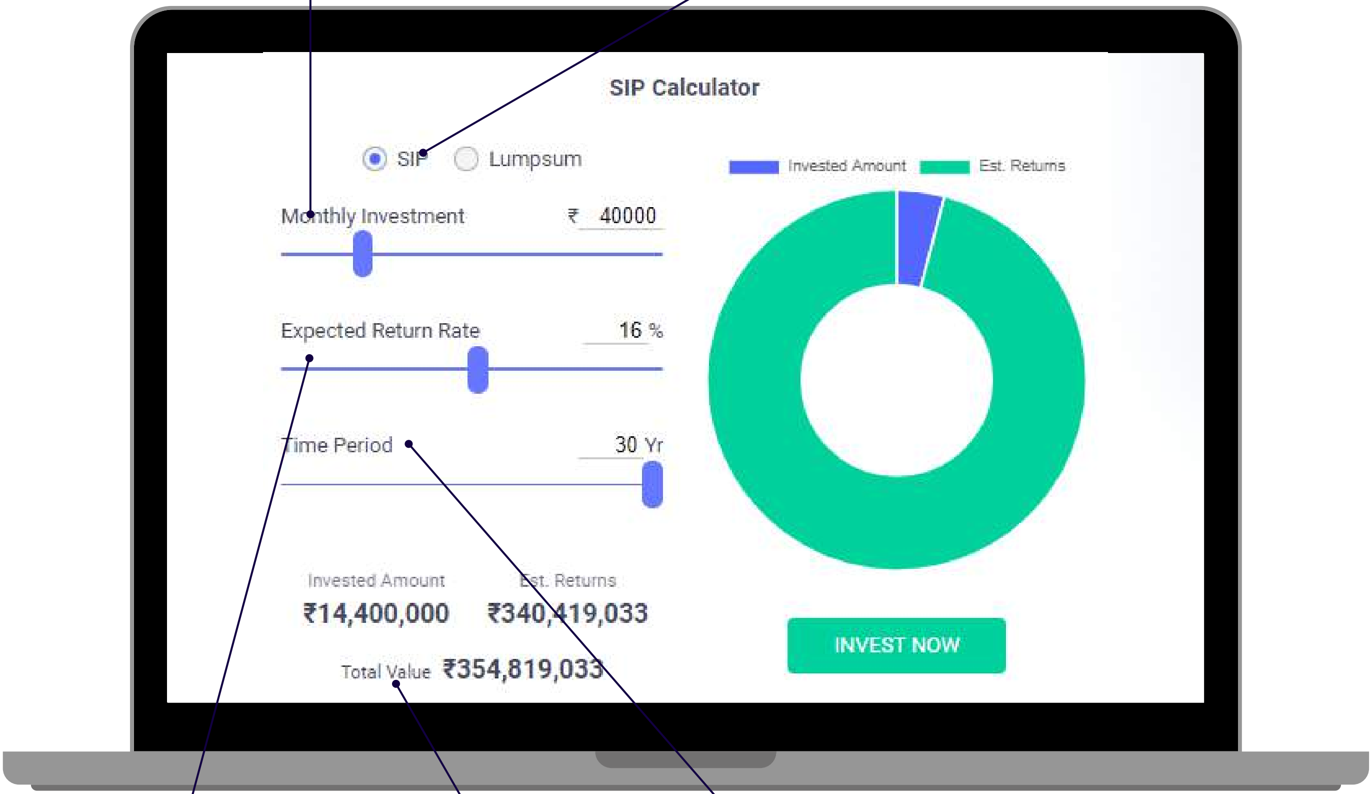


INVESTMENT

It refers to the amount of investment we need to make today to meet future goals. In case of SIP, it is the amount we need to invest every month. In the case of lump-sum, it is the total amount we need to invest initially to reach our goal.

SIP OR LUMPSUM

Firstly, select the appropriate method of investing i.e. SIP or lump-sum.



EXPECTED RATE OF RETURN

Check the 7-year average returns of all the selected categories on the Morningstar Mutual Fund Screener.
Based on asset allocation to different categories, we will calculate the weighted average return. This is our expected rate of return. We will understand this better using an example shortly.

TIME PERIOD

It refers to the number of years we have from today to meet the goal.

TOTAL VALUE

This is auto-calculated. It is approximately the total amount of money that we will have after the investment period. This is a rough estimate and amount will be somewhere around this.

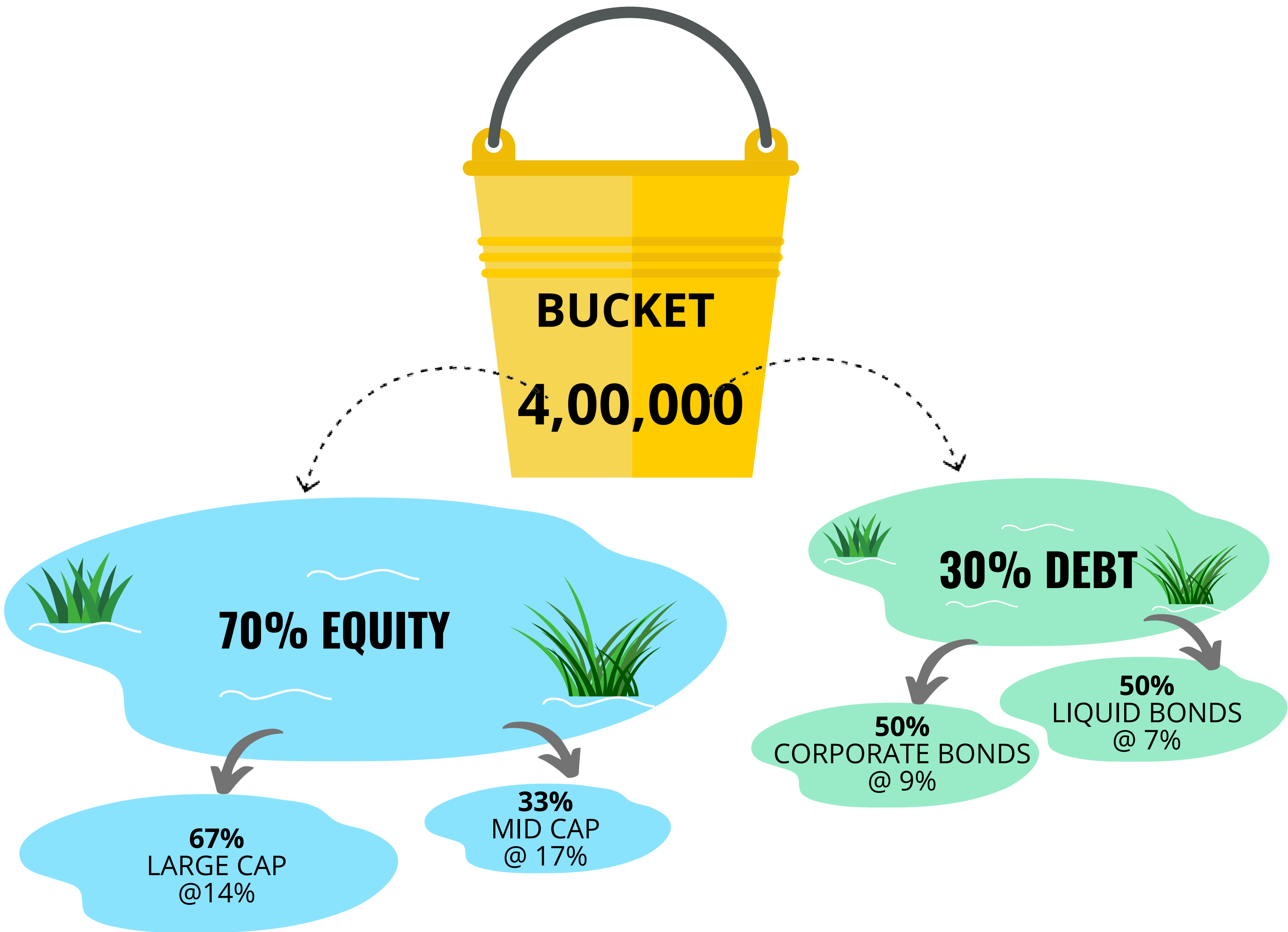
We know the expected rate of return, time period and the total value we need to fulfil the goal. We need to find out the 'investment' i.e. the amount we need to put in today. We will do this with a trial and error method. Enter time period and the expected rate of return. Now experiment by entering different amounts in the 'investment' column (based on monthly investment or lump-sum). Look at the 'Total Value' we get with the different amounts. We want to try with different 'investment' amounts until we get a total value that is closest to the fund requirement to fulfil the goal.

