

Child education: consider the alternative investments

POWER POINT

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With running a financial planning practice for more than a decade now, it seems clear to us that children's education and retirement planning are the top two financial goals for families with their own home. In the more recent past, we have seen a significant change in how parents plan for the education goal. The aspiration has moved from domestic education to a foreign one for many of these parents. While there seem to be multiple reasons for this—ranging from enhanced aspirations and increased competition domestically—the monetary impact of this shift has been significant.

To provide a perspective: currently a Masters' in Business Administration (MBA) course in India costs approximately ₹20 lakh at an Indian Institute of Management. A similar course could cost around \$200,000 (or six to seven times ₹20 lakh) at an Ivy League college in the US. In addition to the sharp cost differential between similar programmes in both these countries, there is also the added impact of depreciation of the rupee.

For example, in the last five years the Indian rupee has depreciated 8.30% at a compounded annual basis against the US dollar, which means your education cost would go up by at least 8.3% per annum just due to currency depreciation. Similarly, over the last 10 years the rupee has depreciated at 3.8% on a compounded annual basis against the dollar.

The exact level of currency depreciation is hard to estimate when planning for a child's education many years into the future. But you will need to assume that as long as inflation in India continues to be significantly higher than in the US, there is every chance that in addition to cost of education going up—which is approximately 5-7% per annum in the US—annual currency depreciation of 3-5% will also need to be factored in. While a portion of the currency depreciation risk can be mitigated by investing internationally, investors will also need to build an investment strategy that generates returns that are at least in line with the effective increase in education costs and potential currency depreciation. Therefore, an India-centric portfolio comprising fixed-income strategies such as Public Provident Fund (PPF) and

deposits, is unlikely to be enough and will need to consist of exposure to growth assets such as equities.

Considering the huge cost of children's education, and the detrimental impact it can have on other goals such as retirement and health care, you obviously need to start investing early and work diligently to a plan. However, parents don't have to stake their future for the sake of their children. Consider these alternatives of financial investments.

Manage expectations continuously: Many parents avoid money-related discussions with their children either because they think it is a taboo to discuss, or that their children are too young to understand, or that it is their responsibility to ensure that all of their children's education needs are taken care of. It is critical for children to be told and to understand that a neighbour or a close friend or a cousin going overseas does not mean that they can simply follow in their footsteps. A combination of structured conversations and learning moments need to be used to help your child better understand how her education will be financed.

Help your children think and find solutions themselves:

Depending on how the numbers stack up for you in terms of your other financial goals, especially retirement, you may decide to fund their education only up to a certain stage. For example, you may tell them that you can possibly fund their graduation programme overseas, but you will not be able to fund their postgraduation, or that you may be in a position to fund the first two semesters of a programme but not beyond that. The value of such conversations is invaluable, as they help the children understand how they can work towards achieving their own goals. They can evaluate whether to:

explore the loans options; seek scholarships, for which they need to study harder; or work part-time or full-time for a few years to support their education. This process allows children to build character and values that are critical for them to achieve success as they become more independent later in life.

Explore the alternative of a student loans: Since you are clearly not going to get a loan for your retirement, and therefore should certainly not be compromising on your retirement corpus to meet the child's education goal, funding your child's education goal through a loan may be an alternative that you can explore closely. The costs of these loans vary significantly, depending on whether you take these loans in India or overseas (especially for top notch universities). In addition, there are also tax benefits that you can get if the loans are from eligible financial institutions, and they include some attractive moratorium periods.

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