Bridge the gap between dreams and reality

Financial planning

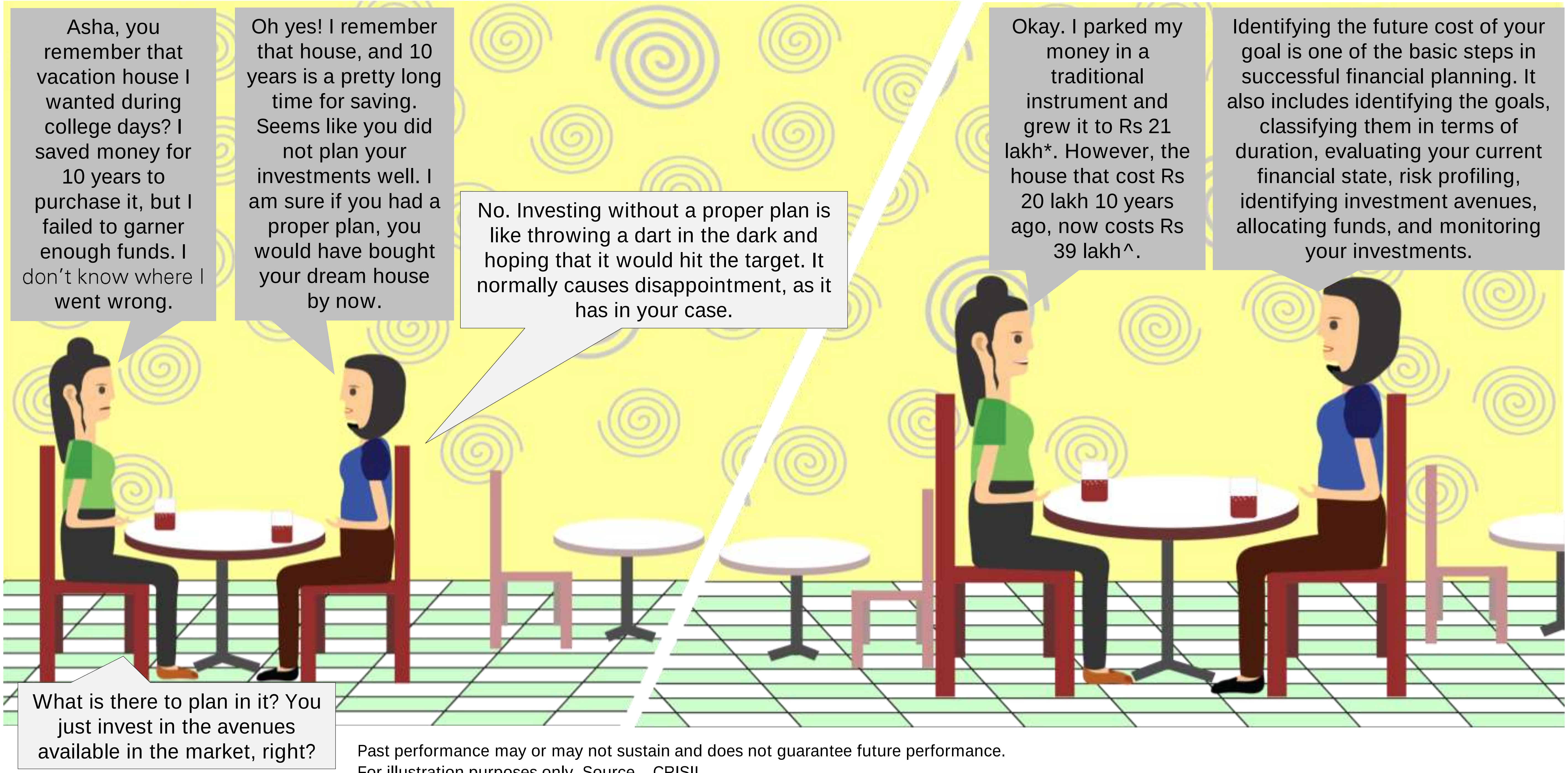
An Investor Awareness & Education Initiative

HSBC Mutual Fund | Opening up a world of opportunity

February 2023

Financial planning: failing to plan is planning to fail

Nisha and Asha meet after 10 years and the topic of finance comes up



Past performance may or may not sustain and does not guarantee future performance.
For illustration purposes only, Source – CRISIL
^Assuming rise in price at 7% per annum, which is the average CPI-IW inflation rate between 1993 and 2022.
*Rs 12,000 per month grown at 7.3%, which is the CAGR returns of 1-year FD index between Jan 1999 and Dec 2022.

