NSDL
Technology, Trust & Reach

The Financial Kaleidoscope
Defining the different shapes of investment

October 2016

IT'S NEVER TOO EARLY TO THINK ABOUT RETIREMENT PLANNING

From The Editor's Desk

Dear Reader,

Retirement Planning has been gaining a lot of importance of late in India. Importance is more in financial magazines than among those who need it the most. As part of a financial plan, retirement planning in India could be significantly important in the coming 2-3 decades. Till a decade ago, retirement meant receiving pensions, purchasing a house to live in and going on vacations randomly. Retirement was a peaceful phase and no such planning was needed for it. Investments produced high returns with decent safety.

However, the world has changed. Recessions, political changes have increased leading to an everlasting situation called **"Uncertainty"**. Further, rising inflation numbers, slowing economy growth, love for Gold and of course too many financial products do not make life easy for any individual planning for retirement. What it does mean for a middle class person is to be extra careful with his money and start thinking about a future phase called "**Retirement**".

Let us look at three different types of investors i.e. risk averse individuals who stay away from equities, moderate investors who have some exposure to stocks and aggressive investors who are willing to take more risks. It is found that the risk-averse investor's nest egg is considerably smaller than those of the moderate and aggressive investors. This is largely because apart from Provident Fund and investments in small savings schemes, risk averse individuals has invested in low-yield life insurance policies and pension plans than the aggressive investors has invested into equity which are critical for long-term goals such as retirement. The route of equity investments is never a straight line. It will have ups and down, which is an inherent feature of this asset class. However, in the long term these investments will prove more rewarding than fixed income options such as PPF and Fixed Deposits.

To conclude, the ideal time to start saving for retirement would be 1-2 years after you get your first job. If you have not started yet, it is time to start now. We are sure that the contents of this issue will help you plan a better retirement life.

Best Regards,
NSDL

It pays to start early

When it comes to planning retirement, the stark reality is that any delay could be the difference between a dream retirement and just a dream. 'You must be joking' is a typical response one gets from a 20 year old kid when asked about their retirement plans. When we first start out in the workforce, retirement often seems a long way off. After all, most of us will have a career spanning 30-35 years, or even more. Rising longevity has meant that for all practical reasons one will need to work significantly longer to build a sizeable corpus to see through the retirement years. The fear of outliving retirement savings is a very real risk given the volatile stock markets, high inflation and low interest rates; in the midst of advances in healthcare.

The reality, however, is that as time goes by we get caught up with buying a home, raising a family, and doing all the things that make life rewarding. All these financial activities result in planning for retirement being pushed to the backburner. Ideally, the moment one starts earning a regular income they should start retirement planning.

The earlier you start, the better

Generally speaking, the sooner you start saving, and the more you save, the more money you could have set aside when it's time to retire. In addition to helping contribute to your future financial security, there are also benefits you can enjoy today when you participate in your retirement plan. Moreover, when it comes to investing, time can literally be money. This is particularly true with respect to an investment process known as compounding. Compounding is what happens when the money you save (in a savings account, a mutual fund or the provident fund) grows—and that increased amount remains in your account to be reinvested to potentially earn even more.

In your 20's you have your first proper job with a proper salary, and even though retirement may seem a long way down the future, the mandatory contribution to the provident fund scheme is a good option to take seriously and get used to. Contributing to your retirement plan is one of the best ways to give yourself greater long-term financial security—regardless of your age.

To address the dilemma of how much you need in your 20s and 30s, make sure that you are saving a significant part of your income towards retirement. The approach needed is of income replacement in this stage. So if you are earning ₹1 lakh a month, think of inflation adjusted figure that you should invest towards when you retire 25-30 years later. Likewise, when you are closer towards your 50's, you would be in a better position to know of your essential expenses, which will help you save and invest to build a corpus that can take care of the expenses you will incur in retirement by way of expense replacement calculations.

Cost of delay

Like every other financial goal, there is a cost of delaying, which could be significant on how long you delay. Here's an example. Two friends – Ram and Lucky – start working for the same company at age 25. During their first 10 years there, Ram saves ₹1,000 a month through a retirement plan, while Lucky saves nothing. After 20 years, Ram stops contributing entirely. Meanwhile, after a decade of no savings, Lucky starts saving at age 35, saving that same ₹1,000 a month. But unlike Ram, Lucky continues investing till he retires at 60. Ram has put only ₹2.4 lakh into his account while Lucky has saved ₹3 lakh. But because Ram started sooner, he has ₹31.58 lakh in his account at retirement, versus only ₹12.98 lakh for Lucky, assuming they both earn 10 per cent a year on their money (See Early Bird Advantage). **That's the power of time and compounding**.

