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Pros and Cons of Life Insurance Plan with special reference to ULIPs and Endowment Plan

Pooja Agrawal 1, Dr. Ugrasen 2

1. *MBA Scholar, Madan Mohan Malviya University of Technology Gorakhpur, (India)*
2. *Assistant Professor of MBA Department, Madan Mohan Malviya University of Technology Gorakhpur, (India)*

Abstract

Life insurance is a contract between an insurer and a policyholder in which the insurer guarantees payment of a death benefit to named beneficiaries upon the death of the insured. ULIP is life insurance solution that provides for the benefits of protection and flexibility in investment. The investment is denoted as units and is represented by the value that it has attained called as Net Asset Value (NAV). Endowment plan is a life insurance policy which provides you with a combination of both i.e.: an insurance cover, as well as a savings plan.

As we are aware that insurance is a way to manage the risk whereas ULIPs are not risk free investments, so a dilemma arises whether to avoid the risk or to accept risk. In this perspective, the study identifies the risk factors of ULIPs over the Endowment Plan as well as the benefits of ULIPs and Endowment Plan. In addition, the paper also investigated the preferences of the customers of Gorakhpur district regarding ULIPs and Endowment Plan. The result is that people are more conservative than being aggressive investors as they have chosen more to the endowment than to the ULIPs.

Key words: *Endowment, Life Insurance, NAV, Risk, ULIPs*

1. Introduction

It is well known fact that Insurance Industry is fundamental to the wellbeing of our society. It would have been nearly impossible for the developed economies to emerge without risk sharing. Without insurance, society's capacity to mitigate risk would be limited and the protection of assets from catastrophic loss would be impaired. Today world poses serious challenges in the form of changes in natural, economic, social, and political environment, along with the shifting of stakeholder's expectation and wide reaching technological innovations which lead to a perpetually changing and risky environment. This calls for continuous adaptation from businesses around the globe. This in turn led to the emergence of insurance industry with the ability to innovate and to deliver insurance at competitive prices which is vital for all the stakeholders.

The insurance is primarily classified based on the basis of compensation to be paid to a person for an anticipated loss to his life, business or an asset. Insurance is broadly classified into Life Insurance and General Insurance. Life Insurance is considered to be an important part of an individual's investment portfolio, not necessarily to accumulate wealth, but to feel financially secured. The life insurance keeps the family of life insurance holder

secured. The early 21st century made a grand welcome to the private sector in India. Within a period of 10 years, the entire scenario has changed tremendously with the entry of many companies. To overcome the competition between them, the life insurance companies started to offer the new policies; among those the Unit Linked Insurance Plan has changed entire performance of life insurance policies in a limited period.

1.1 Life Insurance

A life insurance policy is a contract with an insurance company. In exchange for premium payments, the insurance company provides a lump-sum payment, known as a death benefit, to beneficiaries upon the insured's death.

Typically, life insurance is chosen based on the needs and goals of the owner. Term life insurance generally provides protection for a set period of time, while permanent insurance, such as whole and universal life, provides lifetime coverage. It is important to note that death benefits from all types of life insurance are generally income tax-free.

The value for the policyholder is derived, not from an actual claim event, rather it is the value derived from the 'peace of mind' experienced by the policyholder, due to the negating of adverse financial consequences caused by the death of the Life Assured. To be a life policy the insured event must be based upon the lives of the people named in the policy. Life policies are legal contracts and the terms of the contract describe the limitations of the insured events. Specific exclusions are often written into the contract to limit the liability of the insurer; for example claims relating to suicide, fraud, war, riot and civil commotion. Life-based contracts tend to fall into two major categories:

• Protection policies - designed to provide a benefit in the event of specified event, typically a lump sum payment. A common form of this design is term insurance.

•Investment policies - where the main objective is to facilitate the growth of capital by regular or single premiums. Common forms are whole life, universal life and variable life policies.

1.2 ULIPs (Unit Linked Insurance Plan)

Unit Linked Insurance Plan (ULIPs) provides for life insurance where the policy value at any time varies according to the value of the underlying assets at the time. ULIP is life insurance solution that provides for the benefits of protection and flexibility in investment. The investment is denoted as units and is represented by the value that it has attained called as Net Asset Value (NAV). ULIP came into play in the1960s and is popular in many countries in the world. ULIPs essentially combine the benefits of an insurance policy and a market-linked investment.