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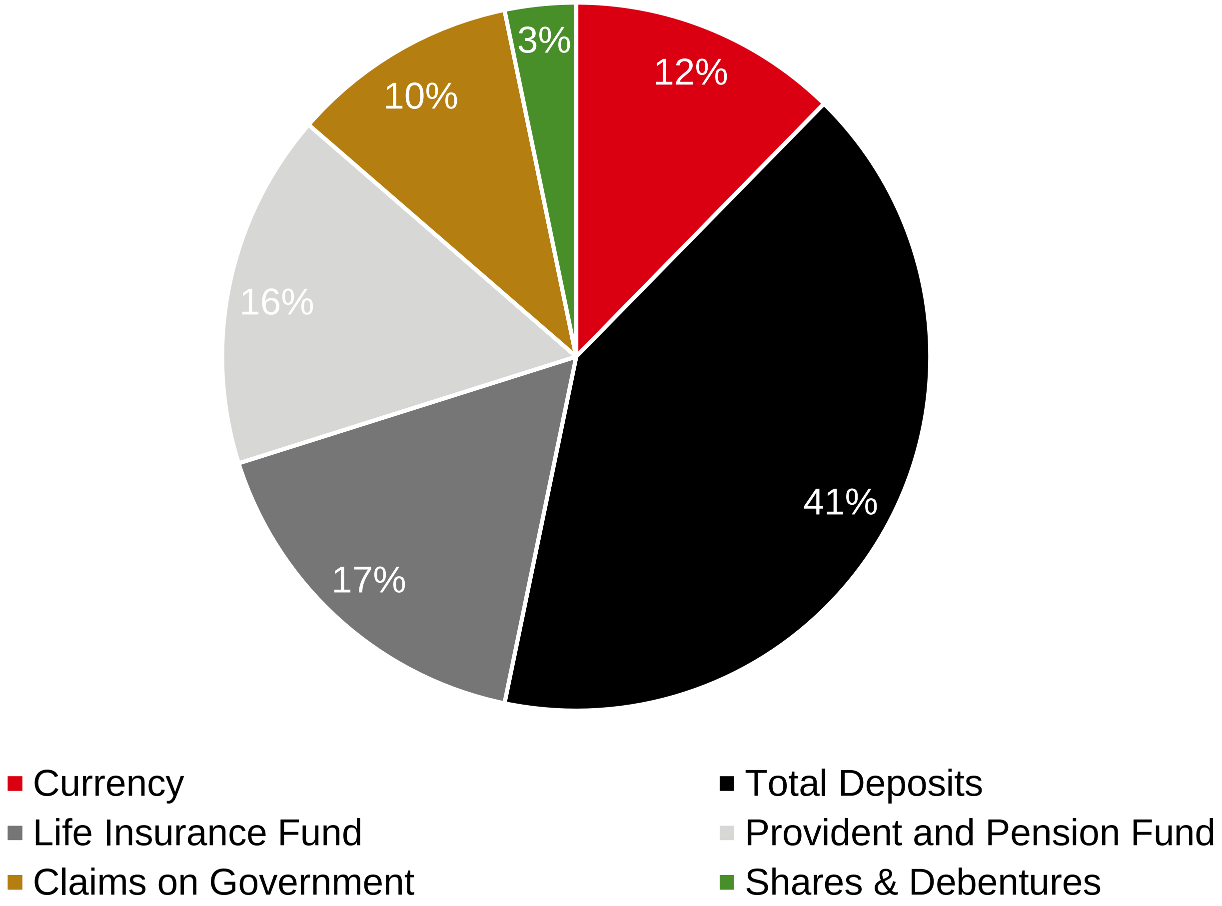
