Rising Interest Rates and Canadian Household Debts

Rising Interest Rates Will Cost Canadians!

For the first time in seven years, the Bank of Canada has raised interest rates. With Canadian household debt at record levels, this rate increase of 0.25 per cent is seemingly small but will impact your household budget, especially if you have a lot of debt or live paycheque to paycheque.

What's more is that there is a good chance that this rate hike could be the first of a few in the coming months and/or years. No one knows the timeline or the amount for sure for more rate increases, but one thing is for certain. This is a wake-up call for debt holders and an opportunity to pay down debt proactively to reduce household costs now.

Here are some hints on how to protect yourself against rising interest rates.

Pay it Down

"For seven years we've been in a state of historically low interest rates, which has given many people a false sense of reality when it comes to debt, borrowing and affordability. This has pushed Canadian household debt levels to the brink. Now the focus has to be on controlling your debt or your debt will control you as costs increase," says Jeff Schwartz, executive director, Consolidated Credit Counseling Services of Canada.

Halt your debt accumulation and reverse the debt cycle. It's even more important than ever to embrace the cornerstones of responsible financial management: good budgeting and saving for emergencies to reduce the need to rely on debt for major expenses.

A rate hike is a bit like a pay cut

What an increase in interest rates does is essentially give your money less mileage when it comes to debt. With higher interest rates, your household costs go up because it costs you more money to service the debt that you've got. So, until your wage or salary increases to keep pace with a rate increase, you've got to make due with less. That's an even more compelling reason to pay down your debt aggressively.

Mortgage holders need to be proactive

Homeowners take note: this rate hike will impact you today and tomorrow. 0.25 per cent is not a lot, and you may not see a big increase in your actual monthly payments. But what you really need to consider is how much more that “small” increase is going to cost you over the next term of your mortgage. You could be talking thousands of dollars depending on how large a mortgage you’ve got. Bottom line, it is going to take more money out of your wallet to service that debt.

When is your mortgage up for renewal? It can be worth your while to consider locking in for an early renewal. Do you have any extra cash? It’s worthwhile to make a lump sum payment down on your mortgage in advance of your renewal so that you will require less financing.

“Mortgage holders at the very least need to plan ahead for their mortgage renewals to anticipate what your increase in mortgage costs might be and to decide how to adjust their budgets accordingly,” says Schwartz.

Don’t forget your other debt

Although the focus in the event of a rate increase is on mortgages, your credit cards and your line of credit will be impacted as well. Don’t forget to anticipate these increases in payments in your budgeting.

If you’ve got an auto loan, double check the fine print. Most car loans are installments, but some are based on variable rates (which mean that your payments will go up with this rate increase). This is another reason to avoid those long car loan amortizations, which can cost you a great deal more than you bargained for.

Do you have a household budget in place? If not, now is the time to do so that you can pay down your debt.

For more information on this and other financial literacy and credit issues, visit the IICanada Financial Literacy Resources page or the Jamati Budget Lounge, a web-based financial education centre that has been set up exclusively for our Jamat through Consolidated Credit Counselling Services of Canada, a national non-profit organization. The Jamati Budget Lounge offers unbiased debt-counselling service and offers alternatives to help people get their debts under control. In addition to offering solutions to alleviate and eliminate debt, the site also focuses on financial education and understanding. Strategies include teaching basic, but vital concepts such as how to: budget; understand credit; and manage money. The toll-free number **1-844-329-3834** has also been set up for our Jamat to speak to a trained credit counsellor from Consolidated Credit in English, French or Farsi on a confidential basis.

Although all communications will be confidential, any connections via the Jamati Budget Lounge or via the toll-free number to Consolidated Credit will be tracked for statistical purposes.