When to go for traditional insurance policies and when to opt for Ulips

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CHOOSING the right life insurance product is not easy. It requires careful thought and consideration, and, a thorough evaluation of your present financial circumstances and your requirements in the future.

Life insurance products are broadly categorised into traditional and unit-linked (most commonly equity-linked) products. The difference between traditional and equity-linked products depends on whether the investment risk is borne by the insurer or by the customer. In simple terms, a traditional product is where the premiums are invested by the insurer (as per the regulatory investment guidelines) and the customer gets certain guaranteed and non-guaranteed benefits for paying premiums. In unit-linked products, the customer chooses (from a list of available funds), the investment option, and, his/her premiums are allocated after deducting charges. The value of these invested funds could then go up or down depending on the performance of the underlying investment (typically equity shares), and this risk is borne the customer and not the insurance company.

So, how does one decide which product is more suitable? Before buying, it is important that you review your financial plan.

One should note that the core objective of buying insurance is protection of the family in unfortunate circumstances. Whichever type of product you choose, first ensure that the level of protection is in line with your requirements, that is, your income, number of dependents and age. In both traditional and unit-linked products, you can tailor the protection level by choosing the appropriate sum assured and add-on protection riders. Once your family protection is assured, we can set out some general guidelines.

Are you comfortable with investment risk? The past experience of investment returns suggests that equity investments have the potential to deliver superior returns over a longer period of time. In the interim, however, your investment value will go up or down. Higher the investment risk, higher the potential reward. Hence, if you are looking for longer-term gains, and have the risk appetite of being comfortable with your investment values moving on a daily basis, go for equity-linked products. Traditional products, typically, invest a limited (regulated) percentage in equity and, hence, the potential returns are lower.

Do you need your investment to provide a minimum guaranteed return? Traditional products will, typically, guarantee the payment of the 'sum assured' on maturity or in the unfortunate event of death of the insured. For equity-linked products, if you have the choice of equity investments, then, there is no guarantee of return or protection of the invested capital.

Are you likely to change or control your asset allocation during the investment period? In unit-linked products, you can see the value of your investment on a daily basis through the net asset value (NAV), published by insurers on their website. If you don't want to actively manage your asset allocation and are comfortable with the insurer's guaranteed returns over the policy term, then go for traditional plans.

Do you understand the implications of early exit or discontinuing premiums? You may be unable to pay your premiums for the planned premium paying term. All life insurance products are suitable for long-term financial goals and, hence, there are costs associated with premature surrender, and often, with discontinuing premium payments. In unit-linked products, there is a five-year lock in, during which, you will not be able to access your funds and stopping premium payments Traditional products normally provide some flexibility on withdrawals through loans against the policy, which are available from the insurer.

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