

# MoneySmart Bootcamp

A crash course in money basics to boost your financial fitness

BY ERICA ALINI



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# MoneySmart Bootcamp

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CHAPTER 1

# How to manage the money you have





Welcome to MoneySmart Bootcamp – I’m so glad you’re here. My name is Erica Alini and I write about personal finance at The Globe and Mail. Let’s dive right in.

The key concept I want to talk about in this first chapter is: Spend less than you make. That’s the foundation of any kind of healthy relationship with your money. There can be no saving, investing or financial planning unless you’re able to set aside some cash at the end of the month. But how exactly do you do that?

The concept is obvious, the execution much less so. Personally, it took me years to perfect the art of managing my (and later my family’s) cash flow. Along the way, I realized that what works is a matter of personality and lifestyle. My dad, for example, is a track-every-cent kind of guy. I prefer a go-with-the-flow approach (more on that below). But the bottom line is that everyone needs a system.

Let’s take a look at three common ways to manage cash flow as well as a couple of “traps” that might keep you from reliably spending less than you make – and how you can get around them. Next, we’ll tackle savings. And at the end of the chapter, you’ll find some activities to try on your own.

## Three ways to track your income and spending

Where is all your money disappearing to? You need a system to track your expenses – and your income, too, if you’re a freelancer or have more than one paycheque. Below are three common ways to do that.

### OLD-FASHIONED BUDGETING

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The kind of money-tracking typically done with a spreadsheet. You note your income in one column and your expenses – grouped by broad categories – in adjacent columns. At the end of the month, you add it up and take stock of how much, if anything is left. Going forward, you can set yourself savings targets and decide what expenses to eliminate or trim back. If you’re not sure where to start, there are many budget templates online. ([This tool](#) from Canada’s federal financial consumer watchdog allows you to create and download a personalized budget spreadsheet. You can also shop budget templates on Etsy.)

**PROS:** Some people thrive on the strict discipline of a budget.

**CONS:** Others find that constantly keeping tabs on their spending can be time-consuming and mentally draining.

**PRO TIP:** Avoid budgeting with too many categories. “Coffee shops, takeout, clothes, pet, housing, bills – the list goes on ... It’s so unrealistic! ... Enough already. Budgeting like this sets most people up for failure,” writes financial planner Shannon Lee Simmons. All you really need is four larger categories, she argues.

## MONEY BUCKETS

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Instead of columns, set up a few different accounts – what I like to call “money buckets” – to earmark money for various expenses and savings.

When your pay lands in your main chequing account, the first step is to set aside enough to cover your monthly fixed expenses, such as rent, utilities and any debt payments. Then you allocate the rest among your savings: Maybe that’s \$500 for your monthly retirement contribution and \$200 to your “vacation bucket” for a \$600 long-weekend getaway that’s three months away.

**PROS:** Compared with budgeting, this is a low-maintenance approach.

**CONS:** It may not work for absolute newbies. You have to have a pretty good idea of what infrequent expenses are going to crop up through the year and how much you should set aside for your longer-term savings goals.

**PRO TIP:** Money buckets can quickly get pricey unless you’re using no-fee bank accounts. More details on that [here](#) (look for “map your cash flow”).

## BUDGETING APPS

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Let a bot do some of the work for you. Apps like YNAB (for You Need a Budget) and Mint, provided by Intuit Inc., allow you to create spending and saving categories and assign dollars to each of them.

**PROS:** As low-maintenance as money buckets, without the need for so many accounts.

**CONS:** If you want a budgeting app to automatically track and classify your expenses, you'll typically need to allow it to connect to your bank accounts. If you have privacy concerns, this may be a turn-off. Also, these apps will either charge you a fee for their services or serve up ads for financial products based on what their algorithm has learned about you.

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## Money traps

These might keep you from reliably spending less than you make.

### FINANCIAL SURPRISES

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Your laptop breaks, your client's cheque bounces and your childhood friend invites you to their wedding. Anything that unexpectedly blows up your spending or scrambles your income can throw your finances off track.

### SOLUTIONS:

- **Expect the unexpected.** Set up an emergency fund for what you can't predict. Without some rainy-day cash, you'll have to borrow to cover what you didn't plan for.
- **Practise year-round cash flow planning.** Did friends' weddings also dig a hole in your wallet last year? It's a sign you should expect that kind of expense. Looking at your spending patterns throughout the year can help anticipate and plan for infrequent expenses so they're no longer surprises.

## IMPULSE SPENDING

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Resisting temptation is exhausting so make it easier on yourself to stick to the plan.

### SOLUTIONS:

- **Erase** your credit card info from online shopping accounts.
- **Pay with debit or cash** for anything but bills or use a prepaid debit card for “fun spending.”
- **Automate** your bill and debt payments as well as transfers to your accounts for longer-term savings.

## HOW MUCH TO SAVE AND FOR WHAT

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It's hard to save when you don't know what you should be saving for and how much you should squirrel away.

