

FINANCIAL MANAGEMENT PRACTICES OF INVESTORS: AN INSIGHT FROM MONTHLY BUDGETARY ALLOCATION

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Abstract

With less than 1% of population in organized employment coupled with shifting of government focus from a regulator to a facilitator socialist welfare state the onus of retirement planning and life after retirement has been rested with individual. The budgetary allocation towards investment irrespective of its type has become imperative for investors in order to take care of their post retirement life. The study investigated budgetary allocation of retail investors for various budgetary heads which included daily necessities in order to fulfill their short term and long term goals. Two important constituents of financial management namely goal setting and budgetary allocation were inquired and it was found that majority of investors though acknowledge the importance of financial planning, they do fail to put it into practices and seldom engage themselves in record keeping and disciplined investing mode. Rather to achieve the goals majority of respondents do not have fixed provision or proportion of income that is set aside to achieve it.

Keywords- Budget, financial management practices, financial planning

1. INTRODUCTION

The benefits of financial planning cannot be denied for the simple fact that in order to take care of one in gray days, would require greater diligence towards expenses and income. Though there seem to be diverse views about savings and investment two school of thoughts seem to be dominant, one which views Savings= Income –Expenses, whereas other views Expenditure= Income-Savings. Both school of thought are widely popular and have their own viewpoint which view savings from different perspective. One of the most important basic steps in financial planning is goal setting followed by budgetary allocation.

Both, goal setting, budget preparation and allocation

are primary requirements of financial planning. According to the FPA, financial planning is a process that "involves taking stock of all your existing resources, developing a plan to utilize them, and systematically implementing the plan in order to achieve your short- and long-term goals" [Financial Planning Association (FPA), 2007a].

Coined in other words the process of financial planning involves following key steps

- a) Finding out present net worth of an individual.
- b) Formation of objectives
- c) Estimating future cash inflows and outflows (Budgeting)
- d) Keeping track of current expenses (Record keeping).

As Garman et al, (1999) point out that Recordkeeping, Budgeting, Comparison and Estimation of net worth are four essential prerequisite of effective financial management. The benefits of financial planning though universally agreed are difficult to quantify for each individual. The benefits of using a financial plan potentially include increasing wealth, protecting wealth and smoothing consumption. The investors who refer to a financial planner can feel confident about their investment decisions as they are endorsed by experts. As quoted that sound financial management practices are at base of overall happiness which shall lead to lower stress, and sound financial management practices in turn are a part of financial advice by most of financial planners. "Financial advisors encourage people to examine their most basic desires and priorities, establish concrete goals, withstand (and even taken advantage of) adverse events, and feel confident about their future."

Macro economic factors influencing financial planning

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Macro economic factors influencing financial planning

In India the government has decided to withdraw pension benefits for those employed after 2004. Hence it has introduced the National Pension scheme where a participant according to his risk appetite chooses any of the options. At the backdrop of this the onus of managing one's retirement now rest with an individual who would be required to exercise more prudent choices of investment and shall need a professional help to manage it.

As have pointed out Life Expectancy has increased and will continue to increase. This increased life expectancy means more years in retirement which ultimately would not be painful unless and until properly planned and thought of.

Current and future retirees will face rising cost of health care. Those rising cost combined with increased life expectancy will require planning over a longer lifetime. The average education level has been increasing in India for the past few years. "Research suggests that Individuals with higher education attainment were more likely to seek help of financial advisor."

As both the macroeconomic and micro economic factors point towards the growing importance of financial planning for individual investors it would be worthwhile to inquire the responses of these individual investors towards basic building blocks of financial planning namely goal setting and expenditure pattern or allocation towards investment.

Statement of Research Problem

As the present study deals with inquiring two primary steps in financial management practices including goal setting and budgetary allocation the research problem in the present study could be stated as follows

"To what extent financial management practices such as goal setting and budget allocation are adopted by individual investors?"

OBJECTIVES OF STUDY:

The objectives are as follows

1. *To understand the extent to which financial planning practices are adopted by investor.*
2. *To understand the adoption of financial goal setting amongst individuals.*
3. *To understand the budgetary allocation or percentage of income allocation on various expenses.*
4. *To understand the investment allocation amongst individual investors.*

2. Literature review

Financial management practices such as goal setting and budgetary allocation towards savings and investments is strongly associated with attitude towards retirement planning. conducted an exhaustive qualitative study to understand the gender differences towards retirement planning. The findings from the in-depth interviews conducted by them indicate that males and females adopt different perspectives when it comes to retirement planning.

