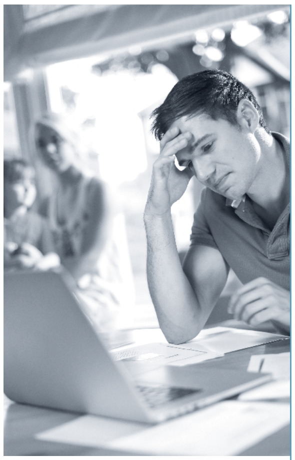
HBKS® Wealth Advisors

Paying Down Debt

Do You Have a Snowball's Chance?



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It's not an uncommon dilemma. You're looking at a mountain of debt and don't see how you're ever going to pay it off. Well, there are a couple of approaches that might just work for you — ways to tackle debt that you might not have been aware of.

First of all, be careful about responding to ads or robocalls offering debt relief or credit repair. If you are considering a service, read the fine print and make sure they are accredited. Many are scams that promise to reduce or remove debt for an upfront fee — sometimes a substantial fee. And if you miss a payment, you could incur outrageous late payment charges. We've seen penalties as high as 400 percent interest.

But there are also a couple of methods that many people have found effective in paying off debt in the least amount of time and for the least amount of money. The so-called "snowball method" and "avalanche method" are much alike, just different in how you employ them to attack your debt.

FIRST STEPS

The first step toward getting out of debt is to stop incurring debt. In particular, if you have high interest rate credit cards, put them aside. The general rule for credit cards is to use them to build your credit and to pay them in full every month. You don't want to fall into the habit of making minimum payments and letting the balances ride; it's just too easy to get behind and find yourself unable to catch up. The second step is to create a debt relief budget. How much each month will you dedicate to reducing your debt?

Once you have a budget and the determination to stick to it, you can choose your debt reduction method.

SNOWBALL OR AVALANCHE

The snowball method involves paying off your smallest balance first then moving on to the next smallest. You first make your minimum payments on each debt. Then whatever is left in your debt budget you apply to the smallest debt. The avalanche approach involves tackling high interest rate debt first. Make your minimum payments and apply the rest of your monthly budget to the debt with the highest interest rate and so on.

The two methods each have avid followers, adamant defenders. The method you choose will be based on your particular situation and how you are going to apply it. So do the math — you can find a debt relief calculator online — to see which one works better for you. Most important is to pick a debt, any debt, and hone in on it until it's paid, then move on to the next one.

Another misconception is that a bank loan, if you can get one, is the best way to alleviate debt. "Consolidate" is a favorite pitch. If you have several credit cards and you're paying 25 percent interest with no end in sight, a bank loan might be your way out. But the loan payment calculator tells an interesting story.

Take a couple with a combination of a student loan at four percent interest, a doctor bill at zero percent, two car loans at seven percent, a bank credit card at 13.5 percent, and a merchant credit card at nine percent, for a total debt of $54,000. Using either the snowball or avalanche method and a debt payment budget of a thousand dollars a month, the loans are eliminated in just over five years at a cost of between $8400 and $9400 in interest. Meanwhile a bank loan at seven percent costs more than $11,000 in interest to pay off in the same amount of time.

No matter how you attack your debt, you'll need two things: a loan repayment budget and the determination to stick to it. So get motivated and get started.

If you'd like to discuss your debt and how to tackle it, please give us a call. As always, we're here to help.

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Michael serves as a financial advisor in the Fredonia, New York. office of HBKS® Wealth Advisors. He specializes in providing personal financial planning for investments, retirement, protection planning, retirement income, estate planning strategies, education funding, tax management strategies and wealth preservation strategies.

Michael joined HBKS® in 2018 after working as a financial advisor and field director for Northwestern Mutual for six years. He earned his Bachelor of Science degree in Finance from Duquesne University.