Chapter 3

The Temptation Into Debts

"I don't know if I want them to come over to the house. Should we just meet them at a restaurant?" – Love your Life Not Theirs by Rachel Cruze.

That is the question Rose asked her husband, Peter, after they had made plans to have dinner with a couple that they knew. She was hesitant and worried because they barely had any furniture in their house. Therefore, she did not feel very comfortable. As a newly married couple, they had little money to furnish their new home.

Rose had done some furniture window shopping and she was surprised how expensive furniture was. Ideally, Rose wanted to acquire nice furniture and not just cheap stuff that they would have to replace in a year or so. Their house was nearly empty and the thought of having someone over for dinner was quite disturbing for Rose. She became so worried about it. A number of their neighbours and family friends were more established and had beautiful homes that were full of furniture, beautiful décor and kitchen appliances among others.

When the guests arrived for dinner, Rose started explaining to them why they didn't have a lot of stuff. However, the guests kept smiling and re-assuring her that it was fine. Apparently, they did not seem to care as they just wanted to hang out with them. When the guests left that night, Rose was still embarrassed and for the first time, she understood why people go into debts. She had started suddenly thinking how easy it could have been for her just to walk into a furniture shop, open up a credit account and get all the furniture and décor that she wanted!

Quoted from the book *"Love your Life Not Theirs"* by Rachel Cruze, the above story resonates with most of us on how we got into debts. Personally I'm a victim. Lured by a friend and the urge to make extra money in business, I used my payslip to borrow KES 1.2 million (USD 12,000) and KES 4.2 million (USD 42,000) to finance supply of building construction materials and import of merchandise from China for sale respectively. As a busy corporate executive and with no idea how these businesses are run, you can guess what happened – I lost all the money and had to pay the loan to the banks besides getting into the Credit Reference Bureau (CRB) listing for years. I also estimate another (confidential) loss of about KES 8.5 million (USD 85,000) to debts. A total loss of KES 13.9 million (USD 139,000) due to debts is massive! The question that you may need to ask yourself is how much money have you lost into debts singly, as a couple or as a family?

The Path to Accumulation of Debts

The path to accumulation of debts begins in earnest upon taking higher education loans for children in colleges or universities. This is either a cultural practice in some societies or the result of lack of savings for higher education for children. In some cases, students are able to access education loans, for example from the Higher Education Loans Board (HELB) in Kenya and in other cases, parents may acquire education loans for their children deliberately to educate them in certain schools. In other instances, the student may acquire a loan to cover part of the education cost while parents acquire an additional loan to cover the difference. In some countries, students are able to take an educational loan using credit cards.

The idea behind taking the education loan is that the student will get a job after completing education and be able to pay off the loan as soon as they start getting employment income. The danger with this thinking is that, debts incurred today have already accrued interest that will be payable in future. The effect is that this will basically erode the income of the student if they will be lucky to get the job in the first place. The other risk with student loans, especially the use of credit cards, is the accumulation of debts through unnecessary expenditure coupled with the new found college freedom. In this case, students tend to spend on credit on items like expensive meals, weekend parties, new clothes, trips (*safari*) and many other unnecessary expenses whose effect is the accumulation of huge debts that will need to be paid in future.

The next debt trap comes in with employment, for those who are lucky to get a job after graduation. Enticed with the readily available credit, you just need to produce a payslip and a few other simple requirements like identity card details to get a car loan. Therefore, you just pay for a brand new car that fits in with your new status. I have already mentioned that I was a victim of this car loan mistake. Anyway, back to your story. Now you have two loans to start payments with your new employment income - the higher education loan and car loan.

The third debt trap comes with a loved one, your spouse. Your friends and family members encourage you both to formalize your marriage through a wedding. Because you have not saved enough money, you and your spouse agree to take a wedding loan. Then you both move to a spacious rental house to start your married life and family. Your friends and family further influence you to own your own roof that you have been contemplating and finally you decide to take a house mortgage. Soon thereafter you also take a loan facility to finance the purchase of furniture and décor of your new home.

Soon you realize that you have too many debts and almost both your salaries are going to pay the accumulated debts (higher education loan, car loan, home mortgage and furniture and décor loan) and you barely have enough left to meet your other pressing needs. To meet these needs, you and your spouse get into a debt lifestyle where you both start borrowing from shylocks, friends and family. At this time, you cannot even qualify for more debts from the bank and some of the money you are now borrowing is being used to pay the earlier debts. Things become very serious. You are in a deep hole of debt and are suffocating from increased cost of living coupled with debts!