"Males tend to adopt an individual choice perspective, whereby it is assumed that retirement will be another stage in life which will provide for a lifestyle conducive with their current standard of living. Women, on the other hand, adopt very much a life course perspective, which makes no assumptions or predictions about future life stages, but one that views outcomes as contingent on the circumstances of one's life." Similarly some studies are also found to understand the association of occupation with retirement planning. As find in their study that a large number of business owners reveal that they do not have any retirement plan nor do they engage in systematic retirement planning. This may be since many business owners are self-employed, it is accordingly difficult to characterize exactly what "retirement" might entail for this group.

"Planning is strongly correlated with financial and political literacy and that the relationship between planning and wealth remains strong, even after controlling for many socio demographic factors."

"Majority of individuals face difficulties in planning for retirement and lacking financial literacy seems to lie at the heart of the problem. Personal mastery, along with health, income, and job conditions, are key predictors of planning. Also important are prior biographical pacing, gender, and relational contexts (at home and at work)."

Though there is no dearth of literature on retirement planning efforts and its relation to socio economic and demographic variables of the respondent but as noted, the majority of Asians are either self-employed or work on a part-time basis. Additionally, many of these individuals expect to continue working as long as their health permits. To these individuals, therefore retirement as a complete termination of full-time work is immaterial. The present study shall help us understand the attitudes towards retirement, average age of retirement, retirement efforts and its association

with financial literacy can be generalized in the Indian context.

“Among the respondents whose annual income is below Rs1.00 Lakh save to create wealth and to meet contingency. They are conservative risk takers and have invested in insurance. Among the respondents whose annual income is between Rs 1.00 and 2.00 Lakhs save to create wealth and for contingency management. Among the respondents whose annual income is between Rs 2.01 and 3.00 Lakhs, 45% of their savings objective is to create wealth, 38% are moderate risk takers and 28% are conservative risk takers. Among the respondent whose annual income is above Ruppees 3.00 Lakhs, 41% of their savings objective is to create wealth 41% are moderate risk takers and 41% are conservative risk takers.”

“Investors' major saving objective is wealth maximization, contingency management and Children welfare. Investors reveal that most of them are unlikely to meet their financial goals: be it for their retirement or children's education. This is because they don't have a proper financial plan. Very few respondents plan their savings well in advance every month. Mostly investments are made in a random fashion. Sometimes there would be a goal in mind, but even in those cases there won't be any follow up. In most cases, people don't bother to review their investments periodically and make additional investment if needed to realize their goals.

3. Methodology

Based on the classification of Ahmednagar district according to the population size three broad strata as suggested by the District Statistical Authority are as follows

1. Ahmednagar Municipal Corporation
 2. Talukas having Municipal Corporations include R a h u r i , S h r i r a m p u r , P a t h a r d i , Shrigondha, Sangamner, Kopergoan, Rahta..
 - Talukas not having Municipal Corporations Akola, Shevgoan, Parner, Karjat, Jamkhed, Newase.
- A sample of 225 respondents was taken from two strata and 150(0.03%) was selected from the Ahmednagar City based on the connivance.

Data collection Instrument

A structured closed ended questionnaire was used for recording the responses of respondent. The questions included multiple choice questions, dichotomous

questions and also questions based on a 5 point Likert scale. The data and information for the study is collected through primary as well as secondary sources. In the primary source, structured questionnaires are used to collect the information on various aspects of financial management from selected respondents.

In the general information along with name his/her qualification, profession, contact details, age and gender, these attributes are covered. Other three questions are based on five points or three point likert scale. Setting of goals, investment provision and means to achieve goals, methods of record keeping are some of the attributes which are covered in financial management practices of selected respondents.

4. Discussion

The family budgeted expenditure in terms of percentage of total income on accounts like grocery, clothing, education, fuel, health, travel, bills including electricity, telephone, house rent, entertainment and investment was collected from respondents. The different accounts were analyzed by using Principal Component Analysis in order to form different groups of account according to importance level. The four principal components or group of accounts are given below according to descending order of importance level.