There is a small trick here i.e. the model assumes that we will be earning the given 'expected return rate' throughout the journey. However, we will be earning lower returns for shifting our money towards safer assets later So, the 'investment' amount that we calculated using the above method, will be amped up by adding 10% to it which will be the final amount to be invested every month to meet our goal.

EXAMPLE

Let us say we have a goal that is to be met in 6 years. We need Rs. 4 lac for the same. We have decided to invest 70% in equity and 30% in debt.

For equity, we will be investing 67% in large-cap funds and 33% in mid-cap funds. Large-cap has a 7-year category average of 14% and mid-cap has an average of 17% p.a. For the debt, 50% will go in corporate bonds and the rest 50% will go in liquid funds. Corporate bonds give a return of 9% and liquid funds return 7%. To find the expected rate of return we will calculate a weighted average of returns. There are 3 steps for this. First, calculate the expected return of only equity. Second, calculate the expected rate of only debt. Lastly, use these two to calculate the overall expected rate of return.



EXPECTED RETURN OF EQUITY

A × A + B × B

WEIGHT OF CATEGORY A		RETURN OF CATEGORY A		WEIGHT OF CATEGORY B		RETURN OF CATEGORY A
67%	x	14%	+	33%	x	17%

= 9.38% + 5.66% = 15%

'Weight' refers to the allocation made to that asset category and 'return' refers to a 7-year average return

EXPECTED RETURN OF DEBT

CORP. BOND × CORP. BOND + LIQUID BOND × LIQUID BOND

WEIGHT OF CORPORATE BOND		RETURN OF CORPORATE BOND		WEIGHT OF LIQUID BOND		RETURN OF LIQUID BOND
50%	x	9%	+	50%	x	7%

= 8% =

'Weight' refers to the allocation made to that asset category and 'return' refers to a 7-year average return. Similarly, if there are more than 2 categories, keep adding them in the formula.

OVERALL EXPECTED RETURN

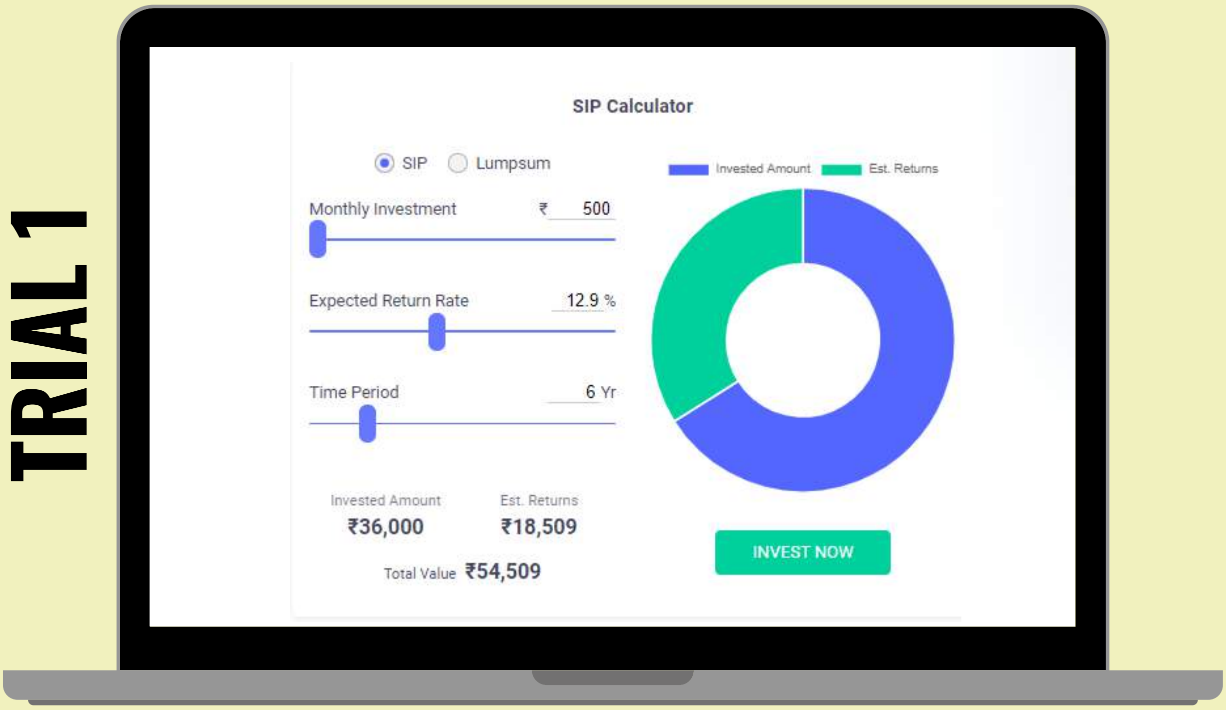
EQUITY × EQUITY + DEBT × DEBT

WEIGHT OF EQUITY		RETURN OF EQUITY		WEIGHT OF DEBT		RETURN OF DEBT
70%	x	15%	+	30%	x	8%

= 12.9%

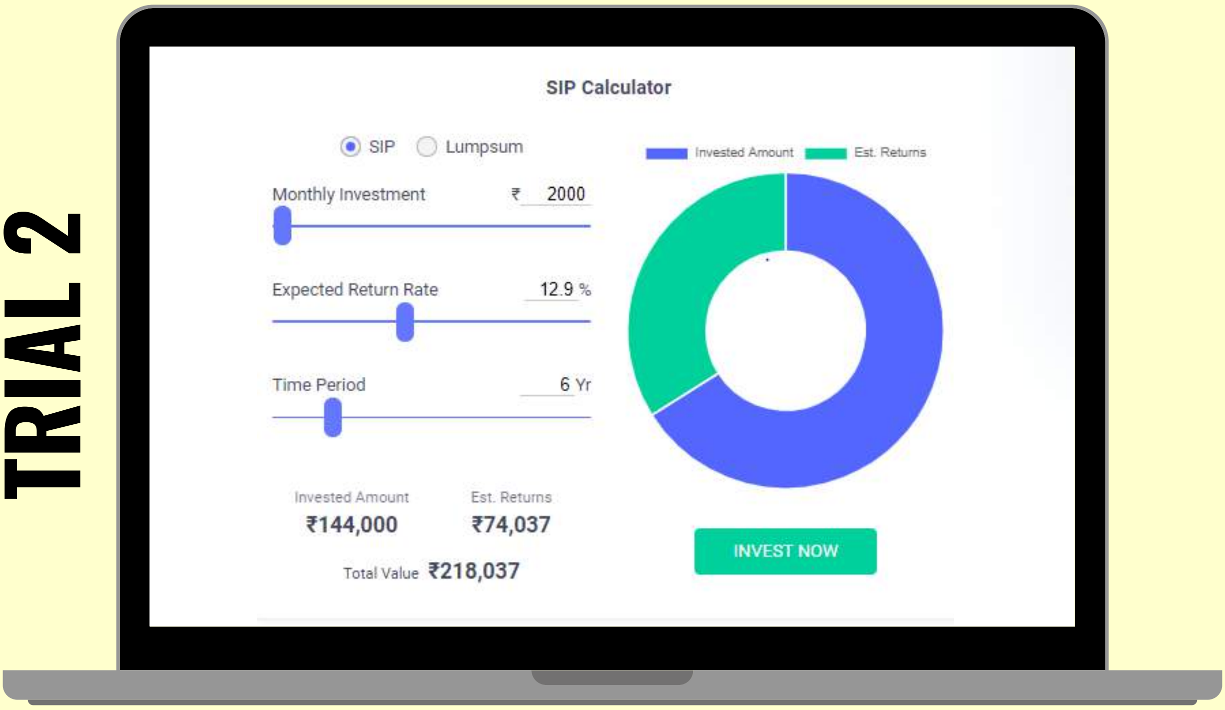
So, the expected return that we will enter in the graph is going to be 12.9%. Note that whenever we do any kind of calculation for weighted averages, the sum total of all the weights used the formula should be 100%.