In the absence of any form of social security, it's up to you to ensure that you have enough to maintain your lifestyle after retirement. As one can take higher risk with investments in their early years of working, it is advisable for them to allocate significantly in equities as an asset class to benefit from its ability to beat inflation in the long run.

Planning for retirement is a lifelong process, not just something you worry about once you are nearing it. But a good way to start working towards your retirement plan is to set a financial goal, a roadmap that will lead you to it. The inherent advantage of starting early is that it becomes a habit which pays off in the long run.

We know what you're thinking. You're hale and hearty and probably in your 20s or 30s, so why should you be planning for your retirement right now? The truth is that many industry experts believe that you should start planning for your retirement from the very first day you start to earn. But let's be honest. How many of us have really done that? Chances are, very few. There's no need to fret. Follow these 7 rules for retirement planning and you should be well on your way to comfortable retirement years.

1. Stack away 10% of your pay check as a nest egg for your retirement

This is one of the most basic rules of retirement planning. When you start working, you and your employer both contribute 12% of your basic salary (plus dearness allowances, if any) into your EPF account. The entire 12% of your contribution goes into your EPF account along with 3.67% (out of 12%) from your employer, while the balance 8.33% from your employer's side is diverted to your EPS (Employee's Pension Scheme). It's important to note that if your basic pay is above ₹15,000 per month, your employer can only contribute 8.33% of 15,000 (i.e. ₹1,250) to your Employee's Pension Scheme (EPS) and the balance goes into your Employee's Provident Fund (EPF) account. This is a great little mandatory nest egg that you are compelled to save by law. There's no escaping it, the government wants you to save some cash for a rainy day.

It is often that this compulsory savings plan becomes a retirement plan by default for many people. It doesn't matter how much you really contribute each month, what matters is the consistency of contribution. This is long term savings plan which may pay off big time in the future through the power of compounding. That is why it is important to start early.

Mutual funds that suit your age profile and risk appetite are good options. Be sure that you are disciplined about putting that sum of money away every month. You could do this by starting an SIP in a mutual fund and applying an ECS system to automatically debit your money each month. This ensures that your retirement planning stays on track.

Investors should plan their old age income by opening a NPS account (National Pension System) as one of their investment options. Pension Fund Regulatory and Development Authority (PFRDA), the regulatory body for NPS, appointed NSDL as Central Recordkeeping Agency (CRA) for NPS. CRA issues a Permanent Retirement Account Number (PRAN) to each subscriber and maintains data base of each Permanent Retirement account along with recording transactions relating to each PRAN. NPS is a voluntary, defined contribution retirement savings scheme designed to enable the subscribers to make optimum decisions regarding their future through systematic savings during their working life. NPS seeks to inculcate the habit of saving for retirement amongst the citizens. It is an attempt towards finding a sustainable solution to the problem of providing adequate retirement income to every citizen of India.

2. As your income increases, increase your investment too

Just got a raise? Congratulations! But that doesn't mean that you should go out and buy the PS4 or that new Gucci handbag. What you should be doing is increasing how much you put away in terms of your investments. Sure, everything is more expensive than it used to be. But inflation is part and parcel of life and increased cost of living is no reason not to increase your investments.

We delay things especially when it comes to financial investments. And when you add the angle of retirement which, for many of us seems like ages away, it doesn't become a priority. The instant gratification with that PS4 is looking way more attractive than a retirement plan. Think about it this way, if you are 30, earn a monthly salary of ₹50,000 and put away 10% of your salary for your retirement in a scheme that gives you 9% interest per annum, by the time you are 60, you will have accumulated approx. ₹97 lakh.

Say you get a raise of around 10% every year and subsequently increase your investment accordingly, you could get a retirement corpus of up to ₹2.76 crore. That's a pretty impressive sum of money.

3. Try not to plunge into your corpus before retirement

Every time you switch jobs, your retirement fund is at risk. That is because when you leave a job, you have the option of transferring your PF balance to the PF account with your new employer or withdrawing it. Then there's the option of withdrawing your PF balance if you need it, like to buy a home, for a wedding, medical emergencies etc. If you keep dipping into you PF corpus, your investment won't be able to enjoy the full potential of compounding.

Many people today simply opt to withdraw their PF fund when they switch jobs, more so because the paper work involved is minimal. Always remember that all EPF withdrawals within five years of joining are taxable. When a large sum of money comes into your possession, what do you do? Go on a shopping spree of course! Or spend it on stuff you would not have bought if you had just your monthly salary to contend with. This can put quite a large spoke in your retirement planning.

