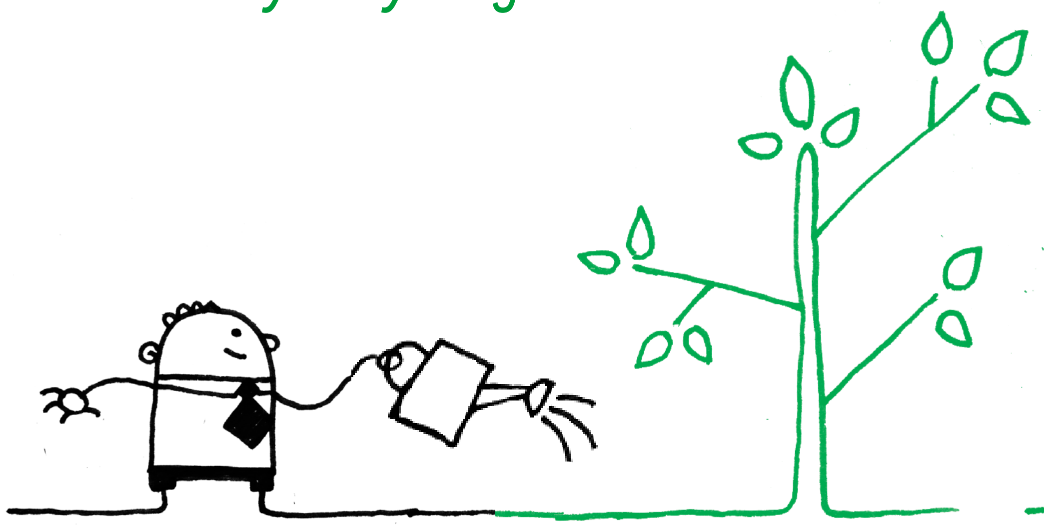
How to Grow your Savings?

'If you really want your money to grow,
stocks is the only way to go'



SARAL GYAN CAPITAL SERVICES
www.saralgyan.in
An Independent Equity Research Firm

Saral Gyan
Investors guide providing insight to equity market

How to Grow Your Savings?

How to Grow Your Savings?

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PREFACE

Many investors are absolutely fascinated about investing in stock market. But, in our opinion mere fascination is not enough. Investing wisely and with the right insights helps one to grow his savings by taking right investment decisions.

If investors do not have the right perspective, investing could be a puzzle. Investors could go down the wrong path, reaching an unwanted destination.

The purpose of this e-book is to provide all the necessary information so that you can acquire new skills and expand your knowledge, in order to accomplish profitable investments in the stock market.

The intention of this e-book is not only to provide advice on investments for beginners, but also aims to offer fresh ideas for experienced investors.

This e-book does not claim to give tips on particular investments, but rather aims to provide the reader with the broad, important and useful advice necessary to be translated into stock market success.

Through this e-book, Saral Gyan team has tried to capture their experience for the reader's benefit. The logical and straight forward way in which this e-book is written and organized will enable the reader to make right investment decisions to achieve long term goals and securing the future.

We hope it will be an informative and useful read for you.

Wish you always Happy Investing!

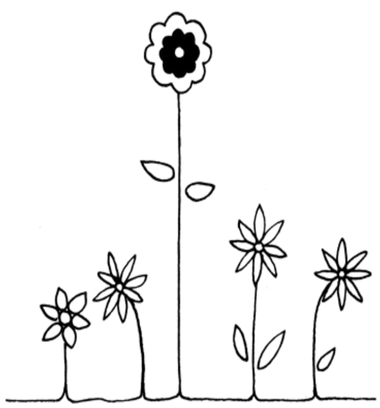
- Saral Gyan Team.

INTRODUCTION

"How to Grow your Savings?"

A guide to help you ensure, you get the best returns on your investments from equities.

This book will provide you important & relevant information supported by facts & figures to help you grow your savings by investing in stocks to succeed:



Key Mantra's:

1. Adopt discipline approach for Savings
2. Find out the ways to get passive income
3. Set your financial goals & start Investing
4. Do invest in equities for long term

Getting the most out of this book is simple, "How to Grow your Savings?" requires practical approach. Execute your learning experience in your day to day life by managing your finances effectively and achieve your long term goals.

Traditionally, Indians are Savers. The savings rate is as high as 30 percent. If not a direct savings in the bank, the money goes into a fixed deposit, gold or real estate. That trend might change soon if more people invest in stocks, which have outperformed every other asset class from 2001 to 2007.

Stocks have outperformed other asset classes by as much as 60 percent, yet only 3 percent of Indian population directly invests in stocks.

The main reasons for this is a lack of knowledge, awareness as well as unethical practices by a small minority of participants who encourage regular churning based on tips and rumours without giving proper financial planning to investors.

If someone invested in a Bank of India fixed deposit account in 2001, he or she would have an 8 percent return per year. If the same person invested in Bank of India stock he or she would have a total return of 4,800 percent as the stock rose from 12 rupees to all time high of 588 rupees in 2010.

How to Grow Your Savings?

Though Indians continue to be underinvested in the stock market there is more interest coming in from all corners. 200,000 new demat accounts are opened every month. Recent transparency measures should also bring more people in. The stock market will no longer be treated as a gamble but will be put on par with real estate and gold.

The irony is that even though stock markets as a long term asset class have given the highest returns, short term trading in futures and options has also caused the maximum losses. The maximum numbers of bankruptcies were caused due to the stock market crash in 2008-2009 amongst high risk speculative traders.

Power of Investing in Equity Market

Now, Just Imagine...

How much can you make in 30 years by just investing Rs.10,000 initially in any of financial instruments?

Take a wild guess?

Let us look at the real example.

If you have subscribed for 100 shares of "X" company with a face value of Rs. 100 in 1980.

- In 1981 company declared 1:1 bonus = you have 200 shares
- In 1985 company declared 1:1 bonus = you have 400 shares
- In 1986 company split the share to Rs. 10 = you have 4,000 shares
- In 1987 company declared 1:1 bonus = you have 8,000 shares
- In 1989 company declared 1:1 bonus = you have 16,000 shares
- In 1992 company declared 1:1 bonus = you have 32,000 shares
- In 1995 company declared 1:1 bonus = you have 64,000 shares
- In 1997 company declared 1:2 bonus = you have 1,92,000 shares
- In 1999 company split the share to Rs. 2 = you have 9,60,000 shares
- In 2004 company declared 1:2 bonus = you have 28,80,000 shares
- In 2005 company declared 1:1 bonus = you have 57,60,000 shares
- In 2010 company declared 3:2 bonus = you have 96,00,000 shares

In 2010, you have whopping 9.6 million shares of the company.

Any guess about the company?

(Hint: It's an Indian IT Company)

Any guess about the present valuation of Rs. 10,000 invested in 1980?

The company which has made fortune of millions is "WIPRO" with present valuation of 450+ crores (excluding dividend payments) for Rs. 10,000 invested in 1980.

Unbelievable, isn't it? But it's a Fact! Investing in companies with good fundamentals and proven track record can give far superior returns compared to any other asset class (real estate, precious metals, bonds etc) in a long run.

Will Wipro provide similar returns in next 30 years? Probably not, it's already an IT giant.

You need to explore companies in small and mid cap space with good track record and stay invested to create wealth in a long term.

It is a garden out there and one need to simply provide sufficient time to grow his quality seeds to get the fruits. One has to know what he is doing and has to be cognizant about it. With a little research and patience stock market investments can yield maximum returns.

So, how will you grow your savings? What are you investing in?

How to Grow Your Savings?

HOW TO READ THIS E-BOOK

Many authors tell readers that they can read their book any way the reader wants – in the sequence it is presented or dip into it depending upon their interest. This is not such a book. "How to Grow your Savings?" is presented to you in seven parts. Each part contains short subsections of ideas. You need to read the parts sub sequentially, in the order in which they are presented. Otherwise, the book will not serve its purpose, and you may not get the complete benefit from its reading.

Part I presents the basic understanding of inflation. Reading this section, one can easily understand, how exactly the purchasing power of currency decreases over time? This is important to know to work out the actual amount of savings required to meet your future goals.

In Part II, we will look at different ways to ensure high Income and high savings. What precautions one needs to take to reduce his expenditure and increase savings.

Part III clarifies the basic difference between saving & investing and why investing is important. Knowing different asset class available for investments and which needs to be chosen. This section also focuses on benefits of long term investing and explain how saving grows over time considering power of compounding.

In Part IV, we will look at how one can manage his investments by making his own investment plan. This is important for those who have started savings and want to build their diversified portfolio by investing in different asset classes to meet their needs in future. By answering a simple questionnaire, one can figure out his risk tolerance capacity and know whether he is an aggressive investor or a conservative investor.

The first four sections are then the foundational pillars on which every individual must build his life's investments to achieve his short as well as long term goals.

In Part V, we focused on the importance of building diversified portfolio keeping a significant investment in equities. When one can invest directly in individual stock and when he can prefer mutual funds.

In Part VI, we discussed the different types of risks involved while investing in stocks.

Finally, in Part VII, we discuss what it means to be a successful investor?

As your read this book, you will come across a wide range of examples, some positive, some negative. Presenting these examples has an inherent problem – because there is no 'correct' answer. It is quite probable you may have a different take from the one we present and that is absolutely ok.

Please visit www.saralgyan.in where you can leave your comments and suggestions on how the body of knowledge contained in this e-book can be preserved and expanded in the years to come.

How to Grow your Savings?

PART 1: VALUE OF MONEY

1. Inflation

What is Inflation?

We observe that the prices of all goods and services keep increasing. Take anything - sugar, petrol, vegetables, cost of postage - anything, you would see that its price has increased manifold over years.

This is Inflation that what we always keep hearing about. And it can have a disastrous impact on your savings and investments. Reason enough to understand it better?

Understanding Inflation

Inflation means reduction in the purchasing power of the currency. Simply put, it means that the same amount of currency would be able to get you less goods (and services) over time.

For example, today rice costs Rs. 20 per kg. After a year, its price goes up to Rs. 22 per kg. This means that its price has gone up by 10%, or that the inflation is 10% for rice.

This means that for Rs. 100, you can buy 5 kilos of rice today. But after a year, you would be able to buy only 4.5 kilos of rice for the same amount.

Thus, the purchasing power of Rs. 100 has reduced, or, generally speaking, the purchasing power of the currency has reduced. This is known as inflation.

(Note: In practice, inflation is derived from the price movements of a very large basket of goods and services. In the example, for simplicity's sake, we considered only Rice).

This means that the value of a Rupee today is not the same as its value at a later time. This brings us to another interesting concept.

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2. Past & Future Value of Money

Time Value of Money

Through the example, we saw that the value of the Rupee keeps decreasing over time. The value is highest today, and becomes less and less as time goes by. Although the unit (the Rupee) remains the same, its purchasing power decreases over time due to inflation.

That is only reason why we transact using 500 Rs & 1000 Rs note today which was not available in old days. Coins not is use with smallest denominations like 5 paisa, 10 paisa, 20 paisa, 25 paisa shows that we could not buy any goods or services using them now a days. Infact 1paisa, 2 paisa coins were also used half of the century ago.

Therefore, you can not compare an amount today with an amount at a later date without considering the time.

Say you lend someone Rs. 1000 today, and he returns Rs. 1000 after a year. Are you at par? No - because the value of Rs. 1000 after a year is not the same as its value today due to inflation. If inflation is 5% for the year, actual purchase power of your money is Rs. 950 only. In such a case, you can invest the Rs. 1000 today at the rate of 7%, and can get Rs. 1070 after a year to beat inflation.

How Inflation and Time Value of Money impacts your finances?

The fact that inflation reduces the purchasing power of Rupees over time has very significant impact on your savings.

Suppose, a post graduate degree costs Rs. 2,00,000 today. You are planning for your daughter's education, and want to save for it today when she is 10 years old. She would need the money after around 11 years.

How much should you plan to have at that time?

Rs. 2,00,000? No! It is not enough to save that much, because this amount would have lost considerable purchasing power in all those years.

You would need to have a lot more at that time, because due to inflation, the same service (post graduate education) would cost a lot more at that time.

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PART II: INCOME, EXPENDITURES & SAVINGS

1. Income Expenditure Ratio

This ratio is an important budgeting tool, but there is not a specific percentage that is ideal for every single family. That does not mean that you can not determine what ratio is best for your family, just that you will have to look at all of your budget factors, amounts, and columns to arrive at this ideal number for your unique family. Ideally all households would only spend between fifty to seventy five percent of income on expenditures, and the balance would be used for savings, but this is often not possible. First you need to make a list of all the income your family has each month, as well as a list of all the expenditures that are paid out every month.