TRIAL 1



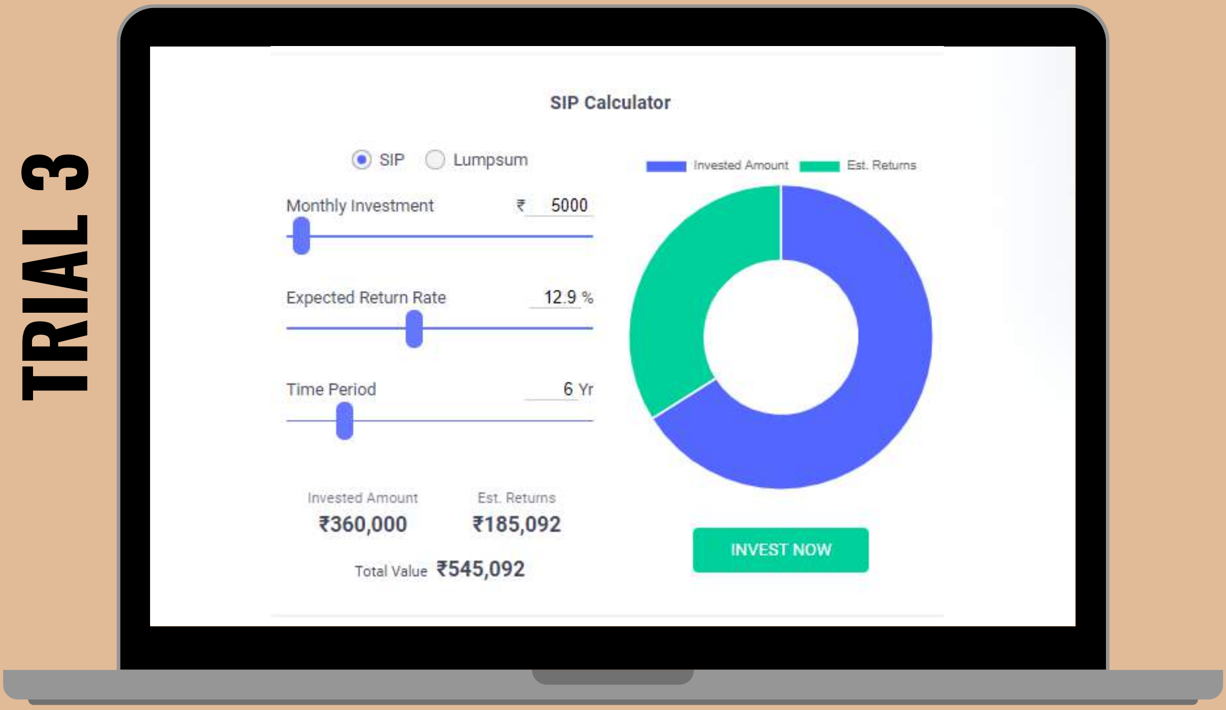
If we invest INR 500 every month, the total value comes up to INR 54,509. This is much lower than what we need. So, we will increase our monthly investment.

TRIAL 2



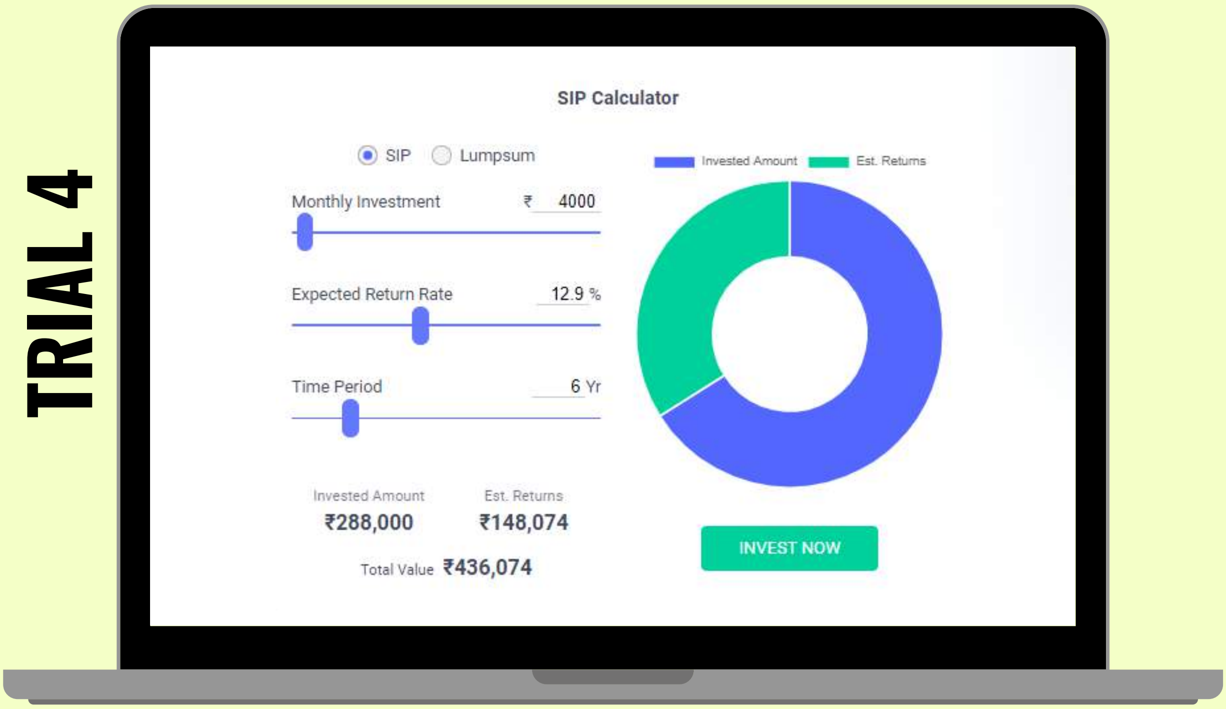
If we invest INR 2,000 every month, the total value comes up to INR 2,18,037. This is still less than what we need. So, we will increase our monthly investment.

TRIAL 3



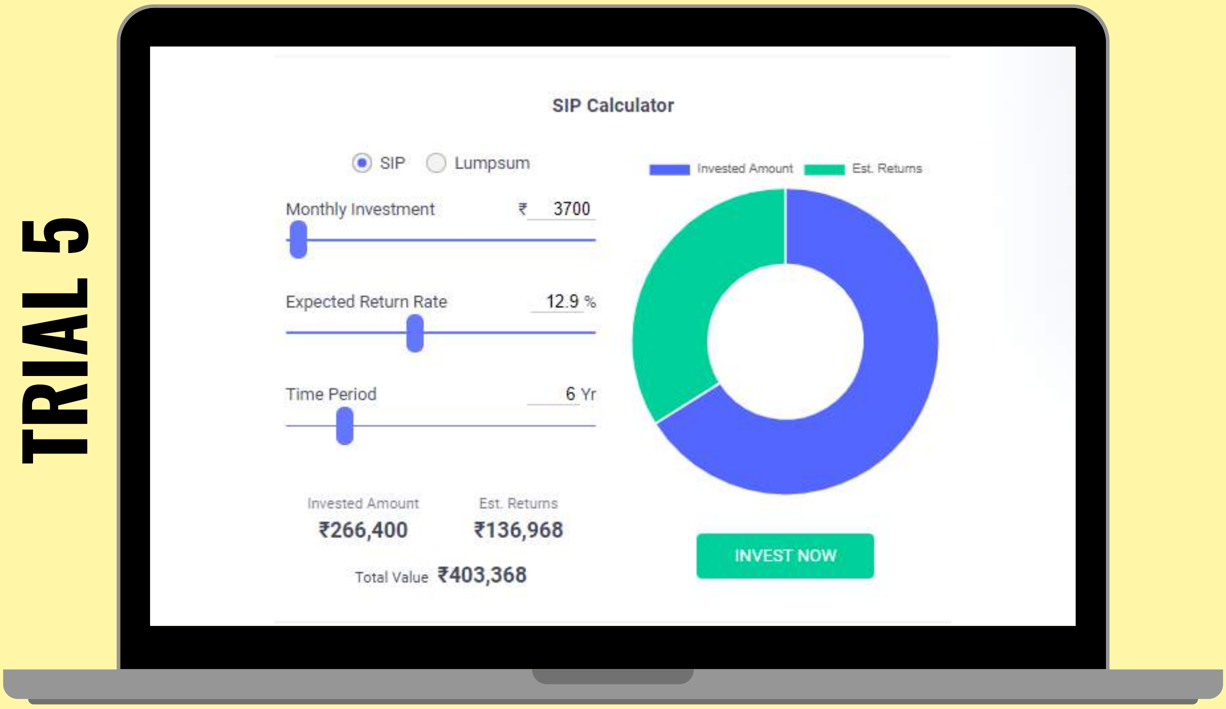
If we invest INR 5,000 every month ,the total value comes up to INR 5,45,092. This exceeds the amount that we need. So, we will decrease our monthly investment.