4. Save for retirement, borrow for education

Our kids are our first priority and every parent wants to give their child the very best in life. But that often means compromising on your own future. Whether it is to fund a child's education, or wedding or just to make sure they want for nothing, many parents tend to dig into their retirement savings.

This is risky business, as saving for your retirement is a crucial aspect. You have to contend with the fact that your retirement is going to be different from when your parents retired. You will probably have to fund the entire thing. But this doesn't mean that you have to be selfish. You just need to be smart about it. A child's education can be funded by an education loan, which can be paid off by EMIs.

Off late, EMI schemes have made the purchasing of several items much more accessible. Loans are available for pretty much everything - education, homes, cars, consumer durables and even travel. Having said that, there is no loan available for retirement. You're on your own where that is concerned. One more reason you should choose an education loan for your child is that it makes them directly responsible for its repayment, thereby instilling a sense of responsibility in them early on in life.

5. Withdraw 5% a year initially, then step up

One of the biggest challenges for tomorrow's retirees is to ensure that they don't outlive their savings. This is a distinct possibility because of two major factors: **rising cost of living and an increase in life expectancy**. High inflation, in fact, is enemy no. 1 for the retired investor. Sure, the inflation rate will not remain as high as it is right now. However, over 20 years, even a nominal inflation of 4% will reduce the value of ₹1 crore to ₹44 lakh. Besides, Indians are living longer. Life expectancy rose from 61.3 years in 2000 to 66.46 years in 2010. By 2020, the average Indian can expect to live till 72 years. In urban areas, where people have better access to healthcare, and in higher income groups, the life expectancy could extend beyond 80 years.

To ensure that you don't run out of money in your old age, you must have a drawdown plan in place. The thumb rule is not to withdraw more than 5% of the corpus in the first five years of retirement. This can be progressively increased to 10% by the time the retiree is 70. This essentially means that the retiree should draw down less than the appreciation in the initial decade, but in the next 10 years, he can withdraw more than the accretion to the corpus. At 80, even a 20% annual drawdown rate would be considered safe.

The problem arises because most Indians are not comfortable with the idea of drawing down from their corpus. There is an overarching desire to leave something behind for their heirs and dependents. Given the inability of a corpus to beat inflation in the long run, the retirees should be prepared for a depletion of their corpus.

6. 100 — age = Your allocation to stocks

An investment portfolio's performance is determined more by its asset allocation than by the returns from individual investments or market timing. How much you have when you attend your last day at work will depend on how you divided your retirement savings between stocks, fixed income and other asset classes. Experts recommend that you should have an equity exposure of 100 minus your age. So, at 30, you should have about 70% of your portfolio in equities. At 55, the exposure to this volatile asset class should have been pared down to 45%. After you retire, your exposure to stocks should not be more than 25-30 % of your portfolio.

Even within equities, the type of stocks (or equity funds) in your portfolio should vary with age. This is not a hard and fast rule and should also take into account the financial situation of the individual. It assumes that all people at a certain age will have the same risk appetite. This is not true. A 45-year-old person with a good income and few dependants will be able to take on more risk than someone who is 30 but has a low and unsteady income.

7. Save 20 times your annual expenses

This rule is different from others because it is based on how much you spend, not on how much your investments earn. Knowing your post-retirement expenses is crucial to retirement planning. Some expenses, such as those on clothing and entertainment, come down. Others, such as transportation, medicine and insurance, go up. Add up all the expenses you are likely to incur after retirement to know how much you will need per month. Then, multiply this amount by 240 to know how much should be your retirement corpus. However, this calculation is based on a number of assumptions. Firstly, you should not have outstanding loans when you hang up your boots. Secondly, you and your spouse should have sufficient health insurance.

So plan for your retirement early on in life and plan smartly. This could help you lead a life of independence in the future with your head held high.

Understanding Financial lingo

- **Point of Presence (POP):** Points of Presence (POPs) are the first points of interaction of the NPS subscriber with the NPS architecture. The authorized branches of a POP, called Point of Presence Service Providers (POP-SPs), will act as collection points and extend a number of customer services to NPS subscribers.
- **Pension Fund Regulatory and Development Authority (PFRDA):** An autonomous body set up by the Government of India to develop and regulate the pension market in India.
- **Pension Funds (PFs)/Pension Fund Managers (PFMs):** The Pension Funds (PFs) appointed by PFRDA would manage your retirement savings under the NPS.
- **Annuity Service Providers (ASPs):** ASPs would be responsible for delivering a regular monthly pension to you after your exit from the NPS.
- **NPS Trust:** The NPS trust has been set up and constituted for taking care of the assets and funds under the NPS in the interest of the beneficiaries (subscribers).
- **Annuity:** An annuity is a financial instrument which provides for a regular payment of a certain amount of money on monthly/quarterly/annual basis for the chosen period for a given purchase price or pension wealth. In simple terms it is a financial instrument which offers monthly/quarterly/annual pension at a specified rate for the period you chose.