Once you have the total income and expenditure amounts for your family you can determine your income expenditure ratio. This is done by dividing your income amount by your expenditure amount. The resulting number should be as high as possible. There are some special circumstances that can cause you to get a very low ratio percentage through no fault of your own. If you have special considerations, such as a chronically or terminally ill family member, a child in college, or other extenuating circumstances you may find your percentages greatly lowered. In these cases there is probably not a lot you can do except hope they get better in time.

A good income expenditure ratio is between 1.25 and 1.50, because this means roughly one fifth of your income is not going out, but getting saved instead. If you have a ratio that is just one this means all of the income you have coming in for the month is going back out, leaving nothing for your savings. This can result in not having an adequate savings amount built up, so that if you experience a job loss or other financial difficulties you may not have the resources you need.

A fantastic income expenditure ratio will be between 1.5 and 2, or even higher. This means that you are only spending about half of your income or even less each month, and in these circumstances you can really watch your savings grow very quickly. There may not be a perfect number that is ideal for any family, but you can use this ratio as a tool to help you budget more effectively, and provide for your family in the best way possible. This ratio is just one of the many tools you can use to increase your savings and keep your expenses as low as possible. Just like any budget tool, using this ratio will only work if you use it properly. When you see your income and expense ratio it can be an eye opener, and force you to really look at your financial health.

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2. Passive Income

The basic idea of passive income is that it is money received with little or no effort required to maintain the flow of income once the initial work has been done. Some common examples of passive income are:

- Rent from real estate properties
- Royalties from books, songs, publications, or other original works
- Profits from businesses in which you have little or no day-to-day role or responsibility
- Dividends from stocks, REITs, equity mutual funds, or other equity securities
- Interest from owning bonds, certificates of deposit, other cash and cash equivalents
- Pensions

Why You Should Prefer Passive Income to Active Income

Passive income is attractive because it frees you to spend your time on the things you actually enjoy. A highly successful doctor, lawyer, or publicist, for instance, cannot "inventory" their profits in the words of one well known author. If they want to earn the same amount of money and enjoy the same lifestyle next year (the year after that), they must continue to work the same number of hours at the same pay rate. Although such a career can provide a fantastic life, it requires far too much sacrifice unless you truly enjoy the daily grind of your chosen profession. Even worse, once you desire to retire, or find yourself unable to work any longer, your income will cease to exist unless you have some form of passive income. In the past, this was accomplished by employee participation in company-sponsored pension plans.

The Two Broad Types of Passive Income

There are two types of passive income and throughout your career, which ones you focus on will likely depend upon your current financial situation, talents, skills, and personality. The two categories of passive income are:

1. Passive income sources that require capital to start, maintain and grow
2. Passive income sources that do not require capital to start, maintain & grow

Those who choose to focus on the first category of passive income will need family money, funds from investors, or the nerve to borrow large sums by taking on debt to fund the purchase of assets. The easiest to understand is someone who takes out substantial bank loans to build an apartment building or buy rental houses. Although this can turn a very small amount of equity into a large cash flow stream, it is not without risk. When using borrowed money, the margin of safety is much smaller because you can't absorb the same degree of setback before defaulting and finding your balance sheet obliterated.

Another example of the first category of passive income is someone who has an ownership stake in an operating business such as a factory or furniture store and allows the business to issue debt to fund expansion.

Large investment portfolios also fall into this category of passive income. If owned Rs. 10,000,000 worth of blue chip stocks, you could reasonably expect dividends of Rs. 500,000 per year. Whether or not you spend your days playing golf, painting, or writing the great American novel, you would collect checks as those businesses paid out a portion of their earnings. The problem, of course, is that it takes the ten million to be in that position.

The second category of passive income - that is, passive income sources that do not require capital to start, maintain, and grow - are far better choices for those who want to start out on their own and build a fortune from nothing. They include assets you can create, such as a book, song, patent, trademark, Internet site, recurring commissions, or businesses that earn nearly infinite returns on equity such as a drop-ship ecommerce retailer that has little or no money tied up in operations but still earns profits for the owner.

The Path Most Often Taken to Passive Income

It seems that most common path to generating large passive income streams is to work at a primary job and use your actively earned income to buy assets that generate passive income on a regular basis.

The doctor or lawyer in our earlier example, for instance, could use his income to invest in a medical start-up or buy shares of medical companies he understands such as Johnson & Johnson.

Over time, the nature of compounding, rupee cost averaging, and reinvesting dividends will result in his portfolio generating substantial passive income. The downside is that it can take decades to achieve enough to truly improve your standard of living but it is still the surest way to wealth based on the historical performance of business ownership and stocks.

How to Grow Your Savings?

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Taxes and Passive Income

A major advantage of earning passive income is that it is often taxed more favorably than active income. That may seem unfair, but the idea is that it will give people an incentive to invest in assets that will grow the economy and create jobs.

A business owner that works in his company, for instance, would have to pay extra in self-employment payroll taxes compare to someone who merely had a passive interest in the same limited liability company who would pay only income taxes. In other words, the same income earned actively would be taxed at a higher rate than if it were earned passively.

3. Tips & Tricks to Save Money

Saving money is a basic concept of personal financial planning, and key to financial success. Yet many of us don't have a formal savings plan. Without such a plan, the chances of ever saving enough money to meet long-term financial goals or achieve financial security are very slim.

It seems simple. In order to save money, you need to have "extra" cash, right? This is a common misconception. Having a spending plan (budget), will help you create money for savings. Most of us, by setting spending goals, can manage to save regularly, so if you're tempted to hit your back button because you simply don't have enough money to have a formal savings plan, STOP! We will tell you the "secrets" to savings.

First, set a few short-term and long-term financial goals to work towards, like a down payment on a car or home. Include the rupee amount and a time frame for achieving the goal. It's much more motivating to save when you know what you're saving for. And remember, a goal that isn't written down is only a dream.

Set up a separate savings account. If you mingle your savings with your regular checking account, you'll almost certainly dip into your savings and may never pay them back. Having your savings in a separate account is a constant reminder that these funds are earmarked for your future, and watching the balance grow is not only rewarding and motivating - it's downright exciting!

If you don't already have a written budget that includes tracking your expenditures each month, begin one now. Whether you make thousands of rupees or hundreds of thousands of rupees a year, you need a budget. Budgeting can be relatively simple and entirely guilt-free.

Decide on a percentage of your gross income to designate as savings. 10% is a good starting point, but if you've developed a budget and have analyzed your spending and you honestly can't find a way to set aside 10% for your future, then start out with 8%, or 5%, or whatever you're able to do with perhaps a little bit of discomfort but without great sacrifice.

If possible, have your employer or your spouse's employer deduct a set amount from your paycheck each pay period and deposit it into your savings account automatically. The old adage "out of sight, out of mind" works well here. Having to transfer money to your savings account is a little like giving someone who is trying to quit smoking a cigarette to carry around in his pocket and expecting him not to light up. Why tempt yourself? Make it easy and increase your chances of success with automatic deposits or transfers.

Whenever unexpected money comes your way, put all or most of it into your savings account. Bonuses, salary increases, tax refunds, rebates, overtime pay, income from hobbies or yard sales and other windfalls can pump up your savings account nicely without requiring additional cutbacks.

If you're forced to dip into your savings for an emergency, consider it a loan which must be paid back in a reasonable period of time, and set up a repayment schedule.

That's all there is to it! The "secret" is that there's no magic involved. The key is to start now and stick to it.

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4. Saving Strategies

It can be tough to increase our personal and family commitment to building our savings. It requires some very real discipline and careful budgeting to make it happen. Here are some tips and tricks to increasing our savings and getting our family finances better under control.

Create and live within a budget

The most important technique to find money to put into a savings account is to develop a realistic and manageable family budget. Start with a good estimate of your family income for each pay period, and then plug in your critical needs like housing, food, and utilities. With what's left, pay other bills and then make sure part of goes into savings. Without a budget, you may spend money on things you just want but don't need, sacrificing your savings.

Pay off consumer debt

Develop a family and personal debt elimination plan. Getting rid of high interest rate debt will open the door to putting the money you would have spent on interest into the savings account.

Plan ahead for grocery shopping

Living within your grocery budget is easier when you plan ahead. Make a comprehensive list of what you need to get through the next period of time, and then stick to it. Buy store brands rather than name brands for extra savings. Any money you spend at the grocery store that is less than what you budgeted can get transferred painlessly to your savings account.

Take advantage of employer programs

Many employers have a matching program for employees who save. For example, if you put 4% of your income into a provident fund, your employer might match it at the same rate or less. Don't let your employer's money for that match go to waste because you don't participate.

Use coupons, rewards and bargains

A little careful planning will help save money on the things you would otherwise buy at full price. You can find some great bargains always available in the market.

These good ideas will help you and your family finds ways to spend less, save more, and build your family's financial stability.

PART III: SAVING & INVESTING

1. Difference between Saving and Investing

In simple economies, there is little distinction between savings and investments.

One saves by reducing present consumption, while he invests in the hope of increasing future consumption.

Therefore, a fisherman who spares a fish for the next catch reduces his present consumption in the hope of increasing it in the future.

Most of the people probably have savings accounts with ATMs to access their hard-earned cash and be able to store away any extra cash in a place a little safer than a mattress. A few of you may even have some stocks or bonds.

Let us explain why while a savings account in the bank may seem like a safer place than the mattress to store your money, in the long-term it is a losing proposition.

If you open a savings account at the bank, they will pay you interest on your savings. So you think that your savings are guaranteed to grow and that makes you feel extremely good. But wait until you see what inflation will do to your investment in the long-term.

The bank may pay you 5 percent interest a year on your money, if inflation is at 4 percent though, your investment is only growing at a mere 1 percent annually.

Saving and investing are often used interchangeably, but they are quite different.

Saving:

Saving is storing money safely, such as in a bank or money market account, for short-term needs such as upcoming expenses or emergencies.

Typically, you earn a low, fixed rate of return and can withdraw your money easily.

Investing:

Investing is taking a risk with a portion of your savings such as by buying stocks or bonds, in hopes of realizing higher long-term returns.

Unlike bank savings, stocks and bonds over the long term have returned enough to outpace inflation, but they also decline in value from time to time.

The rate of returns and risk for savings are often lower than for other forms of investment.

Return is the income from an investment & Risk is the uncertainty that you will receive an expected return and preservation of capital.

Savings are also usually more liquid. That is, you may quickly and easily convert your investment to cash. The decision about which investment to choose is influenced by factors such as yield, risk, and liquidity.

Investments may produce current income while you own the investment through the payment of interest, dividends or rent payments.

When you sell an investment for more than its purchase price, the profit is known as a capital gain, also called growth or capital appreciation.

How to Grow Your Savings?

2. Understanding Your Assets

Whatever its complexity, an economy stands or falls upon very basic foundation stones. Individuals must be free to think and act on their decisions.

They must be able to gain the rewards of being right and must bear the cost of being wrong.

They must be able to concentrate on what they do best, and what they most enjoy doing, instead of spending their time providing for their immediate wants.

They must be able to make provision for the future by preserving a portion of what they have produced.

In short, they must think, they must produce and they must save. And to do that to the greatest and most efficient extent possible, they must trade with each other.

A person alone in nature can certainly think, act, and gain the rewards of being right or bear the cost of being wrong. He can also, by means of great effort, put aside savings, but only for a limited period of time. Indeed, anyone alone in nature has no choice but to do these things, if he is to survive at all!

In our advanced economy, physical survival is not often an issue. The extent to which individuals can think, work, produce and trade freely determines the potential of the economy. The confidence with which individuals can save and invest long term determines the prosperity of the economy.

To save, invest, and plan for the long term is a luxury not granted to anyone alone in nature. It is the exclusive preserve of those living in an advanced economy.

The evolution of any civilized society is dependent on the discovery of the idea of money, and on the discovery of something that can be used as money. The future of any civilized society is dependent on the quality of what can or is used as money.

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3. Investing in Different Asset Class

Money can also be described as an asset. Assets not immediately consumed can be turned into investments.

Investments are falling into one of two following main categories:

1. Real &
2. Financial

Real assets, also known as tangible assets, may be broken down into three groups:

1. Real Estate
2. Commodities, such as gold and silver &
3. Collectibles, like art, stamps, coins etc.

In part due to their finite supply or unique characteristics, real assets normally show the best appreciation when inflation is high.