TRIAL 4



If we invest INR 4,000 every month, the total value comes up to INR 4,36,074. This is closer to the amount that we need. So, we will decrease our monthly investment.

TRIAL 5



After various trials & errors, a monthly investment of INR 3700, gives the closest estimated amount that we needed. Hence, we will go with INR 3700, after adding 10% to it .

We adjusted the monthly investment multiple times and then concluded that Rs. 3,700 is closest to have an ending value of Rs. 4 lacs. Now, we will add 10% to Rs. 3700 i.e. Rs. 4070, so Rs. 4100 for simplicity. Rs. 4100 will be split 70-30 between equity and debt respectively, Rs 2900 in equity per month and Rs. 1200 in debt per month. After this, we can divide this money further based on the categories that we had decided.

This is how we determine the amount that we need to invest today to meet our goals. We have to follow the order of priority so that we first allocate resources to the high on priority goals and then to less important ones. We will also consider timeline implications of the same.

Re-adjustments and calculations have to be made again every 2 years and re-do the allocations for all goals. The is because our weightage of assets keeps on changing and therefore the allocation towards each goal and mutual funds needs to change and adapt accordingly.

For lump-sum, we will use a similar method. Instead of regular monthly investments, we will invest a larger amount initially and raise it over the years. Use the SIP calculator to determine the amount of investment required initially. However, remember that we face valuation risks here. We might end up buying when the market is too expensive and as a result generate very low returns. This is why we are better off using SIP or STP framework.

If we are unaware of our major goals, as is the case with many young people in their 20s, then we will invest the amount for general portfolio growth and when the goals become clearer, we will re-allocate the funds accordingly. This can also be done for those who have extra resources even after planning for all their goals.

For this, we follow a very simple approach to allocating between debt and equity. 100 minus current age will determine the percentage of assets that should go in equity while the rest in debt. So, if someone is 24 years old, 76% of the amount should go in equity-related funds and 24% shall go in debt-related funds. At the same time, if someone is 64 years old, they should invest 64% in debt and 36% in equity related funds. However, this is only suitable for general portfolio growth.

With this, our base plan is ready. We have created a base plan only using mutual funds and it is good to meet almost any financial goal. However, most people will not be comfortable with having only financial assets in the portfolio. As a result, we will add other asset classes in the base plan based on our comfort. Also, we will go through each element of the canvas and make adequate improvisations to the Lazy Financial Plan.

WORD OF CAUTION

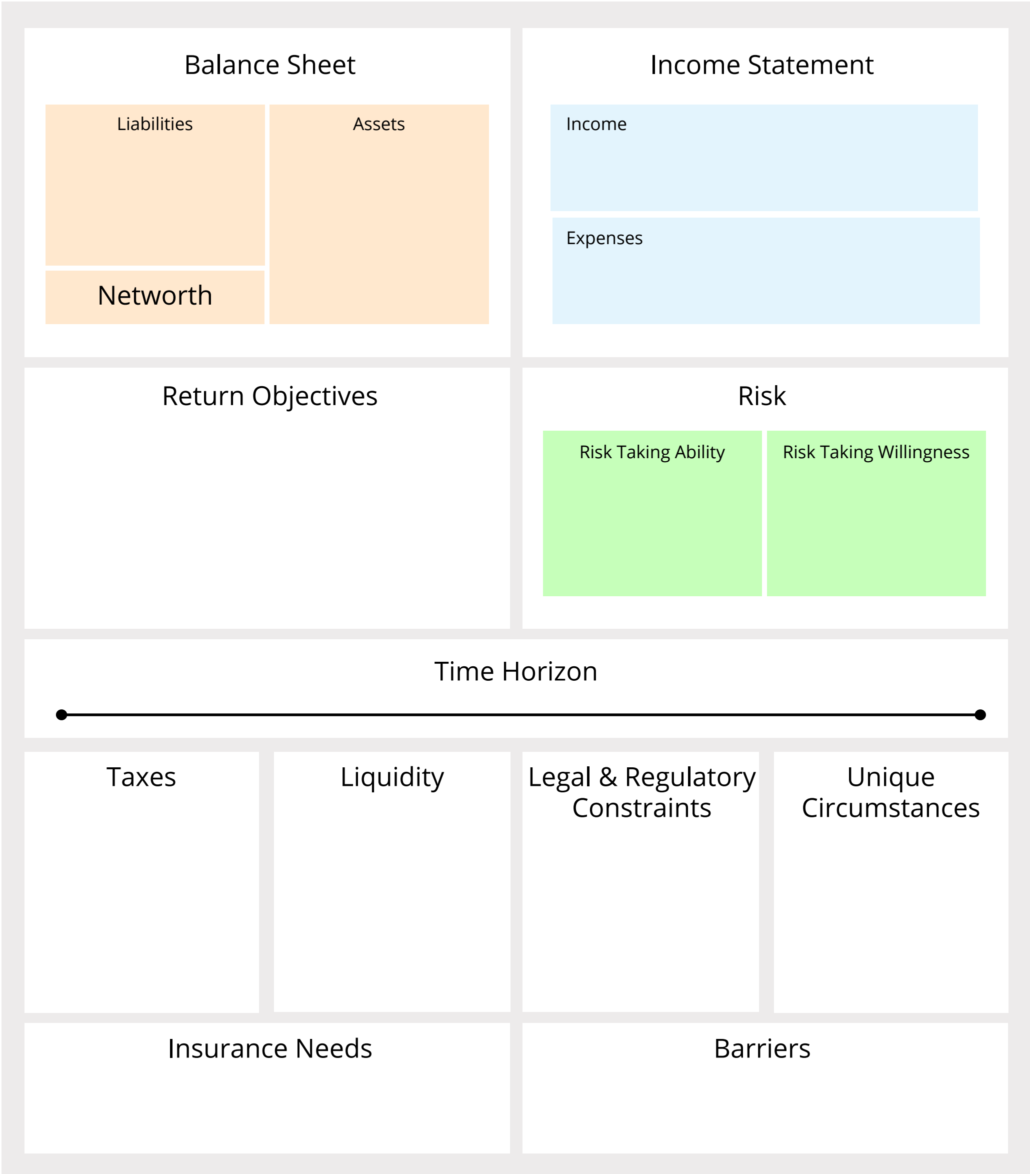
The profiling procedure for each major financial goal involves a lot of assumptions. We have estimated an amount for the goal to be met. We have then taken the 7-year category average to estimate future returns. We know that the actual returns may not be the same. Also, when we invest in assets, the value of the same may go up as well. It will be an emotionally and mentally painful journey. Moreover, unexpected life events will impact our plan.

The idea behind the Lazy Plan is to regulate the direction and steer the vehicle towards the goal. We cannot control the speed and distance. That is for the market to decide. However, the Financial Plan makes sure that we are at a place where we will be at least 80-90% prepared to meet the financial goal. Even if we are not ready 100%, we can manage the last 10-20% at the end from other sources. We can also over-perform our expectations. The exact speed and distance will only make a difference of 10-20%, i.e. under or above our expectations. However, if the entire direction or vehicle is wrong, we may be left far behind meeting the goal and may not be prepared when the time comes. With the Lazy Financial Plan, we make sure that we are in the right direction and we are prepared for most financial goals when the time comes, in a very structured way.