### SOLUTIONS:

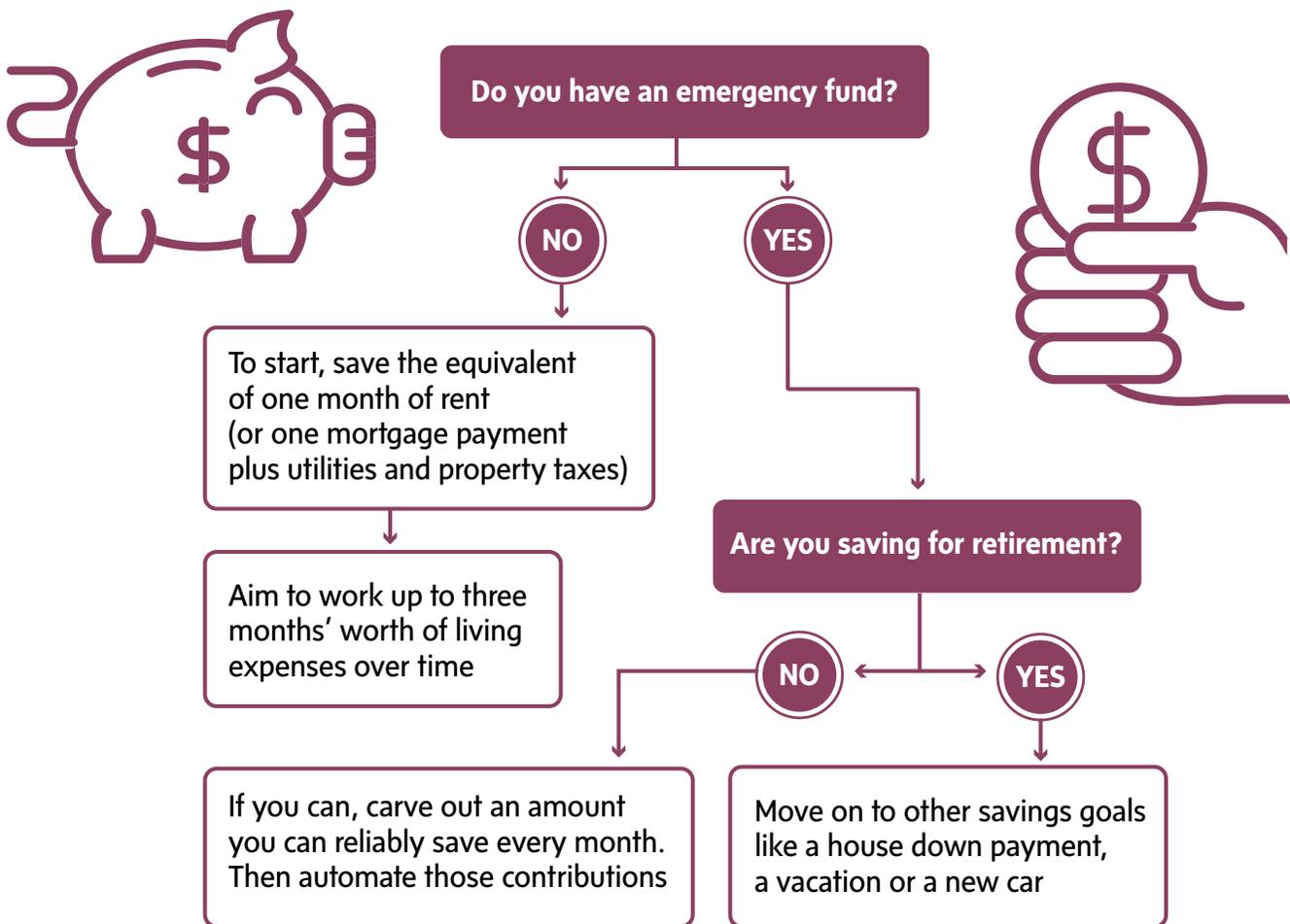
- **Emergency savings:** The general rule is to set aside enough cash to cover three to six months of living expenses. If that seems daunting, aim for the equivalent of one month of rent at first.
- **Savings with a clear timeline and end amount:** You need \$3,000 for a beach vacation in six months or \$80,000 for a down payment in five years. Work your way back to how much you need to set aside monthly or biweekly (depending on how often you get paid). If the math gets tricky, here's a handy-dandy [calculator](#).

- **How much to save for retirement.** That's a tough one, especially when you're young and not sure about when you'll retire and how much income you'll need. Some financial planners recommend working backward: Figure out how much you need for essential expenses, debt payments and to establish an emergency fund. Then carve out a little more for retirement without nixing out all your fun spending, which isn't realistic.

If you're further along, head over to The Globe and Mail's [Retirement Readiness Calculator](#) to gauge whether you need to save harder.



## Picture this



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## Try this at home

- Track your spending for a month.
- Now check your cash flow for the past three months: How many surprise expenses did you have?
- Spot your infrequent bills. From annual subscription fees to property taxes, there are plenty of them that don't come due every month. See whether you can switch to monthly billing or plan ahead and save for them monthly.
- Now track your variable expenses for a year: From clothing to car maintenance, how much would you have to set aside every month to cover them?



**POWER-UP MOVE:**  
Once you've got a handle on inflows and outflows, try to automate some of your bill payments and savings.

CHAPTER 2

# Get to know your debt





Let's dig into how to use money you don't have yet. I am, of course, talking about borrowing and managing debt.

Naturally, the spend-less-than-you-make principle stands. But for some of life's biggest expenses – from getting a postsecondary education to buying a house – debt is hard to avoid. And there's nothing inherently wrong with whipping out a credit card at the check-out either. If you can pay on time and in full when the bill comes, using credit costs you nothing and may even earn you reward points.

This chapter isn't about avoiding debt at all costs. Rather, it's about becoming a debt connoisseur. Below we'll go over some basic – and some not-so-basic – debt features everyone should understand. We'll also look at different approaches to pay down debt. At the bottom you'll find some try-at-home exercises.

## DEBT DETAILS TO LOOK OUT FOR

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# Interest rate: How lenders charge it – and hide it

Interest is, of course, the cost of borrowing. That cost is usually expressed as a percentage of the amount you're borrowing, which is known as the principal. And that percentage typically indicates the annual interest rate, or what it will cost you to borrow the money over one year.

Here's a quick look at some of the ways in which lenders charge interest:

### **Simple interest**

Let's say you're borrowing \$10,000 with a 5 per cent annual interest rate and repaying it all at once after three years. At the end of Year One, you'll incur \$500 in interest. By the end of Year Three you'll have incurred \$1,500 in interest, which is your total cost of borrowing. Student loans and car loans, for example, often charge simple interest.

### **Compound interest**

Now let's say you're borrowing that \$10,000 over three years with a 5 per cent interest rate that compounds annually. As in our first example, at the end of Year One, you'll incur \$500 in interest. At the end of Year Two, though, the 5 per cent charge will be based on the principal plus interest from Year One. That's 5 per cent of \$10,500, or \$525. And at the end of Year Three your interest charge will be 5 per cent of \$11,025 (\$10,500 plus \$525), which yields \$551.25. Think of it as "paying interest on the interest," or 5 per cent of the accumulated interest of previous periods. Your total cost of borrowing over three years is: \$1,576.25 instead of the \$1,500

you'd have paid with simple interest. Borrowing can quickly get expensive when you're paying compound interest, especially if the interest is compounded frequently (more on that below).

### **Hidden interest**

Here's a magic trick some lenders pull: They'll make your interest look lower and apply a variety of fees and charges they're not calling interest. Do not let them fool you. Look for something called the annual percentage rate (APR), which is a standardized way of calculating the total cost of borrowing every year. The APR will also help you compare different ways of borrowing.

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## **Interest math**

Even if you know the APR, how lenders actually calculate interest matters. Take credit cards, for example. In Canada, some charge simple and others compound interest.

