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Save More! Spend Less! Build Wealth!

Follow Prudent & Creative Strategies



Save More ! Spend Less ! Build Wealth ! Follow Prudent & Creative Strategies



Achieving innovation in Financial Planning is all about using financial products and services creatively, understanding the financial regulatory system thoroughly and making them work to your advantage. Innovation in this sphere is inseparably connected to meeting investor goals and needs. Goals, needs and wants change over time influenced as they are by the macro environment and our own aspirations which fluctuate with our prosperity levels. Thinking about ways and means to stretch the rupee to its limit can be stressful, but by taking control of our spending and saving even just a pocketful of change can help alleviate some of the worry. Whether you want to be a millionaire or simply want to stop spending your paycheck before you get it, there are some surprisingly easy ways to save, invest and build wealth. While there's nothing wrong with spending when you can afford it, it is important not to neglect your financial goals.



Girish Aswani, CFP™

In earlier days, when so many avenues for investments were not available, for an ordinary household building wealth meant accumulating money by setting aside some amount from their income. They inculcated similar savings habits in their children. In many families a thumb rule was adopted that a minimum 20% of the income or salary must be saved. Most people would have then invested their savings in gold, and those who were richer would buy land etc.

Things have changed now. While basic savings still mean setting aside money from

income, there are other ways that one can save on expenses; reason being the financial environment has evolved so that citizens are incentivized for spending. These incentives can take the form of reward points, loyalty points, cash backs, discounts etc. Even as you spend, there is scope for utilizing these numerous incentives so that you get an additional amount to spend, which is 'free', so to speak.

The investment climate has also changed substantially and we have progressed to buying financial products where one can take advantage of existing rules and regulations to

save on tax outgoes – whether in the form of income tax, capital gains tax etc.

Within the existing structure of our rules, regulations and taxation laws, how can we maximize our savings and get more out of what

consumers supplemented by the feedback received by investment professionals and financial planners, I felt the need to do a study and analyse what exactly happens in the lives of such people in terms of income and expenses. These responses are standard despite

“ Within the existing structure of our rules, regulations and taxation laws, how can we maximize our savings and get more out of what we spend? ”

“ Income has increased more compared to costs ”

we spend? Here are some creative strategies for our avid readers. Remember savings are also additional income sources.

Different Scenarios with Different Generations

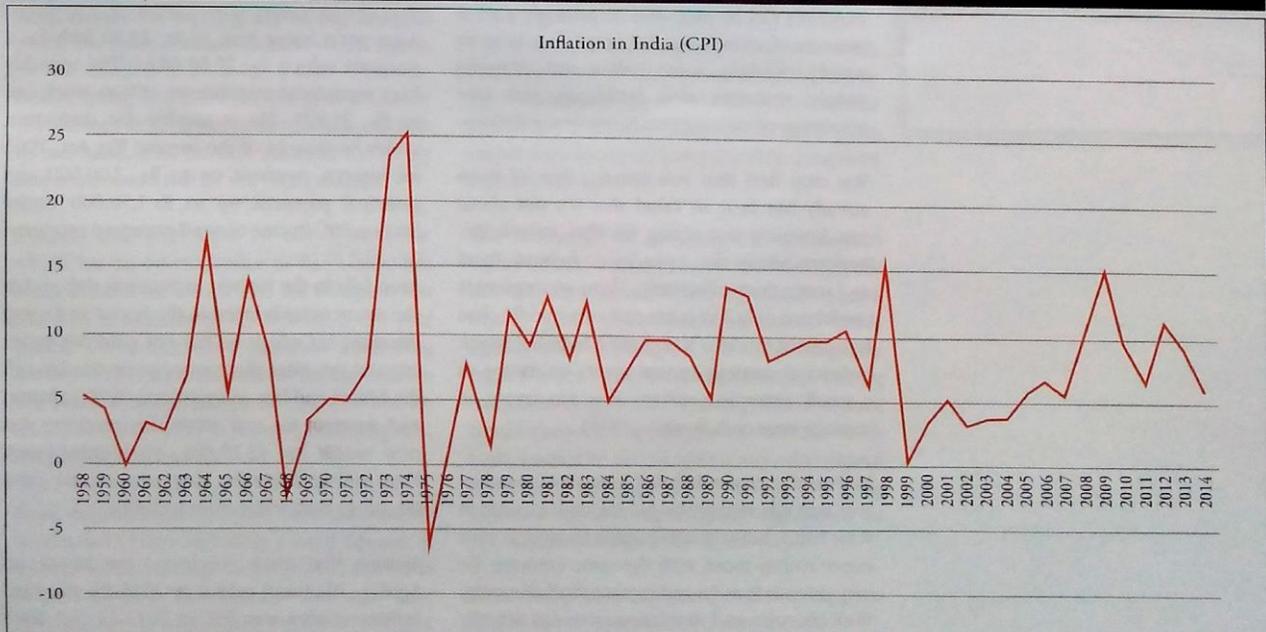
When anyone is asked to invest more or make additional savings for wealth creation the normal response that most investment professionals are accustomed to hear is “with the current income, meeting month-to-month expenses is tricky enough, from where do I generate additional savings?” Another usual response is “these are all necessities. We don't spend extravagantly.”