There will be times when the value of all our assets go down significantly and it becomes difficult for us to keep owning them, let alone investing additional money into it. It is in these times that we need to trust the plan, have faith and continue to follow it. This is an opportunity for us to buy assets at very cheap prices.Market prices have gone down numerous times in past but never have they stayed low. They always bounce back. It has worked historically and will work going ahead as well, it is the nature of the asset. Keep the faith and keep following the plan.

To improve the state of the other elements of RRTTLLU principle, we will have to make changes to the base plan as per the reality influences. Once we have done this, the next thing we will do is introduce other assets in the Lazy Financial to better suit our needs and make us more comfortable with the Lazy plan. These are the two last steps in the Lazy Financial Plan. With this, we will have created our Lazy Plan and we will be set to go. So, let us get started with other elements of Lazy Canvas.

LOOKING BACK AT THE LAZY CANVAS



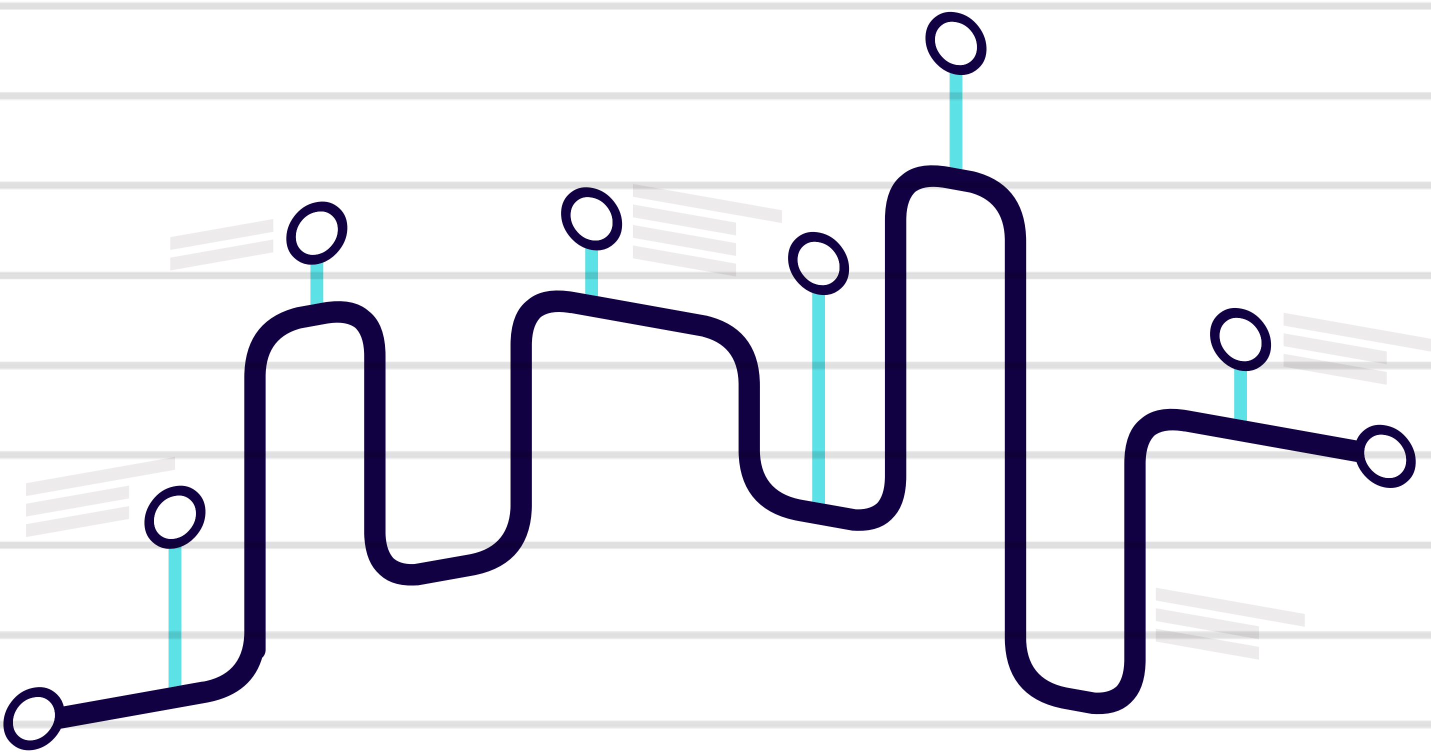
With this we have worked on the base plan. We have a base plan ready in place which is built mainly around the Financial Goals, Risk Taking Ability and Willingness and the time horizon and has only used Equity and Debt related Mutual Funds. The next thing we will do is, make improvisations on the base plan.

We will make changes to the base plan to better reflect the other elements of RRTTLLU principle. We will make changes as per the reality influences. Once we have done this, the next thing we will do is introduce other assets in the Lazy Financial to better suit our needs and make us more comfortable with the Lazy plan. These are the two last steps in the Lazy Financial Plan. With this, we will have created our Lazy Plan and we will be set to go. So, let us get started with other elements of Lazy Canvas.

So far, we have created a base plan but we have only dealt with personal income sheet, personal balance sheet, return objectives, risks and taxes to create our Lazy Plan so far. Now we will improvise the plan based on other elements of the RRTTLLU principle by making adjustments to change a few assets that we are not comfortable with. This is the last step of the plan. Let us begin with the RRTTLLU elements. Out of this, return objectives, risk, and taxes have been taken care of. Let us see how others impact the plan.

TIME HORIZON

We had divided the entire timeline into smaller segments based on financial events and life events. A very important goal that is coming up in 10 years, will take a back seat in terms of focus and we might end up focusing on a relatively less important goal that is to be met in 2 years. So, we might change the order in which we plan for goals based on the time horizon. Our short-term priorities change. Thus, we will stop here and make changes to the Lazy plan in a way such that it balances the 'urgent' and 'important' goals.