Why People Get into Debts

Honestly, why do people get into debts? Rose's story above speaks to us and for many of us who got ourselves into debts. Given, you are not immune if you are contemplating getting into debt – that urge is extremely enticing! Most people do not set out to get into huge amounts of debts intentionally, no. It's a snowballing phenomenon, where you start by taking one debt here, then take another debt over there and just passively taking on more and more debts so as to satisfy your immediate wants without realising what you are getting into in the process. Only to find yourself in a big hole of debts! Anyone can fall into the debt trap and we will see how to deal with that later.

Appreciating why people get into debts is the first step to help you in coming out of it and not get into it carelessly. The following are some of the main reasons people get into debts:

Debt paradigm

People have a tendency to believe that debt is something good that can help them succeed in life faster. With this in mind, they justify their decision to go into debts.

Social influence and elevated lifestyles

People worry more about their social circles and how they are perceived by their neighbours, friends and even family members. This drives them on how they spend their money. Eventually they are likely to incur debts in order to maintain a false perception of their financial situation. In Rose's story, she worried so much about guests visiting their empty house to the point of considering taking debts to buy household furniture and décor. This is not a good move but people do it anyway.

Spending money without a plan or a budget

One of the major money mistakes people make is to spend money without a budget or plan for it. Without a budget, it is not possible to track your expenses and understand where your hard earned money goes to. With a budget however, it is easy to see where your money goes, be able to cut down unnecessary expenses and avoid getting into a trap of debts.

Lack of self-control

Some people just lack self-control and discipline with their spending. They therefore, end up spending more than their income. How do they do that? By borrowing to meet the gap. That means they spend what they do not have. It is often said that doing well with money has a lot to do with how you behave when you have it. Behaviour is difficult to teach and a "genius who loses the control of their emotions can be a financial disaster", (Morgan Housel in, *Psychology of Money*).

Lack of adequate income

Sometimes people do not have adequate income even to meet necessities due to the nature of their sources of income. Therefore, they borrow to simply survive and provide for their families.

Reduced income

In some circumstances, income or profits may reduce. This leads to expenses exceeding income and people usually borrow to make up the gap. For example, during the Covid-19 phenomenon, most people got half of their monthly salary while others lost the jobs and entire incomes. It is sensible to reduce expenses when income reduces and avoid incurring unnecessary debt to support an unsustainable lifestyle.

Limited savings

Lack of savings for emergency and other financial goals will easily lead one to borrowing in order to meet the pressing needs. Therefore, some people go into debts to finance things like car break down, cooking gas, illness or sickness in the family, as well as, things like holidays and Christmas celebrations, instead of saving over time to build an emergency fund that can take care of these urgent needs when they arrive.

Financing a business venture

With a viable business, the owner can seek a business loan from banks in order to raise additional capital to expand the business. In that case, the banks will evaluate the business to ensure that it is profitable and that it will be able to pay back the loan. However, some people engaged in business may not meet the criteria required by banks to qualify for business loans while others just want quick money because the loan processing by banks may take too long. In such instances, they may end up taking personal loans and putting it in an unviable business, or, they may be tempted to borrow from friends and shylocks in order to have quick access to the needed money. This way, people can end up in a vicious circle of unpaid debts for years.

Buying on credit

When people want to buy something and they do not have enough money, they may be tempted to buy it on credit. Usually, the credit purchase price is higher than cash price because of the interest applied. This includes the use of a credit card to make purchases where it is not paid in full before its due date; usually at the end of the month to avoid the punitive interest rate.

Perks or reward (bonga) points

Some people prefer to buy on credit using credit cards so as to take advantage of the offers from the use of credit cards such as cash back programs, clothes like T-shirts, free meals, airlines' frequent travel miles and many others. Unfortunately, people do not take into account the amount of money lost into the credit cards as well as the stress and worry of the accumulating debts compared to the meagre perks that were promised.

Readily available credit and related offers

People easily get enticed into debts from adverts and notifications that they receive on their mobile phones and other forms of adverts about the loans available. Those who have already borrowed get further offers for topping up their already existing loans. Before they know it, they have accumulated huge sums of debt that is mind boggling.

