INFORMED INVESTOR

VANTAGE CORPORATE SERVICES LIMITED

Publication:	INFORMED INVESTOR	Edition:	ONLINE EDITION (E-PAPER)
Date:	13 - 17 APRIL 2015	Category:	INDIANOTES.COM
Editor:	MR. RAJESH DEDHIA	Author:	BANK BAZAAR
Title:	GOLDEN RULES OF FINANCIAL PLANNING		

March with its feverish frets and yearly targets is over. April 1st was (no, not All Fools Day) the start of the New Financial Year. So, did you make those financial resolutions for the new year? Or did you end up like Teena and Prateek?

Teena and her husband Prateek, a newly-wed couple, had a tough three months from Jan to March 2015, as they realised that they had not made the tax-saving investments that they had declared at the start of the financial year. If they had failed to make it, they would have received their salaries after big tax cuts.

They were barely left with any savings after splurging at the time of marriage, and there are no options now but to borrow from parents. They were already paying EMIs for car and personal loans, and could not afford any more cuts in salaries.

This is a typical case of last-minute tax planning that we hear of so often. As the new financial year has already begun, it would be prudent for many like them to take a look at their finances and plan in advance to avoid a last-minute scramble.

Step 1: Start tax planning early

Contrary to popular belief, tax planning is a year-long process, and not an annual ritual that comes in March. A little number crunching with the help of a CA, financial planner or free online tax calculators would give you enough idea about your tax liabilities in this new financial year. Based on these you can start investing in the right tax-savings instruments on a regular basis.

There are many tax-saving investment instruments to pick from: Public Provident Fund (PPF), Tax-Saving Mutual Funds, the National Pension System (NPS), a Term Insurance Plan and the Employee Provident Fund (EPF).

Lest you forget, premium paid to purchase a health insurance plan, and the principal repayment and interest payment for home loans are eligible for tax deduction.

Illustration: Sanjiv has a taxable salary of Rs 12 lakh. He contributes Rs 60,000 every year in EPF. He can claim income tax deduction on EPF, but to exhaust the full limit of Rs 1.5 lakh under the Section 80 C of Income Tax Act, he still needs to invest another Rs 90,000 during the financial year.

Sanjiv can invest Rs 7,500 every month if he starts early instead of accumulating his investments in the last couple of months. If planned early, he can judiciously choose the investment options instead of opting for a wrong product in a rush.

Of course, he must have a term insurance plan, the premium of which is tax deductable. The rest can be invested in a tax-saving mutual fund through systematic investment, PPF, NPS or Sukanya Samriddhi Yojana. If he fails to make those investments, he would end up paying an additional Rs 27,800 (30% of Rs 90,000) in tax.

Step 2: Plan your investments

If you have not already started investing for the future financial goals, the new financial year is probably the time to start. It could be short-term such as buying a car, medium-term such as buying a house or long-term goals such as building a retirement corpus.

Setting financial goals helps in choosing the right product, allocating funds to right asset classes as well as evaluating the realistic chances of achieving them. If needed, you may want to allocate a higher sum to or defer the financial goal by a year or two.

Illustration: Shoaib has recently joined a firm as marketing executive at a monthly salary of Rs 35,000. After paying for his travel and other miscellaneous expenses, he saves Rs 15,000 every month. Shoaib plans to buy a car (which today costs around Rs 4 lakh) in a year's time and he wants to save enough to pay 40-50% of the cost as down payment. He also wants to save a little to buy a house in 10 years' time.

For buying a car, he needs Rs 1.5-2 lakh. Since it's a very short-term goal, he should either put money in a one-year recurring deposit or start an SIP in an open-ended accrual debt fund. Both could offer between 8.5% and 9.5%. If he allocates Rs 10,000 every month for this goal for one year, he would end up with at most Rs 1.25-1.30 lakh, which is below his target amount.

He could either increase his allocation by a couple of thousands or defer the goal by another six months.

Step 3: Manage your debts properly

Flashing that premium credit card may give you a 'kick' especially if you do so in front of someone special, but flashing it too often may give you the rashes. Whether it is credit card, personal, auto or home loan, availing of debt beyond the paying capacity is the first step towards ending up a financial mess.

While banks would pay you loan as long as the EMI is below 50% of your monthly salary, it is up to you to assess what is your paying capacity. A little assessment of your own paying capacity would save you from many blushes—missing EMIs, sullying credit history and recovery agents knocking at your door.

Illustration: Ajay, who works with a market research firm and earns a monthly salary of Rs.20,000, just received a credit card from his bank. Unable to resist the new-found buying power in his hands, he buys the latest smart phone of his choice for Rs 35,000. He converts the purchase amount into a 12-month-EMI repayment scheme, which after including the processing fee and the monthly interest of 2%, comes to around Rs 3,400.

However, Ajay is already paying an EMI of Rs 4,000 for the bike that he bought recently. His total EMI now stands at almost Rs 7,500. After paying for EMI, rent, food and fuel, Ajay barely saves anything. Soon, he starts defaulting on the EMI for the credit card dues. The interest and penalties keep piling up, and before he realises it, his credit card dues start touching the Rs 1-lakh mark.

He starts getting calls from recovery agents, bank notices and even a court notice for defaulting on credit card loans. He finally had to take a personal loan and borrow from friends to settle the credit card debt.

Parting note: Don't let bad financial planning practices creep in. Take control of the situation. By adhering to a few simple rules, you can be financially safe: plan ahead, plan right, and plan completely. Above all, remain disciplined and curb the urge to borrow beyond paying capacity. This way, on April 1st 2016, you will be wished "Happy New Financial Year" instead of… well, you know what April 1st stands for, don't you?