With annual interest rates typically around 20 per cent on purchases, your borrowing costs can quickly swell even with simple interest. Here's a simplified example. Let's say you make a single purchase for \$1,000 with your credit card, on which the interest is calculated annually but charged monthly. Your first interest charge will be \$16.70 (that's that annual interest of \$200 divided by 12 months of the year). If you make only the minimum payment – which is usually 3 per cent of the principal or \$30 in this case – your balance will dip to \$986.70. If you only made minimum payments for a year, over 12 months you'll pay just under \$186 in interest, according to this [nifty calculator](#) from the Financial Consumer Agency of Canada, the federal financial consumers watchdog. Click on Summary Report for Option

to see how payments would work out every month if a borrower only made the minimum payment.

But what if your card charged compound interest? The lender will charge you interest not just on any balance owing, but on any unpaid interest as well. This can get especially expensive if your credit card charges interest daily, as many do. For example, the FCAC [warns](#): “A credit card with an APR of 28.8 per cent that is compounded daily has an effective rate of 33.36 per cent.”

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## Always look beyond the interest rate

There’s more to borrowing than the interest rate you’ll be paying. Here are a few examples of other details to consider:

### Repayment length

All else being equal, the longer your loan term, the lower your installment payments will be. The flip side of that is you’ll be paying interest for longer, with a higher overall cost of borrowing.



**WARNING:** Watch out for long loan terms, especially when buying a vehicle, which will quickly lose value after you drive it off the lot.

### Prepayment privileges

Can you pay off a chunk of your debt ahead of schedule? That would save you a lot of interest but also deprive your lender of part of the expected return on the loan. Your loan contract will say whether, and how much, you can pay early without penalties.



**WARNING:** When it comes to mortgages, so-called prepayment penalties can vary significantly based on what kind of interest rate you have and whether you're borrowing from a big bank.

### **Flexibility**

Credit cards and lines of credit allow you to borrow only what you need and free up room to borrow more, up to a set limit, as you repay what you owe. This can come in handy when you don't know exactly how much money you'll need, as when you're using a student line of credit to help pay for your living costs while in school.



**WARNING:** This flexibility can also be a psychological trap because you're allowed to make minimum payments – which sometimes amount to the interest charge alone. With no set schedule to pay off what you owe and the ability to keep tapping your credit, both credit cards and lines of credit can turn into a slippery slope of unmanageable debt.

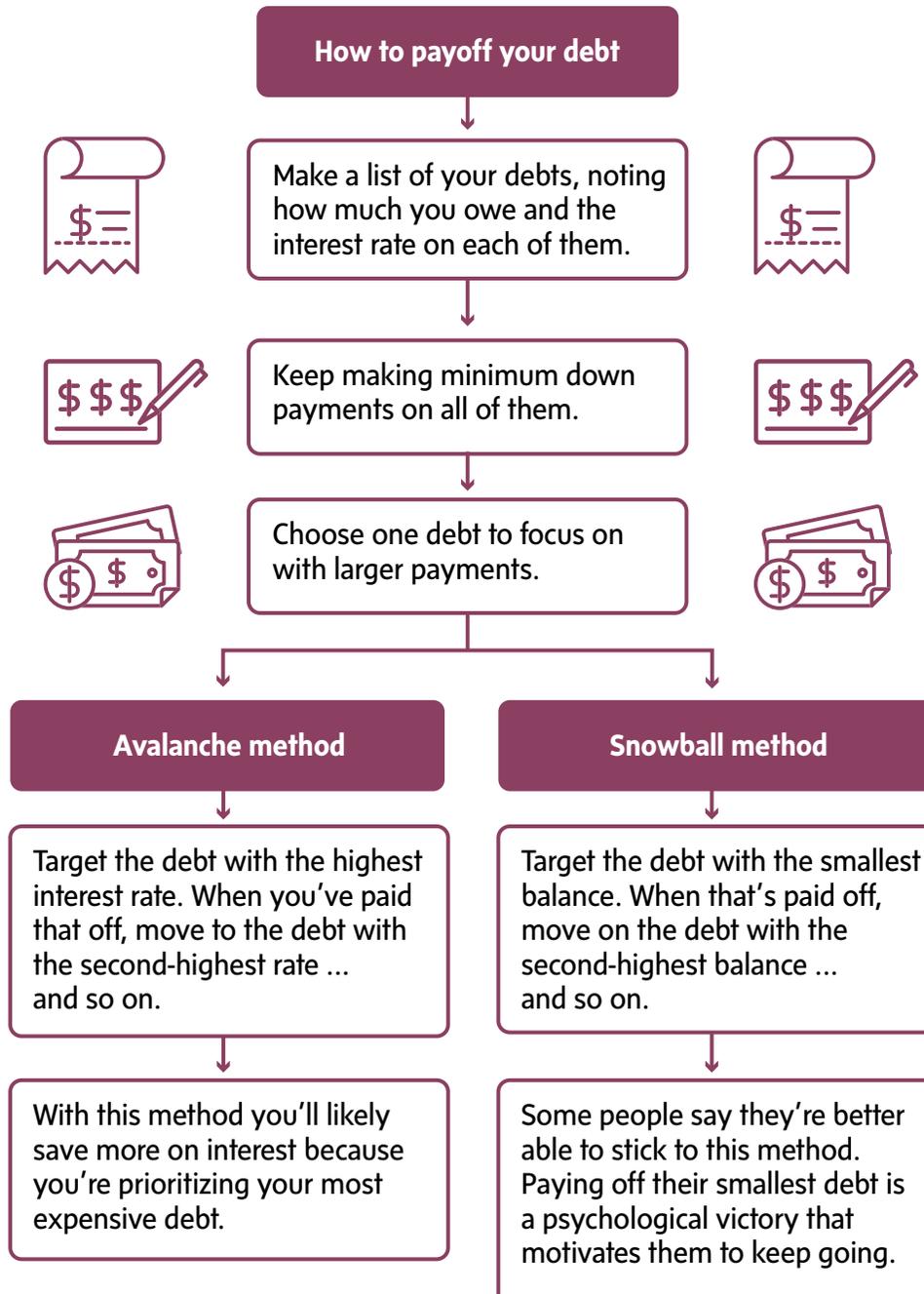
### **Perks**

If you're a student, borrowing from the government typically comes with perks. For example, you can usually claim a portion of the interest on your student loans on your tax return. And if you hit a financial rough patch, the [Repayment Assistance Plan](#) will allow you to reduce or temporarily pause payments.



