You need to plan your retirement from the day you start earning - Here's why?

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You receive your first paycheck and you feel on top of the world. Suddenly you feel more responsible and at the same time sense the freedom to spend as you like. While it is a positive start to your career, there is something else you need to be aware of. Your work life could span another 25-30 years and once you retire at 60, there is a non-earning period that can go up to another 2 to 3 decades. Yes, we are talking about retirement right at the age when you have started earning. And, there are enough reasons to make you sit back and realize the importance of making the right moves to plan your retirement well in-advance. After all, you will want to continue the financial freedom even in your retirement years.

Retirement Planning is essentially a long-drawn process and involves your active participation from the day you start earning. A lot of investors ignore retirement early in life and procrastination keeps them from delaying their retirement planning. But, as with all other good things in life, it helps to start early.

Here are some basic advantages to build a robust retirement plan early-on in life.

Regular income during retirement – Unlike developed countries, private sector employees in India do not have the cushion of a state-sponsored pension. This means one is on his own after retirement . Retirement planning helps you save, invest and build an adequate corpus in your working life and then invest it diligently after retirement so that it provides you with the necessary cash flows to lead a financially relaxing post retirement life

Medical Expenses – With rising age comes the need for preventive health checkups and several health problems that need the best of medical facilities. Catering to these expenses can make a massive dent to your finances post-retirement.

Counter Inflation – Rise in prices over the years, due to inflation, makes an enormous difference to the amount needed for leading a comfortable retired life. For instance, if you need Rs. 50,000 per month to meet your living expenses today, you will need Rs. 1,10,000 per month after 20 years and Rs. 2.4 lakhs (up by almost 5 times) per month after 40 years, at an annual inflation rate of 4 per cent. Your portfolio should be primed to provide for the rising expenses

Falling interest rates – The interest rate on fixed income investments are falling and global central banks including India want them to remain low in order to help the economy grow. As a retired investor, the options to earn high inflation adjusted returns remain low. Prudent retirement planning can help you mitigate such shocks to a great extent

Protection from Taxes – Taxes and Inflation are the two biggest enemies of a retiree. Most retirees look at gross income (before tax) while deciding on optimal investment options or strategy. The good news is, you can reduce the tax liability using simple techniques and hence higher income in hand.

Why and how an early start helps
It is often said that starting early helps savers more than someone starting to save at a later date. If you start late you have to invest a disproportionately higher amount to get the same corpus on retirement. Starting early gives more time to your investment to benefit from compounding. Let's see how:

TABLE 1

How starting to save early helps			
		Late by 5 years	Late by 10 years
Scenario	A	B	C
SIP amount (Rs)	10000	17000	29000
Tenure	30	25	20
CAGR	10.00%	10.00%	10.00%
Principal invested (Rs)	3600000	5100000	6960000
Corpus (Rs)	2.3 crore	2.3 crore	2.3 crore

- A delay of 5 years means your monthly SIP amount has to go up by 70% to get the same corpus.
- A delay of 10 years means the SIP amount has to be 3 times of the original amount, in order to get the same corpus.

Starting your Retirement Planning early in life puts you well on course to build a secure future. If you start late, you have less time to achieve your financial goals, and the time horizon plays a massive role in shaping your corpus.

Moreover, in a conventional setup, one would look to retire around 60. For this, you need to start planning for your Retirement at least by your 30s. But what if you want to retire by 50, then automatically, the Retirement Planning has to be done in the 20s.

The bigger the time span you give the Retirement Plan to grow, the bigger the Retirement Corpus becomes. The first few years of your employment / profession, when you have fewer expenses and responsibilities, is the best period to start planning for your retirement as you can save and invest more.

Three phases of retirement

When the destination is far-off, we generally do a break-journey. Similarly, to reach your destination of a comfortable retirement, you need to make the best use of the three phases of your retirement plan.

Accumulation phase – The Accumulation phase in retirement planning consists of that time-period when an Individual is earning, saving and investing to build an adequate corpus by the time of retirement. Typically, it starts around age 25 and goes till age of around 50. Simply put, the time from the start of your career till retirement is the accumulation Phase. The main objective in this phase is to maximize your retirement corpus at the time of retirement. As per experts, the sooner you begin this phase, the better it will be for the final retirement corpus. An early start will give your investments more time to benefit from the power of compounding.

