#WiseWithEdelweiss

What is SIP Investment? Systematic Investment Plan in Mutual Funds

Systematic Investment Plan (SIP), is the ideal way of investing in mutual funds in a regular and systematic manner. A SIP works on the basic rule of investing regularly, enabling you to build wealth over time. Under SIP, you invest a fixed sum every quarter, month, or week as per your convenience.

How does SIP work?

Before you start investing, it's important to understand how SIP works. A SIP works on the basis of periodic and consistent investments, quite like a recurring bank deposit. The investment amount can be auto-debited from your bank account on the basis of standing instructions, and the corresponding amount of mutual fund units are allocated to you. The number of units received depends on the scheme's current Net Asset Value (NAV).

In SIP offered by SEBI registered mutual funds, your investments are managed by a team of professional fund managers for which you pay a nominal cost as disclosed in the Scheme Information Document of the respective Scheme.

Benefits of Systematic Investment Plan over Lump Sum investment

Investing through SIP provides a number of advantages as compared to lump sum investment (where you invest a large amount in a single instalment). The advantages are:

- Low Entry Level: You don't need to accumulate a large sum to make SIP investments. You can invest small sums of as little as Rs.500 at fixed intervals.
- Timing the market is not needed: Regularly investing through SIP helps you take advantage of market volatility and eliminates the need to time the market. As against this, in lump sum investing, your entry point becomes important since you could possibly face book losses if the market falls soon after you invest.

- Rupee Cost Averaging: As you invest fixed amounts periodically, you get more units of your chosen mutual fund when the market is low, and fewer units when it is high. Over a period of time of consistent SIP investing, your average cost of purchase reduces to below the current NAV of the scheme. This concept is known as rupee cost averaging.
- Power of compounding: As SIP investors remain invested for the long term, they get the benefit of compounding (returns over the returns already earned, exactly like compound interest). As an example, an investment of Rs. 5,000 per month made consistently over 10 years at an investment return of 12% can result in wealth accumulation of Rs. 11.50 lakh.

Types of SIPs

Let us take a look at the 4 main types of SIP facility:

1. Top-Up SIP: As you progress in your career and start earning more, you can use the top-up SIP facility to increase your SIP investments. Under top-up SIP, you can increase the existing SIP amount periodically (for example, you could increase your existing SIP of Rs.1,000 per month by Rs. 500 after every 6 months; this means, after 6 months, your monthly SIP will become Rs.1,500; after another 6 months, it will rise to Rs.2,000 and so on).

2. Perpetual SIP: The end date of your SIP is not defined at the time of starting a perpetual SIP. Your periodic instalments continue to be invested unless you give specific instructions to stop them.

3. Flexible SIP: Flexible SIPs give you the convenience to increase or decrease the periodic investment amount as per your cash flow. While a fixed investment amount is still specified when starting a flexible SIP, you have the option of changing the investment amount up to 7 days before the instalment date. This is even easier if you do SIP online.

4. Trigger SIP: Experienced investors can opt for SIP through Trigger. These enable you to set a trigger to automatically redeem and/or switch from one scheme to another if the market becomes volatile.

A SIP is a great tool in the hands of investors to build wealth with regular investments. SIPs through mutual funds are also ideal for individuals who want to save before they spend and are looking to become disciplined investors.