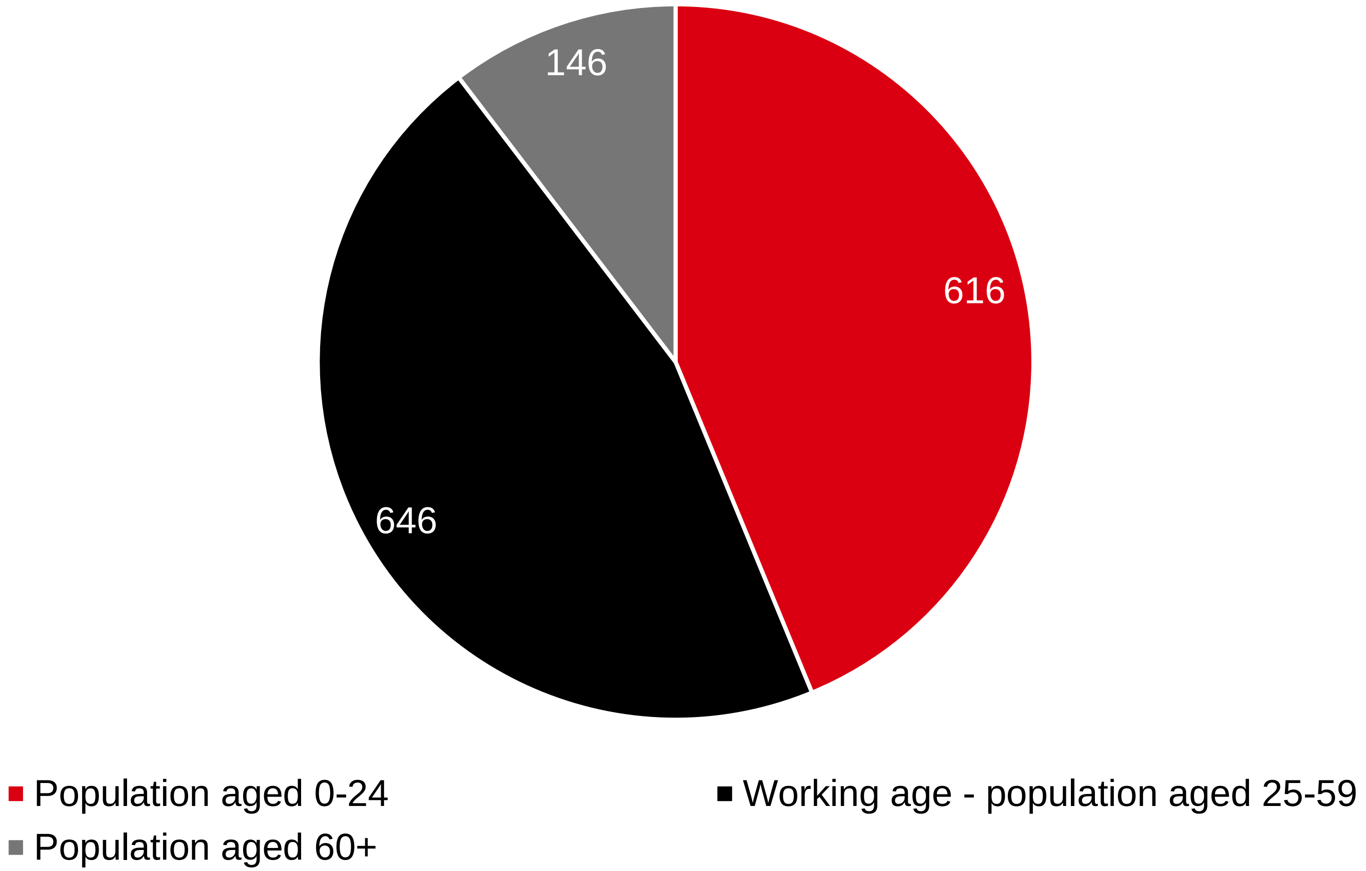
Traditional approach: investments sans a proper plan

