

Repaying Credit Debts and Loans

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“Money often costs too much.”

(Ralph Waldo Emerson, 1803-1882)

What is credit?

Credit is the ability to borrow money. Credit is an important part of the financial functioning of individuals, families, cities...and ultimately nations. Without credit, many people would not be able to purchase an automobile, unless they had the entire cost of the auto in cash.

What is credit debt?

Credit debt is the unpaid balance on auto loans, credit cards, student loans and any other non-mortgage debt. In 1970, Americans had \$5 billion in credit card debt. By 1995 total credit card debt equaled \$395 billion — an increase of almost 2,000 percent, after accounting for inflation. Over that same 25 year period median U.S. family income increased only 5 percent after accounting for inflation.

Counting all forms of credit debt, Americans have gone from \$131 billion in 1970 to just over \$1 trillion in 1995 — a 110 percent increase in 25 years, after accounting for inflation. This increase has far exceeded the very modest increase in real median family income.

Why is credit debt dangerous?

Excess borrowing creates high monthly payments, which can strain even a well-planned budget. As demonstrated by the national data above, the pace of borrowing can often exceed the growth in incomes, creating a form of “credit debt bondage”. The interest cost of credit debt can be very high, even 21 percent per year in some cases. For example, Jim has a \$1,200 credit card balance. The credit card has a 21 percent APR (annual percentage rate). If Jim makes a \$40 payment each month it will take 43 months (or 3.5 years) to repay the balance. Jim will end up paying \$520 in finance charges (i.e. interest) on the \$1,200 balance!

Individuals, families, cities, and nations which have high monthly payments going toward debt repayment often sacrifice financial goals, most notably saving and investing money. Moreover, budgets which are strained by high amounts of debt repayment are less able to deal with crises situations, such as unexpected repairs to a car or home, or medical emergencies.

How can credit debt bondage be eliminated?

There is no easy way out of excess credit debt. The most obvious solution

is to begin a debt repayment plan. If a person has sufficient income to meet all his/her monthly obligations, the task of repayment will simply take TIME.

There is no instant gratification when it comes to repaying debt

A vitally important ingredient is persistence. Prepare a monthly budget and stick to it! Stop spending money in frivolous ways. Take a lunch to work instead of eating out. Stay home and play games or work on hobbies instead of purchasing entertainment. Keep track of expenditures. Don't purchase big ticket items on the spur of the moment.

If a person does not have sufficient income to repay each month's bills, help will be needed. One form of help is Consumer Credit Counseling (CCC). There is a CCC office in most large cities and in many smaller cities (check your local phone directory under “Consumer Credit Counseling”). The job of CCC is to assist individuals in formulating a debt management plan. CCC will not repay bills for individuals, but they can help negotiate with creditors to accept lower monthly payments which allow the individual to balance his/her monthly budget.

Some people choose bankruptcy.

Bankruptcy should only be considered as a last resort. Bankruptcy has long term negative effects on an individual's credit rating.

How can a budget help to avoid or eliminate credit debt bondage?

A budget is a plan for spending money written down before the spending takes place. For example, the monthly budget for November would be

prepared at the end of October. November's income (if known in advance) is compared to November's estimated expenditures. Many people find it helpful to budget expenditures by category, such as rent or house payment, utilities, food, gasoline, debt payments, phone, etc. A budget worksheet is printed below. Feel free to make photocopies of it so that you can budget your income and record your expenditures each and every month. If you

don't keep track of expenditures as they occur it's easy to overspend. By budgeting income and recording expenditures each month you may be able to spend less. Money saved by careful budgeting can then be used to accelerate the repayment of debts, you will reduce your finance charges and save money! For more information on budgeting see MU publication [GH 3830, Managing Your Money.](#)

Budget Worksheet for the Month of _____					
	<u>Source 1</u>	<u>Source 2</u>	<u>Total Income</u>	<u>Expenses</u>	<u>Surplus or (Deficit)</u>
Income: \$ _____	+ _____	= _____	- _____	= _____	_____
<u>CATEGORY:</u>	<u>PLANNED:</u>	<u>ACTUAL:</u>	<u>DIFFERENCE</u>		
Mortgage/Rent	_____	_____			
Utilities	_____	_____			
Phone	_____	_____			
Food	_____	_____			
Clothing	_____	_____			
Gas	_____	_____			
Car	_____	_____			
Insurance	_____	_____			
Debt	_____	_____			
Medical	_____	_____			
Educational	_____	_____			
Recreation/Misc.	_____	_____			
Gifts/Donations	_____	_____			
Investments	_____	_____			
Savings	_____	_____		_____	
TOTAL EXPENSES:	_____	_____	_____	_____	_____



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