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16 PERSONAL FINANCE PRINCIPLES EVERY INVESTOR SHOULD KNOW.

MASTER YOUR FINANCIAL LIFE
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Written by **Manish Chauhan**

Bestsellers 18

16 PERSONAL FINANCE PRINCIPLES EVERY INVESTOR SHOULD KNOW.

Financial (Products will change…

Personal finance tools will change…

Financial planning models will change…

Strategies RARELY change

and

Principles NEVER change!.

This book is based on principles of personal finance.

DISCLAIMER

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Testimonials

“A must read for people who are starting their career fresh out of college. If I would have read it 6-7 years back when I started working I would have avoided so many mistakes that I committed in investing”
-Reader 1

“One needs some courage to go through this book. It first shakes you up from your slumber (financial laziness), then squeezes off you, your mislearnings about saving and investment”
-Reader 2

“Only One Word….WOW…!. I have been searching a lot and met a lot of finance people. None have quenched my thirst for finance know-ledge”
-Reader 3

One thing which this book stand apart from others is that it is written in dead plain and simple language that everyone can understand
-Reader 4

What an excellent book…. This is my shortest expression on completion of reading the book
-Reader 5

This book is- Simple, Powerful, Relevant, Thought Provoking, Insightful, and Out of clutter-much needed effort towards empowering a Common Man
-Reader 6

Acknowledgement

To most readers, a book often appears to be the creation and handiwork of just one person – the author. If the book is appreciated, all the credit goes to this one person. But let me tell you that there is no way that this book could have become a reality, without the support of many people. I would like to take this opportunity to thank each of those people here.

I would like to start by thanking all the readers of my blog. Over the years, my readers have approached me with thousands of queries, appreciated my advice and enabled me to learn from their doubts. They have given me the opportunity to help them in myriad ways. Each question they asked, each suggestion I have offered and all the feedback that I have received, have contributed to the creation of this book. So, they are the first ones whom I would like to thank for making this book a success.

I would like to also thank Nandish Desai, my teammate, who has guided me all along and contributed substantially to some chapters. Without his inputs, this book might not be what it is today. He has given me deep insights and extraordinary motivation and I will never forget how he has pushed me all along to give my best.

I would also like to thank my teachers, my parents and my wife for all the support they have given me, especially at times when I needed them the most. I would like to say big thanks to Joanna Punjabi for editing this book and giving a polished look to each line; she has done a wonderful job and it has contributed greatly.

Lastly, I would like to thank Network18 for publishing this book and showing confidence in my work.

Manish Chauhan
Financial Coach

Preface

"A man's reading program should be as carefully planned as his daily diet, for that too is food, without which he cannot grow mentally."

- Andrew Carnegie

There is a lot in Andrew Carnegie's statement. The first thing to note are the words "reading program". It is missing in the area of personal finance. Ask yourself if you have carefully planned your personal finance reading program or not. How many books have you read so far to develop mastery in the area of your personal finance? If you want to achieve that mastery, this book can be your first step.

Having this book in your hands is akin to making a commitment to grow your personal finance acumen. I can say this from my years of experience as a blogger. I am very clear that if you carefully plan your personal finance reading program, it will bring about that BIG change which you seek in your financial life. At some point, when you are reading this book, it will look straight into your face and wake you up; it will show you the missing elements of your financial life.

Most people graduate from college and go in search of their dream job or venture. Many a times, they do get that dream job and start earning money that can make their life comfortable and exciting. Getting a dream job was all they planned for. But getting a well paying job is not the end; it is just the beginning.

People get caught up with various big and small experiences that they encounter in the first few years of their career; they have no idea that managing money is as important as earning money. Lack of direction leads to either accidental growth in money or it invites unavoidable bad experiences in money management and investments; some forced learning also takes place in life when one buys various financial products from friends and relatives. **All this can be avoided if you carefully plan your personal finance reading program.** This book can act as an action guide to you. It will help you make strategic choices, which can take you from where you are to where you want to be in future.

While you read this book, you may experience some tremors under your chair; the tremors are asking you to take some action in your financial life.

Right about now you may feel the first tremor: I have some good news and bad news for you…

The good news is that you are your own boss when it comes to personal finance; the bad news is that you are your own boss when it comes to personal finance. The one person who is coming in between you and an extraordinary financial life is YOU. While reading this book you will realize how you do that to yourself. But this book will also teach you to become more financially accountable to yourself.

There are only two outcomes for investors: either they reach their financial goals or they don’t. The bookwill act as a passive coach towards ensuring that you reach your financial goals.

Money is considered one of the most emotional subjects in the world. Money as a subject is never taught to us in schools or colleges and has a very limited space in our overall education system. But on the other hand, it is something around which our life revolves and evolves. Yet not much light is thrown on this subject.

It is said that when it comes to money, we all belong to the same religion. Money has the element of oneness in it. If the subject belongs to all of us how can this book belong to me.

This is your book, not mine; you own it. Read it as you want to, think whatever you want to think, make notes all over it… Just remember, you are spending your valuable time and energy reading it. Make that time and investment pay by taking some action that will mobilize your financial life to the next level.

That would be the best ROI you can receive from buying this book!

Manish Chauhan

Financial Coach

CONTENT

Chapter 1

BURNING THE JUNGLE

Over the last couple of years, I have come across thousands of investors who wanted that one secret for wealth creation; that one secret which can change their financial lives. Everyone is looking for that magic formula which will transform their wealth creation process. Sadly, there is no single thing in life which can make it happen; but one thing comes very close. And I am going to share that open secret with you. I call it an “open secret” because its not hidden; you’re probably aware of it…you just have to recognise it, that’s all! That secret is “Start investing early”. In the next few pages, I want to make you aware of the power of early investing and the impact it can have on your financial life.

These days, common Indian investors are worried about how to save money to meet financial goals. These could be the finances required for their child’s higher education, a nest egg for retirement, the money needed to buy a house… or any other big ticket dream on the horizon. When they think about the amount of money they would need after 10-20 years to fund a particular goal, it scares them! It starts to look like a daunting and unachievable task. For example, a man who is 30 years old today would require several lakhs after 20 years to fund his child’s graduate + postgraduate education. The big figure could be anywhere between 40-50 lakh, who knows! If you consider all the expenses you have to shell out right from your child’s primary school till she completes her college degree and add to that living expenses, it can total up to an amount which might literally give you shock. Think about it.

So what is it that this common investor should have done to make the whole process of wealth accumulation much, much simpler? Many think that the answer lies in some “hidden” knowledge or a big secret or just plain luck. While all of these may be important, they are not the key! The key to accumulating wealth is unbelievably simple – just start investing early in life. This doctrine is so powerful that it sometimes even discounts the mistakes or stupidities you make in your financial life. It’s such a “common sense” thing that it is not visible to the common investor, they just over look this simple fact.

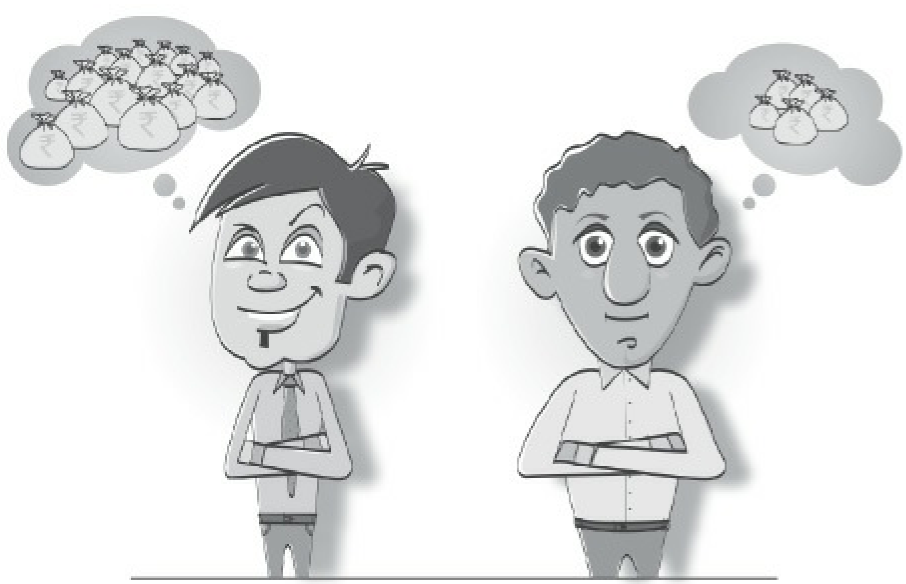
Are you procrastinating?

A lot of people procrastinate, some by choice and some due to ignorance. They always think that starting with a small amount would not make much of a difference, when they aim to accumulate great wealth. They feel,

How much can saving of few thousands per month impact my goals which require lakhs and crores!"

Imagine a person who wants to accumulate 2 crore by the time he retires, 30 years from now. He may not be motivated to save Rs 1000 or Rs 2000 today as it looks too small to have any impact on that BIG goal. He can't see the power of small investments and how these can contribute to his final goal of accumulating Rs 2 crore. But let me show you some examples, which may look unbelievable to a common investor. These examples will motivate you to read further and find out what you may not know yet. Then we can move deeper into the ocean of "early investing" and "the power of compounding".

Example 1



Imagine two friends Ajay and Vijay. Vijay invests Rs 1,000 per month for 30 years at 12% per annum, whereas Ajay invests Rs 2,000 per month for first 10 yrs at 12% and then just lets it grow for next 20 yrs. And Ajay is going to accumulate 45 lacs at the end of 30 years although he has contributed a total of 2.4 lacs during the first 10 yrs.

Vijay will accumulate only Rs 36 lakh, despite investing Rs 3.6 lakh over the 30 year period…

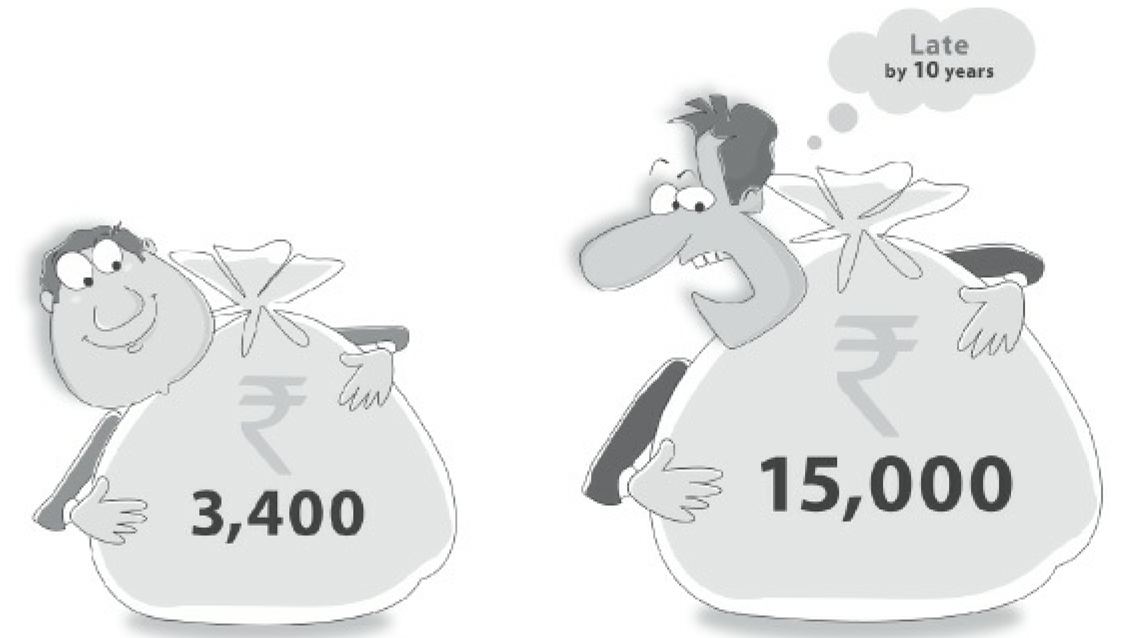
Even though Vijay invested more than Ajay, he was not able to accumulate more money than Ajay. This is simply because Ajay contributed more at the start.

Example 2

Suppose you have 30 years in hand and you decide to invest a certain amount every year, in a financial product that gives you a 12% return. You will collect a certain amount – principal and interest–after 30 years.

Now, let's say you reduce the investment tenure by half–from 30 years to 15 years, and allow the money to grow in that same financial product which gives you a 12% return for the next 15 years. The amount that you collect after 30 years – principal and interest – will be only 14% less than it would have been in the first case…where you contributed for all 30 years.

Example 3:



Investment required per month to generate 5 crores in **35** years, assuming a 15% return

Investment required per month to generate 5 crores in **25** years, assuming a 15% return

The above examples might have opened your eyes wide to what early investing can do to your financial life. Now let's explore why this is possible…

Assumption

From here on, whenever I refer to investing and compounding in this chapter, I will be assuming a capital of Rs 5,000 per month invested for a period of 30 years at a rate of interest of 15%, unless I state otherwise. I have chosen the rate of 12% as a benchmark because it is considered a standard return for equity over the long term. In case you don't understand all this, don't worry; just skip it and move forward. Don't let these assumptions create a block towards understanding the examples that are coming up.

The 12% return assumption is on products like Equity Mutual funds, Index Funds or stocks. Note that in this chapter when we refer to any investment with 12% return, its main investment in Equity Mutual funds, over long term.

Time in hand is like a powerful sword

> **"Start investing early. If you don't, you are committing a crime which you will pay for all your life…"**

When we coach people with regard to their financial life, we notice something: The biggest reason why their financial life is in a deep mess is not because of their lack of knowledge or their lack of earnings. In fact, most of them earn well and are pretty smart. will pay for all They are all successful at what they do. The biggest reason is that your life…" they have lost that part of their financial life which could have created magic - "the starting years". It all boils down to not having taken action early in life. Time is that one weapon which, if present in your financial life, increases your chances of financial success greatly. You can call it the **"Bramhastra"** of creating wealth.

I see a lot of people spending too much time worrying about money and wondering how their financial goals will be acheived. They spend so much time on things which matter so little - like "which is the best stock to invest in" or "which mutual fund should I put my money in" or "which policy gives the highest returns". In doing so, they are lost in the confusing world of personal finance and deviate from the only solution they should have implemented long back in their lives, which is starting to invest early!

When we start earning, we are generally single. We have less responsibilities and have ample ways of cutting down on our expenses. We are in a position to save a substantial part of our income. We usually have some years in hand before we get into a marriage and all the responsibilities that come with it. Instead of using that precious time and opportunity, a lot of us waste it thinking that we can always start saving later; perhaps when we have more money or when we get a job that pays better. But sadly, life is not like the 'Saas bhi kabhi bahu thi' serials, whose structure can change every week or with every episode.

Tell me frankly, how different has your life been from what it was last year or from how it was the day when you first started procrastinating over your saving and investing plans? Life does not change, it's we who have to change and take bold decisions. We always have some reason or the other to not save or make the effort to start investing early. Remember that 5 or 10 years lost at the start is a crime which will haunt you for the next 40-50 years. Don't commit this crime!

Creating long term wealth is like growing a tree

Have you ever planted a small sapling? One month after you sow the sapling, it may not look any different; but you will notice some changes after 3 months. After 2 years, it will probably have grown to a good size. Yet it would not be big enough to repay you by giving shade and fruits. When you see the same tree after 20-30 years, it will be so big that it's hard to believe that it started out so small. But to help it grow to that point requires a lot of patience, hard work and belief that it can happen.

Growing wealth is somewhat similar to growing a tree. We start small and keep investing for the long term. We may not be able to invest a lot in the beginning but we can increase our contribution when we earn more or start saving more, as life progresses. However, nothing compares to starting early in life.

> **"Early investing is very much like growing a tree…. If you take good care of it at the start, it will take care of itself later!"**

How does money grow and multiply?

Before we figure out how money grows, I would like to share with you an example which I call **“Fire in the Jungle”.**

Have you ever heard news of a whole jungle catching fire and everything getting burned down? Now imagine how it might have all started… Do you think someone went from tree to tree, burning each one down one by one? I don’t think so! Perhaps one can go from tree to tree and bush to bush and set fire to each one, one by one, to get the same effect, i.e. a jungle on fire… but you don’t need to work so hard! All you need to do is to make sure is that you fire up some of the trees to a self sustaining level so that the fire catches on and spreads to other parts of the jungle. There will come a point when it would be idiotic to burn up more trees because by the time you burn a single tree, hundreds of trees would be catching fire on their own! It’s called **“compounding”.**

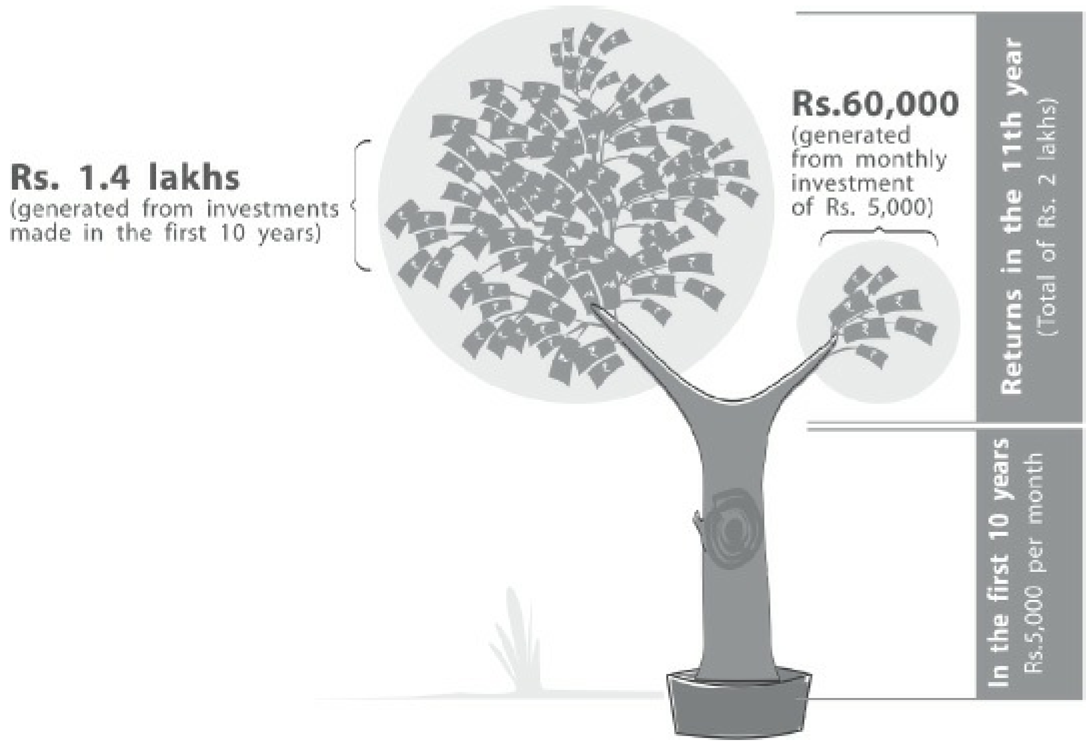
What on earth has this fire in the jungle to do with growing our wealth and starting early in life? It has a lot in common. The investments made in the early years of your life are the same as spreading a fire in the jungle… after a point, just like the fire compounded itself and spread so vigorously, your money will also grow to some extent and then the returns generated on it will be so great that your contributions will look small in comparison. A lot of investors miss this part and never act on starting early!

So now can you tell what makes money grow? The answer is “Money itself”! And obviously, we also need to help it to grow by investing it. When you start investing, your money starts getting accumulated and every year it starts generating returns which are added to the investments. While that return is a small amount in the starting years, over time it keeps on accumulating and then the interest per year becomes really significant.

Let me show you how…

Suppose you start out by investing Rs 5,000 per month for 30 years. In the last year (the 30th year) you will invest 60,000 from your pocket. However, the return for the 30th year itself would be Rs 18 lakh. Just imagine that! And guess what, out of this return of Rs 18 lakh, which you get in the last year, 12 lakh comes because of the contribution that you made in the first 10 years and the remaining 6 lakh comes from the investments made in the next 19 years.

It’s critical to understand why this has happened. Imagine your wealth as a Money-Tree, which was small when you started, but grew bigger in size over the years. At some point, branches begin to emerge and grow in all directions. Coming back to the example, your wealth at the end of the 10th year will grow to Rs 11.6 lakh. So visualize your Money-Tree; it has become bigger and it’s worth Rs 11.6 lakh at the end of the 10th year. What happens after 1 more year, i.e. the 11th year? How much more will be added to this Money-tree? There will be 2 kinds of additions. The first one will come from you, which is Rs 5,000 per month or Rs 60,000 per year. The other part will be the return generated on the wealth that has already been accumulated. This turns out to be around Rs 1.4 lakh. So the total addition in the 11th year will be Rs 2 lakh, out of which only Rs 60,000 was due to your contribution and the remaining Rs 1.4 lakh was generated by the existing wealth itself. Now, if you consider these two branches, the branch which is a result of returns generated from the existing wealth will be much much bigger than the branch which you contributed afresh. I guess you got my point here.



Now, if you fast forward to the 29th year, your corpus would increase to Rs 1.56 crore. In the 30th year, you will add another 60k from your pocket, but your own wealth will add a 12% return to it. And that would be close to Rs 18 lakh! You can actually skip contributing that 60k in last year and it won't really be missed. The best part has happened already, which is the accumulation of wealth in the early years!

The take-away

You will agree that the money you invest early in your life has a drastic effect on the money you accumulate over the years. This is true for long term investing. But if there is no "long-term", there is no time for "compounding". Time is a great ingredient and everyone has a good amount of it. If you loose time at the start, you lose wealth. So, it's no wonder that they say "Time is money"!

Investing early lowers your burden later

I want to convince you that early investing is the best way to make sure that you are not burdened later in your life …Here's an example…

Ajay, a 26 year old software engineer from Bangalore, has recently started his career. He has around 30 years in hand till his retirement and he wants to accumulate a good amount of money, which can fund his needs and aspirations. He has decided to accumulate a minimum of Rs 3.5 crore by the age of 56. Towards this end, he has a "plan". I will call his plan OPTION 1 and it's the most obvious way anyone would think.

Option 1

Assuming, very logically, that his income will keep increasing as he progresses in his career…

- Ajay decides to start by investing Rs 5,000 per month for the first 10 years

- Thereafter, he will invest Rs 15,000 per month for the next 10 years

- And finally, he will invest Rs 50,000 per month for the last 10 years.

Using the above plan, he will be able to generate around 3.5 crores in 30 years. We are assuming a standard long term equity return of 12% CAGR.

This seems like the most intuitive way to formulate a plan. Do you agree?

Now, let's look at the other options he has to reach the same target.

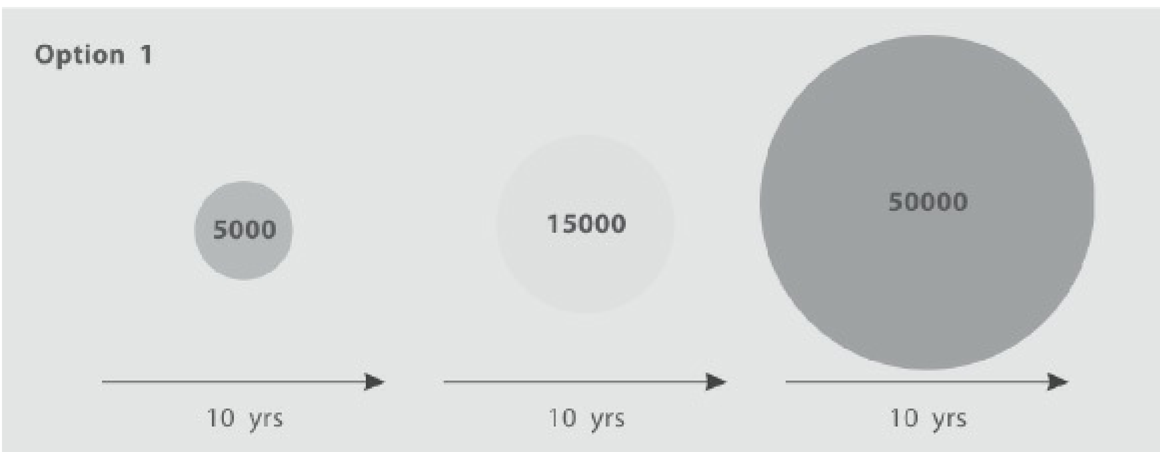
Option 2:

He can invest Rs 10,000 per month for all 30 years. In this case, by increasing his initial investment amount in option 1 by Rs 5,000 per month for the initial 10 years, his situation changes to a level where he can continue with the same investment amount and not increase it later.

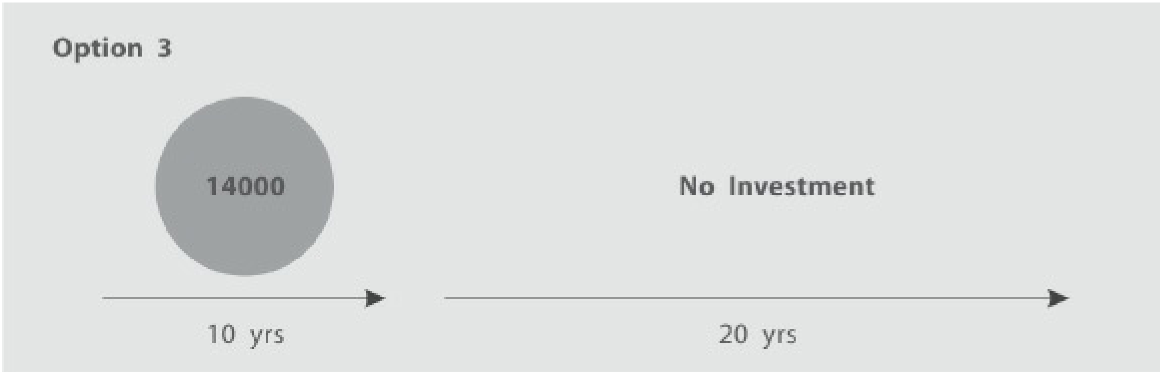
Option 3:

If he invests Rs 14,000 for first 10 years, he does not have to invest any further. In this case, he is investing Rs 9,000 more than he planned to in option 1. You can see that this extra investment of Rs 9,000 in the starting phase is so powerful that he does not need to invest anything for the next for 20 years. So, an investment of Rs 9,000 extra in the first 10 years can replace his old plan of making future payments of Rs 15,000 per month for 10 years in between and Rs 50,000 per month for the last 10 years (as per option 1). You will appreciate from this example that a greater contribution in the start helps him to accumulate the same amount of money without any later contributions.

What this tells us is that if one contributes more in the start, it's equivalent to investing a lower amount initially and gradually increasing in future years.



OR



In a nutshell, if you look closer, you will realise that investing more at the start gives you the freedom to invest less in the future. So, if you want to invest for 30 years, the investments that you make in the first 15 years will make up a significant portion of your whole corpus; contrary to popular belief, it is not the investments that you make in the last 15 years. Your investments in the last 15 years will, of course, add to the corpus, but the contribution will not be as significant. For example, if you want to invest Rs 5,000 per month for 30 years at the rate of 12%, you would accumulate around 1.76 crore. However, if you only invest for half the tenure and leave the money to grow for the remaining 15 years, you would still amass Rs 1.51 crore, which is 85% of the final corpus.

> **"Early investing gives you the liberty to reduce or stop your investments in the future, without compromising much on the final results"**

You can also increase your investments by Rs 830 per month (i.e. from Rs 5,000 to Rs 5830) and invest only for 15 years and you will still make the same Rs 1.76 crore at the end of the tenure (provided you leave your money to grow for the interim 15 years).

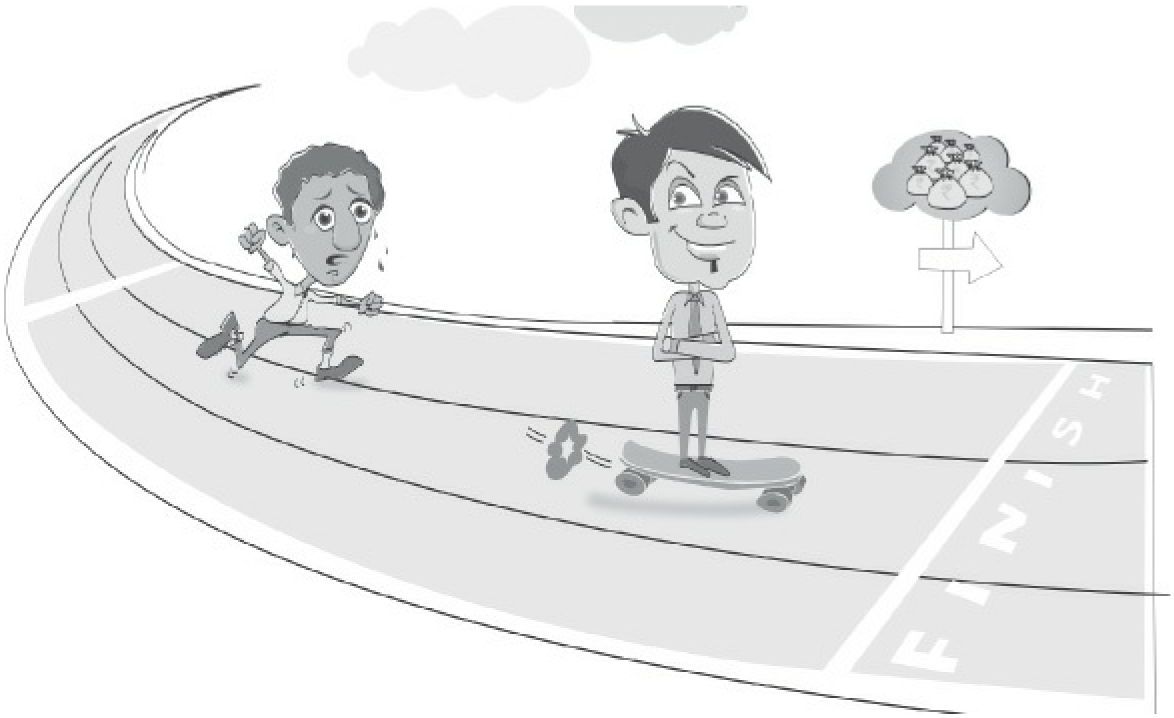
Early investment and returns required

Suppose you and your friend decide to race for 20 km. Your friend decides to pace himself by running at a steady rate of 4 km per hour. Accordingly, he will complete the distance in 5 hours.