- The chart below shows that despite having a large young population, the financial investment pattern of Indian households is skewed towards fixed income

Households savings structure for 2021



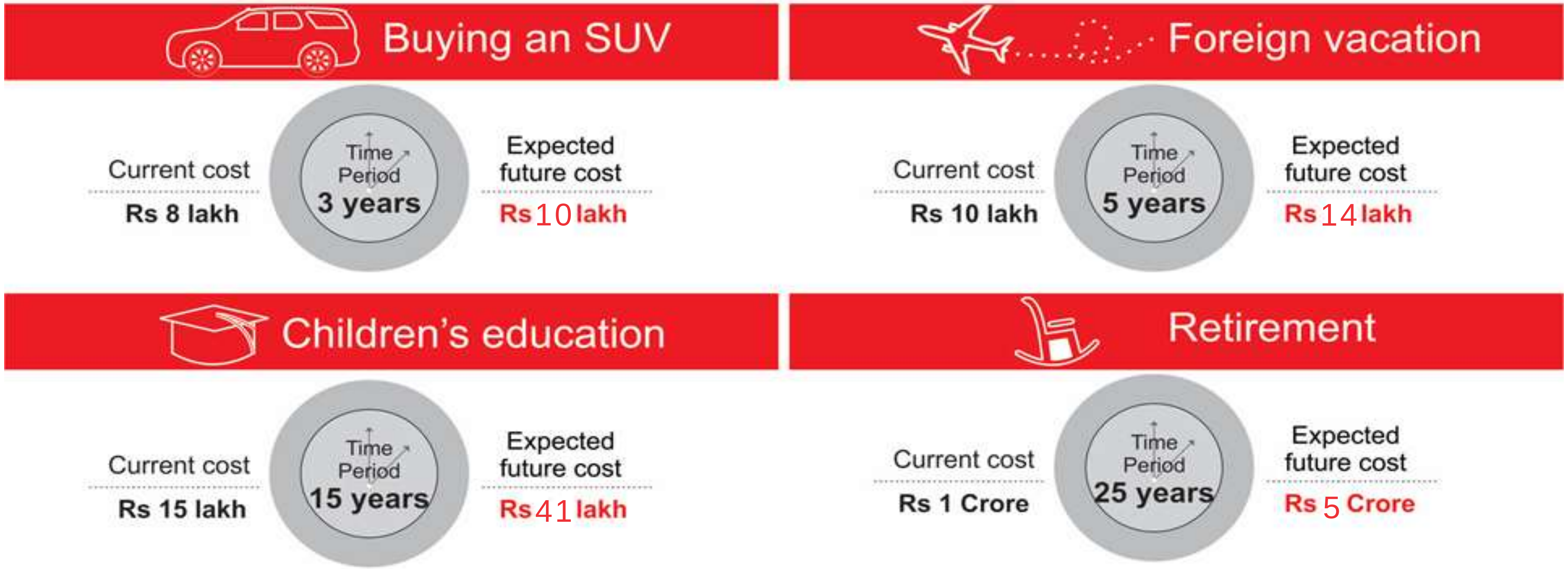
Population estimates for 2021 (million)



Source – RBI, United Nations, CRISIL

Are you prepared to achieve goals on time?

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



Source – CRISIL, Note - Assuming a rise in price of 7% per annum, which is the average CPI-IW inflation rate between 1993 and 2022

Common mistakes in goal planning

Not factoring in inflation is a grave mistake, but there are other blunders as well

Failure to think of the goal as a future cost: Investor wants to buy an SUV 3 years from now. He believes his salary will rise enough during the period to be able to finance the car.	Resolution: He must estimate the cost of the SUV in 3 years and calculate whether his savings will be enough. If not, he must invest for this goal.
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 fixed deposits (FDs).	Resolution: As the investor is young and capable at this stage of his career to bear a 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 ~Rs 30 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 4,488 per month compared with Rs 10,901 per month 5 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 historical performance of 15% annualised returns of S&P BSE SENSEX, i.e. average of daily annualised 15 years' rolling returns of S&P BSE SENSEX as on Dec 2022 and since Dec 1979 (Source: CRISIL).

The value of S&P BSE SENSEX on January 31, 2023 was 59549.9.

Source – CRISIL, Note – Past performance may or may not sustain in the future and it does not guarantee or assure future returns.

Behind every successful goal is 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 investors to bucket their money according to a purpose or goal
- It increases investors' commitment to goals and helps them measure the progress towards meeting goals

Did you know?

The global financial crisis of 2008 brought goal-based investing into the limelight, as 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

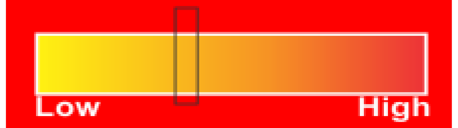
Six steps to goal attainment

Define goals – what do you wish to achieve

Classify them into short-, medium- and long-term goals

Evaluate the current financial state and future cost of goal

Measure the risk-taking ability through risk profiling



Identify investment avenues and allocate your disposable income to different asset classes

