AU COURANT HOUSEHOLD INVESTMENTS PLANNING AND EXECUTION MODELING

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ABSTRACT: ***Pecuniary affairs in any Indian household can be thought of as excess of income over their expenses or vice versa. A household cannot afford to lag in the latter scenario for an elongated period of time. Sooner or later it must elevate itself to that of the former category. Surplus remaining after meeting all financial outlay is treated as savings. Many households, for want of robust pecuniary planning, channelize their savings into restricted avenues of bank deposits, gold and jewelry which results in paltry earnings, leave alone capital appreciation. Consequently, they tread a rough financial terrain during their life time devoid of hailing entertainment activities and healthy financial relationships with family members and fellow beings. Only a few seek the help of dexterous financial connoisseurs. Even such professionals fall short of fulfilling the ever varying demands of the households living in the contemporary dynamic financial realm. The present study enlightens the household on the subtleties and techniques of household investment planning and execution, and endeavors to throw open to them the fascinating investment world with its nuances and intricacies carrying high potential for exalted returns and suggests live financial modeling tailored to their varying needs after considering their time horizon and risk appetite for various investment avenues.***

Keywords: *Household pecuniary planning, Implementation process, Financial modeling.*

INTRODUCTION

Consumption and savings in any Indian household is contingent upon the income it manages to earn. Excess left out after consumption results in savings which in turn is channelized for investments. If the income falls short of their consumption needs, either they attempt to down size their consumption or borrow to make both ends meet. This situation cannot continue for long as the household may be completely drowned under the obligation of financial burden in the form of servicing the debts. The household should contemplate enhancing their earnings so has to see a surplus for investment. Conventionally, a majority of Indian households park their funds in gold coins or jewelry, bank deposits to be ultimately utilized for meeting children's education and marriage, post retirements pecuniary requirements, cars and a own land or house to dwell. They mostly turn a blind eye to other avenues like equity, debt, bonds, mutual funds, commodity market, real estate, etc. The present study endeavors to throw open to them the fascinating investment world with its nuances and intricacies carrying high potential for exalted returns and suggests live financial modeling tailored to their varying needs after considering their time horizon and risk appetite for various investment avenues.

RESEARCH GAP

Majority of the available literature concentrates on financial modeling for big investors and corporates. There seems to be no financial modeling suggested for Indian households who are good savers in small amounts. The present study seeks to address this gap by suggesting and evaluating financial modeling designed for Indian households so has to enable them to materialize their pecuniary ambitions. Steeped deep in Indian culture and owing to encouragement extended by Governments, Indian households save to their might, though in meager amounts. But since they lack acumen in deploying their hard earned money in well thought off robust investment avenues or portfolios, they generally fall short in actualizing their pecuniary ambitions in their life time. This study addresses this issue and endeavors to instill in them the nuances involved in making smart investments in tandem with their risk appetite and the time span envisaged for achieving their life-time pecuniary ambitions.

OBJECTIVES OF THE STUDY

1. To understand household financial situation and contemporary financial planning process

2. To identify the financial goals

3. Evaluate financial modeling of households proposed to materialize their pecuniary ambition.

LIMITATIONS OF THE STUDY

The study excludes derivative instruments and trading in commodity markets which requires poignant financial acumen. As these pose above the reach of the majority of Indian households, they have been omitted from this study.

DENOTATION OF HOUSEHOLD PECUNIARY PLANNING

Household pecuniary planning is a continuous act of planning and managing one’s economic affairs to materialize and maintain financial satisfaction throughout one’s life which also encompasses smooth transfer of garnered wealth to heirs, thereby ensuring mental and emotional tranquility when one is in the twilight of his or her life.

As each household operates in a different financial predicament, there can be no common household plan which will satiate the varying, sometimes divergent, needs of individual unique households. Each household pecuniary plan needs to carefully drafted taking into account their unique financial operational environment, their risk appetite, financial discipline and obligations, staggered financial requirements spread across a reasonable period of time. It greatly reduces the inevitable financial uncertainty. Without an effective financial planning one is tossed up and down and across like a leaf in the wild financial ocean.

COMPREHENDING FINANCIAL SITUATION

Financial preparation enables a household have passable earnings or resources. This may be in excess of present and prospective spending s and needs in the future. Earnings mainly originate from: (1) Primary Source: This is earnings from occupation or commerce or vocation (2) Secondary Source: This originates from possessions like rentals from tangibles, yields from money kept in bank custody and debentures, returns from equity holdings and units. Surplus earnings of primary source after meeting all consumptions expenses will lead to create the secondary sources income by way of prospective investment strategy. Large investment such as real estate, buying a car, etc. is not amenable to being met out of primary sources of earnings but requires leftover surplus aggregated over a staggered interval. Customarily they are procured from private resources and borrowings. Such borrowings need to be served from both present and prospective cash inflows in the future.