However, you are more relaxed at the start and decide to run at a pace of 2 km/hour, thinking that you will cover up for this slow start later. You keep running at a pace of 2 km/hour for 3 hours and cover a total of 6 km. Now you decide to increase your pace. But imagine the situation. You have just 2 hour left and 14 km to cover. It's a situation where you have to run at a speed of 7 km/hour. It might not be impossible, but it's certainly not easy! Your chances of winning come down considerably. Many things can prevent you from achieving that pace in the last 2 hours - you may get a cramp, you could meet with a small accident while running so fast, you could get exhausted… Overall, your task is rather challenging!

What could you have done? If you had decided to run faster than your friend at the start, at say 5 km/hour (while your friend ran at 4 km/hour), you could have completed 15 km in the first 3 hours. Then even if you jogged at a speed of 2.5 km/hour for the next 2 hours, you could easily have won. It becomes much simpler than the previous situation. Even if you wanted to rest for 30 minutes, you could afford to do so and still complete the rest of the race at a speed of 3.4 km/hour. Or you could alternate between jogging and walking towards the end. This leisurely pace would be possible only because of the effort you made at the start.

Your financial life is no different. It's a race. If you are happy with what you have acheived in life, you have won the race. If you contribute more at the start, things become manageable at the end.



And, each and every opportunity or chance to save more or contribute more, means a lower burden later.

Now let's look at how this applies to wealth creation…

Suppose you and your friend start your careers at the same time and have 30 years in hand before retirement. Your friend starts investing Rs 60,000 per year in an avenue that delivers a 10% return. He would collect Rs 1.62 crore at the end of 30 years. Now, let's say you start investing the same amount per year but 10 years later, thinking that you will apply some smart investment strategies which give you a much higher return. Even if you get a return of 20% on your investments year after year, you will still have less money than your friend in the end. And that's despite somehow managing a 20% return on your investment…to achieve which you need to be an investment NINJA!

However, your friend's life will be a lot easier… getting a return of 10% is almost 10 times easier than getting a return of 20%!

If you are a conservative investor, early investing is more than necessary… its critical. You should see early investing as a “strategy” rather than a “fact” for your investments.

Investment table

Formulas scare everyone. So, I’m putting down a table as a ready reckoner for how much you can generate by investing some amount for several years at different rates of return: namely, 6%, 8%, 10%, 12% and 15%.

Table 1: A one time investment of 1,000 for X number of years at R%.

It’s very simple to use this table. If you want to invest 1 lakh in an FD which gives a return of 8% and your investment tenure is 7 years, run one finger down the column titled 8% and another finger across the row titled 7 and they will meet at 1,714. Now that’s how much Rs 1000 will become in 7 years at 8%; so, Rs 1 lakh will become approximately Rs 1,71,400.

In the same way, if you consider a mutual fund which says that its overall return was 12% per annum for the last 23 years, you can quickly see that Rs 10,000 invested in that mutual funds would have been worth 135520 (13552×10) or around Rs 1.35 lakh after 23 years.

One time Rs 1000 invested for X yrs at R interest rate per annum

	Interest				
Years	6%	8%	10%	12%	15%
1	1060	1080	1100	1120	1150
2	1124	1166	1210	1254	1323
3	1191	1260	1331	1405	1521
4	1262	1360	1464	1574	1749
5	1338	1469	1611	1762	2011
6	1419	1587	1772	1974	2313
7	1504	1714	1949	2211	2660
8	1594	1851	2144	2476	3059
9	1689	1999	2358	2773	3518
10	1791	2159	2594	3106	4046
11	1898	2332	2853	3479	4652
12	2012	2518	3138	3896	5350
13	2133	2720	3452	4363	6153
14	2261	2937	3797	4887	7076
15	2397	3172	4177	5474	8137
16	2540	3426	4595	6130	9358
17	2693	3700	5054	6866	10761
18	2854	3996	5560	7690	12375
19	3026	4316	6116	8613	14232
20	3207	4661	6727	9646	16367
21	3400	5034	7400	10804	18822
22	3604	5437	8140	12100	21645
23	3820	5871	8954	13552	24891
24	4049	6341	9850	15179	28625
25	4292	6848	10835	17000	32919
26	4549	7396	11918	19040	37857
27	4822	7988	13110	21325	43535
28	5112	8627	14421	23884	50066
29	5418	9317	15863	26750	57575
30	5743	10063	17449	29960	66212
31	6088	10868	19194	33555	76144
32	6453	11737	21114	37582	87565
33	6841	12676	23225	42092	100700
34	7251	13690	25548	47143	115805
35	7686	14785	28102	52800	133176
36	8147	15968	30913	59136	153152
37	8636	17246	34004	66232	176125
38	9154	18625	37404	74180	202543
39	9704	20115	41145	83081	232925
40	10286	21725	45259	93051	267864

Table 2: Monthly investments of 1,000 for X number of years at R%.

Now suppose if instead of a one time investment, you decide to keep investing some fixed amount of money in a particular instrument every month. Here's a table which will tell you what you will have amassed over the years, i.e. the sum of your contributions and the interest there on.

For example, if you wanted to invest Rs 5,000 per month for the next 25 years in an instrument which returns an interest of 10%, you can see from the chart that you will have collected Rs 13,37,890 for every Rs 1,000 invested per month, so you can just multiply this 13,37,890 by 5 and get Rs 66,89,450 as the final amount that you receive for investing Rs 5,000 per month.

Monthly Investments of Rs 1000 for X yrs at R interest rate/annum

Years	Interest 6%	8%	10%	12%	15%
1	12397	12533	12670	12809	13021
2	25559	26106	26667	27243	28135
3	39533	40806	42130	43508	45679
4	54368	56726	59212	61835	66044
5	70119	73967	78082	82486	89682
6	86841	92639	98929	105757	117120
7	104594	112861	121958	131979	148968
8	123443	134761	147399	161527	185937
9	143454	158479	175504	194822	228848
10	164699	184166	206552	232339	278657
11	187254	211984	240851	274615	336474
12	211201	242112	278742	322252	403585
13	236625	274740	320600	375931	481484
14	263616	310076	366841	436418	571906
15	292273	348345	417924	504576	676863
16	322697	389791	474357	581378	798693
17	354997	434676	536698	667921	940108
18	389290	483287	605568	765439	1104255
19	425698	535932	681649	875325	1294790
20	464351	592947	765697	999148	1515955
21	505388	654694	858546	1138674	1772673
22	548957	721567	961117	1295896	2070659
23	595213	793989	1074429	1473057	2416548
24	644321	872423	1199606	1672687	2818040
25	696459	957367	1337890	1897635	3284074
26	751812	1049360	1490655	2151112	3825025
27	810580	1148990	1659417	2436736	4452936
28	872972	1256888	1845849	2758585	5181786
29	939212	1373742	2051804	3121252	6027803
30	1009538	1500295	2279325	3529914	7009821
31	1084201	1637352	2530671	3990405	8149702
32	1163469	1785784	2808335	4509297	9472825
33	1247627	1946536	3115075	5093998	11008645
34	1336975	2120631	3453934	5752854	12791356
35	1431834	2309175	3828277	6495269	14860645
36	1532543	2513368	4241818	7331841	17262582
37	1639465	2734510	4698662	8274511	20050641
38	1752980	2974005	5203343	9336736	23286893
39	1873498	3233379	5760871	10533677	27043388
40	2001448	3514281	6376780	11882420	31403755

Early investment can help you enjoy semi-retirement

Now I'm going to touch upon one of the most ignored aspects of early investing. I dont see anyone talking about it in the personal finance space.

For how long do you want to keep working at your job? Till you are 60? Don't fool yourself! A lot of people are forced to work till their retirement, battling daily pressures only because they are suppose to bring home money to provide for the family, year after year.

By now you know that if you invest early in life and utilize the time to compound your money, you can rest assured that the money starts working for you. This means that in the later years of life, you get freedom from worries about contributing each month to that big wealth pool.

If you do it in the right way, you could even enjoy a semi-retirement. Semi-retirement is nothing but that phase of life wherein you don't stop working, but definitely stop worrying about money. You can take up some light job or some consultancy work, which gives you enough time to enjoy your life while some money still comes in. If you want to retire at the age of 55, you can semi-retire at the age of 45, at least.

Just recall the initial part of this chapter where we saw how early investing gives you the freedom to exempt yourself from contributing too much at the end. That's exactly what you can do and as a result, there will be less pressure to earn a lot nearer your retirement. Even if you are earning less, your money takes care of itself.

So take action towards contributing more at the start!

3 strong conclusions regarding early investing

By now you must be suitably impressed with all the magic that early investing can do to your financial world. So, at the risk of sounding repetitive, let me neatly wrap things up for you with three conclusions which capture the essence of early investing and explain what exactly happens in the process.

Conclusion #1: Even if you cut your contribution at the end of the tenure, it won’t affect the final corpus drastically.

When you see a huge 30 year old tree, in which part of its entire life do you reckon it required the most amount of care and nutrition? It’s always the initial years during which the roots have to take hold. It’s also the initial years in which a plant is most vulnerable to weeds and bad weather. Once it has safely made it past the first few years, you can leave it to grow on its own; the tree will be able to extract nutrients from the soil on its own. It wont hurt if you forget to water it once in a way. In fact, there’s a good chance that it doesn’t need your care now; it has become so big that it can expand and grow well. Hence your contribution does not matter much at a later stage.

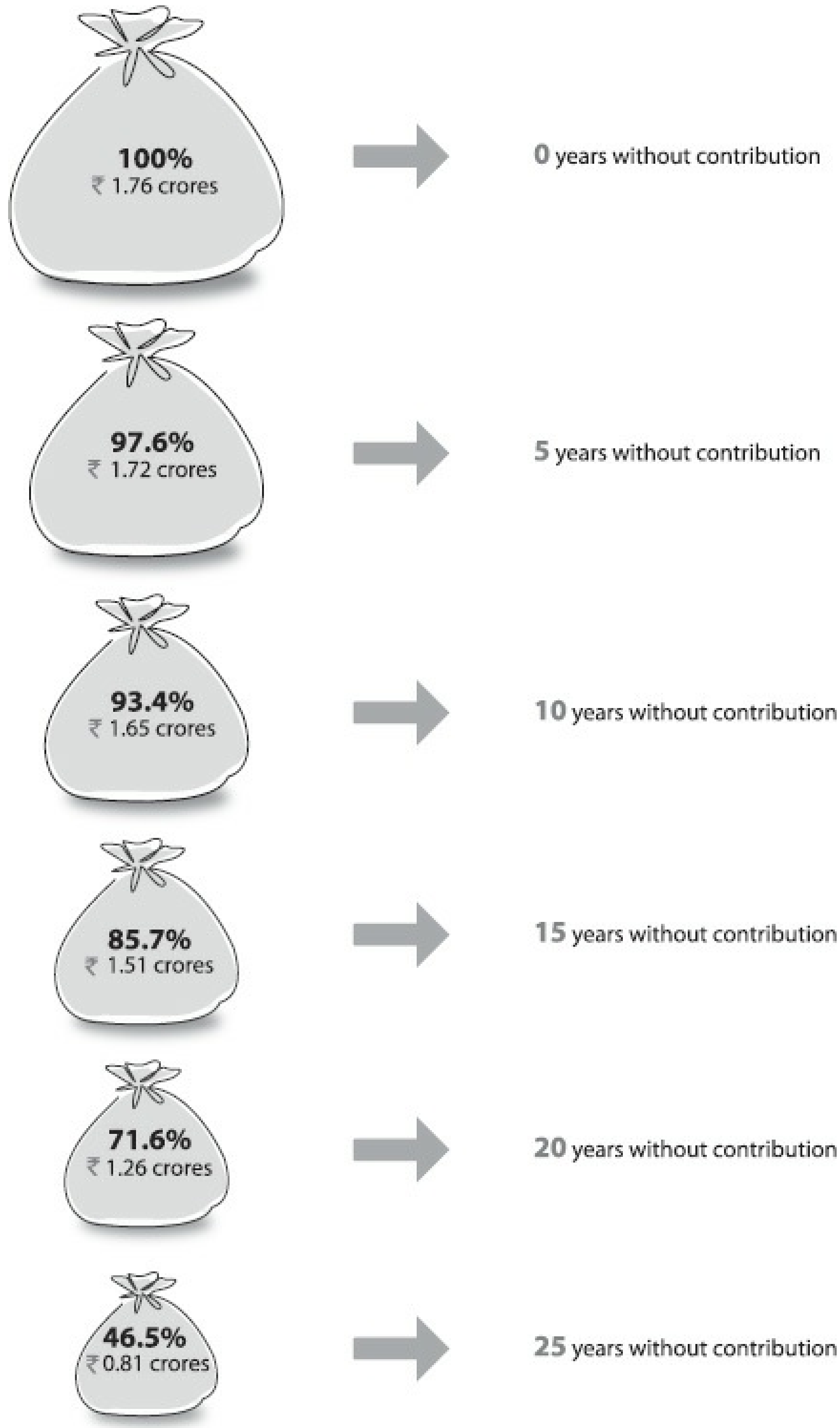
Something very similar happens in the case of your investments. The initial period is very critical. If we take care of it very well at the start, later on we can achieve good results without actually putting in much effort at the end, in terms of contributing money. Naturally, effort in terms of analysis and monitoring will still be required.

Just as an example, if you invest Rs 5,000 per month for 30 years (let’s suppose you wish to build up a fund for your retirement), you can generate around 1.76 crore if you get a return of 12% (compounded monthly).

Now what happens if you do not contribute anything in the last 10 years? At the end of 30 years, you will still accumulate Rs 1.64 crore, which is 93% of the original corpus.

If you do not contribute for the last 15 years? You will still make Rs 1.51 crore, which is 85% of your original corpus.

Here’s a chart which shows the percentage of corpus generated when you do not contribute anything for a certain period at the end.



It’s no magic; it’s pure maths and compounding. Whether you lose the last 10 years or 15 years, one thing remains certain, you have put in enough effort in the start and then given sufficient time to your investments to grow.

Here’s a table which gives you the exact corpus generated and what proportion of the original corpus it forms when you don’t contribute in the latter years.

Number of years without contribution at the end of a 30 year period	% of corpus generated	Total corpus
0	100.00%	1.76 crores
5	97.6%	1.72 crores
10	93.4%	1.65 crores
15	85.7%	1.51 crores
20	71.7%	1.26 crores
25	46.2%	0.81 crores

Conclusion #2: If you reduce the length of your tenure substantially, the additional amount you need to invest to create a corpus of a particular size does not increase drastically.

In Conclusion #1, we understood that if you reduce the tenure during which you contribute to your corpus by 25-50%, your final corpus reduces by a small margin. Naturally, it depends to some extent on how much you have shortened your tenure by. Now, this indirectly tells us that if we increase our investments by a small amount, we can still reach the same corpus.

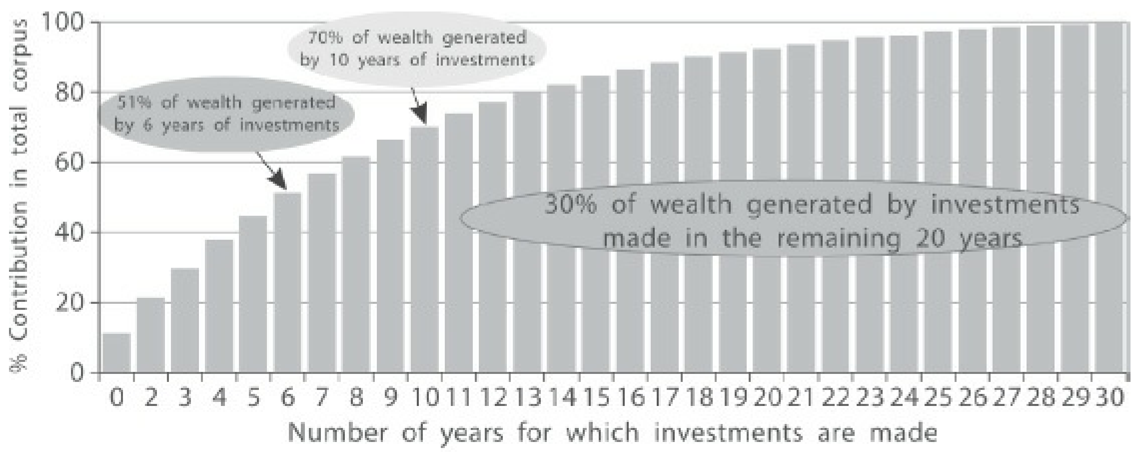
For instance, let’s say you need to invest Rs 5,000 per month for 30 years to reach a target of Rs 1.76 crore. Now suppose you do not want to make any investments for the last 15 years, but are willing to leave your corpus to grow. All you need to do is increase your investments by Rs 830 per month and invest 5,830 for 15 years instead of investing Rs 5000 for 30 years. This will make sure you reach your targeted corpus.

Here are some other situations in which you can reduce the tenure of your contribution, without impacting the amount of your final corpus, simply by increasing each contribution marginally.

Years without contribution at the end tenure	Amount required per month	% increase in investment to reach the same corpus
0	5,000	0.00%
5	5,120	2.41%
10	5,350	7.01%
15	5,830	16.6%
20	6980	39.6%
25	10,830	116.0%
29	43,100	762.0%

Conclusion #3: Investments made in the initial years form the main chunk of your final corpus

The investments that you make at the beginning get sufficient time to grow and compound drastically over the years. Using the same example, take a look at a chart which shows you how a huge part of your final corpus gets built because of the investments made in the initial years. Out of the total wealth you create in 30 years, almost 50% is a result of investments made in the first 6 years and 70% is generated due to the investments made in the first 10 years. The contributions in the last 20 years account for just 30% of the wealth generated. Which again shows that early investing is so critical for wealth creation. However, do remember that the above conclusions hold true only if we have a total time horizon of 30 continuous years. If you discontinue your investment in between, the above will not hold true.



Years of contribution	Percentage of total wealth accumulated
1	12%
5	46%
10	72%
15	86%
20	93%
25	97%
30	100%

Your next best alternative

Now don't be disheartened if you have not yet started contributing towards your future. Start today. It's always earlier than tomorrow and investing today will give your investments a chance to grow in future, irrespective of how long or short that future is. The main principle that you need to follow is invest as much as you can today… don't put it off for later!

Here's what you can do to maximize your investments today. Take a closer look at your life and you will find several ways in which you can generate more money to invest. A few suggestions which come to my mind are:

1. Cut out on unnecessary outings once in a while

2. Try-to use a bike instead of a car, if your situation permits it. I see many people using 4 wheelers when they can do just fine with a 2 wheeler!

3. Buy a smaller car instead of a bigger one, if it doesn't hurty our ego

4. Change to a prepaid mobile instead of a postpaid (this works out well for a lot of people)

5. When you go shopping, write down what you want and calculate approximately how much it will cost you. Then carry that amount of cash, with a small margin, perhaps.

6. Walk or ride a cycle when you want to get to a place that's relatively close; don't become a slave to two wheelers or cars

Any small savings undertaken and invested today are going to have a huge effect later. The stronger your focus is on investing more at the start of your life, the bigger will be the relief you can expect later. But the focus is on discipline and not on getting bogged down by short term deviations, which are bound to come along the way.

Final Thoughts

Make sure you don't over do your "belt tightening" exercise and start cutting down on those things which make you happy. The whole idea is to look at increasing your investments by cutting down those costs which are relatively dispensable. You don’t have to and should not compromise on todays life to build a great tommorrow. The whole idea was to motivate you into early investing and show you what it can do for your financial life.

Now you have to do the most important and the toughest part, ACT ON WHAT YOU HAVE LEARNT!

Flashback Learning

- Investing more money in your initial earning years will make sure that you quickly build your corpus and it eventually grows without your support
- Investing more later is the same as investing less today; the choice is yours!
- Don’t lose time. 5 years wasted in the start is worse than wasting 15-20 years towards the end of your earning life.

2 hour Action Plan

1. Identify all the areas of your life in which you can cut down on costs, without compromising on your current life style and find out how much you can save.
2. Find out how much money you are able to additionally save per year and what kind of additional wealth it can generate for you by the time you retire.

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[1] **Assuming that the interest is compounded monthly**

Chapter 2

HAVE YOU PROTECTED YOUR GARDEN?

Once upon a time, there was a small village in a province. The village was very famous for its gardens, which were very beautifully laid out with different kinds of flowers, plants and trees. Each garden had its own caretaker; some even had two caretakers. The caretakers made sure that they watered the gardens under their care each day, so that all the flowers, plants and trees got proper nutrition and grew well.

Watering them was not an easy task. Each day the caretakers had to travel for miles to bring water from a far away river. The king of the province had made provisions for storing water within each garden. He had built a huge water tank within each of them. The caretakers would fill some water in their respective tanks daily to replenish their supply of water. It would take thousands of trips to and from the river to fill a tank to its brim. What's more, bringing water to the tank was not easy. There were many risks along the way - there were wild animals, who attacked them some times and very often enemies from other provinces lay awaiting them. So, effectively, no garden had a tank that was full or even close to full.

The king came up with a plan to make sure that no garden of his kingdom ever remained without water. He told every caretaker to contribute one glass of water everyday from his stock to the king's own water repository. Accordingly, the king would collect a huge amount of water each day, as thousands of caretakers would contribute one glass each. Whenever a caretaker fell prey to enemies or was injured or killed by a wild animal, the king would make sure that his water tank was filled full of water. This would suffice for that caretaker's garden for life. By contributing just one small glass of water each day, every gardener had a great way of securing his garden's future.

But guess what happened. A large number of caretakers believed that they were too strong to be put down by any wild animal or enemy. Some even claimed that they never faced any attack and would never encounter one. Others went to the extent of feeling that if they were not around later, it did *not really matter what happened to their garden. They wouldn't be around to enjoy the fragrance of the flowers and the beauty of the landscape anyway!*

So, you can imagine what happened to the gardens of the caretakers who did not contribute to the king's repository. In their absence, no other caretaker would come and water their plants. The gardens didn't always die immediately. Sometimes they lived long but they were not as colorful and full of fragrance as they would have been if their caretaker had provided for enough water for them.

Does this story give you any hint? I am sure it does.

Just like the story you have just read, our families are our gardens and we are the caretakers of those gardens. The money we earn can be likened to bringing water from the river. And the water tank for our garden is our store of wealth. While we are young, we have the capacity to provide for our families. However, we are not likely to have saved up enough money to ensure that if we are not there tomorrow, the wealth we have accumulated will enable our family to live comfortably and meet all their aspirations for years to come. But is it possible for us to contribute a small amount every year and gift a lifetime of protection to our loved ones? We know we can. And that's what "Life Insurance" is all about.

There are different kinds of life insurance products in the markets, but not all of these are for pure "Protection". The only product which is a pure protection plan is called "Term Insurance". With such plans, you pay a fee and get financial security. We will talk about it in detail a little later and debunk some of the beliefs you have about life insurance. We will also see how your insurance cover may not be adequate for your family and why you need to work on it!

Are you truly unselfish when it come to protecting your loved ones?

Every one hates the idea of purchasing insurance, but every one loves their families. Do you see some conflict here? How can we hate something which could benefit someone we love? We try to give our families all the happiness possible… we buy gifts for them, take them on vacations, make sure that we protect them from tough situations and all the worries and problems in life. But suppose you die tomorrow, what have you done to take care of them then? That's the real test of what you have done for them. Have you gifted them the biggest thing in life - "Adequate Protection"?

It's so wrong to say that we do not understand Insurance as a concept! We all know about insurance and use it in our daily life. Here are some small instances of insurance; perhaps these are not examples from mainstream finance, but they illustrate the concept of insurance nevertheless…

Insurance	Covers from you	Price we pay
Wearing a helmet while driving	Huge damage in an accident	Inconvenience of wearing the helmet
	Losing a	The small token fee which is

We pay token money for a flat which we want to rent or buy	good opportunity	blocked and may even go waste
We reach the airport 1 hour before the scheduled departure time	Missing your flight	Time wasted just sitting at the airport

What I want to say is that we are all aware of the concept of insurance. The only thing is that when it comes to life insurance, something happens to us. We tend to run away from it because perhaps we are conditioned to think that it does not offer any great benefit…if nothing happens to us. We have always heard that “Insurance policies do not return your money to you!” So we are conditioned to believe that anything which does not give some return is not worth considering. But that’s not really true…let me show you why.

Some tough questions for you

Let me tell you one very simple and ‘to the point’ reason for the dismal state of life insurance coverage in India. It’s very simple - people do not buy adequate life cover in India because they don’t ask themselves tough questions. We never take time off to think about unpleasant situations – like an untimely demise. But this can happen to anyone. Why should we carry on thinking that we are above it and it cannot happen to us. Why do we think, **“Arre who to doosro ke life me hota hai!”** We take the idea of unforeseen eventualities very lightly and, as a result, when bad things happen to us, we really have no recourse.

Let me tell you a small story, which you have probably heard in your childhood…

There was a small boy who used to take his cattle out to graze each day. He was very naughty and never missed an opportunity to make fun of or irritate the people from his village. One day when he was out grazing the cattle, he started shouting, “Save me from the tiger! Save me from the tiger!” All the villagers and all his well wishers dropped everything they were doing and ran to help him. But when they reached him, there was no danger there. The little boy laughed at them and told them he was just joking.

He was taking things very casually and didn’t think about the possibility that some day a tiger could really come to attack him or his cattle. He thought, “A tiger will never really come to attack me.” It was because of this callous attitude of his that everyone lost faith in him.

One day, when a tiger really came to attack the boy, he started shouting. But no one came, even though everybody heard him. They didn't believe him anymore.

If you are wondering why I am telling you this story, it's because it has a big lesson! A lot of us do not believe that death can really come to us. We believe that it's just a bad thing which happens in the lives of others. We don't make any contingency plans. But if you die without proper protection for your family, no one will come to rescue them!

Uncomfortable conversations

Our society is not very comfortable talking about certain issues. If a man tells his mother that he is planning to purchase life insurance, she is likely to get all dramatic and behave as if he is going to war and may never come back. In the same vein, if you ask a woman how much money would be enough to meet her needs if her husband dies in an accident, she is bound to give you the cold shoulder just for bringing up the idea that her husband may not survive her! It's a crime in India to talk like that.

Let me share an incident with you which would give you a better idea of what I want to convey:

There was a client of ours who had an insurance cover of Rs. 6 lakh through 3 endowment policies. He was living in Pune with his mother, his wife and his two year old son. He was doing well for himself and had recently purchased a home on a loan. Now his situation was not extraordinary. It was pretty much how an average big city middle class person's profile looks. And, he was hell bent on not wasting money on insurance.

I did my simple exercise with him, which I call **"Writing down the answers to tough questions".** The three of us-the husband, the wife and myself-sat down in a windowless room. Then I gave them a pen and piece of paper each, on which I had printed out my tough questions for them separately and then addressed the husband first.

“Since you don’t want to buy life insurance, I am not going to badger you about it again,” I told him. “Ok, so now what?” he inquired curiously.

“Without life insurance to fall back on, I would like you to do a small “Till in the blanks” exercise. On the sheet of paper I have given you, I have listed out a few goals, which I am certain that you aspire for. All you have to do is list out the sources of finance from which you can envisage that they can be met. I don’t expect you to put down a lot of detail…just enumerate the sources. For instance, ‘x’ amount from my bank balance, ‘y’ amount from my investment in so and so instrument, ‘z’ amount from the proceeds they will receive from selling my property, or whatever you have in mind. It’s just a game of matching your finances to your aspirations for your family. Then we’ll play match the columns with all that you leave them and all that you would like them to have…,” I said with a hint of a smile on my face!

Here’s what the tough questions on the paper were:

1. I estimate that the monthly expenses of my family will be ____ for the next ____ years. In case I am not around, this is where they will get a regular income from:

1. ____

2. ____

3. ____

4. ____

5. ____

6. ____

2. I want my child to have a great education. This is how it will be funded in case I am not there

3. I want to make sure that my wife lives comfortably and this is how she will receive the money to take care of all her additional needs:

4. Incase some emergencies arises (in the form of illnesses or accidents), here's were the funds to meet these will come from:

5. I know that I have an outstanding home loan of Rs 35 lakh (my original home loan was worth Rs 40 lakh). As I am paying a huge sum of money as EMI, my family will have to continue paying the EMI or

clear the loan in one go. This is how they will achieve it. Write it down, step by step.

“Once you fill it up, let your wife go through it and sign below as a gesture that she accepts your arrangements and is comfortable with them.” That’s all I said.

Then I turned to the wife and asked her some really tough questions too. At first she did not want to listen to the questions, let alone answer them. But I was as blunt as I could be-that’s my job as a financial coach. After all, I was responsible for putting their financial life on track. I had to be tough for their own good!

Here are some snippets from my conversation with her:

“Suppose your husband is not there tomorrow to provide for the family, will you be willing and able to take up a job?”

“What! I don’t know… I don’t want to think about such things…” came the answer after a long weird look.

“If, in such a situation, you had the option not to work and to just live a comfortable life - as you are living right now - and concentrate on other things like raising your son and doing something part-time just to keep yourself gainfully occupied, would you prefer that?”

“Hmm .. Yes that would be good, but why are we even talking about this? Is my husband ok? Have you met his doctor?”

“Oh don’t worry, I am just trying to help the two of you! Please help me to help you by filling up your sheet with suitable answers.” And I brought her attention back to the paper, which I had given her earlier.