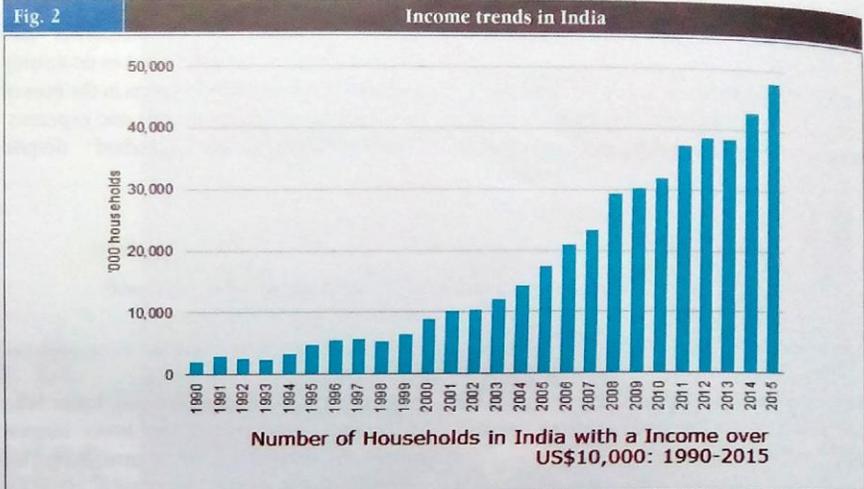
After receiving such responses from various

improvements in their cash flows, lower bills, a decline in inflation index, lower interest premiums, improved equity returns, higher tax exemptions etc. What then possibly could be behind this apparent squeeze on liquidity or an inability to save more?

People who are now in their 50s will remember that in their youth, when income was low and expenses even lower, roti, kapda aur makaan (food, clothing and shelter) was the basic aspiration for an average middle-class citizen. These were not only the needs but also the wants with some additions thrown in such as inexpensive holidays (that was taken care by leave travel concessions that financed a journey to their hometown or native place). If costs have multiplied now and what were

Fig. 1 Inflation trend in India





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Savings is the first step towards wealth creation. The second step is investing these savings in securities and instruments to generate returns that contribute to wealth creation.

once considered luxuries have turned out to be general needs, the income of a person has also multiplied. Of course we can still indentify some of the wants as normal or luxurious.

By looking at the price trend, measured by changes in the Consumer Price Index, and salary levels over the years (Figures 1&2), what stands clearly visible is that salary has increased more than the costs. This brings us to the question of why families still find it difficult to meet their monthly expenses and save sufficiently. Is it really the expense which is a problem or is it something else?

There are various ways by which monthly expenses can be met; and surprisingly a great amount of money can be saved in a year by simply tweaking some habits and adopting simple strategies that build up and take advantage of existing provisions in regulations.

You may find that you know a few of them already but bear in mind that it's not about just knowing but acting on that knowledge, understanding the economics behind them and using them effectively. These strategies are useful not only if you are part of a middle-class household but also if you are a high net worth individual owning several assets or owner of a small enterprise, where you are trying to manage your cash flows.