Group One: *Grocery and Clothing*

Group Two: *House Rent*

Group Three: *Bills, Entertainment, Investment*

Group Four: *Education, Fuel, Health care*

The above grouping is consistent with the essentials needs of human being as discussed in economics. The mini tab output of Principal component analysis when only four components are extracted is given in table 1

Table 1: Component Matrix

Variable	PC1	PC2	PC3	PC4
Grocery	-0.374	0.002	-0.268	0.186
Clothes	-0.349	-0.193	-0.279	-0.328
Education	-0.310	-0.271	-0.334	-0.423
Fuel Expense	-0.312	0.186	0.093	-0.468
Health care	-0.375	0.045	-0.233	0.401
Travel	-0.348	0.175	-0.155	0.496
Bills	-0.209	-0.417	0.492	0.106
House rent	-0.057	-0.748	0.137	0.178
Entertainment	-0.349	0.225	0.415	0.004
Investment	-0.338	0.194	0.468	-0.101
Eigen Value	0.534	0.493	0.437	0.391
Proportion	0.053	0.049	0.044	0.039

Highlights of Group One

In group one 39.61% respondents have 5-10% budgeted expenditure on grocery and cloth each. Even 7.2% respondents spend 10 %to 15% of their gross monthly house hold income on grocery and 5% to 10% on clothing. The percentage respondents spending 10% to 15% on grocery and clothing are 6.51%. There are very less percentage of respondents spending 20% or more of their gross monthly household income on these two accounts.

Highlights of Group Two

It is found that 27.4% respondents spend 5% to 10% of their gross monthly household income on house rent. There are also 63.02% respondents spending 10% to 15% of their gross monthly house hold income on house rent. Even nearly 10% respondents have not given any response to budgeted expenditure on group two items as this might may be because they have owned houses. None of the respondents communicated that their monthly budgeted expenditure on house rent is more than 15% of their gross monthly house hold income.

Highlights for Group Three

It is observed that 21.6% respondents spend 5% to 10% of their gross monthly house hold income on different bills such as light, electricity etc. There are 11.50% respondents spending 10% to 15% on different bills. These respondents have not mentioned any budgeted expenditure on entertainment and investment. There are 9.14% respondents having budgeted expenditure of 5% to 10% of their Gross monthly house hold income on each of three accounts in group three. The number of respondents spending 10% to 15% on bills and 5% of gross monthly house hold income on entertainment and investment each are 6.99%. Even there are 6.09% respondents having their budgeted expenditure of 10% to 15% of their gross monthly house hold income on each of these three accounts. None of the respondents communicated that their monthly budgeted expenditure on either or all three accounts is more than 15% of their gross monthly house hold income

Highlights for Group Four

The percentage respondents with 5% to 10% expenditure on education, health and travel of their gross monthly household income are 15.24%. The expenditure of 6.09% respondents on education, health, travel and fuel is 5% each of their gross monthly household expenditure. The percentage of

respondents spending 20% or more of their gross monthly household income on fuel is incurred by 2.63% respondents. On health 5.40% respondents incurs 20% or more of their gross monthly household income. Even 12.74% respondents incur expenditure of 20% or more of their gross monthly household income on travel.

Highlights for budgetary provision on investment

The respondents planning to have 5% to 10% of their gross monthly household income on investment per month are 26.32%. Even 18.84% respondents also plan 10% to 15% of their gross monthly household income on investment. Majority of respondent (54.85%) do not conveyed any response on budgetary provision of investment.

Goal Setting by Investors

Every family or individuals have certain goals or objectives in life. In present study objectives are classified as short term and long term objectives. It means that objectives which are planned within next 5 years are referred as 'short term objectives' whereas objectives that are panned after 5 years or more are treated as 'long term objectives'. Since these two types of objectives have effect on investment decision and investment options, using factor analysis different future plans are factorized into three factors as follows.

Factor One: *Purchase of land, construction of house, purchase of land and development of land;* this factor mainly deals with 'infrastructure development'.

Factor Two: *Marriage and Education of self, near and dear ones;* this factor mainly deals with 'Human resource development'

Factor Three: includes all other plans that are not included in the list.

One can develop infrastructure either for residential that is noncommercial purpose or for commercial purpose or both. Purchasing a plot or land and constructing a house or bungalow is mainly for residential purpose or noncommercial future plan whereas purchasing an agricultural land and developing it is a common future plan. Therefore in the first factor separate summary of Noncommercial and commercial future plan is given in table 5.15 and 5.16.

