FLY WITH THE WIND!

Engaging Inuit Youth in the Canadian Economy

Good Debt vs. Bad Debt
Which Do You Have?

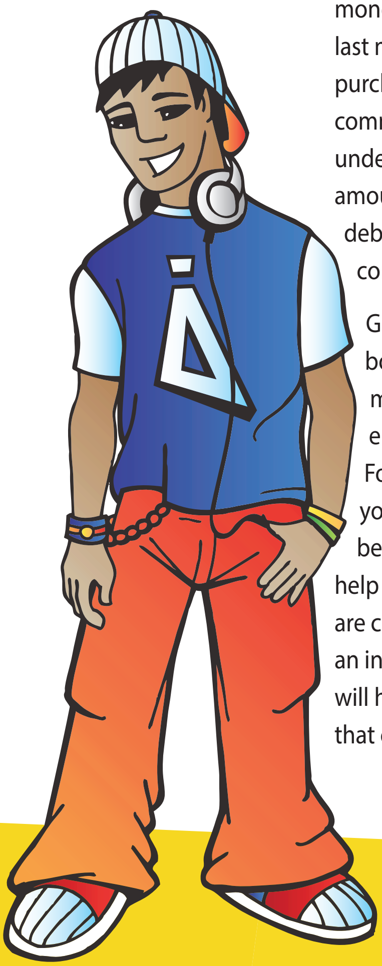
There has been a lot of news lately about how much debt Canadians have. Debt basically refers to money you owe to various sources, such as credits cards, car loans, a mortgage on your house or student loans.

Basically, if you owe money to anyone you have a debt.

The issue isn't that all debt is bad,but there are a couple of factors to consider: Can you afford the debt you have? And is your debt "good" or "bad"?

This fact sheet focusses on the differences between good and bad debt. Understanding the differences can help you understand how debt affects you and your wallet and how to determine what kinds of debt are good or bad.

Most adults have debts of some kind. You may owe money on your credit card for purchases you made last month, or you may have taken out a loan for the purchase of a boat or snowmobile. One thing common to all kinds of debt is that you need to understand the debt terms (including the interest amount and repayment terms) and monitor the debt so it doesn't become a huge monster that controls your life.



Good debt generally means that you have borrowed money to improve your life in a meaningful way. That borrowing will help you to either earn more money or save more money. For example, taking out a loan to help pay for your education is generally a good debt. This is because having more education and training will help you get a better job or increase the income you are currently getting from work. This kind of debt is an investment in your or your children's future and will help you get a better job and all the benefits that come with it.

Another form of good debt is considered to be a mortgage on a home. Although many Nunavummiut live in public housing, some people are able to buy their own homes. Without going into all the details about how much a house is worth and what people paid for it, a mortgage can be considered a good debt in most cases. It means you are helping to control your living costs. Eventually, you will pay off the mortgage and not have to make more payments. Mortgage debt helps people in the long run by helping them own their homes, rather than paying rent all of their lives. In addition, the home will likely be worth a lot more money than when it was purchased – another bonus to owning your home. Of course, owning a home involves a lot more planning than simply getting a mortgage. People need to consider a number of other issues before determining if home ownership is right for them.

Other forms of "good" loans include money to invest in things like a Registered Retirement Savings Plan (RRSP) or to invest in your own business. These investments are made to save on taxes or to hopefully make more money. Borrowing money to make money can be a good thing. Just make sure the investment is a wise one.

There are more examples of "bad" debt than good. Putting a trip to Las Vegas on your credit card when you know you can't pay it off quickly is considered to be a bad debt. You could argue whether you "need" or "want" a trip to Vegas. But, in reality, impulse purchases with no long-term value and with little likelihood of early repayment are considered bad debts. Also, consider the interest costs of carrying debt on your credit card. A "bargain" may not seem so cheap if you have to pay a lot of interest on the debt. Too often, the joy of the purchase doesn't last as long as the payment of the debt.

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Take a moment and look over your last credit card statement. See if you can determine which is good debt and bad debt. Most people have a lot of smaller purchases on their credit card that make their life easier and more fun. You should let yourself have small things to make you happy, if you can afford them. The trick is to keep these impulse buys under control. Try not to get the debt level up so high that you can't pay it off in a month or so. When buying bigger things, like holidays, make sure you have most of the money saved up for them ahead of time.

Similarly, borrowing to buy a car is usually not considered to be a good use of debt as the car will be worth less as time goes on. This loss of value often happens faster than the amount of money that have to be paid back from the debt and a lot of people are shocked when their car falls apart before their loan is paid off.

In the North, the situation becomes less clear when talking about borrowing money to purchase a boat, snowmobile, or other equipment for harvesting. These items can be an example of good debt, if used to supply food to a family or to sell it to other people. In this case, they are being used to get important sources of food for the family, to make money or to help others in the community. Borrowing to buy the same equipment only for fun however, would fall under the same case as buying a car.

In summary, bad debt usually involves:

- Buying things on credit that you don't really need;
- Buying things on credit that you can't afford; and/or
- Buying things on credit that don't increase in value or bring you more money and that take a long time to pay off.

If these things sound familiar, then most likely the purchase is in the "bad" debt category.

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