

**Title: 17.5% tax free Fixed Deposit for 30 years. Interested ?**

**Country: INDIA Date: 27<sup>th</sup> November 2009 No of Pages: 2**

Very often in public seminars I do get an opportunity to talk on investments and interact with retail investors on it. I make it a point not to miss it, especially when the markets are at extremes; Very high or Very low. One selfish motive is that it keeps you grounded and such interaction's enables me to think from the perspective of non-professional investors. It makes me understand the issues and dilemma's confronted by small investors.

The most discussed and debated issue is such public seminars in the Questions & Answers session is "How to create and sustain wealth? ". Many of the investors are of the opinion that managing investment's or wealth creation is a complex job. And one can learn it only with help of complicated models, advanced software and fat books. It remains a myth. If that was the case, legendary value investors, like Graham and Dodd would have never been successful in the 1930s when the world was grappling with the Great Depression. Simplicity was there virtue.

One doesn't need to be knowledgeable or have a doctorate in investment management to create wealth. It's much simpler than the rocket science it appears to be. One requires some basic skill sets and more importantly DISCIPLINE to make investments work for you and achieve your financial goals.

Every one of us had Mathematics as a subject at school or college levels, where we learnt addition, multiplication, simple or compound interest etc. Understanding "Multiplication" is surprisingly one of the most vital inputs in managing your money. Multiplication or compounding (cumulative multiplication) has overwhelming influence on long term wealth creation.

Your wealth creation is a function of three simple factors:

1. For how many years you have saved and invested?
2. What are the returns on your investments?
3. To what assets you have allocated your wealth?

Before coming to the above principles, I would like to dwell upon another myth on making creating long term wealth. Wealth cant be created by making large one time bet, which turns out to be profitable. Though an one time bet would be largely profitable, it will never make substantial wealth or large fortunes. But on the other hand, a large bet which turns sour could wipeout equally larger fortunes and more importantly might deprive the investor of subsequent profit making opportunities. Similarly large fortunes are hardly made out of your monthly wages or the bonuses and adding them over your working life, though it remains an important source for long term wealth creation. But it's not the primary source.

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More than addition as discussed above, multiplication has more telling effect on investments. Coming back to the 3 simple factors :

For how many years you have been saving and investing the same regularly with lot of discipline has a larger positive impact on your wealth, rather than a one time killing you might make in the markets. That's where the power of multiplication and compounding comes into play. And the simple formulae is :

$$\begin{array}{ccc} \text{Amount saved \& Invested per yr} & \times & (1 + \text{Long Term Rate of Return in \%})^{\text{No of years}} \\ \uparrow & & \uparrow & & \uparrow \\ \text{FACTOR 1} & & \text{FACTOR 2} & & \text{FACTOR 3} \end{array}$$

For instance if you had saved & invested Rs 1,000 pm in a asset which gives you 10% pa, at end of 10,20, & 30 years you could have Rs 31,125, Rs 80,730 & 209,893 resp. Further at 15% returns pa, you could have at the end of 10,20, & 30 years you could have Rs 48,547, Rs 80,730 & 209,393.

Let's take each of the factors independently to discuss.

FACTOR 1 is a function of your post tax income less your spending. To make it simpler, lets assume to loans repayments. It's important for an investor to freeze the amount that you will save and invest regularly in a disciplined manner. If the income is volatile, the spending needs to be adjusted to maintain the savings and investment amount. Your savings should drive spending, viz spending should be adjusted to maintain the pre fixed level of savings to be invested every month. Take that amount of as a fixed expenditure like your cell phone or grocery, come what may. Higher the investments, higher will be your wealth creation.

FACTOR 2 is a function of your proportion of your assets allocated to higher yielding assets such as stocks. Stock Markets offer an excellent opportunity to create wealth in long run, even though you may not understand it and may not be able to even time it. For instance the SENSEX till date has offered you a return of 17.50% pa since its inception in 1978-79. I have not even included the dividends, which could add another 1-2%. And if you are smart enough to time the market, the returns might go higher. Treat stocks markets like a 30 year fixed deposit at 17.50% tax free, assuming there is no tax on long term gains and dividends for next 30 years. Systematic Investment Plans do this and funds market the same with this unique selling point. Higher the returns and proportion of your investments, in stock markets higher will be your wealth creation.

FACTOR 3 is simple. The earlier in life you start setting aside those fixed savings, longer will be your investment horizon and the power of compounding will make your wealth grow exponentially.

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**To conclude, One need not be a smart Harvard educated fund manager to manage your own investments. Its simpler than its made to be. All you need is DISCIPLINE,PATIENCE and some COMMON SENSE on the way to the path of Wealth creation.**

**Devendra Nevgi**  
**[deven@dgp.co.in](mailto:deven@dgp.co.in)**  
**Tel: + 91 9867 277 977**

**Delta Global Partners**  
**Founder & Principal Partner**

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