How to make a sound financial plan that can help you reach all your goals

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The impact of the COVID-19 pandemic on our cash flows due to job losses and demise of loved ones in the family, has been felt by many of us and has exposed those without a financial plan.

Over the past decade, financial planning has gained importance. You can either seek an expert for your financial planning exercise or do it yourself. But there are steps involved in making a healthy financial plan.

Ask: What am I saving for?

The first step is to have clearly-defined financial goals. You could have a single or multiple goals, depending on where you stand in your life cycle. A millennial with a first job may have just one goal: to save for post-graduate education. A family would, typically, have many goals at the same time: funding children's education, buying a house, planning for retirement and so on.

FUNDING YOUR HOME LOAN DOWN-PAYMENT

Current age (years)	30
Current Net Take Home income (p.m.)	Rs 40,000
Current Property Cost	Rs 50 lakh
Property to be purchased at age (years)	35
Net Take Home Income after 5 years	Rs 64,420
Property Cost after 5 years	Rs 73.47 lakh
Maximum Loan EMI possible after 5 years	Rs 38,700
Maximum Loan Amount possible after 5 years	Rs 54.76 lakh
Down payment amount required after 5 years	Rs 18.71 lakh
Fixed monthly amount required to be invested over the next 5 years	Rs 24,200
Monthly investment amount, increasing by 5% p.a., required over the next 5 years	Rs 22,100

Expected growth in income and property cost 10% p.a. and 8% p.a., respectively.

Source: Tru-Worth Finsultants

Tivesh Shah, Founder of Tru-Worth Finsultants, gives an illustration. Say, you wish to buy a house in five years. You are 30 years old now, your take-home salary is Rs 40,000 a month, and the property that you wish to buy costs Rs 50 lakh. Shah calculates that at the rate at which the property's price would rise – as would your salary – you may have to make a down payment of Rs 18.71 lakh after five years. How do you get there? Invest, he says, Rs 24,200 every month over the next five years. Or, in the first year, invest Rs 22,100 and then increase your monthly

investment by 5 percent from the second year onwards, once annually (refer to the graphic). Remember: you would also have to take a home loan later and pay EMIs.

The loan is assumed to be taken for a tenure of is 25 years at an interest rate of 7 percent. Now, the EMI to income ratio considered by financial institutions is 60 percent, and expected returns on investments are 10 percent p.a. and increase in investment amounts is assumed at 5 percent p.a.

How much risk can you actually take?

One of the most important aspects of financial planning is risk profiling. "Avoid investing haphazardly in risky products that could ruin your finances," says Renu Maheshwari, a SEBI-registered investment advisor, CEO and Principal Advisor at Finscholarz. Analyse your risk-taking capacity by answering a set of questions online or with your financial advisor. It will help you understand your risk appetite.

Through risk profiling, a financial advisor can determine your emotional and financial risk tolerance, as well as the risk perception. "Formulating the risk-profile of the investor helps the financial advisor in deciding the debt-equity mix to be incorporated in the portfolio, which investments could achieve the financial goals within the timeframes and risk levels," says Shah.

Manage your cash flows well

Get a clear understanding of the cash flows that you have, from your regular salary and other sources such as rental income and royalty. Most of the investors are much behind the basic goal of building the emergency corpus for six months of expenses, because they use credit products to maintain cash flows. Avoid converting your monthly purchases on credit cards to equated monthly instalments (EMIs) because interest rates on credit cards are higher. You could end up in a debt trap. Do not overspend, analyse the monthly expenses and restrain yourself within the allocated budget.

"These days, millennial investors are using credit products to manage cashflows. For instance, they swipe their credit cards for necessities towards the end of the month or apply to a fintech for personal loans to holiday. These are risky tools being used to manage cashflows," says Uday Dhoot, Partner at VennWealth.in and Founder of OyePaisa.com. "If you cannot take care of short-term cash flow requirements, your long-term planning fails," Dhoot adds.

Get your inflation right for various expenses

Things get expensive over time. It's called inflation. "But, it's incorrect to assume one rate of inflation for all your needs. Costs of some items go up more than others," says Shah.

At the same time, you have to be conservative about saving up for expenses that are largely non-negotiable – your children's education and medical expenses, for example. You must assume a higher inflation for such heads because you want a bigger corpus when you reach your goals. Therefore, you save some more, every month.

Financial planners typically assume grocery items to increase 8 percent every year, education costs to rise by 10 percent, medicines, tests and doctor consultation costs to surge by 12 percent every year.
Review the financial plan and portfolio

Don't just make your financial plan and forget about it. Review it occasionally. Are you nearing your goals or straying away from them? "Any changes in the investor's life situation, for instance, a baby's birth, inheritance etc. will affect the financial plan," says Maheshwari.

The equity and debt markets are volatile, and so you must rebalance your portfolio from time to time. "Your investment portfolio checks might happen more frequently, may be every three or six months," says Vishal Dhawan, CEO & Founder, Plan Ahead Wealth Advisors.

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