As we are aware that insurance is a way to manage risk whereas ULIP are not risk free investments, so a dilemma arises whether to avoid risk or to accept risk. In this perspective, the study identifies the risk factors as well as the benefits of ULIPs over the Endowment Plan.

1.3 Endowment Plan

Endowment plan is a life insurance policy which provides you with a combination of both i.e.: an insurance cover, as well as a savings plan. It helps you in saving regularly over a specific period of time, so that you are able to get a lump sum amount on policy maturity, if the policyholder survives the policy term.

There are four types of Endowment plan:

Unit Linked Endowment Plan under unit linked policies

Full or With Profit Endowment

Low cost Endowment

Non-profit Endowment

1.4 Review of Literature

Kishore, R.B. (2006), has highlighted the success story of Life Insurance Corporation. According to him, the Life Insurance Corporation has recorded a successful growth rate of 20.6 per cent due to the introduction of time-tested traditional products and market-savvy unit-linked plans in tune with the market demands. He identifies an upward trend in terms of number of policies sold, sum assured and the total assets held by the Life Insurance Corporation. He has expressed hope that, with the vast network of the agent force, the Life Insurance Corporation would march ahead to maintain its supremacy.

Nair, K.K. (2009), conducted a study on Unit Linked insurance plans (ULIP) based on secondary data available on its emergence, concepts, parameters, benefit, current position and future outlook. The study suggested that India has a plethora of opportunities for insurance companies because three-fourth of the population was uninsured also majority of the investing population were small and medium investors and majority of the investors lacked the expertise to directly enter the stock market and earn good returns. The Study emphasized the about facts to be the reasons for increased importance of ULIP. The study observed that ULIP will continue to be a good investment option for the investors as it combines the multi aspects of insurance, investment and tax benefit.

1.5 Objectives of Study

1.5.1 To identify the risk factors associated with ULIP over the Endowment plan.

1.5.2 To identify the benefits of ULIPs and Endowment Plan.

1.5.3To determine the customer preferences between ULIPs and Endowment Plan of Gorakhpur District of Uttar Pradesh, India.

1.6 Significance of study

This study would help in explaining the risk factors of market linked products of the ULIPs plan over the endowment plan, the benefits which can be availed through both the ULIPs and the Endowment Plan and to analyze the customer's preferences of Gorakhpur district of life insurance plan with special reference to ULIPs and Endowment plan.

Since no study on Life insurance with special reference to ULIPs and Endowment plan has been done till date in the Gorakhpur district of Uttar Pradesh so, it would assist the life insurance companies and help them to take necessary steps so as to make the less preferable plan amongst the customers, a preferable one.

1.7 Methodology of study

Sources of data

The source of data for research work is grouped as

- Primary source
- Secondary source

Primary data is collected from the policy holders of life insurance companies through questionnaire. And the secondary data is collected from the insurance company's articles, website of IRDA, magazines, journals, and internet.

Type of Research Design used is Descriptive in nature.

For the purpose of Questionnaire, the data is collected from the area of Gorakhpur district in Uttar Pradesh, India. The sample size used is 210 and the sampling technique is convenient sampling.

2. Risk Factors of ULIPs over the Endowment Plan

Risk is a term that keeps coming up invariably during discussions of investment. Thus, it is essential that one understands what risk is and its different types. Any uncertainty in the return rate of any investment cites it as a risk. Higher risk higher gain is one of the most commonly used phrases in the investment world. Any positive or negative deviation from your expected return numbers is a risk.

2.1 Market exposure

Any fund which deals with the capital market faces the fluctuations in it and thus there is no guaranteed return which it can assure.

The NAVs of the fund may also go up or down on a regular basis depending on the equity market or even the changes in the interest rates.

This is the basic difference between the ULIPs and the Endowment Plans.

2.2 Performance Indicators

One of the most common and effective way of selling an investment tool is to show the successful past results which makes good impression on the customers and influences them to buy it.

Although it looks that the past data are good indicators and will also be continued in the likely way in future but they are merely the past data and cannot predict the guaranteed fruitful future of investment tools.

2.3 Risk of Liquidity

ULIPs have a lock in period of five years within which you cannot withdraw your money. On emergency, if you withdraw the money prematurely then as a result you will lose out some money. You end up paying additional charges on surrender of the policy prematurely.