**WARNING:** If you consolidate your government student loans into a line of credit, you'll lose access to the tax perks and repayment assistance.

## Picture this



NOTE: NEITHER THE AVALANCHE NOR THE SNOWBALL METHOD APPLIES TO MORTGAGES.

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## Try this at home

- Check out your credit card agreement: How is the interest calculated?
- Should you pay down debt first or invest any extra money instead? It's time to crunch the numbers (but keep in mind, as you use the calculator, that investment returns often aren't guaranteed).
- If you have a mortgage, check the contract with your lender. What does it say about prepayment privileges? Curious how your mortgage payments might change based on payment frequency, amortization or term? Use our [mortgage calculator](#).



**POWER-UP MOVE:**  
If you have an outstanding balance on your credit card, use the FCAC credit card payment calculator to see how much faster you'd be paying off your debt if you bumped up your payments by just \$10.

## CHAPTER 3

# Investing: How to make your money make money





Let's dig into how to use money you don't have yet. I am, of course, talking about borrowing and managing debt.

Naturally, the spend-less-than-you-make principle stands. But for some of life's biggest expenses – from getting a postsecondary education to buying a house – debt is hard to avoid. And there's nothing inherently wrong with whipping out a credit card at the check-out either. If you can pay on time and in full when the bill comes, using credit costs you nothing and may even earn you reward points.

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## Compound interest is now your friend

Interest piling on interest is a dreadful thing when you're in debt. But when you're an investor it becomes the engine that turbocharges your gains. Here's a quick refresher:

- Imagine that, instead of borrowing \$10,000 from the last chapter, you're now investing that money at a 5 per cent annual interest rate. At the end of Year One, you'd have earned \$500 in interest. You'll now have \$10,500, which will grow by another 5 per cent, or \$525, by the end of Year Two. You'll start Year Three with \$11,025 ( $\$10,500 + \$525$ ), which will grow by another 5 per cent, or \$551.25, for a total yield on your investment, after three years, of \$1,576.25. The math is the same if you owned \$10,000 worth of a financial asset whose value increases by 5 per cent a year.
- Over long periods of time the power of compounding gains becomes really impressive. That \$10,000? With annual returns of 5 per cent, over 30 years it would turn into more than \$43,000.

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## Stocks, bonds and other useful lingo

Buying financial investments is one way in which you can get your money to earn compound returns (although those returns are rarely guaranteed – that would be too easy). Here are some of the main types of investments:

### **Stocks**

Buy one and you become the owner of a tiny share of a company (think: Apple or RBC). That's why stocks are also called "shares." Companies issue shares to raise

money they can use to expand their business, and investors trade those stocks in the stock market. Some stocks also come with dividends, an amount companies distribute to their shareholders out of their earnings on a regular basis. Stock prices are typically volatile, rising or falling (or a bit of both) over short periods of time. History, however, shows that over the long term, the stock market trends up.

### **Bonds**

Buy one and you become a lender. Both companies and governments use bonds to borrow funds. In return, they pay you a set interest, usually once or twice a year, until maturity, when you get all your money back. You can also try to sell your bond in the financial market at a gain, somewhat like a stock.

### **Mutual funds**

You can purchase units of a mutual fund. This allows you to gain exposure to a broad basket of investments without buying and holding those investments on your own, which would be unaffordable for many of us. You may also want to diversify across investment types, for example, holding a mix of stocks and bonds.

### **Exchange-traded funds (ETFs)**

Also a collection of investments, but unlike a mutual fund, an ETF trades on the stock exchange. You can buy shares of it (also called units), just like you would any other stock.

### **Guaranteed investment certificates (GICs)**

You lend money to the bank and in turn get a – you guessed it – guaranteed rate of return. Many GICs pay you an interest rate, but, unlike with a savings account, you have to park the money at the bank for a set period of time (usually the longer the term, the higher the interest rate). There are also cashable or redeemable GICs, but they typically come with lower rates.

## Investing risk and how to manage it

Why can't we all finance our retirement by stashing our savings in GICs? Unfortunately, lower-risk investments also typically come with lower returns. This is also the reason that stocks, whose prices are notoriously volatile, generally have higher expected returns compared with bonds, whose prices don't fluctuate quite so much. But that doesn't mean you need to play roulette with your life's savings. Here are ways to manage the risk you take on when you invest in the financial market:

### **Put your eggs in many baskets**

What happens if you put all your money in one company's stock and that company goes belly up? You get my point. One way to manage your risk is to spread your money across many different companies, industries and even countries. That is where mutual funds and ETFs come in handy: They allow you to gain exposure to a broad basket of investments without buying and holding those investments directly, which would be unaffordable for many of us. You may also want to diversify across investment types, for example, holding a mix of stocks and bonds.

### **Play the long game**

The stock market goes up and down, but, historically, it has followed an overall upward trajectory over long periods of time. The longer you can keep your money invested, the better your chances of riding out short-term drops and benefit from long-term growth. An example: When the market crashed in the financial crisis of 2007-08, it took five years to climb back to where it was.

A common piece of advice is to put money in the stock market only if you can leave your money invested for a minimum of five years. More conservative advisers often recommend having a time-horizon of at least 10 years. If you're saving up

for a shorter-term goal such as a wedding or a down payment, a GIC or a savings account with a competitive interest rate can be good options.

### **Choose the ride you can stick with**

Investing in financial markets is like riding a roller coaster where you can step on or off any time. Wouldn't it be wonderful if you could catch the train on the way up and hop off just before it starts heading south? This – called “timing the market” – is what many investors try to do, and it almost never works. Instead, the key is to stay put and keep your cool. But not everyone can stomach wild ups and downs. Generally, investing only in stocks comes with higher expected returns but also makes for a bumpier ride. Adding some bonds to your portfolio usually helps to smooth out both the highs and the lows.

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## **Low-cost investing for busy people**

Beyond what you invest in, you should also think about where you're holding your investments and how much you're paying to invest. Taxes and investing fees can make a huge difference to your bottom line when you stay invested for a long time.

### **Taxes**

Luckily, so-called registered accounts, such as tax-free savings accounts (TFSA) and registered retirement savings accounts (RRSPs), allow you to invest tax-free or defer taxes.

