When Interest Rates Rise

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One way to curb rising inflation is to increase interest rates, and that is what the Bank of Canada (BoC) is expected to do incrementally - over the next year. As interest rates begin to tick upward, it is an ideal time to look at your financial position, including your debt and savings strategies.

Rates hikes and your debt

Simply put, higher interest rates increase the cost of borrowing money. This is especially true for any variable-rate debt you may have. Variable-rate debts include home equity lines of credit and some types of mortgages, loans, student loans and credit cards.

Variable-rates are tied to the BoC's interest rate, so they are a prudent financial choice when rates are low. However, when rates go up, the cost of repaying debt might rise dramatically. These increased payments barely touch the principal that you owe, so it just costs more to maintain your debt without measurably changing your financial situation. Not only do these higher payments eat into your budget, but funds spent on debt may also impede your ability to save for the future.

The positive news is that you can take some concrete steps to prepare for and potentially mitigate the impact of rising interest rates. It's a good idea to:

- determine which of your debts are variable or fixed
- avoid taking on any new debt
- pay down as much of your existing variable-rate debt as you can
- switch to fixed-rate mortgages and loans if your lender(s) will allow it
- review your budget to see where you can save money in the short term
- target your highest rate debt with any extra funds you may have

If you do have the ability to pay some debt down before rates hit their peak this year, it could potentially save you a significant amount in interest fees. This tactic may also help free up funds that you can put toward a savings goal or create a financial buffer in case inflation and interest rates continue to rise.

Rates hikes and your savings

Regarding how interest rate hikes could impact your portfolio this year, it depends on the types of assets you have. Higher interest rates may position you for better returns on some fixed-rate savings investments, or there may be opportunities for long- and short-term growth that you are not seeing. There is no better time than now to speak with a financial advisor who can help minimize the impact of rising interest rates on your long-term plans.

A financial advisor can help you analyze your current financial situation and help you build a budget that maximizes your income to reduce debt and increase savings. They can also help you set or re-establish savings goals considering the current economic situation while refining a long-game investment strategy that positions you for the future while overcoming today's challenges.

Contact our office to get the conversation started [1]. We are here to help you make the most of your money and keep your savings goals on track.

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