

The credit trap - how \$4000 debt became \$47,000 – 8 April 2007

Twenty-five years old, nearly \$50,000 in debt and facing three more years of Weet-Bix for lunch. It's a numbers game for Waikato resident Sarah Brown, who clocked up \$4000 of holiday expenses on a credit card eight years ago and now owes almost what she earns in a year.

The details of the \$47,000 debt are set out on a colour-coded spreadsheet written by her budget adviser.

"This is my little bible at the moment. I know exactly what I owe, I know exactly how much I pay, who to, and how much money I can't spend." Brown is determined to clear her debt and has been sticking to her budget for more than a year. But despite a well-paid job in international freight forwarding and a second job in a cafe, there is no money for shopping, eating out or going out with friends. And it's noodles or Weet-Bix for lunch.

Her story is a warning to others as New Zealanders' consumer debt reaches a record of \$150 billion. Budget advisers want creditors to stop lending to people who are already struggling to manage their debts.

Brown didn't buy anything flash with the borrowed money and doesn't have anything to show for it.

Her message: "Just don't get a credit card and don't go to a loan shark - ever."

Brown was 18 when she put about \$4000 on a credit card for a business trip to the United States, where she spent time with her mother who lives overseas. Then she borrowed from a finance company to pay it off and then another company to pay the first company off.

Within two years, the debt had grown to about \$15,000. New loans or refinancing attracted a \$300 establishment fee which was added to the total and incurred interest -one company charged 28%. Penalty fees for missed payments and high interest rates meant the total snowballed over the next four years.

She often tried to pay hundreds of dollars to clear one debt, but would then fall behind on the minimum payments due on others. She did not understand then how penalty interest worked.

"I would have got behind on a payment or something came up and then it got in arrears and you think, 'They're being nasty, I better get another company involved to pay them off and shut them up.' I can't even remember in which order I would have gone to these companies."

Brown has not borrowed any money or had a credit card for more than two years. She owes most of the \$47,000 to three finance companies, two credit cards and two banks.

Federation of Family Budgeting Services boss Raewyn Fox said it was a familiar scenario. One loan with one company was manageable, but things got out of control when people borrowed to pay off other debts.

Interest rates on loans range from 12% to 35%, and when borrowers miss payments, penalty interest can climb to nearly 40%. Reminder and repossession letters can cost up to \$50. One company charges \$450 to set up a \$5000 loan.

Fox wants more onus put on creditors to stop them lending to vulnerable people unable to repay their loans.

Brown agrees. She said it was incredibly easy to borrow money. Often all it took was a phone call.

"I might have been young, but when you go to a loan company you give them all your details of what you're doing. It's amazing that someone hasn't said, 'You really shouldn't be doing this.'

Brown has been to a budgeting service and advises anyone in financial trouble to get help. The reminder letters and phone calls have stopped, she has repayment agreements with all her creditors and can finally see an end to it all.

"In three years' time I won't have to worry about if my rego can get paid or where I'm going to eat. It won't be fixed, it won't be brilliant, but it will be well under control."