Sources of Personal Debts

The formal institutions offering personal loans in Kenya are the Commercial Banks; Microfinance Banks (MFBs); Savings and Credit Cooperatives (SACCOs); Micro-Finance Institutions (MFIs); Digital Lenders and mobile telephone apps debts such as fuliza, okoa jahazi, mswari among others.

With the resurgence of digital loan platforms, Kenyans will get deeper into the pit of debts. This is because digital loans have gained popularity due to their ease of application for borrowers seeking quick cash for emergencies and survival without requiring collateral (Business Daily, March 11, 2024).

The formal lenders offer products such as credit cards, mortgage loans and others.

Informal lenders include shylocks, investment groups (*Chama*), family members, friends and others who allow you to take credit for say, shop and groceries, school fees and pay later.

Raising Capital for Business

While this book is about personal finance and not corporate or business finance. But to avoid any confusion between the two let me give you an overview of business finance or simply business capital.

Businesses can raise capital mainly from equity (issuing shares to investors) or debt (taking a loan from financial institutions). Business can also do a hybrid (mezzanine) of equity and debts. Overdraft is a form of a bank debt. The other way in which a profitable business can raise additional capital is to plough back the profits or simply retain earnings. The cost of issuing share capital is dividends paid to the shareholders if the business makes profit while the cost of loan is the interest rate charged on the loan whether business makes profit or not.

What you need to understand is that, most businesses die before they even start, either because they are poorly funded, they get the wrong kind of funding or take too much funding upfront without figuring out why they are raising capital. To share my experience, I had started a butchery business that collapsed within 3 months simply because I did not have an adequate capital plan – the butchery rent, attendant's pay and other overheads were fixed monthly; daily meat sales (demand) were below target; and meat is a perishable stock!

To avoid this common mistake, entrepreneurs need to consider three vital questions before raising capital, including, taking a loan to finance the business venture:

1. **Why are you raising capital?**
When starting a business, you must first assess how much money you will need to invest in it (budget) until it begins to make a profit (break-even analysis). A firm that does not earn a profit is dependent on the owner's capital, and the danger is that if the capital is insufficient, the business will fail. Unfortunately, when capital is depleted, most people fall into a haphazard borrowing trap to finance unprofitable businesses, and they remain in debt for an extended period of time. Without an adequate capital plan for my butchery firm, I could have slipped into debt easily if I did not fold it promptly.

   So, as the business starts making profits, the first question that you need to ask yourself before raising more capital is, does your business need to raise capital at this point in time? Is raising capital the first thing that you need to do to get started or are there alternative things that you can still do to start or run the businesses without raising capital? The raising of business capital must be demand driven by business growth. That is, there is a growing demand for your products or services and you need to raise the capital in order to fund the growth of your business. Any other reason like raising capital so as to have financial freedom; to get rich and to fund something else other than business growth are disastrous. Just do not, because the end game will be to kill the venture quickly. Remember that a growing business will be able to generate revenues to pay the loan plus interests, and profits to be able to pay dividends.

2. **What will the funds that you are trying to raise do for your business?**
Do you have a budget of the items or resources that you want to fund with this capital? You need to have valid needs which have a direct impact on the revenue and growth of business in order to raise capital and fund them. Some of the valid needs for raising capital include, the need to expand your market as driven by the demand for your goods and services; hiring new staff, for example, due to market expansion; product development, for example, to add a product line, financing acquisition of production assets among others. In short, understanding the key drivers of your business, whether goods or services, is very critical because these will help you link business growth and capital required.

3. **How will you raise the capital for the business?**
Once you are clear why you need to raise capital and you have planned how that capital will be used, the next logical thing to do is to understand what your business needs to do in order to raise capital.

In other words, think about those investors for example shareholders, banks and others who you are targeting to provide capital for your business: how do they see your business? To understand whether your business is viable for funding, those investors will look at the financial statements of your business. These are profit and loss and other comprehensive income which shows performance of your business in terms of revenue, growth, costs and profits. They will also look at the statement of financial position or balance sheet, which shows the size of your business in terms of non-current assets; current assets, and equity. The study of these financial statements is beyond the scope of this book. But if you are in business and intend to raise capital, then the key thing to remember is that you need to prepare these financial statements as required and maintain all proper business records.

In general, the main providers or sources of business capital are:

(i) *Equity capital:* private investors and public offering;

(ii) *Debt:* family and friends, commercial banks and development finance institutions;

(iii) *Mezzanine:* commercial banks, development finance institutions, private capital and mezzanine funds.

