How to Ditch that Holiday Debt

By Shelly Gigante

It was another joyful holiday season and your gifts to friends and family did not disappoint. Sure, you went a bit over budget, but you did elicit some memorable “wows.” Now, as you set your sights on a happy and halcyon 2017, you must first settle up/make peace with the credit card companies that bankrolled your generosity.

Indeed, the “holiday hangover” is all too real for gift givers who overindulged in the month of December, making the first few months of the year (or longer) an unwelcome exercise in the art of juggling debt.

“It’s fun to give gifts and very easy to put it all on a credit card,” said Erika Safran, a financial professional with Safran Wealth Advisors in New York, noting it’s tough keep track of your spending when you pay with plastic. “The holidays give them more of a license. They may feel justified because they are buying for someone else.”

Shoppers around the country were planning to spend an average of $752 for gifts for the 2016 holiday season, down from $830 in 2015, according to a recent Gallup poll.[1] But actual spending can be far more excessive, depending on one’s income, financial discipline and expenses. It costs money, after all, to host holiday parties, purchase new clothes for year-end social events, and travel to see friends and family.

If you count yourself among the many that spent beyond their means, you’ll need a plan of attack to dig out – and stay out – of debt.

Put a Dent in Your Debt
First, said John Gajkowski, co-founder of Money Managers Financial Group in Oak Brook, Illinois, stop using your credit cards. You’ll never pay down your balance if you keep running up the bill.

Next, assess the damage.

“Gather the troops to make sure you have a complete picture of just how bad your holiday hangover is,” said Gajkowski. “Usually, the husband has a few cards and the wife has some, too.”

Keep in mind it may not be too late to mitigate the effects of your (well-intentioned) spending spree by returning duplicate gifts, sweaters that didn’t fit, and surplus gifts that never got wrapped.

Many consumers, especially those who impulse-buy, purchase two or three things for friends or family with the intention of taking some of it back. But six months later it’s still sitting in the bag by their back door.

“Return the gifts you didn’t use,” said Safran. “Don’t let them sit around forever.”

Once you know what you owe, make a list of all your unpaid balances, and prioritize them according to their interest rate fees. Make minimum monthly payments on all your cards, said Gajkowski, while applying any extra money to knocking out the credit card balance with the highest interest first. Once that’s paid off, move to the card with the second highest rate, and so on, until you bring your balances to zero. (Related: Credit Card Debt Problems and Fixes)

“Paying the highest interest rate card off first is just cheaper,” said Gajkowski, because it minimizes the cost of the money you borrowed.

There is a caveat: If “stick-to-itivness” isn’t exactly your strong suit, you might instead consider a strategy of paying off the credit cards with the smallest balances first, which may deliver the psychological boost (sense of success) you need to stay the course in the difficult months ahead.

Depending on your debt level, you may also wish to explore transferring your balances to a single, lower interest credit card that may offer low or even zero percent interest for up to two years, said Gajkowski. The lower interest rate may help you pay what you owe faster and avoid defaulting on your credit card bills, which can seriously damage your credit score.

Be forewarned, however, that balance transfers are not well-suited to everyone, he said. Generally speaking, your credit rating must be good to excellent to qualify. You may also be subject to a balance transfer fee of 3 percent to 5 percent.

“If you haven’t paid your balance off by the time the (teaser) rate ends, your payments can be very costly,” he said. “Balance transfers are not a bad idea if it’s one and done, but if this is a habitual problem and you are transferring balances back and forth it really can screw up your credit. Borrowers need to look at the fine print." (Related: New Credit Cards and Your Score)

Homeowners who do not qualify for a balance transfer may also consider consolidating their high-interest debt to a home equity line of credit (HELOC), which typically also offers a favorable interest rate, said Safran. The interest you do pay may be tax deductible in some circumstances.

But there's a downside to everything. HELOCs can be pricey to set up, and many offer a variable rate, so be prepared for your monthly payment to change over time. The biggest drawback to using a HELOC, however, is that the loan is secured against the equity in your home. Failure to pay means you could lose your house.

A financial professional can help you determine whether a HELOC makes sense for you.

Boost Your Income, Trim Expenses

You will pay off your credit cards faster, of course, if you can manage to boost your income. Contractors and freelancers may be able to take on an extra gig, while others may be privy to a year-end bonus they can apply to their debt.

Those with a fixed salary, however, will need to be more creative to free up cash flow, an exercise that will serve them well going forward.

Borrowers in repayment mode should resist the temptation to halt contributions to their workplace 401(k) or kid's 529 college savings plan, said Safran. And, except in the most dire circumstances, do not borrow from your nest egg to pay off short term debt unless. Focus instead on opportunities to trim waste from your budget and eliminate unnecessary expenses — like unused gym memberships, premium cell phone plans, vacations that involve travel, and dinners out.

"If you cut one dinner and a movie out of your budget every week for a year, you would have saved about $5,000 right there," said Safran. "In January and February at least, make the decision to stay home and enjoy your family, remembering that you spent a lot in December."

Even a little extra money applied to your credit card bill each month can save you a bundle. It would take 153 months (nearly 13 years) and cost you $1,673 in total interest, for example, if you made only the minimum monthly payment of $37.50 on a $1,500 balance at 18 percent interest, said Safran. By boosting your payments to $140 per month instead, you would pay off that credit card in one year, and cost you $148 in interest.

Debt Free At Last

Once you’ve brought your credit card balances back to zero, that extra jingle in your pocket can be redirected to other financial goals – like a down payment on a home or building your nest egg. It can even be used to finance a bucket list vacation, so long as you save the money ahead of your trip.
Indeed, financial goal-setting and a commitment to keeping your spending in check are the keys to creating a sustainable budget – a particular challenge for many consumers, especially during the holiday season.

According to an October 2016 survey by market research firm The NPD Group in Port Washington, New York, 16 percent of consumers said they planned to pare their spending ahead of the 2015 holiday shopping season, but more than 20 percent later disclosed they had actually.[2]

The widespread use of credit cards, which are painfully easy to use at the check-out counter (or online), may also contribute to overspending. Thus, many financial professionals suggest those who struggle with debt adopt a policy of paying with cash for discretionary expenses.

By setting a budget, lowering your expenses and keeping your future spending in check, you will be far better equipped to stay debt free during the holidays and beyond.

“Use this as a lesson learned,” said Safran, noting binge borrowers may want to try paying for everything with cash since it’s harder to part with. “Never put anything on a credit card that you can’t pay off in 12 months or less. If you don’t have a plan to pay it off in that time frame, you probably can’t afford it.”