### **Fees**

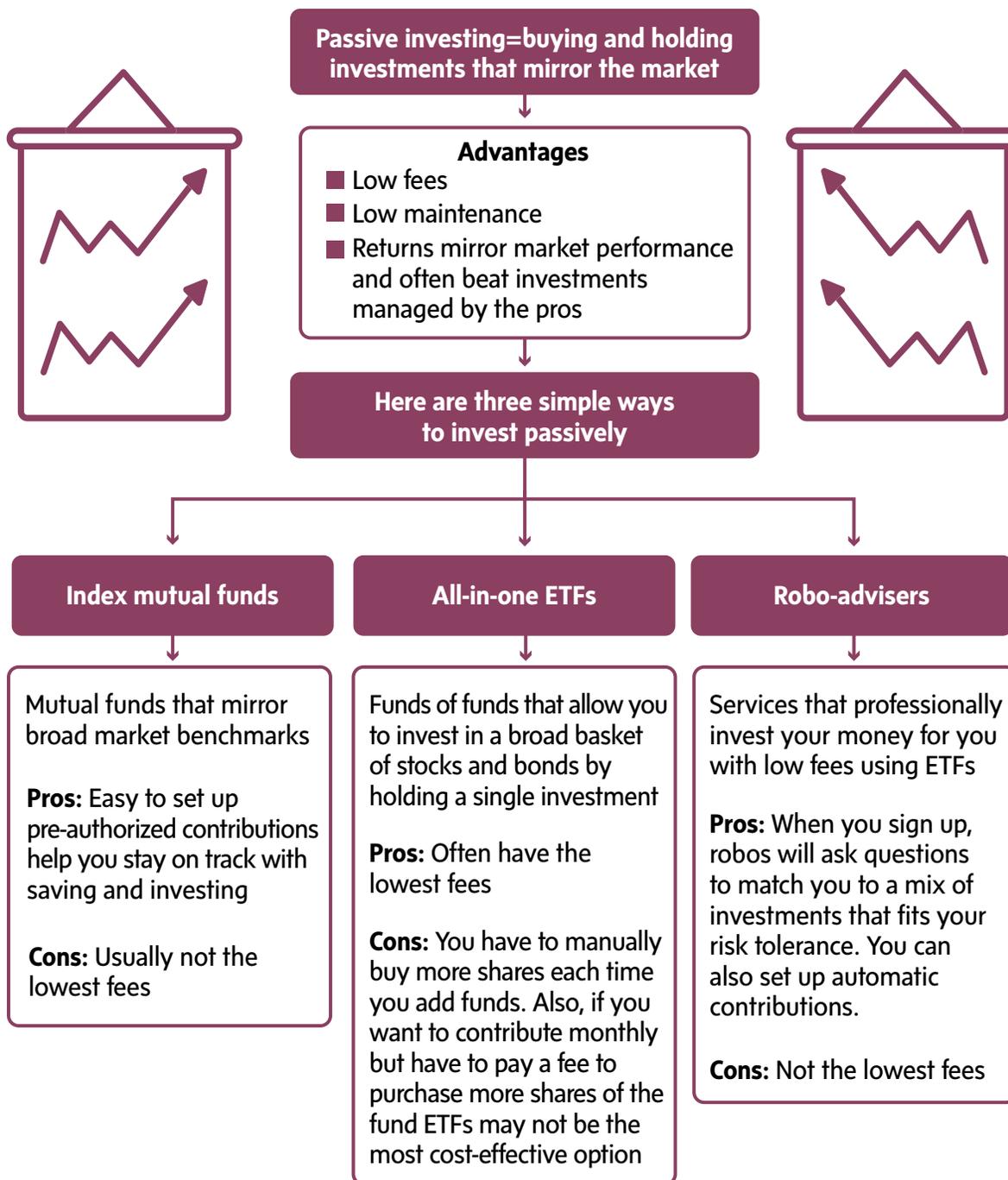
Companies that help you invest in the markets will charge you for it, and how much you pay makes a big difference to your long-term returns.

## Yes, but what about crypto?

Here's what everyone agrees on: Cryptocurrencies are extremely volatile. On the thrill scale: If stocks are a roller coaster, crypto is skydiving. And digital coins haven't been around for long, so there's no historical evidence that their value trends up over longer periods of time, as is the case with stocks. If you really want this speculative investment in your portfolio, the advisers I've spoken to recommend limiting it to 5 per cent of your investments or less.



## Picture this



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## Try this at home

- For more on investing basics, check out the Ontario Securities Commission's [GetSmarterAboutMoney.ca](https://www.getsmarteraboutmoney.ca) website and the B.C. Securities Commission's [InvestRight.org](https://www.investright.org)
- Some recommended reading: *The Little Book of Common Sense Investing* by John Bogle, who is often called the father of index investing. Try also *Reboot Your Portfolio* by Canadian Dan Bortolotti for an accessible, up-to-date guide to ETF investing.
- How brave of an investor are you? Try this [questionnaire](#) by investing giant Vanguard.



**POWER-UP MOVE:**  
Read The Globe's [ranking of investment brokers](#) and our [guide to robo-advisers](#).

CHAPTER 4

# Renting vs. buying a home





This chapter's financial workout focuses on that age-old housing question: Should you rent or buy?

People have opinions on the matter. On the one hand, generations of Canadians grew up hearing at the dinner table that renting is a waste of money. Also, many people in this country have come to see homeownership as a great way to build wealth – and after years of enormous home price gains, how can you blame them?

On the other hand, some people decry what they call Canada's "homeownership cult." You can save a lot of money by renting and use that spare cash to grow your wealth by investing in the stock market.

In practice, whether you should rent or buy depends on a number of variables specific to your situation. So instead of giving you an answer, here's a process to help you think through the issue.

## Step one: How long will you live there?

If you're likely to move in the next five years, there's usually an easy answer to your dilemma: Rent. Why? Because buying and selling a home is really expensive (not to mention, a lot of work).

### **When you're buying**

Be prepared to spend the equivalent of 3 per cent of the home purchase price in various fees and taxes. On a \$600,000 home, you're looking at \$18,000. And that doesn't include your down payment or any mortgage insurance. The good news is there are federal, provincial and municipal tax breaks for first-time homebuyers that help defray some of costs.

### **When you're selling**

One of the biggest costs will be your real estate agent's fee, which is typically 3 to 7 per cent of the home price. Let's say your \$600,000 home is now worth \$700,000. A 5 per cent fee would set you back \$35,000. There are also legal fees and a host of other possible expenses, including the costs of fixing up and staging the property to maximize buyer appeal. You do not have to worry about capital gains tax if you're selling the home you've been living in.

