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How to make investments after retirement

Understand a product before investing in it. Make sure your capital doesn't erode, and grows to beat inflation

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Keeping it simple: Swapan Deb, 62, has invested most of his retirement corpus in Senior Citizens' Savings Scheme and bank fixed deposits. Photo by Indranil Bhoumik/Mint

A lot of the personal finance advice you read is about getting your retirement funds in place, but there is little on how to deploy these once you hit retirement. You may be completely dependant on your retirement funds or you may have some current income from work, but how to use your retirement funds remains largely unanswered.

Your biggest challenge is keeping your money ahead of inflation. "Among the biggest risks retirees take, many times unknowingly, is not investing in instruments that beat inflation, on a post-tax basis. As a result, their income becomes insufficient after a few years as cost of living inches up," said Srikanth Bhagavat, managing director and principal advisor, Hexagon Capital Advisors Pvt Ltd, a Bengaluru-based investment advisory company.

Here's a look at the things to keep in mind when investing post retirement.

Regular income flow

As majority of individuals in this age bracket stop earning, it becomes a priority to ensure a source of regular income and have investments that are more liquid to meet any untoward emergency. Long-term investments, such as the Public Provident Fund (PPF), become unviable. Senior Citizen Savings Scheme (SCSS), meant only for the retired, is a government guaranteed scheme where one can deposit anywhere between `1,000 and `15 lakh and earn an interest of 9.3% per annum. It has a lock-in period of five years that can be further extended by three years. The investment is exempt from tax under section 80C of the Income-tax Act, 1961, but the interest payment, paid quarterly, is taxable.

Swapan Deb, 62, is a retired senior executive from the Reserve Bank of India's (RBI) office in Delhi and is now settled in Kolkata. Even though he gets a pension, he wanted to have regular income and also some money to meet little expenses. "I have invested majority of the lump sum I received on retirement into SCSS and fixed deposits (FDs). I have spaced out my investments in such a way that I receive my interest payment every month," he said. When asked why he didn't invest in other higher interest earning segments such as mutual funds, Deb said that his FDs are with the bank where his wife works and due to the ease of transactions there, he prefers keeping the money there. Also his health cover is provided by his organisation, so the earnings are sufficient for him.

A lot of seniors are apprehensive of taking risk with their retirement corpus and lose out on capital due to inflation.

"Clients have spent most of their life earning it (money) and thus must take precautions to preserve its value post inflation. Therefore, investments should be made be across assets which enhances wealth and also makes returns more predictable. Further, besides having allocation towards safe debt products which caters to cash flow requirements, one of the mistakes made is avoiding equity-oriented investments," said Ashish Shanker, head, investment advisory at Motilal Oswal Private Wealth Management Ltd.

Experts that Mint spoke to are of the opinion that although regular income is a priority for retirees, they have to choose wisely and ensure that the portfolio has a mix of debt and equity, and that they keep the risk level low.

And when investing in mutual funds, one may focus more on funds investing in large-cap companies instead of small- or micro-cap companies, as these come with high risks even though they give higher returns.

According to Bhagavat, an ideal retirement fund should consist of 70% debt and 30% equity. "Retirees think they are taking risk by investing in equity, but I think the bigger risk is not investing in equity. However, one should limit their exposure to 20-30% in equity, ideally through mutual funds to own an inflation beating portfolio," he added.

Annuity schemes, where one invests a lump sum and gets a stream of income at regular intervals until death or the end of tenure, are also popular. The corpus at the end of the accumulation phase will be paid out in two parts—one-third as lump sum, with the remaining being converted into annuities. However, as the interest paid is locked for life, it fails to beat inflation with time.

“Annuity investments are a good option for a part of the portfolio to cover longevity risk. But considering that the returns are taxable, does not adjust for inflation and principal normally not easily accessible, there is a need for annuities to be only a small portion of the portfolio. Cash flow needs can be covered through a combination of rent, dividend, interest income and systematic withdrawal plans (SWP),” said Vishal Dhawan, founder, Plan Ahead Wealth Advisors.

