FINANCIAL POST

Friday, May 1, 2009

Family file: Too much, too soon?

Dana Lacey, FP Magazine

Kagan McLeod

Like a lot of families, Julie and Don Stanley have found themselves struggling to rebuild their wealth after the market nosedived last year, taking a third of their retirement and RESP savings down with it. If their situation were more straightforward, Julie and Don, aged 41 and 39 respectively, could look for ways to put aside more money and rebuild their battered savings. After all, they've got decades to go before reaching retirement, and the oldest of their three children won't finish high school for another eight years. Problem is, the Stanleys (not their real name) have also gotten into hot water over their near-term budget. Over the past two years, they've borrowed to invest in real estate and renovate their home. They've also taken time off work to pursue a new business venture that has yet to pay off. Complicating matters is the fact that they're currently scheming to make a major life change that will uproot the whole family from their home in B.C.'s Port Coquitlam for a move to Mexico, where they plan to start a second small business.

With their minds on so many projects, this usually frugal family has lost touch with their finances. Over a short, chaotic period, the Stanleys have virtually wiped out their savings and built up nearly $73,000 in debt. It started with an entrepreneurial itch. A year and a half ago, Julie, a teacher, invested $13,500 from the family's savings to launch an online business. "I needed a career change. I wanted more control over my own creative output," she says, "but I didn't feel I could leave my job completely until the business was up and running." So she took a 20% leave - and a 20% pay reduction on her $80,000 salary - in order to spend time researching her new venture. That decision reduced the Stanleys' household income from roughly $120,000 to $105,000, including Don's $35,000 income as a manager at a small business, along with others sources, such as child tax credits.

Financial Snapshot

Income	
Julie	65,000
Don	35,000
Other	5,000
TOTAL INCOME	$105,000
Expenses	
Income tax	35,100
Property tax	3,900
Mortgage	13,800
Hydro, gas, communications	4,300
Food, supplies	12,000
Professional fees	1,800
Bank, interest charges	2,400
Clothing	1,800
Transportation	9,600
Entertainment	3,000
Children's activities	4,000
Charity, gifts, misc.	5.900
TOTAL EXPENSES	$97,600
Savings	
RESP	1,400
Other	6,000
TOTAL SAVINGS	$7,400
Assets	
House	475,000
Rental property	56,300
RRSP (Don)	17,600
Non-registered	7,200
Cash	5,200
TOTAL ASSETS	$561,300
Liabilities	
Mortgage	256,900
Mortgage share on rental	35,100
Debt	72,900
TOTAL LIABILITIES	$364,900
NET WORTH	$196,400

The following summer, the Stanleys took out a $9,000 personal line of credit to pay for outdoor renovations on their home. Then they drew on their savings again to invest in a small rental property with a group of friends, but soon realized they had reached the limit of - and probably gone over - their ability to carry debt. "I started ignoring my finances," Julie says. "Maybe I hoped the problems would just go away."

So far, the impact of their reduced income hasn't done much to impact their general family budget. "We're frugal spenders," says Julie. "We write a yearly budget, and I track everything we're spending monthly." Their ability to save, however, has essentially been wiped out. More worrisome is the impact of the market crash on their already slender investments, now worth $30,000 in both registered and non-registered vehicles.

To grow the family's income, Julie is hoping to increase her monthly earnings by $1,000 to $1,500 by year's end, assuming she can launch her online business this summer. The biggest hurdle at the moment is building the website, which is taking more time than she has set aside for the task. In the meantime, Julie has joined an investor club to start putting some money into stocks "while the prices are so low."

All of this effort is geared toward

achieving the Stanleys' ultimate goal: a new life in Mexico. Both Don and Julie have lived there and want their children to experience a new culture while they're young. "We decided we had been saving all this money for retirement instead of living the life we want now." The Stanleys now say that they'd like to sell their B.C. home, valued at $475,000, while keeping their rental property and setting up a small business in Mexico to complement Julie's online venture. Overall, the Stanleys figure they'll need $5,500 a month to achieve their goal, but they say that they need to do more research into issues such as the cost of living in Mexico and school fees.

For that reason, they haven't set a hard timeline for making their move to sunnier climes, but the Stanleys hope to be sitting on a Mexican beach within three years. The question is, how can they organize what they've got to achieve their goal?

What the experts say

Our advisers have one top-line recommendation for the Stanleys: Slow down. "They're trying to do too many things at the same time," says Karin Mizgala, president of LifeDesign Financial in Vancouver. "They have kids, a business, rental properties, investing club, two jobs and a plan to move to Mexico that all need time and attention." Kevin Cork, a certified financial planner with Absolute Group in Alberta, agrees. "Given their short-term horizon for moving to Mexico in three years, it seems odd that they would be dealing with distractions like rental properties, starting businesses and an investment club." If the Stanleys want to start moving forward, Mizgala and Cork continue, they have to set priorities. Their first should be to ensure they are living within their means, that they don't incur more debt and that they use every dollar of their income as effectively as possible.

For Mizgala, the Stanleys second focus should be to get Julie's business up and running so that the family can start generating more income. To do that, she says, Julie should set aside a block of time to hammer out a solid business plan with realistic goals, financial projections and timelines. Then she must make sure to follow that plan. "Then, once the business starts to generate income, they should direct the profits to short-term (building an emergency fund), medium-term (moving to Mexico) and long-term (financial independence) savings - not to expand their lifestyle."

Given that the Stanleys are relatively young and have time to figure out their retirement-planning strategy, Cork suggests that they start to focus on how much it will cost to move to Mexico. "They need to factor in one-time moving expenses, starting or buying a business, buying a house, and ongoing monthly expenses," he says. "Like any small-business owner, they will also need to consider how they're going to pay for health-care costs, disability insurance and so on."

On top of that, they'll have to consider the costs of educating their children, a service they get for free in Canada. Then there are Mexican taxes, regulations and visas to consider. Cork adds that Mexican banks have become just as tight with their money as Canadian banks for small-

business loans, so the Stanleys should have other options in place. He suggests one of them head to a local community college for courses on the core aspects of owning a business. If their online business can generate $1,500 a month, it may be a good idea, he says. But will they have the time to run both companies? "And what if the site only makes $100 a month? How long do they spend time and money on it?" Besides, Cork says, since Julie makes nearly twice as much as Don in their regular employment, why is he not taking the time off instead? "That would have half the impact on their income than the current plan does."

Alternatively, they could wait until the kids are in university to make the move as a sort of semi-retirement plan, he says. That will give them a decade to build up a much larger nest egg, establish the online business and save for Mexico.

Waiting to make the move has other advantages. For example, it would give the Stanleys more years to contribute to RESPs and take advantage of the federal government's 20% matching benefit of up to $1,000 a year for each child. That free money won't be available to them once they move. But if the Stanleys are determined to move soon, Cork and Mizgala say they should at the very least wait until they've got money to buy a house and live for a year, on top of whatever they need to buy a business.

"And before they pack their bags," Mizgala says, "they should have a solid business plan that shows how they will generate income." Cork adds that, if they're determined to move in the near future, they should consider selling their home now and renting to avoid the risk of further declines in the real estate market.

As for other parts of their plan, Cork and Mizgala both say that the Stanleys need to simplify their financial activities and start building a coherent strategy, for both short-term and long-term goals. That will ensure they're getting maximum value out of every dollar they earn - and get them that much closer to a new life in Mexico.