Bridge the gap between dreams and reality

Financial Planning

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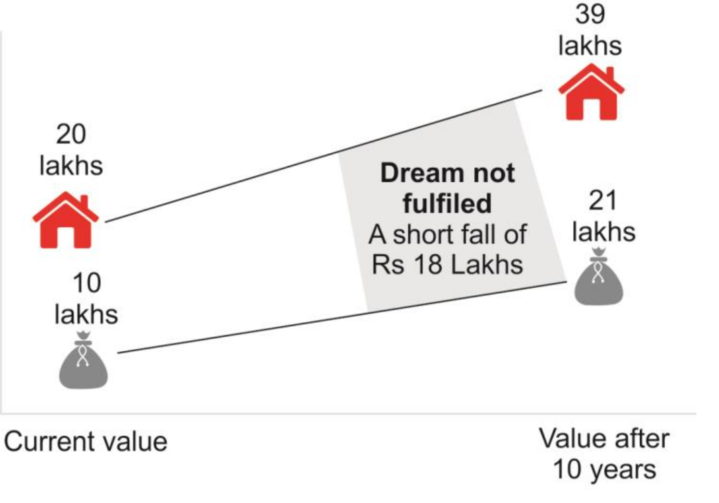
HSBC Global Asset Management

An Investor awareness program initiative

Are you on track to meet your dream goal?

- Nisha wants to buy a vacation home, which costs around Rs 20 lakh at present
- She mobilises her accumulated savings (Rs 10 lakh) in fixed deposits (FDs) for this purpose. She expects the investment, which is noted for capital safety, to help her reach the goal in future
- After 10 years, Nisha's FD investment grows to around Rs 21 lakh* and she feels she can fulfill her dream of buying a vacation home
- But her happiness is short-lived after she realises that the price has risen to Rs 39 lakh^
- Nisha can't buy a vacation home because of paucity of funds (shortfall of Rs 18 lakh)



^ Assuming rise in price at an 7% per annum which is the average CPI inflation rate between 1993 and November 2019
* #Grown at 7.60% represented by 1-year FD index returns between October 1999 and December 2019
For illustration purpose only

Investments are subject to market risk. Past performance may or may not sustain in the future and does not guarantee or assure future returns

Are you prepared to achieve goals on time?

- Like Nisha, we all have dreams. But our dreams may not convert into reality as generally we don't quantify them into financial goals
- Every goal requires proper financial planning, which takes into account various factors including the future cost of goal (which Nisha ignored)
- Below are hypothetical illustrations of various priority and lifestyle goals along with their costs and time horizon

Buying an SUV

Current cost
Rs 8 lakh

Time Period
3 years

Expected future cost
Rs 10 lakh

Foreign vacation

Current cost
Rs 10 lakh

Time Period
5 years

Expected future cost
Rs 14 lakh

Children's education

Current cost
Rs 15 lakh

Time Period
15 years

Expected future cost
Rs 41 lakh

Retirement

Current cost
Rs 1 Crore

Time Period
25 years

Expected future cost
Rs 5 Crore

Note - Assuming rise in price at an 7% per annum which is the average CPI IW inflation rate between 1993 and November 2019

Common mistakes in goal planning

Just as many investors fail to factor in future price rise, there are other common mistakes when it comes to goals and investment planning. Some of these blunders are illustrated below.

Failure to think of the goal as a future cost: Investor wants to buy an SUV three years from now. He believes his salary will rise high enough in three years to be able to finance the car.

Resolution: He must estimate the cost of the SUV in three years and predict whether his savings will be enough. If not, he must invest for this purpose.

Not picking the right asset class: A young investor has just begun his career and wants to kick start retirement planning early. For this, he begins investing his savings in FDs.

Resolution: As the investor is young and is capable at this stage of his career to bear higher risk, he should invest in equity and switch to other safer asset classes later in his career.

Delaying goal planning: Investor wants to build corpus for her children's higher education 15 years from now, which would cost around Rs 40 lakh. She feels she can begin planning for this a little later.

Resolution: Investor should not delay. Assuming that savings can be deployed in an investment that provides 15% annual growth, a person who begins investing today needs to save Rs 5,983 per month compared to Rs 14,534 per month five years later.

The above calculations and potential appreciation of investments are given for illustration purposes only. The illustrative appreciation in investments given above are based on the historic performance of 15% annualized returns of S&P BSE SENSEX i.e. average of daily annualized 15 years' rolling returns of S&P BSE SENSEX as of 31 December, 2019 and since June 30, 1979 (Source: CRISIL).