One can also put a portion of their portfolio into bonds and plan an SWP. The SWP is a withdrawal strategy wherein a fixed amount can be withdrawn from the portfolio every month; the remaining stays invested. The usage of the portfolio becomes more efficient and there is lower tax impact due to the SWP effect. The withdrawal must be planned in such a way that it increases every year with inflation and it does not deplete the corpus too quickly. “The withdrawal amount should be calculated in a way that the life of the corpus is more than the life expectancy of the investor and the spouse,” said Bhagavat.

You can also choose from post office monthly income schemes (Pomis) and such schemes offered by mutual funds (i.e., MIS). “Here, a lump sum is invested in various instruments to provide the monthly income. Pomis comes with an interest rate of 8.4% per annum, payable monthly and the maturity period would be five years,” saidAnil Rego, founder and chief executive officer, Right Horizons, a financial advisory. However, do keep in mind that these schemes do not enjoy tax breaks, and the interest income is taxable at the marginal rate.

Liquidity

Post retirement, medical expenses gradually become a part of your monthly expenses. Other expenses such as vacation, motor insurance and home equipment depreciation and replacements, also tend to come up so it’s important to keep money in hand. Thus, investments with long lock-in period should be avoided.

“One of the biggest mistakes that clients commit is that in order to keep their accumulated money safe, they tend to go for long-term schemes, without considering inflation. These are not tax efficient and also affect liquidity,” said Hemant Rustagi, chief executive officer, Wiseinvest Advisors. He said at this age, it is important to invest in a manner that you have money available at all times and the investments don’t compromise on your capital and inflation.

Sardari Lal Doda, 70, a retired banker from Delhi who is now settled in Chandigarh, has been investing in PPF for the past 40 years. “I am finally closing my PPF account this year, as at this age I want more liquid cash,” he said. He plans to put a chunk of the matured amount in bank tax-saving FDs and invest some in debt. He has a very small portion of investments in equity.

Asset-based investments

Post-retirement investment decisions are directly linked to your financial goals and need to be regularly assessed to see if they are in line with each other.

“How much one invests in a particular instrument is completely based on how much corpus she has accumulated for retirement. One can broadly invest 15-20% in equity investments but don’t take risks without understanding the product,” said Achin Goel, head, wealth management and financial planning, Bonanza Portfolio Ltd.

Also, don’t forget to keep a contingency fund for medical emergencies and check-ups.

Awareness

Siddhartha Pradhan, 63, is a retired medical officer with the central government health scheme and is currently working as a medical consultant with the RBI in Kolkata. He has been tracking mutual funds and the stock market since his early 30s and continuously invests in mutual funds, direct equities and equity-linked savings schemes. “I am not a man of finance but I have always gathered information on understanding it. Retired people often don’t think about inflation-adjusted returns. We are sceptical of falling markets and interest rates, but it’s a cycle and it (rate increase and decrease) changes every 5-7 years,” he said. He has 15 systematic investment plans of `2,000 each and invests in direct equities as well. And for his retirement corpus, he has invested `15 lakh each in SCSS in both his own and his wife’s names.

Sudipto Roy, managing director, Principal Retirement Advisors Pvt. Ltd, said the company, which imparts training on retirement planning and doesn’t suggest a product as such, found out that people consider equity-related investments as a “negative” thing and often prefer simpler investments.

"It is important to create awareness among the elderly about diversifying their money. Medical inflation is higher than food or other price-based inflations and they (senior citizens) tend to forget it completely. So, it is important to follow the keep-it-simple rule while dealing with the retirees," said Roy.

Mint Money take

Most retirees stop earning post-superannuation. They want to pursue a hobby or travel every year. Thus, regular income is important but when you are investing your life's earnings, don't opt for an investment instrument without understanding it. Make sure your capital doesn't erode and grows to beat inflation. When investing, see if the returns are taxable and how easily you can access the money when needed.

Retired life is supposed to be the golden period of our lives, and if we manage our money with some rules, we will be able to enjoy it as well.