The questions it contained read as follows:

1. **If my husband were not around, the amount of money which I would need every month would be Rs _______________ and this is how I would arrange for it:**

2. **I will take care of my child and his upbringing by giving him a good education. This is how I would provide for him:**

3. **These are my dreams in life… all the things that I would love to do and this is where the money that I need to do them will come from…**

4. **Once my husband is not around to pay off the house loan, I will have to take care of it. This is how I will take care of it alongside other responsibilities?**

"The moment you both fill up your respective sheets and are satisfied with your answers and each other's, let me know…" I told them.

After 40 minutes…

As I expected, they could not fill up the sheets and they looked like "kumbhkaran coming out of his sleep after decades"…They took a Rs 85 lakh term insurance plan the very next week.

Now, if you don't personally believe in life insurance or believe that you are adequately covered, it's time for you and your wife to undertake this exercise and see if you can answer these questions satisfactorily. If you can, then well and good! But if you can't, then it's high time you should be considering protecting yourself with a higher cover. It does not even cost 2-3% of your entire annual salary, just go for it!

Review the adequacy of your current insurance policies

Now I would like you to undertake a mini-exercise, which is bound to help you. How much life insurance do you have? This is the first thing that you need to find out. And I say "find out" because a lot of us do not know exactly how much insurance cover we have. When we start working with our clients, I am amazed to hear responses like "I have life insurance, but I'm not sure of the policy name", "I think I have 12 lakh of insurance cover", "I have no idea which plan I was sold. It was my uncle who sold it to me; let me call and ask him…"

Jokes apart, just "find out" the amount of life insurance cover that you already have. If it's 3 lakh, 5 lakh or 10 lakh, you'd better be embarrassed. But don't be too hard on yourself; most people in our country are as underinsured as you are. In fact, you may be pulling the average upwards. Then, imagine you are not around from tomorrow onwards. Your family will get some amount of money from your insurance company after a few weeks. Stop and think about how long it can sustain your family's regular expenses alone. Assume that the insurance amount is kept in a bank fixed deposit and earns a return of 8% per year and inflation is around 6%.

Your family will require some amount of money every month. Let's say they start withdrawing that much money every year and use it on a monthly basis. How long will it be able to support them?

If that sounds confusing, let me put it across with the help of an example. If your family requires Rs 30,000 per month and you have Rs 15 lakh worth of insurance, it would last for just 4 years and 4 months. Thats all…

The chart below gives you a rough idea of how long the money will last under different scenarios.

	Insurance Amount					
Expenses/month	300000	500000	800000	1000000	1500000	2500000
10000	2.6 yrs	4.3 yrs	7 yrs	9 ys	14.1 yrs	26 yrs
15000	1.7 yrs	3 yrs	4.6 yrs	5.6 ys	9 yrs	15.9 yrs
20000	1.3 yrs	2.1 yrs	3.4 yrs	4.2 ys	6.6 yrs	11.4 yrs
25000	1 yrs	1.7 yrs	2.8 yrs	3.4 ys	5.2 yrs	9 yrs
30000	10 months	1.5 yrs	2.3 yrs	2.8 ys	4.3 yrs	7.3 yrs
40000	7.5 months	1 yrs	1.6 yrs	2.1 ys	3.2 yrs	5.4 yrs
50000	6 months	10 months	1.3 yrs	1.7 ys	2.5 yrs	4.3 yrs

Assumptions
* Expenses are increasing at 6% per year
* Money lying in the bank earns 8% per year
* Money withdrawan on annual basis

In reality, the insurance money will get depleted even sooner than the chart indicates since we have not taken into consideration any emergency and one time large expenses, which are bound to occur.

Term insurance-true protection for your loved ones

Let me brief you about term insurance and what it is all about. Term insurance is the purest form of life insurance. You pay only for protection in term insurance and there is no investment component in it. So you pay the premium each year and your family is covered in the event of your death. That is to say, if you die, they get the money. If you don't die, then nothing happens: they don't get the money and neither do you. It's as simple as that. If you know about a simpler insurance product than this, please mail me.

If you recall the example given at the start of this chapter, you will realise that paying premiums for term insurance is just like contributing a glass of water to the king's reservoir. If anything happens to you, your family will get financial protection for a long time. If nothing happens to you, it's a small price to pay for such a cover.

Let's look at a simple numerical…it always says things more clearly than words can. 30 year old Ajay buys a term plan with a tenure of 30 years and a cover of Rs 1 crore. Towards this plan, he pays a premium of Rs 15,000 per year for the next 30 years. He can stop paying the premium at any point of time, but then the contract becomes null and void. If Ajay dies during these 30 years, his family will get Rs 1 crore, if he has been paying his premium regularly.

Here's some practical information on term insurance:

- All life insurance companies offer term insurance plans.

- You can buy these plans offline from an agent or online (without involving an agent). However, only some companies offer the online version of term plans, not all.

- Online term insurance is cheaper than offline term insurance.

- You can pay the premium annually, quarterly or monthly.

- The older you are at the time when you purchase a policy, the higher the premium that you pay will be.

- You can return the policy within 15 days of receiving it in case you are not satisfied with it.

- You can discontinue the policy whenever you wish to; so in a way it becomes an annual contract.

Buying adequate life insurance = buying peace of mind

Buying insurance is easy. Buying adequate life insurance is not.

I would like to take you back to a scene from Lage raho Munna bhai, where Munna slaps Circuit and then Gandhiji asks him to apologize to Circuit…

It goes something like this.

Munna:Ye mafi mangna jaroori hai kya?

Gandhiji:Dekhna chahta hurt tumme kitni himmat hai.

Munna:Boleto?

Gandhiji: Chanta marna aasan hai. Mafi mangne ke liye himmat chahiye beta …Ye kayron ka kaam nahi hai!

If you have seen the movie, you can see the discomfort on both Circuit and Munna's faces. It embarrasses them to talk about an apology and show their emotions to each other. But I am sure you would appreciate the peace of mind Munna felt after having said "Sorry" to Circuit! Did you see the energy and enthusiasm Munna felt?!

Taking life insurance is a courageous decision too. It's not an easy thing to accept that you are paying for the security of your family's happiness and you will not get anything out of it personally. It’s a way of showing your commitment to your loved ones. It’s not everybody’s cup of tea! If you re-read the dialogues, putting yourself in Munna’s place and your inner self in Gandhiji’s, you will hear this…

You: Ye term insurance lena jaroori hai kya

Your Inner Self: Dekhna chahta hun tumme kinti himmat hai.

You: Bole to?

Your Inner Self: “Money invest karna aasan hai. Term insurance lene ke liye himmat chahiye beta…Ye kayron ka kaam nahi hai!

Term Insurance does not return the money

You should be glad that it does not! Because if it did return your money, guess what would happen? The premiums would shoot up so high that you would not be able to afford it.

Imagine you are going to buy a traditional plan or any policy which combines investments and insurance and offers its customers money back later. Now imagine that your requirement is to cover yourself for ₹ 1 crore. What do you think the premiums will be? They would run into lakhs of rupees per year…

That may work out to around half of your salary! And then what do you do? You would only pay as much premium as you can afford. But that would get you peanuts in terms of insurance cover. Your whole motive of buying life insurance is nullified! Instead of life insurance, now you have an investment product which is merely labeled as an insurance policy. That's the story of every Indian.

When you ask most people why they are not interested in term insurance, the standard reply is "You don't get anything back. What a waste!" I don't back off when I hear this reply. Instead, I simply ask them:

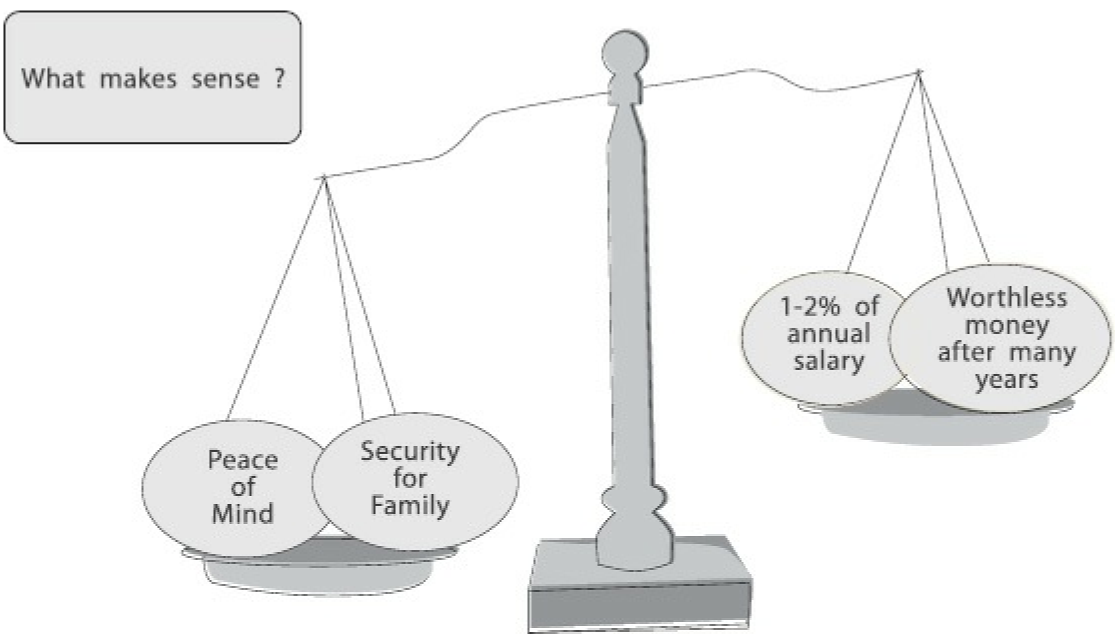
"Incase you did get the money back from your term insurance plan, what would you do with it?" They begin to calculate and start to think hard. Now before you do too, let me give it to you, all cut and dried:

Ajay is a 30 year old guy. Let's say he buys a term insurance policy with a cover of ₹ 50 lakh and a tenure of 30 years. His premium would be around ₹ 7,000 per annum by today's standards. As a result, he will pay ₹ 2.1 lakh over these 30 years. Let's say that after paying his premiums for all these 30 years, he gets back all that money, i.e. ₹ 2.1 lakh. But that's 30 years from today! If his monthly expenses today are ₹ 30,000 per month, his monthly expenses after 30 years would be ₹ 1.72 lakh per month, assuming a modest rate of inflation of 6%. He would finish off what he gets back in less than two months. Alternatively, he could take a short vacation with the family, (which costs around ₹ 50,000 today and may cost a little over ₹ 2 lakh, 30 years from now). That's all!

So coming back to the question of what he will do with his ₹ 2.1 lakh after 30 years… Should he use it to meet his household expenses for close to 2 months or should he spend it on a short vacation? You get my point?

Most people who reject the idea of buying term insurance due to the excuse that they will "not get any money back" are too attached to the numbers. They look at the numbers so closely that they forget to consider the value it can truly render when it is actually available for use. Remember that even an elephant looks like an ant from some distance. So right here and now, abandon the idea that term insurance does not pay any money back! It's just a sentence which does nothing more than discourage you! It does not inspire you to buy security. Rather focus on the security that you will feel once you purchase term insurance.

Now, let's weigh your basic choices and see what your options offer: On the one hand you have "Family security for 30 years", "Peace of mind for 30 years" and on the other hand you have" 1-2% of your annual salary[1] which can compensate you for not more than 2 months' of expenses after 30 year or afford you a short vacation with your family". Which will give you more value for money?



How much Insurance do you need?

If you look at the insurance policies of most people, the amount of cover they have is not linked to anything. It is just a collection of random policies bought with the premium they could afford at the time. In all probability, the cover is likely to be around ₹ 5–10 lakh. They never calculate how much cover they need in a logical manner before they purchase insurance. So how can you calculate how much insurance cover you require? How much is enough?

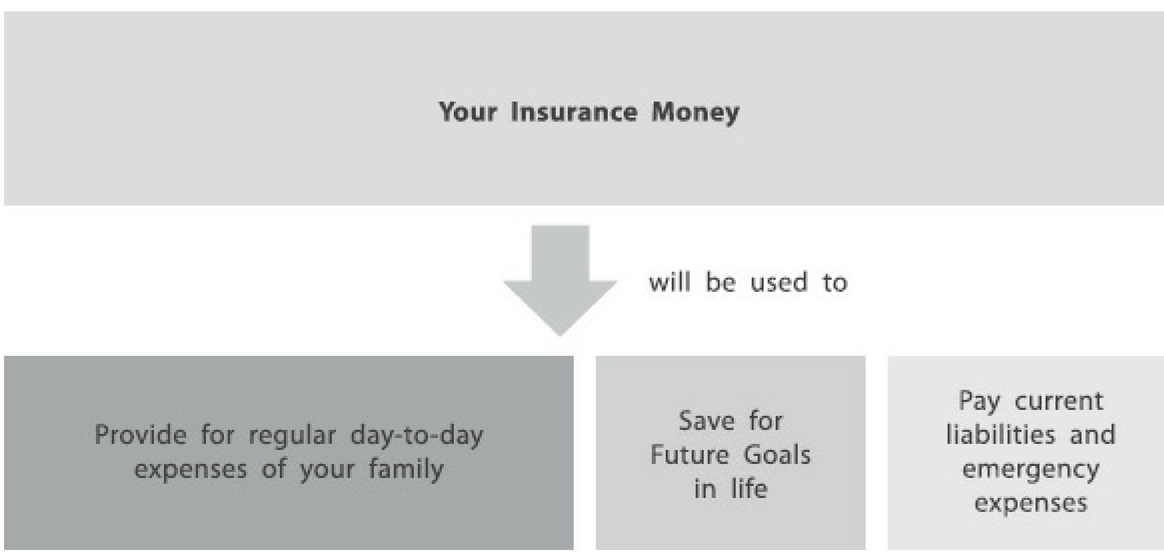
The best way to find it out is through an approach called the “fill in the gaps” strategy. This is a very intuitive way of finding out your insurance requirement. It’s the amount required to fulfill all those goals in life which could have been fulfilled if you were around or which you want to provide for.

The insurance amount which your dependents receive should be able to

A) Provide them with an inflation adjusted monthly income of ₹ Y for the next X years

B) Pay back all the debts you have outstanding till date

C) Meet the goals you share and buy assets which you wanted them to own.



Lets take an example

Suppose you want to purchase enough life insurance to provide your dependents with a monthly income of ₹ 20,000 for the next 30 years. Assuming that the expenses also increase by 6% per year and the money stays invested at the rate of 8% in a fixed deposit, how much should be the insurance amount? The answer is ₹ 54 lakh.

Here's how. Let's work backwards. If your family invests ₹ 54 lakh in a fixed deposit which earns them 8% per annum, they can start withdrawing ₹ 20,000 per month from that pool of money and increase their drawings by 6% every year. Accordingly, in the first year they will withdraw ₹ 20,000 per month; in the second year their expenses will increase by 6% and they will withdraw ₹ 21,200 (a 6% increase over ₹ 20,000) and so on… This way all the money will be exhausted in 30 years, but it will cover their monthly expenses for all 30 years.

A ready reckoner for you

I've done the calculations and put them in a table for you. It shows you the amount of insurance cover that you will require to generate ₹ 1,000 every month under different scenarios.

So, for instance, suppose you want to generate a monthly income of ₹ 25,000 for your family for the next 25 years, assuming that the rate of inflation will be around 8% and the amount they receive from insurance will be invested in an instrument which will provide them a return of 6%. You will have to look at the 2nd table, which assumes an inflation rate of 8% per annum.

Now, you will see that cell E1, i.e. the cell which is the meeting point of column E (a time frame of 25 years) and row 1 (a rate of return of 6%) has a value of ₹ 3.57 lakh. This means that you will require insurance of ₹ 3.57 lakh to generate a monthly income of ₹ 1,000 for your dependents for 25 years. Now, since you want to generate an income of ₹ 25,000 per month for 25 years, you should multiply the value of ₹ 3.57 lakh by 25, which gives you ₹

89 lakh. That's how much insurance cover you will need! This may look like a big amount, but remember that we have taken future inflation into account. In addition, the money is growing at a moderate rate in this example. If one is confident that one's dependents can get a better return, say 10% for instance, the insurance cover required can be lower.

This ₹ 89 lakh will be able to provide for your dependents' monthly expenses. But suppose you have a home loan worth ₹ 20 lakh and a car loan worth ₹ 5 lakh, then put an additional ₹ 25 lakh to your ₹ 89 lakh and opt for a cover of ₹ 1.14 crores.

Now, suppose you have ₹ 30 lakh worth of property (excluding the value of the house you are living in). If you can safely assume that your dependents will liquidate that investment, you can deduct ₹ 30 lakh from the ₹ 1.14 crore and get an insurance cover of ₹ 84 lakh. This will stand as a good enough approximation of the cover you need. A rough estimate is all you need. Don't try to arrive at an exact number; 5-10 % here or there won't make much of a difference. Stay focused on the big picture, which is getting adequate life cover.

TABLE 1 At 6% Inflation

	A	B	C	D	E	F	G	H
	Return/Years	**10**	**15**	**20**	**25**	**30**	**40**	**50**
1	**6%**	113208	169811	226415	283019	339623	452830	566038
4	**8%**	108432	155505	198378	237425	272988	334879	128036
3	**10%**	104343	143691	176387	203555	226130	260474	98748
4	**12%**	100854	133908	159007	178066	192538	211873	82327

TABLE 2 At 8% Inflation

	A Return/Years	B 10	C 15	D 20	E 25	F 30	G 40	H 50
1	**6%**	123319	194181	271985	357411	451206	667263	927727
2	**8%**	120000	180000	240000	300000	360000	480000	158552
3	**10%**	117322	168387	214976	257480	296259	363916	118036
4	**12%**	115220	158896	195311	225671	250984	289682	97028

TABLE 3 At 10% Inflation

	A Return/Years	B 10	C 15	D 20	E 25	F 30	G 40	H 50
1	**6%**	134500	222906	329300	457341	611435	1020061	1611887
2	**8%**	132927	209116	292626	384160	484490	714995	203249
3	**10%**	132000	198000	264000	330000	396000	528000	143969
4	**12%**	131677	189134	241642	289626	333476	410167	115701

So what's the take home for you?

I hope this chapter has given you enough reason to think about your loved ones' protection and enough motivation to purchase it. Arranging for that protection is not a big expense these days. You can buy term plans for your family and secure them. And remember, while concentrating on today is important, don't lose sight of the future. Hope for the best but be prepared for the worst!

Flashback Learning

- The first and most important lesson in insurance: Life Insurance is Life Insurance only. Don't try to squeeze in some investment angle.

- Taking life insurance is a courageous decision. It takes commitment to and love for the family to accept that life insurance is for them.

- Adequate life insurance is the most important gift you need to present to your family.

- Buy term insurance. It's simple and easy to understand.

- Not getting your money back from term insurance is just a mind block. Even if you did get the money back, you can't do much with it as it will have little value after so many years…

2 hour Action Plan

1. List down all the insurance plans you have and find out what your current life insurance cover is.

2. Now as the second step, find out the actual cover you need for your family.

3. In case you feel that your current life insurance policies are too costly and won't provide much value, discontinue them all.

4. Find out about term insurance plans from different companies and take action to purchase them. Make sure you have adequate life cover within the next 1-2 months.

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[1] Assuming you earn around 5-10 lakh per annum. Accordingly, a premium payment of Rs 10,000 will afford you an adequate amount of life cover. Otherwise too, the insurance premium that you pay will not cross 2-3% of your income per year in most cases.

Chapter 3

GET-SET-GOAL

“Setting goals is the first step towards turning the invisible into the visible.”

Very often in life, we don’t seem to have a plan. Everything “just happens”. Things are moving on each passing day in our financial lives too. We buy an arbitrary insurance policy because the salesman was really persuasive or some uncle (or dad’s close friend) happened to be an agent and sold us a policy to secure our future. We buy mutual funds because the poster on the road showed us a fortune and an opportunity we cannot miss! Our decisions are made based on our friends’ recommendations and what we see on the television or read on the internet. Just revisit your portfolio and ask yourself how much of it is because of your purposeful planning and meticulous thought? How often have you sat down, studied a product, compared it with other similar ones and then come to the conclusion that it is the most suitable one for you? When we have to fund a financial goal like our child’s education, or a car or house, it is then that we start thinking about how to generate the required money by sifting though our existing investments. We break FDs, withdraw cash from the bank, redeem some part of our mutual fund holdings and sometimes even go in for a personal loan, if possible! If things still do not fall into place, we just postpone the whole goal itself by a couple of years.

But all this leads to unnecessary stress. In today's world, where life has become nothing beyond going from home to the office and back, we just ignore out financial life. We have started taking actions in our financial life only when we reach that stage of "urgency". Sounds familiar?

An important principle of time management suggests that we must make sure that we complete the important tasks, which are still not urgent, rather than delaying them. We have many things in our financial life which are very important but not "urgent". So we do what we are best at: We postpone them! This could be purchasing term insurance, starting an SIP, making 80C investments, filing tax returns, etc. All these tasks are important but not urgent until some point of time. Once they become extremely urgent, that's the time we wake up and take action. It's very obvious that you cannot pay much attention to detail or undertake thorough research when you have reached that state of "urgency".

Shopping for products

Have you ever visited a super market with a list of items written down on a paper? If you have, you will notice that you tend to be more focused on what you have to buy and what you actually need. Now take a situation where you know that you have to do some shopping for your house, but you end up in a store without a proper plan. Even though you will buy most of the things you need, you can be sure that there will be some things which you have missed out! What's more, you tend to buy some items that are not really required and you probably even overshoot your budget because you buy additional items that you do not really need right now.

That's exactly what can happen in your financial life too. Sometimes, we are just shopping for products without a plan. We purchase products which are introduced into the financial market and make the headlines; we buy things which our friends and colleagues at work buy. We keep buying or investing for all the wrong reasons - like pressure from a family agent (who is an uncle/aunty), a perceived need to save tax, etc., and at the end of the day, we call it our "portfolio". It's time to accept the fact that what we have accumulated over the years is mostly governed by randomness and a lack of planning and strategy.

In this chapter, I will give you reasons to change the rule of the game and show you why it should be the other way around, i.e. you must first decide what you want to achieve financially in your life, fix your priorities and then buy products or invest in such a manner that it helps you to achieve your targets. It's like deciding on your main destination and a route that you would like to take to get there and then finally planning your whole journey (based on the destination and the route that you choose). You can decide on your pace and speed based on your stamina.

What is your target?

Why are we in this world and what is our life's objective? Why are we working hard at the jobs we have? For a moment, just ask yourself why you are reading this book? What is that one single reason that makes you go to work everyday? If you say "To earn money!", I will give you 9/10 points for your answer; because you were true to yourself. Everyone is here to earn money at the end of the day but if you go one level deeper, you will realise that earning money is not the final goal. It's because you want to do something with that money that you are working and earning; effectively, you are working to reach your financial goals in life.

All of us have some financial goals. These may include buying a nice house, a second house, going on a world tour, getting a better regular income, funding your children's education, a retirement free from money-related worries, etc. What do you think would happen if someone comes to you and tells you that all your financial goals in life will be met? With a 100% guarantee; irrespective of how much you earn; no matter what happens; in fact, even if the world were to end! Your goals will all materialize.

Then do you think you would still carry on with your investments? Would you still worry about buying the best mutual fund and not the 3rd best one? Would you still shift your investments to a new financial product for that extra 1% return?

No, you wouldn't. I am sure that you would then concentrate on how to achieve your goals faster rather than on how much returns, product names, fancy strategies… You would start thinking at a different level and that would result in a simple financial life! Your only concern would be how to achieve your financial goals fast and as easily as possible.

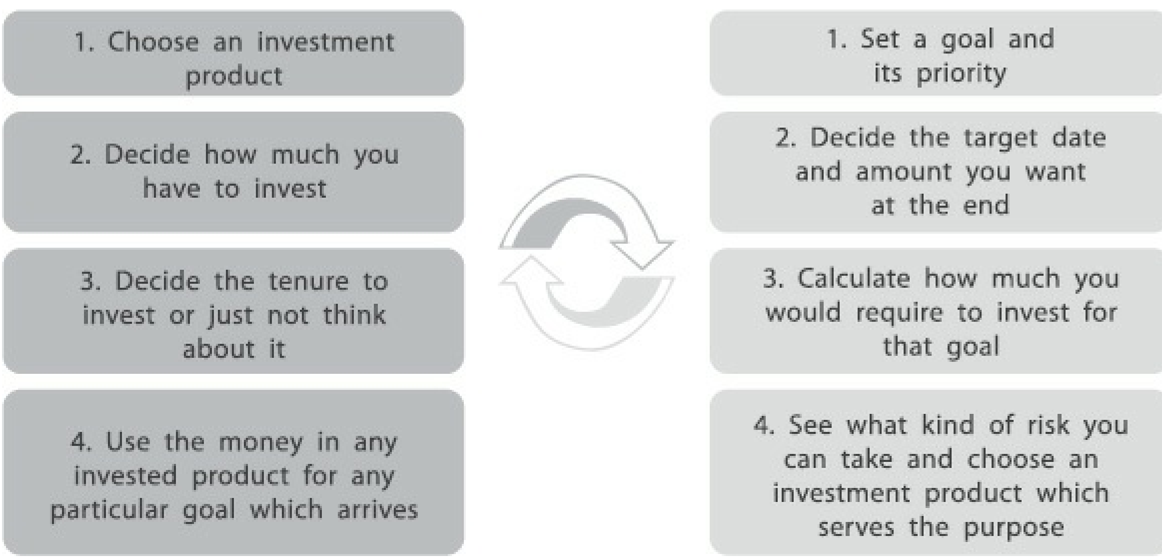
Change your process by 180 degrees

For a moment, let me tell you that whatever you are doing in your life is actually fine; all you need to do is just tweak it a bit.

Most people make their investment decisions like this: They find some product they want to invest in. They hear about it in an advertisement, or via the internet or through some friend or in a sales call. They look at the product and try to see if they get excited about it or not. If they are, then they take the next step and decide how much they want to invest in it. The popular numbers you will hear from agents are ₹ 12,000, ₹ 24,000 or ₹ 60,000. These are all multiples of 12, so that there is a nice round number for each month. You start with whatever fits your budget.

A majority of investors do not consider how long they plan to invest in a product at the time when they begin investing. They think about it later, perhaps once they start facing a financial crunch or they feel that there is something more exciting in the market. Then they say goodbye to the old product. Usually, the last step is to think about how that money will be used. The decision regarding which goal in life will consume the money blocked by that product is determined by the "urgency" of the situation. So, if you suddenly decide to buy a car or make a down payment for a house or come up against any medical emergency, you tend to disinvest from some financial product.

Now this approach has some issues, which we will look into in a moment. But let me tell you that all the steps taken are correct; unfortunately, they are not in the right order. To get the maximum from our investments, what we need to do is change this whole approach by 180 degrees and follow the reverse order. The whole experience will be more satisfying and have less stress overall. The right way of doing the planning is to first focus on your financial goals in life. Once you set a goal, you can choose the time required to achieve that goal and also an approximate amount you have to generate towards meeting it. After that, you can decide which financial product to invest in. Notice that all these steps are much the same, but reordering them results in a more robust structure.



Difference between wish lists and goals

“Unless you know which port you are sailing to, no wind is favourable.”

A lot of people think that their goals in life are pretty clear. After all, there is an obvious list of goals like buying a home, educating one’s children and saving for retirement, to name a few, which everyone strives for… However, these are just wish lists, nothing more. If I ask you to keep your goals in front of you and then take a photograph of them, what will that photograph look like? Let me tell you: It would look as if you shot it with a cheap quality camera, which you bought second hand from Janata Market! Yes, you may be able to see blurred shapes, no fine details and naturally, you will have no motivation to frame it up!

Here's an example to explain what I mean: One of my friends told me a couple of years ago that his goal was "to buy a house". When I recently asked him about it, he told me that even today he has it on his list of goals. I don't think it's his 'goal'; it's only his 'wish' because he never thought carefully about it and has never defined it in detail. So, naturally, he can't create an action plan for it and start working towards achieving it. If he has no idea of 'by when he wants it', 'how big he wants it', 'which part of the country he wants it in', then how will he start moving towards getting it?

I am sure he will not get it at this rate. He needs to define his goals smartly. And when I say smartly, I mean it should have proper dimensions- be of a certain size, realistic and aligned to his potential. A lot of people call this setting SMART Goals.

Smart Goals - Smart Results

Let me ask you a question: Can you share what is on your list of "things to achieve" in your financial life this year?

You will think for a moment and then say of course I have a list, so what if it is not written down; its in my head and it is very clear to me. You will start saying," I want this thing to happen" and "I want that thing to happen" this year. But is all of this written down somewhere, where you can see it? No, it is not. For a moment, really check: Are you and your goals are on the same page or not?

Now, we have heard a lot about goals. We have also heard about SMART goals all our life and it is one of the best tools to define and achieve financial goals. Most people try to set SMART Goals but they miss out on something. It is important to see where your SMART Goals are leading you eventually. What purpose do SMART Goals serve after entering your financial life?

Be clear that setting SMART Goals is one thing and achieving SMART Goals is a very different thing. Setting SMART Goals can be the first step of the process. The car called ‘Goals’ needs fuel called ‘rigor’, an engine called’ monitoring’ and a steering wheel called ‘scorecard’ to run at its top speed.

Financial Goals that aren’t tracked and scored are meaningless. Imagine watching a football game for 3 hours without knowing the score? Wouldn’t that be a waste of time? Without knowing the score, who cares about what they’re doing down on the field.

Keeping the score leads you to achieving your financial goals.

The real benefit of setting SMART financial goals is achieving SMART Results!

Success – Setting SMART Goals leads to **Success.** Your bank balance will tell you the truth about whether your goals are SMART Goals or not. To experience financial Success, set one SMART goal in your financial life and see the difference. Then set another and then the next one.

Momentum – Setting SMART Goals builds **Momentum.** It gets you into action as you are very clear on what needs to be done towards each financial goal of your life. Your financial project begins to gain momentum and velocity.

Attitude – Setting SMART Goals leads to the right **Attitude.** Your conversation about personal finance gets different and you become a student of wealth. Your attitude can make or break your financial life. The right attitude leads to higher financial success.