### **Bottom line**

Transaction costs can easily erase any gains from an increase in the value of your home if you sell less than five years after moving in.

## Step two: The 5 per cent rule

If you expect to stay put for five years or longer, it's time to do some math. To see how renting stacks up against owning a home you can use a back-of-the-napkin formula known as "the 5 per cent rule." Here's how it works:

### **Homeowners also waste money**

When you pay rent, you give money to the landlord. When you buy a home, you'll own an asset that usually goes up in value over time. Is that a slam dunk argument for owning? Not so fast. When you own a home, you'll also spend money every year on things that do not increase your ownership stake in it (like paying off your mortgage principal) or drive up your home value (as is often the case with renovations).

Transaction costs, as we've seen, are an example of unrecoverable costs for homeowners. The interest you'd pay on your mortgage as a homeowner, as well as property taxes, wouldn't build home equity either. And guess what? If a pipe clogs, it's on you to pay for a plumber, a cost you would have been able to pass to the landlord as a renter.

There is also a more subtle cost of homeownership that you should consider: The cost of tying up your money in a home when you could earn better returns in the financial market. While home prices can certainly rise faster than stocks in any given year, over the long term, stocks have historically yielded better returns than real estate.

### **The math**

The [5-per-cent rule](#) is a simple way to compare the unrecoverable costs of renting

and owning to gauge whether you'd be better off pouring a bunch of money into a real estate asset or renting while investing your extra cash in the financial market. The rule goes like this: If a year's worth of rent adds up to less than 5 per cent of the value of a home similar to what you're renting, being a tenant is financially attractive. If you're paying more than 5 per cent, you might want to consider owning.

An example: Let's say you're renting a two-bedroom apartment for \$2,000 a month. A year worth of rent would add up to \$24,000, which is 5 per cent of \$480,000 (divide the annual rent amount by 0.05 to calculate 5 per cent). If a two-bedroom condo or similar home in your area costs more than that, you may want to keep renting.

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## Step three: Housing costs vs. your income

Whatever the 5 per cent rule shows, the next step is to compare your expected housing costs with your income. Whether you're paying rent or carrying a mortgage, spending too much on housing will suck the air out of your budget. You won't have breathing room to save for important things like retirement – or fun things like vacations.

### **If you're buying**

A good starting point is this [online mortgage qualifier tool](#) provided by the federal government. It simulates how most lenders will vet your finances when you apply for a mortgage. But the banks won't take into account many big monthly expenses you may have, such as daycare fees. For a more complete picture of whether your

mortgage would leave you house poor, you can use The Globe and Mail's [Real-Life Ratio Calculator](#).

### **If you're renting**

A commonly used general rule holds that rent plus utilities should amount to less than 30 per cent of your income before tax. But in many high-rent cities, few tenants would be able to meet that bar. A less stringent gauge of affordability that also takes into account different spending needs is this: Make sure that your fixed expenses – including but not limited to rent and utilities – are no more than 55 per cent of your income after tax.

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## **Step four: The quality-of-life variable**

Regardless of what the math says, many Canadians find they simply can't make long-term renting work. Sure, in countries like Germany, where less than half of households own a home, you'll find plenty of happy forever renters. But the realities of Canada's rental market are different.

When being a tenant means living in fear of a rent increase or eviction, many people understandably opt for owning, if they can. And if you have or are planning to have kids, finding a rental big enough for a family can be a challenge.

That said, sometimes life nudges you toward renting instead of owning. For example, I've spoken to people who decided to rent in retirement and never looked back. That pipe clog, being someone else's problem? There can be a psychological relief factor in it that the math just doesn't capture.

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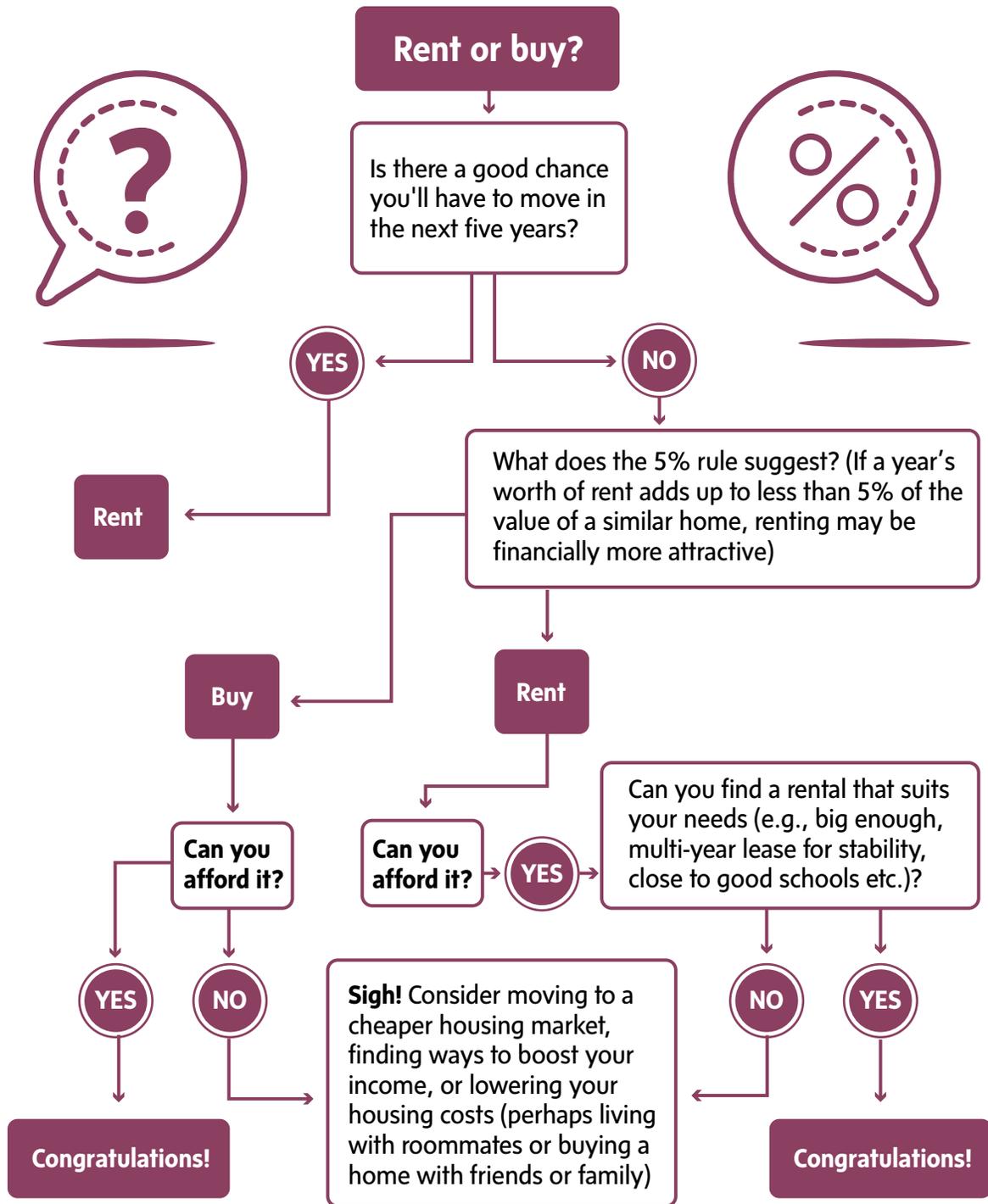
## Step five: What if you can't buy or rent?

