The Truth About Debt Consolidation

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Myth: Debt consolidation saves interest, and you have one smaller payment.
Truth: Debt consolidation is dangerous because you treat only the symptom.

Debt consolidation is nothing more than a "con" because you think you've done something about the debt problem. The debt is still there, as are the habits that caused it – you just moved it! You can't borrow your way out of debt. You can't get out of a hole by digging out the bottom. True debt help is not quick or easy.

Larry Burkett, noted financial author, says debt is not the problem; it is the symptom. I feel debt is the symptom of overspending and undersaving. Our financial coaches will not recommend debt consolidation for a client. Why? Because debt consolidation doesn't work.

Debt Consolidation Statistics

A friend of mine works for a debt consolidation firm whose internal statistics estimate that 78% of the time, after someone consolidates his credit card debt, the debt grows back. Why? He still doesn't have a game plan to either pay cash or not buy at all. He also hasn't saved for "unexpected events" which will also become debt.

Debt consolidation seems appealing because there is a lower interest rate on some of the debt and a lower payment. However, in almost every case we review, we find that the lower payment exists not because the rate is actually lower but because the term is extended. If you stay in debt longer, you get a lower payment, but **if you stay in debt longer, you pay the lender more**, which is why they are in the debt consolidation business.

Debt Consolidation Example

For example, let's say you have $30,000 in unsecured debt, including a two-year loan for $10,000 at 12%, and a four-year loan for $20,000 at 10%. Your monthly payment on the $10,000 loan is $517 and $583 on the $20,000 loan, for a total payment of $1,100 per month. The debt consolidation company tells you they have been able to lower your payment to $640 per month and your interest rate to 9% by negotiating with your creditors and rolling the loans together into one. Sounds great, doesn't it? Who wouldn't want to pay $460 less per month in payments?

But they don't tell you that it will now take you six years to pay off the loan. This may not sound that bad to you at first unless you realize how much more you will actually pay in additional payments. You will now pay $46,080 to pay off the new loan vs. $40,392 for the original loans, even with the lower interest rate of 9%. This means you paid $5,688 more for the "lower payment." Not such a good deal after all. This example shows you why they are in the business – because **they make money off of you.**

The Real Way to Get Out of Debt

The answer is not the interest rate; **the answer is a Total Money Makeover**. The way you get out of debt is by changing your habits. You need to commit to getting on a written game plan and sticking to it. Get an extra job and start paying off the debt. Live on less than you make. It is not rocket science, but it is emotional, which is why most people need help getting through it from someone like Dave Ramsey. Don't try debt consolidation!

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