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Pay Down Your Mortgage More Quickly

Some of the best advice that may be given to new home owners relates to the value of paying down a mortgage more quickly. Over the past decade, housing costs have risen substantially. Current low interest rates have made it easy for many people to obtain a mortgage. As a result, Canadians have been taking on more and more mortgage debt, which doesn't come without risk.

In 1984, the average price of a Canadian home was about $76,000, which is about $158,000 in today's dollars. Today, the average house price is about $502,600. In Vancouver, where prices are the highest nationally, it is $708,500.*

As the economy continues to recover, interest rates are expected to rise which may pose a significant risk to many mortgage holders as mortgage interest payments increase. Recall that in 2008, mortgage interest rates were above 6 percent.** If interest rates were to rise by 3 percent, the monthly payments on a 25-year, $160,000 mortgage would increase by over $265. Over the life of the mortgage, this equates to $80,000 of additional interest costs.

The change in the financial position of a mortgage-holder may also create risks. Many mortgage holders fail to contemplate a potential loss of income. A sudden job loss or an unexpected illness could put a strain on meeting mortgage obligations. This may be further complicated by other expenditures such as the cost of supporting a child's post-secondary education.

Here are some thoughts about home purchasing and opportunities for retiring a mortgage sooner:

1. **Buy within your means.** Make sure that you can afford the mortgage. One way to measure this would be to determine if you can afford the mortgage payments on a five-year fixed mortgage with a 20-year amortization. If so, a 25-year amortization could be used to allow for a bit of room should interest rates rise.

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1. **Familiarize yourself with the terms of the mortgage.** Understand the terms of conditions of the mortgage before entering into it. Be sure you have liberal pre-payment privileges.

2. **Set up "accelerated" weekly/bi-weekly payments.** An accelerated payment allows for extra payments to be made against the principal as part of the regular payment stream. This step alone may save around three to four years on a 25-year mortgage.

3. **Use tax refunds.** Tax refunds, such as those received after contributing to a Registered Retirement Savings Plan (RRSP), can be applied to "retire" a mortgage earlier.

4. **Give your payment a raise when you get one.** It may be surprising how additional dollars contributed to each payment can impact how quickly a mortgage is paid over the long run.

5. **Use the annual lump sum option.** Most mortgages allow for an additional annual lump sum payment. Extra funds, such as a work bonus, can be effectively used to make a one-off payment.

*Canadian Real Estate Association figures, August 2015. **Canada Mortgage and Housing Corporation, Average Residential Mortgage Lending Rate – 5 Year.

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