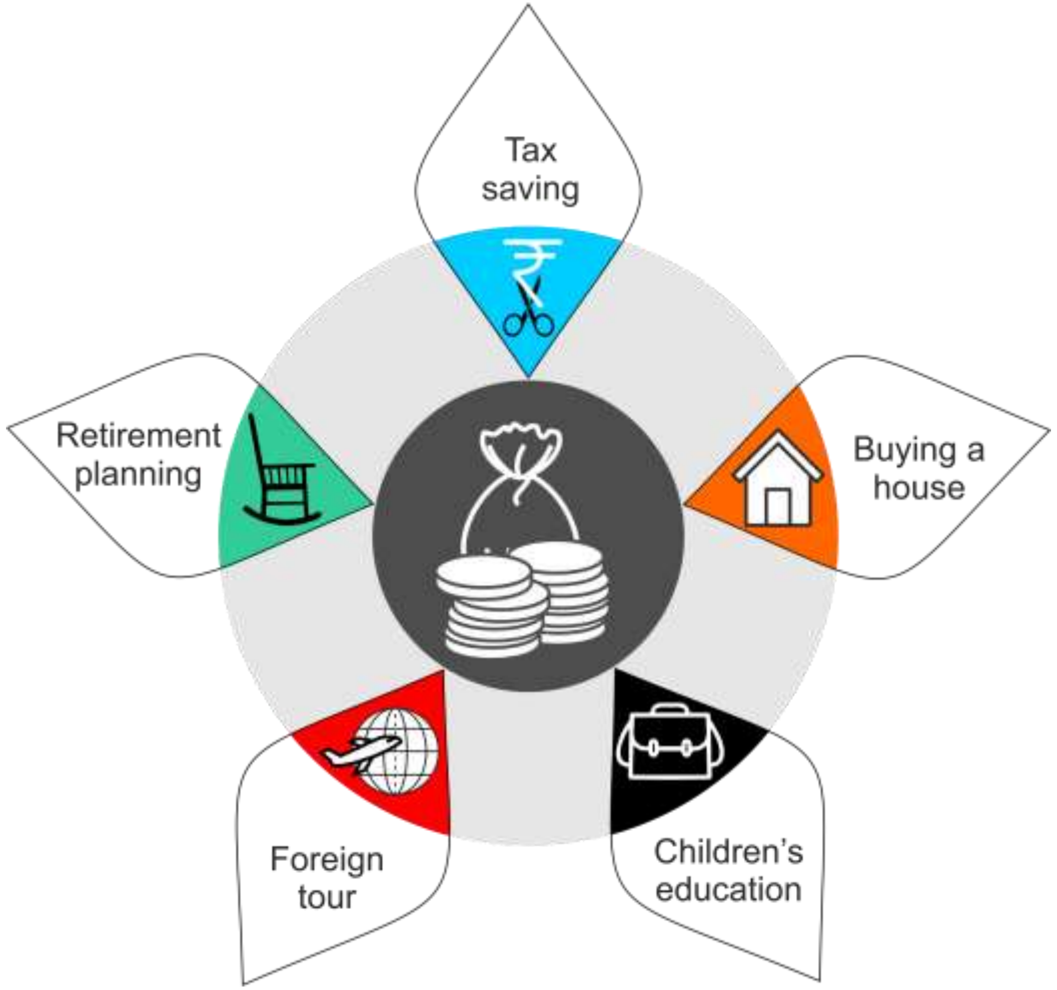
Monitor your investments, rebalance your portfolio and stay abreast of market trends

Goals

For representation purposes only, Source – CRISIL

Goal planning: identify and segregate

- Make a list of all the goals that you want to achieve, such as:



- Segregate goals into priority and aspirational – the former get precedence over the latter, as these are essential

For representation purposes only, Source – CRISIL

Goal planning: classify as per duration

- After prioritising, align the goals with the expected time horizon as per the life stage
- Broadly, goals can be divided into – short, medium and long term
- For instance, goals can be mapped across life stages in this way:

	Priority	Lifestyle
Short term	Down payment for home	Buying a smart watch or iPhone
Medium term	Children's education	Purchasing an SUV
Long term	Comfortable retirement	Foreign vacation or buying vacation home