Financial assets, sometimes referred to as intangibles, are separated into 3 areas:

1. Stocks
2. Bonds &
3. Cash

Each category has its own risk and reward characteristics.

A stock represents an ownership stake in a company and provides the stockholder with a slice of the company's profits.

A bond reflects a loan made by an investor to either a government or a corporation. To compensate the investor for making a loan, the borrower agrees to pay back the principal sum of the loan plus interest payments on the principal.

The third component of the financial asset menu is cash, though this does not equate with the paper stuff in your pocket. In the investment world, cash is lingo for an asset that is virtually risk free, such as a bank certificate of deposit.

Stocks are used to build wealth due to their capital appreciation potential, while bonds offer income, and cash is valued for its safe-haven characteristics.

4. Pay off your Debt or Invest

Maybe it was the financial planner on CNBC, a casual conversation with a friend, or just the small voice inside, but something has caused you to keep asking yourself the same thing: should I pay off my debt or start investing? This question, perhaps more than any other, has plagued investors for generations. Ironically, it is one that can be easily decided by using a bit of simple math.

Whether it's a mortgage, home loan, car loan, student loan, credit card, or medical bills, you probably have some amount of debt in your life. It is only natural that you want to pay it off as soon as possible. On the other hand, it is understandable that you want to start putting money away for your retirement or your daughter marriage or some other important milestone in your life. Since there is only so much cash to go around, a decision normally has to be made between the two, neither of which leaves a person feeling completely satisfied.

What should you do? The answer depends on two variables:

1. The rate of after-tax interest you are paying on your debt
2. The after-tax rate of return you expect to earn on your investments

Before you answer the first question, you must understand that there are two different kinds of debt. On one end of the spectrum is high-interest credit card debt that originates from things such as credit cards and department store charge accounts. This type is the deadliest and generally should be avoided unless absolutely necessary. The second type of debt is the lower interest variety; your mortgage, student loans, etc. Often, the interest on these types is partially or wholly tax-deductible, making it even more attractive.

With that in mind, the answer to the debt reduction vs. investing problem can be solved with this one statement: If you can earn a higher after-tax return on your investments than the after-tax interest rate expense on your debt, you should invest. Otherwise, you should pay off your balance.

Example of debt reduction Vs investing calculation:

Scenario 1

Assume you have a thirty year, Rs 15,00,000 mortgage with a six percent rate. Also assume you are in the 30% tax bracket. Due to the itemized deduction of mortgage interest, your after tax annual percentage rate is really 4.02% (not the 6.00% you are paying). Hence, if you expect to earn an after-tax return higher than 4.02% on your investments (odds are substantial you will if you have a long-term horizon), then you should invest.

Scenario 2

You have a Rs 10,000 balance on a credit card with a 22% annual percentage rate. Credit card interest expense is not tax deductible, meaning you should only invest if you think you can earn a 22% after tax return on your investments. Given that the historical long-term return on equities has been somewhere around 11-12%, this seems highly unlikely. In this case, it would be foolish to invest.

The Bottom Line

Although you may be eager to invest, you need to do what is best for your bottom line. Regardless of which is the wiser course of action at this stage in your life, the ultimate goal should be to have no debt and an abundance of great, lucrative investments. With enough patience and hard work, this is a goal that you can, and will, attain.

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5. Power of Compounding

Compounding is a mathematical phenomenon that basically means the longer you stay invested - and reinvest your earnings - the faster your money will grow!

Therefore, the two important keys to taking advantage of the power of compound interest are:

1. Leaving your money invested in the markets for the long run &
2. Reinvesting your income and gains.

Most of us would like to have a million rupee cash at some point in our life. Most of us also work 40+ hours a week at our job. What little amount we save can and will accumulate over the years, but the odds of reaching the 1 million mark is relatively small.

However, if we take advantage of the power of compound interest, then we can begin realizing our 1 million goal.

For instance, let's say you decide to invest 100 per month in an investment that yields 6% interest compounded monthly, for the next 30 years.

In 30 years, you would have 100,451.50!

That's not too bad, considering you made 64,451.50 in interest.

Now, let's say you kept that up another 10 years

You would then have 199,149.06.

In 10 years, you almost double the value of your investment.

Understanding CAGR

CAGR stands for "Compound Annual Growth Rate"

It is the growth rate of a company expressed on an annualized basis. This also takes into consideration the effect of compounding. Let's look at an example to understand it better.

Say the sales of a company 4 years back was 100. Today, after 4 years, it is 200. A simple conclusion is that sales have increases by 100% in 4 years. But does it mean that it has increased by 25% each year?

That would not be correct, as simply dividing 100% by 4 doesn't take into consideration the compounding effect.

So, to find out the per year growth rate of a company, we use the compound interest formula.

*A = P * ((1 + r) ^ n)*

Where

A = Final Amount
P = Principal amount
r = Rate of interest, expressed in %
n = Number of years

In our example,

A = 200
P = 100
r = The annual growth rate (that we want to find out)
n = 4 years

From the above formula, we find out that r is around 19%.

How to interpret?

It means that the average growth of the company over these 4 years, taking into account the impact of compounding, is 19%.

In the first year, the company grew from 100 to 119. In the second year, it grew 119 to 142. In the third year, it grew by 19% from 142 to 168.5, and in the fourth year, it grew from 168.5 to 200.

This principle is very important to understand, because it is used at many places.

For example, it is looked at while examining at returns generated by mutual funds (MFs). Whenever one sees returns for more than 1 year, they are expressed in terms of CAGR. If they are not expressed in CAGR terms, the returns are not accurate!

How to Grow Your Savings?

CAGR should also be used while considering any investment. Just take the example of the Bhavishya Nirman Bonds issued by NABARD.

These have been issued at around Rs. 9750. The investment is for 10 years, after which the investor gets back Rs. 20000.

Thus, the return is Rs. 20000 – Rs. 9750 = Rs. 10250, or 105% in 10 years.

<u>Does this mean that the return is 10.5% per year?</u>

No! It has to be calculated using the CAGR formula, where:

A = 20000
P = 9250
r = Rate of return to be found out
n = 20 years,

Using the formula above, we find out that the rate is actually 7.5% per annum. Now, that's quite far from 10.5%.

How to Grow Your Savings?

6. Benefits of Long Term Investing

Like the fabled tortoise that beat the hare in the race, the investor who stays in for the long term is more likely to achieve his or her goals than the investor who chases "hot tips" for quick profits in the stock market.

Time is an investor's best friend (or worst enemy if you wait too long) because it gives compounding time to work its magic. Compounding is the mathematical process where interest on your money in turn earns interest and is added to your principal.

Consider the following four investors ages 25 – 55. Each invests Rs 2,000 per year and earns 8%.

At age 65:

The investor who started at age 25 has over Rs. 585,000
The investor who started at age 35 has just Rs. 250,000
The investor who started at age 45 has just Rs. 98,800
The investor who started at age 55 has just Rs. 30,700

The results are quite dramatic and, as you might expect, the youngest investor comes out the best. However, look at the difference starting 10 years sooner can make. The fewer years invested the more dramatic the difference with the next youngest age. The investor who starts at age 45 still earns over three times as much as the investor who starts at age 55. Of course, part of the difference is the 45-year-old investor has 10 years (Rs. 20,000) more to invest, but the rest of the difference is the power of compounding.

This may not be the most "real life" example, since we can't go back to age 25 and start over. Let's look at the power of long-term investing from a different goal. What will it take for each of these investors to accumulate Rs 750,000 at age 65, assuming they all earn 8% and ignoring inflation and taxes?

The investor who started at age 25 needs to invest Rs 213 per month
The investor who started at age 35 needs to invest Rs 500 per month
The investor who started at age 45 needs to invest Rs 1,650 per month
The investor who started at age 55 needs to invest Rs 4,072 per month

While all four investors reach the goal of Rs 750,000, it is obvious that the younger investors get a lot more "heavy lifting" from their investments. The lesson is clear: The earlier you start the less you have to invest to reach your goal.

Problems & Corrections

The examples above describe the mathematical advantage of starting early, however they don't represent a "real world" situation. It is highly unlikely that you could achieve a constant return of 8% over a long period. The reality is there will be times when your investments earn less and other times when you will lose money. There may also be times when you will earn more.

The investor with a long- term perspective can also correct for mistakes along the way. For example, that stock you thought was going to soar like an eagle turned out to be a turkey. If you have a long-term perspective, you can change investments that aren't working for other alternatives. However, if you will need the money from your investment in the near future (fewer than 5-7 years), a wrong investment can create real problems in meeting your goals.

Long-term investors, especially those who invest in a diversified portfolio, can ride out down markets like the one that began in March of 2000 without dramatically affecting his or her ability to reach their goals.

However, for the investor just starting out at age 55, a market downturn can be disastrous. There is no room for error with only 10 years left before retirement at age 65. The reality of investing is that the market will go up and the market will go down. Investors that begin early and stay in the market have a much better chance of riding out the bad times and capitalizing on the periods when the market is rising.

How to Grow Your Savings?

7. 10 Key Investing Mantra's

We spend a great deal of time explaining things to our clients as well as many other individuals that do not necessarily revolve directly around specific "investments". Over time we have seen that there are a number of issues that individuals should know and understand prior to making investing decisions. This is our list of the top 10.

i) Investing in a vacuum is never a good idea

Set and establish goals for your future and determine how those goals are influenced by the results of your investing. It is never wise to invest solely for the sake of "doing well" or "I want to retire comfortably". Goals such as these leave too much ambiguity and room for error. Your portfolio should reflect your goals (to retire at 55 with a specific income), risk tolerance (I feel comfortable with a -8% annual loss exposure) and time horizon (the kids start college in 10 years, I have 18 years until retirement). Think of it this way, you are on a journey. How do you know if you have arrived if you do not know where you are going?

ii) You have an advantage over the professionals

Professional money managers are usually always tied to beating "the market" month to month and quarter to quarter. They are judged solely by their performance and are therefore influenced to take more inherent risk in order to beat indexes and peers. The professionals also do not have the luxury of holding on (or buying more of) when a specific security starts to tank. You should have no such worries over performance measurement but can simply sit back, focused on the long-term, and wait it out.

*iii) Asset allocation is the most important part of investing**

Much more so than choosing the right security or being lucky enough to own the next Infosys, asset allocation determines over 91% of the total portfolio performance according to an Ibbotson study. A good, sound selection of asset classes mixed together will establish the framework of your portfolio performance over the long run.

** Asset Allocation cannot assure a profit nor protect against loss. Investments are subject to market risks including the potential loss of principal invested.*

iv) Investing is risky

No matter what you invest in there is an inherent level of risk associated with all investments. If you choose to be ultra conservative and invest in cash deposits then you are assuming inflationary and income generating risk. Investing in bonds can contain as much risk as stocks at times.

v) The higher the rate of return the higher the risk you assume

Earning a high level of return requires taking more risk, but taking more risk does not always equate to a higher return. It is a well-known fact that in order to achieve higher return rates you must assume a higher level of risk which can and typically does equate to losses within a portfolio greater than many investors are comfortable with accepting. However, just because a holding or portfolio is high risk it is not necessarily capable of generating high returns. In some cases something is considered "high risk" because it is unlikely to generate a moderate or high return.

vi) The Rule of 72

The rule of 72 is one of those rules of thumb for quick and basic calculation. Take the rate of return and divide it into 72. This will be the approximate amount of time it takes for the money to double at the specified rate of return. For example, if you assume a 12% rate of return and divide 72 by 12 then your money would double in 6 years. For those of you who wish your money to double every 3 or 4 years this should give you an idea of the level of return (and subsequent level of risk) you must achieve.

vii) Never allow the tax to eat returns of a portfolio or holding

Tax decisions absolutely have an impact on the overall return of a portfolio but allowing the tax issue to drive portfolio decisions can have detrimental results. Investors hold onto an asset much too long because of not wanting to pay capital gains on the sale of the asset. Instead they realized a much larger loss from movements within the particular asset when the price falls. Make sound investment decisions on logic and do not let the emotion of taxes drive you.

viii) Watch what you watch and read

Turn off the talking heads on TV and put down the latest investment periodical. These formats are informative if taken lightly and in the proper amount but they are more interested in selling subscriptions and driving ratings than they are about giving quality advice. The movements generated by the advice of those in the television and print media are not always the best for the investor. News only sells when it gets our attention and unfortunately that hardly ever equates to good news.

ix) Good well-established companies do not always make great stocks

It seems counterintuitive that a well-established, well-known company would not automatically make a great stock to hold. Good, even great companies can and do falter as well as the lesser-known companies. In fact many of the well established companies have a hard time growing beyond the boundaries in which they have typically always existed. Too much exposure to too many of these giants can have a less than stellar effect upon your portfolio.

x) This one could really be 2 in 1

Do not put more than 10% of your money in your companies stock or within any 1 individual stock. In addition, within any portfolio (look at the holdings in the aggregate and not strictly by account) make sure that you have any individual stock position limited to no more than 10% of your holdings. We all think that the stock we have loaded up on is a high flyer and because of their business model or sales or new product coming on the market it is bound to double in price. Every stock you purchase was from someone else who wanted out. Do not expose yourself to excessive risk with excessive positions.

