Tips and Strategies for Cutting Credit Card Debt

Today we're going to talk about a financial challenge that impacts many Americans – credit card debt. There's no shortage of information and analysis when it comes to credit card debt. A few of the resources we'll be citing today are an Investopedia article that was updated in November of 2018, "Expert Tips for Cutting Credit Card Debt." We'll dive into the article's tips and share our own perspectives about them. But first, let's start with the numbers.

According to the May 2018 Federal Reserve Report on the Economic Well-Being of U.S. Households in the year 2017, 83% of American adults have at least one credit card. However, only 45% always pay their credit card balance each month. 21% of American adults with a credit card pay their balance off some of the time and 28% carry a balance on their credit cards each month. Certainly, a lot of people carry some degree of debt, but credit card debt is especially dangerous. According to the Investopedia article mentioned earlier, average credit card interest is about twice the nominal interest rate on loans like home equity or a mortgage.

So, it sounds like there's a lot of expensive debt out there. So, what can you do about it? Well, the first tip is to have a realistic plan to eliminate the debt. One way to organize your debt is to pay off the debt with the highest interest rate first. Over time, you'll pay down the debt and your financial prospects may improve. I do caution against adding new debt while you're paying down current debt. Don't let your excitement about your improving circumstances stop your momentum.

Another option for eliminating credit card debt is to transfer a higher-interest credit card balance to a lower-interest rate card. Credit card companies will sometimes offer limited rates, or even short interest free periods, that would allow you to erase debt faster than paying it off at a high interest rate.

Credit card debt can be a big problem for many Americans. According to the Investopedia article, some financial service professionals suggest that you should only be paying a maximum of 10% of your monthly income in credit card and other consumer debt. Nationally known debt counselor Howard S Dvorkin also notes in his book, "Credit Hell: How to Dig Out of Debt" that it should be possible to pay off any of your debt in 12 to 18 months, maximum. If you have more debt than you can pay off, it might be useful to reach out to a financial services professional, or reputable credit counseling agency, to create a financial plan to eliminate your debt.

Add up what you're paying each month to pay your credit card bills. Now imagine that you were investing that much into the market or into your savings. According to the article, if you were to save an extra $100 each month, or $1,200 a year, and invested it into a fund with an annual rate of return of 9% over 30 years - you could add $184,000 in income before taxes. What could you do with that extra money in retirement?

Avoiding interest charges will help you save even more money in the long run. It's a great way to improve your financial situation. You mentioned that in your experience debt can be a danger for many Americans. Let's dive a little further into that. Another resource that I want to utilize today is an article from TheBalance.com from December of 2018 entitled, "Reasons Debt Is Bad for You." It's common to say debt is bad, but let's take a moment a detail exactly why debt is a danger.

The first reason mentioned in the article from TheBalance.com is that debt creates the temptation to spend more than you can afford. Debt allows for the emotional high of getting new things or having new experiences without feeling the pain of parting with money immediately. It may even feel like you're getting something for nothing when, you're trading immediate gratification for a potentially higher payment down the road.

This ties in neatly with the second reason mentioned in the article is that debt does cost real money. That cost comes in the form of interest, the higher the interest rate, the more you'll end up paying. One exception would be a zero percent annual percentage rate promotion but often those have limits and qualifications and if you don't follow the rules, could potentially incur an even higher rate down the line.

That seems like a simple equation, but the article does a good job of offering a sample scenario. Let's say that you decide to get a new living room set for home. The total cost of this set is $2,000. You use a credit card with an annual percentage rate of 11% to pay for the living room set. As detailed in TheBalance.com article, if you make the minimum payments to pay off the living room set, you would end spending more than $3,400 for that living room set! High interest rates are another reason debt can be bad for you.

I do want to point out that debt isn't necessarily bad, it is simply something that is part of your financial picture. In order to make some of life's larger purchases, like a car, home, boat or some other large item, you will need a history of using debt correctly. In my opinion it isn't a question of avoid all debt but more a question of how to use debt correctly to manage your long-term financial health. This is absolutely something that I have worked with my clients to help them achieve and something that any financial services professional could do as well.

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