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Which Credit Card Debt Payoff Strategy is Best?

Q. I've heard I should pay down my higher interest rate cards first. I've also heard I should pay the ones with the smaller balance first. What's the right answer?

A. There is no single answer to your question, but different strategies. You should use whichever strategy will help you stay motivated to continue paying off your credit card debt, said **Claudia Mott, a certified financial planner with Epona Financial Solutions in Basking Ridge**. It comes down to a combination of financial planning principals and psychology. Before you pick a method, Mott said you need to be sure you understand your monthly budget and what additional resources you can put toward debt repayment. She said an online budgeting tool may help you set up a spending plan that incorporates the extra payment you will be making.

Now for a closer look at the strategies. Paying off high interest rate cards first is often referred to as the "debt avalanche" or "debt stacking method," Mott said. The advantages are reduced interest payments and faster balance payoffs. "With this method of debt repayment, you pay extra on the card(s) with the highest interest charges while continuing to make minimum payments on the others," she said. "As the balances decline, you'll be charged less interest and the minimum payments will also be reduced." The lower minimums will make the extra you are paying go even further towards eliminating the debt, Mott said. With this strategy, it may be many months or even years before the balance is eliminated and you actually feel like you have more money in your bank account. This can be discouraging because it may seem like you aren't making any progress towards your goal of being debt-free.

Hence the second option of paying off the smaller balances first, or using what is known as the "snowball approach." "Snowballs start out small, but the more you roll them, the bigger they become. When it comes to debt repayment this momentum can be a motivator," she said. "By focusing on paying off the smaller card balances first there is an immediate sense of accomplishment and this can help you make steady progress towards achieving your target." In addition, you will get the satisfaction of fewer minimum payments and seeing zero balances on your statements, Mott said. Keep in mind that you must continue to make the minimum payments on your other debt and any extra savings that result should be rolled into an additional payment towards another card.

Alison Williams, a certified financial planner with Stonegate Wealth Management in Oakland, recommends you start with the highest interest card that has the lowest balance. Next, take the higher interest with the high balance, followed by the lower interest/low balance, then lowest interest/high balance. That's because saving on interest payments should be your paramount concern. Williams said you could also see if any of your existing credit cards have zero interest balance transfer offers available. Or, you could open a new card with a similar offer. There is typically a fee of 3 to 5 percent of the transfer amount, but the benefits are twofold, she said. "There will be zero percent interest for the offer period, which could range from six to 18 months and potentially save you quite a bit.," she said "Additionally, if the credit line is large enough to transfer multiple balances, you can consolidate payment due dates."

When using these offers, those cards with the highest interest rates should be considered, even if you are only able to transfer in a portion of one account, Williams said, and be sure to keep track of when the promotional period is up and what the interest rate will be when that time comes. If you do work with balance transfers, make sure you don't rack up new debt while you're paying off the old.

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