You need to remember that in most of the cases you may not actually be getting cash as such in your hand, but you will be able to stretch your rupee to buy more with the same amount. We may refer to it as an indirect method of saving. With tax rules and regulations you can actually

have more of your disposable income in your hands, which can be invested to create wealth.

Create Asset in Residential Property

Savings is the first step towards wealth creation. The second step is investing these savings in securities and instruments to generate returns that contribute to wealth creation.

Let us consider an example of investing in a residential property. When a person takes a home loan he becomes eligible for certain tax deductions, which can be considered as his additional savings.

Arup got a home loan of Rs. 23.50 lakh for a property valued Rs. 27.50 lakhs. The monthly loan repayment installments (EMIs) work out to Rs. 21,905. He is eligible for deduction under Section 24 of the Income Tax Act, 1961 for interest payment up to Rs. 2,00,000 and principal payment up to Rs.1,50,000 under Section 80C in case of a self-occupied property.

Arup falls in the highest income tax slab and at the moment he is living in the house and using the asset for which he has not paid the entire amount yet. After three years he decided to sell the house and buy a bigger one. With inflation and demand for real estate, his property was now worth Rs. 42,15,000. After three years, Arup will be liable for long term capital gains tax, along with indexation benefits.

Assume that Arup purchased the house on April 1, 2012 and sold it in 2015-16; the Cost Inflation Index was 852 in 2012-13 and 1081

in 2015-2016. Therefore, indexed cost of acquisition of his house will be calculated as $27,50,000 \times (1081/852) = \text{Rs. } 34,89,143$. Further, Rs. 42,15,000 is the sale price of the house. Therefore, Rs. 7,25,856 (i.e. Rs. 42,15,000 – 34,89,143) is the long term capital gains on which he is required to pay long term capital gains tax @20%, that is Rs.1,45,171.

To save capital gains tax, Arup decided to invest his gain (Rs.7,25,856) as a down payment to buy the new house. Thus, he has saved on his tax outgo and used the entire gains from the transaction by investing in property, which will further enhance his wealth.

Now, suppose the first house had not been occupied by Arup and he had let it out on rent. In such a case, he can claim the entire interest on the loan for tax deduction without any limit. This may have the effect of placing him in a lower tax slab also.

This makes Arup's house as an income generating asset which would contribute towards savings. If it is self-occupied, it saves on rental expenses; if let out then it generates regular rental income stream while saving on tax outflows.

Use Low Yield Investments to Fund Financial Goals

Another prudent way of saving big time money is by analyzing the cost of capital. In case we need money for meeting any of our financial goals, the most obvious thought which comes to our mind is to look for a loan. However, before going ahead we should always analyse the yield generation potential of funds available in our hand, post tax and inflation. Let us try and understand this by way of an example.

Assume that you want to buy a new car, which has an on-road price of Rs. 9 lakh. You scout around for a loan and the cheapest you can find is available at 13.15% for a five year period. Also, there is a one-time processing fee of 1.14%. Your total interest on the loan for five years works out to be Rs.3,32,820 and an additional Rs.10,260 towards processing fee, totaling to Rs.3,43,080.

Now, consider that you also have investments worth Rs.15 lakhs including a fixed deposit of Rs.8 lakhs, cash savings of Rs.1,00,000 and some other long-term investments. You now have two choices; to either buy the car in outright

cash by redeeming part of your investments, or else go for the vehicle loan. You are reluctant to touch your investments because you feel that you may need it in some emergency and that a loan would be a safer option, especially as you have five years to pay it down.

But before taking a final call, let us look at what your bank fixed deposit is doing for you. At a quarterly compounded rate of 8.25% for five years you earn an interest of Rs.3,89,130 which is taxable at the marginal tax rate. So, this means in case you take a loan there is a net saving of Rs.46,050 (Rs.3,89,130 - Rs.3,43,080). This looks attractive and you are more than ever resolved to take the car loan. While all this looks good on paper you have to realize that with inflation at 5.6% your effective return on your investment is barely above 2%.