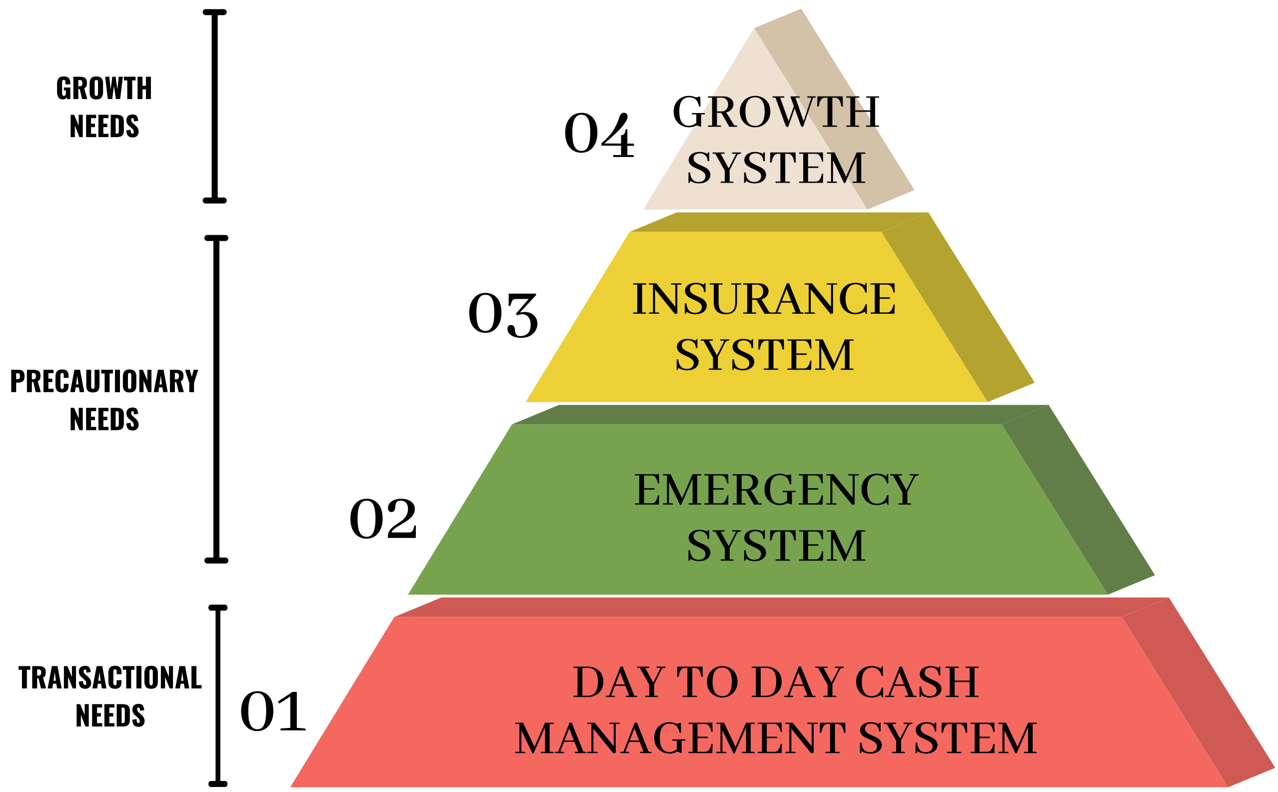


LIQUIDITY NEEDS

The lazy financial plan along with different tiers, is built in a manner such that the liquidity needs are automatically taken care of. We have three kinds of liquidity needs– Transactional Needs (for day to day transactions), Precautionary Needs (for emergency needs) and Growth Needs(for capital growth).

In our Lazy Plan, transactional needs will be taken care of by the cash flow system. Emergency system and the insurance system will take care of the precautionary needs. Lastly, the growth system takes care of general growth needs. We already know how money is managed in each of the systems.

Any unique circumstance not reflected in our lazy plan will be added. If we have any special requirements of liquidity, we will move resources to more liquid assets. For instance, we might have a larger emergency system required if a family member has a chronic disease. Such circumstances need to be reflected in the Lazy Plan.



LEGAL AND REGULATORY CONSTRAINTS

It is quite impossible to know all the legal and regulatory constraints from the beginning. Once the complete plan, we can conduct a review to ensure that all the parts of the plan can be followed without any legal or regulatory restriction. If there is any part that is not permissible, we will have to replace that part with alternatives. However, all assets that we discussed are open to the public and can be invested in by most individuals.

UNIQUE CIRCUMSTANCES

Lastly, we need to assess any unique circumstances that we have that are not reflected in the Lazy Plan. We will make changes to the plan accordingly. For instance, we might have an emotional attachment to certain assets, or we might have an ancestral property that is disputed etc. In such cases, our plan should not involve a sale of these assets. Or if we are not comfortable with asset classes like equity, even after consistent education and consultancies, then we will replace all equity investments with alternatives. In the end, we should be comfortable with the plan.

REALITY INFLUENCES

We had identified a set of six hurdles that come in the way of following the financial plan. These include family pressures, black money, fear factor, and so on. We need to tweak the plan and make changes as per the hurdles that affect us.

We understand that the changes made at this stage can be significant and the result can be different from the base plan. However, after these changes, the plan is much more efficient and customized for our needs. Next, we will adjust the assets based on our preferences and comfort.

ADDING OTHER ASSETS TO THE MIX

So far, our Lazy Plan mainly consists of mutual funds with a few adjustments. The plan at this stage is completely fine to meet all our financial goals. However, not everyone will be comfortable putting their entire Investible Portfolio into financial assets. Many would want to invest a larger proportion to those assets they are comfortable with. Here, we will add various other assets to the base plan to make the plan more comfortable. Let us see how each asset class can be added to the portfolio.

FIXED DEPOSITS

Fixed deposits can be used to meet any goal that is due in less than 2 years. It is a substitute for money market and liquid funds. Fixed deposits have similar returns to these and can be withdrawn prematurely as well. Fixed deposits can also be used for emergency system cash.

However, we should be careful to select a safer bank for fixed deposits. Also, we will avoid putting all our life savings in fixed deposits. These are safe but produce very poor returns and as a result, are not ideal in the long term scenarios.

DIRECT EQUITY

Direct Equity has the same risk-return characteristics as an equity-related mutual fund and an ETF. If practiced appropriately, the former gives a better return than later. This is because mutual funds also charge an expense fee that reduces the effective return. However, direct equity requires skill and time. We will opt for this route only if we have adequate skills and time to practice the same.

If we have the skill and time and we are willing to put these two to work, then we can replace the equity mutual fund component with direct equity. It is expected to question the extent of it. If we are completely confident about our skills and have been practicing the same for at least 10+ years, we can replace up to 100% of the Equity Mutual Fund component with direct equity. Here, the complete risk of selection and the responsibility of return is on us.

However, if we are not 100% confident, we can substitute a smaller portion of the equity funds with direct equity, say around 20-30%. It is subjective to our comfort and confidence. Remember that overconfidence in this case will cost us a lot. For most people, it is better to avoid direct equity. Note that short term 'trading' (buying and selling within a few days) does not form a part of direct equity investments.

Secondly, investing based on tips, recommendation from friends or brokerage firm etc. are also not a part of direct equity investing. It is a faulty process. We do not know the underlying reasons for buying the share. The conviction is borrowed and we will want to sell the stocks the moment prices go down and incur huge losses. A faulty process that might have worked in the past does not mean it will work in the future.

Direct equity investing involves understanding the industry, business, financial, valuations etc. in and out before taking an informed decision based on various factors. This is a time-consuming process. So avoid shortcuts and sign up for direct equity only if you have the required skills and time.

FIXED INCOME

Same as direct equity, fixed income assets can replace the debt mutual fund component in the portfolio. We can replace up to 100% of the debt mutual funds that are not required for the next 2 years. However, this also requires skill and time and only those who have been practicing this for 10+ years now should be doing it.

There are a few obstacles when we invest directly in fixed-income assets. First, these are generally sold over the counter. This means there is no market place for the same and we have to manually find the buyers and the sellers. So, a simple purchase decision becomes very difficult to execute.

Second, fixed income assets have to be bought in 'lots'. This means one cannot buy one bond, instead, a specific group of bonds need to be bought. For example, 5000 bonds make a 'lot'. The lot size can change. This implies that large amounts need to be invested in a single bond and hence diversification becomes difficult. Mutual funds can overcome these two problems in a very systematic manner. They have industry networks to find buyers and sellers. They manage large funds which helps them diversify the portfolio despite large lot sizes. As a result, for most of us, investing in fixed income assets is better done through mutual funds.

REAL ESTATE & REITS

We understood real estate as an asset class earlier. It is illiquid, needs a higher amount of investments and it is a cumbersome process to buy or sell it. On the flip side, it is a physical asset and hence psychologically comfortable for many to own. People have a high affinity with it and understand the asset well It can also consume black money which is an attraction for many. Lastly, real estate gives recurring rental income.

Real estate that is required for consumption i.e. when someone intends to open a shop or wants to buy a house. Buying these assets should be treated as financial goals and then the asset should form a part of support assets and not an investible portfolio. The investment value of the asset is a side benefit.

From an investment perspective, debt and equity combinations perform better. However, people prefer real estate as it is psychologically more calming. In such a scenario, a person can substitute up to 50% of their equity component with a real estate component. This means if the equity component should be Rs. 50 lac, they can invest Rs. 25 lac into real estate. However, we have seen plans with the entire equity component being replaced by real estate. It is just about how comfortable people are with different assets. This is not the optimal utilization of capital, but people still do it and it works well for them if the original asset base is sufficient.

Also note, 'Trading' of real estate does not form a part of 'Investing' in real estate. Trading refers to buying and selling of an asset within a few months just to cash in some profits. The traditional 'Buy and Hold' approach is what we consider while investing in real estate. We want to invest our money for at least a few years.

A better way to buy real estate is with the use of leverage. Buying real estate for 100% cash is not a good idea when it comes to the rate of returns. From an investing perspective, it is always advisable to buy real estate with a part of it coming from leverage i.e. debt. We understood its math' and that it multiplies the returns. However, this again is a personal choice and if we are comfortable without leverage, and it still meets our goals, then so be it.

Even though people understand the asset much better, still it requires skill and time and we need to consider the same. Also, we can consider REITs to get exposure in real estate without having the requirement of skill and time.

