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Switching Investments Frequently: Not A Good Idea!

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I am a 30 year old, planning on buying a life insurance policy as I do not have any insurance, so far. I am told that buying an endowment policy will give me cover and also make a good long term investment at the same time. The yearly premium will be ₹1 lac for 30 year with a cover of ₹26 lacs. I will also get a bonus on maturity. Is this the right thing to do?

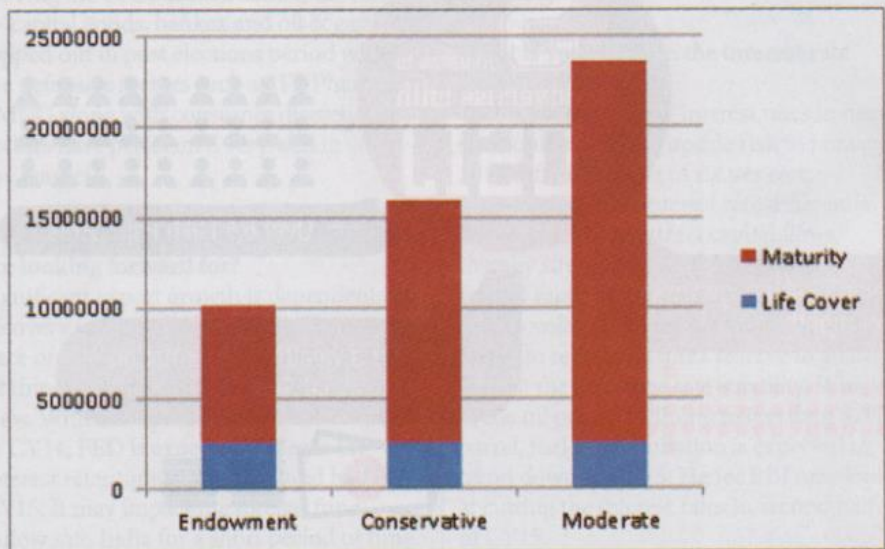
- Sunder Pillai, Mumbai

Sunder, the happy thing is that you have woken up to the fact that you need to protect your family and secondly to invest! I would like to examine the second proposition, first – that of the endowment plan being a worthwhile investment for the long term. Though you have not mentioned the name of the company, I shall go by past experience as to the bonus rates and eventual returns from such plans. If one survives the policy term, the sum received on maturity would translate to an annual compounded return of about 4.5% to 5.5% per annum only. Even a PPF can do better at 8.7% per annum, tax free!

But what about the protection that one would get from the insurance policy? The

same protection can be got from a term life policy, too. The premium for your age would be only ₹5,000 per annum on a ₹26 lacs policy. Of course, in a term policy there is no maturity sum – only a death benefit of the sum assured. (Let us remember that the point of taking an insurance cover is a death benefit for the family.) And you are still left with ₹95,000/- every year to save! This amount saved in a PPF will return you

₹1.33 Crores at the end of 30 years!! With such a combination one can get the protection and a better investment return. If one were a more aggressive investor and invest in a mix of PPF and Equity Linked Savings Scheme then your gains could be even more, in the region of ₹2.1 cr at the end of 30 years, if one were to assume a rate of return of 15% pa from ELSS.



ENDOWMENT VERSUS TERM LIFE + INVESTMENT COMBO

But again, of what consequence is ₹26 lacs as a death benefit to your family? It will hardly be of any economic relief. You must look at a policy of at least ₹1 crore so that the family receives a meaningful amount if you do not survive the policy. In the case of a traditional plan, the premium would be prohibitive for this size policy – but in the

case of a term life policy it would cost only ₹11,000 per annum of premium at your age. This is affordable. The balance ₹89,000/- when saved diligently in a PPF can fetch you ₹1.24 crore at the end of 30 years! So you can have your cake and eat it too!!

Like in the previous example, if one were a slightly aggressive investor and mix PPF

with an ELSS, he can stand to gain more, in the region of ₹2 crores at the end of 30 years!

It is important to understand that the investment plan should not get interrupted, nor should there be a temptation to frequently switch investments.

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