How to get out of credit card debt

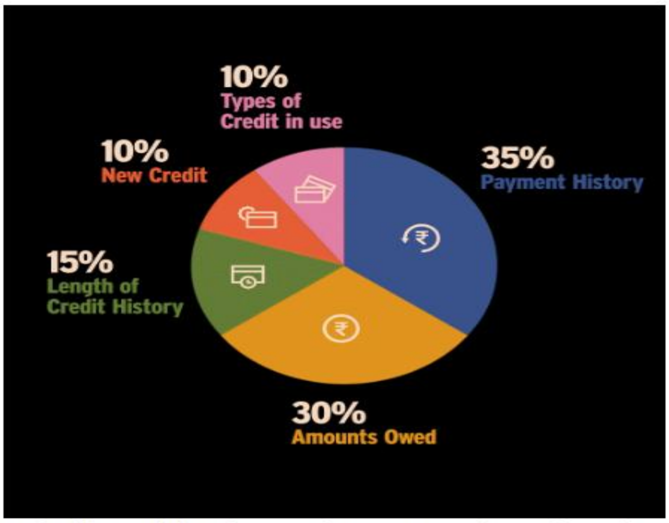
By Gouri Shah | The Established | 01 April, 2022

HOW TO PAY OFF THE LARGE OUTSTANDING ON YOUR CREDIT CARD AND BREATHE EASY

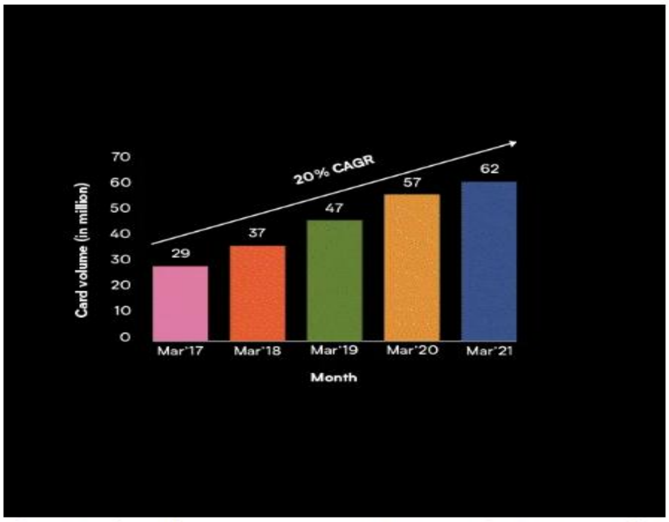
Credit cards, if used wisely, have a host of benefits. A beautiful, shiny carousel loaded with rewards—VIP lounge access, loyalty points, delicious buy-now-pay-later deals, discount coupons, among other things. According to a 2021 report by Pricewaterhouse Coopers India titled 'The Changing Landscape of India's Credit Industry', credit card issuance has grown significantly in India over the last four years.

Clocking in at a compound annual growth rate (CAGR) of 20 per cent, the total number of credit cardholders in India grew from 29 million in March 2017 to 62 million in March 2021. But the shine is wearing off quickly for consumers who are waking up to the pitfalls of owning a credit card. With high-interest rates at approximately 30-42 per cent per annum, all that unchecked spending, minimum payments on the outstanding balance and lack of financial discipline are pushing more people into the credit card debt trap.

Here's some expert-backed advice to help you get on top of your credit card debts.



Lack of financial discipline is pushing more people into the credit card debt trap. Image: Investopedia



If your credit card statements are going unopened, it's time to take stock. Image: Pricewaterhouse Cooper

ACCEPT THAT YOU HAVE A PROBLEM

Inspect your bank and credit card statements carefully for a clear idea of how much money you are bringing in each month after deductions and how much money you owe the credit card companies or banks. The ideal option is to pay your credit card bill in its entirety. If you can't, pay off as much as you can, cutting down on every other expense except the essentials. There are several ways to tighten that belt. The easier ones come in the form of substitution, like a walk on the beach instead of that fancy gym membership. The tougher ones could include selling assets or moving to a smaller home.

DO THE MATH

Not paying your credit card dues in its entirety costs you more than you can imagine. If you had ₹1,00,000 outstanding on your credit card and paid only the minimum amount due (about five per cent) each month, you would need approximately 50 years to pay off that credit card debt. Read that again. Over 50 years. This is presuming you didn't incur any new expenses along the way. "You would have also paid the credit card company over ₹1 lakh purely in interest by the time you hit year two on that payback from hell. About ₹4,00,000 purely in interest if you actually had the patience and discipline to see that through to the 50th year without another purchase on that card," says Vishal Dhawan, CEO and founder, Plan Ahead Wealth Advisors, a Mumbai-based SEBI licensed, registered investment advisory firm.

