How We Went from Indebted Students to Landlords in 6 Years

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The October 2007 edition of MoneySense magazine featured their popular "How I Did It" series, a collection of articles describing how ordinary Canadians found extraordinary financial success. Tales of exceptional achievement often garner much attention and hype. But, hype aside, it helps to learn from those who, through hard work and smart planning, achieve financial security.

Following the, "How I Did It" theme, I would like to share my story of financial success. Whether or not my story is exceptional is for you to decide. However, it is a story of success that will inspire anyone to pay off their debts quickly and consider investing in real estate as a means to build their financial future.

"How We Went from Indebted Students to Landlords in 6 Years"

When we married in May 1998, my husband and I had $20,000 in student loans and a decision to make: should we focus on paying off the loans first, or just make the minimum payments to save up for a down payment on a house? We were renting a one-bedroom, high-rise apartment for $900 per month, a short walk from James' work. He had a good entry level job at a computer company, while I found work in the classroom and the office with Young Drivers of Canada.

Our apartment was small and the rent payments seemed such a waste that we quickly agreed buying a house would be our first priority. To save up the down payment, we lived frugally, making do with free dial-up internet through James work, packing lunches everyday and rarely eating out. We drove an older, economy car and spent vacations car camping in Ontario. Entertainment consisted of rented movies on our hand-me-down 80's style console TV.

In the spring of 1999, we turned $10,000 in savings into $15,000 by funneling it through James' RRSP and withdrawing it under the Home Buyer's Plan 90 days later. This provided just enough for the deposit on a brand new development in Richmond Hill. We checked all the area builders and chose the one offering the best value, an 1800 square foot townhouse for $197,000 closing

February 2000. Between signing and closing we managed to save the balance of a 10% down payment plus closing costs. To this day we joke that we bought that house by the skin of our teeth and we didn't have two twenties to rub together!

Buying a house in 2000 was the best thing we could have done, as real estate prices in the GTA soared over the next 5 years. Buying new construction also allowed us to get a foot into the real estate market even before we had a full down payment since we only needed to cover the deposit on signing. Had we not made every sacrifice possible to get into our home as early as we did, we would have missed out on big gains.

Over the next few years, we continued to live like poor students, driving the same old car, taking more camping trips and saving every dollar we could. With a house in hand, we now directed our savings toward our student loans, finally paying them off in August 2001. Next, we turned our attention to our mortgage, accelerating the payments to build up our equity faster.

We had made the mistake of locking in our mortgage rate for 5 years. Three years later, prime had fallen 2% and we weighed up our options. Doing the math, it made sense to pay the penalty to break our mortgage at 5.65% to get a lower one-year rate of 3.5%. The following year, we scored an unbelievable 2.98% on another one-year term, saving an additional $5000 in interest over the higher rate. However, we calculate that our mortgage misstep had cost us around $10,000 in additional mortgage interest over the first 3 years.

As soon as we got into our new home, we began monthly RRSP contributions to offset some of my husband's growing tax bill. We also donated regularly to charity, increasing our giving each year as we were able. Every fall, we filled out the T1213 form to reduce taxes withheld at source in light of our RRSP and charitable contributions. Boosting James' paycheque made our cash flow more manageable while also preventing CRA from holding our money until the following April.

Early on, I learned the basics of investing and especially the huge impact high fees can have on returns. Initially we invested in index funds with TD Waterhouse (e-funds with MERs of 0.3% to 0.5%). When our RRSP balance swelled to $40,000 we chose active management with Phillips, Hager and North, because of their low-fees (around 1%) and solid long-term track record. Today we continue to contribute $1000 every month to RRSPs and the balance has swelled to over $150,000.

In the fall of 2004, the necessary repairs on our old Mazda exceeded the value of the car. It was time (finally James would say!) to replace it. We settled on a brand new, 2005 Mazda 3 hatchback for its versatility, fuel efficiency and reliability. Though a used car would have been cheaper, we calculate that by keeping this car for 10 years, we can achieve the same value as a used car. We had about $15,000 saved up through James' employee stock purchase plan. We financed the balance and managed to pay it off within 8 months.

As our home equity grew, we set up a secured credit line and began looking for some rental real estate. In March 2004 we took $53,750 for a 25% down payment on a semi-detached bungalow with a basement apartment in an older area of Newmarket. The home was a steal at $215,000 but it was vacant and desperately needed some maintenance. We managed to secure tenants for April 1st and worked every spare day for 3 weeks to fix the house up before they moved in. We continued to make improvements to the property over the summer and fall.

Amazingly, even fully financed, the house carried itself. The rental income from the two units is $2145 per month, nearly 1% of the purchase price, which I consider a good rule a thumb in evaluating the income potential of a rental property. We have also seen house values in the neighbourhood rise to about $250,000 in 3 years.

Today we feel wealthier than ever before: we took up motorcycling and own a 1993 Honda CBR motorcycle. We enjoy a beautifully decorated home and are gradually upgrading our furniture. In the past few years, we have traveled to Europe, Calgary, California, Newfoundland, New York City, Cuba, Vancouver and Florida.

When my husband and I married in May 1998, we had $20,000 in student loans. Today, our net worth is approaching half a million dollars and includes two homes, a sizeable RRSP and a paid-off newer car. How did we do it?

- We bought an affordable home as quickly as possible at the best price we could find.

- We drove our old car as long as it would reasonably run, long after all our friends had upgraded to cool new wheels.
- We got smart about our mortgage and fought for the lowest rate at each renewal.
- We avoided the hefty fees on retail mutual funds by investing directly with a low-fee company to grow our savings faster.
- We leveraged the equity in our home to purchase a rental property.

Our path to financial success can be summed up by these two key philosophies:

- Money now is worth more than money later. Similar to “the time value of money”, saving money while you are young to create a strong financial foundation early on is crucial to long-term success.

- Find big savings on life’s biggest expenses. Despite a major misstep with our first mortgage, we have learned that saving money on big expenses goes much farther than pinching pennies.

By living frugally in our twenties and making smart choices on our major expenses, we have built a solid financial foundation for a comfortable life in the years ahead. My book, “**Spend Smarter, Save Bigger**” (White Knight Books, November 2006) is an excellent guide to help anyone find BIG savings and accelerate the path to financial freedom. Read chapters 1 & 2 for free at www.spendsmarter.ca

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