Even if you disregard the inflation element in your calculations, the post-tax interest becomes 5.425% annually (30% Income Tax deductions) compounding quarterly and you would be actually earning Rs.2,46,806 as interest in five years.

Taking a loan to continue the FD of Rs.8,00,000 would cost you Rs.96,274 (Rs.2,46,806 interest earned – Rs.3,43,080 interest paid) over five years which is a big sum of money. In fact it would make more economic sense for you to liquidate your FD to buy the car.

Set-off Your Capital Gains

One of the best ways to generate tax-free wealth over a period of time is to invest in equity instruments such as stocks or equity-oriented mutual fund schemes. Short-term capital gains tax for such securities is at 15% while long term capital gains tax is nil.

The advantage of investing in equities and equity-related instruments is that you can set off long-term capital losses against long-term capital gains and short-term capital losses against short-term capital gains and long-term capital gains. Long term capital losses arising out of exchange traded shares/stocks or mutual funds (provided securities transaction tax is paid) cannot be set off against any other capital gains. Long term capital loss can be set off only against long term capital gains and cannot be set off against short term capital gains.

Also, losses from any non-speculative business can be set-off against speculative income.

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Another prudent way of saving big time money is by analyzing the cost of capital - taking a loan versus using investments.

After setting off the losses against gains, if there is any unabsorbed loss remaining, such a capital loss can then be carried forward for eight assessment years and set off as above.

Take Credit Card Freebies

Credit card issuers are increasingly wooing customers in various ways to increase the credit card culture and move from cash to plastic. One of the ways they incentivize customers, especially those who indulge in big ticket purchases, is to offer them the option of repaying in installments at 0% interest. For example, if you buy a LED television set for Rs.47,990 you can either repay the entire amount in a shot or convert the due amount into 12 monthly equated installments of Rs.4,000 each (not taking processing and other charges into account). In the first option your cash reserves are reduced to the extent of your payment. However, in case you choose to pay the amount in EMIs, i.e. the second option, you have the flexibility to use the remaining balance (after paying the monthly instalment) to either meet your other goals or else invest it profitably.

Use Plastic Money to Save

Credit cards and debit cards are available in the market for different products, services and sectors. Some of these cards offer free movie tickets on every purchase, discounts on electronics, extra air miles and even reversal of surcharge while refueling your vehicle. Bundled with a lot of discount coupons, these cards should be seen as an opportunity to save on your spending (and leaving more cash at your disposal), which is not available to those who do not have these cards.

Let us do a simple calculation. Suppose you refuel your car with 15 litres of petrol at Rs. 66 per litre. The total comes to Rs. 990. On this the surcharge will be Rs.24.75. That's Rs.1.65 per liter extra cost. If you refuel your vehicle six times a month the surcharge cost comes to Rs.148.50 and in a year it is Rs.1,782. With the amount that has gone towards payment of surcharges, refueling could have been done almost two more times.

Reversal of surcharge puts that extra cash in your hands. Some co-branded cards offer higher rewards points for the same amount of spend; some offer up to 10% cash back when buying from specific merchants; still others

allow you to accumulate frequent flier miles etc.

Make Every Spend Count

There are various methods wherein points can be collected on purchases. Frequent flier miles, loyalty points when shopping at department stores, discount vouchers if expenses cross a certain amount and rewards points on credit card purchases etc., are all ways that one can capitalize on every purchase. These points and miles collected can be redeemed later to lower future expenses. This works best if you shop consistently with certain merchants or use the products and services of particular manufacturers. Equity brokerages also incentivize customers for their loyalty by reducing brokerage rates when their transaction amounts are above a particular value for a certain period of time. This leads to considerable savings.

Explore e- Purchase

Online shopping is a new trend in India which has picked up very fast. At the moment low and discounted prices are the way that e-commerce players are trying to woo customers and create brand loyalty. Right from furniture, white goods, flight tickets to groceries and household items – everything is available at substantial discounts to their original price. The convenience of home shopping and free home delivery saves on travel costs and this does lead to savings provided you are not tempted to splurge while shopping online.

Even otherwise, original product manufacturers, who have an established brick-and-mortar presence, offer lower prices while shopping online and this is especially prevalent for consumer electronic items.

