5 mistakes to avoid to maintain a healthy financial standing

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We often come across phases in life which force us to think, "What went wrong?" Most people think that their lavish lifestyle or increased spending is the primary cause of all the financial troubles in their lives, But the actual reason is spending before saving & not investing what they are saving. Because it's not how much you make, but how much you save and invest. Also, there are certain circumstances in life which are beyond anyone's control, such as the recent one – COVID-19 which has by far been one of the most challenging and unprecedented times in the history, leading to global downturn, layoffs, pay-cuts and other anomalies and has impacted one's financially standing a lot. The current crisis has taught us and reiterated that one should be saving & investing right.

Also, in the current times, it is important to carefully manage personal wealth and stay clear of financial decisions which can impact your financial standing in the longer run.

You can avoid these 5 mistakes to maintain a healthy financial standin

1. Investing without proper asset allocation & understanding of risk

Improper asset allocation is by far one of the biggest obstacles in one's journey towards wealth creation. One needs to know why is the investment being made, where is it being made and what are the expectations out of it? The proverbial eggs in a basket applies here. Be wary of how much of your investments do you want to allocate to each instrument (like equity, debt, real estate etc). Returns are an integral part of investment and so is the risk and it should not be just about what you get at the end. At the same time, an appropriate diversification will avoid overconcentration on one asset. If you do not understand the nitty-gritties, take help from a financial advisor.

2. Investing without keeping your future goal and timeline in mind

Currently, we are getting to hear more of news such as: GDP down to negative figures, or the Rupee is going to sink further. The disappointing performance of the economic indicators has made every investor cautious to tread an investment path. However, one of the biggest factors that can help you stay on your path is if you are aware of the goal for which you are investing and the timelines to achieve them. This will allow you to be focused and avoid short term disruptions or any deviations.

Proper goal planning ensures that you are aware that how much you want to achieve, in how many years, how much to invest and where. One should be mentally sure of when are they planning to buy that house or send their child for higher education or retire. At the same time, being mindful of what these goals will amount to at the target year, weighing in the impact of inflation. Without a clear sense of purpose, arbitrary investment would be more like shooting in the dark. The idea is to have a sense of direction of what you want to achieve and how you want to achieve it.

3. Being very conservative and keeping balances in account for a long time or only choosing FDs for Investments

Wealth Creation and being conservative seldom go hand in hand. Indians are obsessed with fixed deposits and it is one of the most popular investment tools in the country. One of the major realizations that people have had in the current scenario is that although they have been saving for long, yet their investments are not enough. This is because they either kept their money in savings accounts or invested in FDs. Thus, their post-tax returns were equal to or slightly lower than the inflation and hence the purchasing power of their savings never increased.

FDs in general have lower returns which are taxable, and they attract a penalty, should you need to withdraw the money before their fixed maturity dates. Moreover, the interest rates are in decreasing trend. The current situation saw rates diminishing substantially and are expected to be so in future, as India is a growing economy. On the other hand, bank balances are highly volatile and can vanish in the thin air if checks are not made in spending. Both these are conservative approaches to investments. While the FDs are a good way to invest for a long term, it is only as good as a savings plan for risk-averse investors and can yield low returns than other instruments. In such a scenario, a debt mutual fund is a good option to choose, for it provides better returns and liquidity and has similar risk levels as that of FD.

4. Not reviewing your entire portfolio regularly

Monitoring your portfolio is as important as building it. Taking cues from nature, merely sowing the seeds and expecting it to grow into a tree would not be wise. One would need to watch over it in case a storm comes, protect it. Similarly, one must monitor and review one's entire investment portfolio from time to time. Usually people don't review the portfolio regularly and even if they do that for the sake of it, they only review the Mutual Funds or Stocks. MF and Stocks are not the entire portfolio and one should review entire investments including FDs, real estate, equity, MF, gold, bonds etc. Due to the volatility in market conditions, some investments thrive while others don't do that well and need to be re-balanced if required. This will help mitigate the risks in case of market shifts and also give a direction to align the assets with the investor's risk handling capacity.

5. Ignoring Taxation and Compliance

Taxation and compliance are two very important aspects to keep in mind while making investments. This holds true for both resident and non-resident Indians. Your portfolio returns should be tax efficient. For instance, NRIs should carefully understand NRO and NRE investments before making any monetary commitment or building a portfolio. Tax and compliance parameters if ignored can result in creating troubles for the individual and their portfolio returns at a later stage.

(By Nishant Kohli, Founder, Director and Business Head-Wealth, Mudra Portfolio Managers)