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Behind every successful goal there's an investment plan

- Traditional approach of investing focuses only on return expectations, and uses returns to meet goals as and when they surface.

- In contrast, goal-based planning is a holistic approach that maps investors' goals to their investments in sync with their risk profile, time horizon, inflation and personal factors such as income, expenses, age and other financial responsibilities.

- The biggest benefit of goal-based investing is that it allows investor to bucket his/ her money according to a purpose or goal.

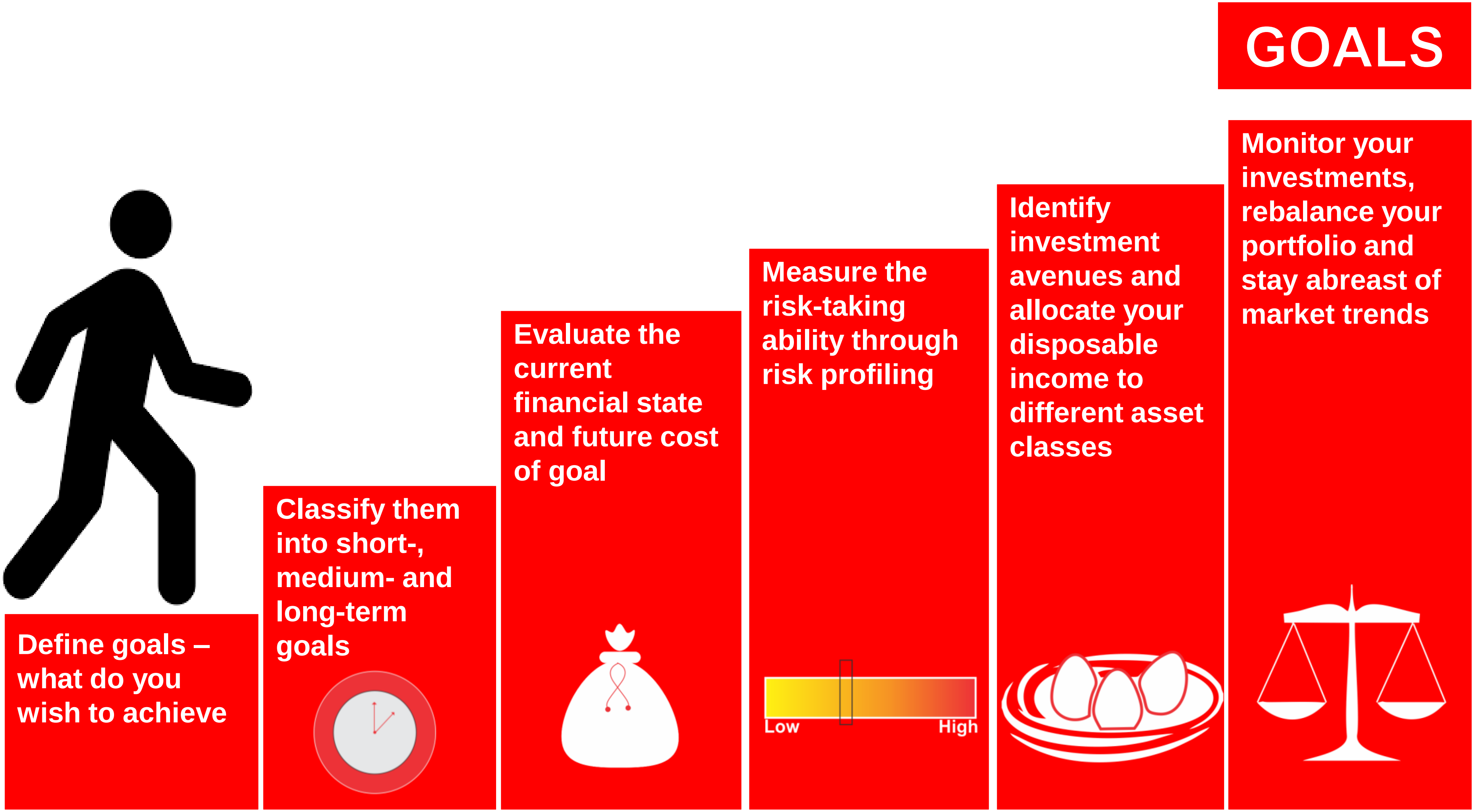
- It increases investor's commitment to goals and helps him/ her measure the progress towards meeting goals.

Did you know?