Implications of Debts on Your Money

To many people, debt is part of their life plan, knowingly or unknowingly. For example, people borrow money to go on vacation; buy clothes that they like; acquire personal use cars and other things that they want ***now*** even without having saved enough money to pay for it! Yes, with debt, you can have whatever you want immediately. However, the implication of choosing to use debts to finance the things that you want now is that you will still have to pay that debt in future, inclusive of interest. Interest is the cost of the debt.

Therefore, with debts, you will spend more money (to pay it back) than you earn which means that debt will be depleting your income. For example, a person earning KES 50,000 (USD 500) a month and spending KES 35,000 (USD 350) monthly will build more wealth over time compared to someone earning KES 500,000 (USD 5000) per month *(10 times !!)* but spending KES 550,000 (USD 5,500) per month. This is because the first person is earing little but saving KES 15,000 (USD 150) per month while the second person is earning 10 times but incurring a debt of KES 50,000 (USD 500) every month.

Additionally, with debts, you lose the control of your money. Remember that the borrower is servant to the lender (Proverbs 22:7). This means that if you have debts, you are like a slave to your creditors or lenders because you are obligated to pay the debts. Therefore, you do not have the freedom to decide how to spend your money. For example, you can't choose to take your money and save it, invest it, spend it, fund retirement, upgrade home, take an amazing family holiday, or give it away because you have to pay creditors every month. When you surrender your ability to make choices on your money to your lenders and fall into the lifestyle of debts, you will no longer be managing your money but juggling debts.

Another thing the debt does in stealing your options is that it may force you to do some work that you are not passionate about or qualified for just to earn some extra money that you need to pay off the debt, among other pressing needs.

The Pain of Debts

Debts hurt productivity and derail expected results

Enterprises usually incur significant indirect costs from consequences of distracted staff and entrepreneurs who face daunting challenges of debt. They are continually looking for extra money to stay afloat as they pay off their debts. Employees are always looking for greener pastures and this causes a lot of distraction from their work, leading to low levels of productivity. Eventually this will result in high staff turnover and increased recruitment cost.

On the other hand, entrepreneurs or owners of the enterprise work hard and see money coming in and out of the business. In the process, they think that this is their money and most squander it. Soon they start experiencing cash shortage but work even harder, more money comes in and they take more of it as it comes in. Have you ever seen a puppy chasing its tail? Something akin to that.

What most entrepreneurs do not realise is that, they are just a line item in the profit or loss statement of their business. This line item is called salaries. Profitable businesses also share profits and pay dividends at the end of financial year: this is an additional line item where entrepreneurs belong in the business financials. Therefore, make sure that you earn a salary from your business for the efforts that you put in it whether the business is making profit or not. The business money is not your money and stop taking it away, for your venture will soon vanish from the financial ruin that you will have inflicted on it.

Debts Cause Financial Risks

Debt can pose significant financial dangers such as:

- **Limited financial options:** always remember that the borrower is a slave to the lender. A debt limits your financial flexibility. Without the freedom to adjust your financial situation because you have to pay off your debts, is a serious financial trap that's hard to escape from.
- **High-interest rates:** whenever you borrow, you always pay more than it costs to pay in cash. This is because debts come with interest. The interest causes you to pay more for an item than it costs. The interest is applicable whether you get a physical loan or hold unpaid credit card balance.
- **Reduced buying power:** when you're paying off debt, you will most likely have to cut back on other expenses or delay purchases until you've paid everything off. Both debt avalanche and snowball methods of debt clearance require one to cut back non-essential expenses as one way to save money to put in debts. Keep reading, you will see details in the next section.
- **Effect on Credit score:** Credit Reference Bureaus (CRBs) lists those who have defaulted payment of bank loans and other qualified institutional lenders. This may hinder employment of a person on integrity grounds, among other considered criteria.
- **Wage garnishment:** debts may lead to a legal procedure where a person's earnings are required by court order to be withheld by an employer for the payment of a debt such as child support. This reduces the disposable income further and piles up the debt stress.
- **Bankruptcy:** debts may eventually lead to bankruptcy where your assets are liquidated in order to raise money to pay off your debts. It is a legal process designed to help borrowers obtain relief from (qualifying) debt that they can't afford to repay while also ensuring that lenders or creditors receive some payment based on the borrower's financial situation and assets.