For representation purposes only, Source – CRISIL

Goal planning: do the maths

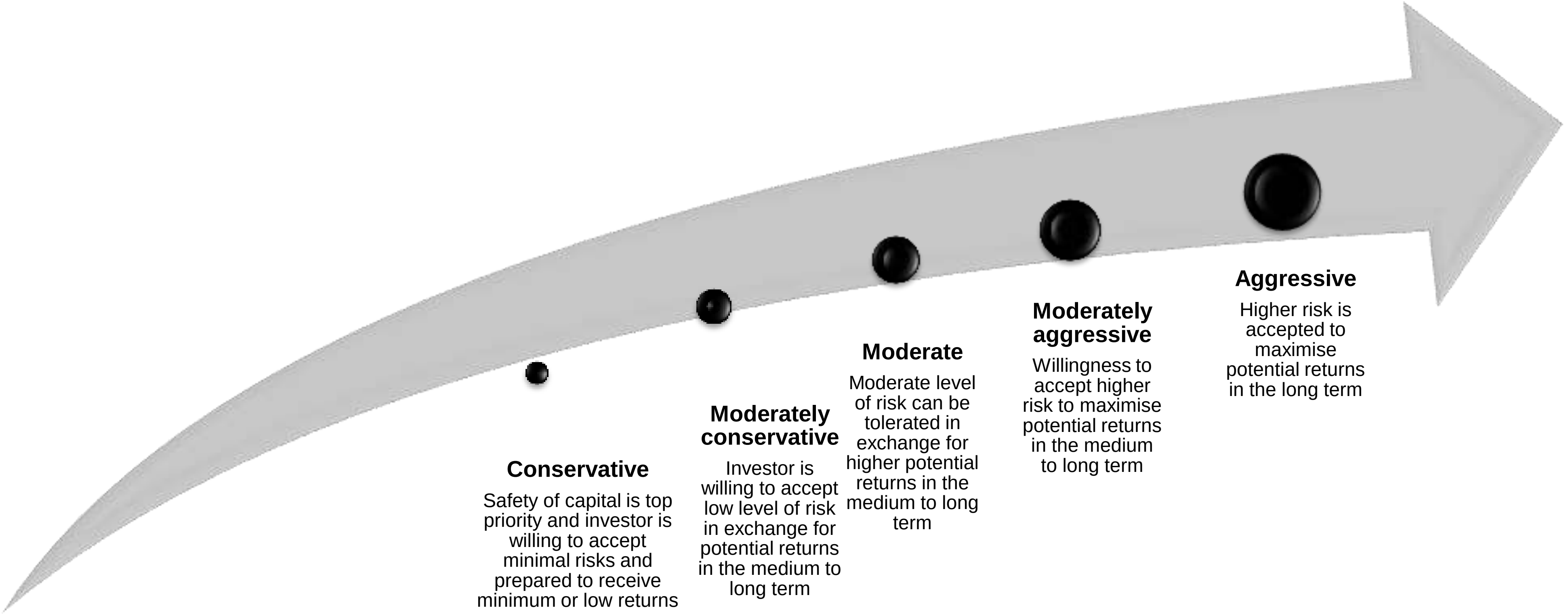
- Make a cash flow statement to understand your income, expenses and savings
- Find out the amount needed to achieve each goal after factoring in inflation
- This will help you work out the realistic time span for achieving each goal

Source – CRISIL

Goal planning: gauge your risk appetite

- Risk profiling caters to investors probing their risk appetite keeping in mind parameters such as age, income, expenses, financial responsibilities, liquidity needs, and time horizon
- 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

