Spend Smarter Save Bigger

Finding BIG savings
in your Home, Mortgage,
Vehicles, Insurance
and Investments

MARGOT BAI

Chapter One From

Spend Smarter,
Save Bigger

By Margot Bai

www.spendsmarter.ca
margot@spendsmarter.ca

Chapter 1

Sarah & Mitch

A piercing shriek caused Sarah to look up from the latest Margaret Atwood novel captivating her attention. Her five-year-old grandson, Eddie, was splashing with delight in the lake with his dad, Sarah's son John. The excitement came from a new game where John would lift Eddie out of the water with his feet standing on John's palms until Eddie lost his balance and fell back in with a splash! Sarah smiled to herself at how much she enjoyed having the children up at the cottage in the summertime. Growing up, her family didn't have the money to buy and maintain a cottage, and they did a lot of tent camping.

In fact, as she reflected on the life journey she and her husband Mitch had taken together, she was proud of their accomplishments. At 55 and 52 years of age, Mitch and Sarah took the plunge into early retirement. Today, their lives are busy with a variety of activities. Summers are spent almost entirely up at the cottage outside Red Deer with visits from a steady stream of friends and family. Activities such as canoeing and fishing on the lake and hiking on the many trails help them keep in shape and enjoy the great outdoors.

Mitch and Sarah always loved dogs and started breeding about five years ago. Each January, they have a litter of Golden Retrievers for a wait list of hopeful buyers. Mitch volunteers at the Calgary Humane Society, walking the dogs and helping with grooming. Sarah prefers people to dogs and volunteers with the Meals on Wheels program. She brings warm meals to seniors and stays awhile with each one to hear their stories.

They also use their free time to help fundraise for charity. This year, they participated in the weekend to end breast cancer with a team of friends raising $42,000! Mitch also volunteers with Habitat for Humanity, helping install electrical wiring in the new homes. He enjoys meeting new people and using his skills in a practical way to help young families.

They are both active in their church, exercise almost daily and take turns creating various culinary masterpieces at dinnertime. Sarah recently started writing children's books and has had some success publishing them. Since retiring, Mitch has had more time to pursue his favorite hobby, carpentry, creating furniture with his own unique design.

How did they do it?

Of course, their lives hadn't started this way. Sarah and Mitch worked as hard as anyone to build the nest egg that made their early retirement possible. They married young, right after Sarah graduated from teacher's college and Mitch completed his two-year post-college apprenticeship as an electrician. They both started out working fairly modest jobs: Mitch worked his way up at Epcor, Alberta's electricity supplier, for twenty years, before being laid off in a down cycle. He took the opportunity to start his own business as a contractor, focusing on electrical installations in commercial developments. Sarah was a grade school teacher for six years before taking a break to have her son John and daughter Rose. Later she went back to teaching for another sixteen years.

It seems incredible that they have managed to achieve so much financially in thirty years. Early on, Sarah and Mitch agreed on the importance of owning a home of their own. They lived in a basement apartment for their first two years of marriage, packing lunches and saving every dollar until they had enough for a down payment. When they found a smaller, neglected house selling for $160,000 in a desirable neighbourhood in Calgary South East, they recognized the excellent appreciation potential! Over the next few years, they restored it to a comfortable, entry-level home and watched it gradually rise in value.

Rather than locking in to a five-year mortgage term, they opted for a lower rate on a one-year mortgage. Though the interest rate varied each year, it did not affect them directly since they made extra mortgage payments from the beginning. They felt it was important to get the lowest possible rate, especially early on when they had the highest mortgage balance. By taking a shorter term with a lower interest rate, they accepted some risk in exchange for paying down their principal faster.

Soon after moving into their house, they also began ambitious monthly RRSP contributions with their bank. By arranging for less tax to be taken from their paycheques, their cash flow increased, making the contributions manageable. They started learning about investing including the many fees that could eat away their savings. After researching different options, they eventually transferred their RRSPs from the bank to a low-fee mutual fund company with a sound investment philosophy. Without the hefty fees typical of advisor-recommended funds, their money grew much faster!