This is where the going can get really tough. Sometimes the math will show that you can't afford to either rent or buy in the city where you live. Or maybe your only option is to rent – usually cheaper than owning – but you can't find a place that fits your needs.

There is no way around it: You'll have to either find a way to increase your income or reduce your housing costs (by moving to a lower-cost city or taking on roommates, for example). These can be hard choices, especially if you're pondering them when you're well past your 20s, as is the case for a growing number of Canadians. Still, keeping your housing costs in check will spare much financial pain and heartache in the future.



## Picture this



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## Try this at home

- Try out the 5 per cent rule for yourself. If you're a tenant, compare 12 months of rent with the value of similar homes in your area. If you own, use an online calculator to estimate your current home value, then look for a similar property that's up for rent nearby. What does the math show?
- If you're pondering a home purchase, it's a good idea to get some practice with the [FCAC's online mortgage calculator](#). If you're comparing homes in different municipalities don't forget to input an accurate estimate of property taxes. You'd be surprised how much they can vary and how high they can be in some smaller towns.



**POWER-UP MOVE:**  
Curious how  
your mortgage  
payments might  
change based on  
payment frequency,  
amortization or term?  
Use our [mortgage  
calculator](#).

CHAPTER 5

# How to disaster-proof your life





Our final chapter is about an essential but often neglected aspect of personal finance: disaster-proofing your life.

Of course, we all know to do at least some worst-case-scenario-planning. Car insurance is mandatory. Home insurance is a no-brainer. And many people take out life insurance when they have kids.

But do you have tenant insurance if you're a renter? Did you write a will? Do you know what a power of attorney is? (No judgment: I didn't know either until I started covering personal finance.) You may not even realize those should be on your crisis-prep checklist.

And even some of the obvious line items on that list aren't as straightforward as you might think. For example: Does your home insurance protect you against flooding or a sewer backup? And will your employer's disability policy keep paying if you're unable to work for more than two years? You'll be surprised at what you might find in the fine print.

Here is an overview of common holes that you may want to plug in your disaster plan and tips on how to go about it.

## Home and tenant insurance pitfalls

Just because you – or your landlord – have home insurance doesn't mean you have enough coverage. Watch out for these three pitfalls:

### **Tenant insurance (also called renter's insurance)**

Think your landlord's insurance policy will cover the cost of repairing or replacing your stuff if it's damaged or stolen? Think again. If you rent, you need tenant insurance, which also protects you if someone sues you for causing damage to other units or for injuring themselves or incurring damage to their property while in your rental. A general rule is to get at least \$100,000 of coverage, though some recommend \$1-million.

### **Flood insurance**

A standard home or tenant insurance policy will kick in for things like broken pipes and a leaking dishwasher. But if outside water is streaming in through your door and windows or backing up into your basement you're likely on your own unless you've signed up for additional water-damage coverage, which is optional. This isn't just for those who live near a river, lake or the ocean. Climate change has helped make flooding the No. 1 source of home insurance claims in Canada – and an estimated 1.7 million households are exposed to that risk.

### **Condo insurance**

Condominiums – also called strata in British Columbia and parts of Alberta – have a commercial policy that will cover the building structure itself and common areas. Condo owners often think that's all they need. In fact, you'll want to take out your own individual condo policy if you don't want to be stuck paying out of pocket for things like damage to your belongings, extra living expenses if your unit becomes

unlivable, or compensation to your neighbour if your showers leaks into their living room. You may want to talk to an insurance broker to make sure your policy properly complements your condo corporation's insurance so you don't have to foot the bill for anything neither plan covers. Finally, tread carefully when choosing your condo in the first place. Soaring insurance rates and deductibles have become the bane of many condo owners. Before buying, ensure that your building has adequate coverage and the condo corporation is setting aside enough money in its reserve fund, which serves to pay for repairs and maintenance. Your real estate lawyer will help you with that.

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## Watch for this catch in your disability insurance

If an injury or illness knocks you out of commission for an extended period of time – or even permanently – long-term disability (LTD) insurance will replace part of your paycheque.

Keep in mind:

- **Your workplace coverage.** If you have a group benefits plan at work, it likely includes an LTD policy. Some employers have coverage for work-related injuries or sickness through provincial workers' compensation boards, which is mandatory in some industries. These employers may also offer a supplemental group plan.
- **The catch.** If you have a group plan, check your insurance booklet. Some plans offer coverage only for a limited period, such as 10 years. But even if your maximum coverage period extends until age 65, many insurers adopt stricter eligibil-

ity rules after you've been on disability for two years. Often, after the two-year mark you'll lose coverage unless you're deemed unable to perform not only your old job but any job for which you're reasonably qualified, something called an "any-occupation" test. The risk is you'll lose your income when you're still too sick or injured to go back to earning your regular paycheque. If you can't figure out whether your insurer will switch to an any-occupation test after a period of time, it's worth e-mailing HR to get clarity.

- What then? You can buy a supplemental individual policy, but it will be pricey. One way to limit your premium is to elect to have a waiting period of two years before receiving the benefits from your personal LTD insurance. Remember: Your workplace plan will likely cover those first two years.
- **If you don't have coverage through work.** If you work for yourself or a smaller employer who doesn't offer a generous benefit package, it's worth considering an individual policy that would replace at least some of your earnings. Keep in mind that, generally, disability income from an individual plan is tax-free. This means you could match your regular take-home pay with benefits that are substantially lower than your pretax paycheque.