As we have stated on a very frequent basis, and will continue to do so at every opportunity, investing is risking and should be approached with care. One should never avoid investing but should approach it with diligence and understanding. The lack of knowledge of basics is one of the biggest hurdles we see most investors struggle with in regards to what they are looking for and what they expect. Balance out expectations with reality and see how well they fit. Get a good understanding of investing basics, especially including the emotional side to investing and utilize sound logic and reasoning. Chasing returns on the up side or running away from them on the down side never accomplishes either race. Utilizing logic and emotional balance as well as good asset class selection and you should find a much better fit. You and your portfolio will be much better served and more comfortable as a result.

PART IV: FINANCIAL PLANNING

1. Financial Planning

Understanding Financial Planning

Financial Planning is a critical use in ensuring your Long-Term Financial Security in all possible ways, Indeed it's a roadmap to achieve Financial Freedom in different stages of your life like buying a Home / Car or planning a vacation abroad.

- *Emergency Money Planning*
- *Child's Education / Higher Education Planning*
- *Child's Marriage Planning*
- *Retirement Planning*
- *Passing the Created Wealth to the next Generation.*

There are some basic questions to answer for doing financial planning:

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

For a financial plan, you need to analyze your financial needs & goals here as mentioned above.

One should measure in terms of money that what resources one needs to meet these stages of different goals and also the time period to achieve these goals.

Finally, one has to write an action plan so that to fulfill the Plan what products are useful to buy and savings to be done or increase/decrease in future too.

Your Life - Your Goals

What financial goals should you be thinking about?

Anything you want to do in your life can usually be quantified in terms of the money that you will need to spend on the goal you wish to fulfill. All goals have a financial value attached to them. For instance, if you want to buy a Car, you can easily calculate whether it will cost you Rs. 4 lakhs or Rs. 12 lakhs.

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Some of the Financial Goals can be classified as:-

• Retirement Planning
• Education for children
• Children's Marriage
• Emergency Fund Planning
• Buying a house or a car of your own etc

Depending on person to person we all have priorities that which goal is having highest importance and for that what to start saving to meet those entire goal on time. Financial conditions should be built on solid foundations.

Once the basic needs are met one can start thinking about the goals for their changing lifestyle, this goals can be different from one to another as different people have different needs according to their lifestyle for them and their family so that it's extremely personal.

Examples of these goals can be:

• Buying an LCD television
• Big Vacation Abroad
• Creating your own Gym

Financial Planning is a peace of mind

Someone has rightly said: - If you have dreams, you need a financial plan!

It depends on how much effort you willing to put in for your financial plan, like in terms of Expenses, Income & Asset, and Liabilities too.

2. Managing Your Finances

Managing your finances involves a lot more than just investing or worse – just saving. Though many say they are saving, if you look closely, you will find that every individual spends more than he/she saves. But there are ways which help you manage your money.

Don't be ignorant when it comes to money:

Many people think that they cannot be affected by a crisis. This is not true. It is important that you understand your financial position and manage it in a manner that you can save and spend at the same time. People think it's difficult to understand financial jargon. You can always consult to a financial planner. He is the right source to go to, to help you get a better grip of your financial situation.

Take control:

As an individual, it is very important that you take personal control of your finances. If you feel that you are not spending your resources, take a look at your credit card bills. You will be able to see a distinct pattern as to where your money is going.

Set your goals and then plan:

Planning is important. But understanding the reason for the same is an important step to manage your money. Set your goals so that you know what you are working towards. If you feel that you have too many goals, segregate them into short term, medium term and long term goals with specific time period. This will help you make a plan as to how to reach those goals.

Educate your family members:

Education and information is the key. Preparation your finances is not just about an individual, it's a family matter. Educate your family members about the course of action that will be taken to manage your finances better.

Be open to options:

You may think that to have effective management of your finances, you will have to cut corners and give up on the smaller joys of life. This is not true. Make a plan in such a manner where you don't have to give up on your needs or face financial crisis. You can always diversify your investments so that you reap good returns over a period of time and still achieve your goals.

3. Making Your Own Investment Plan

"It is planning not gambling that produces profit and security!" - Marcus Aurelius (121 - 180)

Basic information about investing is one of the most powerful tools you can use to find success in the market.

Stock brokers are your link to information in the stock market. They will recommend whether to buy or sell shares, help you get the necessary information, develop your investment plan and check the performance of your holdings.

Always remember the following seven critical facts:

1. If investment success was easy, everyone would be wealthy!

2. Focus on the long term, trying to make a "fast buck" is the fastest way to lose money!

3. Understand and believe that your two major enemies are panic and greed!

4. Realize that, depending on personal attitudes, the market is always either "half-full" or "half-empty"!

5. Never invest on "tips!"

6. Nobody can see the future! And finally,

7. The rich rule over the poor and the borrower is the servant to the lender!

Make an investment plan with the help of the following ten basic rules, and do put it into action:

1. Determine the Kind of Investor You Are:
What are your goals for investing and how do you feel about risk?

2. Decide how You Will Allocate Your Investment Money:
What portion of your money will you invest in stocks, in bonds and in mutual funds? How much do you want to keep in liquid investments? Determine how much you need to invest, and how to make these allocations.

3. Select Your Investments:
Choose them cautiously and create a broadly diversified portfolio, so you can minimize and spread your risk over a variety of investments.

4. Follow up on Your Investment Plan:
Once you've launched your investment plan and you have your portfolio, make sure it continues to reflect your goals and keeps working its hardest for you.

5. Monitor the Progress of Your Investments:
Regularly review your portfolio to determine if the value of your investments is increasing. Compare your returns with similar investments and investigate all the facts.

6. Review Your Financial Circumstances and Objectives at Least Twice a Year:
By doing this, you can verify that your investment plan still meets your needs and pinpoint where, when and which changes may be necessary.

7. Make any Necessary Adjustments to Your Portfolio:
Relocate money among your investments to reflect any changes in your investing approach.

8. Patience Is a Virtue:
Invest for market returns year in and year out. Maintain the discipline to hold onto or add to investments through down markets as well as up markets.

9. Cash Is King:
Always keep sufficient funds on an "instant access account" to meet any sudden emergencies, e.g. repairs to your home, a sudden medical expense, or etc. This may be obvious to you but from our experience we can tell you that the number of people who fail to keep this simple rule is truly amazing.

10. And Above Everything Else:
Choose a stock advisor / financial planner you can trust, an investment planner with a proven reliability.

How to Grow Your Savings?

4. Your Investment Profile & Risk Tolerance

To get an idea of your investment profile, start by calculating your investment horizon.

Investment Horizon:

Investment horizon is the period of time, in years, that you wish to remain invested. Investment horizon may be measured as the point in time when you begin taking distributions, or it may be measured as the point in time when you expect to complete taking distributions.

This is the number of years that you can invest. Your investment horizon depends on your financial goal.

Financial Goal:

A financial goal is a goal that involves saving and investing to reach a specific amount by a specific date.

For example, a financial goal may be to save 2,00,000 for a college education fund for a child in 14 years, or it may be to save 30,00,000 for a retirement fund in 20 years.

You can achieve your financial goals through a combination of saving more, saving longer or earning a higher rate of return.

Your goal may be to save for college, retirement, or a down payment on a home. Each goal has its own investment horizon.

For example, saving for retirement at age 65 when you're 20 gives you an investment horizon of 45 years. The longer the investment horizon, the longer you can save and benefit from compounding.

Next, estimate your risk tolerance.

Your risk tolerance is your willingness to accept some volatility in the rate of return of your investments in exchange for a chance to earn a higher return.

If you expect a higher rate of return, you should be willing to accept a higher degree of risk. This is called the risk-return trade-off.

How to Grow Your Savings?

Risk-Return Trade-off:

A basic investing principle that says the higher the potential rate of return, the higher is the investment risk. Academic and industry studies support this relationship.

For example, stocks historically offer a higher rate of return than bonds. They also have a higher degree of investment risk. Investment risk is measured by the volatility of investment returns.

To get an idea of your risk tolerance, take a few minutes to complete the below risk tolerance quiz:

Question:	1 Points	2 Points	3 Points	4 Points
1. I plan on using the money I am investing:	Within 6 months.	Within the next 3 years.	Between 3 and 6 years.	No sooner than 7 years from now.
2. My investments make up this share of assets (excluding home):	More than 75%.	50% or more but less than 75%.	25% or more but less than 50%.	Less than 25%.
3. I expect my future income to:	Decrease	Remain the same or grow slowly.	Grow faster than the rate of inflation.	Grow quickly.
4. I have emergency savings:	No	--	Yes, but less than I'd like to have.	Yes
5. I would risk this share in exchange for the same probability of doubling my money:	Zero	50%.	25%.	10%.
6. I have invested in stocks and stock mutual funds:	--	Yes, but I was uneasy about it.	No, but I look forward to it.	Yes, and I was comfortable with it.
7. My most important investment goal is to:	Preserve my original investment.	Receive some growth and provide income.	Grow faster than inflation but still provide some income.	Grow as fast as possible. Income is not important today.

To get your own profile add the number of points for all seven questions

Add one point if you choose the first answer, two if you choose the second answer, three for the third and four points for the fourth question.

If you score between 25 and 28 points, consider yourself an aggressive investor.

Aggressive Investor: An aggressive investor is an investor who is willing to accept a higher degree of investment risk in exchange for a chance to earn a higher rate of return.

Investment risk is the volatility of investment returns. A basic investing principle states that a higher degree of investment risk is required to earn a potential higher rate of return.

If you score between 20 and 24 points, your risk tolerance is above average.
If you score between 15 and 19 points, consider yourself a moderate investor.

Moderate Investor: An investor who is willing to accept some investment risk in exchange for a chance to earn a higher rate of return. Investment risk is the volatility of investment returns.

A basic investing principle states that a higher degree of investment risk is required to earn a potential higher rate of return. On the risk-tolerance scale, a moderate investor is in between an aggressive and conservative investor.

This means you are willing to accept some risk in exchange for a potential higher rate of return.

If you score fewer than 15 points, consider yourself a conservative investor.

Conservative Investor: An investor who is unwilling to accept a higher degree of investment risk in exchange for a chance to earn a higher rate of return. Investment risk is the volatility of investment returns.

A basic investing principle states that a higher degree of investment risk is required to earn a potential higher rate of return.
If you have fewer than 10 points, you may consider yourself a very conservative investor.

This is only an example of a short quiz used by financial institutions to help you estimate your risk tolerance. For specific investment advice, you should always consult your financial adviser.

PART V: BUILDING AN EQUITY PORTFOLIO

1. Investing in Equities

Traditional investments like fixed deposits are good and safe and one must have a part of their savings invested in such risk free options. However, your portfolio is not complete and balanced in the absence of stock investments.

If invested wisely, you can minimize the risk of loss in stocks and increase the earning potential of your hard earned money.

Here are some statistics for you:

Nature of Investment	% Returns after 5 Years	% Returns after 10 Years
Real Estate	30%	13%
Gold	10%	7%
Bank FDs	8.50%	12.50%
Equity	35%	16%

As compared to fixed deposits, investments in equity will pay 26.5 percent higher returns in 5 years. Even for a longer term, investment in stocks pays higher returns even in comparison to real estate and gold.

To begin with, when you purchase equity in a company, you must ensure that the stock prices are reasonable. If you over pay for stocks of a company, naturally you will have to wait longer to make profits on them.

This is because, if you buy stocks at a time when the prices are soaring at unreasonable levels, you will have to face an immediate setback when the market comes to normal levels, and the stock price drops to its average range.