Blog

Investments in Mutual Funds

By Mr. Raghupathi Hegde
CFA

Introduction

"Today the leading causes of death are no longer tuberculosis, diarrhea & respiratory infections but heart diseases, stroke and cancer. Yet life expectancy is still increasing (albeit more slowly than it did before 1950) driven upwards not by cleaner water & more complete vaccinations but by medical advances and changes in behavior."

It is comforting to know that, in the rich world, post 50 years of age, an individual lives on an average 7 years longer today than in 1950. It is also heartening that economies like India are witnessing a similar trend. The fact that one lives longer (longevity) should feel good but poses a nice to have issue – Planning the management of investments to sustain a longer tenor given objectives and constraints.

Investment Management for Retirement

For retirement, the principal objective would be to:

- Enjoy the same lifestyle in retirement as before (or a better one).
- Accumulate sufficient wealth as desired to leave behind as a bequest.

An investor is also constrained by the following during the retirement phase:

- Income from financial assets is critical given absence of salary/working earnings (other than Pension).
- Willingness & ability to take risk (Risk Tolerance) is low.
- Desire for liquidity is high.

Given this backdrop, below is a summary, of the typical requirements of funds and sources of funding from appropriate investment avenues, during the retirement phase of life.

Factor	Requirement	Sources
Planned Spending	• Meet living expenses • Factor longevity	• Life Annuities • Interest & Dividend
Unplanned Spending	• Unanticipated one time spending • Increased recurring spending	• Liquidation of Equity Shares\Fixed Deposits • Safety Reserves (Typically 2 years spending)
External (Non-Controllable) market factors that affect the factors above		
Inflation	• Reduces the value of money • Permanent increase in spending	• Inflation Indexed Bonds • Gold Linked Bonds or Gold ETFs • Appreciation provided by Equity Shares
Market Volatility	• Asset prices tend to fluctuate especially equity in the short-run	• Safety Reserves (Provides a cushion for a fall in asset prices or poor returns)

It is imperative to utilize multiple avenues to meet desired goals and mitigate specific risks. For e.g. Life Annuities brought from Insurance Companies provide a constant & stable pension like stream of income as long as one lives and are not subject to market volatility but they do not provide protection against inflation & have withdrawal restrictions. For inflation protection investment in Gold or Equity are good shields. Fixed Deposits/Government of India Sponsored Bonds are quasi risk free assets and the % of these assets increases as one age's while the % of risky assets such as Equity falls. Also concentration (e.g. Single Company Equity investment holding) should be avoided to diversify away risk. Secondary factors such as taxes, level of financial wealth, etc. should be appropriately factored. A customized plan should capture objectives, risk tolerance, constraints & determine the appropriate mix of investments

Conclusion

Adam Smith, the father of modern economics says, **"Money, says the proverb, makes money. When you got a little, it is often easy to get more. The difficulty is to get that little"**. This not only emphasizes the importance of one's hard earned savings during working life but also highlights that one can meet retirement objectives in the absence of working income. The key lies in planning & to invest prudently.

1. How to Plan for Retirement?

You can plan for your retirement by investing in some of the investment products available for retirement. Some of the investment products for retirement are:

- **National Pension System (NPS):** PFRDA, the regulatory body for NPS has appointed NSDL as Central Recordkeeping Agency (CRA) for NPS. CRA issues a Permanent Retirement Account Number (PRAN) to each subscriber and maintains data base of each Permanent Retirement account along with recording transactions relating to each PRAN. You can enroll in the NPS at any time if you are a citizen of India and at least 18 years of age; no entry is, however, allowed after 60 years of age. You should take advantage of compounding of your wealth by starting right away. The earlier you start, the greater will be opportunity for the growth of your pension wealth.

  You can open an NPS account with authorized branches of service providers called 'Points of Presence' (POPs), appointed by PFRDA. To enroll in the NPS, you have to submit the registration form to the Point of Presence Service Providers (POP-SPs) of your choice. You have the option to shift from one branch to another branch of a POP at your convenience. The registration form is available at any of the POP-SPs or can be downloaded from NSDL website **www.npscra.nsdl.co.in** and PFRDA web site **www.pfrda.org.in.**

- **Mutual Fund Retirement Plans –** Mutual funds have multiple plans for both building a corpus as well as investing the corpus accordingly. Charges involved are minimal. However, choosing such plans needs a bit of financial knowledge since only past performance may not help you choose the best.

