Is building an emergency fund more important than other financial goals?

Sami, 51 and single, wants to put extra mortgage payments and RRSP contributions on the back burner until her savings are built-up. Is this wise?

Q. I am 51, single and have no dependents, with many working years ahead of me. I earn about $70,000 annually at my tech job. Due to life circumstances, my finances are not in the best shape.

I have $6,000 in emergency fund savings in a high-interest savings account, $16,000 in an RRSP ($70,000 contribution room still available), no TFSA contributions and no unregistered investments. I also have a company pension and no personal debt except for a mortgage of $239,643 (at a variable rate of 3.2%), with a bi-weekly payment of $868 ($768 payment plus an extra $100 towards principal).

I have between $1,500 and $1,800 per month in cash flow available after all expenses and commitments have been met.

My current financial goal is to build the emergency savings to $20,000 (six months' worth of expenses) and not make any RRSP contributions or extra mortgage payments until the goal is met (eight months from now, by my estimation). Would this be wise?
–Sami

A. Thanks for your question, Sami—and congratulations on having no debt other than the mortgage; that is the cornerstone of good financial planning. You are also doing great by having $6,000 in emergency savings and, as a single person, that should be the first thing to build. You can fall back on that money in case you are laid off or have an urgent, unexpected repair on your home.

It's also important to note that you may also have some disability insurance coverage from your employer to cover you when off work from illness or disability so that will give you an extra level of financial security. And the $16,000 you have in RRSPs could be accessed if required, although you're likely best off to consider this RRSP money strictly retirement savings to utilize when you leave the workforce.

Building on that, you say you'd like to grow your emergency fund to six months' worth of savings, which would require an additional $14,000 and roughly eight months of time to achieve. In the meantime, you wouldn't make an RRSP contribution. This is doable and something you can easily execute as the first step in your plan.

To decide how best to allocate your $1,500 to $1,8000 per month in excess cash flow once your emergency fund is built up to $20,000, you can do a couple of things. At your current payment pace, interest rate and top-up amount, your mortgage would be paid off completely in 13 years. With your current annual income, an RRSP contribution will give a moderate tax deduction today but you may not want the additional future RRSP taxable income in retirement.

I would suggest calculating your estimated pension (you can obtain a pension estimates statement through your employer) to see what savings are needed for your planned retirement lifestyle. Depending on your planned retirement date, you may want to consider increasing both your optional payments to your mortgage, as well as opening a Tax-Free Savings Account (TFSA) and making modest contributions over the next few years. That’s because a TFSA can be invested for long-term savings with no tax consequences at withdrawal time and still provide income in retirement, thus making saving and investing in a TFSA a good option for you. (If you haven’t contributed at all over the years, then your accumulated TFSA contribution room as of 2020 is $69,500.)

You have a lot of the pieces in place already but I suggest you speak with a fee-for-service financial planner to map out your retirement strategy in more detail.

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