Identify Value Deals

There are peak season rates and there are offseason rates. For example, sale of air conditioners and refrigerators soars during the summer months and so do the prices, though retailers may try to temper it with so-called "discounts" and exchange schemes. Plan your purchases during times when demand for particular products are low and you are sure to get a better deal than if you bought them during peak demand times.

Identify multi-product retailers who often

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Identify multi-product retailers who often cross-subsidize items and offer bundled products that are cheaper.

cross-subsidize items and offer bundled products that are cheaper. Never buy during peak 'season sales'. Wait till the rush has died down. Retailers and shopkeepers will then be trying to get rid of excess stock and that is when the prices are really low.

Do not buy products when they are just launched. Wait for a few months till the initial excitement and demand has died down. The same goes for airline fares and hotel rates. Plan your holidays just before or after the tourist 'rush season'.

Timing works with respect to entertainment too such as movies. Weekends are the time that you get to watch movies with your family and that is when the rates are high too. Cinema halls have started screening early morning shows on weekends, tickets for which are available at nearly half of the regular price.

If you consider going to a movie, weekend prices range from Rs.400 to 900 per ticket whereas on weekdays it is Rs.100 to 200 per ticket. If you are lucky to get a 'buy one, get one free' offer let us see how much you can save. If you and your partner watch two films a month, on weekends it will be between Rs.800 to 1800 and if you throw in some refreshments as well you can easily spend up to Rs. 2,000 per outing i.e. Rs.4,000 a month, which translates into spending up to Rs. 48,000 in a year. If you watch movies during weekdays, you can easily contain the cost between Rs.600 to 800 a month which translates into a cost of up to Rs.9,600 a year, a savings of Rs.38,400 annually.

While purchasing apparel, again try and look for 'buy one, get one free' deals that almost all retailers offer at some point or the other, especially during the slack season. This is especially true during the summer holidays and winter holidays when most people are on vacation and go off to other places.

There are a lot of discount retailers who have tie ups with restaurants, parlours and multiplexes which bring you attractive deals on services and dining every day or for a specific period. With these discount vouchers you can substantially reduce your expenses for such services.

Clear Dues Before Time

There are plenty of bills to be paid – electricity bills, landline bill, mobile phone bill, gas bill, cable connection bill, house maintenance

bills, credit card bills and so on. All of them come with deadlines – the due date – and if we overshoot that date we have to pay a penalty and sometimes other charges as well. Many service providers try to incentivize and encourage consumers to pay before time by giving them discounts. Some utility companies even pay you an interest if you deposit excess cash with them for making payments. The amounts charged as fine for each missed due date can seem like a small change, but they all add up over time and in the case of credit cards or even home loan repayments they can affect your credit score, which will have an impact if you ever try for a loan with any financial institution.

In fact, late payment on credit cards with interest costs could be as much as Rs. 2,000 - 5,000 on a single bill even on a moderate purchase of a few thousand of rupees, apart from the fact that you lose the interest-free period while the credit card issuing company can actually levy higher interest rates on you if it finds that you are always making late payments.

Paying bills much before the due date saves cash in so many ways – you can get a discount; you only pay for what you have consumed as you avoid the fine and interest rates on the outstanding and you will be in good credit standing with the company. In order to avoid late payments you can opt for a direct debit facility with your bank or credit card issuer. You can also opt for online payment of bills with due date reminders.

Summary: Considerable savings can be done with the strategies outlined above, provided you understand the rules and regulations governing them. If you want to create wealth then you need to channelize these savings into those instruments which further make you eligible for either tax deductions, tax free returns, tangible usage of assets or maybe all the benefits together.

Sticking with a routine will help you accomplish more in your financial life, like monitoring a budget, keeping an eye on your investments, and saving more money. Find out the best money and productivity tools and apply some basic money management techniques to smoothen your financial life.

Girish Aswani, CT, NLP, CFP^{CM}, is Director Aternity Training and Consultants Pvt. Ltd.

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Thanks for reading the above article,
Request you to share your valuable feedback on: girish.aswani@gmail.com
Girish Aswani, CFP^{CM}