Reality – Setting SMART Goals grounds you in **Reality.** It is important to get grounded with numbers as numbers don't lie; the more grounded you are, the better it is for you. It actually reinforces your confidence in your own financial goals.

Trust – Setting SMART Goals generates **Trust.** When you produce results in your financial life, you start trusting your decisions and that helps you to move forward. You not only do well; there is a point where you also start helping other people to achieve their goals.

SMART Results start showing up almost immediately when we keep score of setting SMART Goals. So, let's add a new meaning to SMART:

When GOALS are:	**S-M-A-R-T**	**These RESULTS arrive:**
Specific	S	Success
Measurable	M	Momentum
Attainable	A	Attitude
Relevant	R	Reality
Time-Based	T	Trust

Categorizing your goals

Use bucket lists

It’s not unusual to find that you have a number of goals in your life. Quite often, you could get confused about which one to take up first and which ones you can leave for fulfillment later. Naturally, you cannot entertain all of them at the same time. Also, it might so happen that you have too many goals which might not makes sense, given your current and future earning capacity. The best way to take care of such a situation is to categorize your goals into committed goals and interested goals.

Committed Goals

Committed goals are those goals for which you are truly committed to achieving. These goals are most important in your life and you are ready to compromise on other goals to achieve them. For a lot of people it includes children’s education, retirement, buying a house. These are the goals which are a priority for you and given any crisis situation, the thought of not achieving these goals will worry you.

Interested Goals

Interested Goals are those goals which take a backseat in someone’s mind. There is nothing wrong in having interested goals. But most people would not like to achieve these at the cost of their committed goals. It generally includes vacations, a bigger car, a second house, etc.

The whole idea is to categorise your goals into committed goals and interested goals so that you can gauge how much money you have to collect towards achieving them. You can first cover the committed goals and only if you can still afford to, you can move towards the interested goals.

Here are some hypothetical examples of these goals and how they can be categorized:

	Committed goals	Interested goals
Near Feature	• Initial expenses on child: ₹ 2 lakh Future in 2015 • Invest in a unique startup idea in year 2016: ₹ 2 lakh	• Vacation abroad with spouse ₹ 5 lakh in 2016
Distant Future	• Child's higher education expenses: ₹ 40 lakh in 2035 • 60% down payment money for a house: ₹ 45 lakh in 2025 • Retirement corpus: ₹ 5 crores in 2035	• House in a small town: ₹ 15 lakh in 2025 • Passive monthly income of ₹ 50,000 per month starting in year 2030

This way, you can categorize your goals according to their importance. You need to categorize your goals because not everyone in your life might think alike. Ask your spouse what she thinks about a certain goal. How important is it for you? How much will be the target amount? Based on these answers you can find out how much you can save per month and the maximum investments you can make.

The next part is to link each of your goals to an investment. You can make seperate investments for each of your goals. That could make tracking them easy. For instance, you could start SIPs in mutual funds for your children's education; you can invest in a PPF account for the goal of starting your own business and invest in debt oriented funds for your vacation. This way you know how your money is growing in each product. It will also lead to diversification of your overall portfoilio.

However, a lot of people prefer not to differentiate between investment products on the basis of goals. They would rather keep all their investments in a variety of products and then take money out of the pool of wealth as and when the goal arrives. You can choose either of these methods, depending on what looks better to you.

Make small promises to yourself

Have you noticed a very simple fact in life: We all make promises to ourselves and then break them very easily. For instance, we promise: “I will reduce my weight by 25 kgs in 1 year” or “I will quit smoking in 3 months” or “I will save ₹ 5 crores for retirement”, and so on. These are all wonderful goals and very inspiring and we have to set these goals for ourselves to move ahead in life. But still, most of the people who set these goals never remember them within the next 1 month. These intensions just evaporate or at best, we start working towards those goals but then, in between, we giveup. Let us see why this happens and how we can make the situation better by changing the way we look at them. There are two different kinds of goals outcome goals and process goals.

Outcome goals

Almost 99% of all the goals which a person sets are outcome goals. Outcome goals are those goals which have an outcome at the end of a particular period; they involve meeting a target. To achieve these goals requires a lot of effort. All the examples we saw above were of outcome goals. Most people set these goals and start trying hard to achieve them. In the process, they create a situation wherein they are overwhelmed by the goal itself. The goal, which initially inspired them or gave them happiness, now begins to haunt them.

After a while, they start feeling that “it’s unachievable”. We lose interest in the goal because we feel there is no point in trying so hard.

Process goals

While outcome goals involve setting a target and overwhelm you at times, there is a better and a more systematic approach to achieving outcome goals. The well known secret is to create process goals. Process goals are nothing but mere small and ‘easy to achieve’ tasks, which you can complete daily, without feeling overwhelmed. You can be sure that you can do it. These are power goals, which give you a sense of achievement every time you complete them. It makes you a winner each time you complete them and shows you that you can do it. Such goals do not give you room to make excuses because you can complete them comfortably.

Here’s a very simple example of a process goal:

One of my friends has a goal coming up after 20 years – he wants to have a substantial corpus of funds to spend on his child’s education. To achieve this goal, he had to invest ₹ 2000 per month for the next 20 years. Setting aside a sum of ₹ 2000 per month may look easy enough, but at the end of the month, after all his bills were paid and he was already running low on funds, that ₹ 2000 felt like a big chunk of money.

He managed to scrape together the funds for a month or two and then he began to lose focus. It started to look unachievable. He used to feel awe-struck when he focused on his larger goal of collecting ₹ 30 lakh after 20 years. And once he skipped setting aside the ₹ 2000 for a month or two, his motivation dwindled further and his goal seemed to die a natural death.

Then, as fate would have it, his wife intervened. Somehow, she made sure that she extracted ₹ 100 each day from him and put it in a piggy bank. By the end of the month, she comfortably had a sum of ₹ 3000 to invest instead of ₹ 2000; all because it was easier to save ₹ 100 per day than ₹ 2000 per month.

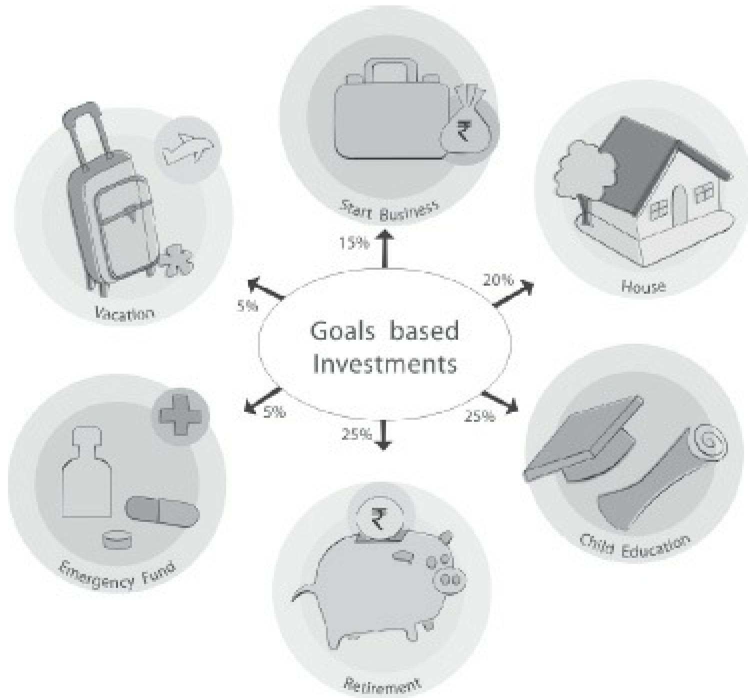
This is an example of a process goal.

Here are some more examples of how outcome goals can be broken down into process goals:

Outcome goals	Process goals
Lose 25 kgs in 1 year	Walk for 20 minutes per day, eat 1 less pizza per month, exercise on Wednesday and Saturday for 1 hour
Quit smoking in 3 months	Have 1 less cigarette each day for next 15 days and thereafter keep reducing 1 every 15 days.
Garner ₹ 30 lakh in 20 years	Keep aside ₹ 100 per day in a piggy bank.

Advantages of goal based investing

Once you are clear about your goals, you start investing towards them. There are some advantages of linking your investments to your goals. For instance, you can invest in mutual funds A and B for your children's education. You can invest in a PPF account to meet your daughter's marriage expenses and you can invest in index funds to build up your retirement corpus. There are 3 main advantages that arise from goal based investing. These are:



1. It keeps you more focused and disciplined

Suppose you planned for your financial goals in life-you have taken your term insurance; you have started SIPs in mutual funds for your long term goals; you have also started investing for your retirement. Now here's what happens… as you have set your goals and understand that each of your actions is going to take you closer to your goals, you will be inspired to make sure that your premiums continue, your SIPs keep going and you don't disturb your investments for insignificant reasons. If you go on a vacation, you will make sure that either it's planned separately or it's scheduled only when your bigger and more important goals are achieved.

If some new product hits the market, you will be less curious to find out what it has to offer you, as you have already started taking action towards your goals and are already on the path to achieving them. You will not waste your time and energy on it because you have already planned for everything and all you need to do is be disciplined enough to follow the plan and review it again after few years to make sure that you are on track. You will notice that the biggest advantage of goal settings is that it inspires you to be committed and gives clarity to your financial life.

On the other hand, if you have no goals set, you have no idea how much to save or how long you need to keep saving or what kinds of products you should be investing in. Every now and then you will consider investing in fresh products; products of the month. You invest in a particular mutual fund and then shift to another, incase the first one comes down in ranking. Incase you have no goals set, you will just be putting your money in arbitrary products, without understanding how they are going to lead you to your financial milestones!

Let's say you have a goal which is to collect a certain amount of money for your children's education. Towards this end, you invest in two mutual funds for the long term. You know that after 15 years you will garner enough funds to help you achieve this goal. Now, when you have to buy a Plasma TV in between, will you say, "Let's take some money out of our kids future education money and buy it"? I don't think so. However, if there was no goal associated with that investment and you had no targets and you were just investing your surplus money in those mutual funds, you would say, "Let's take some money out of these funds and we will invest more in them next year." You see the behavioural change?!

2. You don't disturb compounding

Imagine you have not set any goals; you have no investments as per a plan and their are no target dates. What do you do when suddenly some unnecessary or low priority expenses comes up? You dip into your investments and break them to use the money. The other thing which we keep doing in our financial lives is that we keep on shifting our money from one place to another. It can mean selling something, keeping money in cash for some months, if the markets are doing badly and then investing it later in some other instrument. Do you see what is happening here?

You are disturbing the wealth creation process. Money does not grow when you keep disturbing it. This is not because you have less capital to invest or because you lack knowledge. It’s because you just don’t allow it to happen. You disturb it! You have clearly seen in the first chapter that compounding has to happen and linking your investments to goals will make sure you don’t disturb your investments for a long time.

3. You realize that your financial life is unique; you stop comparing it with that of others

One of the major advantages of setting goals and then linking your goals to investments is that you separate your financial life from the rest of the world and start chasing your goals rather than out performing your peers! It’s an understanding between you and your financial life, where you are convinced that if you follow what is required, you will achieve a goal, maybe early or a little later, but eventually you will.

Imagine this: You start investing ₹ 5,000 per month towards your child’s education. You know that if you make 10% year on year, in 20 years you will reach the target of approximately ₹ 50 lakh. Now suppose in a particular year, your mutual funds gave a 21 % return, but your friend’s mutual funds gave a 34% return. This will definitely make you think that your fund performed poorly compared to that of your friend. But you know that you are still on your path and have outperformed your own benchmarks. You have made better progress than expected. On the other hand, if your funds give a 5% return and your friend’s mutual fund gave a negative 10% return, you might be a bit relaxed and happy about the fact that atleast your mutual funds performed better than his. But the next moment you will come back to your own financial life and feel that whatever the case, you have under performed your target of 10% each year.

In both cases, it will be about YOU and YOUR GOALS first and only then will you see it from a comparison point of view. If you don’t have any goals and targets, the only benchmark you have is a comparison to others. Then you start looking at your friends' returns, the best funds in India and the average in the category in which you have invested. While all that is fine and required, to some extent, the only point I want to make is that after setting goals and linking your investments to them, your financial life becomes simpler and you have less things to worry about.

In the above example, the per-year-comparision was just for illustration. You should not be worried just because your mutual funds didn't perform well during one particular year. You would be better off considering the returns over a longer time span. In our example, you could check if your funds have given a 10% yearly return for a 3-4 year time frame before you get judgmental.

Flashback Learning

- Goal setting is the first thing you have to do in your financial life. It's the foundation of your financial house. Better make it a strong one.
- Make small promises, which are easy to achieve. This way you can reach your bigger goals.
- Linking your investments with goals in life keeps you more focused and satisfied in your financial life.
- Categorise your goals into different buckets so that you prioritise them and chalk out a plan.
- Whatever steps you are taking right now are all relevant steps individually. But they may not be in the right order. Just rearrange them!

2 hour Action Plan

1. Sit with your spouse (if you are married) or alone (if you are not) and list down whatever you want to achieve in your life.

2. Define the target amount and duration and also make sure you give a priority of “High”, “Medium” or “Low” to each goal.

3. Define what you are going to do to achieve each of the goals on a daily basis or monthly basis. Make sure you define the process goals for each of the main goals and then be disciplined in meeting those processes in the short term.

4. Identify how you want to start working towards each goal. If you are confused, choose a financial planner based on the value you get out of him and not just his fees. Fees are merely a number, which you will recover during the next month!

Chapter 4

BUSTING YOUR MYTHS ABOUT RISK AND RETURNS

Do you realise that the actions that you take and the decisions that you make today are a result of the good or bad experiences that you have had in the past? What would you say if I told you that whatever you heard or learnt in your life has an impact on how you think about a particular thing today? Let me tell you a story:

Fleas in the jar

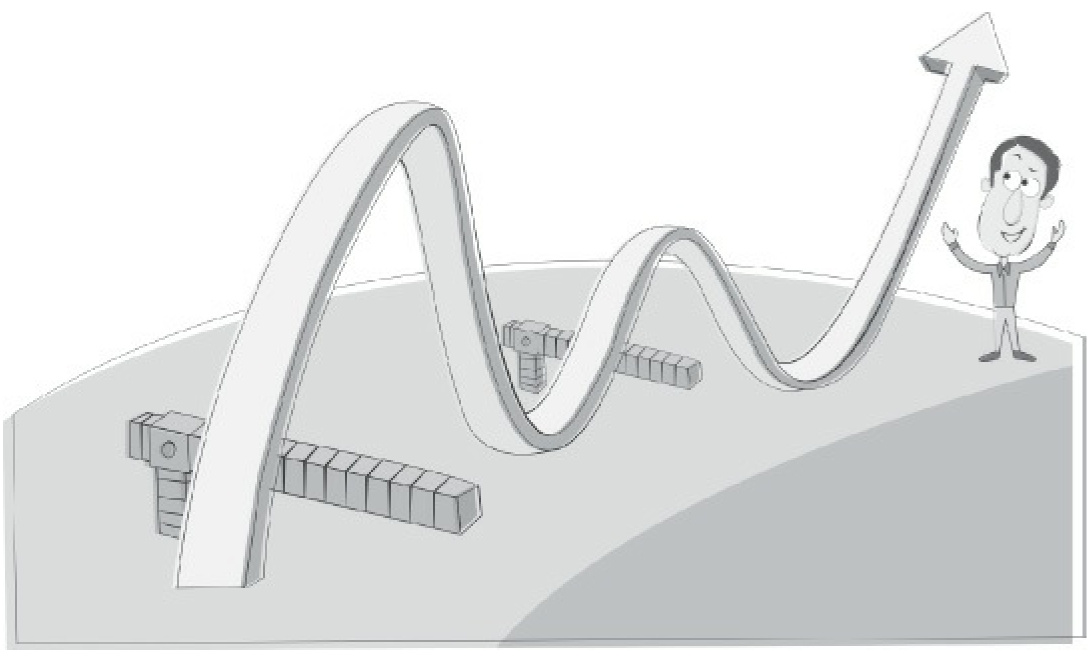
A scientist was conducting a study on limiting beliefs. For the experiment, fleas were collected and kept in a jar. A lid was put on the top of the jar. Little holes were made in the lid so that air could circulate in and out and the fleas could survive. Now, fleas can jump extremely high; so they tried to get out of the jar. Every time they tried to get out of the jar, they would hit the lid and get hurt. The fleas were smart; they started learning from other fleas' bitter experiences, just like you and me learn from experiences we hear about (most people have never experienced a loss from investing in equity but still they think equity is risky and therefore, stay away). They started communicating to each other about the danger of hitting the lid. They made sure that they did not jump higher than 1 inch below the lid.

The scientist kept observing the fleas. He was observing how the imaginary limits they had set kept them from getting too close to the lid. After a while, he removed the lid. There was no lid now; yet all the fleas were still constrained by the imaginary limit. The lid was on their mind and not on the jar.

All the fleas stayed within the "1 inch below the lid" limit. Over time, they convinced themselves that they were happy staying in the jar. Then one of the fleas decided to stray from the herd. He decided to experience the risk of going within 7 inch of the lid. He didn't wanted to be constrained by the other fleas' past experiences of hitting the lid. He took a risk; he broke the imaginary limit and got out of the jar. The whole world opened up for him.

We too get constrained in life by our imaginary limits. We have learnt the art of staying comfortable within our imaginary investment limits. Investment or money management is a skill and can be learnt by anyone. The instruments are not risky but our half-knowledge and imaginary limits make them risky in real life. It's time to break your imaginary lids and welcome new investment opportunities in your financial life.

Our past experiences



Imagine a family in which the main bread winner lost a lot of money in the stock market. His family, which was once very happy and rich, saw all their wealth and happiness washed away by market crashes. Obviously, after this happened, they made no further investments in the stock market. Everyone stays away from the markets or anything which has any element of stocks in it. Now, let’s zero in on a small child in this family. He will always hear statements like, “Stock markets are evil”, “Never invest in stocks”, “You will loose everything in the markets”, “Stocks are nothing but gambling”, etc, etc.

When this child grows up, what do you think he will believe about stock investing? Will he be comfortable with mutual funds, ETFs, investing directly in stocks? No, very unlikely!

In the same way, let’s take another example:

Think about a family who made a lot of money during a stock market boom, with or without a sound knowledge of stock investing; that’s not relevant to our example. The only thing is that they made money, and a good amount of it. Apart from this, the bread-winner of the family earns his main income by investing in someone else’s business, taking losses sometimes and usually making huge profits at the end of the year. This family has never seen a bad money crunch. The father rose from being a small middle class person to a rich man. This family believes that taking a risk had always resulted in something good. Yes, there were pains and problems, but eventually it helped them. What do you imagine a small child from this family grows up thinking (and experiencing)? Well, “Returns come only when you take risks”, “Stock markets are not for fearful people”, “If you want to grow rich, you need to be an enterpreuner”, etc, etc.

When this child grows up, if you ask him to put his money in an endowment plan for the next 20 years, will he listen to you? No! He is conditioned to think in a certain manner and that’s in his blood now. I am not saying he will personally be successful in the stock markets, but he might be ready to take the risk of investing in them.

These two examples must have given you some idea of how our past experiences and people we associate with, leave a powerful impact on us and our approach to certain things. This is very true of our financial lives too.

As a financial coach, I take upon myself the task of ridding you of two misconceptions:

1. Equity is very risky (stock investments, equity based mutual funds, ETFs and ULIPs)

2. Debt products are safe and secure (fixed deposits, PPF, NSC, bonds)

Equity is Risky

For readers who don’t know, let me quickly explain what equity is. In simple English, equity means ownership. So, in the world of investing, equity would mean any product which is related to the stock market, and the underlying instrument is shares. This product could come in various forms like stocks, equity mutual funds, ULIP’s, ETFs or Index funds.

Getting back to the myth - “Equity is risky” - if someone tells you this, just ask him what he means by it. In all probability, the answer will be “You can loose your money” and it will be followed by dozens of examples of people who lost money by investing in shares. And guess what, they are right to some extent. But the only problem here is that they have limited knowledge and a limited number of examples. They have looked at one part of the story and not at the complete story. Most of these people are short-sighted and concentrate on short term investments.

Investors who do not invest in equities for the long term may have this opinion too-”Equity is Risky”, and they invest in PPF accounts, FDs, insurance plans for years and years, decades at times. They are 30 years old and they invest in PPF accounts for their retirement.

Investing in Equity is “Investing in an Idea”

Most people who invest in stocks and fail to make money never look at them as an asset. They don't perceive stocks the way they would perceive a house or land or jewellery. They never feel as if they are investing in a business, which is someone's idea. They feel as if it's a quick way to make money. If you are going to invest in equity, keep in mind the fact that you are actually buying into an underlying idea. Investors who have stayed invested in Bharti Airtel or Infosys for years and years are investing in the ideas which these companies have. Its not just "investing for profit".

I will share with you some very simple statistics, which show you how equity has given excellent returns to those who have had the patience to wait and let their investments grow over the long term, i.e. a period of 8-10 years or more. I will show you that the risk of making a loss from equities comes down with each passing year.

Learning from History

Let's begin by taking a look at some instances from the Indian markets. For the sake of simplicity, and to convey the concept, I have taken the index value of the Sensex for my calculations. One can also invest in index these days through an Index fund, which mimics an index value, however even if one invests in a mutual funds, same kind of results should be expected. I have recorded the Sensex value at the start of each year, i.e. the first day on which the market is working each year. More explicitly, the values are those recorded on the first working day in January each year, starting from 1980 right up till 2010 (a total of 30 years).

Now in the last 30 years, there were different instances of various holding period. To illustrate: there will be 30 different instances of 1 year holding periods, like 1980-1981, 1982-1983 till 2009-2010. What this effectively assumes is that you invest at the start of each year and sell at the end of that year.

In the same way, there are 29 different instances of 2 year holding periods, like 1980-1982, 1981-83 and so on, till 2008-2010. Then there are 28 different occurrences of 3 year periods etc etc.

Now take a look at a table which shows the returns generated for different time frames. All percentages are for yearly compounded returns or CAGR, as it is called.

Duration of Investments

	A Year	B Index Value	C 1 year	D 2 year	E 3 year	F 5 year	G 7 year	H 10 year	I 15 year
1	1980	118.16	29%	46%	26%	18%	24%	21%	26%
2	1981	152.26	66%	24%	18%	29%	16%	21%	22%
3	1982	253	-7%	0%	3%	16%	15%	23%	19%
4	1983	236	7%	8%	33%	13%	19%	27%	20%
5	1984	252.8	8%	47%	29%	21%	22%	30%	18%
6	1985	273.41	101%	41%	17%	23%	32%	31%	22%
7	1986	549.43	-1%	-11%	6%	13%	24%	19%	14%
8	1987	542	-19%	10%	13%	29%	30%	20%	13%
9	1988	439	50%	34%	32%	42%	37%	24%	15%
10	1989	659	19%	23%	44%	39%	25%	17%	16%
11	1990	783	28%	58%	48%	38%	23%	21%	15%
12	1991	999	96%	59%	51%	26%	21%	15%	16%
13	1992	1957	30%	33%	26%	11%	7%	5%	14%
14	1993	2539	36%	24%	7%	8%	11%	3%	15%
15	1994	3465	13%	-5%	-2%	-2%	2%	5%	7%
16	1995	3932	-20%	-9%	-2%	6%	-3%	5%	10%
17	1996	3127	4%	9%	-1%	5%	1%	12%	
18	1997	3260	13%	-3%	18%	0%	9%	16%	
19	1998	3694	-17%	21%	2%	-2%	9%	19%	
20	1999	3060	76%	14%	2%	14%	17%	12%	
21	2000	5375	-26%	-22%	-14%	4%	15%	13%	
22	2001	3955	-18%	-7%	14%	19%	26%		
23	2002	3246	4%	35%	27%	34%	17%		
24	2003	3390	74%	40%	40%	43%	26%		
25	2004	5915	13%	26%	33%	11%			
26	2005	6679	41%	44%	45%	21%			
27	2006	9390	48%	47%	2%				
28	2007	13942	46%	-16%	8%				
29	2008	20300	-51%	-7%					
30	2009	9903	77%						
31	2010	17558							
		Total positive return instance	22	20	24	23	23	21	16
		Total instance	30	29	28	26	24	21	16
		% positive instance	73%	69%	86%	88%	96%	100%	100%
		Simple average of top 5 best years	85%	52%	46%	39%	30%	27%	22%
		Average of worst 5 yrs	-27%	-13%	-3%	1%	3%	6%	12%
		Average of all + years	40%	35%	23%	21%	19%	17%	16%
		Average of all - yrs	-20%	-9%	-5%	-1%	-3%	None	None
		Average of 5 bad but + years	7%	12%	3%	7%	5%	7%	12%
		Best Return	100.95%	59.42%	51.37%	43.04%	36.78%	30.55%	26.32%
		Worst Return	-51.22%	-22.29%	-14.24%	-2.46%	-2.70%	2.93%	7.25%
		Difference	152.17%	81.71%	65.61%	45.50%	39.48%	27.62%	19.07%

How to read the table

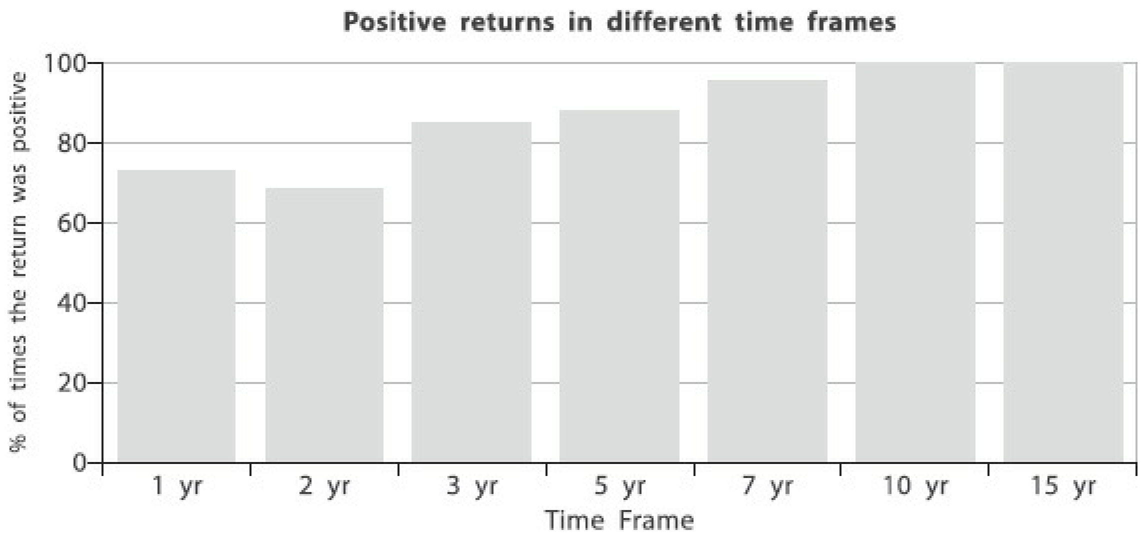
If you take any arbitrary cell from this table, say cell E5 which has 29%, it means that if someone had invested an amount of money for 3 years, starting 1984, he would have reaped an annualised return of 29% (CAGR). If you double check my calculations, you can see that the index moved from 252.8 to 542 in 3 years, that means that it gave a total return of 114% for a 3 year period on an absolute basis. Accordingly, if we consider a yearly compounded return, it would be 29%.

By now, you may have got some idea about why I said at the start that "Equity is not so risky in the long term", but let's look at some strong indicators which give us proof that long term investing has given great returns.

Positive Returns

Let us see how many times the markets delivered positive returns when investments were made for specific numbers of years.

Investment Tenure	1 year	2 year	3 year	5 year	7 year	10 year	15 year
Total positive instance	22	20	24	23	23	21	16
Total instance	30	29	28	26	24	21	16
% positive instance	73%	69%	86%	88%	96%	100%	100%



You will observe that as the tenure of investment increases, the percentage of times one could have got positive returns increased. In the case of a 1 year investment duration, there were a total of 30 instances, out of which 22 offered positive returns. If you consider a 5 year tenure, 88% of the instances gave returns that were positive and when the holding period or tenure is raised to 10 years or 15 years, no one lost money even a single time!

Quantum of returns

It's not enough to just look at the number of years for which you could have got positive returns, but also the quantum of those returns, on an average. While there are quite a few instances when there were positive but low returns, we have to look at the bigger picture and concentrate on the average scenarios. So, lets look at some of the figures from the quantum of returns point of view. One thing you, as an investor, have to understand is that the longer the time frame, the more stable the returns are and the less they are prone to luck and short term fluctuations.

Highest and lowest returns

Let's consider the returns for the 1 year holding period: different instances gave different returns, ranging from 100% to negative 50%, at times. But the moment you look at a 5 year holding period (for which there are 26 instances), the range between the highest and lowest returns contracts and becomes 43% (2003 - 2008) on the upside and just negative 2% (1994-1999) on the downside. When you further increase the holding tenure to 10 and 15 years, you see a much tighter range and even the lowest returns are positive. Let's look at the table below, which shows the highest and lowest returns in different time frames for the 30 year period.