2.4 Higher cost

ULIPs because of several charges (like fund management charges, administration charges, mortality charges etc.) annexed to it add risk for its investors. In case the capital market goes down, the fund value and in turn the portfolio value also goes down. And with the higher costs, it becomes double risky.

A ULIP is perfect investment tool for someone who just wants to invest their money and leave it. Anyone with a mid-term to long-term view can park their money in this instrument. Because they provide a wide array of funds to choose from, it caters to people from different life stages as well.

3. Key Benefits of ULIPs

In terms of return, equity-oriented schemes like equity-linked savings schemes (ELSS) and unit-linked insurance plans (ULIPs) score over other instruments. ELSSs are tax-saving mutual funds, while ULIPs are insurance plans that invest in the stock market through a mix of equity, balanced, and growth schemes.

3.1 Lock-in period

Since ULIPs come with a lock-in period of five years, thus it helps in developing a habit of disciplined investing. In ULIPs, tax benefit can be availed every year till the premium paying term.

3.2 Potentially better return among peers

ULIPs help in earning better return than any other insurance product because of its equity advantage. The premium paid by policyholders can be invested in various asset classes through different funds. Unlike fixed deposits, which too come with a lock-in period of five years, maturity amount is tax-free in the hands of the policy holder.

3.3 Flexibility

ULIPs come with the option of switching funds during the term. The policy holders can choose among the growth, equity, balanced, income funds as per their risk capability. Generally, four switches are allowed free of cost per year.

4. Key Advantages of Endowment plan

4.1 Safe

Albeit the lower returns on endowment plans, they are risk-free in terms of the sum assured unlike the ULIPs and thus they are safer.

4.2 Loan facility

The endowment plan facilitates the loan providing as and when needed and this is usually without the need to secure the loan against collateral.

4.3 High liquidity

Endowment policies are highly liquid in nature.

5. Customer preferences between ULIPs and Endowment Plan in the Gorakhpur region of Uttar Pradesh, India

5.1 Results, Analysis and Interpretation

The survey was done on 210 respondents who were all aware of the life Insurance plan. 200 responses were the usable ones out of 210 as 10 of the respondents had not taken any life insurance policy. Thus the total number of analyzed responses here is 200.

5.1.1 Demographic information

In this survey, it has been found that the endowment plans were more preferable than the ULIPs in the Gorakhpur district amongst the policy holders. The 200 respondents included 150 males and 50 females which indicated that most of the policy holders were male in the Gorakhpur region.

Types of Plan and the Respondents of that plan (Table no. 1)

Type of Plan	Respondents
Term Plan	120
Endowment Plan	80
ULIPs	70
Child Plan	30
No Plan	10

It had been found that most of the respondents invested in the Term Plan because of their low risk appetite. The number of respondents who invested in Endowment and ULIPs were 80 and 70 respectively.

There was certain number of respondents who invested in more than one plan.

For example- A respondent of more than 50 years of age (male) who was a government employee opted for both the ULIPs and Term plan. (Refer Table no.2)

There was also certain number of respondents who opted for child plan.

Number of Policyholders divided on the basis of Gender, Age, and Plan. (Table no. 2)

Gender	Age group	Endowment Plan	ULIPs	Term Plan	Child Plan
Male	20-30	50	50	60	10
	31-40	10	-	-	-
	41-50	-	-	10	10
	›50	-	10	10	-
Female	20-30	10	10	10	-
	31-40	10	-	30	-
	41-50	-	-	-	-
	›50	-	-	-	10

It is to be noted that most of the female respondents of age group 20-40 had opted for the term plan as it is less risky. Even if they had opted for more than one plan, most of the time one of them would be a term plan.

The female respondents who were above 50 had opted for the child plan.

The endowment plans had been opted by the female respondents of age group 20-40 only and comparatively lesser number of female had opted for the ULIPs which indicated that they were risk averse.

For the male respondents, it had been found that equal number (60) had opted for the ULIPs and Endowment which indicated that males were more aggressive investors in comparison to females.

There were also certain male respondents of age group 20-30 and certain of 41-50 who had opted for the child plan.