Mitch and Sarah both agreed that buying or leasing new cars every few years was an expensive luxury that didn't fit their long-term plan. They kept the used car Mitch bought at graduation for almost ten years. When the car finally needed more repairs than they could justify, they replaced it with a two-year-old car they bought privately and paid for in cash. They were committed to sharing one car, alternately carpooling with friends and occasionally taking the bus to get back and forth from work.

A few years after they moved into their home, Sarah became pregnant and their son John became the joy of their lives! They lived a simple lifestyle, especially in those early years. They went camping in the Rocky Mountains, bought groceries from a discount grocer and clothing on sale toward the end of the season. Apart from their RRSP contributions and savings for John & Rose's university education, every extra dollar went toward paying down their mortgage. Twelve years after they bought their first house, Mitch and Sarah were mortgage-free!

With a growing family, Sarah and Mitch were both ready for a slightly larger home. The real estate market had risen steadily in the years since they bought their little house and they were confident it would fetch a good price. After living in an older home, they both wanted a new construction home for the open concept designs and improved energy efficiency. They researched all the area builders before putting a deposit down on a spacious four-bedroom home for $350,000 with a one-year closing. Compared to existing neighbourhoods, the new construction homes offered excellent value!

Sarah and Mitch talked about using a real estate agent to sell their little house but it didn't make sense. After all, they had a well-kept, starter home in a desirable neighbourhood where demand was high. They learned what was involved and listed their home online on the Multiple Listing Service for a flat fee. After a month, they found a sweet young couple without an agent in tow who were interested in their house and agreed to a sale price of $280,000. Over twelve years, their little home had appreciated an impressive $120,000 and by selling privately they saved $14,000 in real estate agent commissions.

They put all the money from the sale as a down payment on their new house and arranged a small mortgage for the other $70,000. Even so, they had substantial equity in their home and they arranged a secured line of credit. They were interested in buying a rental property and started learning everything they could on how to do it. They decided on a six-unit apartment, in good condition, for $450,000. They put a 25% down payment from their credit line and arranged a conventional mortgage for the rest. The monthly rental income of $5000 more than covered the mortgage, property tax, utilities and other expenses. The surplus each month was put against their credit line. Because it was an investment property, all the expenses, including the mortgage interest and credit line interest, were tax-deductible.

By continuing to put as much money as possible into the small mortgage on their new house, they were able to pay it off in just three years! Next they began saving up for the down payment on their cottage, which they bought five years later with $100,000 down.

Ten years after buying their new home, Sarah and Mitch retired. Mitch had a decent pension with Epcor totaling about $184,000 and Sarah's teacher's pension was about $122,000. After over two decades of steady contributions, their combined RRSP savings had grown to a staggering $674,000 while their house had appreciated to $450,000. These assets alone totaled nearly $1.5 million! The rental property was worth over $500,000 and even though it was still mortgaged, it generated a positive cash flow of about $18,000 per year after expenses!

They knew they had enough in their combined pensions and RRSPs to fund a comfortable retirement. They didn't need a big income to live the life they wanted and they preferred their escape from the world of work to an expensive lifestyle. There is so much more to life than working for an income and finally they had the freedom to focus on the things that really matter.

What Would You Do?
Imagine that you are Sarah or Mitch. You've worked hard, saved steadily and are ready to retire from full-time employment. What would you like to do with your time? Sarah and Mitch didn't simply sit in a rocking chair on their front porch. They built a full, balanced life with a variety of activities. They used their financial freedom to help others in more difficult circumstances. What would you like to do if you no longer needed to work to pay for your current expenses or past debts? Would you travel? Take up a new hobby? Become involved in charity work? Write a book?

