

Module 2: Debt Elimination Strategies

Financial Freedom Blueprint

Lesson 2.1: Debt Snowball vs. Avalanche Methods

Two proven methods to pay off debt. Both work—choose based on your personality and what keeps you motivated.

The Debt Snowball Method:

How it works: Pay minimums on all debts. Put extra money toward the smallest balance first. After paying it off, roll that payment into the next smallest debt (creating "snowball" effect).

Psychological advantage: Quick wins keep you motivated. Small debts disappear fast, building momentum.

Example:

- Credit Card A: \$500 (minimum \$25) — pay \$200/month

- Credit Card B: \$2,000 (minimum \$50) — pay \$50/month
- Car Loan: \$8,000 (minimum \$150) — pay \$150/month
- Student Loan: \$15,000 (minimum \$200) — pay \$200/month

After Card A is paid off, roll the \$200 into Card B (\$50 minimum + \$200 = \$250/month). After Card B, roll \$250 into car loan. The payment grows as debts disappear.

The Debt Avalanche Method:

How it works: Pay minimums on all debts. Put extra money toward the highest interest rate first. After paying it off, move to the next highest rate.

Mathematical advantage: Saves the most money on interest. Mathematically optimal approach.

Example: Same debts, but order by interest rate (highest first):

- Credit Card A: 24% APR — pay extra here first

- Credit Card B: 18% APR

- Car Loan: 7% APR

- Student Loan: 5% APR

Which to choose?

- Snowball: If you need motivation and quick wins
- Avalanche: If you're motivated by math and saving money
- Hybrid: Start with smallest (snowball), switch to highest interest once momentum builds

The best method is the one you'll stick with. Both get you to debt-free—the path just differs.

Lesson 2.2: Negotiating with Creditors Effectively

Creditors would rather negotiate than send accounts to collections. You have more power than you think.

When to Negotiate:

- You're behind on payments or about to be
- Financial hardship (job loss, medical issues, divorce)
- Credit card interest rates are crushing you
- Medical bills you can't afford
- You want to settle for less than owed

What You Can Negotiate:

Interest Rate Reduction:

- Call and ask for a lower rate (especially if you've been a good customer)

- Mention you've received offers from competitors
- Be polite but firm: "I want to pay this off, but the rate makes it impossible. Can you lower it to X%?"
- Success rate: 50-70% if you've made on-time payments for 6+ months

Payment Plan:

- Ask to spread payments over 12-24 months at lower interest
- Many creditors offer hardship programs with reduced rates
- Get everything in writing before making payments

Settlement (Pay Less Than Owed):

- Offer 30-50% of balance as lump sum settlement
- Best for accounts already in collections

- Request "pay for delete" to remove from credit report

- Get written confirmation BEFORE paying

Fee Waivers:

- Late fees (especially first-time)
- Annual fees on credit cards
- Overdraft fees at banks
- Simply asking works 50%+ of the time

The Negotiation Script:

1. "Hi, I'm calling about my account [number]. I'm committed to paying this off, but I'm struggling with [specific issue]."
2. "Can you help me find a solution? I'd like to [specific request: lower rate / payment plan / settle]."

3. If first rep says no: "I understand. Can you transfer me to a supervisor or someone who can approve this?"

4. Be polite throughout—aggression backfires

5. Get any agreement in writing before paying

Lesson 2.3: Consolidation Strategies That Work

Debt consolidation combines multiple debts into one payment. Helpful in some cases, harmful in others.

When Consolidation Makes Sense:

- You have high-interest credit card debt
- You can qualify for a lower rate
- You're committed to not accumulating new debt

- Simplifying payments would help you stay organized
- You have steady income to pay off the consolidation loan

When to Avoid Consolidation:

- You haven't addressed why you accumulated the debt
- The new loan has fees that negate savings
- You're extending payments longer (paying more total interest)
- You might be tempted to run up credit cards again

Consolidation Options:

Balance Transfer Credit Card:

- 0% APR for 12-21 months

- Transfer high-interest cards to this
- Pay off before promotional period ends
- Transfer fee: 3-5% of balance
- Best for: \$5,000-\$15,000 in credit card debt

Personal Loan:

- Fixed rate (usually 6-36% based on credit)
- Fixed monthly payment for 2-7 years
- No collateral required
- Best for: \$10,000-\$50,000 across multiple debts

Home Equity Loan / HELOC:

- Lower rates (uses house as collateral)
- Tax-deductible interest (consult accountant)
- Risk: Could lose your home if you can't pay
- Best for: Homeowners with significant equity

401(k) Loan:

- Borrow from your own retirement
- Pay interest to yourself (not the bank)
- Risk: Lost growth, plus must repay if you leave job
- Generally not recommended unless desperate

Lesson 2.4: Avoiding Debt Traps and Lifestyle Inflation

Getting out of debt is only half the battle. Staying out requires changing patterns that created the debt.

The Lifestyle Inflation Trap:

Every time income increases, spending increases to match. This prevents wealth building no matter how much you earn.

The Fix: When income increases, immediately allocate the raise to:

- 50% to savings/investments
- 30% to lifestyle improvement
- 20% to debt payoff or goal acceleration

Example: \$500/month raise → \$250 to investments, \$150 to lifestyle, \$100 to debt. You still get a life upgrade, but you're building wealth.

Common Debt Traps:

"Buy Now, Pay Later" Services:

- Afterpay, Klarna, Affirm, etc.
- Seem convenient but hide fees and encourage overspending
- Can lead to multiple overlapping payments
- Better to save and pay cash, or use credit card with rewards

Car Payment Upgrades:

- Every few years, trading up to a more expensive car
- A \$500/month car payment for 5 years = \$30,000
- Drive reliable used cars, invest the difference
- Rule: Total car value shouldn't exceed 35% of annual income

House Poor:

- Spending 30%+ of income on housing
- Leaves little for savings, emergencies, or enjoyment
- Better: 25% or less on housing, even if it means smaller space

Credit Card Rewards Trap:

- "I'm earning points/miles, so it's okay to spend more"
- 2% rewards on \$10,000 extra spending = \$200 back
- But you spent \$10,000 you shouldn't have
- Use rewards cards for purchases you'd make anyway, then pay in full

Building Debt-Proof Habits:

- Wait 24 hours before any non-essential purchase over \$100
- Use cash for categories you overspend (grocery, entertainment)
- Unsubscribe from marketing emails and unfollow shopping accounts
- Delete shopping apps from your phone
- Track net worth monthly—if it's not growing, adjust
- Celebrate debt payoff milestones (each paid account is progress)

The Ultimate Goal: Transition from paying interest to earning interest. Once debt-free, redirect those payments to investments. Your money starts working for you instead of against you.