Consolidated loan can make debt easier to manage

By Kira Vermond

When it comes to credit cards, too many can be too much of a good thing.

According to the Canadian Bankers Association, there are 73.9 million Visa and MasterCard credit cards in circulation in Canada today. Yet an excess of household bills can be difficult to track come payment time. That debt is pricey, too. High interest rates, particularly those charged by retail credit cards to the tune of 29 per cent and up, can put a serious dent in buyers' wallets if they pay only their minimum monthly balance.

While it's sometimes possible to negotiate a lower rate and better terms on a credit card balance, there's another option: take out a debt consolidation loan. These loans, generally offered by financial institutions, allow you to repay your debts in full, all at once. You're then left with only one bank loan to pay off. And, because the new interest rate is lower than the combined interest rates you were paying before, it's cheaper too.

"Consolidating all of your debt into one debt can really simplify things," agrees Sheila Walkington, a Vancouver-based certified financial planner, founder of Money Coaches Canada and co-author of Unstuck: How to get out of your money rut and start living the life you want. Still, she admits the debt management tactic is not for everyone, particularly if your credit rating is on the low side.

Is it right for you? Consider the upside and downside of going the consolidation route:

The upside

You keep it simple. If you're struggling to pay off five credit cards, utility bills and a line of credit each month, consolidating that debt makes a lot of sense. Merge the debt and there's only one major bill to track. You're protecting your financial future too, says Walkington. "If there's only one payment, there's a lot less likelihood you'll miss it and damage your credit rating."

You may save money. By its very nature, a consolidated loan is economical, with a lower interest rate. For instance, say you have $10,000 on a 19 per cent interest Visa or MasterCard card, $8,000 on an 8 per cent line of credit and $4,000 on a 29 per cent retail card, for a total of $22,000 in debt. Merge that debt into a bank-consolidated loan that charges 13 per cent interest and you'll save $840 annually for the four years it takes to pay off the loan. As long as you don't run up new balances on those cards, you've just saved a bundle.

The downside

You can't always get what you want. If your credit rating is decent, you have a job and own assets such as a home, receiving a consolidated loan from your bank is straightforward, says Walkington. But many who find themselves heavily in debt don't have such a stellar financial track record, and that new, cheaper loan is out of reach.

Another alternative is using a credit card's balance transfer option. That is, move the loan balances to a new card that offers a low interest rate for a set period of time. Just be sure to think it through before moving the money. Can you truly pay off the debt before the interest rate shoots back up? If not, you could wind up paying more in the long run.

You may run up your debt again. The truth is, some people who combine their debts actually end up in more trouble if they use their cards again. Not only do they have to pay them off, but the consolidated loan too. Walkington recommends developing a debt and spending plan before making the decision to consolidate.

"It's great to consolidate, but it's not a clean slate," says Walkington. "What made you run up your cards in the first place? You really have to buckle down and make sure it doesn't happen again. You need a clear plan to stay on track."