IndiaFirst
LIFE INSURANCE

Publication: Business Standard
Edition: National
Date: Monday, 9th June, 2014

Hold on to Ulips for 1-2 years to maximise returns

Markets are expected to rise another 20% in the next couple of years and, thus, waiting could make sense

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If you bought a unit-linked insurance plan (Ulip) in 2008-09, you probably paid a large amount as various charges. Some insurance companies charged as much as 100 per cent of the premium as allocation charge for the first one to three years. In other words, there was no money invested in the first couple of years of the policy. Consequently, even after five years, you would be sitting on a huge loss.

So, when the market goes up 20-25 per cent in a year, does it make sense to exit?

The good news is that you can exit easily now also if you want to because you have completed the lock-in period of three years mandated for Ulips bought pre-September 2010. Those who bought Ulips post September 2010 can't exit now because the lock-in period was increased to five years and most of these individuals would not have completed this.

As for exiting Ulips on the back of upbeat markets, insurance experts feel this is not an opportune time as the markets are expected to do even better. The benchmark indices are expected to gain another 20-25 per cent in the next one or two years. The Sensex and Nifty have scaled record levels after the Narendra Modi-led Bharatiya Janata Party secured a majority at the Centre. The Sensex moved up to 25,019.51 from 24,121.74 on May 16.

Most importantly, you should wait to recover your capital invested. Say you had invested ₹1 lakh every year between 2008-09 and 2013-14, or ₹5 lakh in the past five years. As some insurers charged up to 100 per cent of the annual premium in the first couple of years, your investment in the first two years could have been zero. Even from the remaining ₹3 lakh you invested between 2010-11 and 2013-14, the investment charge would have been very high and you would have invested close to ₹2 lakh (or even less in many cases).

Certified financial planner Anil Rego advises comparing the cost of maintaining the Ulip investments and starting a new investment. That is, calculate the cost of surrendering Ulips and investment charges for subsequent years. Ulips charge a fee for mid-term surrender. These could be up to 100 per cent of the fund value in pre-September 2010 Ulips (25-50 per cent in older Ulips and average seven per cent in new Ulips). Of course, the cost reduces as the policy tenure progresses. "If the charges are high for Ulips, you may want to exit," he says.

Charges in a Ulip include mortality charges for the life insurance provided. In addition, premium allocation charge (average seven per cent), fund management charge (1.35 per cent) and administration charges (as percentage of premium a fixed ₹50) are applicable. Mutual fund charges include the annual fund management charge (1.25 per cent) and an exit load (typically one per cent), if applicable.

As the stock markets didn't go anywhere in the past five years, you would have made very little money. According to data from Morningstar Life Insurance Corporation's Money Plus Growth has returned close to nine per cent in the past five years. Similarly, SBI Life Insurance's Equity Fund returned nearly 14 per cent in the past five years and PNB Met Life's Multiplier Fund II returned close to 10 per cent in the past four years. (*see table*).

This implies, someone who invested ₹2 lakh would be sitting on ₹2.18 lakh with LIC's Money Plus Growth, ₹2.28 lakh with SBI Life's Equity Fund and ₹2.20 lakh with PNB Met Life's Multiplier Fund II. Would you want to exit with less than half the capital invested? The answer should be no.

Even if your Ulip had followed the index you would have made only only 11 per cent in the last five years or ₹2.22 lakh, just half the capital invested. The BSE's Sensitive Index or Sensex has returned nearly 27 per cent in the past year and close to 11 per cent in the past five years. National Stock Exchange's 50-stock index or Nifty has returned 25 per cent in the last year and 10 per cent in the past five years. Both the Sensex and Nifty are among the best performers in the emerging economics with over 15 per cent gains since the beginning of 2014.

P Nandgopal, managing director and CEO of IndiaFirst Life Insurance suggests switching instead of exiting. "Move to debt or balanced fund options and at a later date move back to equities. Redeeming will cap your returns," he explains. Ulips allow switching between funds. On an average, four annual switches are free of cost. Or, you also have the option of re-directing future premiums into a new fund and leaving the current investment untouched.

Debt funds did very well in the past five years with nine per cent average annual returns. But even those who had invested in debt funds of Ulips would not have been able to recover their capital. In fact, insurers are of the view that those who missed the ongoing rally can take advantage of it even now, over the next two years.

Says Sanjeev Pujari, chief actuary at SBI Life Insurance, "Though this may seem like an opportune time to exit Ulips, staying put will help get better returns. Also, one should exit only if there is a better alternative for investors." Additionally, redeeming from Ulips will lead to losing out on the insurance cover also, he adds.

Typically, mutual funds are recommended as better investment products to Ulips because those are pure investment products and cheaper than Ulips. Pujari of SBI Life Insurance argues mutual funds have a risk-reward mandate and, hence, are meant for churning out the best possible returns. But the same is not true for Ulips.

LONG-TERM PLANS FOR LONG-TERM GAINS

Returns (%)	1-year	2-year	3-year	4-year	5-year
HDFC Life – Growth Fund Investment Life	35.02	28.37	11.74	9.70	13.39
ICICI Prudential Life – Maximiser Fund II	31.78	27.15	13.02	11.65	13.98
PNB Met Life – Multiplier Fund II	24.25	22.70	10.37	9.73	-
SBI Life – Equity Fund	29.69	28.49	13.87	12.63	13.95
LIC of India – Money Plus Growth	26.17	20.84	9.18	8.16	8.80

Source: Morningstar

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