ETF insight

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Mitigating the effects of the unexpected

Protecting yourself from a crisis

Pondering the possibility of a personal health crisis is not easy and, despite the growing prevalence of debilitating illnesses and other disabling events, many people put it on the backburner. However, when the unexpected happens, the immediate financial impact can be devastating and negative effects on longer-range plans such as retirement are a real possibility.

The Sun Life Canadian Health Index found that 28% of Canadians have already experienced a serious health event or accident, and 39% of them said it triggered a significant lifestyle change. The report also found that, while 82% of Canadians realize a major health event could negatively impact their personal finances, only 13% have money set aside for unforeseen healthcare costs.

A report by the BMO Wealth Institute supports those data and says that 84% of Canadians believe they would face a major financial hit in the event of disability. Of those who have tapped their rainy day funds to pay for unexpected health expense, 58% couldn't cover its full cost.

Given those figures, it is not surprising that 53% of Canadians aged 45 to 54 years are struggling financially after a major health incident. They have been turning to credit cards or personal lines of credit, personal savings, borrowing from loved ones, and remortgaging or selling their homes.

Preparation for any unexpected problem period begins with accumulating sufficient savings to cover short-term needs such as childcare, eldercare, and mortgage or interest payments. The common rule of thumb is to have the equivalent of three to six months' income but, with a quarter of Canadians living paycheque to paycheque, some see it as a pipe dream.

However daunting the figure may seem, it must be tackled and should be more achievable if tough decisions are made, such as cutting non-essential items. Just forgoing a daily latte can add over $1,800 per year. A review of options in expenses like cell phone or cable fees may find more. An automatic savings plan is also useful. Opting for automatic transfers of a set dollar amount or percentage of income to a separate rainy day fund lowers the temptation to spend. Any unexpected windfall or tax refunds should go to savings.

Such savings, while important, still only provide a short-term solution. Actuaries estimate that an individual, who saved 5% of their income for 10 years, would run out of money after only six months of total disability. Clearly, self-insuring is not the best approach to the possibility of a long-range problem.

For financial protection in the event of a longer-term issue, Canadians should consider insurance in their planning. It is a risk management tool that can ensure long-term financial stability with coverage such as disability, income replacement, long-term care and critical illness.

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The insurance goal seems simple enough – ensure funding to carry on after a negative event - but needs are unique to individuals. For instance, the disability protection needed by a professional athlete will likely differ from someone at a desk job. It is advisable to review specific requirements with an insurance professional.

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