Debts Hurt Relationships

When you lend money to close friends or family members, chances are that some of them will not pay it back or it may take too long to pay. The delayed or defaulted debt payment will result into suspicion on how your friends and family members are spending their money and it will freak you for example to find them spending on luxuries when they have not yet paid back your money. This will cause suspicion and lack of trust that will eventually lead to a breakdown of your relationship. To nail it down, the relationships usually end as soon as the debt is defaulted.

Debts Hurt Marriages

Debt puts unnecessary pressure on your money and family finances. It creates a lack of financial security for your spouse and your children. When the couple feels overwhelmed, it can spark arguments about spending habits, who is creating more debt, and how much debt is too much, and so on. These arguments can escalate into fights that may eventually lead to breakdown of most marriages.

Debts may also tempt spouses to venture into illicit sex for money so as to supplement the dwindling income, or basically to settle debts. This is not a pleasant solution and it will lead to unsustainable and broken marriages sooner than later.

Debts Cause Stress and Other Health Problems

When you have debt, it is hard not to worry about how you are going to make your payments or how you'll keep from taking on more debt to make ends meet. The deeper you get into debt, the more likely it is that you will face health complications that will limit your ability to enjoy life. You will probably be working on multiple jobs to raise additional income to pay off debts; the constant harassment by creditors-calls; and living in chronic fear and possibility of property attachment will exacerbate debt related stress. The stress from debts can lead to mild to severe health problems such as ulcers, migraines, depression, loss of sleep, emotional outbursts, loss of self-esteem, self-confidence and self-respect, abusing alcohol and other substances and even heart attacks.

Debts Cause Death

There are increasingly reported cases of death by suicide as a result of debts. Terminating your life to escape debt is not a good idea. After all, your death will not pay off the debt, you will just have escaped from it immaturely. Illicit sex for money is also a serious cause of death of death-related issues. This is where some people may choose to engage on the vice as an alternative source of income. This habit will expose them to fatal sexually transmitted diseases among other serious risks including being sexually lured for extortion purposes.

Instead of choosing the death path to escape debt, it is advisable to use the ideas discussed below on how to get out of debts.

How to Get Out of Debts

Getting out of debt is a deliberate choice that you need to make every day. There are no two ways about it: either you are in debt, or you are not. Period. The following are some of the ways you can use to change your financial habits in order to free yourself from the burden of debts.

Avoid Debts

The borrower is servant to the lender (Proverbs 22:7). This means that if you have debts, you are like a slave to your creditors because, now you are obligated to pay the debts and therefore you do not have the freedom to decide on how to spend your money. The best way to avoid debts is to defer your gratification by breaking your purchase goal into smaller amounts and saving little amounts every month until it is enough to use and finance your goal. Remember, if you instead borrow to make the purchase, you will end up paying more and lowering your standard of living because of interest on the debt. To stay a debt free life is a deliberate conscious decision and a choice that you have to make every day: if you do not have money, DO NOT BUY IT. Experience can be the best teacher but you do not need to be in debts - to understand the pain that it causes people. Therefore, the first thing is, say NO to debts.

Create a Working Budget and Live Within it

We have already discussed some practical steps on how to track your current spending; set SMART financial goals; categorise your spending into essential, not essential but important, and, not essential and not important; how to prepare a working budget, taking your priorities into account; and monitoring actual versus budget. Things have been made simple for you, and you can just to use the online CGCents App to implement these steps.

In your budgeting, you should be able to identify the items where you can reduce spending and get more money for important goals like paying stressful debts quickly, creating emergency fund, plus other short-term to long-term goals. This is illustrated in figure 6.

Pay Off Your Debts

The whole idea is to be able to know your outstanding debts, prioritize and pay off quickly. There are two main methods people use to pay off debts faster. One is the Debt Avalanche method and the other is the Debt Snowball method. Both methods require that you have some extra money that you can put into the debt so that you can pay it quickly. Therefore, as discussed in the budgeting process section of this book, you need to identify the items of expenses that you can cut down so as to save some extra money that you can put into paying off your debt. You can also get some extra money from other legitimate sources of income that you may have, like another job, selling merchandise and others. Armed with the extra money, now you can use any of the two methods to clear your debt.

Let's now look at the key steps for each method.