As tempting as it may be to make the minimum card payment and give into indulgences, it's just plain stupid. Instead, start putting away everything you can towards paying off your credit card debt. Experts advise liquidating other assets—unless they are emergency funds. "If there is any money back, endowment, or whole life policies, we recommend surrendering them and using that money to pay off the credit card loan. Most of these policies offer meagre returns, and the cash thus generated can be used to pay off costly credit card loans. We would recommend using funds in FDs, RDs, Debt mutual funds, Equity Mutual funds, and Direct Equity (in that order) to pay off the credit card loan," says Renu Maheshwari, a SEBI registered investment advisor and co-founder and principal advisor, Finscholarz.

"IF THERE IS ANY MONEY BACK, ENDOWMENT, OR WHOLE LIFE POLICIES, WE RECOMMEND SURRENDERING THEM AND USING THAT MONEY TO PAY OFF THE CREDIT CARD LOAN." Renu Maheshwari

JUMP SHIP

Consider transferring your entire outstanding balance to a lower interest credit card regardless of the perks you may lose out on. In a highly competitive market, banks and credit card companies are always trying to lure new customers with attractive interest rates and payment facilities. Use this to your advantage. Find out which cards offer a lower interest rate than your existing credit card and, two, a low balance transfer fee (charged to the customer transferring an outstanding balance from one card to another).

Certain banks may even offer you a few months at zero per cent interest, provided you meet their criteria. Everything you pay towards that credit card loan during that time is making a dent in the amount. So make sure you stay disciplined—using the interest-free period to buy more time is self-defeating, say experts, and will only spring another financial leak.

CONSOLIDATE YOUR DEBT

Juggling various debts across different cards? You may want to consolidate by opting for a personal loan to settle all the others. While an unsecured personal loan is not cheap and comes at 10-15 per cent per annum, it is half or even a third of what you are eventually paying your credit card company—at easily, a compounded interest rate of 40-45 per cent per annum. You will have one debt to keep track of with fixed outgoings towards it each month.

Moreover, the repayments each month are unchanged, and the debt is guaranteed to be gone by the end of the term. This also ensures that you don't slide back into the comfort of a minimum-payment mode, as the payment amount is fixed. The catch: your credit rating will determine how high or low the interest on your personal loan will be.

"IS YOUR SPENDING LINKED TO AN EMOTION? IS IT LONELINESS OR A NEED FOR ACCEPTANCE THAT LEADS YOU TO OVERSPEND ON GIFTS FOR OTHERS CONSTANTLY? RECOGNISING AND ACKNOWLEDGING THESE EMOTIONAL TRIGGERS COULD BE THE FIRST STEP IN THE RIGHT DIRECTION." Vishal Dhawan

THE SNOWBALL OR THE AVALANCHE

If your credit card statements are going unopened, and you're on a spending spree without worrying about the consequences, it's time to take stock. Make a list of how much money you owe each credit cardcompany or bank and the interest rate on each loan. There are two ways to approach this: The first method financial planners call—snowballing. You pick the lowest amount first, irrespective of the interest rate, and focus on paying that outstanding amount. You then move to a credit cardwith the next largest balance, and so on. The other option, known as the avalanche method, is to start with the most expensive loan—zero in on the card charging you the highest interest rate and attack that first.

"In our experience, the snowballing method is more successful than most other methods. It allows clients to celebrate small victories and motivates them to keep going," says Maheshwari, adding that, if it comes to prioritising among all your loans, throw every methodology out of the window and focus on closing the credit card loan first.

BRING IN THE TROOPS

Credit card companies have security measures in place to protect you against fraud. Use these measures to protect yourself... from yourself. Go over your credit card statements with a fine toothcomb to spot a pattern. If you have a weakness for online shopping or ordering in, try blocking your card for all online transactions. This will make you re-think each purchase for which you may need to trek to a physical store for.

Those cute boots at 60 per cent off? You may feel differently about them in the morning. If international websites have been luring you with delicious deals, block all overseas transactions. If you've been withdrawing cash on your credit card (the interest on this is high and immediate— no 50-day credit window here), block cash withdrawal on your card. "There is a need to do a brutal analysis of your spending patterns to get to the root of it all. Is your spending linked to an emotion? Is it loneliness or a need for acceptance that leads you to overspend on gifts for others constantly? Recognising and acknowledging these emotional triggers could be the first step in the right direction," advises Dhawan.

ASK FOR HELP

Speaking to a professional could help you steer yourself out of the deep debt end. "It's just like when you get sick. Your GP can handle it if it's just the flu or a minor ailment. If it's more serious, you need to consult a specialist," says Dhawan, who explains that if you have the means to pay off your debt and just lack the financial discipline to do it, then a personal finance expert could help you navigate your way out of it.

If you've exhausted all your options and have your back against the wall, try consulting a credit counsellor who could help you take stock of your situation, set up a plan for you and even add professional weight to your plea when you talk to your creditors or negotiate with the bank.

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