Having real estate in a portfolio has more to be with comfort than its return potential. It can be avoided completely if one is comfortable with financial assets alone. For most young people in their 20s, it would be best to avoid real estate.

MUTUAL FUNDS

Mutual funds form the base of our entire Financial Plan. They are sufficient to plan for any financial investment. With mutual funds, we get experts to take the decisions on our behalf.

The downside of mutual funds is that they are paper assets i.e. in exchange we only get certificates of units and it is not to everybody's liking. Secondly, mutual funds is still a developing concept in India and the Indian market. This means not everyone understands the asset class like they understand other asset classes like real estate, fixed deposits and gold. Due to the above two reasons, many individuals are not very comfortable with mutual funds, especially, those in their 50s and above.

Mutual funds are one of the most suitable asset classes in regards to its ability to meet financial goals. Different types of mutual funds ensure that our money is put to the most efficient use.

DERIVATIVES

We are including derivatives here, just to remind that derivatives are 'weapons of mass destruction'. This means they can earn sky-high returns overnight and lose the same amount overnight. With derivatives, we are exposing our portfolio to bankruptcy risks which is never a good idea. It requires complex systems and structures. We will stay as far away from these as possible. We will leave these for professional traders.

SMALL SAVING SCHEMES

The main objective of most of the small saving schemes is financial inclusion i.e. making financial services and products available and accessible to those who do not have it. However, for most readers of the platform, this will not be the case and can avoid those schemes that were introduced to ensure financial inclusion.

We have already invested in NSC and PPF to take advantage of the tax benefits. Small saving schemes can be used to substitute debt component if there is extra room under the Section 80C deduction.

Besides financial inclusion and tax savings, certain other small savings schemes serve specific purposes. For instance, Sukanya Samriddhi Scheme is for the welfare of girl child and Senior Citizen Savings Scheme is for the benefit of senior citizens exclusively. So, one can substitute the debt element from their plan using these small saving schemes if the numbers are attractive for them. These are generally suitable for old and retired due to the benefits they offer. Revisit the list in the assets category and re-evaluate the suitability of various schemes that are suitable as per our needs and those that fit in our Lazy Plan.

NATIONAL PENSION SCHEME

We have already been introduced to NPS in great details while learning about the Growth System. It can be ignored by anyone below the age of 40 years. For those above the age of 40, they shall take benefit of the E-class till the age of 50 and then reduce E-class and increase G-class or C-class in the mix. NPS enforces discipline by imposing strict withdrawal limitations.

PROVIDENT FUNDS

Provident funds are compulsory for many. It ensures discipline over the long term. We will go ahead and maintain a balance between money that is being managed by us and money that is given to the government institutions for our retirement. This way we will be able to maintain a balance between returns and the safety of our portfolio.

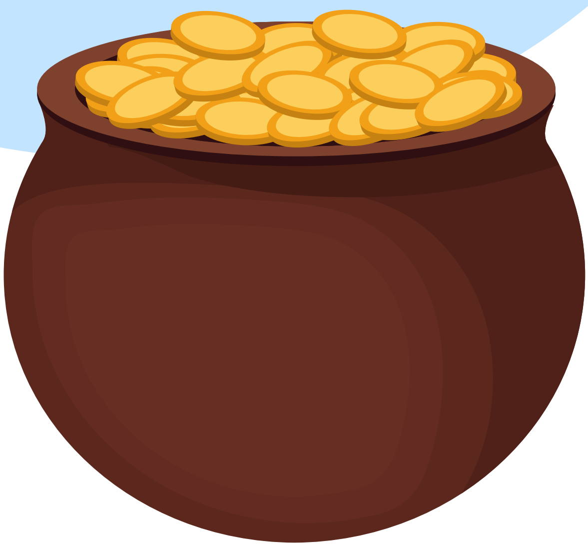
Earlier, we saw how to deal with EPF and PPF. These can substitute the long term debt component in our financial plan if there is any. By long term, we mean 7+ years. PPF should be the preferred investment asset in case we are planning for a 10+ year investment, using a fixed income asset. However, this is only suitable for those with extremely low risk-taking ability.

GOLD

We understood the long term investment performance of gold earlier. We saw that it is one of the most underperforming asset classes in the long term. However, it is something that is deeply built in the Indian culture and it brings a lot of social and consumption value along with the investment value.

Those looking to buy gold for its social and consumption value shall go ahead with the same. Buying gold should be treated as a financial goal being met. Gold purchased for social and consumption value should form a part of support assets and not an investible portfolio.

Anyone who prefers gold and is ready to accept the low returns can go ahead with it if they have a larger asset base to invest. They must buy gold bonds and not physical gold. Gold can neither replace equity nor debt. As a result, gold should be bought by replacing both equity and debt in the same proportions in which they are present. We will cap the gold investments to a maximum of 10% of the investible portfolio. Gold is not the most optimum long term investment and in the shorter term, it is quite volatile which makes it difficult for us to plan goals using gold as the base asset.

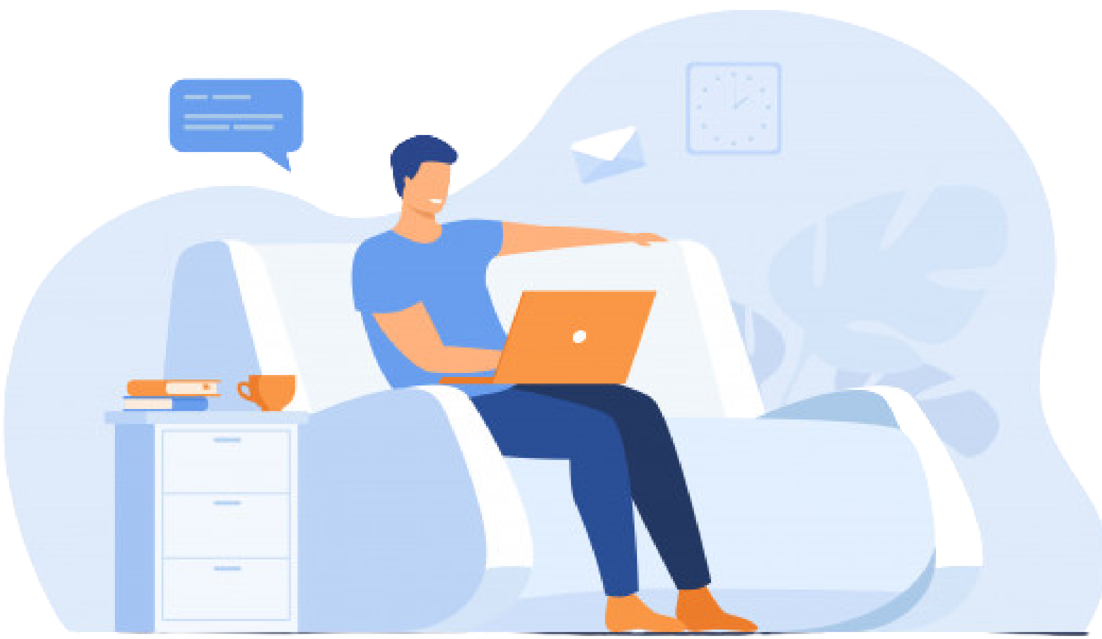


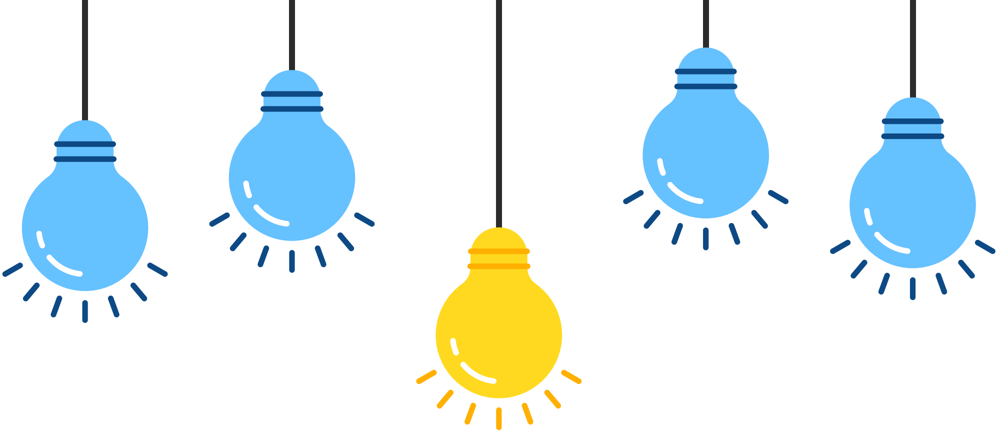
QUEST FOR COMFORT

We now know how we will add other assets to the base plan that we had created. We will add/ reduce/ substitute assets based on our comfort and willingness. We will invest in the assets we are comfortable with, the ones we can follow through for multiple years. However, we will also keep in mind to draw a line and not push this too further and in the name of comfort, create a Lazy Plan that does not meet goals itself. We will follow comfort, but not at the cost of meeting financial goals.