Debt Avalanche Method

The Debt Avalanche method focuses on paying off the debt with the highest interest rate or riskier debt first. It involves the following steps:

- List down all your outstanding debts, for example an education loan; car loan; mortgage; SACCO loan; Micro-Finance Institution loan; bank loan; mobile app loan etc.;
- For each outstanding debt, write down the amount outstanding, the minimum monthly payments, the interest rate and the number of months remaining to complete payment of the loan;
- Arrange the list in descending order, with the highest-interest debt at the top and the lowest-interest debt at the bottom of the list;
- Make the minimum payments on all your debts as you were doing before to ensure that you are paying something for each loan every month;
- Get the extra money found from your expenses or other income sources and put it to the first ranking high interest debt. For bank loans, make sure that the extra money goes to reduce the principal amount of the loan which is the base for the accruing interest. Continue this process every month until the first debt is fully paid off;
- Once your highest-interest debt is paid off, move on to the second highest interest debt. Allocate the extra money to this loan every month until it is cleared. Note that every time you clear a debt, you free up more extra money that you put in the next debt;
- Repeat the process until all your debt is fully paid.

The Debt Avalanche method enables you to pay off the most expensive debts first and this saves you more on interest over time. However, if your highest interest debt is also one of your largest debts, it may take a long time before it is paid off and you need to be patient and stay motivated as it clears.

An example to illustrate the debt avalanche method at work

Partier is 37 years old and wants to get out of the debt of KES 1,200,000 that has accumulated over time, some of which can't be accounted for. Out of the debt, KES 700,000 was from family members and it was used to buy a car; KES 200,000 was from colleagues at work; KES 220,000 with a 20 % interest rate was from Jitegemee Micro-Finance and KES 80,000 with a 24 % interest rate was from mobile phone apps. Partier earns a net salary of KES 120,000 p.m.

Partier's monthly expenses budget includes food at KES 20,000; rent and house expenses at KES 30,000; dining out with friends and personal care KES 20,000; total monthly debts payment KES 45,000. Additional expenses are fuel, parking and others at KES 5,000. After attending a recent seminar on debt management, Partier has decided to free up KES 15,000 from monthly expenditure and use it to pay debt repayments. You are required to help Partier to prepare a debt payment plan using the Debt Avalanche method. You can also work out these figures in USD by using a conservative conversion rate of KES 100 to USD.

The Debt Payment Plan for Partier under the Debt Avalanche method is presented in figure 7.

Figure 7: Partier Debt Payment Plan - Debt Avalanche Method

Partier - Debt Avalanche Method								
Loan	**Outstanding Amount KES**	**Interest Rate**	**Monthly Payment KES**	**No of Months to Complete**	**Debt Ranking**	**Extra Amount KES**	**New Monthly Payment KES**	**No of Months to Complete**
Loans from mobile phone apps	80,000	24%	10,000	8	1	15,000	25,000	3.2
Loan from Jitegemee Micro-Finance	220,000	20%	5,000	44	2		5,000	44
Loan from colleagues at work	200,000	0%	5,000	40	3		5,000	40
Car Loan from family members	700,000	0%	25,000	28	4		25,000	28
Total	**1,200,000**		**45,000**	**120**		**15,000**	**60,000**	**115**

For Partier, the debt with the highest interest is loans from mobile phone apps and it is therefore ranked at the top of the list as priority number 1. The current amount outstanding for this loan is KES 80,000 and it will take another 8 months to clear if Partier continues to pay only KES 10,000 per month. However, because Partier is using the Debt Avalanche Method here, s/he will allocate the extra KES 15,000 to this loan and the new monthly payment is KES 25,000. With this, Partier will clear this loan faster in just 3.2 months instead of 8 months.

After 3.2 months, Partier will put the extra money in the second ranking high interest loan from Jitegemee MFI. Note that the extra money here is KES 20,000 comprising earlier minimum payment of KES 5,000 plus the extra KES 15,000. The MFI will therefore be paid very quickly and Partier will do the same with the other loans.

The Debt Snowball Method

The Debt Snowball method concentrates on paying off your smallest outstanding debt first, regardless of the interest rate. The following are the key steps applied in this method:

- List down all the debts in ascending order, from the smallest to the highest outstanding debt amount;
- Make the minimum payments on all your debts as you were doing before;
- Get the extra money and put it to the smallest outstanding debt first. Again, for bank loans, make sure that the extra money goes to reduce the principal amount of the loan. Continue this process every month until the smallest debt is fully paid off;
- Once your smallest debt is paid off, move on to the next smallest debt in place and put the extra money to this loan every month until it is cleared. When you clear a debt, you free up more extra money that you put in the next debt;
- Repeat the process until you pay off all your debts.

