

CHAPTER 16

Paying Down Debt vs. Saving Money

Just about every book on personal finance you can find today will talk about many of the “financial rules”.

There are many that we have been taught as well as picked up along the way. The startling truth about many of these financial rules is some of them **ARE WRONG!** They can be deadly to your chance of ever achieving real financial independence in your desired time-frame.

One of the biggest “financial rules” that is most difficult to break free from is the principle of “Saving Money”. This can be true but only after you are debt free!

Many authorities will counsel you to save 10 percent of your income as investment for your future. Although this is not bad advice as a general rule you must still question if it is the best advice for your situation. If you are carrying any form of credit card debt your interest rate on the card will certainly be much higher than the interest rate you will be collecting with your savings account. Again, remember that the financial institution is in business for themselves and not you. Remember your credit card interest rate maybe as high as 29% (COMPOUNDED DAILY) please read that again (COMPOUNDED DAILY). The interest you are earning in the savings account will be between 3-5% (COMPOUNDED MONTHLY). Let’s say you have the \$2,000 balance on your credit card with an interest rate of 15-25% (we are using interests rates as examples...this maybe lower or higher than your actual rate).

The Example on the next page breaks down the advantage of paying off your debt versus saving the money in a low interest baring account.

The Blue shade represents the interest savings accrued with a starting balance of \$2,000 without ever making another deposit.

The Green shade represents the credit card interest paid on a \$2,000 balance while **NEVER** charging another penny on the card while making the required minimum monthly payment.

EXAMPLE:

| Total Interest on \$2,000 at the end of the Year Listed | SAVINGS ACCOUNT Money Earned w/ Interest Rate Compounded MONTHLY | | | CREDIT CARD Money Paid w/Interest Rate Compounded DAILY | | |
|---|---|-------------|-------------|--|--------------|--------------|
| | 3% Interest | 4% Interest | 5% Interest | 15% Interest | 20% Interest | 25% Interest |
| 1 - Year | \$60.83 | \$80.00 | \$100.00 | \$280.21 | \$382.19 | \$488.72 |
| 5 - Years | \$323.23 | \$433.31 | \$552.56 | \$1,059.77 | \$1,578.99 | \$2,216.00 |
| 10 - Years | \$698.70 | \$960.49 | \$1,257.79 | \$1,557.99 | \$2,534.76 | \$3,940.89 |
| 15 - Years | \$1,134.86 | \$1,601.89 | \$2,157.86 | \$1,756.93 | \$3,113.21 | \$5,283.47 |

- At 15% interest it will take 15 years and 3 months to pay off the card with a total interest of \$1,758.16.
- At 20% interest it will take 21 years and 6 months to pay off the card with a total interest of \$3,464.90.
- At 25% interest it will take 39 years and 4 months to pay off the card with a total interest of \$5,283.47.

Now, just so you understand, putting money into a savings account while carrying high interest credit card debt is not bad advice. It's just the most practiced process often used that causes people to slowly move toward their goals of living debt-free.

Think of paying off your debt first as being in the fast lane to your financial success. Now compare this to the slow lane to your financial success if you continue to put money into a savings account while also paying the minimum debt payments. Which lane do you want to travel in???

We'll explain further in the next chapter...