From table 2 it is seen that 46.26% respondents do not have any short term or long term plan of noncommercial infra-structure development. 17.04% respondents have long term plan of purchasing a plot

and constructing a house where as 8.86% respondents have some short term plan.

Table 2: Distribution of respondent by noncommercial infrastructure development plan

S.no	Purchase of Plot		Construction of House		Number of respondents	Percentage of respondents
	Aft er 5 years	Ne xt 5 years	Aft er 5 years	Nex t 5 years		
1	N	N	N	N	334	46.26
2	N	N	Y	N	43	5.94
3	N	N	N	Y	32	4.43
4	Y	N	N	N	46	6.37
5	Y	N	Y	N	123	17.04
6	Y	N	N	Y	40	5.54
7	N	Y	N	Y	16	2.22
8	N	Y	Y	N	24	3.32
9	N	Y	N	Y	64	8.86
Total					722	100

6.37% respondents have only long term plan of purchasing a plot where as 2.22% respondents have short term plan of purchasing a plot. 96% respondents have long term plan of construction a house or bungalow where as 4.43% have short term plan of construction of house or bungalow. 49.72% respondents have neither long term nor short term plan of commercial infrastructure development. 15.10% respondents have long term plan of purchasing and developing agricultural land where as 5.68% respondents have short term same plan. 1.52% and 1.80% respondents respectively have long term and short term plan of purchasing agricultural land. 10.53% and 5.54% respondents respectively have long term and short term plan of developing land. The summary of second factor including marriage and education is given in table 3

Table 3 Distribution of respondents according to human development plan

Sr. no	Marriage		Education		Number of respondents	Percentage of respondents
	Aft er 5 years	Ne xt 5 years	Aft er 5 years	Ne xt 5 years		
1	Y	N	N	N	44	6.09
2	N	N	Y	N	45	6.23
3	N	N	N	Y	75	10.39
4	Y	N	N	N	12	1.66
5	Y	N	Y	N	90	12.47
6	Y	N	N	Y	198	27.42
7	N	Y	N	N	13	1.80
8	N	Y	Y	N	63	8.73
9	N	Y	N	Y	182	25.21
Total					722	100

From table 5.19 it is seen that 6.09% respondents have no short term or long term plan of self or family development. 12.42% respondents have long term plan of marriage as well as education where as 25.21% respondents have same short term plan. 1.66% and 1.80% respondents respectively have long term plan and short term plan of marriage. 6.23% and 10.39% respondents respectively have long term and short term plan of education.

5. Conclusion

Percentage of respondents having self or family development plan are very high whereas percentage of respondents having plan of commercial infrastructure development is less among three groups. 48.34% respondents do not have any other plan. 39.75% respondents have some other long term plan where as 11.91% respondents have some other short term plans. The respondents having some other plan also have either or all future plan regarding family development and infra-structure development.

As goal formation is described as crucial step in financial planning the respondents were asked about their future intentions such as marriage, education and many other goals and were also requested to specify the time frame for achievement of these goals. It was observed that almost 50% of the respondents have not conveyed their intentions either in coming 5 years or next 5 years for commercial infrastructure development which includes purchase of agricultural

land or development of land. Percentage of respondents having self or family development plan are very high whereas percentage of respondents having plan of commercial infrastructure development is less among three groups. This means that investors are looking for products which can satisfy their goals of self-development such as education and marriage. Also it can be seen that with increase in gross monthly household income attitude of long term commercial infrastructure development shifts to short term commercial infrastructure development.

It can be observed that 80% financial planners agree that clients can state their short term and long term goals which are goals to be achieved in coming 5 years and after 5 years respectively.

As income and expenditure pattern influences saving and investment decisions which in turn may affect the propensity to avail consultancy of financial planner the investors were asked to describe their expenses on various heads. It can be observed that highest preference was given to grocery and clothing and least preference was given by investors for budgetary provision for expenses on education, fuel and healthcare.

Majority of respondent (54.85%) did not convey any response on budgetary provision of investment. This in turn means that investors or respondents in the present study lacked fixed provision on investment.

As financial management practices and attitudes towards them form basis for availing professional advice respondents were queried on such practices. 47.09% respondents keep track of different transactions by self-memorization while 38.78% respondents use diary for the same. About 48.20% respondents have not given any response on the use of any of three methods for recording their financial transactions. In general non response level is high which might be because individuals are not well aware about the benefits of financial planning through keeping records.

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