Tenure	1 year	2 year	3 year	5 year	7 year	10 year	15 year
Best Return	101%	59%	51%	43%	37%	31%	26%
Worst Return	-51%	-22%	-14%	-2%	-3%	3%	7%

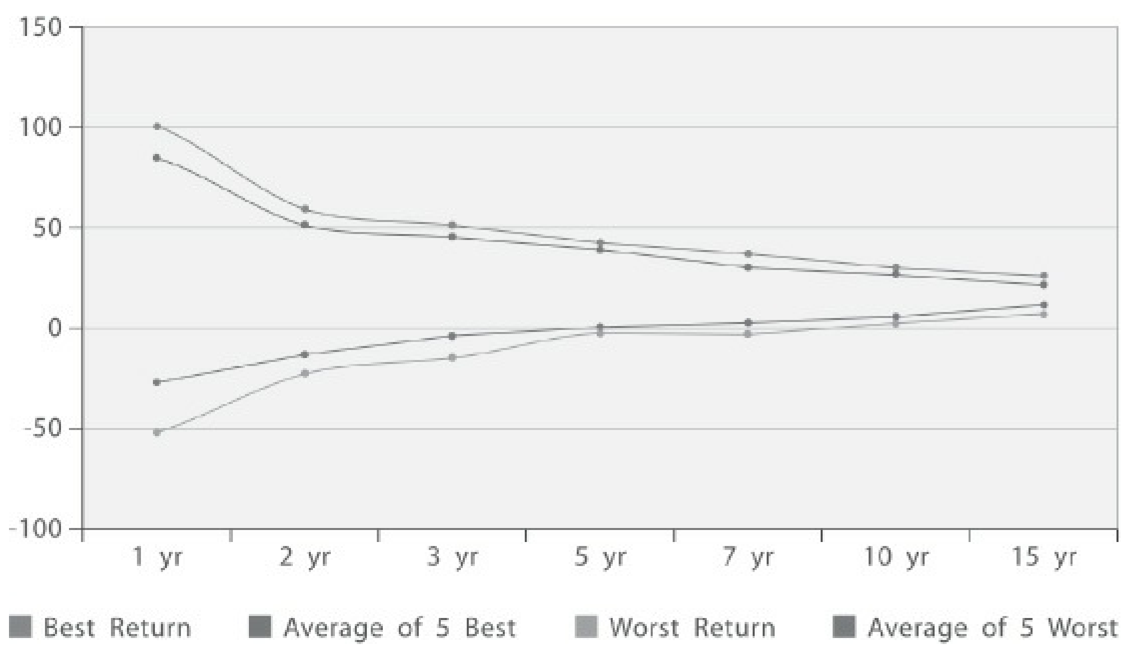
The 5 best and worst returns

Many people will query, "What if I don't actually invest in the time frame which delivers the top returns, then will I still be doing well for myself by investing in equity?" To clarify, let's look at not just the top returns, but the average of the 5 best returns in all the time frames. You can see that not just the top most, but the average of all the top 5 best years are also good and in fact, very close to the top one. This means that your chances of getting high returns are much higher than you think.

On the other hand, if things go wrong, do you lose as much as the worst returns or thereabout? Not really. As you can see in the table below, the average of the worst returns are almost half of worst return in magnitude, in cases where the returns are negative and at least double the worst returns, in cases where the worst returns are positive. So on an average, your bad returns are not likely to be very close to the worst return.

Look at this statistic for the holding period of 15 years: the average returns for the 5 worst instances was 12 percent!

Tenure	1 year	2 year	3 year	5 year	7 year	10 year	15 year
Best Return	101%	59%	51%	43%	37%	31%	26%
Average of 5 Best	85%	52%	46%	39%	30%	27%	22%
Worst Return	-51%	-22%	-14%	-2%	-3%	3%	7%
Average of 5 Worst	-27%	-13%	-3%	1%	3%	6%	12%



Negative returns

You can't get positive returns every time. Sometimes you are faced with losses. So let's look at negative returns too. While it's true that there are bad years, by now we can see that bad returns come down with an increase in the investment tenure. For instance, take the case of 1 year instances: if you take an average of all negative return years, it works out to -20%, whereas it decreases to - 5% for 3 year tenures and 0% for 10 year or 15 year investment tenures.

We'll let the data speak for itself…

Tenure	1 year	2 year	3 year	5 year	7 year	10 year	15 year
Worst Return	-51%	-22%	-14%	-2%	-3%	3%	7%
Average of worst 5 years	-27%	-13%	-3%	1%	3%	6%	12%
Average of all negative years	-20%	-9%	-5%	-1%	-3%	NA	NA

Note that all these illustrations assume that the investments were made at the start of the year, i.e. January. But if you look at the pattern for investments made from June to June, it will be quite similar.

Equity is risky in the short run and quite safe in the long run

The data I shared with you above shows you that in the short term, equity can be very volatile and it is difficult to gauge which way markets will move. But over the long term, it becomes more stable as well as safe. You can expect good returns from equity in the long run. There will naturally be some cases in which the returns have not been great even with long investment periods. For instance, investments for a 10 year period from Jan 1993 - Jan 2003 gave a return of just 3%; but that's very rare. It does not happen in general. That's the risk of investing in equity which you take in order to get higher returns. Also, note that this is true for an index like the Sensex or the Nifty and it would be similar for mutual funds, which do not rely on a single stock. You might get very different results for some single stocks.

So, if you believed that equity is risky and that's why it's not for you, you would be right, if you wanted to invest only for the short term. If, on the other hand, you have a long term view for your investments, equity is something you should definitely invest in, especially if you are young and have plenty of time on your side. Also, remember that the data shown above is based on the assumption that you don't monitor and review your investments. In case you put in elements of monitoring and active review, your returns could get a further boost.

Are Secure Products really Secure

In this section my aim is to break one of the biggest myths in our country which is "Debt products are very safe". Now, if your definition of "safety" is assured returns and "the face value of your investment not going down", you are correct. But let me tell you that your definition of safe products is flawed and it can pose a problem in your financial life.

When we think about "safety", we only think about assured returns and security of capital. We forget to look at the maturity value in terms of its purchasing power.

When we say "debt products", we mean any product which does not have much of a risk element and we are more or less very sure of getting our money back. This includes fixed deposits, PPF, bonds, insurance plans or debt schemes of mutual funds. The biggest problem with debt is that it does not have the strength to fight inflation. Inflation, over the long run, erodes the purchasing power of your money and debt products give returns which barely compensate you for inflation. If you factor in taxes as well, you will be left with nothing in real terms.

A safe investment is of no practical use if it does not have the power to help you reach your financial goals. It's like going onto the cricket ground with your head, legs, stomach, everything, covered…you can be sure that you will not be hurt; you will be "safe". But guess what? I would not like to be in your team because your safety does not help you to hit 6s and 4s, which could make us win. In all probability, you will lose! But I have no doubt that you will be "safe".

We have always been taught that debt products like FDs, insurance plans, PPF accounts, NSC, etc., are very safe and there is no risk in these products. But that low risk factor is only limited to the fact that you will receive assured returns. It does not assure preservation of purchasing power.

Let me give you some examples:

Suppose you have ₹ 100 today and you want to buy oranges. If an orange costs ₹ 20, you will get 5 pieces. Suppose you invest this amount in an FD for the next 10 years, at the rate of 9%, your ₹ 100 will become ₹ 236. But what will be the cost of 1 orange be after 10 years? Even if it increases to ₹ 50, you will not be able to buy 5 oranges with that money 10 years down the line! This means that the purchasing power of that money has decreased.

Even though your money has grown, it has not grown in real terms. Its purchasing power has come down. That's the problem with debt and that's really something which should concern you. Just take a look at the previous generation, in which people purchased endowment plans with a sum assured of ₹ 2 lakh or ₹ 5 lakh or even ₹ 10 lakh. Their policies are maturing now and they safely get their money back; no risk. But will it help them to cope up with the escalated cost of living today? It can only help them survive in this world now; they will certainly not be able to enjoy the lifestyle they always desired because for that, they would require a lot more money!

This is one of the major reasons for limiting even your PPF account contribution. Don't over do it, even though it's a secure, government backed investment product, you might be losing out on a lot of opportunities to reap great returns from equity if you are over doing your PPF investments. Don't get me wrong; PPF is not a bad investment product. By all means have a PPF account and invest in it, but keep your investments within a limit. If you have 30 years in hand before you retire and you are saving ₹ 1 lakh per year, I don't see a reason why that 70k should go into your PPF account and the rest in equity; rather, it should be the other way around.

So what's your recipe for wealth creation?

Two simple yet immensely significant rules to remember are:

1. Equity is risky in the short term, but safe in the long run.

2. Debt is safe in the short run, but extremely risky in the long run.

The clear message to be gleaned from these is that for any short term financial goals, you should use debt products like fixed deposits, debt funds, etc., which do not have any risk element. However, for any long term goals, you should invest in equity, as far as possible. In the short term, the focus is mostly on achieving the goal and preservation of your money to reach that goal, rather than growth of your money. A great return with assurity can come only by luck; if you want a great return with low risk, then you will require "TIME" on your side.

I get a lot of questions on my blog, like "Where can I get the best return if I want to invest for 2 years? I need to make a downpayment on my house around then…" or "I want to invest for my dream restaurant around 20 years from now; should I buy an insurance plan?"

People who ask such questions have to understand what I just communicated. If you want fabulous returns in the short term and you also want to have safety, you are living in some unreal world. You can never get excellent returns with safety in the SHORT TERM; that can only happen in the long term.

Now let's consider different scenarios and see what you should do, using our rules - equity is for the long term and debt for the short term.

Case 1: You want to put up a down payment for a house 2 years from now; where should you invest?

In terms of time, you have just 2 years to go. So, you can't compromise on assurity or the safety of your money; the available time element is not adequate to allow your money to grow. In this case, you should be investing this money in some safe products like fixed deposits or debt funds, if you can take some very nominal risks. But under no circumstances should you be investing your money in stocks or equity mutual funds, if it has to go towards meeting your down payment.

Case2: You want to start a restaurant after 20 years; where should you invest?

You have ample time in hand. Your money has enough time to grow and hence, investing in equity is the answer, in this case. You can invest in debt products too and have your restaurant. But then it would be a small, constrained one. If you want to start a restaurant which will be the talk of the town, then you will have to invest in equity.

What your money plate should look like

By now, you are very clear about 2 things - that equity products are for the long term and debt products are for short term goals. But does that mean that you should be completely invested in either equity or debt?

Have you ever given a serious thought to the food on your plate? It might consist of many items: it may have chapatis, dal, rice, curry, salads… Now imagine that one day you decide to eat just RICE. That's all! One hundred percent of your meal consists of RICE. Does it make sense? Will it be tasty? And more than that, will it be what your body needs? NO!

You need to eat balanced meals. They should have the right proportion of everything and yes, you may consume more of what you like or need to eat. For instance, some people like to eat a lot of salad; their meals may contain a lot of salad. Other people enjoy curries and their meals are likely to contain a lot of curry. But overall, a healthy, tasty meal will contain more than just one or perhaps two items.

In the same way, our portfolio should not be extremely tilted towards one type of financial product. You shouldn't have a 100% of your money in equity or 100% in debt, at any point of time. You should strike the right balance between the two and hold both in a combination which makes you comfortable.

Our financial life is very much like the food on your plate, wherein each financial product can be likened to some kind of food item. Over the long term, if we do not have a balanced financial life, which has exposure to each component in the right quantity, it will not be in the best interest of our long term financial health.

A balanced portfolio does not mean a 50:50 ratio of equity to debt. It means investing in a combination of debt and equity which makes you feel "comfortable" and at the same time, it has the potential to enable you to reach your financial goals.

To illustrate my point, here are the profiles of Rajesh and Ajay, two very close friends.

Rajesh: Rajesh is 28 years old. He is married to Kavita. Rajesh works in a software company where he earns very well; Kavita is a government employee. Rajesh wants to start his own company at some point of time and wants to retire early. He wants to make sure that his children pursue their education abroad.

Ajay: Ajay is 38 years old. He has two children and his wife, Heena, is a housewife. Ajay has already built up a large corpus over a span of 15 years.

He works in the middle-east and has a very high salary, but he has no job security. He plans to come back to India and start a business in his hometown, which is a tier III city.

Now if you imagine the current and future financial lives of both Rajesh and Ajay, they should look very different from each other because they at very different stages of life; they have different risk profiles and different goals. Can you imagine Ajay investing a major chunk of his money in equity mutual funds or pure equity and having very little or no insurance? On the other hand, can you imagine Rajesh with very little money invested in equity and most of his money in a PPF account, some FDs and an extremely large life insurance cover with his wife as a nominee?

As you can see, Rajesh is still very young and earning well. His wife also has a stable job. This couple can afford to take high risks in thier life. Even if things go a bit awry somewhere in their financial life, they have enough time and the scope to get back on track. As they have a lot of time in hand, they need to invest in equity for the long term, then be patient and let it grow. Obviously they need to take a good amount of life insurance, but must take into account the fact that Kavita is already in a secure job. Accordingly, they should not go overboard purchasing insurance.

On the other hand, you can see that Ajay's situation is very different. Being the only member of the family who is earning, he has to make sure that he has sufficient life insurance cover. It should be enough to provide for his family and supplement his savings till date. You can see that because of the nature of his job and his current worth and future aspirations, he needs stability from his financial life more than growth. So his exposure to equity should be limited and he should mainly concentrate on investments which can provide him with a monthly income. He should focus on debt products like MIPs, PPF and balanced funds rather than pure equity or equity funds.

So what is Asset allocation?

In simple terms, asset allocation is the exercise which involves dividing your money into different asset classes in some ratio which you feel comfortable with. So, if I am the kind of person who understands the stock market and I'm up to date with developments in the real estate sector, I can have 50% in equity mutual funds, 35% in real estate and the remaining 15% can be in FDs and liquid cash. Whereas, if you are a person who does not have the time to track your investments and are around 45 years old with many financial responsibilities, you need financial stability and should allocate 60% to FDs and PPF, 15% could be in the form of liquid cash and just about 35% can be Invested in stocks or equity mutual funds.

So you have to decide on your own asset allocation. It might not be a simple task. Ask yourself: If I have a total of ₹ 20 lakh in my portfolio, can I afford to put 50% of it in equity mutual funds? Will I be able to survive a hit in case markets move up or down? If your answer is yes, then you can allocate 50% of your money to equity and the rest to other asset classes. If you are not comfortable with 50% in equity, then ask yourself whether you would be comfortable investing 40% of your money in equity or perhaps merely 25%.

Different stages of life and a typical portfolio for that stage

Life keeps changing and with it, people's financial responsibilities and priorities change too. For convenience sake, we can break it down into 5 stages. Each of these stages is associated with a typical asset allocation pattern, which differs from one stage to the other. Here's a look at those 5 stages and what is usually recommended for good financial health:

1) Bachelor

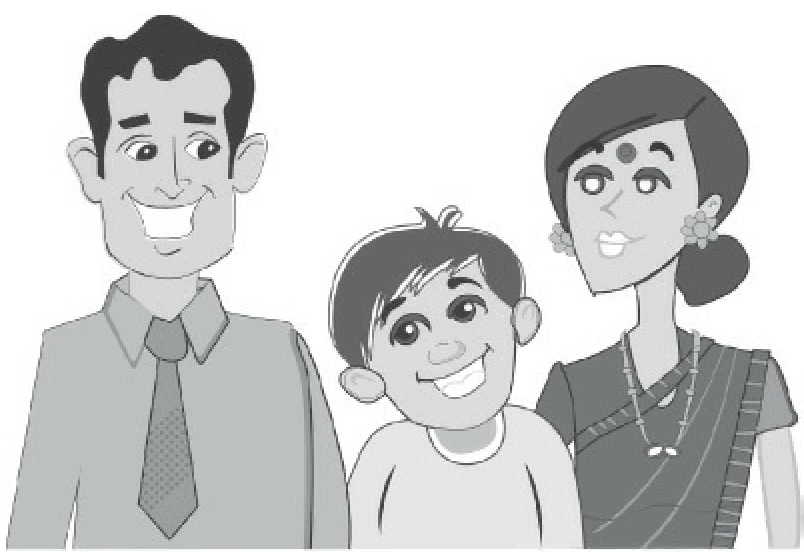
At this stage, you are most probably free from any responsibilities; you have a high risk appetite and your expenses are relatively low. This is the time to enjoy your life but also the best time to save and invest. Your exposure to equity at this stage should be the highest. If you are a salaried person, your contributions to your EPF will account for an adequate proportion of savings in debt and enable you to invest the rest of your money in equity. Liquidity is not a big concern at this stage. So don't keep a lot of money in your bank account. You equity component can be anywhere between 80-100% of your total portfolio at this stage. You should make sure that you invest heavily in equity at this stage and save most of your money because the more you save right now, the more you will be able to relax later, where your finances are concerned. And once in a while - **Party Hard!**

2) Newly Married

At this stage you are likely to have more responsibilities than you did as a bachelor. You now have to pay rent, meet household and other expenses and pay other bills. This is the time when you have to get more serious and start planning your finances to accommodate payments towards big ticket purchases like a car or the downpayment for a house or expenses associated with having a child. This is the time when you need some regularity of income, but you can still invest a substantial amount in equity. It's the time when you should build up an emergency fund, invest for short term goals in debt oriented instruments and still put a majority of your investments into equity. As a rule of thumb, the allocation towards equity should be around 75-90% of your savings till date.

3) Parents with Kids

This is a stage when you have a lot of responsibilities and you can’t afford to face a lot of volatility and risk in your investments and income. By now, basic goals like owning a car or a home would be already met and you may be paying back the loans with which you purchased these. You may still be investing in equity, but from a psychological point of view, you might feel uneasy taking risks. You can go in for balanced investments in debt and equity and can put upto 60% of your investments in equity.



4) Near Retirement

By this stage, you are likely to have achieved most of your goals in life and you still have a few good working years in hand. While you plan your retirement, you can still have some exposure to equity but your involvement and interest should decide how much it can be. Another way to gauge the permissible extent of your exposure to equity can be to check whether your actual retirement corpus is on track towards your targeted retirement corpus. If you are not on track and there is a large gap between your target and the actual retirement corpus, you might want to allocate some investments towards equity for the next few years, depending on your situation at that time. Otherwise an outer-limit for the extent of equity in your portfolio can be 30-40%.

5) Post Retirement

This stage comprises the years after you have retired. Until now, in all the other stages, the focus was on the growth of your money. In this stage, preservation of your money and its growth, if possible, become your aim. Stability becomes an important criteria. A major portion of your money should be in debt oriented schemes like debt funds, pension schemes, PPF, bank FDs, etc. You can have some amount of equity in your portfolio, but now it should be a limited amount. If you are still a risk-taker and like equity games, the amount can be higher. But by now, in all probability, you are likely to choose assurity of returns over risk in investments. Your exposure to equity can be below 20% at this stage.

The 5 stages discussed above are generic and the advice comprises standard recommendations. The ideal asset allocation at each stage could vary considerably from individual to individual.

Rebalancing a portfolio

Let’s assume that you read this book and understand the whole concept of asset allocation. Then you say to yourself, “I will allocate 50% of my savings to equity and 50% to debt”. Then 5 years go past. Stock markets zoom upwards and your money doubles or even triples in value. Your current asset allocation is 65% in equity and 35% in debt. Perhaps by then, the ideal asset allocation for you may be 40% in equity and 60% in debt. What this implies is that you need to “Rebalance” your portfolio to bring back your comfort level. You need to sell off 25% of your assets held on equity and invest the proceeds in debt.

Just like we need to have balance in all the areas of life, there are times when we have to look at our portfolio and keep it in a balanced form so that our asset allocation at all times is suitable. As you are now aware that asset allocation is all about dividing your investments into different asset classes like equity, debt, real estate, gold, etc., it may so happen that due to an extreme upward or downward move in one asset class, the whole portfolio gets skewed towards one asset class and becomes deficient in another. If this movement away from your ideal asset allocation is small, it's ok. But if it begins to make you feel uncomfortable, then you need to undertake a rebalancing exercise.

I will give you another example:

Suppose you are 32 years old and you decide that you are comfortable with 75% in equity and 25% in debt because that's the kind of composition which meets your risk appetite and also accommodates your return expectations. Now, if it changes a little bit, to say 72:28 or 77:23, you can carry on with it. But beyond a point, it starts getting into an uncomfortable zone. Let's say it becomes 85:15 or 60:40. Now, it has moved beyond your expectations and does not meet your requirements anymore. So, the best thing would be to rebalance it and bring the ratio back to one that you are comfortable with.

Profit case

Suppose at the age of 32, you have ₹ 10 lakh to invest and you decide that you will invest it in an equity: debt ratio of 75:25. Let's say you invest ₹ 7.5 lakh in equity (it can be directly in shares or equity mutual funds, ETFs, index funds or some other equity based product) and you invest ₹ 2.5 lakh in debt (it can be PPF, FDs, debt funds, etc). Now, if in the next two years, equity has done fantastically and the value of your equity doubles, your holding in equity reaches ₹ 15 lakh. In the meanwhile, let's say the value of your investment in debt has also increased marginally from ₹ 2.5 lakh to ₹ 2.8 lakh.

7.5 lacs -> 15 lacs

2.5 lacs -> 2.85 lacs

Initial ratio: 75:25

New ratio: 84:16

From a debt to equity ratio of 75:25, your asset allocation has become 84:16. Now, this is a big change and you should bring it back to the original ratio, so that you are back to your comfort zone. For this, you will have to sell a part of your equity and move it into debt products.

Loss case

On the other hand, suppose the stock markets plummeted in the next two years and the value of your money in equity falls to 50% of its initial value.

7.5 lacs -> 3.75 lacs

2.5 lacs -> 2.85 lacs

Initial ratio: 75:25

New ratio: 57:43

This is a big change too and you should bring it back to the original ratio, so that you are back to your comfort zone. For this, you will have to sell a part of your debt and buy fresh equity.

Note that this example does not consider the tax implications in either case. You will need to work out that part.

Rebalancing-a passive way of timing the market

Most investors take decisions based on market levels. If the markets are very high, they will wonder what to do. If markets are down, they still wonder what to do. They are so confused with the whole exercise of timing the markets that they take incorrect decisions quite often. One of the most beautiful things which a lot of people miss is that portfolio rebalancing is a passive way of timing the markets. When the market goes up, your equity allocation will go up and by rebalancing it, you will sell some equity and buy debt by default. Effectively, what you are doing is selling when markets are high. In the same way, when stock markets go down, you buy more equity so that you bring back your asset allocation to the right level. Here you are buying equity when the markets are down.

So for the simple investor, who does not have access to advanced research or the time to study the markets, portfolio rebalancing is the best way to take care of extreme situations in the markets. It’s a common man’s way of timing the market, but you need to undertake this exercise every 1-2 years and not every month. You need to be consistent with it and over time you will see that your wealth grows at the right pace. It might not be the best pace, but it will be a good, comfortable pace.

Conclusion

Sit down and think about this: Are you a victim of “past experiences” when it comes to thinking about “equity and debt”? You can now design your own way of looking at investing and start a long term plan for how you want your financial life to take shape.

Flashback Learning

- We are conditioned by our past experiences and they largely determine how we think about different issues. A lot of this is true in our financial lives too.

- Two popular beliefs “Equity is Risky” and “Debt is Safe” are only half true. They are true only in the short term, but in the long term, the opposite holds true.

- Asset allocation is dividing your wealth among different asset classes in a way which makes you comfortable.

2 hour Action Plan

1. You need to sit down and find out what the position of your current asset allocation is? Find out how much you have in equity/debt/real estate/gold investments.

2. Once you are aware of your current asset allocation, ask yourself if you are comfortable with it? Ask yourself: If the stock markets drops by 50% this year, will I be ok with it or will I regret leaving so much in equity? Now define your real asset allocation.

3. Based on your new asset allocation, draw up a plan regarding what you should sell and what you should buy. Take the tax aspects of your decisions into consideration.

Chapter 5

CHANGE YOUR RELATIONSHIP WITH MONEY

"If a man is after money, he's money mad; if he keeps it, he's a capitalist; if he spends it, he's a playboy; if he doesn't get it, he's a ne'er-do-well; if he doesn't try to get it, he lacks ambition. If he gets it without working for it, he's a parasite; and if he accumulates it after a life time of hard work, people call him a fool who never got anything out of life."

— Vic Oliver

Why we sometimes get stuck on the ground floor

After writing more than 500 articles on personal finance, replying to thousands of personal finance queries and coaching dozens of people in their financial lives, I have realized that most people are stuck on what I call the **"Ground Floor"** of their financial life. The one thing that keeps them stuck on the ground floor is not having a strong **"want to"** in their financial life. When I coach people, I always suggest that before they start working on their financial life, they must have a strong **"want to"** in their personal finance. This is simple, yet most people overlook this simple fact. They have put all the correct ingredients into their dish called "financial life" but a small pinch of salt is missing; and that's the right "want to".

I find that most people go around in circles when it comes to their financial life. They are unable to crack the code that will make them financially successful; they are frantically seeking out the right financial planner; they are busy searching for the right products (designed by God!) that will help them achieve financial freedom; they are in search of secrets… Well the secret is that there is no secret. When people realize or rather are confronted with the fact that their actions suggest that they don't really want to succeed in their financial life, they get very depressed. They blame the agents, they blame their circumstances, they blame others for not having the right level of financial literacy. They start believing that there is something wrong with their financial life and ultimately, they start believing that there is something terribly wrong with themselves.

But there is nothing wrong with them. That is the truth.

All that they need to do is stop complaining and tune into new beliefs about money. Anyone can do it. Every day I see proof of that. I have no formal education in finance yet no one has ever asked me whether I have any certificate in the area of personal finance or not. People are surprised when they hear about my background or my age or about my actual area of expertise. All that I add to my day and my work each day is a strong **"WANT TO"** - that little extra passion; that little extra commitment to making a difference to people's financial lives and that has always helped me to get all the information I need-to create this book or a value added article for my blog.

Many people die with their music still inside. The dream of having an extraordinary life remains a dream and doesn't turn into a reality. When your eyes are scrolling through this chapter, let your mind realize your level of **"want to"** is totally within your control. You are in charge of its true power. It can be as simple as you tuning into the radio station that you want to hear when you are driving your car; nothing in the external world can stop you from tuning into the radio station of your choice. In much the same way, your financial future is in your hands. You can either stay stuck on the ground floor or add the right **"want to"** and reach to the top and experience your full financial potential.

"If you know how to swim, it doesn't matter how deep the water is."

What drives your financial life?

In a book called “Think Everest”, written by Atul Karwal, a man climbs, rather conquers, Mount Everest. It is an extremely difficult task to undertake. It involves 76 days of pain, and unreasonableness. Mount Everest is too high, too far, too steep, too rocky and too difficult. But the thing that was driving his passion and dream was not Mount Everest but his personal commitment. “I will climb it”.

Building wealth requires a similar passion and a strong personal commitment. Wealth is created brick by brick, just as a plant grows inch by inch. That’s how investments grow in your life.

Your financial life is driven by your beliefs more than your commitments. It is important to see what beliefs, thoughts and feelings are dictating your financial life and how you can change them so that you get fully aligned to the financial life you desire.

The fact is that most of what you believe about money is not true. Some beliefs got downloaded from your parents, some from family, some from friends and some from the society you live in. You feel trapped. You become resigned and cynical about your income levels and you stop seeing investment opportunities that exist around you. Somewhere, you end up being a slave to money. You stop having money and money starts having you.

You need to realize that your un-serving money beliefs block your financial success. When you were growing up, your stories and beliefs about money were also growing up within you. You heard a number of times from your elders that money doesn’t grow on trees. You heard it takes money to make money. You heard that money is the root of all evil. You heard that money is power. You heard that time is money. You heard that beggars can’t be choosers. You heard that more money equals more problems. You saw all the bad guys in the movies taking away money from the poor. You saw them, you heard them and somewhere it got ingrained into your belief system. Somewhere it became a part of YOU.

That's what you heard and saw about money all your life - no freedom, no abundance. It's time for you to step forward and question these beliefs. It's time to de-program your beliefs. It's time to re-program your beliefs and then really get into massive action. This will ensure financial success.

So part of the road to financial success is to de-program and re-program your entire belief system regarding money.

Find your own Master Key

All of the books and blogs that you will ever need to increase your financial knowledge or help you to have an extraordinary financial life have already been written. People that have gone from rags to riches and from financial failure to financial success have taken the time to write down their memoirs, so that you can learn from their experiences and mistakes. They have offered their wisdom and experience so that you can be inspired by it and instructed by it.

For a moment, think about who stops you from exploring such useful books? Who stops you from creating a small library at home? Who stops you from reading informative blogs and websites? Who stops you from studying incredible people's lives? It is no one but YOU! It is your belief system about money that keeps you away from gold; from gaining the right financial literacy; from the right financial knowledge; from taking the right ACTIONS…

You hold that key

Most people look at financial planners as magicians. Deep down, they know they have limited financial resources; they know that their goals are un-realistic, but still they expect the planner to do some magic and fit all their dreams into a 20 page document called a financial plan. Sounds Familiar?… at least to a few of you, it may.

But you are the source of all the money in your life. It’s not an external thing; it is purely internal. It is your beliefs, attitudes, thoughts, feelings, choices and decisions that shape and dictate your experiences with money. When you change, so does your financial world-it has to.

“Time” is the new “Money”

Most of the people I coach don’t find the time for their personal finance. They are serious about it, they believe they don’t have time, it is real for them. They have plenty of valid reasons to prove that they really don’t have time. People can’t seem to find an un-interrupted half-hour during which they can work on their personal finance in an entire month, for some an entire year. Sounds familiar? If you look around, you are connected to everything that can help you elevate your financial life. It’s all here. It’s all available. A few keystrokes away.

The so called ‘busy’ people have no time for their personal finance but they somehow find time to be on various blogs, chats and social media sites. Here you are wasting your time in small installments and you are not even aware of it. Always remember NO capital is getting generated from these activities. NO wealth is getting generated. There is NO increase in your bank balance due to it.

Most people swim around daily on google in search of “FREE solutions”. Two hours later, they step back from the screen wondering where time has flown. What got produced? What is the tangible outcome? Only research. NO action that can lead to financial results.

It’s time to identify such unproductive activates and take action with regard to your financial life. A lot of what you do with your time has a direct connection with what you do with your money.

Financial change begins with choice

If you don't like the way things are in your financial life, change them! You're not a tree. Yes you can take action; you can change your direction; you can bring a shift in your financial life. Many people have done it and it is possible.

It is clear that any day you wish to, you can take charge of your financial life and change it. You can elevate the level by shifting gears. Any day you wish to you can open a new book or get on a personal finance blog that will open your mind to new financial knowledge and insights. This becomes possible when you bring about changes in the choices you make that impact the financial results in your life. Any day you wish to, you can start taking action on your finances. Any day you wish to, you can start the process of change. You can either do it immediately or wait for the right time or the right moment or after you handle a few emergencies or after you have the right bank balance. It's an important CHOICE you make.