To understand if the stock price is reasonable, you have to understand how stock prices are determined. The price for a stock depends upon the demand for it amongst buyers. The base line of a stock price is its EPS (earnings per share).

The market price of a stock is generally a multiple of its EPS. The multiple depends upon the demand the stock fetches. Demand for the stock depends upon company's reputation, customer relations, financials, current news feeds, economic environment in general, political news, market sentiments etc.

If you are new to the stock market, it is best not to buy stocks when the market is influenced by a certain news feed as market sentiments prevail over logic at such times.

For example, the Sensex shot up in mid 2009 after the Congress led UPA Government was elected in the Parliament. Such price upheavals are temporary in nature.

A calm market is good for new investors. If you are looking at stocks as an investment it is best to hold stocks for long term. Further, one should invest in good companies with sound management.

Investing in stocks for the long term

If you invest in stock of good companies for the long term, say 5 years, you will most likely earn good returns on your investment. This is because, a good company with a stable history and excellent growth charts, will grow over time.

Its EPS will also move in a forward direction as the company grows. Over time the demand for the shares will also increase and so will the PE multiple. Therefore, your initial investment will multiply over time if you hold on to the stocks. Also, companies pay dividends and issues bonus shares. These factors add to returns.

Option of investing through mutual funds

If you are vary of investing in stocks or are confused about the company where you should put your money, the option of mutual funds may be right for you.

This way you can invest in stocks of different companies, though indirectly, and gain the benefits of the stock markets without having to research stocks, study the market etc. Fund houses have researchers and experts to study and analyze stocks.

You automatically have a diversified portfolio since mutual funds invest in multiple companies and different industries- this reduces the risk factor. Further you can make a modest beginning since most mutual funds are available for a small investment of Rs 5,000. You can start SIP (systematic investment plan) with as low as Rs. 500 a month.

2. Investing in Bull & Bear Markets

Are we in a bull market or a bear market and should you care?

The financial and popular media is fascinated with labeling markets as bulls or bears as if that somehow describes what is happening to your stocks.

It is true that market risk – the danger that a declining overall market may affect your stock – is real. However, investors who have done their homework know the difference between a general market decline and something wrong with their stock.

Some High and Some Low

Look at any bear market and even at its lowest point you will find stocks that do quite well. Similarly, in any bull market there are stocks that do poorly.

A rising or ebbing tide does not necessarily raise or lower all the stocks in a market.

When the overall market is declining or rising significantly, the intelligent investor has a real advantage over the person who has invested on a whim.

If you know the company behind the stock, you will be able to judge whether the stock's price decline is simply a reflection of the market's general pessimism or a signal that something is fundamentally wrong with the company.

Decisions

Armed with this knowledge, you can then decide whether to:

- Sit tight and let the market work through its problems
- Take advantage of the price decline and add to your holdings if you believe nothing has fundamentally changed with the company
- Sell before the loss becomes worse

Whatever your decision, you are armed with information to make an intelligent decision.

In a bull market, your stock may take off with the market, which is not necessarily a bad thing. However, you may be concerned that the stock will become highly overpriced and will suffer a significant drop when the bull market ends.

Options

Here are some options:

- You could sit tight and let the market work thorough it problems
- You could sell some of the shares (see example below) and buy back the stock when the price falls back to reasonable levels
- You could sell all of the shares for a profit

You can protect yourself from the danger that the bull market had overpriced the stock so badly that it might fall below its true value in a correction several ways.

Strategy

Here is one strategy. Say you own 500 shares that you bought at Rs. 25 per share. The bull market, and nothing else, has pushed the price up to Rs. 40 per share.
You want to hold the stock, but are concerned that a market correction might drop the price below Rs. 25 per share.

You sell 250 shares at Rs. 40 for a gross of Rs. 10,000. Assuming you have held the stock less than one year, capital gains tax takes 15%, leaving you Rs. 8,500, which you stick in a money market fund.

When the market correction comes, you buy back shares at a lower price. For example, say the stock fell to Rs. 20 per share. Your Rs. 8,500 profit will buy you 425 shares.

You now own 675 shares of the stock and have reduced your average cost from Rs. 25 per share to less than Rs. 22 per share and you didn't take a penny out of your pocket.

250 shares @ Rs. 25/share = Rs. 6,250

425 shares @ Rs. 20/share = Rs. 8,500

675 shares @ Rs. 21.85/share = Rs. 14,750

Whatever course of action or inaction you choose, the intelligent investor always works from a position of knowledge. If you know the company and its industry, you will not worry about whether it's bull or bear market.

How to Grow Your Savings?

3. Invest in Individual Stock or Mutual Fund

Many people just assume that mutual funds are the best way to save, but like most "conventional wisdom," it's often wrong.

Conventional wisdom will tell you to put your money in a mutual fund. Well, conventional wisdom does not apply in the stock market. Today, there are more mutual funds with various schemes than there are stocks to buy from the stock indices. A mutual fund can be your worst investment decision.

There is an enormous amount of money being put into mutual funds every year. These so-called "safe" investments have been consistently under performing the markets over the years.

That's right, when the market goes up 40%, your mutual fund probably returned 25%. What happens when the market goes down? And believe us, it does go down! If the market is down 20%, your fund will probably be down 30% and you lose both ways.

If there are almost more mutual funds than there are stocks, then how do you pick a mutual fund?

Do you need a mutual fund that helps you pick a mutual fund? Sounds silly, doesn't it? Guess what, they already exist. There are mutual funds that take your money and pick different mutual funds to invest in.

With all the free information available today, you're better off picking the stocks yourself. You would save yourself a lot of money.

You can dramatically reduce your investment expenses by cautiously selecting your individual stocks, and minimizing the number of your trades. The average mutual fund has fees and expenses of over 1.00% per year for the privilege of underperforming the market. Between 85% and 95% of mutual fund managers underperform the indices, depending on who's doing the counting.

One of the big advantages of mutual funds is diversification. Your mutual fund manager pools your money with thousands of other people and builds a portfolio containing hundreds of securities representing companies in dozens of industries.

Unfortunately, too much diversification isn't good for you. You don't need to hold hundreds of securities to be properly diversified. Increasing the number of securities held does reduce your risk, but the reduction becomes negligible once the portfolio reaches 20 or 25 securities, spread across several industries.

<u>If you need only 25 securities to be completely diversified, why is your fund manager holding 200 securities in your mutual fund?</u>

He can't buy enough stock in the companies he likes, so he has to add second and third rate issues to remain fully invested. Even if your mutual fund manager is a bona fide genius, it's unlikely he has more than 5 or 6 good investment ideas a year. You want your mutual fund manager's best ideas, not the 200 mediocre ones.

Once a mutual fund gets too large, the manager has to buy large capitalization stocks for liquidity. Also there are restrictions on how much of any one stock they can hold.

<u>So, how do you decide what stocks to buy?</u>

People have many different ways to pick stocks. Some people will only look at companies which have good earnings and sound fundamentals.

Others will look at the core of the business and determine if the products or services offered is better than it's competitors or they might only look at the charts of stocks and try to determine if the stock is going higher or lower.

Many might even not look at anything and just get in and get out of stocks in matter of seconds.

<u>Do you think that you don't have time to become an amateur securities analyst?</u>

In such a case stock picking answer is really simple:

Just listen to equity analysts and evaluate their stock research and investment ideas in terms of company background, past performance, management views, dividend payments & risk involvement. Check your risk factor and accordingly break up your stock investments by investing in Small, Mid & Large cap stocks.

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4. Creating a Stock Portfolio

A portfolio is a group of financial assets such as stocks and bonds, held by an investor. In today's financial marketplace, investors need to create well-structured portfolios that suit to their investment goals and strategies. There are investors who are risk-takers and investors who are risk-averse. Constructing a portfolio that reflects the investor's risk profile and tolerance is a key factor for effective investment decision making.

Clarifying current situation and future needs for capital, along with risk tolerance determines the asset allocation among different asset classes. Optimal asset allocation is an effective method of diversification. Investors should diversify between different classes of assets but also, within each class. This allows them to incur long-term investment growth, while their assets are protected from the risks of large declines and structural changes in the economy over time.

Another important factor to be considered when constructing a portfolio is the stock volatility. Typically, market fluctuations are subject to interest rates changes, inflation, political turbulence, corporate news etc. Investors should keep an eye both on current developments and broader socio-economic environment and on historical data as these reflect a stock's past performance and assist to a fairly accurate assessment of future performance.

Financial ratios are also important when constructing a portfolio. Price/earnings (P/E), Book value (BV), return on equity (ROE) and total return indicators are highly important tools to assess liquidity, profitability, leverage, capital structure, and interest coverage. Although ratios reflect historical data and past performance, they can also predict future potential and provide lead indications of potential trouble areas.

Optimal portfolios provide the highest possible return for any specified degree of risk. To that end, they need to be revaluated on a regular basis in order to reflect new market realities. Investments should be regularly analyzed and investors should perform reallocation of their portfolio if required.

Finally, investing at regular intervals is a good method to build wealth. Both, risk-takers and risk-adverse investors can smooth out market fluctuations, through rupee-cost averaging that is investing a fixed amount on a regular schedule. This fixed amount automatically buys more shares when prices are low. Consequently, the average purchase price of the stock is lower than the average of the market prices over the same length of time.

Although, Rupee-cost averaging does not automatically produce a profit, still by investing on a regular schedule virtually guarantees to do better in a generally rising market than investors who try to time market highs and lows.

Retails investors often trade in stocks without understanding the deeper implications of their buy or sell decisions. When you invest in stocks, you implicitly are building a stock portfolio.

Here is a set of actionable steps that you must keep in mind to help you with building your stock portfolio.

1. Diversify:

Just buying stocks in 1 or 2 companies is not enough. You could be taking on too much risk through a concentrated portfolio, akin to putting all your eggs in one basket. Ideally, your portfolio should have no more than 20-25 names to give you the benefits of diversification.

However, this also does not mean that you can have just say 5 shares of one company and 2 shares of another, because that is all you can afford because you can't create wealth through just purchasing a handful of shares in a company.

Good stock picking is about knowing how to allocate your capital efficiently across your best ideas in a diverse portfolio.

2. Review Your Exposure Frequently:

While one investment strategy is to buy and hold, that does not imply that you do not manage your exposure by ignoring your portfolio. Market prices move, sometimes dramatically.

As a result, you might have too much or too little exposure to one sector or stock. Avoid this by being disciplined about setting aside some time to review your exposure. This will help you understand if you need to trim or add to the exposure to a certain sector or stock in your portfolio and take care of risk management.

3. Create your own set of rules to guide you:

Formulate your own rules for when to buy or sell a stock based on an investment philosophy that you can be disciplined about. Don't just follow the herd or come under peer pressure.

What is good for others might not be suitable for you or your portfolio because your risk, investment criteria, tax situation and entry price might be different. If a stock has met your price target, have some rules that guide you whether you will take money off the table or stay invested.

If a stock is a constant underperformer, will you continue holding on to it because psychologically you are unwilling to admit that you made a poor decision, or will you be unemotional and make the rational decision to cut your losses and sell?

4. Keep some cash available:

This is one area where the professional investors stand out. They recognize that good investment opportunities come unannounced, but in order to take advantage of them they need to have cash available to make these investments.

So make sure that you keep some cash available in your portfolio to pounce on these ideas. If you are fully invested, you might miss good opportunities due to lack of liquidity.

If the above sounds challenging and tough for you to follow, then a do-it-yourself portfolio management is not recommended. As an alternative you might be better invest in the stock markets based on equity advisor services with stock specific research and recommendations or you can invest through mutual funds, where you can take advantage of the resources and risk management skills of the professionals, rather than compete against them.

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5. Investment Portfolio Mistakes to Avoid

Are you a truly expert investor as you really believe?

Do you consider yourself as a well-informed investor who is capable of anticipating and avoiding the majority of the risks that are usually associated with investing?

Chances are, you are making many common errors that are costing you a lot of money and may even harm your financial independence and security.

Below you can find the two most costly errors investors make with their investment portfolios:

1. Asset Classes and Subclasses

How you allocate your portfolio, rather than which investments you select or when you buy or sell them, determines the majority of your investment performance over time.

The solution is to allocate your portfolio to many asset classes and subclasses and be careful not to over or under weight any asset class.

Do not mistakenly believe that a properly diversified portfolio is a properly allocated portfolio. Properly allocate your portfolio among the different asset classes first and then diversify the investments within each asset class.

