Twins!

Newsletter of Managing God's Money Ministries

Second Edition - March 2002

The Economy

According to the Bank of Montreal, recent Canadian data continue to be more positive than expected: now we know the economy returned to positive growth in the fourth quarter of 2001 after declining in the third.

Most experts seem to think the Canadian and US economies should become more robust by the second half of 2002. Interest rates will likely increase during that period as consumer spending increases and the unemployment rate declines. **If your mortgage will be renewed shortly, ensure you have a goal and a plan before rushing to renew it.**

North American stock markets have surpassed their lows following September 11. Most commentators agree that these markets will continue to recover but will not generate high returns as in the 90's. Meanwhile, the Enron bankruptcy has emphasized the need to diversify investments. Unfortunately, I do not hear the experts advising that your best investment is to repay your debts! This is the subject of this briefing.

The Savings & Investing Decision

In Canada the month of February is RRSP[i] season: we see and hear advertisements telling us to maximize our contributions to our Registered Retirement Savings Plans to enjoy significant tax benefits for the previous year. We are encouraged to borrow to make this contribution to gain from the resulting tax benefit, and to take advantage of the tax deduction from interest on borrowed funds. Regrettably, I do not hear anybody advising about the benefits **of repaying debt and not subscribing to RRSP's!**

Beyond commenting that this Government-assisted retirement savings plan is an **excellent opportunity to save for retirement** under most circumstances, I will not discuss its full implications (for such a discussion, refer *to Managing God's Money-The Basics*, Chapter 13). In this briefing, I will comment on the broader question of **deciding between paying off debt and saving.**

First a caveat! Some of you reading this will have made decisions recently, contrary to the recommendation[ii] in this document. Please do not look back and be tough on yourself! You did what you did with the knowledge you had! Don't worry! Apply these guidelines to the future! Your goal now is to move ahead to transform your situation (if feasible, work with an independent financial adviser). Remember Luke 18:27! **Everything is possible for Jesus!**

Let's look at a disguised, real life situation at 31 December 2001. We will call this couple Patrice & Lucy and assume their marginal tax rate[iii] is 40%.

Things of Value (Assets) at Market Value - C$

Primary Home (cost $ 130,000)	150,000	
Car	7,500	
Furniture & Personal Effects	25,000	
Savings	2,000	@ 1.65%
Bank Accounts	100	
Total	**184,600**	

How Things Of Value Are Financed - C$

Mortgage from Bank	120,000	@ 6.5% -3 years closed
Car Loan	10,000	@ 8.5%
Department Stores' Credit Cards	9,350	@ 28.5%
Visa	6,000	@ 19.5 %
Credit Line (limit of $ 7000)	7,000	@ 7%
Total Loans	**152,350**	
Own Equity	32,250	
Total	**184,600**	

Their combined income is $5250 per month and their monthly mortgage is $844. They pay the minimum monthly amount on each credit card, but insist on saving a small amount monthly: Lucy and Patrice believe it is important to have a nest egg.

Identifying the Source of Value

The critical factor for Lucy and Patrice to grasp is that they make interest and loan payments from after tax income. Accordingly, to pay $100 they must first earn $ 167[iv] and pay tax of $ 67 (40% of 167). Thus, to pay interest of $222 (28.5% of $9350) per month on their department stores' credit card balance, they must first earn $370 (222/60%) and pay tax of $148 (40% of 370). In other words, the pre tax interest cost of these cards for one month is $ 370 (9350 X47.5%/12)!

On the other hand, the savings rate of 1.65% is pre tax. If they deposit $370 in their savings account, it will earn about 50 cents per month (370 x 1.65%/12). However, if they used $ 370 to reduce the balance of their department store debt, they will save $ 15 per month (370 x 47.5%/12) before tax. Their best strategy, therefore, is to repay their loans, starting with the most expensive and ending with the least expensive.

Here is Lucy and Patrice's ranking of the cost of their loans, and interest on their savings opportunity:

Loans/ Saving Opportunity	C$	Pre tax %	Annual Savings from Repaying/ Saving $ 1000	Rank for Payment
Department Stores' Credit Cards	9,350	28.5%/.6 = **47.5%**	**475**	1
Visa	6,000	19.5% /.6 = **32.5%**	**325**	2
Car Loan	10,000	8.5% /.6 = **14.2%**	**142**	3
Credit Line	7,000	7%/.6 = **11.7%**	**117**	4
Mortgage	120,000	6.5%/.6 = **10.8%**	**108**	5
Savings	2,000	1.75% = **1.75%**	**18**	6

The best financial return to Lucy and Patrice is to repay their department stores' credit card balance[v]: They should immediately use their $ 2000 savings to reduce that balance. This will **save immediately $ 79** per month pre tax (2000 X 47.5%/12). If they left this amount in their savings account they would **earn $2.75 per month.**

The principle to apply, therefore, is to **view loans and savings as similar**. Compare the pre-tax cost/return of each and apply funds to the highest pretax percentage item. **The sooner you repay expensive debt the sooner you will be able to start to save. The longer you wait to repay your debt, the longer it will take to accumulate savings.**

If your loan is tax deductible, use the nominal rate (the rate specified by the institution), such as 28.5% for department store credit card shown above, as the relevant rate for your ranking.