Can this work for you?
From modest beginnings, Sarah and Mitch have done amazingly well! They saved as much as they could, especially while they were young, and continued to save throughout their working lives. From an average household income, they created a net worth well over a million dollars. But perhaps you are feeling skeptical about how Sarah and Mitch were able to create such wealth from a middle-class income. Their story leaves some questions unanswered. How did they manage with just one car? How could they afford to contribute to their RRSPs *and* keep fast- paying their mortgage? What sorts of investments could grow so quickly that they could retire so early? Probably the most important question of all: C*an this work for you?*

Big Savings
Sarah and Mitch focused on their long-term goals and created an inexpensive lifestyle to reach those goals. However, beyond penny-pinching, their success stems from their ability to find big savings on the big expenses in life. They realized huge savings by sharing one car and keeping it as long as practical while saving to buy their next car in cash. Instead of paying top dollar for a house in move-in condition, they found a home selling well below it's market potential that needed some TLC. By living there until they paid it off, they benefited from lower mortgage interest, property taxes and utilities costs, enabling them to pay off the mortgage much faster. By both fast paying their mortgage and contributing to their RRSPs they combined the benefits of reduced mortgage interest and income tax savings.

However, Sarah and Mitch did more than create an affordable lifestyle that allowed them to save quickly. They also ensured that every major financial transaction gave them the most favorable terms possible. Rather than locking in to a higher mortgage interest rate with the "security" of a five-year term, they opted for the much lower rate on a one-year term, saving thousands each year. By not leasing or financing a brand new car, they avoided dealer markups and interest charges. Instead of paying real estate agents 5% to find a buyer for their home, they found one on their own and put the savings right into their new home. Rather than allowing a financial advisor to invest their RRSP contributions in mutual funds with high fees, they did their own research and choose a low-fee fund company where their money could grow faster!

These financial choices made a huge difference in their ability to save, yet had little impact on their lifestyle. Finding these kinds of savings involves learning about the options and understanding the risks. But when you do, you can negotiate a better deal for yourself and find low-cost alternatives to expensive financial services.

Sarah and Mitch combined two key ingredients to achieve financial success. First, they created an affordable lifestyle that helped them save a significant portion of their income each year. Second, they realized big savings on all their major financial transactions, from buying homes and cars, to arranging mortgages and investments. Section one will start with the first point, and show how living below your means will enable you to eliminate debt and create savings. Then, in section two, we will focus in on the big expenses and show you how to maximize your savings in each area.

Get Rich Quick?

An endless parade of books promise foolproof ways of making lots of money in a short time. Anyone who has read these books knows they never deliver what they promise. In most cases, it takes a person of extraordinary charisma, intuition or luck to succeed in making millions. If this were not so, we would all be millionaires, for there is no lack of willing candidates!

Hundreds of people have won a fortune in the lottery, but even if you buy tickets for the rest of your life, it remains highly improbable that you will become one of them. A select few people have a special talent or skill that they successfully market to millions of people. But the reality is that most of us cannot sing like Avril Lavigne or skate like Wayne Gretzky! Still others are hoping for a substantial inheritance that will leave them set for life. Few people are fortunate enough to inherit great wealth. Most people inherit later in life and rarely inherit enough to retire. Winning the lottery, becoming famous or inheriting a fortune only happen to a lucky few. The average person will not become rich if they are waiting for these things to happen!

Get Rich Over Time!

There are also a good number of self-help books explaining how to become rich gradually. Unlike their get-rich-quick cousins, these books contain wealth-building strategies that actually can work for most people. Perhaps you've heard some of their common themes:

- Pay yourself first
- Max out your RRSP every year
- Save 10 % of everything you earn
- Save regularly through automatic transfers
- Invest in equities
- Get a financial advisor
- Buy a house

But these simple suggestions aren't always easy to follow. Have you heard these ideas before and wondered:

- How can you "pay yourself first" when you are behind on your bills?
- How do you max out your RRSP contribution room when it has swelled to $50,000?
- Does it make sense to save 10% when you have a mortgage to pay off?
- If you start up a monthly savings plan, how do you live on the lower income?
- Aren't stocks too risky?
- How do you know your financial advisor is putting you in the best possible investments?