Diversification is the cornerstone of asset allocation and is the key to reducing risk, namely company-specific risk. To properly diversify, you should hold sufficient quantities of not-too-similar securities with comparable risk and return trade-off profiles.

2. Inflation

Inflation can destroy the real value of your portfolio over time, thus placing your future financial security at risk.

As a general rule, the longer your investment time horizon, the more you should allocate to equity investments. For shorter investment time horizons, emphasize fixed-income and cash and equivalent investments.

By avoiding these two mistakes, besides other investing mistakes, you will be able to design an investment portfolio that will provide the best opportunity to achieve and protect your financial independence and security.

6. Importance of Stock Diversification

Stock Diversification means buying stock in a range of different industries.

On the face of it, diversification ought to be simple: You don't put all your investing eggs in one basket because if you drop it, all the eggs will break!

But it's not that easy. Suppose you don't invest all your available capital in one stock. Suppose you buy two. Are two baskets enough? And which eggs go in which baskets?

No, not so simple indeed. But it's important to figure out because diversification allows investors to reduce risk in their portfolios without giving up any return.

The idea is that, because you cannot possibly know which stocks will perform better or worse than average, you cannot afford to put all your money into one company, or even in companies within a single industry.

You have to spread the risk and the opportunity.

Diversification of investment holdings is the most important shield against risk. Because some investments rise in value while others fall, diversification smoothes out much of the volatility of the overall return from a portfolio. Diversification sacrifices some of the upside potential, but this should be more than offset by the benefits of a lower level of risk.

The trade-off for the balancing of risk and return in a diversified portfolio is that your overall return might be somewhat lower than you could get in an undiversified portfolio. However, along the way, a diversified portfolio will have less volatility, and steadier returns.

The Point is: *Don't put all of your eggs in one basket.*

Only by diversifying you will be able to realize your average return objective with lower risk. The right level of diversification for you at a given time depends on a variety of factors, including where you are financially, what your goals are, and what the market is doing.

Though literally everyone talks about diversification for their investment portfolio, very few understand the true statistical data underlying the definition. As a result, the majority of portfolios are not properly diversified and an extended risk is being taken, unquestionably unwittingly, but nonetheless evident, by most investors.

In order to cope with the above problem, you have to understand the following:

1. Systematic Risk: This is a risk due to the movement of the market itself. The benchmark could be any Index. If you have one or a few investments in a given area, you could compare its return to that of the benchmark index to determine how well it is doing.

2. Unsystematic Risk: This is the risk of a single company causing a significant move, either up or down. This is usually the risk that most investors would want to eliminate, unless they are "true risk takers!" This risk may be tempered and in fact virtually eliminated, by the purchase of an increased number of stocks.

3. Time Risk: It is usually known that the longer one holds an investment, the less the overall risk. It means that sometimes if you have a risky stock, risk would lower the longer the stock was held.

Proper diversification is the foremost issue in all efficient investments, especially where individual stocks are purchased. It is impossible to properly judge a portfolio if the risk factor is missing. And even if you do understand your holdings, it is mandatory that you must "know your self", and therefore have detailed knowledge of all your investment assets in order to be able to determine the proper diversification and risk.

The importance of Professional Investment Guidance, regardless the performance of the market, cannot be overstated. A qualified financial consultant can assist you with portfolio review and to discuss strategies for achieving your financial goals.

By understanding the basics of investing, working with a professional to design an appropriate portfolio, and allowing your investments time to grow, you can invest successfully.

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7. Investing for Growth, Yield & Income

You've probably been listening all over about the fortunes being made in the stock market. With enough patience and a lot of discipline, you are almost guaranteed to make a considerable amount of money in the markets.

You merely need a willingness to put your savings to work in a balanced portfolio of securities tailored to your age and circumstances.

But you do have to understand how investing works. Investing is not about throwing all your money into the XYZ stock hoping to make a killing. Investing has nothing to do with getting a stock tip from your brother-in-law! Investing isn't gambling or speculation.

Investing is taking reasonable risks to earn steady rewards.

Investing works because it allows you to participate in the relentless growth of the world's economy, this hardly follows a straight line, but does trend upward over time. It's also true that the longer you stay invested, the faster your money will grow.

When you are determining your investment strategy you will always have to consider the following three elements:

1. Growth:

Growth is the rate at which your money appreciates during the time it is invested.

If you think you will need access to your funds sooner rather than later, look for an investment that provides a fairly safe and steady growth rate.

Long-term investments that are influenced by factors such as the inflation rate may lose money in the short term, but they can still grow over long-term. What will matter is not a slow growth rate (or even a loss) during a particular period, but a higher growth rate over time.

2. Yield:

Yield is the interest or dividends paid on your investment. Like growth, it can vary in importance depending on your needs.

If you are retired and your investment is funding your retirement, your investments should generate enough yield to let you live on the interest.

Savings accounts tend to yield small percentages. Stocks can yield the highest percentages but also have the greatest risk.

3. Income:

Income is closely related to yield. Does your investment or the yield from your investment, make up a significant portion of your income.

If so, you may want to be more conservative with your investment choices to ensure that the amount of yield it produces remains consistent and reliable.

You should give careful consideration to where and how often you want to reinvest your money, as it could affect your financial security.

8. Facts & Benefits of Investing in Small Companies

For a stock market investor, it is financial information of the company which guides him whether he should buy or sell the company's stock. For a small or micro cap stock, this information is sometimes not available since some micro cap companies do not even file their financial reports to stock exchanges. Therefore, it is hard to evaluate a micro cap company using normal technical analysis methods.

What is a micro cap stock?

A micro cap company is a company having low or micro market capitalization. The term micro-cap stock (also micro-cap) is used to describe publicly traded companies which have a market capitalization of roughly Rs. 1000 million (100 crore) or less. Micro cap stocks are usually not able to satisfy the eligibility criteria of being listed on major exchanges.

Micro-cap companies are known for their volatility and many such companies are involved in fraud. Since the institutional investors are rarely involved in these stocks, the stock price can be manipulated by the investors. Even though these stocks come in high risk category, investors can't turn their eyes away from them since these can be highly profitable as well. These stocks have given higher returns than large cap stocks since last 10 years. This is the reason there are a few indices specially create t track the performance of micro cap stocks globally. Some of these indices are Russell Micro-cap Index, the Dow Jones Select Micro-cap Indexes, and the Dow Jones Wilshire U.S. Micro-Cap Index.

In India, BSE Small Cap is a well known index. Its good to point out that most of the fortune investors invested in micro cap stocks in early stage of their lives; hence a small pie of your portfolio could be of micro cap stocks, which can have the potential to change your fortune in years to come.

Value investor Warren Buffett also falls in the inefficiency camp, claiming that individual investors should be able to earn 50% annual returns with small amounts of money because they have access to high-return small-cap stocks that he can no longer buy because of Berkshire's huge asset size.

Facts about Small Cap Companies

1. If you want outsized returns, you must invest in small-cap value stocks.

2. All ten of the top-performing stocks of the past decade were small caps and most

were value stocks. We can almost guarantee that the top-performing stocks of the next decade will be small caps as well.

3. Most small caps underperform, so the key is either finding the few small caps that will produce the 50, 60, and 70-baggers, or instead buying the entire small-cap universe to insure that you won't miss out on the big winners.

4. Small caps have above-average volatility and can underperform for long periods, so their outsized returns may require a long timeframe to be realized.

5. Whether small caps are inherently more risky or just inefficiently priced is undecided, but investment prudence dictates that you normally limit your small cap allocation to less than half (some say 35%) of your total equity portfolio and avoid them altogether during incipient periods of severe economic distress.

Benefits of Investing in Small Cap Stocks

A small cap stock, or micro-cap stock, is a stock with a pretty small amount of market share. Most companies differ on their opinions of this, but many firms say that means it is between Rs. 250 million and Rs. 2 billion in market capitalization. Many people see this as an extreme opportunity.

1. Mutual funds often have restrictions on what they can purchase to include in their funds, because if a company is smaller, they would have to purchase a large percentage of available shares to put an adequate amount of that stock into their fund.

2. Small cap stocks are extremely valuable; as they are typically the most sought after for acquisition purposes and have high value potential in the future. The trick is, deciding which small cap stocks are the best for your individual portfolio.
3. There are often many undervalued micro-cap stocks available for purchase, and if you invest at the right time, you may be able to make a great deal of money on something that may have not been well predicted.

4. To find the best micro-cap stocks to invest in, you can contact an investment professional who can walk you through their picks. They will of course charge you a commission percentage off of your earning. You can also contact larger brokerage houses to set up a brokerage account, many of which charge per trade as opposed to on a commission basis.

5. The best small cap stocks to invest in are ones that are about to make a large announcement, purchase another company to acquire, or offer a new product that will be important to the marketplace. Health care and technology stocks often fall

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into this category. Many restaurants often wind up in micro-cap stock recommendations, if they are planning on expanding in a large way or offering new menu items.

Because the best small cap stocks recommendations will always be changing, it is important to get up to date research on advice, either by contacting a professional or doing your own research.

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PART VI: EQUITIES & RISKS

1. Investing Risks Vs Rewards

Before you can begin to build a successful investment portfolio, you should understand the basic elements of investing and how they can affect the potential value of your investments over the years.

When you invest, there is no guarantee that you will end up with more money when you withdraw your investment than you put in to begin with, and that's a very scary prospect. Loss of value in your investment is what is considered risk in investing.

Even so, the opportunity for investment growth that is possible through investments far exceeds that concern for most investors.

Consider why

At the cornerstone of investing is the basic principal that the greater the risk you take, the greater the potential reward. You get paid a higher return only when you're willing to accept more volatility. Risk then, refers to the volatility.

Volatility is the up and down activity in the markets and individual issues that occurs constantly over time. This volatility can be caused by a number of factors such as interest rate changes, inflation or general economic conditions.

It is this variability, uncertainty and potential for loss, that causes investors to worry. We all fear the possibility that a stock or bond we invest in will fall substantially. But it is this very volatility in stocks, bonds and their markets that is the exact reason that you can expect to earn a higher long-term return from these investments than you can from CDs and savings accounts.

Different types of investments have different levels of volatility or potential price changes, and those with the greater chance of losing value are also the investments that can produce the greater returns for you over time.

So risk has two sides:

A. It causes the value of your investments to fluctuate, but
B. It is precisely the reason you can expect to earn higher returns.

You might find it helpful to always remember that all financial investments will fluctuate.

There are very few perfectly "safe havens" and those simply don't pay enough to beat inflation over the long run.

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2. Understanding Stock Market Risks

"Take a chance! All life is a chance. The man who goes the furthest is generally the one who is willing to do and dare. The 'sure thing' boat never gets far from shore." - Dale Carnegie (1888 – 1955)

In 1998 Economics Professor and Nobel Prize winner Paul Samuelson (1915 - 2009) noted that: "Many people now believe that if they simply hold stocks long enough they will not, lose money for statistics have shown that since 1926 the U.S. equity market has not suffered a loss in any given 15 year."

He called it a fallacy, and conceded that it is truly likely that if you hold stocks over long periods of time that they would tend to produce returns higher than other assets. But to believe that it is a God given statement is simply not correct.

Investing and stock market risks do not go to zero over long periods, but there are many articles that reflect how risk goes down the longer the time period. What is seldom introduced is the fact that if there is a significant onetime loss, it can be monumentally overwhelming.

In any case, Samuelson noted that: "The problem is that when stock prices do turn down (as inevitably happens even in the strongest of bull markets) your optimistic equity exposure can overwhelm your gut level risk tolerance, leading to poor short-term judgments and even outright panic"

Risk is a complex, multidimensional concept that manifests itself in various ways. Risk is omnipresent and includes stock market crashes, corporate bankruptcies, currency devaluations, changes in sentiment, in inflation and interest rates, and even major changes in the tax code.

Risk is generally defined as return volatility, or the degree of ups and downs of returns. But there's more to risk than volatility. Risk and long-term reward are generally related. Risk is the chance that your actual return will be less than you expected.

People sometimes think that a good return can be achieved with little or no risk. Unfortunately, that's impossible. To achieve your objectives, you need to assume certain risks and avoid others. Your ability to handle risk is related closely to your individual circumstances, including your age, time horizon, liquidity needs, portfolio size, income, investment knowledge, and attitude toward price fluctuations.

What's highly risky to one individual may be no problem to another. Short-term fluctuations are not that relevant for long-term investors who have the discipline, patience, and understanding to deal with them. Stock funds are actually less risky than money market funds for those with long time horizons.