Your choices can make or break your financial results. You can sit with a financial planner and map out your financial year…which properties to buy, which ones to sell, what investments to make. This can bring a new momentum to your financial life. Now, on the other hand, you can also choose to do nothing about your financial life. You can choose to stay busy with your routine life and let it move and take shape on its own. If the idea of bringing a change in your financial life is uncomfortable or sounds like too much of work, you can remain the way you are, with respect to your personal finance, waiting for your stars to change their position, waiting to get into take-off mode in your financial life.

The choice is yours to make. "The fault is not in the stars…but the choices you make."

You are 100% responsible for all your current financial circumstances. You have created these by your own choices. Buying this book is a choice you have made. You have bought it and have chosen to read it. It isn't what the book costs; it's what it will cost if you don't read it. It is a choice you made in your financial life. All the books, magazines, blogs, planners, people that can help you achieve personal finance growth…make a conscious choice to have them in your life. If you can't attract wealth, atleast attract good books, the right knowledge and the right people in your life. That will eventually help you attract wealth in your life.

Indecision is the thief of financial opportunities in life. We must make a personal commitment to choose actions over thinking and worrying. Making the right choices at the right time is something we cannot afford to neglect. Read on, you'll understand why…

Father and Three Sons-Who will be my leader?

This story is about a man who had three sons. All three were working in the same business and were very obedient by nature. They always did the work that was allotted to them with total sincerity and commitment. The father was very happy to see all this but at the same time he could not decide who should be the business leader after him. All three were eligible but he wanted to choose one from his three sons. He wanted to choose the man who would lead his business to a greater height. The one question bothering him was "Who will lead?"

He thought of an idea that could help him choose the right leader.

He called for a meeting with all three sons. He shared with them the news that he was going on a pilgrimage for the next 6 months and would like to give ten gold coins to each of them before he left. He did not give the many further instructions about what they should or should not do with the gold coins.

He gave them the gold and left.

While the father was gone, each son started thinking about the coins. One of the three traded the gold coins in the marketplace, the other thought of *making something from the gold which he could gift his father and the third, being a very cautious man, took the coins and buried them in the ground for safekeeping.*

Six months later, the father returned. He called for a meeting again and asked each son what they did with the gold coins he gave them. The first son said, "The ten coins you gave me are safe as I have buried them in the ground for safekeeping. "The second one said, "I converted them into a gold chain and would like to present it to you as gift. "The third one said, "I traded the coins in the market place and now I have 15 coins instead of 10."

On hearing what each one did with the gold coins, it was very clear whom the father would select as his business leader. He was proud of his son who had traded the coins in the market and created greater wealth from what he was given. He saw a business opportunity in the coins, which the other two could not.

So what do you see in the money you have? The risk of losing it or an opportunity to create more wealth than you have right now? Most people wait for the big money to come into their life and lose the opportunity to become the leader of their own financial life.

What each son did with the gold coins is what most of us more or less do with our money. Sounds familiar?

Money always seems to be attracted to those who create and multiply their wealth as an ongoing process. Most of us start small. We get our first job; get our first pay; get promotions…the journey is more or less the same. We are either financially broke or we financially rock! It all depends on what we do with all that we earn during the journey.

The moral of the story is that whatever financial resources life has handed us, whether it is a few thousands or a few lakhs or a few crores, it is our responsibility to do something with what we have been given! That is how we change our fortunes--by taking all that we have and all that we are and putting it to work. That's how wealth is created. That is how financial freedom becomes possible in your life.

You are a movie star – Surprise!

If a movie is made at the end of your financial life and shown to the world, how excited will you be? It will show your actual financial life to the world, the reality and not the ideal one that you would like to showcase to the world. Each one of us have a unique financial story to narrate. Each story will have its own twists and turns. Some are proud of the way they have lived their financial life and some regret it. If, for a moment, you have a chance to review your personal finance movie and rate it, how many stars will you give to it out of ten? Be honest. Will it be 8 stars, 5 stars or just 1-2 stars? Some clients we had didn't even qualify for a ZERO rating, they were negative!

Many people will give a poor rating to their current financial life. They are not very happy with the way their financial story ends or the way it started or the way it is moving or the way it is taking shape.

If you could visualize how your financial movie would shape up, given your current direction, perhaps you would become more serious about your personal finance. The good news is that you can still re-write new scripts for your financial life. The game is not yet over. It’s time to JAGO!!

Time to think small

Remember that bigger is not always better; bigger is just bigger. When we ask people to take action in their financial life, they simply delay doing so. They want big results and big changes to take place in their financial life. They don’t want to begin with small actions. This leads to procrastination. They believe that they will take action, but not now…on some fine day. They are unable to realize that it is their habit of procrastination which comes in the way of their financial success. The book written by Brian Tracy “Eat that Frog” explains very nicely how we should begin our day with completing the most important activity first. The same applies to our personal finances as well.

The good news is that you can win your war against procrastination; it's possible. You can always start small; taking small actions, one at a time. Most of the time your mind makes all your personal finance tasks look big and scary. We think of numbers and complicated calculations; we think of graphs and pie-charts when it comes to personal finance. So we procrastinate. Personal finance is not about numbers, it is about YOU and the relationship you share with money!

When we imagine creating a personal finance to-do list, the longer we push it into the future, the more frightening it appears in magnitude. Which financial planner should you trust? How can you find the right products? You can see that objects in the mirror of the future always appear larger than they really are. This is a time to take little actions. Only then will they seem like fun rather than a chore. When we start seeing personal finance as a game, we start enjoying the process and then it's no wonder that you stop procrastinating!

Here, 'Action' is the ultimate answer.

Make small promises to yourself and complete what you set out to do. Start giving your personal finance exercise half an hour of attention each week (You can address some neglected things in the two hours that you allocate to the task each month.) Take small steps. But make a start.

If you take time out to plan your day, you make it more meaningful and productive, just like if you give time to your relationships, they get better. The same applies to your personal finance. It needs your time; it needs your attention. Set aside an hour each week as your "JUST DO IT" time for taking up things you have been procrastinating on! Just make that a policy! It will be the best policy you can add to your financial life.

Just start with one thing…you know what it is…it's the thing you're thinking about right now.

Keep your financial life creative and simple. Think of what needs to be done to your personal finances and do it, little by little. That's all you need to do for now. With this attitude, you'll never have 'procrastination' ever coming in the way of your financial success again.

Start preparing

When you change your beliefs and your personal relationship with money, you will begin to have more and more freedom and money flowing into your life. It's inevitable!

For this reason, it is important to be prepared. What can you do at a practical level to get ready for more money in your life? You can learn more about money-management, explore investing, organize your finances…Get a financial coach…

Ensure you are open to bringing change into your financial life and welcome new empowering possibilities as they will surely come your way.

Here is a short money exercise to help you gauge where you stand with respect to your financial life. Answer these questions honestly:

1. On a scale of 1 to 10, how would you rate your current financial life? (1 being poor and 10 being excellent)
2. What is the one thing you can do to make your financial life simple?
3. Define personal finance areas where you need to take 100% responsibility?

4. Make a list of personal finance actions you know you should be taking but you have been avoiding (This will result in miracles in your financial life)

5. These are the words you want to have on your tombstone…they described your financial life… ____

Bonus: If you complete this money exercise most sincerely, I assure you that you will be a different person altogether once you are done. You can contact the author at manish@jagoinvestor.com with your answers and if time permits, I will reply with your answers.

Is paying for advice an expense or an investment?

Almost everyone I have met till date runs away from paid services, irrespective of whether the advice is being dolled out by a jerk who claims to be knowledgeable or someone who is actually an industry leader. There are many excuses that pop up:

- I am in a cash crunch for the next 2 months; I will come as soon as I have sorted things out

- Can I get a discount?

- But another planner is ready to help meat 20% of your cost and he will file my tax returns for me too. Why should I pay you 5 times more than I would have had to pay him?

- Let me discuss this with my wife and get back to you…and then they never get back!

These are various excuses used to avoid the paid services of an advisor. As per my experience, there is a strong reason why people are hesitant to pay money for advice. It's not about their salary or their knowledge or how much wealth they have… It's more of a psychological reason.

It's because the focus is on fees and not the value. Fees are not seen as an investment. They are considered as an "expense". People look at fees as money that must be spent on something which is for immediate consumption rather than an investment which can provide them with growth in the value of their wealth in the very near future.

Ask yourself: "Is taking advice from an expert regarding my financial life an "expense" or an "investment" which can improve my financial life and enable me to reap benefits over the long term?" I suggest that you should invest in anything that can take your financial life to the next level. Be constantly in search of the best and rid yourself of the attitude of looking for free advice, if you tend to. Remember that free advice can turn out to be extremely expensive in the big picture.

The right attitude would be to look at spending money for good advice as a great investment. So, while we are making this investment, we should not compromise on the quality of the planner that we choose, as it would impact the quality of the advice that we receive. If there are two planners you have to choose from, one who charges a fee of ₹ 10,000 and the other who bills you ₹ 25,000, quite often people tend to go in for the planner with the "more reasonable" fee of ₹ 10,000. This is because they look at this payment as an "expense". If instead they looked at it as an investment, they would see the benefit of choosing the planner who charges more, since a better investment is more likely to result in better results.

While choosing a planner, look for one who is more interested rather than more interesting; look for one who is willing to serve you rather than please you; look for a planner who is committed to solving your problems; look for one who is willing and able to bring about the change in your financial life that you have been seeking… The focus must be on Value and not on Price.

We are wired to bargain

We are simply programmed to try to acquire anything we pay for at a lower cost. When we buy vegetables or any other basic product, we tend to bargain to make sure that we pay the lowest possible price for the same quality of product. After gauging the quality of such products, by touching and feeling them, it makes us feel great when we are able to secure them for a lower price. However, not everything is vegetable. There are many things in life whose quality you can't determine by just seeing or feeling them. Quite often, you buy things on recommendations, other people's feed back or a gut feeling. A financial advisor is just like that. You can acquire the services of such professionals for 10k or 5k or 50k or maybe even for FREE. However, you can't compare a planner who charges 25k and one that charges 6K and imagine that you got a good deal when you choose the latter. It's not like purchasing a vegetable, which would be almost the same in terms of quality and differ in price, mainly because of its location or such factors. There is a reason for the difference in fees and you have to appreciate the difference.

Would you settle for a common school for your child, even if you can afford a better one? Would you opt for a hospital merely because the fees are low compared to others in the vicinity, even though it is the health of your loved ones that may be at stake? No. You wouldn't compromise on these services because you consider them as crucial. In these cases, you want the best quality that your money can buy. If that's so, why is it not the case with a financial advisor? Keep in mind the fact that your financial advisor is going to deal with your wealth; your hard earned money, which is going to be used for your children's education, your dream home, your retirement, your other big goals in life. A financial planner will work with you to make your financial life awesome. So you would be better off hiring someone who knows what he or she is doing. Go in for the best quality that your money can buy because you are putting your life in his hands…after all, your life is governed by the state of your finances to a great extent. Don’t compromise on quality for a couple of thousands.

In fact, I would recommend that you take your time while looking for the right financial advisor. Look for someone who tells you to your face that you are in a financial mess, if you are, and not someone who just tells you “how you can save for your goals”. Then don’t worry about the fees that you will be paying for the former.

Your financial planner should be like a coach to you. He should identify your weaknesses and correct them. He should not be a person who just takes your financial data and spits out a financial plan in 5-10 days which tells you what products you should buy, unless and untill that’s exactly you need from a planner.

Your “Financial Life” is a room in a house called “Life”

Here’s another little fun exercise. Imagine your whole life as a house. Each part of your life is a separate room in this big house. So, you have a room for your family, you have a room for friends, you have a room for your job, you have a room for your hobbies, a room for entertainment and soon.

When you play with your children, when you are with your spouse discussing something or you are having fun with your loved ones, it’s your family time. It’s the time when you enter your “family room”. When you are tense and want to just unwind, you enter your “hobbies room” or “entertainment room” and begin reading a book or watching television or whatever it is that makes you relax. Most of these rooms are adjacent to each other so that you can quickly move from one to another.

I am not sure if everyone in this world has all the rooms mentioned above or not, but there is one room which everyone has for sure. The rich have it; the poor have it and the middle class have it too. It’s called the “financial life room”. Even though it’s one of the biggest rooms in our house, we hardly enter it. It’s just there…Empty. Once in a while, a few people just step into the room by mistake, but they are out of it soon enough. Other rooms in the house get a higher priority. We keep on renovating every other room; painting them every 2-3 years to make sure they are fresh and look attractive, but our financial life room is lifeless and dull, stinking from years of neglect; the same paint on the walls, even some spiders’ webs can be seen here and there…

Interestingly, most of us spend 4-5 days each year in this room. That happens some time towards the beginning of the month of February - during the tax saving season. During that time we enter this room, clear away a little bit of the mess in it, just enough to find a small place to sit down. We spend as little time as possible and as soon as we finish with our work, we just lock it up and throw the key somewhere. We never want to return there till it’s absolutely necessary!

Remember, this room is the room to which you have to keep coming back. It’s the strongest, biggest and one of the most important rooms in your house called “Life”. You may not know it, but others judge you by how beautiful this room is. So enter this room frequently. Keep it clean. Make sure the walls are decorated. Take your family into it sometimes and have a cup of tea inside it!! Enjoy it!!

I hope this chapter has opened up your mind a bit and got you more interested in your financial life.

Flashback Learning

– Unless you have a “want-to” attitude towards changing your financial life, things will not change drastically. You are just expecting to have an awesome financial life by chance. It will never happen without your help!

– Every book, every article, every thing that you need to know about personal finance is already available. The only thing that is required now is your commitment to finding what you need and using it.

- Transform your financial life so that you would give it atleast 8-9 stars out of 10 if you were to rate it. Get a financial coach who can help you move forward.

– Consider paying for advice as an investment, rather than just another monthly expense. Get the best advice at the best price.

– Your financial life is that part of your life on which other parts are dependent. If you keep it fit and well, the rest of your life will probably be fine too.

2 hour Action Plan

1. Spend some time in the park or fishing (Yeah, I know no one does it in India, but you get my point!), and think about how you have handled your financial life till date. Does it deserve more time and attention from you?

2. Find out if you really need a coach in your life; one who can guide you with regards to your finances and try to evaluate the value you can get by working with him or her. Price is important, but don't let it come in the way of your financial success.

3. Make small promises to yourself regarding how you will handle your financial life. Set aside just 1 hour this coming Sunday, after lunch, to have a look at your policies, investments, financial goals in life…and see if you are on the right track or not.

4. Read some nice books on money. Mail me and I can send you some written twice.good e-books.

Chapter 6

SIMPLIFYING YOUR FINANCIAL LIFE

"The *ability to simplify means to eliminate the unnecessary so that the necessary may speak."*

— Hans Hofman

Simplicity - sounds like a simple word, but it’s a tough nut to crack! In every aspect of our lives simple things are much appreciated by everyone. Ask a groom what kind of girl he is looking for -”Simple” is the answer, almost 8 out of 10 times. Ask a person what kind of blogs or magazines he likes to read-the answer is not “full of knowledge” or “powerful content”. It’s mostly “Simple articles”. I can also see people switching from other networking sites to facebook and from their email providers to gmail because these are simple.

Simplicity is inherently appreciated by mankind and no matter how much we deny it, we prefer to deal with things which are simple enough. But there is an irony here - our financial lives do not see this element of simplicity; and I don’t see many people talk about this aspect of financial lives. Almost every other guy is looking for the best plans, the best policies, stocks which can make him rich, a product which can help him to achieve his financial goals, and soon. But one thing which can help to make one’s financial life stronger, more robust, is never paid any attention to: and that’s simplifying one’s financial life.

Ask your self-What are my priorities?

- Do you want to have a smooth financial life which doesn’t require your attention every other day?
- Do you want to earn well and also make good investments?
- Don’t you want to pay all your bills on time and don’t you want to avoid the mess of late fees and penalties?

I am sure you will yell-”Yes, that’s what I really want!”

In today’s financial world, most people get the feeling that a simple financial life can’t exist and in fact, can’t work! Switch on your TV and go to a channel which runs a show on personal finance or any money related topic. What do you see? I can assure that after watching the show, you will feel that the person on the TV is much smarter than you and has been expounding rocket science.

In today's financial world, we are so overloaded with information and choices that investors just keep delaying their decisions in search of the best timing or the best product. The fear of going wrong while choosing a product is so high that it becomes a road block for taking actions.

With so much information, analysis and complexity, everyone has started believing that one needs to have extraordinary abilities or thinking powers to choose products which can make their financial life a success. A common man feels that he needs some strong external support to fix his past mistakes or help him build a good financial life. This is a highly exaggerated notion.

Complexity just takes us away from our focus

One of my friends is really good at his work, but over the last 2 years, I can see that he is not able to put in his best at his job. The main reason is the plethora of worries related to his financial life and consequently, the amount of time he spends working on it. He has bought around 20 mutual funds and to get the best from them, he keeps on analysing them, selling them and repurchasing other funds. He also defaults on his credit card payments; and it's no wonder: he has 5 of them and every month he misses the payment of at least one of them. His inbox is flooded with so many emails and statements from his bank accounts that he does not bother to read them.

To top it all, he has to keep a track of his dozen-odd insurance policies and every now and then he keeps wondering whether to keep them going or not.

All this takes up his time and saps his energy. He can't give his 100% to what can help him to generate more wealth and ideas.

Don't be too surprised if you realise that even your financial life is not well optimized and well simplified. Our overall lives have become so complex these days because of various reasons that the same element of "complexity" has slowly entered into our financial lives.

As I said, we spend a lot of time getting involved in time consuming, unimportant tasks in our financial lives, which can simply be reduced, simplified or at best, automated. Only then can we concentrate on better things in life, like our family, our job, our health or a hobby.

But I see a lot of people constantly worrying about their financial life and being involved in it, as if there is so much to do. If you have 7 bank accounts, 4 credit cards and a dozens-odd financial products, and you have no clue how they work or what they are doing in your financial life, what can you logically expect?

My personal experience

In our financial coaching program, when we interact with our clients, we notice a common pattern. Some people had not taken a lot of wrong decisions in their financial life and have simple portfolios. These clients were the easiest to plan for. They took the least amount of time to benefit from our programme and were on their way to generating more money much faster. But the clients who had complicated their financial life, by buying every other financial product they came across, required a lot of fixing. Some had upto 25 insurance policies with sum assureds of Rs 1 lakh or ₹ 50,000 each, 8-10 banks accounts (husband + wife) and they had dozens of stocks with insignificant money in each. It was as if they just invested to try out something; God knows what!

Over and above that, they had 14-15 goals in their life, which only they were clear about. Each part of their financial life was linked with some other parts and if we moved one thing, it would bring everything down like a pack of cards! Life was tough for them! The element of simplicity was missing in their financial life and it made their life miserable.

Financial clutter only takes away our energy, most of the time, and we don't even realise it. Some of the blame should be shared by the system around us, which has thousands of mutual funds on offer, a hundred different kinds of policies with complex names and dozens and dozens of insurance companies, banks and various other entities with similar products and offers. All this makes sure that we are totally lost in this world of choices. This only leads to delays in action because more choices translate into a greater fear of not picking the best product available.

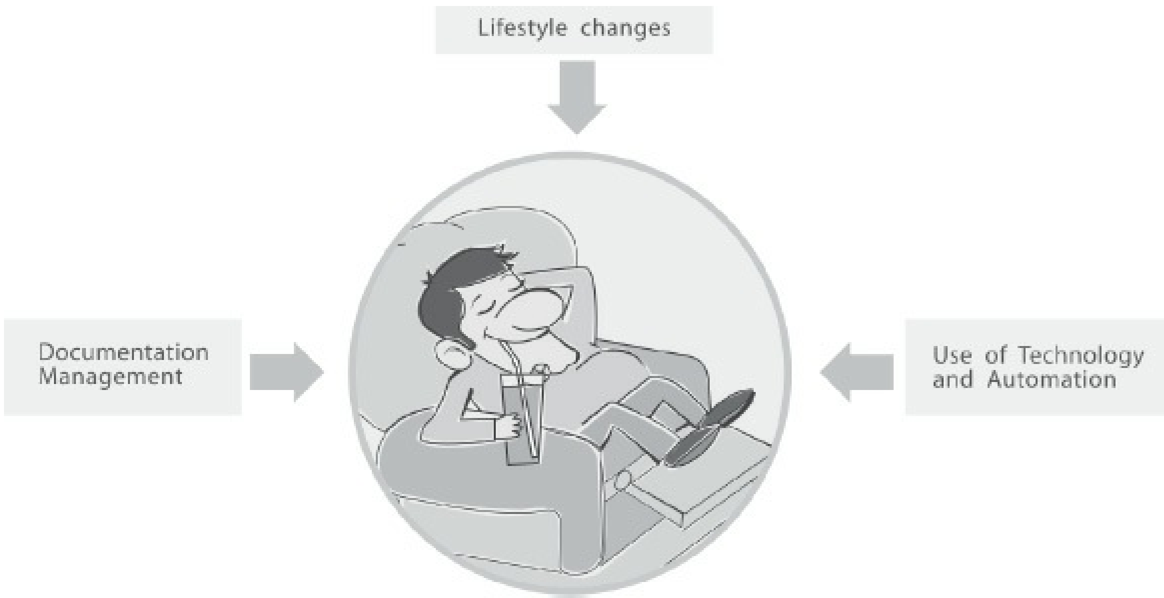
My focus in this chapter is to suggest some small doable changes in your financial life in such a way that your involvement goes down once you undertake a one time activity of restructuring in your financial life. The idea is to lower your involvement and generate more time for you to think and do research.

The idea is to be less sensitive to the outside world and create a tailor made financial life that is simple and effective and takes away less of your energy.

3 things you can do to simplify your financial life

There are 3 main areas which, if made simple, can make your overall financial life simple and more effective.

1. Use of technology and automation
2. Choosing less instead of more
3. Documentation management



1. Use of Technology and automation

How many people have you met who crib about paying motor insurance or the fact that their company cuts money from their salary for their PF every month or the fact that they have to pay maintenance to their residential society every month? Hardly Any! Can you guess why?

I will tell you. It's because each of these payments is compulsory and more importantly, these are on a "by-default" mode! They don't have a choice regarding whether they want to pay for these or not. It is simply understood that these cash outflows must take place. So it becomes part of life and we don't find reasons to avoid them. Just ask your self, if a person had the option to pay for motor insurance or not (like life insurance), how many would really do it?

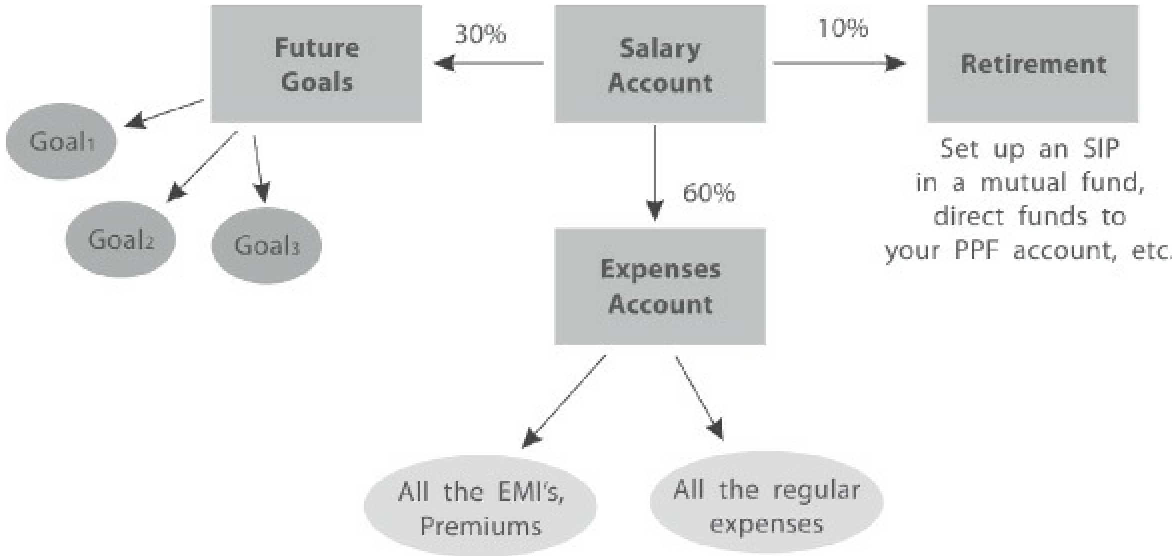
Just imagine if each month, one had to manually transfer 12% of one's basic salary to an EPF account, voluntarily, how many people would be able to do it consistently? If more than 5-10% of people did, it would be a miracle!

When there are things on autopilot and happening on their own or if we feel a sense of compulsion with regard to certain things, humans have a tendency to surrender to them and let it become part of their life.

So when you start an SIP and give your bank instructions to automatically pay the fund, or when you have directed your broker to sell your shares in case a condition is met or when you have just chosen a date on which you pay all your bills and premiums and you are consistent with it, you are on autopilot. Things start happening and you are less likely to disturb the system and that's exactly what you need to do as the first step. Start automating those things which you are doing manually each month/week. Start automating things which you have planned to do.

Another good thing about automation is that there are less chances of forgetting things, which we all often do. I have seen many people making their credit card payment on the last date. Obviously, they forget about it from time to time and get into messy situations and lose money.

So the idea is to automate your financial life in a way that calls for only a minimum level of thinking from your side. Set things on autopilot. This can happen only if you are already clear about your goals. Here are a few simple things you can do.



Let's understand the concept of automation with the example of Ajay, a person who has some financial goals in life and can save 40% of his salary. Here is what he can do: Once his salary comes into his account, he can transfer 10% of the money directly towards his retirement fund (This can be a Mutual fund, PPF or any product) and 30% towards other future goals, like his child's education, buying a home, a car, etc. As a result, 40% of his salary will automatically be invested each month in some financial product (perhaps mutual funds). He can make use of the ECS facility that banks provide or it can go into a recurring deposit account (just another example).

Naturally, you will need to modify the flows in the example to suit your needs but the idea is that a fixed percentage of your money should leave your salary account and you should be left with just the remainder.

Getting back to Ajay's case, out of the remaining 60%, he can now pay his regular bills, like credit card bill, his EMIs (if any) and his other regular expenses towards running a home. The numbers here are 10%, 30% and 60%, but you can see what numbers make sense in your financial life, according to your situation.

The automation has to be simple and this tip is only applicable for those things which can be automated.

Consolidate the dates for your bill and EMI payments

I have noticed that most people pay 5 bills on 5 different days and although they tend to be preoccupied with the whole exercise of paying so many bills, they often forget to make one or two of these payments. While discipline is required here, if there are more than a certain number of bills to be paid every month, I suggest paying them all on the same date. This way all the bills and payments get done together. If you have the option to make payments online, explore it.

To make this point, let me share with you an incident from my own life. I used to pay my phone bill directly by going to the phone company's office. Although it was near my office, the whole process used to take me 30 minutes every month. On the face of it, I was spending 30 minutes but actually it was a lot more. If I take into account the travel time and the inconvenience, it would amount to a lot more. Then, as my internet provider's office was nearby, I used to combine my trip to pay the phone bill with paying the internet bill too. And I thought I was being smart!

Every month I used to consider opening an account with my internet service provider, which would allow me to transfer the payment online, but I kept procrastinating and I kept telling myself "next month". After 24 'next months' I ultimately decided to take 10 minutes off from my busy schedule and I finally did it. I was so amazed to realise how idiotic I was to pay my bill manually, when all it took was a couple of clicks to do the same thing.

I hope you are not making the same mistake that I did. Whatever bills you can pay online, should be paid online. It saves time and energy. And, if you can't think of what to do with the time you have saved, just use it to take a nap!

Set reminders

There are some things which can't be automated and can't be done online. There are various facilities available today that can remind us that we have to do these things but we often ignore these. The best thing that I can think of is the reminders in our phones. But let me tell you about some more complicated ways of setting reminders as simplicity is something which we don't entertain! Other ways of keeping yourself alerted are by using sites like http://www.futureme.org/ or http://www.followupthen.com/. Even google calendars have an excellent feature which reminds you on email and through SMS. Why don't you put reminders for your insurance premiums and other important payment dates each month?

It's Important to meet all your financial deadlines on time; and it's not simply about having to pay late fees. When we miss certain important financial events in our life, they can have more far reaching consequences than we imagine. Let me share with you a real life example of how a person delayed filing his tax returns and got into trouble.

A friend wrote to me:

Hi Manish

One of my friends has his Form 16 for the fiscal years 2007-08, 2008-09 and 2009-010. The tax for 2007-08 was nil. For the other two years, the tax has been deducted by his employer.

Now his Visa needs to be processed and he has been asked to provide his tax returns for the last three years. From what I read in your posts, it seems like he can now file the returns for only 2009-10.

But in your posts I also read that there is a fee of ₹ 5k per late year. Is it possible to file returns for 2007-08 and 2008-09 after paying the late fees?

Is there any solution to this problem?

You can see how this guy didn't pay attention to filing the return, thinking that it wouldn't impact him in the future? He might have missed it or done it deliberately but the point is that one small incident like this is impacting him now! What if he loses a good job opportunity because of Visa issues?!

Track you portfolio and wealth

Another thing which I have noticed is that a lot of people are struggling every now and then to find out the status of their wealth and how their portfolio is behaving. But they never use online or offline portfolio management software. These one time setups can give them many answers at the click of a button.

There are various online and offline tools available (both free and priced), wherein you can enter your portfolio information and track its performance. If nothing else, you can always put all your investment details in a Single excel sheet and keep updating it 3-4 times a year to see the progress of your financial life.

(A simple wealth tracker is part of our free book kit. Just send us a blank mail to book@jagoinvestor.com to get it).

