



You can raise money from your assets but choose carefully

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Before liquidating any investments to meet cash crunch, consider the costs, taxation and other factors

For many individuals, the cash flow problem is yet to improve, forcing them to look at ways to raise money. Taking a loan or selling investments is usually the first solution that comes to mind.

Out of the two, the latter makes more sense as taking on a new liability is not advisable in the present situation. "Many tend to overdraw credit to meet their needs when cash-strapped. If their situation doesn't improve, they will end up defaulting on their loans," said Vishal Dhawan, founder, Plan Ahead Wealth Advisors, a financial planning firm. According to Dhawan, the current situation is an evolving one. With the number of covid-19 cases on the rise, a second wave cannot be ruled out. Drastic measures by the government to control the situation could result in employers extending the pay cut. Liquidating investments if you don't have an emergency fund is a more practical solution. "Many don't plan or prioritize selling their assets. They don't consider the penalties, charges, liquidity when redeeming investments. Liquidating investments haphazardly can lead to lower returns, and it can also affect future goals," said Suresh Sadagopan, founder, Ladder7 Financial Advisories, a financial planning firm.

Order of liquidation

Here is the order in which you should liquidate your investments. However, the order can change in some circumstances, such as when there is a run-up in certain assets.

Liquid funds: It's easy to sell them. If redeemed within three years, gains are added to the income. After three years, gains are taxed at 20% with indexation benefit.

Company deposits: Your deposit is at risk if the company goes bust. They may offer higher rates but have higher penalties as well. They are taxed like bank FDs.

Equity mutual funds: Sell funds before individual stocks. If sold within a year, gains are taxed at 15%. After one year, gains up to ₹1 lakh are tax-free, but the rest is taxed at 10%.

Gold: Physical gold and gold ETFs are liquid but SGBs, sold on exchanges, are not. Physical gold and ETFs are taxed like liquid funds. Interest from SGBs is taxable*.

Pension funds: They are best left untouched. Partial withdrawal from EPF is tax-free for now. You can do so from PPF after seven years and from NPS after three years, tax-free.



Bank deposits: Before you break it, do check for the penalty that the bank would levy on it. The interest is taxed under the head income from other sources.

Debt funds: They are market-linked, so their returns can fluctuate. They are taxed like liquid funds. Preferably, liquidate investments older than three years for lower tax outgo.

Direct equity: Liquidate your investment in stocks in stages as you would have different expectations from each stock. They are taxed just like equity mutual funds.

Small savings: Some products like RDs can only be liquidated after three years. KVP allows withdrawal after 2.5 years and NSC can only be transferred to another person.

SGB: Sovereign Gold Bond; RD: Recurring deposits; KVP: Kisan Vikas Patra; NSC: National Savings Certificate; EPF: Employees' Provident Fund; PPF: Public Provident Fund; NPS: National Pension System; *No capital gains tax is charged if SGBs are held till maturity. If sold on the exchange, they are taxed like debt mutual funds; Take taxation, charges, penalty and liquidity into account before deciding

Source: Mint Research

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Here are the things you should consider when liquidating your investments.

Use your DEPOSITS

Deposits come high in the order of liquidation (*see graph*). But should you break the fixed deposit (FD) or take a loan against it?

Bank deposits have different structures. Some may have a partial withdrawal facility, while some may have higher penalty. For example, say, you have a deposit of ₹20 lakh, but need only ₹5 lakh. In this case, check with the bank whether there is a partial withdrawal facility available.

If the feature is not available, you may need to break the deposit and reinvest the remaining amount, which can lead to reinvestment at a lower rate. Banks have been reducing interest rates on deposits. You

may have invested in the FD at 7-8% some years back. The current rate for most big banks is below 6%.

Some banks have a complex penalty system on an FD withdrawal. Say, you had put money in an FD four years back at 8% for 10 years. When you break the FD, the bank will charge 0.5-1% penalty. Also, it won't calculate your gains at 8%. Instead, it will look at the rate it had for a four-year FD when you had invested. Say, it was 7% then. The bank will pay you at 7% and will deduct a penalty from this.

Due to the penalty that banks charge, it may be beneficial to take a loan against the FD. For instance, when you only need a portion of the FD, and the maturity is after a year. The deposit will continue to earn a higher interest rate while you have a loan only on a portion of the FD.

ALLOCATION

Prioritizing instruments for liquidation helps those who have limited investments and a few asset classes in their portfolios. If you have a large portfolio and don't need significant money immediately, take the asset allocation approach when liquidating assets.

"If you withdraw only the debt portion, the remaining portfolio could be lopsided, with one or two asset classes. Asset allocation helps reduce the risk in a portfolio," said Deepesh Raghaw, a Sebi-registered investment adviser and founder of Personal Finance Plan.

According to Raghaw, an individual can also take a call on the performance of individual asset classes and then decide on liquidation. For example, if gold prices are rising, an individual can choose to sell gold exchange-traded funds or physical gold.

Other factors

If an individual has a traditional life insurance plan, there is an option to take a loan against it, instead of surrendering it. "If you don't have adequate life insurance, don't surrender it. One option the policyholder can consider is converting the traditional plan into a paid-up policy, and then check for a loan against it. The returns on the traditional plan are lower than FDs, and the person should stop paying the future premiums," said Arnav Pandya, a financial planner and founder of Moneyeduschool, an Ahmedabad-based financial literacy initiative. If a life insurance policy is converted to paid-up, it means that though the premium payments have stopped, the plan remains active.

If you have an ongoing loan on depreciating assets, such as a car, evaluate if you need them. "If you can do without those assets, sell them and settle the loan, before liquidating assets," said Pandya.

Employees' Provident Fund, Public Provident Fund and National Pension System should be the last investments that one should touch. They help you accumulate a corpus for the future when you stop working, and should not be liquidated unless there's nothing else left to redeem.

Those planning to sell a property should keep in mind that doing so could take months. Also, there are chances that the seller may not get the desired price in the current market.

Moreover, don't try to be adventurous with money when you are already facing a cash crunch. "As markets have done well in the past few months, many feel that they can make money by trading. They shouldn't take such unnecessary risk when cash-strapped," said Dhawan.

The only long-term solution to the cash crunch problem is to cut down expenses and spend only on essentials. Take stock of your monthly spends and see how you can bring down the expenses.