

// WEALTH CREATION //

HOW TO JOIN THE MILLIONAIRE CLUB?

THE REAL MILLIONAIRES & HOW TO JOIN THEM

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According to experts, you must save at least 25% of your income but not more than 75% of it. If you save more than 75% of your income your life style is unbecoming of your financial status while if you save less that 25% it will tend to send your lifestyle down very substantially after retirement.

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Most of us believe that one has to inherit wealth, marry into money or hit it big in the software boom to become a millionaire. The doctor next door earns a huge amount of money, changes cars every couple of years, lives in a luxurious penthouse whose interiors are redone every year, dines at five stars, and goes on foreign vacations every few months. However, most millionaires don't fit that stereotype. The real millionaire is probably your neighbour who works for a local company and drives an Esteem.

We live with the misconception that the higher our income, the wealthier we are. However, high income does not necessarily mean wealth. Real wealth is money in stocks, in real estate, in PPF, in gold. You can retire comfortably on wealth but you can't do so on income because retirement puts an end to your income.

In my practice as a financial planner for individuals of substantial wealth, I found that only a few have inherited the fortune, whereas the majority of millionaires are simple hardworking people with a different attitude. Their secret is not necessarily earning huge amounts of money but saving what they earn and investing what they save.

It is necessary to know how much should you save and how much should you spend. According to experts, you must save at least 25 per cent of your income but not more than 75 per cent of it. If you save more than 75 per cent of your income your life style is unbecoming of your financial status, while if you save less than 25 per cent, it will tend to send your lifestyle down very substantially after retirement. A millionaire typically is able to continue his lifestyle for up to twenty years after retirement. Those who are spending tomorrow's incomes today by buying cars, appliance and other gadgets on credit finance may be ensuring their retirement disaster right now. That is because, after five years, these individuals discard the older gadgets and appliances and take on new loans for the purchase of newer models. This sets in a self-destructive, income consuming lifestyle with no savings and hence deprives them of an asset base for those retirement years. It requires a lot of self-discipline and hard work to save between the recommended figures but that's what differentiates the 'have not' from the millionaires. Not that no loan should ever be taken but it has to be done judiciously and in keeping with a financial plan. It is the overindulgence and excesses that one has to be wary of.

This brings us to the definition of a rich person. A rich person is one who necessarily spends less than his income. He or she lives well and saves hard. He spends more on items that give him long-term pleasure like a house or an expensive watch and less on short-term gratification like expensive holidays abroad or dining out. A poor person on the other hand is one who spends more than he or she earns, has few assets and an attitude that he can afford practically everything since he or she shies away from saying 'I can't afford it'.

Once you have started saving over 25 per cent of your income, you have crossed a major barrier to becoming wealthy. The next step is asset allocation. Asset allocation involves allocating certain percentage of your assets to real estate, stocks, fixed income and gold. It is all about reducing the risk while achieving the same high returns and about having a sense of satisfaction that your investments have a high probability of doing what is expected of them.

Your assets should be diversified over various asset classes. Each asset class, be it real estate, stocks, fixed income or gold has its own cycles. While it may be stylish to put all your money in the asset class that is currently booming, it's a step on the death spiral. One has to invest when prices are low, not when there is a mad rush for investing in a particular asset. Maintain a balance of up to 50 per cent of your assets in real estate and the remainder spread out over PPF, bonds, stocks and gold. This diversification works because not all asset classes move up and down together. But the up moves are usually very steep compensating you for years of holding by sudden appreciation in one year. The common factor in all these asset classes is that they all result in pre-tax compounding of your money. You don't have to pay taxes till you sell these assets (in case of PPF you pay no taxes at all). The assets keep growing at a compound rate including the money you would normally have paid out as taxes to the government. You must have a long-term horizon of between 15 to twenty years on any of these investments.

Common sense has to be used to pick assets wisely. Don't go to your friend or neighbourhood broker and ask him for a hot stock tip. That's the surest way of losing your hard-earned money. Invest in well-managed, blue chip companies that have been around selling good products for at least the last ten years. While it is always good to buy the stock when it is cheap, it is important to note that it is better to buy a good stock at a

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fair price than to buy a fair stock at a good (cheap) price. Don't keep buying and selling stocks because the prices go up or down. Another alternative is to invest in index funds regularly.

To be a millionaire, equity investment either in a business or stocks is essential. Look at yourself as a partner in the business of the stock that you buy. And ask yourself if you would sell your partnership in a business just because somebody offered you a higher price than you had paid for it? You would sell only if the business was to become unprofitable in future. Apply these same principles to your stock holding. Don't overreach for yield but look at steady appreciation over the foreseeable future say the next 15 or twenty years. Most millionaires do not trade. They buy and hold over their investment for a long time. Remember, more money has been lost by overreaching for greater yield than at gunpoint!

Another point of importance is to start early in life. The sooner you start, the better will be your chances of not only being a millionaire soon but also to take care of any mid-life contingencies. If you start after 10 years, even if you increase your savings per annum substantially, you will not have a comparable asset pool to someone who begins earlier. It is never too early to begin saving and investing. The sooner you start, the more you will benefit from the effect of compounding.

Compounding simply means that, over time, the interest you earn on your original investment (your principal) also earns money. The longer you let your money grow, the more powerful the effect of compounding.

Let us consider that you start investing Rs. 10,000 per month from age 25. Assuming your money grows at 8 per cent p.a., as in the case of PPF, you will already have accumulated Rs.1.7 million at age 35 and over Rs.2 crore by the time you retire at 60.

Now, if you invest even double the amount of Rs. 20,000 per month from age 35, then assuming the same rate of growth as above, you will have only about Rs. 1.75 crores at age 60.

As you can see from the above example, it is always better to begin early to take advantage of the phenomenal effect of compounding.

A millionaire is typically a wealthy individual with lots of assets generating little income but a lot of capital appreciation.

Most millionaires are frugal. Frugal doesn't mean your standard of living has to be below that of your peers. Definitely not. On the contrary, these millionaires are efficient people who spend less and achieve greater standards. It's about plugging those leaky purses and getting more for your money. Buy a good car, a top of the line model, but buy one at the right price and use it for the life of the car. Don't misuse it and don't discard it because a new model is introduced or because your friend has bought a new one. If you do so, you are not going to be a millionaire. Typically, the self-made millionaires buy everything at discounted prices. They may buy used cars in excellent condition at half the price; they compare prices and the quality of every product at the grocery store. More importantly, they never buy anything they don't need. Unlike most of us, they don't wander into a store with a vague idea of what they require. They have lists made out on what needs to be purchased and they stick to it. They have household budgets stipulated by financial plans that are adhered to month after month.

The road to becoming wealthy is simple one, is it not?

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