- How much of a down payment should you save up for a house?

The chapters ahead will answer these questions and more. You will gain practical advice on how to be smarter with your spending and grow your savings faster. Like Mitch and Sarah, you will learn to find big savings on life's bigger expenses, accelerating the time it takes you to become financially free!

The Secret to Financial Freedom

If becoming rich depended upon being able to earn a high salary, most of us would never be rich! Not everyone can earn a six-figure salary, but everyone can save more of what they earn! If you spend all your income each year, you will never become wealthy. How much you earn is not nearly as important as how much you save. Regardless of your income, the secret to financial freedom is to spend less than you earn! The good news is you don't need to save a million dollars to become a millionaire! Money makes money when properly managed so your wealth will eventually grow on it's own. The key is to save enough to get started and to keep saving over your working life.

Nearly everyone wants to be wealthy. Wealth means freedom from work and debt, and freedom to create the life we want. But gaining financial freedom, paradoxically, requires financial discipline. Most people fail to accumulate substantial savings because they choose the enjoyment of immediate spending over the long-term benefits of saving. Canadians are financing a lifestyle they cannot afford, sinking themselves deeper in debt with endless monthly payments and interest charges. Between 1995 and 2005, Canadian's savings rate fell from nearly 10% to below 0%! This means that on average, Canadians are now spending more than they earn in a year for the first time since the great depression!

The instant gratification from spending is often short-lived. But the benefit of making extra payments to your mortgage or contributing to your RRSP will last for the rest of your life! Obviously we need to spend money to live today. But finding the balance between spending and saving is where most of us get into trouble. By following the principles in this book, you can choose to live comfortably *and* save effectively. Distinguishing smart spending from wasteful spending will help you get the maximum benefit from your money today while helping you save more for tomorrow!

The Time Value of Money

Sarah and Mitch achieved substantial wealth by their fifties because they started saving in their twenties. The more time your money has to grow, the greater your wealth will be. Financial experts have named this phenomenon the “time value of money". The idea is money invested today will be worth substantially more tomorrow. The sooner you start saving and investing your money, the less you need to save to achieve the same end result.

I often remind myself of this powerful financial concept with the simple phrase, “Money now is worth more than money later”. What I mean is that $100 today is far more valuable to me than $100 when I retire. If I save $100 today, that could be worth $200 to me ten years from now and $500 over the next twenty-five years! Of course today’s money can only be worth more tomorrow *if you save it*! By putting today’s money toward your mortgage or into your RRSP, it will have a much greater value for you in twenty-five years. Imagine paying off your mortgage before age forty and retiring from work to find a new purpose in life!

Start Saving Today

The sooner you begin saving and investing, the more time your money will have to grow. But, if you are no longer in your twenties, don’t feel that you have missed your chance. Life expectancy in Canada has been increasing steadily, so there is still much benefit to be gained by starting your savings today, even if you are in your forties or fifties. If you are behind in your savings, consider devoting a few years to accelerated savings to “catch up” to where you would be if you had started saving earlier. The sooner you start, the faster you can achieve your savings goals.

Before you can really begin to build wealth, *you must first eliminate debt*. If you have loans, repaying them as quickly as possible is the equivalent of saving. Those struggling under debt have the longest road ahead because debt has the opposite effect of wealth. While wealth creates more wealth, debt grows against you. Eliminating a $10,000 debt takes longer than creating $10,000 in wealth because you must also pay the interest charges on your debt until it is retired. However, if you have debt, it helps to remember that it goes both ways. As you pay your debts down and begin building your savings, you will start to experience a positive snowball effect, where the more you save, the faster your money grows! Since eliminating debt is the first step in any savings plan, chapter two will explore issues surrounding consumer debt and empower you to become debt-free!