The global financial crisis of 2008 brought goal-based investing into the limelight, as the steep portfolio losses experienced during this period made investors realise how poor investment performance could set back the attainment of financial goals by considerably long periods.

Source - Crisil

Six steps to achieve your goals



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Goal-based investing – what Nisha should have done

Step 1	Goal identification	Buying a vacation home
Step 2	Estimating the time horizon	To own the house after 10 years
Step 3	Evaluate the current financial state and future value of goals	Consider the rise in house price in future, which would be Rs 39 lakh
Step 4	Measure the risk-taking ability through risk profiling	Considering longer time horizon and a lifestyle goal, she can take higher risk
Step 5	Identify investment avenues and allocate disposable income to different asset classes	She should invest in equity. Buying an equity mutual fund would be a good option
Step 6	Monitor investments, rebalance portfolio and stay abreast of market trends	In 10 years, her equity fund investment could garner Rs 40 lakh*, thereby comfortably achieving the goal

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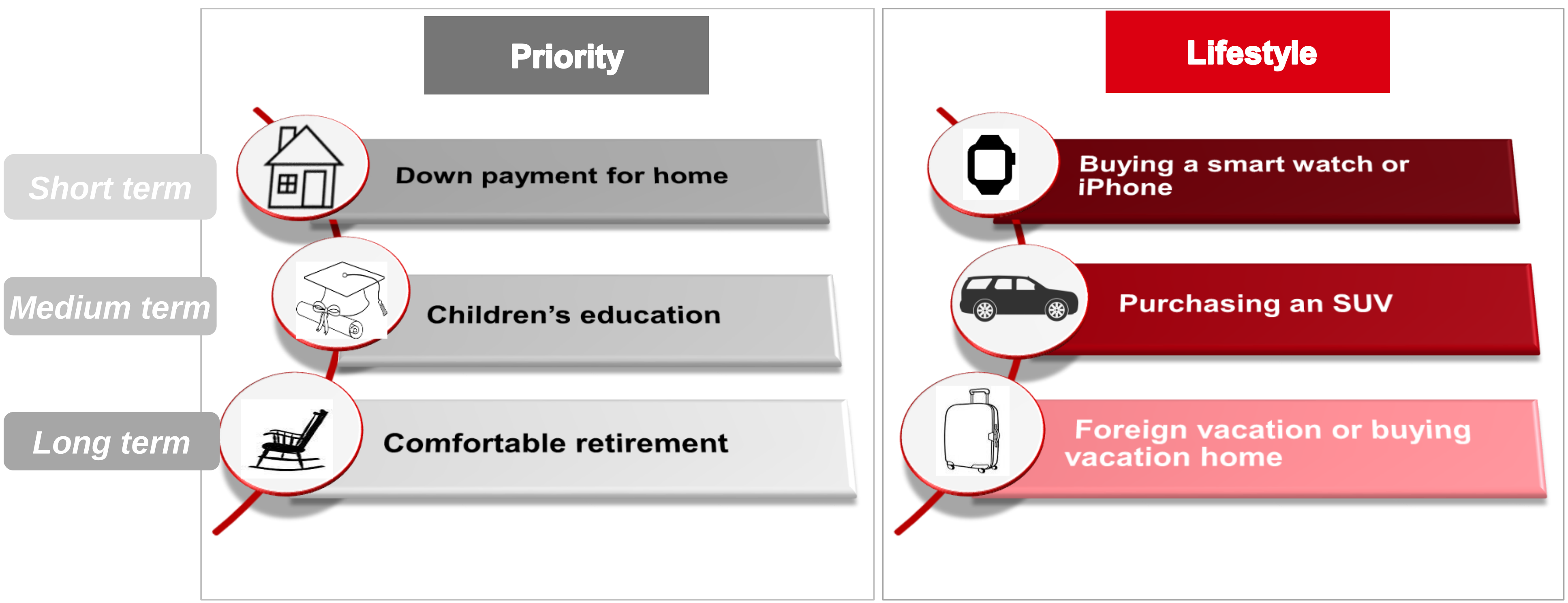
Goal planning process – identify and segregate

- Segregate goals into priority and aspirational – priority goals are essentials and, hence, get precedence over aspirational goals.
- Align your priority and aspirational goals to the time horizon. Some of the common ones across life stages are:



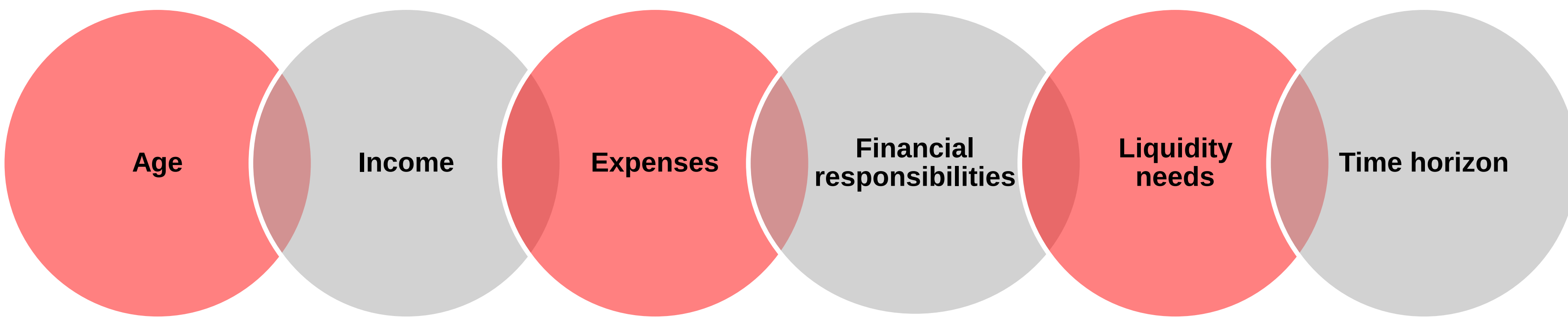
Goal planning process – do your math

- Make a cash flow statement to understand your income, expenses and savings.
- Find out the amount needed to achieve each goal after factoring in inflation.
- This will help you work out the realistic time span for achieving each goal.

Goal planning process – what's your appetite?

- Friends are known to influence our decision making.
- The "peer effect" can also be seen in the investment field wherein you may try to mirror friends'/ relatives' investment strategy.
- But every individual has unique financial needs/ goals and risk profile.
- Risk profile comprises two parts – risk appetite (willingness to take a risk) and risk tolerance (willingness to bear the risk). Both vary among individuals.

Important factors that determine your risk profile



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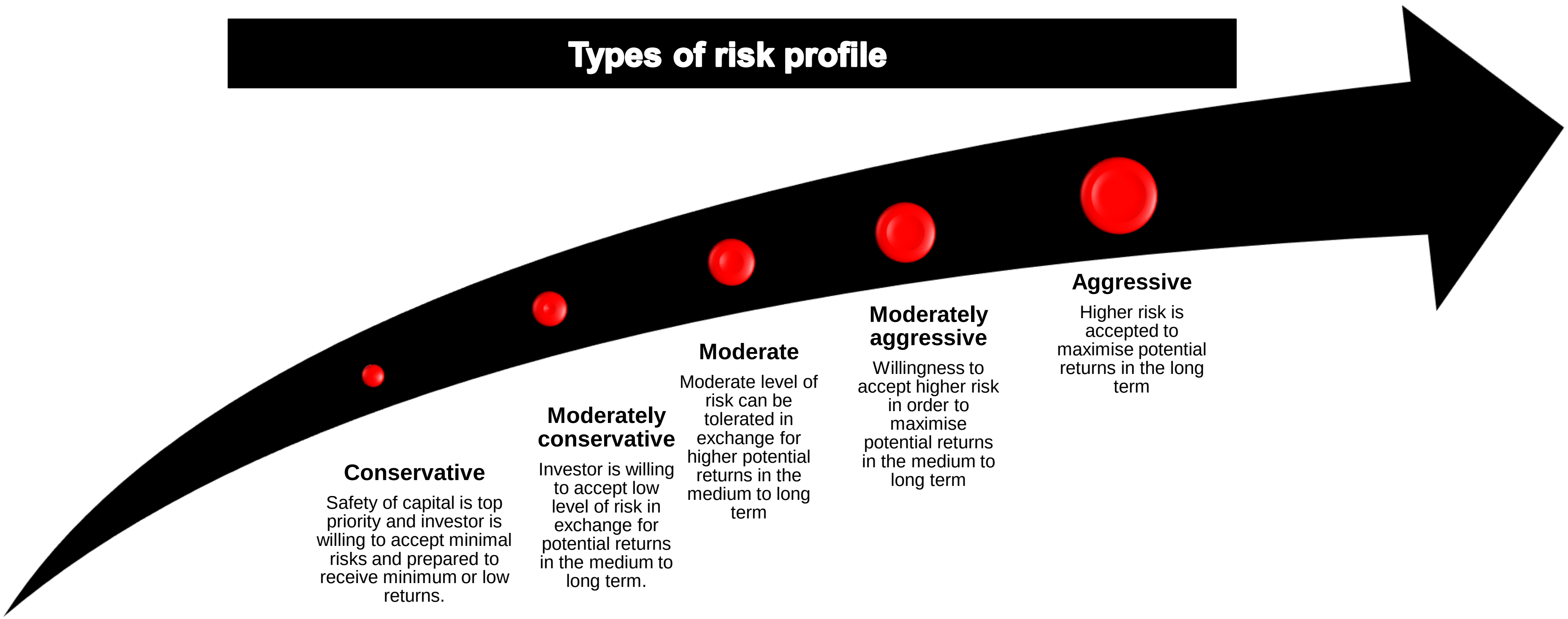
Goal planning process – how much risk can you handle?

