

How Much Debt can I Manage?

Mary Huntley, Credit Counsellor

A government study a few years ago showed that the average Canadian was spending 31% of pre-tax income on housing costs. With the rapidly increasing cost of electricity and heat, due in large part to Smart Meters and HST, we can say that many people spend half of their after-tax pay just keeping the roof over their head.

Another statistic says that 15-20% of after-tax income can be spent on debt repayment, excluding mortgages. Then, follow the golden rule and “pay yourself first” with 10% of your income set aside for savings and/or retirement. This helps us build that 3 month cushion we all know is necessary to be prepared for the unexpected.

This leaves the final 20% for everything else. To put all these statistics in real terms, a person who makes \$30,000 (about \$14.50 hour) has roughly \$550 each month for food, gas or transit, insurances, toiletries, entertainment, gifts and clothes. We won't even mention what happens if you smoke or like a bottle of wine with dinner.

Not adding up, is it? It's a likely bet that many people use their 10% “pay yourself first” portion on debt repayment and/or daily expenses. No emergency fund...scary!

On that same \$30,000 income, your allowable debt repayment would be about \$380 each month. This is roughly what it averages to buy or lease a mid-range new car. That means if you're paying for a car, you can't afford any other loans or credit card payments unless your housing cost is lower than average.

What can you do if you're already saddled with loans and credit cards?

Look at paying off high interest debt as an investment. If you owe \$5,000 on your credit card at 19.9%, compare that to the 1% you would earn on an investment certificate. It becomes obvious that you'll want to knock down that debt as quickly as you can, still realizing that you do need an emergency fund.

Getting worried yet? We don't get guarantees that our current income or standard of living will continue and I think a healthy dose of paranoia never hurt anyone. Try to keep any non-essential debt to a minimum. If you must buy on credit, ensure you can factor the debt repayment into your budget. If your budget doesn't balance then you're taking on a debt you can't manage. Weigh every credit purchase against how long you will pay for it and the real cost with interest and service charges. Is a \$350 item really worth in excess of \$700 to you? Credit Card bills now disclose how long it will take you to clear your debt making the minimum payment only. Look for it...it's a real eye opener!

Remember, Credit Counsellors at a not-for-profit agency are always happy to help you review your budget and options.