2. Choose less instead of more

In addition to the use of technology and automation, we need to simplify our product shopping habits: it's all about limiting our choices.

Imagine a situation in which you are invited to a marriage or a party. There is a buffet lunch or dinner and everyone is ready with their plates, to attack the food. You will see that almost every one feels compelled to try out every dish and after surveying the buffet, their plates are full. If there are 32 items in the spread, I can bet that 80% of the people there have more than 20 items on their plate. The supply of so many items creates a feeling that each of those is great and if we opt not to try out something, it would be our loss. A person with just 4-5 things on his plate is given rather strange looks.

I myself used to pile up my plate with everything that would possibly fit on it and if I saw someone with just 4 things in his plate, my friends and I used to be amused. But now I realise how sensible such people are. Take what you like and focus on just that. Having plenty of choice and taking a limited number of items does not make you an idiot.

The same behavior can be seen in one's financial life. People are overloaded with 20 mutual funds, 8-10 insurance policies, dozens of stocks at times, numerous credit cards and bank accounts. Why? There is no reason why! It's just the availability of financial products and the human mind's need to accept all of it. More appears better!

Abuse of Diversification

A lot of people equate Diversification with MORE! That's a half baked understanding of the concept. Buying 10 different mutual fund schemes is not diversification, especially when they are from the same category. Most people buy so much of the same kind of products that it only leads to duplication and nothing else. It simply wastes their time as they have to track and manage those products.

- **Insurance**

If you take a look at the demand for insurance, you will find so many people who have bought 5-10 insurance policies at different times. The worst part is that all those policies still do not cover them adequately. All they should have done is purchase just 1-2 insurance policies because once they die, the only thing that will happen is that the beneficiary will receive a lump-sum amount, whether it's from 10 policies or just 1. They are going to get the same amount of money. The only exception here is that if a person has bought policies for investment purposes and plans to receive the maturity amounts at different intervals.

• Mutual funds

I have seen thousands of my readers on the blog asking me if they should invest in the following mutual funds and then they list out 10-15 mutual funds. These mutual funds are of the same type and the amount they plan to allocate to each is ₹ 500 or ₹ 1,000 per month. Yet all in all, they want to invest 8000-10000 per month. Now in their mind, they think that by investing in more mutual funds, they are spreading the risk and getting the services and expertise of different fund managers. But in reality, it's like killing a mouse with an atom bomb! All they are doing is creating so much duplication in their portfolio that it will lead to clutter and a waste of time, tracking those mutual funds. In reality they just need a maximum of 3-4 mutual funds and that should give them enough exposure.

In fact, one mutual fund alone can expose them to dozens of stocks. To give you a deeper insight into this, I have prepared a chart which tells you how much exposure a person can get by investing in 2, 5 and 10 mutual funds.

Total Funds	Top stock exposure	Top sector exposure	Top 3 sector exposure	Top 10 stocks	Large Cap + Mid Cap	Large Cap
2 funds	5.52%	24.5%	52.8%	37.06%	96% money in 74 stocks	85%, money in 49 stocks
5 funds	4.67%	21.07%	46%	34%	97% money in 111 stocks	81% money in 59 stocks
10 funds	5.7%	21%	46.5%	37%	98% money in 131 stocks	80% money lying in 60 stocks

** Funds used were HDFC Top 200 & DSPBR Top 100, UTI Opportunities, Franklin India Prima Plus, Birla Sunlife Frontline and other top 5 mutual funds, as on 1st June 2011.*

If you look at the chart above, you will see that a person who has invested in just 2 mutual funds is already exposed to 74 different stocks, out of which 49 stocks are of big companies (large cap) comprising 85% of the investment and the remaining 25 companies are mid size companies, which account for the rest of his investment. Now that's a decent enough exposure already. But still some more funds can be added to the portfolio, if one really thinks he should add more.

By adding 3 more funds (a total 5), the exposure goes to 111 stocks, out of which 59 are large companies comprising 81% of the money invested and the remaining goes into mid-sized companies. Now beyond this point, it does not make much sense to include more funds of the same category because it only adds to the clutter and does not add any value.

I personally feel that one should restrict oneself to just 2-3 mutual funds. This strategy provides decent exposure and makes a portfolio extremely easy to manage.

The same thing is true for credit cards, ULIPs, bank accounts and most other financial products you can think of; limit each of these to a number which is easy to manage for you and does not add confusion to your life.

Think before you act

We are not living in the 60's or the 70's, when life was relatively simple. Today, one needs to be really careful about what one does and also needs to do things on time. I will share with you some cases of people who didn't think a lot before taking some action. They ended up paying for it later, either monetarily or by losing an opportunity.

Here's a real life example of a reader from my blog who was not able to get loans from banks because he didn't think twice before helping a friend and got his own credit history all messed up.

Hi Manish,

One of my friends took a car loan from an NBFC 3 years back and he wanted a reference for this loan (I now realize there is no such thing as a reference for a loan). I obliged and gave him a duplicate copy of my pan card.

For at least 2 years, I have been applying for credit cards and getting rejection letters from all the banks I apply to. I was finally fed up with this and decided to call for my CIBIL report. When I got it, I was shocked to see that I was a co-applicant for the car loan that my friend had taken 3 years back. He had defaulted on this loan, which was reflected in my CIBIL report and that was the main reason for me not getting a credit card.

Like I mentioned earlier, I had given my friend a copy of my pan card but I had never signed any loan application form. So, I followed up with my friend (who still claims that I was supposed to be a reference for this loan) and also with the customer care at the NBFC (who I must say were extremely rude).

I managed to get the loan application form from the NBFC and I'm a cent percent sure that my signature has been forged on the form. Now my friend (do not want to call him a friend anymore) claims that the company who gave him this loan never told him about me being a co-applicant and he always thought I was only a reference.

So now do you see why we should think twice about the consequences of what we do and not just do whatever feels fine? A lot of things can haunt us later in our life and it is not possible to change the past. So beware!

Simple portfolio for a common man

Now that we realise that a smaller and cleaner portfolio is ideal, let's see what it could look like… For a person to keep his financial life simple, I suggest a simple portfolio, which has:

- 3-4equity mutual funds (SIP) + index funds
- 1-2 bank accounts (which has his emergency funds in them)
- 1-2 term plans(life insurance)
- 1 health insurance policy
- 1-2 credit cards(if one needs them)
- May be a PPF account
- 1-2 FDs for short term goals
- A long term view of his financial goals

I can see that one can achieve a lot with a simple portfolio like this. It has all the elements of liquidity, long term growth potential, protection against mishaps (life and health), etc.

Note that this advice is directed at someone who does not want to get too involved in his financial life and wants to keep things simple. This is definitely not the "best" portfolio, but it's a "good enough" portfolio.

3. Documentation management

Imagine some one like you, who has a job and is supporting a family. Now think for a minute about the answers to these questions: Who has all the information and knowledge related to your financial life? Where are your insurance policies kept? Who knows about the FDs that you have recently invested in? What are the passwords and other important details of your important accounts? What's you CA's phone number?

In all probability, you are the only one who knows.

Suppose you die! What happens?

However diplomatically I try to put it, the truth of the matter is that people around you will be sad and crying for a month at the most. Then slowly life will return to normal. Soon the process of confusion and irritation will start. Your loved ones will start to think: How do we claim the insurance money? Who was his agent? What is the agent's phone number? Where are the details of his income tax returns? Let's talk to the CA, but where exactly is his office and what's his phone number? Where are the bank locker keys? Are they in the top shelf of the black almirah or in his office drawer?

I can only think of a limited number of questions which will occur to your family. But believe me, this is just the tip of the ice-berg! I would like to assure you that you should not worry too much about this because eventually, in few weeks and after a huge amount of confusion and irritation, your loved ones will find out everything they want to know, SOMEHOW!

Life does not stop because you didn't organise your stuff. But what if you did? What if you take 2-3 hours of your "precious" time, after reading this book, and just organise all the details which you believe will help your loved ones, in case you are not around forever or for a few days. At times, this small exercise of organising data can even help you. It does not take more than a few hours and lot of commitment to actually do it.

I'll share with you an experience from one of our own events called 'Action-Month'. When we conducted this exercise during the event, more than 850 participants completed the task of organising their documents and placing them in a folder. If 850 people can do it, why can't you? Just go ahead and do it!

I know of a real life example of how a person was facing a problem while getting his policy issued just because he misplaced his income tax return acknowledgements.

A reader of my blog wrote: Hi Manish

I am trying to get a term plan of ₹ 25 lakh from LIC and they have asked me for my income tax returns for the last 3 year. Now, the thing is that I am unable to locate both the acknowledgment as well as form 16 for the year 2009-10. Because of this, LIC is not going to issue the policy. Can anyone tell me how I can secure my income tax return acknowledgments for 2009-10?

I had filled this return through a Bajaj Allianz agent and I am unable to locate him. What can I do in such a case?

These things can happen to you too if you don't take care of the documentation in your financial life. Keep records properly.

Master Document

Now, what if we create a master document, which contains all the information in it? You will have all the details that you need at one place. Store this document at a place which everyone is aware of. This would solve all your problems and also act as reference material for you yourself in many cases. Once you do this, you just need to make sure that you update it once a year, if not more frequently. This document will contain-

- Important details of your life
- A list of important documents and their locations, e.g., passport, driving licence, PAN card, etc.
- Important instructions for your family to carry out, once you are no more. For instance, the insurance claim process, steps to selling off some property, claiming the bank account, investments, etc.
- Important contact details of people like your CA, lawyer, your stock broker, etc.
- A list of all your assets and liabilities
- All your investment and bank details

It will look something like the following documents

1. Important Documents

Document	Number	Location	Expiry Date
Passport	—	—	—
Driving Licence	—	—	—
PAN Card	—	—	—
Voter ID Card	—	—	—

2. Important Contacts

Contact Type	Name	Phone	Email
Lawyer	Ramesh Gupta	9874566363	ramesh@in.com
Stock Broker	—	—	—
CA		—	—
Insurance Agent (SBI)	—	—	—
Insurance Agent (LIC)	—	—	—

3. Critical Documents

Document	Location	Contact for Help
Will	—	Ramesh Gupta (9874566363)
Birth Certificate	—	—
Important Keys	—	—
Insurance Policies	Bottom corner of Black Almirah	—
Property Papers	—	—
Home Loan documents	—	—
EPF	—	—
PPF	—	—

Assets and Liabilities Document

Assets	Amount	Liabilities	Amount
PPF	50000	Home Loan	2300000
EPF	45000	Car Loan	300000
Mutual Funds	1400000	Loan to Ajay (friend)	50000
Shares	20000		
Real Estate	2500000		
Cash in Bank	35000		
Bonds	50000		
Money receivable from Robert	200000		
Total	**4300000**	**Total**	**2650000**

You can get these documents in the book gift kit (just send a blank mail to book@jagoinvestor.com to receive it)

Define your simplification yourself

Each and every person has his own way of defining what 'simplicity' means to him and one can have his own checklist of things, which if completed, can make his financial life simple. You should make sure that you define it for yourself, using whatever takeaways are relevant to you from this chapter.

Make a list of things which will make your financial life simple. Your list could look like this:

- Learning about personal finance
- Understanding each product in your portfolio
- Keeping all your documents properly
- Attending a seminar or class on money

It can be anything, it's your list. Just create one!

6 commitments you must keep in your financial life

So now that you are clear about how you should make your financial life simple and why a simple financial life is powerful. Let's define 6 commitments that you should have in your financial life. Then you need to act on these each month or each week, as time permits and the commitment demands.

Commitment 1: *Slow down and create your financial profile so that you understand yourself*

You will be amazed to hear that many people don't know themselves in the area of money. They are not sure how much risk they like to take, how ambitious they are, what kind of job they want to do, when they want to retire and how much time they want to invest in their financial life. Knowing all this is important because that will define how you will act!

The first commitment you should have is to slow down a bit and understand yourself, define all these points and use them as the guiding principles for your actions in your financial life.

Commitment 2: *Remove the clutter from your financial life and take it back to level 0*

Once you are ready with your profile, you will discover yourself and will become ready to remove the unwanted things from your portfolio and financial life.

- Check how many bank accounts you have and whether they are all required. Can you close down some of them?

- Check all your investments - your mutual funds, ULIPs, FDs, RDs, bonds, stocks and endowment policies.

- Make sure you have a minimum number of products, which can achieve the results you want in your financial life.

Commitment 3: *Automate your financial life and make sure you are involved in the least amount of things.*

The next commitment you can have is to do all the things which make sure that your involvement in manual tasks (tasks which takes time and energy) is minimal. Automate your bill payments, start your SIPs and pay your premiums through the ECS facility or at least make them online.

Define your goals and decide what financial route you will take to achieve them. Then direct investments automatically towards these at the start of each month. Set all the alerts and reminders which are important for your financial life.

Commitment 4: *Exercise and prepare yourself to enjoy retirement and your future life*

I am not sure how many people will agree with this one, but your financial life is there to help you in life. We strongly advise everyone to stay healthy and in shape, else there is no strong reason for accumulating wealth. Start taking care of your body, your overall health and eating habits. If you can only keep one commitment of all the 6, this is the one you should keep!

Commitment 5: *Set aside a week or two just for shopping for financial products*

Now once you have finished pruning and removing unwanted things from your financial life, it’s time to fill in the gap and see what you need to add, so that you can complete your exercise. The commitment here is not to decide on things, but to take action and move your financial life from point A to point B. Define a plan for the next week and implement it!

Commitment 6: *Be prepared to do a great job of monitoring your financial life in future.*

The last part is to equip yourself with knowledge and tools which can help you to monitor your financial life and make sure that you know what's going on as fast as possible. You can use some software to do this or it can be as simple as using an excel sheet, with all the details, which you can update each month or quarter.

Let me know at book@jagoinvestor.com whether you completed your commitments or not.

Chapter 7

10 THINGS TO DO TO MAKE YOUR FINANCIAL LIFE AWESOME

7.1.
Don’t invest just to save tax

7.2.
Start Living with just 90% of your salary

7.3.
Control excessive leverage and careless spending

7.4.
Invest in great things other than financial instruments

7.5.
Become the CEO of your financial life and deliver performance

7.6.
Don’t fall prey to instant gratification in your financial life

7.7.
Teach your Spouse & Kids about money

7.8.
Focus on action, don’t let little things get in the way

7.9.
Re-define “budgeting” as “priority spending”

7.10.
Look at the value or real return of a product

1. Don’t invest just to save tax

We have complete 6 big chapters which conveys a topic to you, however there are many other things which you should follow, I have tried to cover the best 10 things you should follow in your financial life to make it more stronger in this chapter. These 10 rules are short, strong and very powerful if you follow them.

“Tax saving should be the result of your Investment planning and not vice versa.”

When you hear that you will be able to save tax by investing in some financial product, what is your reaction? Do you feel excited? Do you want to purchase that financial product no matter what it does or doesn’t do for you?

For most people, saving tax is such a big thing, that they forget every other rule of personal finance and concentrate all their energy on saving tax. I see many people who are trapped in idiotic products because of their obsession with ‘tax saving’. Most people today have products in their portfolio which do not suit them at all; products which they don’t need and which they do not understand. This all happens because of their singular decision to “Investing for Tax Saving”!

Typical Scenario

In most cases, people don’t do their tax planning at the start of the year or at least much before the month of January. Then somewhere at the end of the year, around February, when they receive a letter from their employers requesting them to submit their documents for tax savings, they wake up and remember their financial lives. But wait, it just makes them stir a little, it does not lead them to take any action, because the deadline is still 10 long days away! If the 10th of February is the last date for submission of documents, most people start collating their documents and arranging for medical bills, HRA related bills, 80C documents, etc only on the 9th evening. And some even call agents because now they want to “invest”. Can you imagine the scenario? It’s actually come to a situation wherein “Giving proof of investments” is much more important than “Making sensible financial decisions”. It’s too late to plan for things! Sounds familiar?

Now all mutual funds and ULIP agents, etc., are ready to take charge and sell you anything and everything which can save you tax. That’s exactly what many people want. At the last moment, they have no choice but to invest, so that they can “save tax”. I can’t imagine a scenario where someone says, “Wait a minute, let me just pay the tax and leave my finances the way they are because it’s better to not get into something which I don’t need”. To many, such a person would appear extremely idiotic and might even become the news of the day!

The problems arising due to this

The worst sufferers are those who don’t need any insurance but invest in endowment polices and money back polices just to save tax. These people do not realise that even though they are saving tax for that particular year, they are actually getting into a commitment for the next 15-20 years (or as long as the policy tenure lasts) and they have no idea how it's going to meet their future financial goals.

People who opt for ULIPs without understanding how these work and how they can help them in their financial goals face a similar problem. They invest for one particular year just to save tax. But they have no idea about the charges or the other formalities. They never even look at the policy and totally rely on their agents. By the next year, many of them have no idea if they can even afford to pay the premium or not! The problem is not the ULIP or any other such product; the main problem is the intention!

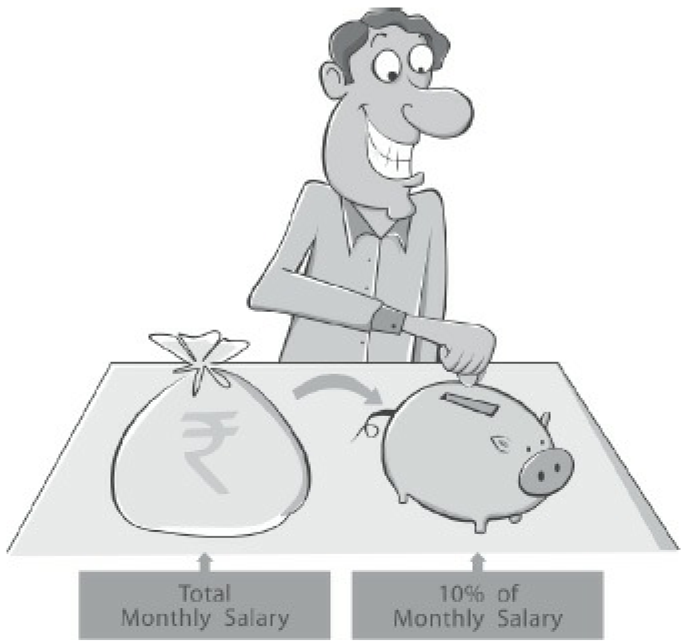
The next issue that arises is the "Liquidity Problem". Most people do not think about the lock-in period and do not take into consideration their liquidity requirements for the next few years. There area lot of cases wherein one has invested in tax saving mutual funds, ULIP's, etc., or even tax saving fixed deposits even though they have some money requirement coming up in the next 1-2 years. While they may be vaguely aware of this requirement, they don't pay much attention to it and just fall prey to the moment. Their sole mission at that moment is to "Save Tax". They repent later and blame companies, agents and the whole world for "trapping them".

What we must learn

Tax saving is simply a benefit provided to you by the government, when you invest your money. Don't make it your primary objective when you invest. What you have to concentrate on is your investment planning and how to structure your investments in such a way that you get the maximum tax benefits from them, side by side. By all means, make sure that you save as much tax as you can but not at the cost of your financial commitments in the long term. Investment planning comes first and tax planning is a by-product or a secondary concern. If you are not able to save tax, it's fine. Pay taxes. But don't get into useless products which you regret later.

It's always better to avoid getting into unnecessary products which don't suit you and affect your financial life in the long run. Tax planning is important, but more than that it's important that you don't get over-obsessed with it.

2. Start living with just 90% of your salary



You walk into the office tomorrow and your boss tells you, "You get a salary cut of 10% from this month! We are sorry. Either take it or just search for another opportunity".

I am sure that you will not like this idea one bit. But just for a moment imagine this situation. How is this going to affect your financial life? Will you be able to still do the following things? Answer this honestly.

– Pay your rent

– Pay your EMI's, incase you have to

– Meet all your household expenses

– Pay your children’s fees

– Spend on things you enjoy like entertainment, eating out, occasional splurging, etc.

Most of you reading this book will answer YES! If people control and prioritize their spending, it is certainly possible for them to live on just 90% of their salary. Don’t say Yes or No just yet. I want you to imagine the situation. Take a paper and pen and do the math. Is it really possible or not? Obviously, there will be some exceptions, but then those people are really, really broke! We are talking about a majority of people here.

Why is this required?

Most people do not save anything at the end of the month. They feel as if their life takes away all the money from their pocket by the month end. However, this is a psychological effect. Many of us never sit down and think about this. We just “adjust” our needs and desires in life to what we earn. If our salaries increased by 50% in 2 years, a bike gets upgraded to a car; a small car gets upgraded to a bigger one and a normal TV is replaced by a plasma. “Supply creates its own demand” is a law of economics and it applies to personal spending too.

When we have money in our hand, we will come up with numerous excuses to prove that we can’t live on less money. Go back 5 years in your life and think again: have you created your own demands in life? Almost all salaried people contribute to provident funds from their salaries. What if there was no concept of provident fund and you got all your money in your salary account? Do you still feel you could have saved that amount each month with discipline! I doubt very much.

What you should do from next month

Are you looking at a 10% cut in your salary from next month onwards? I am sure you are not. But you can certainly pretend that you are. The next time you get your salary, take 10% of it and immediately deposit it in some other bank account, or better still, give your bank standing instructions to cut 10% of your salary and transfer it electronically to another bank account. Try to live your life with 90% of your salary. I bet you can do it.

Saving 10% of your salary can have a drastic effect on your investments and you can create some wealth in the long term. I will not tell you which expenses you can cut out and how you can adjust your finances. The best part of this trick is that it all happens automatically once you start doing this. You will automatically “adjust” to your circumstances. If you are fairly successful, try to give yourself a bigger pay cut!

Does saving 10% means that you start living a frugal life?

Note that saving money does not mean depriving yourself of all the good things in life. The only thing that I am saying here is that we have slowly started going the American Way, i.e. spending more than what we can earn. For the last couple of years, we have been using too many credit cards and in the wrong way. We are a nation which saves but we do not invest properly. Now we have started spending like never before. Spending is important but don’t make it a hobby. It’s like a cancer. It will not hurt you immediately, but kill you someday.

3. Control excessive leverage and careless spending

In recent times, we have been spending like there's no tomorrow. There are enough reasons these days to convince yourself that "I can afford it".

EMIs are available on everything from international vacations to a pair of jeans! All it does is cut a big piece of debt into smaller chunks, to make us believe that we can afford it. If the EMI amount is more than you can afford, just increase the tenure by 3 times and voila…the product just got affordable! You have to pay only ₹ 6,000 per month instead of ₹ 15,000 per month. If it still looks unaffordable, increase the tenure a little more!

It's human nature. If you tell someone the EMI that needs to be paid to purchase a product, chances are that they will believe that they can afford it, even though they would have thought more than twice about purchasing it if they heard the actual price of the product. The problem lies in the numbers. The lower the number, the more affordable it becomes! However, this is not true! Actually, the more you reduce the EMI figure, the longer the tenure, and accordingly the higher will be the total cost due to all that interest you have to pay!

This leverage available today has created a new mind-set - “buy now, pay later”. Unlike our parents and grandparents, we are spending money, which we haven’t even earned. We buy houses, cars, vacations, etc., and then pay the cost for the rest of our working lives. In some cases, it might make sense, but a large section of society just lives beyond their means.

We feel guilty when we pay cash

Research shows that we feel less guilty when we pay with our credit cards than we do while paying in cash. When we use cards, we don’t see money going out; there’s just a consolidated bill once a month. Nothing can be done (or undone) then. You just pay up the amount on the bottom-line. Imagine you are paying cash every time you buy something you really do not need. We buy unwanted clothes and unnecessary gadgets. How many of us can claim that sometimes we just can’t survive without a certain device, or feel that we can’t enjoy our life without certain doodads? Didn’t our parents and the old generation live without them or with limited quantities of them?

Why have we all suddenly shifted to plasma TVs instead of the old TVs we have used in our childhood? Of course, technological changes should happen and we should always move forward, but buying a plasma TV just because it looks cool does not make sense at all, especially, if you haven’t planned for your retirement or taken care of all the important goals in your life. If it’s really your need, then go ahead, I would encourage it. But most of the time, people buy it just to keep up with friends and relatives. Once your other priorities have been met, you can go in for it. But it should not be at the cost of something more important.

I’ve heard horror stories of people who have bought homes and are crying today. They have moved into more fancy homes, but the quality of their life has drastically decreased. They suffer from stress because now even small things in life which gave them happiness look unaffordable…all because that 2 BHK flat’s EMI has to go through next month.

No quality trips and vacations, heavy stress because of insecurities of jobs. Imagine a double income family who collectively earn more than Rs 1 lakh (and belong to the top 1 percentile of the highest earners in our country) may not be leading a happy life because of the excessive debt they have taken on. What's the point of earning so well then? Don't try to be over ambitious at the cost of your current lifestyle and happiness! If you can't manage your life successfully and happily then the car and the house and all that financial planning is just a waste.

Most people take on more debt than they can afford or deserve. The criteria for giving credit is mainly how much you earn. The credit card company never knows how much your expenses amount to or what your future goals are or your risk appetite is or what future plans you have. People earning ₹ 5 lakh per annum sometimes have a debt of ₹ 30 lakh due to a home loan and yet they unnecessarily take on further personal loans to buy LCDs, to go on vacation and to spend on other non-priorities in life. This can have ill-effects later. Also, companies are now keeping an eye on your credit consumption behavior and it affects your credit score, which companies in India have started using as a decision making variable. So, keep your credit consumption behavior within limits.

4. Invest in great things other than financial instruments

When we say “investments”, we just think about money. If I tell you to visualize yourself making some great investments, by default, the only thing which will come to your mind will be putting some money into a financial product. That’s all! That’s wired in us. Nothing wrong with it, but I would like to draw your attention to some other investments which are as important as monetary investments.

In this fast moving world, we tend to overlook some really important things and do not give them as much value, time and effort as they deserve. We think too much about financial investments and assume that they are the surest way to lead a great life in the future. However, that’s far from the truth. A lot of money is good, but not at the cost of other important things in life, such as family, health, education and career.

There are many people in the world who have built a lot of wealth over the years, but during their journey towards their financial freedom, they have lost their health. They have several diseases as they have never spent much time tending to their health. They have money today, but all that money cannot be utilized as satisfyingly as they had imagined. No matter how much health insurance you buy, the best insurance is still a good healthy body and good exercise. You should be spending some dedicated time and effort making sure that you eat right and take good care of your body. Life is full of small moments and a healthy body makes sure you cherish each moment in life. Each moment should be full of energy, confidence and an enriching mindset, which can not come from a lot of money alone. So, invest at least 1 hour each day towards building up your health. Exercise, go for walks, eat right. Even if you have a little less money at the end, you would still be better off.

Coming to the next thing, there are many investors who are so lost in generating wealth and earning more and more money in life that they don’t spend any quality time with their kids and spouse. Life just becomes a daily routine where you eat, sleep and occasionally spend time with family. But it’s not enough. We earn a lot of money and keep investing it to make sure our family has enough in the future. You want your children to have enough money tomorrow to live happily and be able to get whatever they want in life. While that’s a good thing to do, most of us over-do it to the extent that we don’t spend quality time with our loved ones. Remember that humans came much earlier than money and money is a creation of humans. Your parents, children and spouse are more important than any amount of money. So, why don’t we make time for them? Invest in good outings with your loved one so that they feel cared for and connected to you. Investing your time with your family always gives you assured returns.

SIP investment in your Health and Family

The conclusion I want to make is that money is a creation of human beings. It’s a medium to enjoy other things in life which are given to us by nature. If we spend all our energy and time just acquiring wealth, there will be no point in having it, unless that’s exactly what you want in life. So, invest some of your time in your health and your family, which are your real wealth. Most people shower their love and affection on both their health and family in a lump sum-once in a while, depending on the Situation. You need to start SIP investments for your health and family. Join a gym, go for a walk daily and take care of your health on an ongoing basis. In the same way, take care of your loved ones and invest time in being with them on a regular basis. Don't wait for a major event to happen in life which forces you to show that you love them and care for them.

5. Become the CEO of your financial life and deliver performance

Have you even run any company or even thought of owning one? If you are made the CEO of a company, how will you run it? What kind of dedication will you show to make sure that it remains one of the best in its category? Will you spend more time on it? Will you give your 100% attention to it? Will you make sure you employ the right people and ensure that they provide enough value to your company?

What if you don't own a company, you own your financial life today and it's nothing less than a company, which needs proper management and dedication. For a moment, try to change the way you look at your financial life. It's not just another routine job for you; it's not just something like your 9 to 5 job, which perhaps you have to force yourself to do. It's some thing you own. It's something which is 100% yours. What if you don't own a company, you are still the CEO of your financial life and you can act as if you are running a company! Focus on your targets (target returns), your revenues (monthly investments) and what kind of profits you are generating (returns per year from your investments).

Each financial product which you have bought or which you will buy in future are your employees, who will work day and night and will be responsible for the performance of your financial life. That should show you clearly that you need to be very selective about who you choose to work for you and pay full attention to what you are investing in. You need to look at their individual performance records and make sure you reward those who are performing well and get rid of those who are not performing well or you will find that you have made a mistake by employing them.

Here are some parallels between running a company and handing your financial life:

Employing someone	Buying a financial product
Interviewing someone	Doing the pre-buying research and findings
Making profits and losses each year	Getting positive or negative returns
Firing some one from a company	Getting rid of a bad product
Decreasing your operating cost	Optimizing spendings and expenses
Maximizing revenue	Increasing your investments (increasing

	income)
Holding a team meeting	Doing an annual or quarterly review of your portfolio

And there are many more…

Conclusion

The whole idea is to convince you that you actually already own a company and must undertake all the activities required to make that company successful. Be more committed and you will automatically become more successful from now onwards.

6. Don’t fall prey to instant gratification in your financial life

Humans are programmed by nature to fall for things which give them happiness instantly. This is known as ‘instant gratification’. Instant gratification is the habit of always wanting to enjoy now, and not having the patience to wait for future benefits. Anything which gives us temporary happiness or excitement, but is not actually a good thing for your life, can be put in this category. For example…

- You have to get up early in the morning and go out to exercise, but instead you keep sleeping. This gives you instant comfort and joy, but it's not the best thing for you in the long run.