5.1.2 Purpose of taking a particular plan

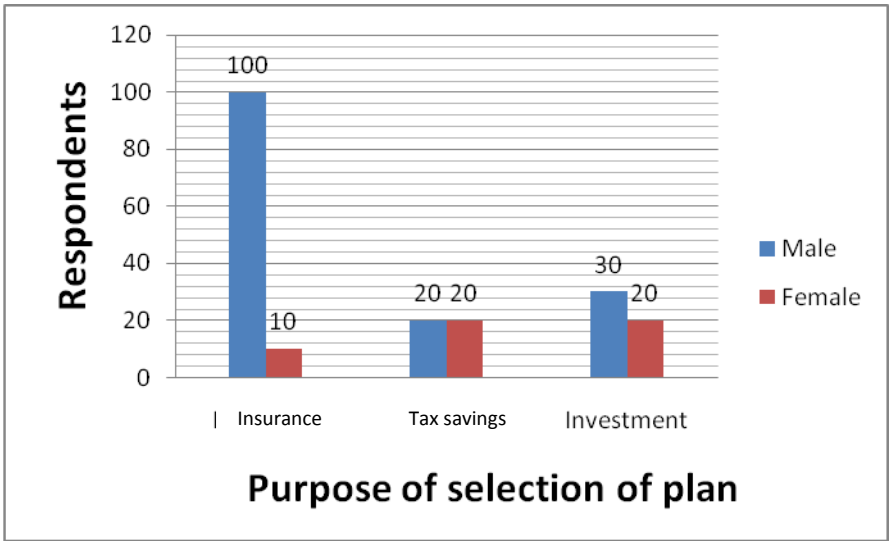

Figure no.1

Fig1. Show the purpose of respondents (male & female both) for selecting the particular plan.

Number of Respondents divided on the basis of purpose along with their respective plan (Table no. 3)

Purpose	ULIPs	Endowment	Term Plan	Child Plan
Insurance	20	50	70	10
Tax savings	20	20	30	-
Investment	30	10	20	20

When asked about the purpose of taking that particular plan, following were their responses-:

Out of 70 respondents who had opted for Endowment plan, the purpose as insurance was cited by 50 respondents and the rest said tax savings was the reason behind the selection of that plan.

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Out of 60 respondents who had taken the ULIPs, only 20 of them cited investment as their purpose and 20 as tax savings while the remaining said insurance as the reason of selection of that plan.

5.1.3 Occupation

Respondents are divided on the basis of their respective occupation for different plans (Table no.4)

Occupation	ULIPs	Endowment	Term Plan	Child Plan
Private employee	30	20	50	-
Government employee	20	20	40	20
Professional	-	20	10	-
Business	20	20	20	10

In Endowment plan, out of 80 respondents equal number (i.e 20) of respondents were the government employees, professionals, business person and the private employees.

In ULIPs, out of 70 respondents none of them are professional and equal number (i.e 20) of respondents are government employee and business person while 30 of them are private employees.

Gender	Age group	Aggressive	Moderate	Conservative
Male	20-30	30	80	20
	31-40	-	-	-
	41-50	10	-	-
	>50	-	-	10
Female	20-30	-	10	-
	31-40	-	30	-
	41-50	-	-	-
	>50	-	10	-

5.1.4 Risk appetite

The Risk appetite of the respondents are divided as per the Gender and Age (Table no.5)

On being asked to the respondents about their risk taking capability, the responses being given by them has been summarized in the above table no.5. It was found that the most number of male and female of all the age groups fall under the Moderate category.

Males in their early age (20-30) are more aggressive than being conservative while female of all the age group fall under only moderate category.

6. Conclusion

The following conclusions can be drawn from the research study:-

6.1 ULIPs have various risk factors and because of various additional charges it becomes a costlier product too in comparison of an Endowment plan.

6.2 Although the policy holders can expect good returns from the ULIPs but due to market linked, the market fluctuation have their direct impact upon it and hence they are less safer when comparing it with a traditional plan.

6.3 After the survey, it is found that there are more policy holders of Endowment plan than of the ULIPs which show that they are more risk averse i.e they want maintenance of their capital more than to their increment at the cost of risk.

6.4 Since in ULIPs, the male policyholders are more than the female which state that males are prone to risk taking than the females.

6.5 It is also observed that the male youngsters of 20-30 age groups are more aggressive investors than any other age group.

6.6 The purpose of most of the policy holders is insurance than to the investment and the tax savings.

6.7 The policy holders who are private employees are more in ULIPs than to the Endowment plan while the government employees equally hold the ULIPs and Endowment plan.

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