How to take control of your debts

Source: AMP Life

How you manage and in what order you tackle your debts may make a big difference to what you pay in the long run.

Managing debts

The money people owe, in comparison to the money they earn has almost tripled in Australia over the last three decades, with the average household debt currently sitting at around $245,000.

If it's something you can relate to (you might have a mortgage, car loan or money owing on your credit card), the good news is debt can have its advantages, but this will generally only be the case if you manage debt properly and prepare for unforeseen events that may leave you vulnerable.

Is debt a bad thing?

All debt costs money (and obviously needs to be repaid) but what separates good debt from bad debt is the ability for that debt to help you build wealth over time.

For instance, debt could be viewed favourably when used to invest in an asset, such as property or shares, which may generate an income and grow in value.

Examples of a bad debt might include money you borrow to pay for day-to-day expenses, or things like an overseas holiday or expensive pair of shoes.

If you're interested to know how the rest of the population fares, more than 90% of household debt is spent building wealth and buying a home to live in, rather than purchasing consumable items.

9 ways to manage your debts

Whether it's a credit card, personal loan, student tuition, car finance or home loan you're paying off, there are many ways you can pay off your debts sooner.

1. Work out the debts you have and what they total

A good starting point is to make a list of how much you owe and to which organisations, including the fees and interest you're paying. It might sound unpleasant, but it's important to get a realistic view of exactly how much you have to pay back and how different interest rates can affect that amount.

2. Compare what you earn, owe and spend

Jot down into three categories - money coming in, how much cash is required for the essentials and how much dough (if any) you've got left over. This will help you identify where there may be room for movement and where you could extract a little bit extra here and there to add to your repayments.

3. Consider rolling your debts into one

Multiple debts can mean multiple fees and interest charges, which is why consolidating debts into a single loan with a lower interest rate may save you a lot of money, depending on what you owe.

A consolidated loan may also be easier to manage, as you'll potentially only need to make one regular repayment rather than having to juggle several. However, do ensure your lender is licenced by ASIC and that interest rates, fees and any additional charges aren't going to see you paying more money.

Also, keep in mind, debt consolidation will only be effective if you're disciplined about making your repayments.

4. Pay your debts on time

Setting up alerts or paying by direct debit can help ensure your repayments are paid on time, so you can avoid paying late fees and added interest charges.

Remember, late payments may also affect your credit report, which includes your personal details, the types of credit you've applied for and details about your repayment history, which may be kept for different lengths of time.

As credit providers use this information to assess whether they want to lend to you, keep in mind if you're history isn't good, you may have problems getting approval on a loan later on.

5. Try to pay the full rather than minimum amount owing

When dealing with debts, such as your credit card debt, it might be tempting to only pay the minimum amount owing, but remember you're still incurring interest on the balance that's leftover. If you're able to pay the full amount, typically you won't be charged any interest at all.

6. Look at whether you can afford to make extra repayments

Making extra repayments can help you pay off what you owe faster and generally you'll pay less interest. Depending on what you owe, this could mean thousands of dollars in savings, but always look at the conditions of the loan as some lenders might charge you for paying off the debt early.

7. Shop around for a better deal

High interest rates and added fees can really impact what you pay back on top of the principal amount. So, if you've got a loan or credit card, see if another provider can offer you a better deal.

If you're hesitant that'll make a difference, research shows a typical household could save over $1,000 on their electricity bill every year just by switching from the highest priced plan to the most competitive on the market.

8. Have a contingency plan

It always helps to factor in the impact of potential interest rate rises and to have a contingency plan around things, such as changes in employment, or if an unforeseen health event could prevent you from working.

9. Know you can reach out

If you're finding it hard to keep up with your repayments, do call your providers as soon as you can and tell them you're experiencing financial hardship.