Using the "Debt Snowball" Method to Pay Off Debt

Objective

To reduce and eventually pay off debt using the Debt Snowball method.

What to Know

You might wonder if you will ever pay off your debt. Maybe you have tried to pay off debt in the past, but you found yourself back to square one – or in even greater debt!

The Debt Snowball method, successfully used by many people, can keep you focused. This debt repayment technique was originally made popular by personal finance expert Dave Ramsey, and it involves paying off your smallest debt balances first while making minimum payments on all your other debts. You will devote any extra money each month to paying off the smallest debt first. Remember, you make only minimum monthly payments on the other debts. When the smallest debt balance is settled, you move on to the next smallest.

This method can be used with just about any type of debt except mortgage loans. When you pay off smaller balances, you get a motivational boost through "quick wins," encouraging you to stay disciplined and keep going with debt repayment.

What to Do

1. Review your spending plan and budget enough to cover the minimum monthly payment for every debt.

2. Gather your credit card or loan statements and any other debt balance information. Arrange the debts by balance, from smallest total payoff balance to largest. Disregard interest rates unless two debts have a similar payoff balance. In that case, list the one with the highest interest rate first. Use another piece of paper if you run out of space.

3. Every month, put the extra money you budgeted for getting rid of debt toward your smallest debt. Once the smallest debt is paid off, take the entire amount you were paying toward that debt (monthly minimum payment plus any extra money) and target the next-smallest debt.

4. Every time you pay off a debt, cross it off the list.

Debt	Total Payoff	Minimum Payment	New Payment*
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*Once a debt is paid off, take what you were paying on that one and add it to the minimum payment of the *next* debt. As the snowball rolls over, it picks up more snow!

Here is an example. You have a hospital bill for $1,500, and you are paying monthly interest-free payments. You have two credit cards with balances of $3,000 (at 23.9% interest) and $5,000 (at 14.9%). Pay the hospital bill first. At first you might think this does not make sense, because it saves you money to pay off debts with high interest rates first! But if you (like many people) require early victories to stick with debt repayment, the Debt Snowball method is for you.

If you choose the Debt Snowball method and your higher-interest debts also have the largest balances, watch for opportunities to get lower interest rates (especially if your credit score is increasing as you pay off debt). Perhaps you can transfer your credit card balances to a lower-rate card or get a debt consolidation loan.

Reflections on This Exercise

What was the most difficult part of this activity? Why?

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What other strategies have you used (or are currently using) to pay off debt? Have they been effective? Why or why not?

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How helpful was this exercise? _____
(1 = not very helpful, 5 = moderately helpful, 10 = extremely helpful)

What did you learn from this exercise?
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