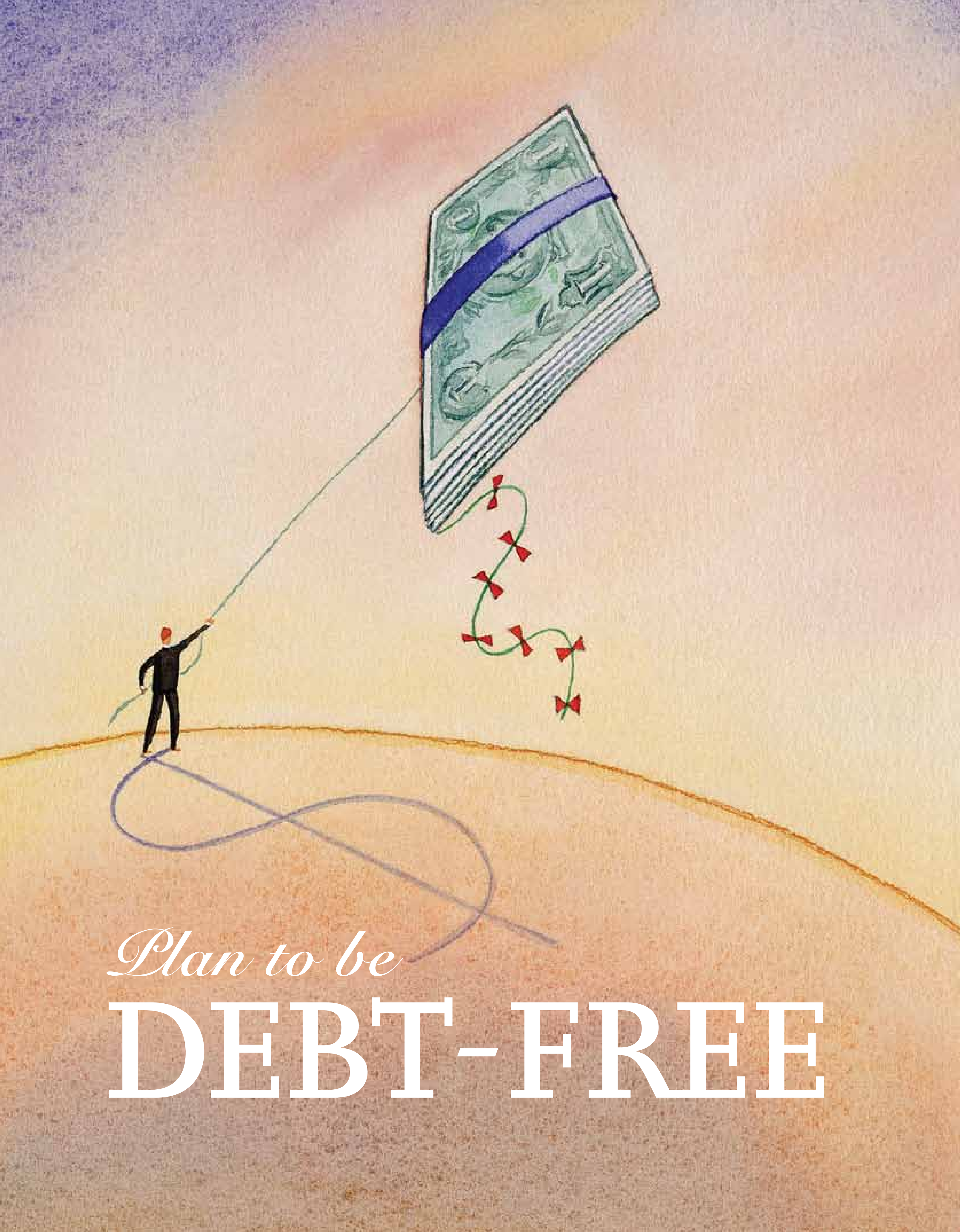

Plan to be DEBT-FREE

STRATEGIES FOR GETTING OUT OF DEBT

Although most homeowners aspire to be debt-free, many are not putting their minds to it. A recent Manulife Bank poll[1] found that three in four homeowners consider becoming or being debt-free to be among their highest financial priorities. In fact, that 75 per cent figure holds true (with only slight variation) across all age groups surveyed, but only half of those surveyed had managed to reduce their debt over the preceding 12 months.

Why are so many Canadian homeowners struggling to reduce their debt?