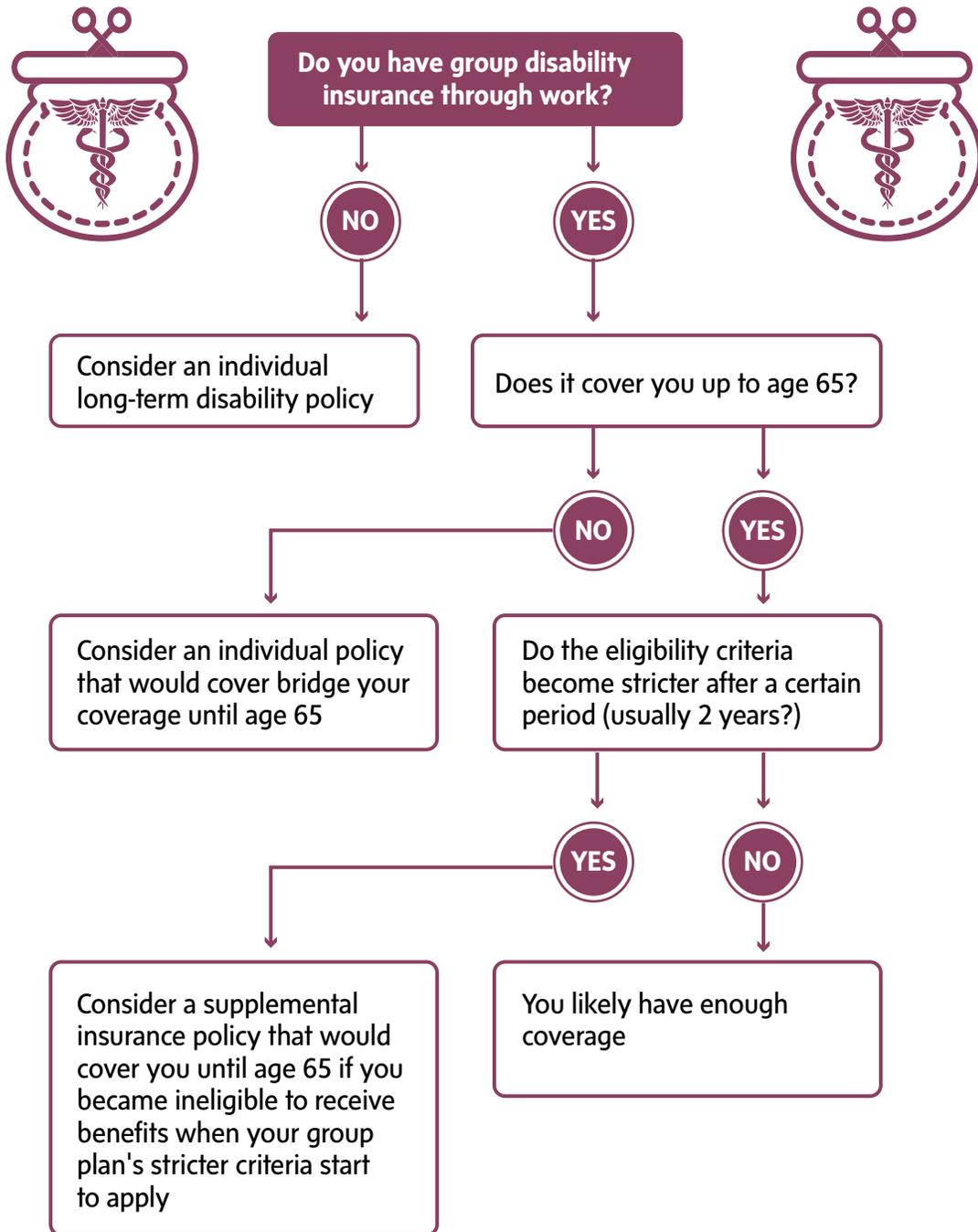
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## Who needs a will and what's a power of attorney?

Writing a last will and testament isn't just for celebrities and rich uncles. And it's also a good idea to have a power of attorney (POA), a legal document that sets out instructions about who should make decisions on your behalf – and how – should you become unable to make your own. Here are a few things to know:

- **Wills are for singles, too.** If you're a parent, a will sets out, among other things, who you want to take care of your children in the event of your death. If you're in a common-law relationship, a will can help your partner stake a claim to your assets, something they may not be automatically entitled to if you're not married. You may want to have a will even if you're single and have no strong feelings about who should get your stamp collection. In general, an up-to-date will makes it easier for your survivors to settle your affairs. Without it, a court would have to appoint someone to administer your estate (what you own, along with any debts), which can take a while. Having a will can also help reduce the chance of family legal squabbles.
- **Two types of POA.** Unlike a will, which only comes into effect after you're gone, powers of attorney apply when you are alive, and set down your wishes about your care and who will act on your behalf should you become incapacitated. With a POA for property, you authorize someone else to make decisions about your property and finances. A POA for personal care appoints someone to speak for you on health care decisions. It also sets out your wishes on matters such as whether you want to be kept on life support if doctors believe there's no chance you'll regain consciousness. Admittedly, these aren't pleasant scenarios to ponder, but they do deserve some thought. A POA for personal care can also be called a health directive or representation agreement.
- **Low-cost options to get it done.** Online services such as [Willful.co](https://www.willful.co) and [LegalWills.ca](https://www.legalwills.ca) work a bit like tax software – you'll get prompts to input information and answer questions – and allow you to make a will and POAs for an affordable fee. If you'd like a bit more hand-holding, some law offices have set up bare-bones services that will guide budget-conscious clients through the process.

## Picture this



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## Try this at home

- Check your home or tenant insurance policy: Does it cover you in case of flooding?
- Now dig out your workplace benefits booklet. What does it say about disability coverage?
- You can get disability insurance quotes online from various insurers – start comparing. Don't forget to check also how your premium would change if you chose a longer waiting period (but don't try to save money by opting for stricter eligibility criteria or a shorter coverage period that wouldn't carry you until retirement).

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## A final word



This is it! Congratulations on making it through the MoneySmart Bootcamp.

I hope this helped you feel more confident about tackling some of the money decisions you're facing. But remember, a one-off boot camp isn't enough for a healthy lifestyle – you have to keep at it. The same holds for personal finance: It's a lifelong learning journey.