Well-informed investors are far less likely to let risk get the best of them. Those who understand the various elements of risk are better equipped to enjoy a profitable long-term investment journey.

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3. Different Type of Investing Risks in Equities

1. Market Risk:

Corrections and bear markets inflict harm on countless individuals. In a classic correction, the broad market averages lose 10% to 20% of their value, whereas they plunge 20% to 35%, or more, in a real bear market. Some equity funds get hit worse than others in a bear market condition.

In addition to short-term risk, there's always a small chance that stocks can do poorly for about a decade introducing a long-term danger.

2. Interest-Rate Risk:

This peril confronts investors directly, especially those in longer-term portfolios. Simply put prices fall when interest rates rise.

If interest rates rise significantly, fixed-income securities become relatively more attractive, so money is shuttled from the stock market into higher-yielding bond and money market funds.

3. Currency Risk:

If your country's currency grows stronger, you will experience a currency loss on your foreign securities. Conversely, if your currency weakens, you will enjoy a bonus.

Fluctuating exchange rates are of particular concern to single-country investors. It can be devastating for individuals who hold funds for short periods.

Some fund managers may try to hedge their portfolios against adverse currency moves with currency futures or forward contracts. However, hedgers are fallible and lose money when the currency goes opposite their predictions.

In addition, a hedge costs money. Currency risk is generally not too much of a problem for long-term investors in well-diversified international funds.

4. Asset-Class Risk:

Stocks, bonds, and cash are the three major asset classes. If you allocate a disproportionate amount to any of the three main categories, or totally ignore one or two of them, you are subject to asset-class risk.

It's prudent to diversify across all three major asset classes even though you want to give primary emphasis to, say, stocks.

5. Management Risk:

The majority of actively managed funds underperform the broad market benchmarks. Even though a fund has beaten the market in the past, there are no guarantees it will continue to do so.

Individuals who stick with poorly run funds risk substantial under performance, which can compound over time. Investors in index mutual funds avoid management risk.

6. Sector Risk:

Industry or sector risk faces those who invest in narrowly focused sector portfolios, such as those focusing on health care or even utility stocks. It also affects individuals holding more diversified funds that make big sector bets.

7. Country Risk:

This danger, which includes economic and political instability, is associated with single-country investments, especially those targeting developing markets.

8. Credit Risk:

The risk of default can be a concern for high-yield bond fund investors. Junk bonds can experience staggering losses when setbacks occur in this sector.

9. Tax-Rate Risk:

Investors have to be cautious in changes in tax laws that could make their holdings less valuable.

4. Managing Investments Risks

"To make a mistake is only human; to persist in a mistake is idiotic." - Cicero (106 - 43BC)

Reduce your risks by:

Setting your sights on the long term, patiently riding with the ups and downs!

If you have the time to be patient, you can benefit from time diversification. The more numerous good years for stocks outweigh the bad, pulling your return up.

Thus, if you hold equities for many years, you can expect to realize significant positive growth in your wealth.

Weeding out your laggards

Don't be too patient with laggards. This is the management risk referred to earlier. Underperforming the market benchmarks is a big risk to which many people are oblivious.

The more years you remain with a subpar performer, the greater the damage to your nest egg. Weed out funds that have lagged their peers over the past 18 to 24 months.

Avoiding hard-core market timing

It's not uncommon for hard-core market timers to move between the extremes of 100% stocks during an up market to 100% cash when their indicators signal a major turning point in prices.

Market timing is especially easy to do with mutual funds. Resist the temptation.

Participation in the best up months is far more important than avoiding the worst down months, and the really dramatic upward surges in stocks are unpredictable, of short duration, and few and far between.

Market timers risk being in cash when the bull stampedes. Missing out can make a big difference in your long-run returns.

Being disciplined and using cost averaging

Investing monthly in a specific stock is a great way to build wealth and cope with market ups and downs. Your fixed investments buy more shares when prices are down and fewer at higher levels.

Cost averaging can help people become more disciplined because it encourages investing during market nadirs when individuals otherwise might be too fearful.

A particularly good strategy is to double up on your investments when prices are depressed, if you're able to. This will help enhance your long-term performance, by further reducing your average cost per share

5. The Bulls, The Bears & The Farm

The Bulls

A bull market is when everything in the economy is great, people are finding jobs, gross domestic product (GDP) is growing, and stocks are rising. Things are just plain rosy! Picking stocks during a bull market is easier because everything is going up. Bull markets cannot last forever though, and sometimes they can lead to dangerous situations if stocks become overvalued. If a person is optimistic and believes that stocks will go up, he or she is called a "bull" and is said to have a "bullish outlook".

The Bears

A bear market is when the economy is bad, recession is looming and stock prices are falling. Bear markets make it tough for investors to pick profitable stocks. One solution to this is to make money when stocks are falling using a technique called short selling. Another strategy is to wait on the sidelines until you feel that the bear market is nearing its end, only starting to buy in anticipation of a bull market. If a person is pessimistic, believing that stocks are going to drop, he or she is called a "bear" and said to have a "bearish outlook".

The Other Animals on the Farm - Chickens and Pigs

Chickens are afraid to lose anything. Their fear overrides their need to make profits and so they turn only to money-market securities or get out of the markets entirely. While it's true that you should never invest in something over which you lose sleep, you are also guaranteed never to see any return if you avoid the market completely and never take any risk.

Pigs are high-risk investors looking for the one big score in a short period of time. Pigs buy on hot tips and invest in companies without doing their due diligence. They get impatient, greedy, and emotional about their investments, and they are drawn to high-risk securities without putting in the proper time or money to learn about these investment vehicles. Professional traders love the pigs, as it's often from their losses that the bulls and bears reap their profits.

What Type of Investor Will You Be?

There are plenty of different investment styles and strategies out there. Even though the bulls and bears are constantly at odds, they can both make money with the changing cycles in the market. Even the chickens see some returns, though not a lot. The one loser in this picture is the pig.

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Make sure you don't get into the market before you are ready. Be conservative and never invest in anything you do not understand.

Before you jump in without the right knowledge, think about this old stock market saying:

"Bulls make money, bears make money, but pigs just get slaughtered!"

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PART VII: EQUITIES & THE TIME FACTOR

1. Stock Investing and The Age Factor

How do you decide how much of your investments to put into stocks and how much to put into other types of investments?

Before deciding how much to invest in each, a little financial planning and self-examination is necessary.

Basically, there are five things you need to consider when trying to decide how much to invest in stocks and what to tuck away in other investments:

1. Your Age

2. The Consequences for Your Retirement Planning

3. Your Personal Comfort Level

4. How Diversification Affects Risk, and

5. Your Overall Financial Goals

You start by placing your age into a formula which tells you what percentage of your long-term investment money should be invested in aggressive growth vehicles such as stocks.

It simply is:

100 - Your Age = The percent of your investment money that should be in aggressive growth investments.

This formula is straight forward and makes logical sense. When you're young, you have time on your side. If one of your investments goes in the tank, it may be upsetting at first.

However, you have many years before your retirement to rebuild your fortune before you actually need to touch the money. The main risk you have to overcome when you are young is not losing your fortune, but not growing your fortune fast enough. And this formula doesn't lie!

Clearly, when you grow older, more of your assets should be invested into conservative, income-producing investments such as bonds.

That's because when you're 50 years old you have a lot less time in the job market to rebuild your retirement fortune than when you're say 25 year old.

This formula generally applies to money earmarked for retirement. Or at least money that you won't touch for 7 years or more.

Investing in good fundamental stocks with long term can deliver huge returns, which proves to be far superior in terms of returns when compared to other investment items like fixed deposits, bonds, precious metals like gold & silver and of course real estate.

2. Don't Count on Stocks for Short Term Goals

Over the short-term, stocks can be battered or buoyed by any number of market-changing events. Announcements about inflation, interest rates and other economic news – good or bad – can push the market up or down.

World and domestic events can also have a negative or positive influence on the market.

None of these events are within the control of companies or investors. Good, financially-strong companies can watch their stock fall with the rest of the market or their sector through no fault of their own.

This is why stocks are not appropriate investments for people who will need access to their money in the near future. Volatility can shrink your investment at just the time when you need to cash out.

Savvy investors know that stocks are for the long run and are willing to watch the day-to-day fluctuation knowing that good stocks will prove their worth over time.

As you approach the time when you will need to cash out of stocks, you should begin shifting assets into more secure investments such as fixed income instruments like bonds, bank CDs or other more stable products.

A good rule of thumb is to begin the transition from stocks to more stable products when you are two to three years away from needing the money. Use your good sense and judgment on when to begin the transition.

If you don't have to move all your cash out of stocks at once, you can stagger the transition over a period of months and years.

Don't let yourself be trapped in the situation of needing a big gain in your stocks at the last moment to reach a financial goal. This risky behavior may make achieving your goal out of reach if the market moves against you.

3. Characteristics of Successful Investors

The techniques and the characteristics of the most successful investors are diverse, and there's not a guaranteed formula of success.

Nonetheless, by looking at the mindsets of certain successful investors, we can learn by following 8 of their key traits:

1. Reason

Arguably reason is the most important characteristic. You need to justify why you hold each company in your portfolio. You must seek out high-quality stocks that are undervalued by the market, and therefore cheap.

2. Commitment

To exploit your strategy you have to do the research - and keep doing it - including surveying all financial data, online investment resources and company reports. Don't forget that "numbers have no prejudices."

3. Discipline

The research process doesn't finish once you've bought a stock. You have to obsessively follow your purchases, to make sure they were sensible. You'll need discipline, because successful investing is about running your profits and cutting your losses. The stock market is a rollercoaster, so you have to ride out the peaks and bottoms.

4. Flexibility

If you're going to have rules you need to be able to break them. The same stocks won't perform well in all markets.

5. Guts

The best time to buy stocks is the time of "maximum pessimism" - when everyone is selling and fleeing the markets. To do this takes bravery.

6. Open Mind

Seeking out opportunities ignored by other investors prevents prejudices coming between you and an opportunity.

How to Grow Your Savings?

7. Patience

"Unfashionable stocks" are unlikely to turn around overnight, so you need to know when to hold on.

8. Know Your Limits

This means accepting you won't be the next Warren Buffett. Professional investors spend their whole day researching companies, have analysts to help them, and can visit companies. That doesn't mean you can't stock-pick successfully as an amateur.

The best trick is to keep it simple and stick with what you know.

4. Don't try to Time Bottom of Stock Market

It's hard to know what the stock market is going to do in normal times, however it is almost impossible to predict market direction in the midst of chaos.

The Sensex sets record high after record high and some investors see a straight line upward into the future or the Sensex gives up 10 percent of its value in a week and the same investors see a death spiral to the poor house.

How is an investor to know what to expect when the market is moving decisively in one direction?

Stock Market Runs:

Bull markets can run for years and so can bears. Unfortunately, there is no absolute way of knowing when a bull will stop or pause or when a bear market will take charge and begin sucking value out of everything.

Investors in the 2008 – 2009 market know it can happen relatively quickly. The Sensex lost almost 60 percent of its value during this bear market following the subprime crisis and global recession.

Was there a day when the market turned? Was there a time when the switch flipped from bear to bull?

Stock Market Switches:

It doesn't happen that precisely, but as investor confidence in the economy and the geo-political situation returned, the market sentiment switched to buying equities.

Sensex & Nifty experienced upper circuits when UPA wins, equity investors were surprised by such an upmove. Thanks to letting the hype out of the market, many formerly overpriced stocks now started looking reasonable. That's one way a bull market starts.

Over the years, market callers have made a living off investors who believed these people had some system that would tell them when the market would turn from bull to bear or bear to bull.

The idea is that if you know in advance you can make profit by trading accordingly.

Most serious investors don't waste their money on these services, rather they stay invested and adjust portfolios as needed.

Research shows you are better off remaining in the market than trying to time an entry and exit on when the market might turn. When the market does rebound, most gains come quickly. Investors, who miss this entry, miss most of the upturn profits.

The lesson is it's better to stay in the market than trying to time when it will turn.

5. Investing in Stocks for Regular Income & Long Term Growth

Stocks offer the potential for regular income and long-term growth

One of the major benefits of owning stocks is their ability to produce regular income (dividends payment) and long-term growth.

The challenges of the 2008-09 financial crisis put a strain on some companies to reduce or eliminate dividends, but for strong companies, this is just temporary.

