Need Somewhere to Park Some Cash? Here's How to Decide Between HISAs vs. GICs

Description

Do you have a large purchase to make in the near future — perhaps a down payment on a home? What about a new car? Are you going back to grad school and have tuition due soon? Or perhaps you're getting married and need to cough up some dough for that dream wedding and honeymoon?

Whatever the case is, your objective here is safety of principal — that is, making sure the money you've saved for any of these goals is still around when you need it. Obviously, risking it in stocks or even bonds is a bad idea, given the current market volatility and rising interest rate environment.

What can I do then?

Your best option here outside of stashing it in your mattress (please don't do that) is to use either a guaranteed investment certificate (GIC) or high-interest savings account (HISA).

Both investment vehicles are considered risk free (they're backed by the Canadian Deposit Insurance Corporation) and offer you interest in exchange for leaving your money with them.

But before you make your selection, make sure you answer these three questions to ensure you pick the right product for your needs.

Am I okay with leaving the money locked up?

This is the first question you should ask. The reason is that some GICs do not allow you to redeem your money before a lock-up period is over. Others (called "cashable" GICs) do but may penalize you with a lower interest rate earned.

Therefore, if you're not sure about whether or not you might need to withdraw your money earlier than expected, a HISA is the better investment vehicle. By using an HISA, you have access to your cash when you need it, without the fear of a lock-in period.

When do I need the money?

If your answer to the previous question is a "yes," you can proceed with a GIC, which generally offers you a higher interest rate in exchange for a lock-up period. What you need to figure out now is how long it will be before you will need to withdraw and spend the money.

In this case, examine the purpose of the funds you are depositing. If it is for a down payment in say, five years, try and get a GIC with a term of at least four to maximize the amount of interest you earn on it. The key here is to be realistic with your timelines, so try to be conservative when estimating.

What interest rate am I targeting?

Once you've decided how long you're willing to leave the money locked up for, it's time to shop around for the best interest rate. GIC providers have a bewildering assortment of offers from market-linked GICs cashable GICs and those earning simple vs. compound interest.

It's easy to get lost in the assortment of choices out there, but the best way is to shop around with the big five Canadian banks for the best rate you can find. Make sure you take your time and don't get suckered into a sub-optimal offer. Always, always read the fine print.

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Date

2025/08/15

Date Created

2022/04/12

Author

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