SIGNIFICANCE OF HOUSEHOLD FINANCIAL PLANNING

1. Cash flow estimation: This is crucial for pecuniary planning as it highlights the anticipated inflows and outflows per month to determine the surplus or otherwise and to take steps as warranted.

2. Ensuring positive net worth: Pecuniary planningis done to ensure the household's assets are greater than their financial liabilities and obligations. Households having positive net worth are looked upon while those with negative net worth are looked down.

3. Assuring financial security to the whole family: This is required to protect the family members from health hazards by opting for various plans devised for varying purposes. This entails outflow of money in the form of premiums which once has to essentially rope in their financial planning.

4. For peaceful post-retirement life: Financialtrauma in the post-retirement period can be averted to very large extent through robust pecuniary planning. It gives a blueprint for leading tranquil post-retirement financial life without relying upon others for funds.

5. Effective tax planning: This is another benefit which flows from effective financial planning. This leads to informed reduction in tax burden. It should be noted that avoiding tax payment is illegal but minimizing tax is legal.

6. Tailoring investment modes and techniques to the needs of individual households: Financial planning takes into account one's risk appetite, investment time horizon, present and prospective future expenses and anticipated financial obligations and selects investment avenues accordingly and tailors appropriate financial modeling to match the needs of the individual household.

7. Wealth creation: Pecuniary planning helps not only in effecting savings but also aids in channelizing them across well-thought out investment avenues so has to lead to wealth creation for the household. Savings alone will not lead to wealth creation unless accompanied by intelligent act of investment.

8. Keeping up with the dynamics of the investment world: Annual review of one's financial planning will enable one to evaluate as to where they stand financially and what needs to be revised or modified to be back on track for materializing pecuniary ambitions.

9. Ensuring smooth transfer of wealth to heirs: Effective pecuniary planning enables one to pass on their hard-earned wealth to their heirs in a smooth and hassle freeway in the form of will creation. This ensures mental and emotional tranquility in the twilight period of one's life.

10. Enhanced quality human relationship: It is a common tiding that a majority of misgivings and misunderstandings stem from financial dealings. A robust pecuniary planning helps one to establish and maintain good financial relationship with near and dears and other fellow beings.

TAILOR MADE PECUNIARY PLANNING PROCESS FOR INDIAN HOUSEHOLDS

Though there cannot be a common household financial plan for all households, yet one can list a procedure that can be adopted and adapted by all Indian households. Such a procedure entails the following steps:

1. Assessing one's prevailing financial standing: This is done with respect to one's income, expenses and savings. A list of one's assets, debts and other financial obligations or liabilities constitutes a solid base for effective pecuniary planning.

2. Chalking out specific financial objectives: Financial goals must not be vague, like "I want to make lot of money". It must be in clear cut and specific terms in order to make financial planning effective and efficient. Such goals vary from spending all income through effective savings to intelligent deployment of savings in various well-thought out investment avenues for desired time frame in tandem with one's risk forbearance to wealth creation for financial security.

3. Spelling out different alternative action plans for achieving household's pecuniary ambition: It is a common adage that an objective can be achieved in multiple ways. So a household must list out all alternative action plans he can possibly conceive to materialize his pecuniary ambitions. Possible alternative action plans can be generally categorized as follows:

(a) Pull along with the existing course of action

(b) Enlarge the current predicament

(c) Reasonably modify the existing course

(d) Chalk out an altogether new action plan

Individual households must introspect to find out in which category they fall and act accordingly.

4. Weighing all the alternative action plans: This is done with reference to one's risk appetite, time horizon for investment, financial goals, personal perceptive values, financial market conditions, stage of life one is presently in, one's financial acumen, decision making ability, whether one wants to be a passive or active investor and the opportunity cost involved.

5. Finalize a financial action plan and put it into practice: Implementation may be staggered or implemented all in one go depending upon the prevailing situation. Post-implementation monitoring and measuring mechanism should be a part of all implementation plans envisaged. In the absence of this control mechanism, the implementation process may result in chaos and at times may result in total derailment of the entire process. When external assistance is needed, it must be opted for without any hesitation.