Those who prefer this method get an instant "win" by clearing the smallest debt first, which gives them the motivation to pay off the next loan quickly so as to get another "win". However, they might not save as much money on their debt repayment (interest) compared with the Debt Avalanche method.

The Debt Payment Plan for Partier under the Debt Snowball method is presented in figure 8.

Figure 8: Partier Debt Payment Plan - Debt Snowball Method

Partier - Debt Snowball Method						
Loan	**Outstanding Amount KES**	**Monthly Payment KES**	**No of Months to Complete**	**Extra Amount KES**	**New Monthly Payment KES**	**No of Months to Complete**
Loans from mobile phone apps	80,000	10,000	8	15,000	25,000	3.2
Loan from colleagues at work	200,000	5,000	40		5,000	40
Loan from Jitegemee Micro-Finance	220,000	5,000	44		5,000	44
Car Loan from family members	700,000	25,000	28		25,000	28
Total	**1,200,000**	**45,000**	**120**	**15,000**	**60,000**	**115**

In conclusion, whichever the method you prefer, the key thing is that, when you finish paying off all your debts, you are now debt free and have extra money that you can save and invest for your other important financial goals.

Other Strategies of Easing Payment of Your Debts

As you pay off your debts using debt avalanche or debt snowball methods, you can also explore negotiation with creditors or lenders for variation of terms such as reducing the interest rate and debt consolidation.

With debt consolidation, you can negotiate with a bank to issue out a new loan or credit card to pay off other existing loans. By combining multiple debts into a single, larger loan, you may also be able to obtain more favourable payoff terms, such as a lower interest rate, lower monthly payments, or both. If you get a debt consolidation, you will have only one loan to pay, so there will be no debt avalanche or debt snowball methods anymore and you will put all the extra money in the principal of the consolidated loan in order to pay it faster. Let us look at more strategies of easing payments of debts below.

Create an Emergency Fund

From your budget, save money little by little over time to build an emergency fund. The emergency fund should be equivalent to a total of 3 (minimum) to 6 months (maximum) of your monthly living or lifestyle expenses. This will help you to cope with the situation in case of an emergency such as the loss of an income. This will give you the peace of mind that you need, by reducing the stress that comes with borrowing to sought out an emergency.

Stop or Control use of the Credit Card

If you have used a credit card to make a purchase, PLEASE make sure that you pay the amount in full before its due date to avoid accruing the high punitive interest rates. Financial institutions often allow users of credit cards to pay a small percentage every month and charge a punitive interest on the unpaid balance. Unfortunately, most users of credit cards do not realise this.

Let's say that you made a purchase of KES 10,000 (USD 100) in a particular month using a credit card (Figure 9). You are allowed to pay a minimum 5% of the balance outstanding every month and you will be charged 4% interest on the outstanding balance. In this case, if you just keep paying the minimum 5% every month and don't purchase anything else using that credit card, you will finish paying that amount of credit in 55.5 years and it will have accumulated an interest of KES 39,998 (USD 400)! by that time. This can be mind boggling where you make your regular purchases using a credit card, month after month and you just pay the minimum amount every month as many people do.

Figure 9: Credit Card Cost

Details	Interest Amount (4%) KES	Repayment Amount (5%) KES	Outstanding Balance KES
Initial Amount of Credit			10,000
Month 1	400	500	9,900
Month 2	396	495	9,801
Month 3	392	490	9,703
Month 4	388	485	9,606
Month 5	384	480	9,510
Month 6	380	475	9,415
Month 7	377	471	9,321
Month 8	373	466	9,227
Month 9	369	461	9,135
Month 10	365	457	9,044

Details	Interest Amount (4%) KES	Repayment Amount (5%) KES	Outstanding Balance KES
Month 11	362	452	8,953
Month 12	358	448	8,864
. . .			
Month 665	1	1	13
Month 666	**1**	**1**	**12**
Month 667	0	1	12
. . .			
Month 984	0	0	1
Month 985	0	0	1
TOTAL	**39,998**		
666 months = 55.5 Years !!			