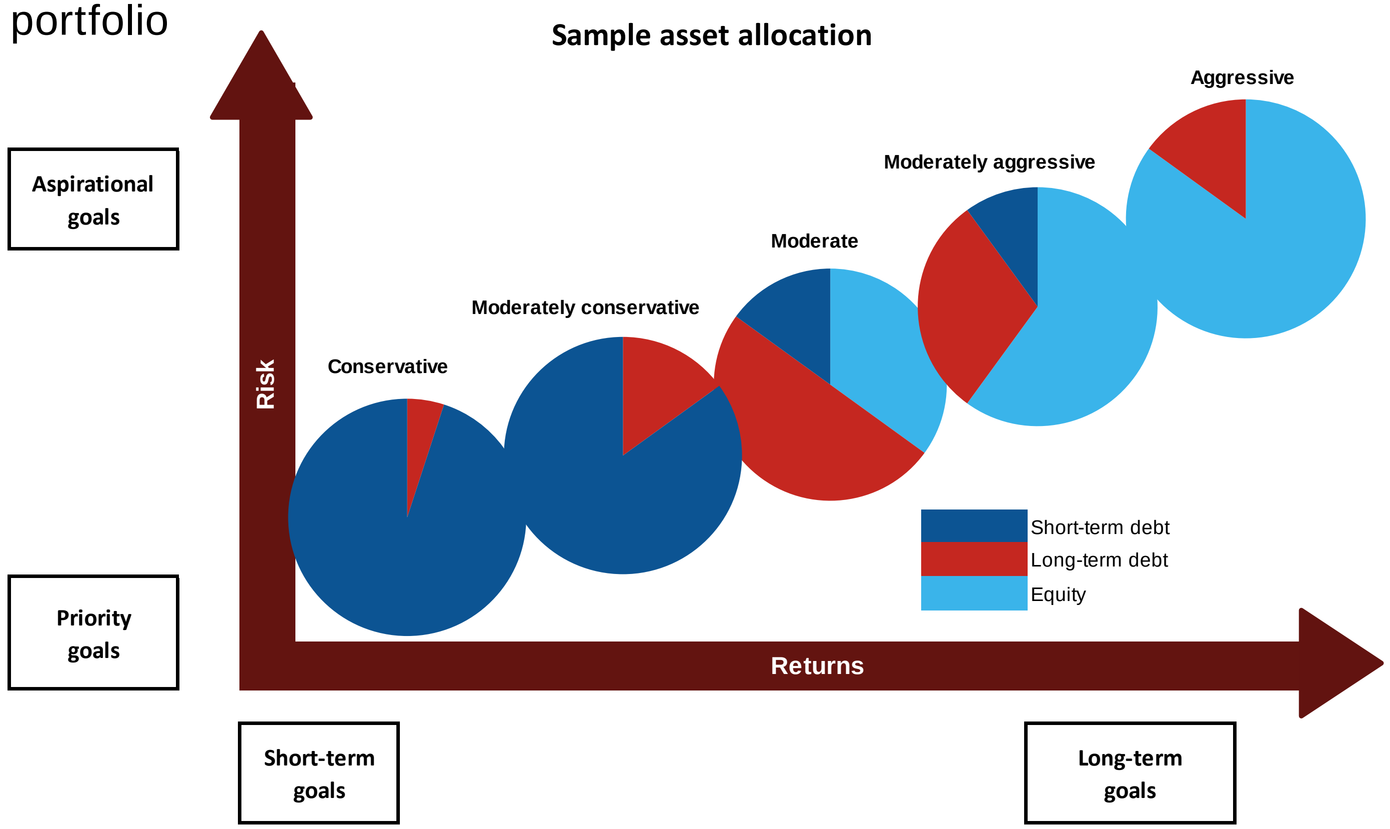
Types of risk profile



For representation purposes only, Source – CRISIL

Goal planning: go for diversified asset allocation

- Once the risk appetite is assessed, the investor should look at putting his/her money in 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, which primarily includes bank FDs/RDs and short-term debt funds such as liquid and ultra-short duration funds
- For priority long-term goals, a moderately aggressive equity-based portfolio should be preferred, while for long-term non-essential goals one can opt for a more aggressive portfolio



(For representation purposes only, it may differ on a case-to-case basis, Source – CRISIL