The idea is to keep it simple. We do not want exposure to all sorts of fancy assets like Bitcoins, etc. Simple works great and makes sure that we meet the financial goals.

Investing is simple, but not easy. All the rules of investing have been known for ages and they have proved their efficiency repeatedly. However, it is not easy for people to follow. The secret to a successful lazy plan is in its execution. The entire Lazy Plan has to be lazy and simple. It has to be one that we can follow thoroughly. With this, our lazy plan is complete. Let us quickly revise what we have done throughout.





SUMMING IT UP

Let us revise what we have done to reach the Lazy Plan. We initiated the process by creating a Personal Income Statement and Balance Sheet. We followed it up by conducting basic checks to understand the health of our finances. Then, we identified our return goals, quantified them, prioritized them and judged their flexibility. We checked our risk-taking ability and risk-taking willingness. We then evaluated ourselves on other parameters of the RRTTLLU principle. Next, we evaluated the risks we face and the insurance needs that we have. Lastly, we identified the six factors that act as barriers to financial plans. With all these elements, we filled up the lazy financial canvas. This completed the profiling stage.

In Part 2, we studied the various available asset classes. We understood suitability, risk-return characteristics, tax benefits etc. of every asset.

In Part 3, we started working on the Lazy Financial Plan. We divided the entire plan into four tiers.
In the first tier, we created a Cash Management System where we segregated money for our day to day expenses and our investments. Then, we created an emergency system where we saved 8-9 months worth of our income. Next, we created a full-fledged insurance system where we bought insurance policies that help us protect our lazy plan from any leakages or major losses.

After that, we proceeded towards the growth system. Here, we created a base plan using mutual funds only and selected the asset mix (equity and debt) based on the time horizon. Then, we identified the categories within equity and debt. Next, made improvisations to the base plan based on the elements of the RRTTLLU principle and based on other asset classes we are comfortable with. With all these, we created a Lazy Plan that is exactly tailor-made to suit our needs.

FOLLOWING THE PLAN

Congratulations on creating a Lazy Plan. The plan is all set to go. Now that we have completed the easy bit, it is time for us to move forward to the difficult part i.e.the execution. Here, we need to keep a few things in mind.

DO NOT CHANGE AS PER MARKET PRICES

There will definitely be times when the market prices are soaring high and there will also be times when the market value of all our assets goes down and holding them will become a challenge. We might want to sell it all and move the money to a Fixed Deposit or a fixed income asset. But we will not give in! Market values have gone down numerous times and have come up every single time. With SIP, we are anyways buying and selling at average values. If we sell when prices are going down, we end up selling at lower valuations, and booking loses.

If anything should be done, the SIP amount should be increased when markets are going down. This is an opportunity for us to buy more assets at a cheaper price. If one is not comfortable with this, one should at least refrain from discontinuing the SIP. Do not take decisions based on market prices.

NEW INFORMATION COMING UP

We will never have full information when we are creating the Lazy Plan. In our 20s, we will not be aware of the major life goals. In our 30s, we will not be certain about our employment status at the time of retirement and when we are in our 40s, we will not know the expenses that we will have to incur for our children and our parents and so on. We will never be sure about any emergency that is likely to arise in the next few days, or about our insurance claim that is being rejected.

The nature of this art is such that information will never be complete. We will plan with whatever information we have at that moment and then keep making changes to the plan as things evolve from there.

THIS IS A DYNAMIC PLAN

As per our prior discussions, this plan is indeed very dynamic. We will keep updating the plan as and when new information crops up or when we change our mind regarding assets. If we do not keep on making the changes, the plan will become obsolete very soon. The idea here is to have a plan that takes us in the correct direction and we can fine-tune the plan as information becomes clearer.

REBALANCE EVERY 2 YEARS

Ideally, the plan should be rebalanced at least once in every 2 years. This means we will have to re-work the ratios and re-allocate the assets. We will make changes to the portfolio as the time horizon to meet each goal would have reduced. Few goals from Bucket C would have moved to bucket B and some from Bucket B would have moved to Bucket A. So to reflect the changes, we will rebalance the portfolio at least once in every 2 years.

BE REALISTIC IN PLANNING

At the planning stage, we at times follow an idealistic approach i.e. what we would ideally do in a situation, but we end up doing something else in the real life.

This is something that makes many Lazy Plans inefficient and renders them useless to meet goals. We will try to reduce this distance between realistic and idealistic mindset for us to the bare minimum. The more realistic plan we have in place, easier it is to follow through.

DISCIPLINE

Discipline is in-built in this plan since the very beginning. We need to be honest with ourselves when we evaluate ourselves and create a profile. Next, it is important to segregate your income for expenses and investments, make all necessary investments in time, to create a plan and follow it throughout, overcome all the temptations and refrain from responding to changes in the market price of assets. Financial discipline is something that most people find it difficult to master, but those who do, never miss out on their goals.

CONCLUSION

With this, we end our discussion of the Lazy Plan. We will create a custom Lazy Plan based on our needs. We know that the plan will never be perfect as we will never have complete information. We will create a plan in the correct direction and then keep making changes to it as information becomes clearer. We will seek help when we get stuck rather than solving it ourselves. Before we end our discussion, here is an overview of the few basic things that are significant enough to be kept in mind.

We need to create a plan that is as simple as possible. Complicated plans sound and feel very intelligent, but in reality, they are extremely difficult to execute. Next, we will ensure that our plan is sustainable and refrain from doing unreasonable things that cannot be continued for a long period.

Understand that there are no right answers when it comes to personal finance. Different people follow different routes to meet their goals and till the time they can meet the goals, it is all good. So, instead of comparing and analyzing other people's choices, we will figure out the most suitable method that works for us. The process is undoubtedly highly subjective and we will have to respect the same.

SIMPLE

SUSTAINABLE

NO RIGHT ANSWERS

NO HARD & FAST RULES

PATIENCE

Next, there are no hard and fast rules. We may see something worked in past, or some strategy is working for one of our friends, and so on. However, all of these do not mean that the method will work for us also. There is no rule that is being followed here i.e. we cannot guarantee anything when dealing with personal finances. Our focus is to stay ahead of the average and with a structured approach, we are doing that.

NOT A ONE TIME THING

It requires a lot of patience. Creating different tiers and then the systems as per the Lazy Plan takes a lot of time, sometimes a few years. We understand that the Lazy Plan is not a one-time thing. It is a continuous effort that should become a part of our lifestyle. The fruits of the stretched out patience are manifold.

PAST EXPERIENCES

Past experiences play a very central role in determining our preferences in terms of assets. If someone has had a poor experience with an asset class in the past, it takes a lot of effort to get them to invest even a penny in that particular asset class. We will deal with each of these factors that might come in the way of following the Lazy Plan in a very systematical manner.

We need to ensure that the plan we are creating has to be executable. We will not give in to myths that are floated around the world of finance. We will create a plan that is based on logic and is tailor-made to our needs. Lastly, we also need to understand there is no financial plan that can substitute ‘earning more’. Unfortunately, no book on the planet can teach us how to earn more. To earn more, one must invest in his skills.

However, all we can do is manage what we earn in a very systematic and efficient manner and make sure we meet our financial goals. This is what the Lazy Plan is all about. With this, we come to the end of the book. It is now the time indeed, to start practising and creating a plan for ourselves. This is an amazing foundation for us to base our Financial Plan. Congratulations on coming to the end. We have taken a huge step towards Financial Intelligence!

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