6. Periodically evaluate and modify the action plan to keep it abreast of dynamism: Pecuniary action plan put into action must be evaluated periodically and adjusted by roping in the current developments and anticipated changes in the market conditions. This alone will ensure the effective operational life of the action plan and keep it in line with contemporary scenario and facilitate in materializing the pecuniary ambition of the household.

Information required at each of the six stages in the decision making process varies. The dynamic interplay of social, political, cultural, economic and global factors requires each household to continuously complement and update their repertoire of knowledge.

IDENTIFYING THE PECUNIARY AMBITION OF HOUSEHOLDS

Households' pecuniary ambition expresses in monetary terms their prospective requisites in the near and reasonably distant time to come. It represents the money required in aggregate. Sketching a pecuniary ambition in black and white enables a household to plan for their income and the consequential expending and diversified investment program

We may be able to narrate household financial goal in many ways as follows: (1) Rs.5 lakhs required a decade hence on the verge of termination of work life (2) Half a million after 24 months for a trip abroad (3) Another million posterior 4 years as part of down payment towards a home loan (4) Rs.2.5 lakhs needed after a year to buy a pre-owned gym equipment for personal use, etc. It is exactly discernible that each financial goal be composed of two constituents, one is monetary equivalent and the other is staggered duration for its materialization.

Monetary terms: Initially a house hold has to work out the present monetary worth of its pecuniary ambition. Then, such presentmonetary worth of thatambition should be translated to their future value. For example: current price of a car is, say, half a million. Common sense will dictate that after a decade the value would have towered because of inflationary pressure. Savings should be effected in the present taking this factor into account to materialize the ambition.

The future worth of the present value can be calculated by multiplying the present worth with (1 plus Rate of inflation) raised to the required number of years.

Assuming the inflation rate to be 10%, the amount needed to procure the car after a decade will be concocted as follows:

Future value of the car = 5,00,000 x $(1+10\%)^{10}$ = 12,96,870. Savings and investments should be effected in such a way as to have 12,96,870 at the end of the target period.

Staggered duration of the pecuniary ambition: Pecuniary goal spread across a span of time can be staggered to short through long phase. To satiate short duration ambition, savings may be deployed in avenues with thin risk and floor returns with minimal capital appreciation. Those falling in medium term may be satisfied by investing in instruments characterized by moderate returns with moderate risk with a reasonable capital appreciation. For meeting long term ambitions, funds may be tactfully diversified into high risk assets with high returns and significant terminal capital appreciation.

EVALUATE FINANCIAL MODELING OF HOUSEHOLDS

Once the financial goals have been pin-pointed back-to-back then plans should be floated to generate adequate income for materializing the ambition. Surplus left after meeting the expenses should be intelligently channelized into avenues that yield the necessary amount to meet the pecuniary goals. While doing so, prospective future pecuniary obligations should also be taken cognizance of.

Ramesh wishes to purchase a car at the end of fifth year for Rs. 7 lakhs. He contemplates investing in equity at an anticipated annual yield of 15% in a fixed deposit in a nationalized bank for an annual yield of 8%. In the case of equity, Ramesh’s savings work out to Rs.7902 each month in order to garner the required fund of 7 lakhs. If he opts for the latter, owing to a lower return, Ramesh’s savings tally to Rs. 9526 each month. If Ramesh hypothesizes an enhanced time horizon of, say, 7 years for the same amount, then the savings in the case of equity and bank deposit tantamount to Rs.4757 and Rs.6243 respectively. This is due to the fact he has more breathing time to save and accumulate the target sum.

The zeroing of an investment avenue is contingent upon the duration planned to materialize the pecuniary ambition and risk appetite of the prospective investor. If the time spans an extended stretched period, then parking funds in equity can be preferred. This is owing to the fact that though the returns from equity are volatile in the short run, in the long run their returns are high nullifying the short term oscillations.

Yuvaraj is saving for to construct a house and needs Rs.7,00,000 at the end of fifth year. For this purpose, if he parks Rs. 1 lakh in a five year equity dominated mutual funds unit anticipating a yield of 15%, then the worth of Rs. 1 lakh after 5 years will be Rs.2,01,000. i.e. 1,00,000 x $(1+15\%)^5$. There is a short fall of Rs.4,99,000 which needs to be mobilized from his financial resources.

CONCLUSION

An investor, who despises risk, prefers to park his fund in a low yield investment with thin risk. In this case, he has to increase his savings rate or extend the time horizon to materialize his pecuniary ambition. A moderate risk-taker may opt partially for equity and partly in debts, bonds or bank deposits with low-risk and low-returns. An avid investor with a high risk appetite may go in for majority equity holdings for high returns in tandem with high risk.

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