

Smart Money: Taking things for granted can cause chaos for your finances

Sep 15, 2021 11:07 AM By: Brad Brain / Smart Money



Brad Brain: "If I was to ask 100 people if taking things for granted was a good idea, I expect that I will get 100 negative responses. But in the real world people take things for granted about their money all the time." | Getty Images

People take things for granted all the time. They may assume that things will stay the way that they are now. Or they may assume that the future will meet their expectations. And sometimes these kinds of assumptions will work out fine. That is, as long as things actually stay as they are, or the future unfolds as expected.

But, of course, in the real world things do change, and the future is unpredictable. The consequence is that taking things for granted can cause chaos for your finances.

Here's what I mean. Many Canadians have a significant amount of their wealth tied up in their home. Some of them will be looking to downsize their home to supplement retirement income. As it stands

today, any capital gains on your principal residence are not subject to taxation. But what if the federal government introduces capital gains tax on your home? How would that affect your retirement?

Some people will look at rental real estate as a solid source of income that can cover a mortgage against the property. And if everything goes off without a hitch it can be. But what if your tenant moves out, and the property stays vacant for six months? Can you still cover the mortgage without that rental income?



 Ad.Plus

Some people will look at a hot investment idea through rose-coloured glasses. They will see the potential for this investment idea to really take off and be willing to pay high prices in order to get in on the action. But what if the future is less than perfect, and the investment fails to meet expectations? Will buying that investment at a high price still be justified?

Some people will look at how much is sitting in their chequing account and think that money is available to be spent. But what if the dishwasher breaks down at the same time that the vehicle needs some repairs? Is there still money enough to cover unexpected emergencies?

Clearly, taking things for granted can put us in a tight spot if the future goes in a different direction than expected. So what can we do about this?

The answer is to operate with a margin of safety. A margin of safety means being cautious in case the future doesn't turn out as well as you hope. It means you still have some resources that you can turn to if you don't get the results that you predicted. It means that you don't go all-in on something if that could leave you in a very bad spot if the future is different than expectations.

Here's how Warren Buffett puts it: "Don't try to drive a 9800-pound truck over a bridge with a 10,000-pound capacity. Go down the road a little further and find a bridge with a 15,000-pound capacity."

Can the bridge with a 10,000-pound capacity handle a 9800-pound truck? I mean, it should be able to, right? Sure, it should. But there is not much room for error. If there is little consequence to being wrong, then the margin of safety concept may be optional. If the question is what to watch on Netflix, then the worst thing that can happen is that you waste some time on a bad show. If the question is whether this bridge will support a 9800-pound truck without failing, now the stakes are different.

People make 9800-pound truck decisions with their money all the time. Should you depend exclusively on your home equity for retirement income? Should you be reliant on rental income to meet your mortgage obligations? Should you pay lofty prices for investments with uncertain futures? Should you spend all the money in your chequing account? Maybe you can get away with these things. But maybe not.

If I was to ask 100 people if taking things for granted was a good idea, I expect that I will get 100 negative responses. But in the real world people take things for granted about their money all the time.

Don't take things for granted. When the risks are meaningful, act with a margin of safety.

Brad Brain. CFP, R.F.P., CIM, TEP is a Certified Financial Planner in Fort St John, BC. This material is prepared for general circulation and may not reflect your individual financial circumstances. Brad can be reached at www.bradbrainfinancial.com.

Comments (0)