Goal planning: revisit and reassess

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

Source – CRISIL

Goal-based investing: what Nisha should have done

Step 1	Goal identification	To buy a vacation house
Step 2	Estimating the time horizon	10 years
Step 3	Evaluate the current financial state and future value of goals	Factor in the price rise
Step 4	Measure the risk-taking ability through risk profiling	Take higher risk based on long time horizon and lifestyle goal
Step 5	Identify investment avenues and allocate disposable income to different asset classes	Invest in equities, such as an equity fund
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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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 risk	Indicative investment horizon	Achievable goals
Equity-oriented funds	Large cap equity funds	Very High	7 years and beyond	Very long-term goals
	Large and midcap equity funds			
	Flexi-cap/multi-cap funds			
	Midcap/small cap equity funds			
	Index funds (passively managed)			
	Focused/Value/Contra/Dividend yield funds			
	Thematic/Sectoral Equity funds, International funds			
Hybrid funds	Aggressive Hybrid funds	Moderate	5 years and beyond	Medium to long-term goals
	Conservative Hybrid funds	Moderate	3 years and beyond	
	Balance Hybrid funds	Moderate	3 years and beyond	
	Dynamic Asset Allocation funds	Moderate	3 years and beyond	
	Multi Asset Allocation funds	Moderate	3 years and beyond	
	Equity Savings funds	Low	More than 1 year	Specific goals (tax savings, jewellery, etc.)
	Arbitrage funds	Low	More than 1 year	
Debt-oriented funds	Fixed Maturity plans	Low	30 days to 5 years	Short-, medium- or long-term goals
	Gilt funds	Moderate	3 years and beyond	
	Gilt fund with 10 year constant duration	Moderate	3 years and beyond	
	Long-Duration funds	Moderate	7 years and beyond	
	Medium Duration funds	Moderate	3 years to 4 years	
	Medium to Long Duration funds	Moderate	4 years to 7 years	
	Credit Risk funds	High	3 years to 4 years	
	Low Duration funds	Low	Around 6 to 12 months	
	Dynamic Bond, Corporate Bond, Banking & PSU Debt funds	Low	Around 6 to 12 months	
	Short Duration funds	Low	1 year to 3 years	
	Floater and Ultra Short Duration funds	Very Low	Around 3 to 6 months	
	Liquid funds	Very Low	Less than 90 days	
	Money Market, Liquid and Overnight funds	Very Low	1 day to 1 year	
Others	Exchange Traded funds (ETFs; including gold)	Moderate	5 years	Specific goals (tax savings, jewellery, etc.)
	Fund of funds, Solution-oriented funds			
	Equity Linked Saving scheme (ELSS)	High	Lock-in period of 3 years	
Solution Oriented Schemes	Retirement Fund and Children's Fund	Moderate	7 years and beyond	Long-term goals such as retirement, child's higher education etc

Source – CRISIL,, For illustration purposes 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 (Systematic Investment Plan)

Benefits

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

One SIP at a time

Retirement

Retirement kitty of **Rs 5** crore

Time Period **30 years**

Monthly SIP amount required **Rs 7,222**

Children's wedding

Children's wedding costing **Rs 80** lakh

Time Period **25 years**

Monthly SIP amount required **Rs 2,466**

Vacation home

Vacation home costing **Rs 75** lakh

Time Period **20 years**

Monthly SIP amount required **Rs 5,009**

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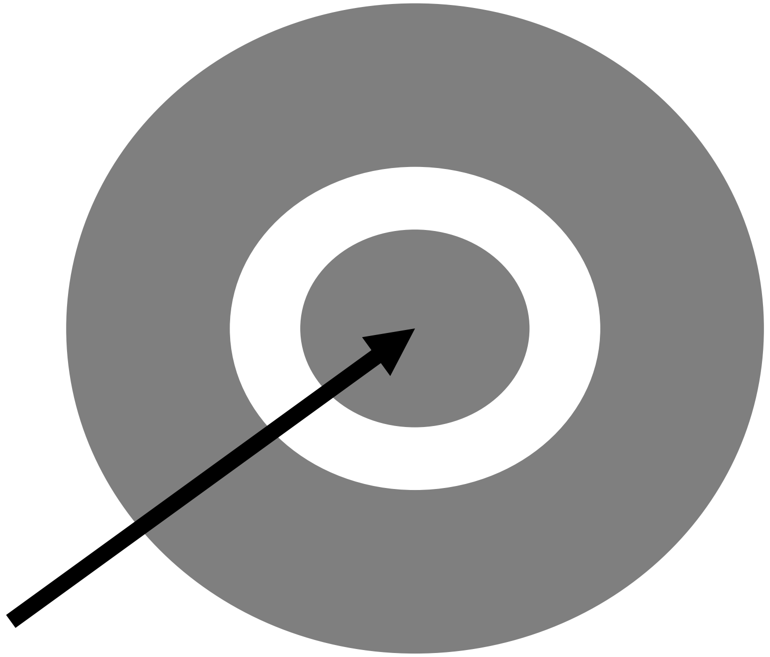
Goal-based investing

- 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 forget the six steps of goal-based planning
  - Identify your goals
  - Classify these in terms of duration
  - Evaluate the current financial state and future cost of goals
  - Measure the risk-taking ability through risk profiling
  - Identify investment avenues and allocate disposable income to different asset classes
  - Monitor the 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



Source – CRISIL

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HSBC Asset Management (India) Private Limited, 9-11 Floors, NESCO IT Park, Building no. 3, Western Express Highway, Goregaon (East), Mumbai – 400 063, India.
Email: investor.line@mutualfunds.hsbc.co.in | Website: www.assetmanagement.hsbc.co.in

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