When the economy rebounds, some companies will be in better financial condition than others. Mature companies with established markets may be in an enviable financial position.

As is often the case, companies providing products or services to businesses may experience rapid growth. Companies that have curtailed spending during the economic crisis will play catch-up, scrambling to capture market share or protect what they still have.

As we work through a recovery, market-leading companies will become cash cows, throwing off extra income in the form of dividends and stock buybacks. It is safe to assume that investors are going to be more wary of risk in the future. Companies with a consistent record of dividend payment and growth will command a premium in the market.

It is almost certain that either through regulation or shareholder action, executive compensation and bonuses will come under close scrutiny. Stocks that return more profits to shareholders may be viewed in a more favorable light by regulators and shareholders. Don’t be surprised if regulators encourage dividends through tax policies.

For investors, the combination of regular income and long-term growth makes stocks a wise choice for those with a long time frame. While there is still be much emphasis on quarterly profits, the investing community is likely to take a closer look at companies that have a longer term approach to growing the business.

With the right stocks in your portfolio, it is hard to beat the potential of current income and long-term growth.

6. Investing Checklist – 10 Most Important Element

Every investor's situation is unique, and you have to make all the right moves that are right for your own situation.

You can use the following list to stimulate your own thinking and make your own checklist and moves.

1. Get the Most from Your Cash:

If you have cash in a money-market fund, you know you're not making much money. You can probably do better than you think if you're willing to do a bit of shopping.

2. Shop for Interest Rates:

If you have money in a bank, find the highest interest rate you can to protect you against inflation.

3. Review Your Emergency Fund:

This should be money you don't think you will need any time soon. Try to make this money work harder for you.

A short-term bond fund will pay more than a money-market fund without much additional risk. If you think you probably won't need this money for four or five years, consider using a fund that owns both stocks and bonds.

4. Check Your Asset Allocation:

The way you allocate your assets is the most important investment decision you will make. Your investment plan should specify your percentage allocations between fixed-income and equity investments.

Within the equity part of the portfolio, you should have target allocations for funds as well as for big-company stock funds and small-company stock funds. Your plan should also specify how much is to be in value stocks and how much in growth stocks.

If you have a financial advisor, set up a meeting to evaluate your current allocation. The advisor can suggest any necessary changes.

5. Rebalance your Investments:

When equities seemed to go through the roof, your investments may have taken you some distance from the proper allocation you determined for yourself.

If you began the new year with a portfolio equally split between stock funds and bond funds, you might be able to change it with about 60 percent of your total in equities and only 40 percent in fixed-income funds. What's wrong with that? Too much risk. A portfolio with 60 percent in equities is riskier than a 50-50 portfolio.

Rebalancing gets you back on track. And there is another benefit:

By rebalancing you will be taking some of last year's profits "off the table" and spreading them around. This is called buying low and selling high. Rebalancing makes it automatic.

6. Diversify:

Maybe you think you're already properly diversified. But the vast majority of portfolios are not that well put together. Most portfolios are heavily over weighted in large-cap growth stocks. That may seem fine in a year like the one we just experienced.

But diversification pays off in good times and bad. It's a rare investor whose equity portfolio couldn't be improved by adding one or more of three kinds of funds:

Value, small-cap and international.

7. Determine Your Investment Policies:

Make a written investment policy statement for yourself. Investors who actually do this are far more likely to attain their goals than those who just casually think about it.

Writing a policy statement requires careful thought, but once it's done it will remind you rationally, when the market is trying to manipulate your emotions, what you should be doing and why.

8. Set Measurable Goals:

Write down your long-term financial goals and make a written retirement plan. That plan should specify a target year you want to retire and estimate how much retirement income you will need from your investments.

From there, you'll be able to tell how big your portfolio will have to be when you retire. For a quick rule of thumb, figure that on the day you retire, your portfolio should be 20 times the size of the annual income you want from that portfolio.

9. Make Specific Plans:

If this is starting to sound like serious work, then you're getting the point. There's no free lunch for somebody who would be a successful investor. But the payoffs from this step could be enormous. You could retire earlier or boost your retirement fund by hundreds of thousands.

At the very least, all this written work will give you a clear picture of where you stand so you don't need to rely on vague hopes or fears. Make a written pre-retirement plan showing how you will accumulate the nest egg you will need on your retirement day.

10. Execution:

Finally, keep looking for more things you can do in the coming years to strengthen your financial muscles.

ABOUT SARAL GYAN

Saral Gyan Capital Services is an independent equity research firm. We publish unbiased thoroughly researched reports that enhance the visibility of innovative public companies in micro, small & mid cap space. Our reports, Hidden Gems & Value Picks, are distributed to our subscribers through our website.

Hidden Gems & Value Picks are a highly detailed report that is written to be easily understood by the financial community. We also circulate articles via free email & mobile subscription which works as a guide and provide insights to equity market. We also offer 15% @ 90 DAYS, which works on buy to sell and gain strategy for short term profits.

Our research reports are written by a team of equity analysts who recognize investor's desire to understand a business in a way that supports an educated investment decision based on facts. Our reports contain meticulously researched facts on companies, their fundamentals, and their industries, validating a company's prospects and enabling the reader to objectively evaluate the company's value.

At Saral Gyan, research is taken as a creative work undertaken on systematic basis in order to increase the wealth of knowledge. We believe that Research is a necessity and forms the basic foundation upon which advice is made with reference to particular stocks with recommendations on buy or sell or hold.

SERVICES

1. HIDDEN GEMS

HIDDEN GEMS

Saral Gyan offers in-depth and extensive research reports of small companies in terms of market capital. Financial Analysts and Experts in Saral Gyan cover a large universe of small cap stocks and evaluate all key parameters of various companies in a particular sector to explore hidden gems. (also known as multibagger stocks)

To find out the right stock which may give you exponential returns on your investment in future is not an easy task. Small cap stocks hold much bigger pie as compared to mid cap and large cap stocks, hence requires extensive research.

Our team of research analysts exclusively does research work and analysis to explore such hidden Gems. Further filtering is done on the basis of company future expansion plans, current earnings, dividend paying history, management views etc. As a result of extensive research every month, we identify one Hidden Gem and prepare complete research report.

On subscription to Hidden Gem section, subscriber will get one hidden gem stock research report on monthly basis. We offer annual subscription and provide complete research report of 1 Hidden Gem stock every month.

2. VALUE PICKS

As most wealth building investors know, investing in the stock market is often divided into large-cap, mid-cap and small-cap investing. Each style of investing being based on the size of the market capitalization of the companies being invested in.

This methodology of dividing up companies by market size has become so well established that most mutual funds get classified on the basis of the size of companies they invest in. Thus, while large cap companies refer to some of the largest, most well-known companies in the country, and small-cap companies often represent little known firms. Mid-cap companies encompass the entire range between these two extremes.

But is mid-cap investing a true road to wealth, and worth a look by the wealth building investor?

Proponents of mid-cap stock investing frequently point to the relative stability offered by firms in this range while still retaining plenty of their upside potential. Large firms on the other hand have a tough time increasing shareholder value owing to their sheer size, and small companies are significantly more risky.

We frequently refer to Warren Buffett's method of evaluating a company based on their fundamentals. Specifically, he asks us to look for companies that:

- *Are in a business that you can truly understand*
- *Have a large competitive advantage (huge moat) over existing and new entrants to the business*
- *Provide a service that is likely to be needed for a long time, and is unlikely to be replaced any time soon.*

However, even companies with the above qualities may never grow to be a large-cap company simply because the management may choose to not grow the firm too quickly. In such a situation, one has to make sure that much of the profits being made are distributed as dividends to all the stakeholders, including shareholders.

The other factor to look for is the overall management of the firm and if they are revealing enough information about the company to its stakeholders, or are they being secretive about its market position. Any sign of stonewalling or misdirection from the management is a good reason to jump ship.

Given the above set of factors, and a company thats selling at a reasonable valuation, a mid-cap stock can indeed yield double-digit growth for many years to come. However, such companies are hard to find - since the moment Dalal Street discovers such a company, it will bid up its value to sky high levels rather quickly. However, such value picks do exist and can be found through careful evaluation.

But a blind investment into mid-cap stock companies is likely to lead to below market performance. Mid-cap companies often have not shown how they would behave in the face of increased competition, in economically tough environments, or when their core product or service is in danger of being replaced or super ceded.

Mid Cap stocks should be a part of your investment portfolio with long term perspective to create wealth. Its advisable to have equity portfolio allocation between 20 to 40 percent in mid cap stocks that offers true value on your investments.

At Saral Gyan, equity analyst team keep on evaluating various companies of different sectors in mid cap space to find out such Value Picks. Equity analysts consider those companies as mid cap stocks whose market capital is in the range of 1000 crore (10 billion) to 10,000 crore (100 billion).

3. 15% @ 90 DAYS

15% @ 90 DAYS

Saral Gyan team of equity analysts select a particular stock from BSE 500 Index based on technical & fundamental stock analysis. Objective of right stock selection backed with in-depth analysis is to ensure returns of 15% (excluding brokerage) within a period of 90 days for our investors.

Equity analysts team will recommend a stock with buying & target price on monthly basis and target price to buying price will be evaluated based on technical's with an upward range of 17% to 20%.

Why 15% @ 90 DAYS?

Many people believe that buy and hold is the best strategy to employ for the long term.

However, over a period of couple of months, a person who buys 100 XYZ shares at 100 each, sees them rise to 120, sees them decline to 85, and then rise back up to 115, he is not getting an overall return as good as he thinks. What he has lost is the opportunity cost associated with the down period of time.

However, the return over the same period would have been much greater, if the investor had sold the securities and then bought them back at a lower price.

This works whether the investor takes the cash proceeds from the sale and puts them to work in a savings account, or for any other investment.

In real life, the investor would not sell exactly at the top and he would not buy exactly at the bottom. He would sell below the top and buy above the bottom. Nevertheless, the return is still superior to the buy and hold strategy.

How 15% @ 90 DAYS works?

15% @ 90 DAYS works on Buy to Sell & Gain Strategy for short term as well as long term investors.

An individual as an investor will buy shares based on the recommendation every month and sell them once target price is achieved within expected time frame of 90 days, he/she needs to sell entire his/her holdings to book profits and use the same principal sum invested earlier to buy the next recommended stock. Hence, using minimum capital requirement, one can keep on realizing the profits at regular time intervals. Needless to say, these stocks would not be part of long term portfolio as the basic objective of investments is booking profits in short term.

Does 15% @ 90 DAYS service delivers returns during market correction?

You do agree that fundamentally good stocks also experience downward move during market corrections. Stock market offers risks along with rewards, that is one of the reason why 15% @ 90 DAYS buy calls will be based on technical chart patterns to ensure limited downside risk. Hence if target price is not achieved in 90 days due to market correction, stock may not tumble down heavily to shrink your working capital.

Benefits of 15% @ 90 DAYS

Returns could be as higher as 75% on Invested sum at the end of the year.

Assuming all 10 stocks recommendation out of 12 in a year hits their target price, an investor will gain almost 75% returns on invested capital with equal amount of investment.

As shown in illustration below, investment of 1000 Rs on monthly basis will yield total profit of 1500 Rs with invested capital of 2000 at the end of the year considering target price is achieved for 10 recommendations out of 12.

MONTH	MONTHLY INVESTMENT	CUMULATIVE INVESTMENT	PROFITS @ 15%	CUMULATIVE GAINS	CUMULATIVE GAIN %
Jan	1000	1000		0	0.00%
Feb	1000	2000		0	0.00%
Mar	1000	2000	150	150	7.50%
Apr	1000	2000	150	300	15.00%
May	1000	2000	150	450	22.50%
Jun	1000	2000	150	600	30.00%
Jul	1000	2000	150	750	37.50%
Aug	1000	2000	150	900	45.00%
Sep	1000	2000	150	1050	52.50%
Oct	1000	2000	150	1200	60.00%
Nov	1000	2000	150	1350	67.50%
Dec	1000	2000	150	1500	75.00%

How to Grow Your Savings?

Limited Capital requirement

The capital invested will be free to invest again once investor books profits on previous investments. Hence, this will be a different way to increase wealth all together for long term investors.

Rupee Cost Averaging

During market corrections, instead of hitting target price recommended stock may fall in next 90 days. Team of Saral Gyan equity analysts may recommend the same stock four months down the line to bring down your average cost, this will help to achieve 15% @ 90 DAYS in next round of your investment for the same scrip.

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