Once you have repaid all loans, if you are paying taxes, **maximize your RRSP contribution**: the higher your tax rate the greater your potential RRSP return! Imagine you had no loans and you decided to apply to savings, the amounts you pay currently to service loans - and the income was sheltered in an RRSP account! The **tax benefit alone, would be significant savings!**

Ignore those mutual fund sales persons who tell you to borrow to save! There is risk associated with financial leverage! Don't go there! In our debt-counseling sessions, Doreen and I have seen too many individuals in debt, who were advised to take another loan to save! I think you will agree from the table above that this is a bad strategy, particularly for someone already in debt!

Patrice and Lucy have decided not to start "saving" until they extinguish their loans. They have developed goals and prepared a plan to be debt free in five years. They have committed to review their performance weekly to ensure they remain on track.

Finally, in my view, the first and essential step to get out of debt is to get your spiritual life in order.

> Though Patrice and Lucy are developing new "Attitudes" toward money, they have decided not to increase their "low cost" Credit Line debt to repay higher-cost debt; if they did, they fear they will not reduce total borrowing because of the current temptations to spend.

Did You Know

- Normally you spend 30% more if you use a credit card than if you didn't!
- Because of changes that the Government made in the late 90's, the Canada Pension Plan (CPP) is now financially sound!
- On a pre tax basis, if you started to save at age 35, $100 per month until age 65, you would accumulate $ 225,000 if the savings earned 10% per year compounded. However, if you delayed five years to age 40, total accumulation at age 65 would be $ 96,000!

Upcoming Events

Please pray for Michel & Doreen as we prepare for these seminars.

When	What	Where
23 March 2002	Managing God's Money Seminar sponsored by Focus on the Family & Briercrest Family Of Schools	Canad Inn Fort Garry, Pembina Highway, South Central Winnipeg
6 April 2002	Managing God's Money Seminar	Cannon Street Baptist Church - Birmingham, England
27 April 2002	Managing God's Money Seminar	Toronto
11 May 2002	Managing God's Money Seminar	Snowdon Baptist Church, Montreal
25 May 2002	Managing God's Money Seminar sponsored by Focus on the Family & Briercrest Family Of Schools	Regina
22 June 2002	Managing God's Money Seminar sponsored by Focus on the Family	Edmonton

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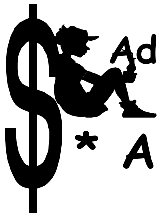
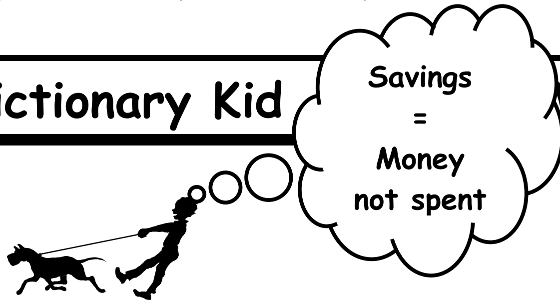


Adie's[vi] Corner (for the kids)

* A * V * I * N * G * S

Dictionary Kid



Why Should I Save?

We're talkin' no spending! I mean S-A-V-I-N-G-S! No posters! No comics! This gets really hard: No CANDY! I guess what they are telling us kids is that we must save some of the money we receive so that when we grow up we don't have to borrow! If we don't save, when we grow up we will get into the habit of spending and always will be broke!

I think we should make a "money schedule", as below, to show the maximum amount of money to spend every week, and the amount of money to save.

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Weekly Money Schedule

Date:______________________ **Weekly Savings Target**____________

Money In:

Allowance	______________
Jobs	______________
Gifts	______________
Total	______________

Money Out:

Giving	______________
Posters, Candy, Comics	______________
Gifts	______________
Total	______________
Balance (Money In less Money Out)	______________

First, set your target to save. Add up the money you expect to receive weekly from your allowance, from jobs around the house, from your neighbours, grand parents, and from birthday and Christmas gifts. Take away from this amount, money you will give to church, money to buy stuff like posters, and to buy birthday and other gifts. The balance is your savings. Increase this amount by spending less. I like to write stories and draw pictures to give as gifts to reduce my spending.

Now I have to start to practice all of this! Ouch! ☺

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[i] RRSP - Registered Retirement Savings Plan. According to the Globe and Mail of 5 March 2002, the 2002 "… season was a bust for the mutual fund industry…" preliminary figures for net sales for January and February was $ 6.9 billion versus $ 7.1 billion for the same period last year.

[ii] Ideally I should have issued this newsletter in January - forgive me!

[iii] The tax rate that applies to the last dollar earned.

[iv] $167 earned will attract tax at 40% and your employer will deduct (167 X 40%) $67. Thus only $100 will be available to spend or save. The situation improves when you give to a registered charity because you get a tax credit.

[v] Sometimes, included in "Furniture & Personal Effects" under "Things of Value…" on page two, are items that you may wish to sell to repay debt in the sequence I describe in this newsletter.

[vi] Adrienne is Michel's nine-year-old granddaughter. Both Michel and Adrienne have worked on several projects over the past five years.