Lack of knowledge may be part of the problem. Some Canadians have not taken the time to learn about the factors impacting their ability to manage and reduce their debt. For example:

- One in three Canadians aged 30 to 39 are not aware that interest rates are relatively low compared to historical norms. As a result, Canadians in this group may be taking on more debt than they could comfortably carry if interest were to return to historical norms
- Most Canadians (85%) in all age groups are not aware that interest payments on non-registered investment loans are generally tax-deductible
- Two in every three homeowners aren't sure what level of down payment they'd need to avoid having to pay mortgage insurance

While lack of knowledge is one area of concern, a gap between expectations and reality may also be keeping us from paying sufficient attention to our debt. The survey found that 55 per cent of Canadians aged 30 to 39 expect to be debt-free by age 50; however, only 17 per cent in the 50 to 59 age group actually were debt-free.

Why is there such a gap between the optimism in our youth and the reality as we approach retirement? One reason may be a lack of willingness to ask for help when it comes to managing our debt. The survey found that only about one in three Canadians have spoken to an advisor in the past year about their debt and day-to-day finances. As with many things in life – a little good advice can go a long way.

Strategies to help you become debt-free

If you'd like to become debt-free but aren't sure where to start, here are six strategies to set you on the right path:

1. Live within your means

It seems obvious but few people actually take the time to ensure they're consistently spending less than they earn. The solution is simple – create a budget and stick to it. Then, periodically check your

[1]Figures cited in this article are taken from the results of the Manulife Bank of Canada poll, which surveyed 1,000 Canadian homeowners between ages 30 to 59 with household income of more than $50,000. It was conducted online by Research House between July 25 and August 6, 2011. Full survey results can be found at manulifebank.ca/debtresearch.

income and expenses to ensure that you're actually spending within the limits you've set. A budget will help you distinguish between your 'needs' and your 'wants' and also help you ensure that you're setting aside enough money to achieve your longer-term financial goals.

2. Plan for the unexpected

One of the biggest challenges for many Canadians trying to become debt-free is an unexpected expense or temporary income disruption. Remember that even with a solid budget in place there will be unexpected challenges along the way. To avoid having these incidents throw your debt-freedom plan off-track, you need to expect the unexpected. Build up an emergency fund that you can tap into if you hit a rough patch. Or, if your contingency plan involves short-term borrowing, ensure you have easy access to a low-interest line of credit so you're not forced to use high-interest credit cards. Finally, when things are back to normal, make it a top priority to replenish your emergency funds or repay your loan.

3. Account for rising interest rates

Do you know what interest rates you're paying on your various loans? Are the rates locked-in or variable? If you don't know the answers to these questions, make it a priority to find out. Often variable rates are lower than fixed rates – which could save you money today. However, only consider variable rate loans if you have some flexibility in your budget to absorb an increase in interest costs if interest rates rise. Fixed rates may be preferable if an increase in rates would cause you financial difficulty or undue stress. Recently, more Canadians are opting for loans that allow them to divide their debt between fixed and variable rates so they can enjoy the best of both worlds.

4. Be proactive and make debt repayment a priority

Just because you have a 25-year mortgage doesn't mean you should take 25 years to pay it off. In fact, almost all mortgages allow you to make extra payments, beyond what's required. Doing so could significantly reduce the amount of time it takes for you to repay the mortgage and could save you significant interest. The same is true of virtually all loans. If you want to become debt-free, make it a priority. Set a debt-reduction goal the same way you'd set a target for retirement savings and then challenge yourself to reach that goal by putting extra money toward your debt each month. To help you stay on track, create a chart showing your actual debt compared to your goal and update it regularly.

5. Consolidate your debt

One of the easiest ways to reduce your debt quickly is to consolidate it all at the lowest rate possible. Moving all of your debt to a single low-rate loan account will not only help you save interest, it will make it easier for you to keep track of how much debt you have. And, knowing how much total debt you have at any given time will make it easier to keep your debt-freedom plan on track.

6. Talk to your advisor about a debt repayment plan that can work for you

Last, but certainly not least, don't be afraid to talk about debt. Debt management is an important part of your overall financial plan and your advisor can help you create and implement a plan for becoming debt-free sooner.

Most Canadians would like to be debt-free. The good news is that, by implementing these few simple strategies, you may be able to become debt-free sooner than you think. •

FIVE COMMON MISTAKES CANADIANS MAKE WITH DEBT

- Staying with your original lender when the mortgage comes due, without shopping around to find a mortgage that best meets your unique needs
- Maintaining multiple separate debts with a range of interest rates, instead of consolidating at a single low rate
- Failing to make extra mortgage payments, when additional money is available
- Not developing a long-term strategy for debt-freedom
- Neglecting to seek out professional debt management advice

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