- You eat those unlimited sweets in your office cafeteria; you enjoy that moment. But from the long term point of view, it's something which you should control else you will have medical issues later.

- Similarly, you eat that burger with EXTRA cheese!

I assume that everyone will agree that none of the above gives you any benefits in the long term. All these examples are to give you an idea about what instant gratification is - mainly concentrating on the immediate result and not thinking about the outcome in the future or how it will affect us later in life. If you can control yourself and concentrate on "delayed gratification", which means what you will get later in your life, your life can change! Considerably. But in our day to day lives, we never bother about all these points and never have any motivation to think so hard! Do you know why this is? Let me be straight and blunt. The challenge is that most of us do not have to face life or death situations, or seek food and shelter or defend our territory everyday anymore. Whatever happens, we will get our next meal and the next movie is definitely on the weekend plan. We are just moving on and enjoying our life. A lot of us have just lost that attitude of looking at things without instant gratification.

The result is that we can't see the impact of our current spending on our future life. Think about a poor person who struggles daily for food. If he has to spend ₹ 100 on something, how will he think? If you offer to buy him a Burger, he will instead ask for the equivalent amount in cash. This is because he knows that the money will help him get food for the next 3 days. He's not focused on taste in this case. The burger might taste better than what a poor person has everyday, but he will not be ready to lose 3 days' worth of his food, by falling for instant gratification.

If I connect this with personal finance, I can highlight 3 areas which force people make bad decisions because they look for instant gratification.

#1 Not surrendering Endowment/ULIPs

This one is my favorite. “What should I do with my policy? Should I surrender it or make it paid up?” is one of the top most queries I come across. It feels bad, accepting and acknowledging that you’ve made a mistake, and it hurts psychologically when you lose by not continuing the policy. But what is the effect, long-term? You still continue paying huge premiums and it delivers a lower return than you can get from other products in the long term.

So you don’t take any decision on your junk policies, ergo you do not have to face a tough situation. By not taking any action, you have not encountered a bad feeling. You do not feel like you have lost some money. But it’s for your own good though. It’s instant gratification, in a way! You should take action and take that loss right now, because right now it’s a whole lot smaller than if you stick with the policy and try to quit later!

#2 Getting into the wrong products for tax saving

When we talk to a lot of our clients about why they have bought Endowment or Money back policies or even ULIPs, the only reason turns out to be “Tax Saving”. Millions of people, get into the wrong products which they don’t need and don’t understand; products which have no power to meet their financial goals in the future, just to save tax!

I sometimes wonder how much tax people really save by going in for such products! If one invests in a ULIP with a premium of ₹ 50,000 per annum, for instance, and if that person is in the 30% tax bracket, he will save ₹ 15,000 in tax. But if that was a ULIP with a 50% premium allocation charge (which is the case, quite often), ₹ 25,000 is lost the moment you sign the documents! So you save 15k and lose 25k as charges! And yet, these are the same people who say “10k for a financial planner—too costly!”

#3 Keep losing money in bad shares and selling your winners

Have you ever bought a share and seen an immediate spurt in its price after that? What was your reaction? Most people would like to sell off such shares and take that profit right now, otherwise the profits may vanish! But what happens in most cases? The same stock or portfolio would have given huge returns in future, if it was left untouched.

Unfortunately, that feeling of instant happiness is so powerful sometimes that so many can’t resist it.

In the same way, you might be holding some stocks which are not performing well. But instead of getting rid of them and investing in better stocks, we keep on holding on to the losers in the hope that some day they will go up! It’s another case of instant gratification as you seek temporary comfort. You don’t take the tough decision of selling the loser, because the moment you sell it, it gives you a feeling of loss, but if you just keep it as it is, it’s a case of “I still have some hope!” Don’t do it!

7. Teach your Spouse & Kids about money

From time immortal, a woman has been dependent on her father or husband for money and to fulfill her dreams. If she wants to go for a trip or buy some jewelry or anything else, for that matter, she has to ask her husband (or demand) for money. Many a times women have their own dreams, which they want to fulfill on their own, but they cannot.

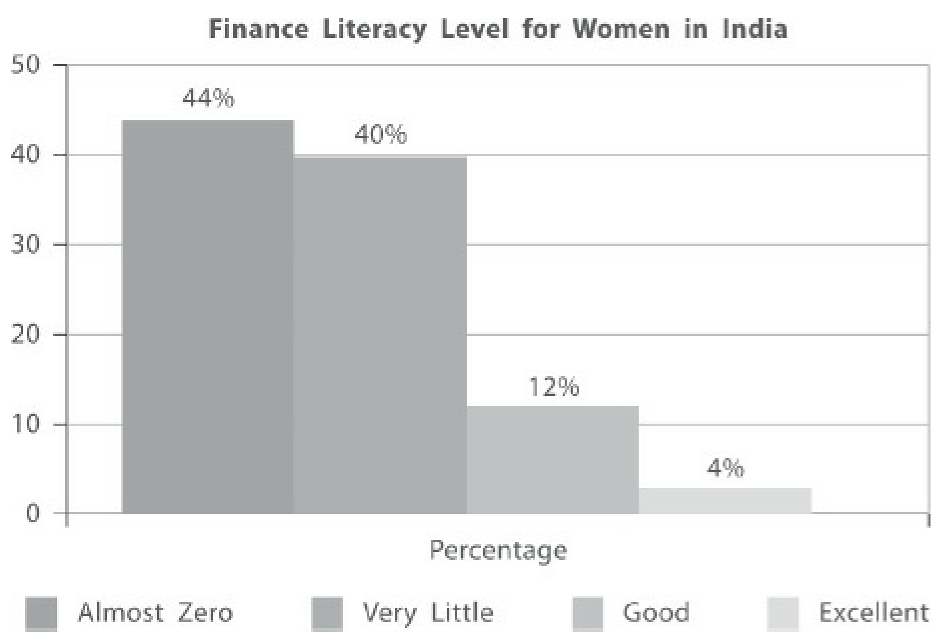
There are many men who do not involve ladies at home in the decisions regarding insurance, investments, retirement planning, banking, budgeting, etc., and it’s not the right thing to do. Most often, women have a better understanding about the future goals of the family, especially children’s education related expenses and so on. Men, sometimes cannot understand long-term expenses, for instance, they may not be able to envision how the family expenses will be after they retire and what kind of situation they would be living in. However smart we feel we are, there are many things that women outsmart us at. We should involve them in every decision we want to take in our life. So, the next time you think about insurance, talk to your spouse about her needs in case you are gone. Don’t shy away, feeling that this is taboo in this country. You have to plan things well and understand her needs. Also while planning for retirement, take her advice and her views on what your standard of living is likely to be after retirement, what your (and her) post retirement plans are, etc. She will give you many suggestions and it will help in planning.

On the flip side, women do not take much interest in personal finance. Here are the top two reasons for it:

1. Women treat the activities that contribute to their earnings as merely time pass: The biggest reason for this is that since the dawn of time, *man* has been the main provider and the primary bread-winner of the family. He was responsible for earning and managing money and taking care of financial goals. *Women*, on the other hand, were mainly responsible for raising children and taking care of household activities and to a large extent, maintaining relationships outside the house and in the community. Many women, despite being qualified enough, and having the skills to earn money, view their earnings as secondary to that of their men. They “feel” that they are not at the same level, even though it’s not true; most of this is psychological.

2. Everyone handling her money but her: For centuries, a woman’s financial decisions were taken care of by her father, then her husband and then her sons. She never got involved and was never encouraged to do so, because she was not considered smart enough! Men have always shown dominance over women in this space. One reason, which could be responsible for this is that women hardly ever ventured outside the house for these activities and never got time enough to do so from their household chores.

As per an in-house poll on my blog, 88% of urban women have either a very basic or no knowledge of personal finance. These are women in metros like Delhi, Mumbai, Bangalore and other tier-1 and tier-2 cities. Only a small percentage of women respondents have a good knowledge of personal finance. Here are the actual results



Why women should learn about personal finance

Our mind is designed to think about good situations and not dwell on situations which are uncomfortable. However, life is not always fair and sometimes we realize that when it is too late. A lot of women never learn about banking, insurance, investments, how to get their money to grow and related topics throughout their lives. They are smart, have good jobs, are earning well, but they never learn about money. Then someday, when sadly, things go wrong-for example they lose their husband because of an accident or some other reason, apart from emotional pain, there comes a bigger pain in life, i.e. taking care of the children's financial needs and overall finances. By then she has no idea how to invest money to ensure that the children's education is funded, her retirement is secured, etc. She suddenly finds herself in a very tough situation and has to rely on others, (relatives, friends etc.). This is not a good situation. Girls! Ladies! Please learn about money, even if you don't like the thought of it… Learn the bare minimum, enough to enable you to take charge of things so that no one can take advantage of your situation.

Teach your kids about money

Do your children know how much you earn? Do they have a clear picture about how you are placed financially? NO!

Kids should know about your work and how much you earn. They should be aware of how you are saving money to fund their education, bike, trips, etc. Once they know about it, chances are they will be a lot more supportive, more realistic in their demands and stay well within their limits.

Kids don't know sometimes, how much effort it takes to earn money. Most of the time, kids know your salary and your designation in a company and assume the family to be a "higher middle class" one. Once you tell them about home loan EMIs, car loans, other liabilities, retirement savings, education expenses, marriage expenses and the medical emergencies for which you are saving, they will have a better idea about the current situation and they will act responsibly.

Parents feel a little uncomfortable telling their kids these things, as they feel that the children are still young and such information will create unnecessary psychological pressures. Parents feel that children should start learning about finance and applying that knowledge once they get a job and start earning. I say, if your finances and spending habits are messed up today, one of the main reasons could be that your parents never talked with you openly about finance. The same applies to spouses. Imagine, if you had a much better knowledge and attitude towards money 10 years ago; or when you started earning? The situation would have been very different today, wouldn't it?

Financial Education for Children

Financial Education for Children is as important as their regular education. Sadly, we do not have financial education as part of our school curriculum. However, you can start teaching your children the basics of money, so that they become more aware, more responsible and think more realistically about finance. It'll not just help your children but even you, as a parent, in many ways. Here, I present 2 things to teach your children as your first step.

Different ways of investing:

Teach them banking basics: how banks operate and what it means to earn interest on an amount. You can also buy them some games which teach investing. Ask them to deposit some amount with you and you can pay them interest per month. When you give them pocket-money, let's say ₹ 500 per month, ask them to deposit ₹ 250 with you, with the assurance that next month you will pay them 10% interest on that amount, i.e. ₹ 275. Though you might be out-of-pocket by ₹ 25, the knowledge you impart to them is priceless! This ₹ 25 gives them the important message, that saving their money and investing regularly can increase their money many times over. When they start earning later in life, this gyan will be something they respect you for! Also, don't forget to open a bank account for your child as soon as they turn 12-13 years old.

How to live on a budget:

If you give your children pocket-money, make sure they live on it the entire month. Make sure that they do not come to you in the middle of month, asking for more, for expenses they could have managed with the amount of pocket-money they had. This happens only when children deviate from their monthly needs and carelessly spend on what they don't need. While they may ask for more because of some emergency need sometimes, over a long-term, you should make sure they stretch that pocket-money through the month. Children will understand budgeting better if you yourself practice it (ouch!). When they see how you allocate expenses each month, and stick to it, chances are, they will replicate it at their level. While, this whole thing can be tough initially, help them out by giving them the extra money they need in the first 2-3 months and then restrict it gradually.

8. Focus on action, don't let little things get in the way

Have you noticed that in your life, you have often wanted to complete something or find out something and then you lose focus, after trying for some time! This is exactly what happens in our financial life. Most investors chase a lot of unimportant things when it comes to personal finance. They will keep running around looking for the best policies; they will keep doing research, study what the best and the worst buys are; they will make sure they find out the best strategy to get more than better results for their portfolio… However, they will fail to do the most important thing and that’s taking action!

Taking action is actually doing things and moving forward. In our financial life, we generally come to a stop because of one reason or another and waste our time doing useless or relatively unimportant things. Details some times block our way and limit our action taking capability. I will give you a real life example of this.

My teammate wanted to buy an amazing book, which he had heard about from someone. He was really excited about buying it and wanted to do so asap. He went to an online bookshop and placed the order; it would cost him ₹ 270 there. As he was going to hit the “Buy Online” button, he remembered that there was another website selling books online and he thought he should check out the price at that online store too. To his surprise, the cost of the same book was just ₹ 245 there. It was cheaper by ₹ 25. He was confused now because he was sure this ₹ 25 profit came at some cost. Looking deeper, he realized that the delivery time was 10 days! The first website promised to ship it in just 2 days. This set him thinking about what he should do now. As he did not need the book really urgently, he didn’t mind waiting for 10 days. But then he also read a customer review on how both the websites’ customer care was bad and ten other problems coupled with some good feedback too. I hope you can see where I am heading. He was clear that he wanted the book. He had the money, but there was too much analysis and no ACTION. He didn’t order that book finally. All his focus was diverted to small things and he never took any ACTION.

Don’t let this happen in your financial life. Once you are clear about something, take action and do it. Let’s look at our financial life and see how we deviate most of the time from taking action.

Example 1: Let’s suppose you wanted to buy a term plan. You know that your family needs it and you know you can shell out the premium easily. But suddenly you realize that your premium will be higher than you initially expected due to some medical issue. Just because you didn’t expect this, you balk at this extra premium you have to pay. Deep inside, you know that there is nothing wrong with anything. That extra premium is something genuine. But then you go to other websites, try to justify your inkling that the first company is a cheat and not transparent. You do everything; but you don’t take action! You just have to accept it and move forward. You mustn’t deviate from your main goal and that’s “securing your loved one’s against some mishap”. I have known people who need a ₹ 50 lakh cover and their premium was originally ₹ 10,000 but after medical check-ups it was increased to ₹ 14,000 and these people just cancelled the policy. They are still searching for the best opportunity. They do some great analysis but take no action!

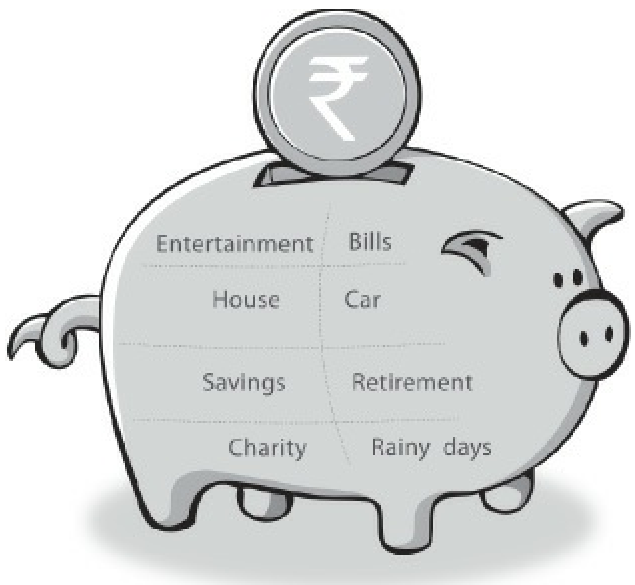
Example 2: Suppose you want to hire a great financial advisor/planner and transform your financial life. Your ultimate goal here is to go ahead and do your financial planning. Now if you find a planner who is exactly all you expected and hire him, you will benefit a lot, for sure. But let's say he mentions that his fees are ₹ 20,000. You show your concern about the fees and try to negotiate with him and bring them down to ₹ 15,000. It doesn't go through and you don't go ahead. Do you know what has happened? You got a mental block here because of the fees! Here fees became such a big thing for you that you deviated from your main agenda. The fees became bigger than your financial life itself. An amount of ₹ 5000 will not make a difference to the financial planner's life, but that same ₹ 5,000 will completely change your life. If today ₹ 5,000 was your reason for not hiring the planner, it can cost you lakhs in the coming years because of the mistakes you might make. This is not to say that you should pay anything that a planner asks for, but a lot of times, we just want to bargain and get things at lower costs. If you succeed in getting your price, you're in luck! Otherwise, just move forward!

Example 3: If you hold stocks or equity mutual funds and your investments have given good returns, it's time to realize your profits. You keep on expecting prices to go a bit higher so that you get a little extra return. Then prices move up and down and you keep getting driven by greed and fear. If you were going to book 70% gains earlier, how does it matter if it is actually 69 or 68%. Why do you have to take it so seriously that it stops you from your actual motive of booking profits! In the end, you might end up with a 50% profit instead of 70%, along with a lot of frustration.

Example 4: You want to open a trading account with a broking house and start buying shares. Here your motive is to open a trading account. If you area serious trader/investor who is going to buy and sell frequently, the costs per transaction should be a big concern. But for someone who is going to undertake a few trades a year, analysing the costs too much will only keep delaying your decision to open that account. Company A will offer brokerage at 50 paisa per trade and company B may offer 40 paisa per trade. You will get lost in these small and unimportant details when what you should really do is just some basic checks and settle for a reputed brokerage house. Now, if you are going to invest just ₹ 20,000 per year in stocks, how does it matter much if your brokerage is .75% or .30%. Again, little things got in the way!

Don't forget to take action. Look at the bigger picture always. Small things are important, but make sure you give them only as much importance as they deserve. Don't make them so big that they start dominating your actual goals.

9. Re-define "budgeting" as "priority spending"



Budgeting works, but only for a handful of dedicated and disciplined people in this world. All the rest just plan to make a budget, start this exercise and then again just plan to make a budget and start the exercise all over again and soon…

Budgeting is boring because it makes you feel as if you don't have any control over where you can spend, in case you really feel the urge to. It requires some follow-up and coming back each month to find out how you have fared and no one likes to fail, so guess what? They just avoid it all together. I have never seen enough people who budget to justify my calling it a popular activity! Budgeting is all about allocating your money for future savings and expenses. So, if you earn ₹ 5 lakh per year, budgeting would require you to define exactly how much will go towards rent, EMI, groceries, **Utility** bills, petrol bills, kids education, clothing, etc., etc. Most people view it as over-defining how you should spend and that really bores them. Finally it de-motivates them to keep doing it month after month.

Can we undertake something that is similar to but not exactly budgeting? Something which is much simpler that budgeting, in a way. I can’t say that it will control your spending, but it could improve the quality of your spending. Here is the rule… “You can spend like crazy on things which you enjoy doing but you must cut down on anything which does not make you feel that you are adding value to your life”. And here’s how you can do it.

List down all your expenses, i.e. list down all the things which you pay for each month. List down each thing one by one and also the amount you spend on it. Now assign a priority number to each of them, starting from 1; 1 being most important. So, if you have 10 things on the list, they will be ranked from 1 to 10. Now, re-write all these things so that what is ranked 1 comes first, then what is ranked 2 comes second and so on until what is ranked 10 comes last. Then, take 30% or 40% of the things towards the end of your list and write down why you need each of those things. Also put down ways in which you can restructure this spending so that it would cost less. For example, when I did this myself, one of the items on the list was telephone expenses, which used to be around Rs 4,000 each month. However, when I thought really hard about it and sat down one day to write down what I could do about it, I realized that if I switched to a pre-paid plan instead of a post paid, I could do a lot better, as prepaid pricing was cheaper and there were many top up plans which saved a lot for me, as per my situation. My telephone bill came down to ₹ 2,500, albeit with a little inconvenience since I had to recharge my phone every week now. But I saved ₹ 1,500 and I was talking for the same amount of time with the same people. No compromise on that.

The whole idea of priority spending is to not cut your expenses, but to make sure you cut out useless stuff from your life and utilize that money on something useful or rather on what you are passionate about. If you love photography, spend well on it; learn more about it, take photography classes, attend workshops, get supreme quality lens, invest in good equipment, etc. But you should do all this only to the extent that you are able to cut down on expenses on other things, which you do not consider as a priority; things which do not add much value to your life. Mark my words: you will need to have strong guts to do this.

Separate your wants from your needs

When you undertake priority spending, it's a good exercise to separate the items on your expenditure list into "Needs" and "Wants". Improper handling of money takes place when you spend too much money on your wants and too little on your needs. The first aim should be to spend/save money for your needs and then take care of your wants or desires. Once you prioritize all your expenses/goals in these categories, it's much easier for you to improve your financial life.

What is the Difference between a Need and a Want?

Needs: A need is something which is essential for you, irrespective of your financial conditions. These are the things you have to take care of first and only then can you spend on other things, i.e. things which you can do without.

Example of needs

– Household expenses

– Children’s education

– Saving money for retirement

– Medical expenses

– School/college fees and related expenses

– Family vacations and outings (within limits)

Wants: These are things which you wish to have, but they are not above your needs. For example, a fancy car is a want when compared to your child’s school fees or saving for her higher education. You can live your life without car, but your child’s education is vital and can’t be compromised on. Some people’s “wants” can be other people’s “needs” and vice versa. It all depends on your personal life style and attitude. But the main point I am making here is that you have to differentiate between your ‘needs’ and ‘wants’. What’s more, your needs and wants can change over time, so qualify them as per time frames-short to medium time frame or long term. Now I do not mean that you shouldn’t try to fulfill your wants in life. My only point is that your needs should not be compromised because of your wants.

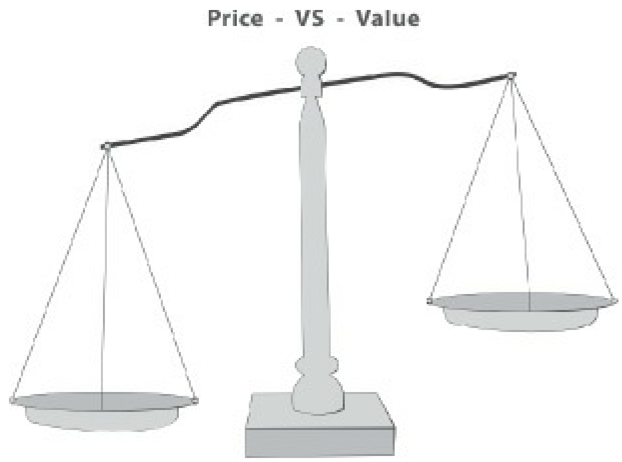
Example of wants

– Extra vacation

– Expensive clothes, over and above your normal requirements

– Fancy car or any vehicle beyond your budget.

10. Look at the value or real return of a product



In today's financial world, a lot of products are made to appear as if they are amazing. The advertisements and promos make you feel that if you don't invest in them, you will miss an opportunity of a life time. The reason why this happens is because buyers concentrate a lot on the price of a product, rather than on understanding its value. Let me define value and price here so that you can understand them more distinctly.

- **Price:** Price is the amount of money required to buy something or the monetary profit arising from something

- **Value:** Value is the worth or importance of something.

Imagine someone offers to create for you a financial plan which will cover all the aspects of your financial life along with research, analysis, recommendations and personal support for 1 year. The cost of the whole package is ₹ 3,000. In all probability, it is likely to be an automated financial plan, created from some software because ₹ 3,000 cannot get you a customized financial plan. Even though it might look like an inexpensive product, it might turn out to be one of the costliest things you have bought, a total waste. Obviously, if you pay ₹ 3,000 for something and you get a ZERO return out of, it's a 100% loss. We have seen many of our clients coming to us with those kinds of plans, which were worthless for them.

On the other hand, another financial planner asks for a fee of 25 k and he can make a major change in your financial life by just sitting with you and counseling you on your financial life and the mistakes you should avoid. It might look expensive (if you look at the price), but if you look at the value you get out of it, it would be a worthwhile product. In fact, if it delivers good results, it could even cover its cost and come to you free, because you save 10 times the money it cost you to buy the plan, just by not doing all those stupid things you did before hiring that planner.

Is purchasing term insurance a waste of money?

Millions of investors have discarded the possibility of buying term insurance as they don't get any money back at maturity. You now realize what they all concentrated on: the price. They feel that they "lose" their money. They have concentrated only on what they don't get and not on what they are getting. These investors do not think, for a moment, about the value which term insurance provides to their family and dependents at the price they pay for it.

Value does not merely mean returns

A lot of people do not surrender their policies, which are doing badly, just because the amount they will get will be lower than what they have paid. All of them just concentrate on "price" and "amount". They never look at it from the long term perspective and never question the value it's providing in their financial life in the present or in the future.

I am sure that if you start incorporating these 10 commandments in your financial life, it would become more strong and robust. A lot of confusion and wrong doings will vanish and your focus will get better and better. There are many other good things which you can practice, but at the minimum try to incorporate these 10 points religiously in your financial life.

Chapter 8

16 PRINCIPLE EVERY INVESTOR MUST KNOW

Finally, your journey through this book has come to an end. While reading it, you have certainly come closer to your tryst with wealth. Although you are motivated and all charged up after reading all the eye-opening insights that you have come across in the book, you have not reached your goal yet. There are 2 things you still need to do:

Remember and Live by the 16 basic ‘Rules for an Excellent Financial Life’.

1. Smart investors are early investors

2. Secure your life to ensure peace of mind

3. Clear goals leads to clear direction

4. Use Equity for long term goals, Debt for Short term goals

5. Instead of asking how to, ask Do you want to or not

6. Simple financial life is awesome financial life

7. Focus on earning more rather than saving tax

8. Don’t consume 100% when you can live on 90%

9. Simply put the First things first not second or third

10. Invest in yourself and not just in financial products

11. If your financial life is your business, then you are the CEO

12. Personal finance Short cut ends up to be long cut

13. Always Educate yourself to educate other family members

14. Focus on bigger picture rather than small things

15. Spend on what you really need, not on what you think you need

16. Look at “Value” not the “price”

Take action - Complete all the important tasks.

What's Next?

Finally, your journey through this book has come to an end. While reading it, you have certainly come closer to your tryst with wealth. Although you are motivated and all charged up after reading all the eye-opening insights that you have come across in the book, you have not reached your goal yet. There are 2 things you still need to do:

Firstly-Remember the 16 basic 'Rules for an Excellent Financial Life'

Based on all the 7 chapters you have read so far, here are 16 foundation rules that you should always live by. These 16 rules will help you lead an excellent financial life.

Invest as much as you can, as soon as you can. The sooner you begin investing, the higher will be the benefits that you receive in the long term.

Protect your family's happiness with a term insurance plan so that in case you are not around, your family can still achieve everything you had planned for them.

Start out by defining your financial goals very clearly the always take actions which will take you closer to those financial goals; anything else you do might be a waste of time and energy.

Whenever you take investing decisions, always remember that "Equity products are best for long term investments" and "Debt(secure) products are best for short term investing"

Always have a 'want-to' attitude when it comes to your financial life. You have to make things change, don't just expect them to happen.

Before you take any action in your financial life, make sure that it will simplify your financial life, not complicate it;, if it complicating things, it might not be worth taking!

Do not invest with 'Saving Tax' as your primary motive. If you are able to save tax as a by-product of your decisions, its fine, otherwise don't even consider it.

Pay yourself by saving 10% of your salary each month without fail and imagine that your salary is only 90% of what it actually is.

Enjoy your life by spending on things which matter; don't spend on useless things which don't add value to your financial life.

Always see your financial life as an extension of your life, not LIFE itself! There are other great investments in life like career, health and family.

Behave as if your financial life is a company and you are its CEO. Think from a CEO's point of view before taking any financial decision.

Do not fall for short term gratification which gives you instant happiness although it is not that good for your financial life. Good things come with patience, so take hard decisions which contribute to a great future.

Teach your spouse and kids about personal finance, it's not just a good thing, but a requirement in today's world. An educated family means a better future.

Focus on actions, not the small obstacles which come in the way and do not matter much.

Define how you will spend your money and on what. Prioritize well.

Rather than Price, look at the Value of something before buying it. If the value you derive is more than the price you pay, the price does not matter.

Secondly-Take action-Complete all the important tasks

The next thing you have to do is complete your important actions points which will take your financial life to the next level. Don't wait for that perfect moment, which is never going to come. Just start work now at this moment. To help you move further in your financial life we suggest:

Option 1-You can buy our next set of books (titles listed below):-

- How to be your own financial planner in 10 steps
- 11 Principles to achieve financial freedom

In the former you, you will see how anyone can undertake base level financial planning all by themselves. The latter is a guide on how to achieve Financial Freedom written by my colleague Nandish.

Option 2-You can also hire a financial planner to give you unbiased advice and a roadmap for your next few financial years. He will work with you on how to take your financial life forward from where it stands. You can either look for one in your city, or you can also hire us, if you feel we are the right people. Just contact us at manish@jagoinvestor.com or visit www.jagoinvestor.com/services

Jago Investor Wealth Club

Our commitment to ensuring that every investor lives an awesome financial life

We invite you to build on what you have learnt in our books and blog today by joining the jago investor wealth club.

The wealth club comprises of an online community of committed investors. We would like to help you to become a more successful investor. The focus of the club is to provide investors with a safe environment where learning personal finance becomes fun. The central theme of this club is 'wealth'; it is designed to help you engage in conversations regarding living a good financial life. And how are we going to do this? By serving up, on a monthly basis, premium material that helps you as an investor. As a member you will receive premium content in audio and video format. You will also get dedicated e-books on different personal finance topics, different financial products, such as ready a reckoner list, excel based different tools, calculators and templates, that helps you facilitate and improve your financial life.

To get things started, we invite you to experience a part of wealth club. Send a mail to manish@jagoinvestor.com and we will send you some useful material that will help you immensely as an investor. We invite you visit www.jiwealthclub.com and become a part of this committed community of investors.

Manish Chauhan,

Financial Coach

Coming Soon

How to be your own Financial Planner in 10 Steps

“How to be your own financial planner in 10 steps” by Manish Chauhan shows us, how a common man can be his own financial planner and complete his financial life in a step by step manner with easy to understand language and actionable tables.

This book is the next step and a powerful extension of “16 Personal finance principles every Investor should know.” You understand the base rules of personal finance in this book, but in the next book, you can learn how to take actions and how to do some of the calculations related to your financial life. You can look at the next book as your passive financial planner which guides you in your financial life.