Use Debit Card

In place of a credit card, use a debit card. One of the main reasons people use credit cards is the convenience that comes with its use, both locally and internationally. The real cost to that convenience is the punitive cost of accumulated credit card balances. Therefore, you can use a visa debit card instead of a credit card. The difference is that debit card charges your bill on your actual cash balance held in the bank account while a credit card enables you to access the money that you do not have in the bank, i.e. it simply gives you a debt facility as soon as you swipe it.

You can also use a visa debit card when travelling abroad. Before you travel, just ensure that you cushion yourself with some cash in case the promoters of credit cards abroad like hotels and cab services seek to sabotage your plan by putting a hold on your debit card. Both debit card and cash (in hand or in mobile apps) have emotional attachment to the purchase because you are conscious that you are actually spending the actual money that you have and are thoughtful when spending compared to when swiping a credit card for a purchase. Just a word of caution on debit card: ensure that your bank sets the limit of the amount that you can spend per day using the debit card to control risk exposure.

Delay Gratification and Buy Things Cash

Sometimes you want to buy something now, but you can't because you do not have enough money to buy it now and getting into debts is not an option. Remember Rose from our earlier example? You therefore need to delay your gratification and be patient as you build up enough cash to make your purchase. Break down your goals into affordable small amounts, save and invest these in your preferred saving and investment vehicle (option) over time to realise the amount of cash needed. Imagine, if you invested your house mortgage payment or car loan instalment at the age of 30 years. How much would it be today (say 20 years later)? How much more could you save and invest? What could you do? What would your retirement look like? Which house would you buy or build? What car would you buy? Where would you go on holiday? How much more could you give? All those dreams would be buried in not a well thought out mortgage or car loan. Just think about if you were to go back in time, how would things look like if you had saved and invested wisely?

For illustration purposes, a monthly payment (instalment) of KES 50,000 (USD 500) say for a car loan, if it is alternatively invested at 10% per month from now, it would equal to approximately KES 34,365,000 (USD 343,650) after 20 years (future value of an annuity). You can also be able to calculate this from the CCCents App, Financial Goal Calculator tab.

Keep Debts Out of Your Relationships

We have already discussed how debts can hurt relationships including marriages. Amidst this, your risk is where your debt is not paid by the time your relationship with the hitherto borrower, a close friend or family member, comes to an end. I'm not making a blanket condemnation. Some close friends and family members borrow and pay back their debts, sometimes with a big "thank you interest".

The best way to help a close friend or family member who seeks a debt from you without risking your relationship, is to give them what you can afford to lose in the event it is not paid back. The idea is to just help them with what you can out of the debt amount they want. This way you will help a lot by preventing turning yours into a borrower and lender relationship with all resentment that comes with it. The alternative is just to say no to the request for debt by a friend or family member if you can't afford anything, or in circumstances where you feel that the money that you may lend will not be put into good use. Some money borrowed from you would for example be only used in alcohol consumption and nothing else. A little explanation as to why you are not able to give a debt would help to remove potential strains on your relationship.

Say NO to Guaranteeing or Co-signing Loans

Often people seek the help of a close friend or someone in their circle to guarantee or co-sign a loan that they are taking. The risk with this arrangement is that if the borrower defaults, then it will become your loan and you can be sure that the lenders will surely pursue you for their debt. With that in mind, you do not want to guarantee or co-sign a loan. Unfortunately, the lenders need to find alternative ways to secure their debt than to pass it to your relationship with your friends and family members. Giving lenders the chance to break your relationships in an attempt to secure their debts is not a good move. Just say no to guaranteeing or co-signing loans. Proverbs 22:26-27 tells us, "Don't agree to guarantee another person's debt or put up security for someone else. If you can't pay it, even your bed will be snatched from under you".

Get off Peers, Family and Social Media Pressure

Social pressure from friends, peers, family members, face book, twitter, instagram and other social media platforms largely influence behaviour and spending patterns from those who you listen to and follow. When you are listening to and following them, you will be looking at what they have, which you do not have. These include things like the places where they travelled to; possessions that they have, such as Jewellery, cars, electronic gadgets, houses and other activities and things posted on their social media platforms.

The tragedy with this social influence and comparison mode is that others will always have more than you do or can possibly get. You need to realise that you cannot have everything you want all the time, so you need to stop letting others steal your joy by influencing you on how to spend your money and live your life. And for sure, taking debts is not a good plan for acquiring everything that you need now. It goes back to deferring gratification, keeping at your budget, saving and investing for your affordable goals.