Action

Now it's time to stop listening to me and start thinking about what financial success means to you. Sarah and Mitch saved carefully to create a lifestyle just right for them, but it is probably not exactly what you are looking for. What do you really want in life? Below is a list of some of the reasons people want wealth. These aren't things that people want to do with their money, but rather they are life qualities people hope money will bring them. Read the list carefully and rank them in order of importance for you.

_ Security: knowing that I will always have a home, food and a caring community.
_ Freedom: being confident that I have the means to pursue any dream I choose.
_ Relationships: feeling better connected to my family and friends.
_ Variety: filling my days with a blend of activities to create a healthy balanced life.
_ Independence: determining my own path without needing the support or approval of others.
_ Personal Growth: learning new things and sharpening my skills.
_ Charity: reaching out to others in need with love and practical assistance.
_ Fun: feeling happiness and excitement through activities I enjoy.
_ Adventure: seeking out new experiences that may include taking some risks.
_ Relaxation: taking each day at an easier pace and reducing stress in my life.
_ Other: ________________________________

Have you ranked each item in order of importance for you? Is there anything I missed that you could think of? Write it down in the extra space. Now, take your top three most important qualities in life and explain why each one is important to you. To help you get started, I have listed my top three with explanations.

What is most important to me in life and why?

1. Freedom: Because I have many dreams that I want to chase over the course of my life. Life is filled with so many possibilities and I don't want to live my whole life with just one narrow set of experiences.
2. Relationships: Because good relationships with others is what really brings meaning to life. I value my friendships and want to grow them.
3. Charity: Because there is so much suffering in the world, I want to do what I can to help other people live a better life.

Now it's your turn. List your top three desired life qualities and explain why each one is important to you. If you thought of a benefit that I missed, please use it instead.

1. ____________________ is important to me because
____
____
____

2. ____________________ is important to me because
____
____
____

3. ____________________ is important to me because
____
____
____

How Does Your Life Measure Up?

Consider your top choices: are they a reality in your life today? For example, if you said relaxation was important, but you are actually very busy and stressed out, perhaps you should be cutting back on some non-essential activities, taking time to relax with a good book or getting more exercise. If you said adventure is important but you rarely try new things or visit new places, it's time to start planning some adventures! Maybe you listed freedom as being important to you, but you are actually burdened with debt. Perhaps you always wanted to volunteer for a charity or sponsor a child in a third world country but never felt you had enough time or money to make the commitment.

If your life doesn't measure up to your priorities, **now** is the time to make changes! Improving your lifestyle doesn't need to cost a lot of money; it just requires that you refocus on the things that really matter to you. Knowing what you value most in life will help you make financial decisions that are consistent with your goals. Don't waste your time and money on useless things. Spend your money on the things you value.

Cheat Sheet

- Sarah & Mitch saved carefully over their entire lives and were able to retire in their fifties with well over a million dollars!
- Sarah and Mitch did more than create an affordable lifestyle that allowed them to save quickly: They also ensured that every major financial transaction gave them the most favourable terms possible.
- Winning the lottery, becoming famous or receiving a large inheritance will not likely happen to you.
- The secret to financial freedom is to spend less than you earn.
- The instant gratification from spending is often short-lived but the benefit of saving will last for the rest of your life!
- Money now is worth more than money later: $100 today is far more valuable than $100 when you retire because it can be invested and grow to $500 or more over 25 years.
- If you have debt, eliminating it is the first step toward saving.
- Decide what is really important to you in life and spend your money in ways that will create the life you want to lead.

Sarah and Mitch achieved financial independence from an average household income by saving on all their big expenses. In the pages ahead, you will meet George and Kathy, a young couple who are well-educated, come from successful families and have decent paying jobs. However, they believe they are entitled to a certain lifestyle right away and try to create that lifestyle before they can pay for it! Find out just how deep they dig themselves in as you read on.