

Attack your debts

Your debts are at the frontline of your financial battlefield. Combat your debts and you will win the financial battle – ASIC Commissioner Jeffrey Lucy explains.

Even though ADF members have access to some great benefits such as Defence Force accommodation, chances are that like most of us, debt is part of many members' lives. Credit-card debt, mortgages and car loans are common examples. The high interest rates on debts like these can shoot holes in your savings plans, so I would encourage you to consider the following tips – you could save thousands in interest payments.

There are other advantages to paying off your debts faster. For example, if you are being deployed overseas it is vital to ensure your debt-repayment arrangements are in order before leaving. When on active duty, you don't want to be worrying about your personal finances at home.

Which debts to attack?

You should always pay at least the minimum amount due to every lender, on

time. If you can afford it, making payments over and above the minimum is an excellent strategy for clearing debts faster. Start with the loan charging the highest interest (most likely your credit card) to make the biggest difference.

You should only make extra payments into your lower-interest loans once the most expensive one has been paid off. The lowest-priority loan would most likely be one that has tax-deductible interest, for example, on an investment property.

If you are late with a loan repayment, you may incur penalty fees and/or affect your credit report.

More strategies

Another simple strategy to get ahead is to pay your debts fortnightly instead of monthly. In effect, you make the equivalent of 13 monthly payments a year instead of 12. This is especially easy to manage if

you are being paid fortnightly and you have a routine in place.

Taking advantage of fortnightly instead of monthly payments will cut four years off a 20-year home loan of \$200,000. And if you can pay an extra \$100 per fortnight, you will cut seven years off your loan!

If you have some extra money, for example from a bonus, you could also consider paying a large chunk off your debt (again, starting with the one charging the highest interest). Paying \$1000 off a credit card charging you 16 per cent interest obviously beats putting the same money into a term deposit paying you 5.5 per cent.

Your credit card issuer will require you to make a minimum repayment each month. This amount is generally only a fraction of your outstanding balance, often as low as 2.5 per cent or \$25 for every \$1000 owed.

Suppose you spend \$1000 on your credit card, and can only make the minimum repayments. Your first 2.5 per cent minimum payment (\$25) pays off about \$13 interest, and just \$12 comes off your debt. By only

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paying the minimum payment, it will take more than 11 years to pay off the \$1000, by which time, you will also pay about \$860 interest (assuming the interest rate stays at 16.5 per cent and you stop using the card).

As you can see, it makes sense to attack your credit-card debts with more than just the minimum payment, whenever you can.

Car-related debt

For many younger members of the ADF – like many young Australians – getting a car is a priority. If you don't have the money up front, you might decide to get a car loan. If you do, make sure you get the right loan as well as the right car, as you'll be living with your decision for some time.

Tips on choosing the right car loan:

- ▶ Work out what you can really afford. By using as much of your own money as possible, you cut back the amount you have to borrow.
- ▶ Shop around for finance before going to the car yard, armed with a budget and the right information.
- ▶ It's nearly always cheaper to get a loan from a bank, building society, credit union or specialist lending company than the car yard. Dealer finance may be convenient, but you might end up paying thousands more than you need to.
- ▶ Compare interest rates, fees and penalties imposed by different lenders.

Refinancing?

Some businesses may advertise offers to help you manage your debts. Refinancing your loans can be a useful strategy if you're having trouble meeting multiple loan repayments, but only if you are able to consolidate a number of high-interest loans into a loan with a lower interest rate. It can also help to break the cycle of spending on credit.

However, be careful about claims that refinancing will help you pay off your loans faster. You can only truly pay off loans faster by paying more money.

Only refinance if you know the savings will outweigh the costs in your personal situation and if you're sure you don't have a better option. Look out for fees and charges also. Check out FIDO's multi-loan calculator to make a comparison.

FIDO can help

ASIC's consumer and investor website, FIDO at www.fido.gov.au offers all sorts of help about debts and money. Ask FIDO whenever you're considering an important financial decision.

If you're struggling with your loan repayments and need help to work out your best option, you may find it helpful to speak to a free and independent financial counsellor. Ask FIDO for contact details of financial counsellors around Australia.

This column was provided by the ADF Financial Services Consumer Council. To suggest other subjects to be covered in this column, email ADFcolumn@asic.gov.au