- **Employee Provident Fund (EPF):** EPF is one of the major investment products aimed at retirement. For most of you, a part of salary would be deducted as part of contribution towards EPF (around 12%) and employer would also add a similar amount to your account. This is almost a forced saving. This will help you build decent corpus needed for your post retirement years.

- **Insurance Companies Retirement Plans –** Like mutual funds, insurance companies also provide different variations of retirement plans. However, there may be charges up to 5-6% or even more on these in the name of premium allocation or policy administration.

Asset Allocation

When it comes to planning for any goal including retirement, asset allocation is the key to reaching it. According to various sources, 85-90% of the returns from a portfolio are due to asset allocation. Asset allocation is nothing but deciding how much needs to be put into each financial product. This is definitely the toughest thing to do. A thumb rule is that (100 – age) % should be invested in equities and rest in debt products.

2. How to Calculate Retirement Corpus / Pension?

While planning for retirement, two things will trouble you the most – Retirement Corpus needed and Pension which gets generated from this. There are various financial tools and calculators available in order to calculate these. Having known about various aspects of retirement such as retirement products, need for a retirement plan; only question left out is – who would do it?

Financial Planner versus Self

A qualified and capable Financial Planner such as a CFP could be very handy for you in preparing a retirement plan as part of an overall Financial Plan. However, there is no such mandate on approaching a financial planner for this purpose. You can trust yourself too. You would have to build your financial knowledge for this and of course, allocate some time for your finances on a regular basis.

Investor Education initiatives undertaken by NSDL

- **Investor Awareness Programmes:**

In order to reach out to investors that are spread across the country and to apprise them about the facilities available in NSDL depository system and the awareness on stock markets, NSDL conducts various Investor Awareness Programmes jointly with it's Depository Participants (DPs) & with Institutions like SEBI, NSE etc. NSDL also conducts various training programmes for its Depository Participants (DPs) on Depository related services. During September 2016, NSDL conducted 37 Investor Awareness Programmes with Participants, College Institutions, SEBI, NSE etc. These programmes were attended by around 4,000 investors, details as mentioned below:

Sr. No.	Particulars	
1	**Joint Awareness Programmes with DPs**	**No. of Programmes**
	ICICI Bank Limited	4
	Kotak Securities Limited	3
	Sharekhan Limited	3
	Swastika Investmart Limited	2
	Arihant Capital Markets Limited	1
	BMA Wealth Creators Limited	1
	Globe Capital Market Limited	1
	Trustline Securities Limited	1
	Total Programmes	**16**
2	**Investor Depository Meets (IDMs)**	**No. of Programmes**
	IDMs organized by NSDL	9
	Total Programmes	**9**
3	**Joint Awareness Programmes with other Institutions**	**No. of Programmes**
	Geojit BNP Paribas Financial Services Limited, Eenadu and NSE	2
	Securities and Exchange Board of India (SEBI)	1
	Thatzit Entertainment Pvt. Ltd.	1
	Life Insurance Corporation of India	1
	Total Programmes	**5**
4	**Workshop for College students**	**No. of Programmes**
	The Indian Institute of Technology Kharagpur	3
	The Indian Institute of Technology Bombay	2
	PTVA's Institute of Management	1
	Total Programmes	**6**
5	**Participation at Events**	**No. of Programmes**
	ICC Regional Mutual Fund Summit 2016 organised by Indian Chamber of Commerce (ICC)	1
	Total Programmes	**1**

Read and Win!

Mention any three essentials for Retirement Planning.

Send your replies providing your contact details (Name, address and contact no.) with the subject 'Knowledge Wins Contest -October 2016' to info@nsdl.co.in

KNOWLEDGE WINS Contest

Terms and Conditions

- NSDL shall be solely responsible for the execution and administration of this Contest.
- This Contest is only open to Indian Citizens. (NSDL employees are not allowed to participate in this contest.)
- All personal details submitted must be accurate and complete and are subject to proof upon request by NSDL.
- NSDL reserves the right, at any time, to verify the validity of entries and entrants and to disqualify any entry not submitted in accordance with these Terms or which tampers with the entry process.
- NSDL reserves the right to discontinue the contest at any given point of time without prior intimation.
- All prize drawings will made on a strictly random basis and the decision made by NSDL will be final

Lucky 25 Winners will Win Free Goodies

Your suggestions for newsletter are valuable to us. Send in your suggestions mentioning your contact details (contact name, address & contact number) with the subject "Suggestions for the newsletter" to info@nsdl.co.in

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