- Risk profiling caters to investors assessing themselves on aforementioned parameters, probing their risk appetite and accordingly allocating money to different asset classes.
- A formal questionnaire-based approach is often the best way to conduct risk profiling. Investors have to answer questions that probe their willingness and ability to take risks.



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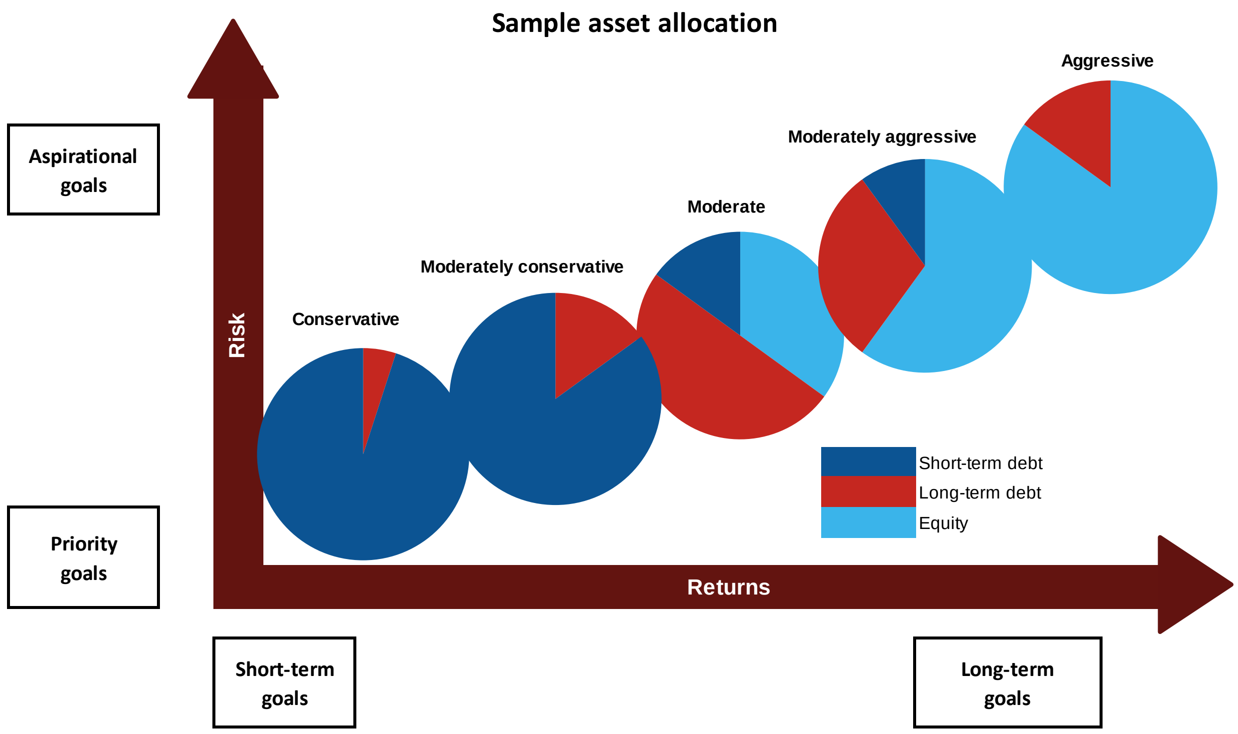
Goal planning and risk profile

- Investments should cover different asset classes (equity, debt and cash) to enjoy the benefits of diversified asset allocation.
- Generally, priority short-term goals may have a conservative portfolio. Priority long-term goals may have a moderately aggressive portfolio and long-term non-essential goals can have a more aggressive portfolio.



