Understanding **debt** and how to **manage** it

To manage your finances, you need knowledge of how to budget, save, spend wisely and grow money through investing. But this process is underpinned by understanding and managing your debt. With the rise in interest rates in 2023 and 2024 many South Africans are over-indebted and struggling to make ends meet. With the right information and tools you, as a member, can learn how to save more and spend less on your journey towards financial independence.

What is debt?

You are "indebted" to somebody if you have borrowed money from them with the intention of repaying them, whether it was from family, friends, or a financial institution. This is called debt. **Debt is never free money. You'll often be charged interest on the loan by financial institutions.**

When borrowing money through a personal loan, it's crucial to carefully examine the interest rate being charged. Many people are unaware that they can negotiate a better interest rate with their lender, particularly if they have a strong credit score and creditworthiness.

What is the difference between good and bad debt?

Good debt:

When we borrow money, some of these debts could be seen as investments. The reason for this is the hope that one day we will receive an increase in value or income generation. Good debt can change your life for the better. We all need good debt at some point in our lives, for example when we want to buy our first home or take out a student loan. ***Good debt is needed but cannot always be paid for in cash. Examples of good debt include:***

- A car you can afford (It will help with travel to work, shop around for best interest rate)
- Studying to further your career opportunities
- Student loans
- Housing loan/ bond

Bad debt:

When we borrow money to pay for things that are not essential needs in our lives, like paying for a holiday on our credit card, we are spending money that we do not have, which is seen as bad debt. ***Bad debt usually has a higher interest rate, such as credit card debt. Examples of bad debt:***

- Luxury car you can't afford
- A luxury holiday you can't afford
- Borrowing money to pay existing bills
- Taking out multiple clothing accounts / store cards

If you're looking for a better way to manage your debt, with a goal of eliminating most or all of it, you have already taken a step in the right direction. As you prepare to move forward, remember too much debt, or the wrong kinds, such as high-interest credit card debt, can hamper your ability to pursue other financial goals.

Seven Steps for more effective management of your debt

1. Take stock of all your accounts

First things first: Make a list of all your outstanding debts. Include the interest rate on each so you'll be able to determine which ones are causing you the most financial pain.

2. Check your credit report

Request a **free copy of your credit report** from one or more of the three credit-reporting agencies. This will help you make sure you haven't forgotten about an outstanding debt. Plus, it's always a good idea to make sure there aren't accounts on there you don't recognize. If you want to find out your credit score, check with your bank or credit card company to see if they can provide you with your score at no cost.

3. Look for opportunities to consolidate

If you have multiple high-interest loans, can you consolidate them into one loan with a lower interest rate? Do you have access to a low-interest personal loan that you could take out to pay off high-interest credit card balances?

4. Be honest about your spending

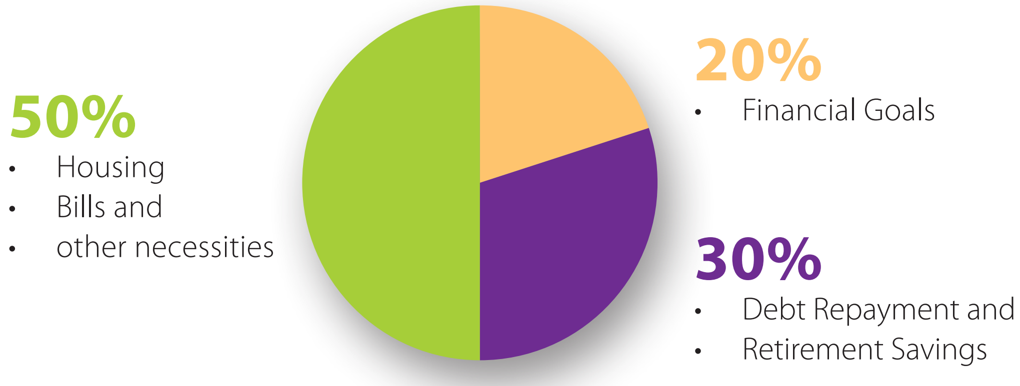
If your debt feels overwhelming, it's worth taking an honest look at what you're spending each month. Are there expenses you can cut back on or eliminate? Part of reducing your debt is limiting the additional debt you take on.

5. Determine how much you have to pay

Determine how much you have to pay each month by noting the minimum payments and adding these amounts to your budget. If the amount is more than you can manage in your budget, you may need to contact lenders to see about arranging different terms. ***Building a budget isn't about limiting yourself to only spending money on essentials. Instead, it's about allocating your money in the way that makes sense for you.*** Think about your financial priorities and goals, as well as what makes you happy. Once you see how much you're spending on certain things, you might want to try adjusting your spending habits to increase your savings.

6. Figure out how much extra you can budget

Once you have the baseline of how much you have to pay each month in your budget, determine how much extra from your budget you can devote to debt reduction. **Creating a budget can be daunting, but the 50/30/20 rule is a straightforward and effective method for allocating your income:**



7. Determine your debt-reduction strategy

How you attack your debt is up to you. The two most popular strategies are to pay off balances with the highest interest rates first or to pay off the lowest balances first. The former will save you more money over the long run, but the latter can help you keep momentum and see progress. ***Either way, you're taking steps in the right direction, so stick with your plan!***

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Please also consider the following to reduce debt:

- ***Don't avoid calls from your creditors.*** Deal with this problem head on and make a payment plan to pay them. Even if it's a small amount.
- ***Try to pay more*** than the minimum amount due.
- ***Create a payment plan*** and set a payment goal and stick to it.
- ***Track all spending*** to find areas to cut.
- ***Prioritise paying off*** debt in your budget.
- ***Try negotiating better interest rates with your current credit providers.*** When you must take out debt always compare interest rates at the various institutions to ensure you get the best deal. The higher the interest rate the more expensive the loan.
- ***Don't always say yes to debt*** when it is offered to you.
- ***Take all retail credit cards out of your wallet*** so you are not tempted to use them for future purchases.
- ***Check your credit score at least once a year.*** This helps you understand your financial position and improve it.
- ***Don't miss monthly payments***. This impacts negatively on your credit score.
- ***If overwhelmed, talk to a registered debt counsellor***; they can help you restructure your debt legally.
- ***Avoid new debt:*** Say no to store/retail cards or unnecessary credit.