Your investments and contributions in PPF, EPF, NPS, mutual funds are all a part of the accumulation phase. The money saved in these investments help you accumulate funds towards your retirement goal.

Consolidation Phase – At an age between 50 and 55, you reach the Consolidation phase when you start consolidating all your assets and investments to get a clarity on where you stand. By the time you reach this phase, you would have already accumulated a sizable amount of funds. This stage is very crucial as it marks the first step towards a retirement that you had envisaged early on in your career. Committing mistakes at this stage should be avoided at all cost. Here, you need to take stock of any shortfall and take appropriate action to enhance the last-mile investment to accumulate the maximum before retirement.

Distribution Phase – The Distribution phase in retirement planning begins with the advent of your Retirement. Post-retirement, you no longer have a regular income source, and you begin to withdraw money from your Retirement corpus to meet your various needs. With no more paychecks coming along and expenses still existent, shifting from Accumulation to the Distribution phase can be a tricky task.

Annuity Plans

When it comes to planning your retirement, there are exclusive annuity plans to help you meet your retirement needs. Certain annuity plans are for during the accumulation phase and are meant to grow your money till retirement. These plans are called deferred annuity plans and NPS is a good example of such plans.

The other type of annuity plan is the Immediate Annuity scheme. An investor can park a lump sum amount in an Immediate Annuity scheme and start getting an annuity. Annuity means a regular income which can be monthly, quarterly, half-yearly or annually.

Simply put, deferred annuity plans help to grow money and Immediate Annuity plans fetch a regular income to the investor. Taken together, a deferred annuity and an Immediate annuity scheme completes the retirement planning cycle for the investor.

Impact of inflation

One big factor that will play a major role in your retirement journey will be the impact of inflation. Inflation diminishes a retiree's buying power. Even if overall inflation remains low, some components such as Healthcare tend to grow at a higher rate. Your expenses on healthcare tend to go higher (as a proportion of your total expenses) as you age. The impact of Inflation, if not provided for, can be devastating in your post retirement life.

Let us see how inflation impacts your expenses and income requirement:

TABLE 2

Impact of Inflation: An illustration					
	Rate of inflation				
Monthly Expenses	**2.00%**	**3.00%**	**4.00%**	**5.00%**	**6.00%**
Today	50000	50000	50000	50000	50000
After 10 years	60950	67196	74012	81445	89542
After 20 years	74297	90306	109556	132665	160357
After 30 years	90568	121363	162170	216097	287175
After 40 years	110402	163102	240051	351999	514286

See how inflation increases your expense budget over time.

- At inflation of 4% p.a. your monthly expenses double in 20 years, more than triple after 30 years and multiply by 5 times after 40 years.
- Imagine you target a retirement corpus of Rs. 1 crore assuming monthly expenses at Rs. 50,000 today, and, by the time you retire in 30 years, you find you actually need Rs. 3 crores, as expenses have tripled!
- And then someone tells you that your expenses are going to multiply by another 5 times by the time you reach age 100!

Role of equity mutual funds

While saving towards retirement, proper asset allocation is also important. Asset allocation is all about investing in the right asset class, which is suited to your investment objective. Since retirement is a long term goal, it makes sense to invest in equity which has the potential to generate high inflation adjusted return over the long term.

Therefore, for saving towards retirement, equity mutual funds can be a good starting point. An early beginning in investing in equity mutual funds also inculcates a disciplined habit of investing.

Start systematic investment plan (SIP) in 2-3 consistently performing mutual fund schemes and keep investing a fixed amount in them. A review of their performance may be done at a regular interval but never try to time the market looking at market conditions. At times, when the market falls, use it as an opportunity to invest more into the same fund folios.

Markets remain volatile on the short-to-medium term but average-out and tend to drift upwards over the longer horizon. An investor having seen the ups and down of such a market remains poised for the long haul and is largely undisturbed with such frequent fluctuations. And most importantly, mistakes made during the initial days of investing helps one learn the basics of investments that come to rescue in the later stages of life.

End Note – Before you start saving for retirement, work out the numbers conservatively keeping your current expense and inflation into account. You will be pleasantly surprised that even with saving a small amount each month, the power of compounding will help you accumulate a large enough corpus to live through the non-earning period of over 30 years comfortably. Afterall, you want to enjoy the financial freedom to the hilt after you retire.