For representation purpose only, it may differ on a case-to-case basis

Goal planning process – RR: revisit and re-assess

- Revisit your investments on a semi-annual (six months) or annual basis.
- It is crucial as financial markets are dynamic and the portfolio needs to be modified in sync with changes in the underlying asset class.
- Re-assessment will help you weed out the underperformers and realign investments in line with the asset allocation and risk-return profile.

Mutual funds are a good play for all goals

- Mutual funds are an ideal option to achieve goals as they invest across the spectrum; and are professionally managed; lighter on the wallet; liquid and tax efficient.
- Choice of a mutual fund should be aligned to investors' risk profile, returns expectations and investment horizon.

Investment category	Fund type	Expected returns	Expected risk	Indicative Investment Horizon	Achievable goals
Equity-oriented funds	Large cap equity funds	High	Very High	5 years and beyond	Very Long-term goals
	Diversified equity funds				
	Small and midcap equity funds				
	Index Funds (Passively managed)				
	Thematic / Sectoral equity funds, international funds				
Hybrid funds	Aggressive Hybrid funds	Moderate	Moderate	5 years and beyond	Medium to long term goals
	Conservative Hybrid Funds	Moderate	Moderate	3 years and beyond	
Debt-oriented funds	Fixed maturity plans	Low	Low	30 days to 5 years	Short, Medium or Long term goals
	Gilt funds	Moderate	Moderate	3 years and beyond	
	Long duration funds	Moderate	Moderate	7 years and beyond	
	Medium Duration Funds	Moderate	Moderate	3 years to 4 years	
	Low duration funds	Moderate	Low	Around 6 to 12 months	
	Ultra Short duration funds	Low	Very Low	Around 3 to 6 months	
	Liquid funds	Very Low	Very Low	Less than 90 days	
Others	Exchange traded funds (ETFs)	Moderate	Moderate	5 years	Specific goals (tax savings, jewellery, etc.)
	Fund of funds				
	Arbitrage funds	Low	Low	More than 1 year	
	Equity Linked Saving Scheme (ELSS)	High	High	Lock-in period of 3 years	

For representation purpose only, Mutual fund investments are subject to market risks, read all scheme related documents carefully. Please read the disclaimer at the end of the presentation before investing.

Achieve your goals SIP by SIP

Benefits

- Reduces average price per unit paid through rupee cost averaging
- Makes market timing irrelevant
- Enhances investments as income grows
- Provides compounding benefits
- Instills investment discipline

Illustration – How you can achieve goals by investing in SIP

Goal	Cost	Time Period	Monthly SIP amount required
Retirement	Retirement kitty of Rs 5 Crore	30 years	Rs 7,222
Children's wedding	Children's wedding costing Rs 80 Lakhs	25 years	Rs 2,466
Vacation home	Vacation home costing Rs 75 Lakhs	20 years	Rs 5,009

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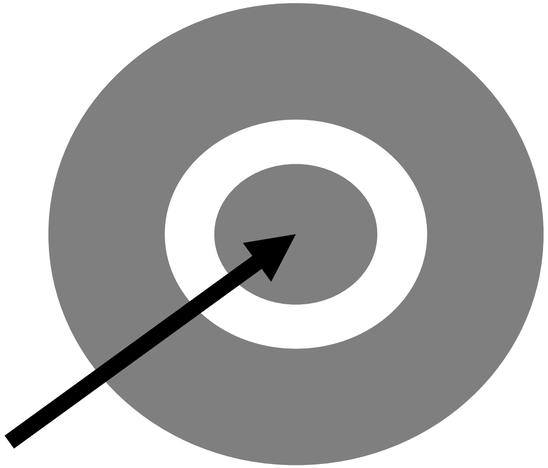
Goal-based investing – key takeaways

- We all have dreams. To turn these into reality, we need to adopt investment planning.
- Often, we are oblivious of our risk profile, our goals, the future cost of goals, etc.
- We need holistic and focused goal-based planning.
- It allows us to allocate money according to a purpose or goal.
- Don’t forgot the six steps of goal-based planning
    - Define your goals
    - Classify them in terms of duration
    - Evaluate your current financial state and future cost of goals
    - Measure the risk-taking ability through risk profiling
    - Identify investment avenues and allocate your disposable income to different asset classes
    - Monitor your investments
- Mutual funds offer a variety of products suitable for all goals.
- SIP in mutual funds is a good and disciplined way to meet goals.



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