PBS Ep146 AskPB Pay Off Debt Transcript Audio

Patti Brennan: Hi, everybody! Welcome to "The Patti Brennan Show." Whether you have $20 or $20 million, this show is for those of you who want to protect, grow, and use your assets to live your very best lives. This is part of the "Ask Patti Brennan" series.

The one question we are getting quite a bit right now is, "Hey, I've got a little bit of extra cash. I'm going to pay off my debts."

The first question that I would ask is, what is your goal in doing so? Is it to help your credit rating? Is it to increase your cash flow? What is the goal behind the idea of paying things off? Because nobody really likes debt. I totally get it. But let's understand what we are trying to accomplish, first.

Also, what are the sources? What is the source of those funds that you are going to use to pay it off? It could be a car loan, it could be whatever. If you are going to use your emergency fund to pay it off, I would be really careful. I would be hesitant to say that that's an OK thing for you to do, because unless you can replenish it really quickly, that emergency fund is there for a reason. It's for emergencies. Once you pay off that loan, chances are you're not going to get another one, at least at the same interest rate, especially in today's interest rate environment.

Now, if you are paying off credit cards and they are at high-interest rates, well then by all means, go for it. If you are paying 19 percent on a credit card and you've got money sitting in a money market account, even at 5 percent, that math doesn't work. I'm OK with you going ahead and paying off that credit card, as long as you take that same credit card, stick it in a glass of water, and throw it in the freezer.

Unfortunately, what often happens is they pay off their cards and they grow back up again. Not OK, especially if you are using your emergency fund to pay it off. Makes no sense whatsoever.

When we think about mortgages, some people come in and say, You know what, I don't want to have a mortgage anymore." I totally get it. Again, what is the source of the funds that you are going to use to pay off that mortgage? By the way, what are the tax implications? Are you going to be selling investments, paying capital gains taxes to pay off that mortgage?

Which might feel great, by the way, but it might end up costing you a lot more in the long run. Also, we have to be cognizant of the fact that most mortgages today are fixed at four percent or below.

I think I've got to be realistic to say to all of you that we're probably not going to see three percent -- maybe even four percent --mortgages anytime soon. If you get rid of that four percent mortgage or below, you're probably not going to get it again. It's OK.

It might feel great, by the way, and by all means, if that doesn't make a difference in your long-term financial security, again, it's all about outcomes here. It's about solvency. It's about making sure that you can accomplish your short-, intermediate-, and long-term objectives.

These are the things that you want to speak to your advisor about and get a second set of trained eyes looking at the whole situation. You might want to pay off that mortgage. That's fine. It's important for all of us, again, to be real. It's probably not realistic for anyone to be able to get a mortgage or refinance and get a lower interest rate. Sure, if you're trying to free up cash flow, you could get a mortgage or you could get a loan that might have a longer term. That's something that we're seeing a lot of with car loans.

It used to be four years, was it? Then it got to be five years. I've got to tell you, a 72-month car loan is a tough pill for us to swallow. Sure, you can get that fancy car… but God bless you. The problem is that they depreciate so quickly, and a lot of people get upside down. They owe more money than what the car is worth. Just be really careful when you're evaluating loans, paying them off, doing what have you. Get an extra set of trained eyes to look at that formula.

When it comes to mortgages, the days of looking at the after-tax cost of a mortgage are probably over for most people listening and watching this podcast because of the law that was passed in 2017. Most people are not itemizing. You're not even taking advantage or you're not getting a benefit of being able to deduct mortgage interest.

When you're thinking about that mortgage and maybe paying it off, it's a pure calculation. What's the mortgage rate? Where are the funds going to come from? Is there a tax implication? Do the math.

I'd also like to say to all of you that I'm always reminded of what Morgan Housel says, "There's a difference between rational and reasonable." The math is one thing, but if paying off your mortgage means that you can sleep at night, terrific. That's great.

Just be realistic in terms of what you're going to do with that cash flow. I wouldn't necessarily assume that you're going to take that cash flow and invest it because to be honest with you, most people don't. Be realistic, and if you still want to pay it off, by all means, do that, especially if it's causing you any kind of discomfort, affecting your peace of mind. You know what? Guess what? It's perfectly reasonable for you to get rid of the thing, get rid of it if it makes you feel better. Because again, as with all of these goals, we're not going to accomplish everything all at once. Sometimes a decision like that makes the rest of it sustainable. We want long-term financial security, long-term peace of mind. That is the goal behind real financial planning.

I am Patti Brennan. We're Key Financial Wealth Management with wisdom and care. I'm really grateful for you tuning in and listening today. If you have any questions, go to our website, www.keyfinancialinc.com. Feel free to ask any questions. Reach out to us.

Let us know what you'd like to hear about. In the meantime, I hope you have a great day. Take care now.