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INVESTOR CLINIC

Should I invest my $100,000 inheritance or pay off debt?

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The Globe and Mail
Published Friday, May 20, 2016 5:17PM EDT
Last updated Friday, May 20, 2016 5:19PM EDT

My wife and I are in our 30s and we have about $130,000 in cash – $100,000 from an inheritance and $30,000 of savings. We also own about $30,000 of stocks (Celgene, Alphabet, Facebook, Polaris Infrastructure, Bombardier and three medical marijuana companies – Aphria, Mettrum Health and Canopy Growth). What do you suggest we do with our cash? For background, we own a $475,000 home with a $250,000 mortgage at a fixed rate of 2.7 per cent. We also have $20,000 on a credit line at 3.7 per cent and $15,000 of student loans at 4 per cent. We are planning to start a family in the next year or so and are considering a move back to Toronto, where I recently began work as a real estate agent after switching careers. Right now I commute to Toronto from our home in a mid-sized city about 100 kilometres away.

There are a lot of moving parts here, so I asked Derek Moran of Smarter Financial Planning in Kelowna, B.C., to weigh in.

Mr. Moran's advice: Ditch the debt, get rid of the killer commute and then focus on raising a family.

First, the couple should pay off the student loan and credit line in full. Next, they should make the maximum penalty-free lump sum payment permitted on their mortgage – it's usually 10 to 25 per cent of the original amount borrowed. When reviewing their mortgage documents, they should also take note of when they can make a second lump sum payment without penalty. Taking full advantage of prepayment options will lower their costs if they decide to move and have to break their mortgage.

"I don't want them to eat a big payout penalty if they sell the house, or feel pressured to port the mortgage to a new purchase," Mr. Moran said.

If the couple see their future in Toronto, selling their current house and moving makes a lot of sense, he said. Commuting such a long distance is not only stressful – it's expensive. "The commuting cost must be huge," he said. Including gas, depreciation, maintenance and other car-related expenses, he estimated that the total cost could be more than $20,000 a year.

What about the soaring cost of real estate in Toronto? "I have no idea about the future of the GTA [Greater Toronto Area] real estate market, but I cringe at the idea of paying such high prices. I would rent," he said.

The good news is that, after selling their house, the couple can move to Toronto completely debt-free and with about $320,000 in cash, plus $30,000 in stocks. (The $320,000 figure represents $225,000 in net proceeds from the home sale, plus the $130,000 in cash they have currently, minus $35,000 to pay off the student loans and credit line.)

With the cash in hand, the couple should shop around for the best rates on high-interest savings accounts, making sure to divide the cash into allotments of less than $100,000 so their savings are covered by the Canada Deposit Insurance Corp., he said.

“Take time to get established in the new career, have kids, chill out and hope a buying opportunity comes in the real estate market. Don’t fritter the cash away. If the [U.S.] Federal Reserve raises rates in June as some predict, the Bank of Canada may follow and that should soften real estate prices a bit,” Mr. Moran said.

“Eventually prices will cycle and the real estate ‘love-in’ will end. The risk of the GTA real estate market and working in the real estate industry has to be discussed and managed. I would not want to have a $600,000 mortgage, kids on the way, wife not working and him gone seven days a week struggling to make ends meet.”

Finally, Mr. Moran said the couple should dial back the risk in their stock portfolio, which currently includes several speculative holdings. “I was surprised by how aggressive the investments are,” he said. He recommends blue-chip companies that pay rising dividends – such as Canadian banks, utilities, telecoms and pipelines. Dividend-paying stocks will provide the couple with another source of income and, over the long run, capital gains.

“I’ve seen hundreds and hundreds of people be fantastically successful investing in blue-chip dividend growers. There’s no need to take so much risk,” he said.

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