

Staying Connected


For the Alumni of the ECCB's Savings and Investments Course




Debt Lock

Unmanageable Debts Have You and Your Future on Lock Down?



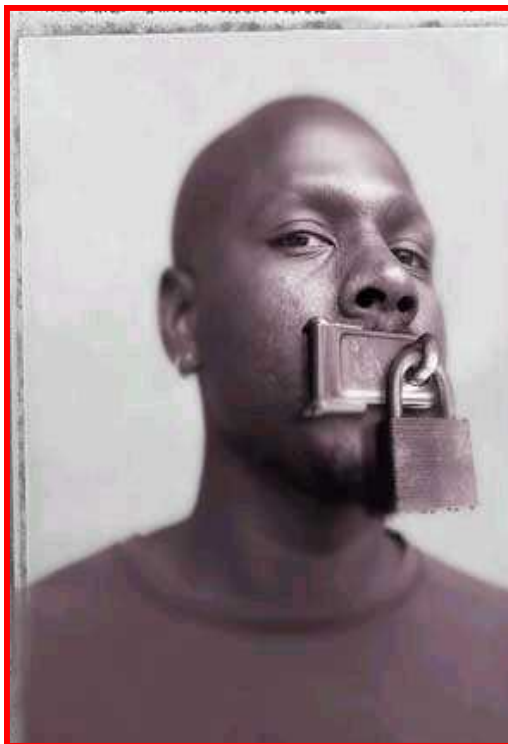
 Learn to say "I cannot afford it."
Spend down to save up.

 **Control your spending. Don't buy on impulse.**

 Borrowing is the easy part, the hardest part is repaying.

You borrow money only to find that after repaying your debts you don't have enough money to make ends meet. So you borrow some more and the cycle goes on and on, entrapping you in a vicious cycle of unmanageable debts.

Borrowing money which you can't afford to repay is the surest way to get yourself DEBT LOCKED. Control your borrowing.



- You are borrowing from Peter to pay Paul;
- Playing dodge ball with your creditors - *This month you make the hire purchase payment for the stove you purchased on credit three months ago but you skip the hire purchase payment for the*

new furniture. Next month, the furniture payment will be made but you will dodge the payment for the stove;

- You avoid answering any incoming telephone calls that show up as "private", just in case it is your banker calling about last month's missed payment;
- Your 19% APR credit card which has a \$5,000 limit has been maxed out to pay for that wonderful cruise. But now that you are back on dry land you are faced with the reality that coupled with all your other debts, that cruise is now a burden to repay and you can only afford the minimum monthly payment of \$100. At this rate, a huge portion of what could have been your potential wealth is being eaten up in interest payments and that \$5,000 cruise can end up costing you \$9,985 (*\$5,000 which is the amount borrowed plus \$4,985 in interest payments*) and 8.33 years to

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The Eastern Caribbean Central Bank

2008/2009 Annual Report Presentation

Monday 29 June 2009 at 8 p.m. on your local radio stations

How does the work of the ECCB affect you and your family?

Tune in to find out!

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repay if you were to continue just paying the minimum amount due;

- Added to all this, two years ago, your friends convinced you that that a new house needs a new car and so you traded in your old car for a new one. So you are also indebted to the car dealership for the next 3 years;

All these debts have made it difficult for you to meet your mortgage payments not to mention your property insurance and taxes and house maintenance expenses. You are literally and figuratively over-extended in your finances and when you add your cost of living expenses to these financial challenges you feel like you are literally drowning in bills.

You try your hands at the casino and buy lottery tickets weekly hoping to hit the jackpot. You dream about finding



a **debt relief pill** that you can take to ease your debt burden.

Directions - Take two capsules a day for six months. IT DOES NOT EXIST!

Getting into debt was easy, getting out however, will be a long uphill battle that will require your

discipline, commitment, and sacrifice. You will most definitely have to downgrade your lifestyle to upgrade your finances in order to rid yourself of the stress of unmanageable debts and secure your financial future.

The first thing that you need to do is to stop accumulating more debts - "spend down so that you can save up". Sometimes it seems that the more indebted you get, the more debts you accumulate, probably trying to spend yourself out of the stress of dealing with the seriousness of indebtedness. However, you only end up adding to your debts and stress.

The second step is to make a list of all your debts, and list the amounts that you are paying each month and the associated interest rates. This will give you a clear picture of your debt situation.

Now where do you go from here? The answer; talk to your banker.

In keeping with this advice, **Your Financial News (YFN)** sat down with Deverson Warner, Account Executive, RBTT to get his views on debt management and debt repayment relief.

YFN: Welcome to YFN. These days discussions about debt management and debt repayment

relief are quite topical. What in your opinion are the reasons why individuals get into debt management difficulties.

Deveson Warner: There is really only one reason. Persons get into debt difficulties when they have over-extended themselves financially. You know we live in a time of want and these days it is quite simple to acquire stuff. There are a lot of sale offers out there and hire purchase is very accessible. Hence, persons fall into the trap of taking on more debts than they can handle.

YFN: What options for relief do individuals have when they have more debts than they can handle?

Deveson Warner: Individuals who are multi-banked *i.e. they have several debts with different entities* may be able to consolidate their multiple payments to different creditors into one new reduced payment to a single creditor. The objective is to reduce their monthly debt payments so that they can have some liquidity (extra cash in their pockets).

NOTE: While loan consolidation serves to reduce one's monthly payment, reductions in the monthly payment require increasing the term of the loan. Getting the new loan may also bring with it additional costs such as the fees associated with establishing a new loan, and penalty fees associated with the early pay outs on the old loans. However, one may be able to save money by getting a consolidated loan with a lower interest rate to pay off debts with a higher interest rate.

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YFN: What do banks consider when determining whether to lend individuals money to pay off existing creditors and consolidate all their debts into one single lower loan payment?

Deverson Warner: Each situation is assessed individually. When a bank provides a loan to assist someone who is unable to meet his or her contractual payments to existing creditors the bank is assuming a greater risk. So the bank has to take this into consideration. The individual's credit history, capacity to repay, debt service to income ratio and other issues are key determining factors.

The other issue to consider is that many times having consolidated clients' debts and freed up some extra cash those individuals are often tempted to go out and start running up their debts all over again.

YFN: One therefore has to be disciplined in repaying this new loan.

Deverson Warner: Precisely. Furthermore, debt consolidation is not the answer for every debt situation. A bank would not consolidate a mortgage loan with a car loan, for example, for obvious reasons. The car loan is a short

term financial commitment while the commitment for a mortgage is long term.

The assessment of each individual and the individual's situation is therefore critical to the bank's decision making process. The bank has to look at the entire situation - the individual's income and expenses, all outstanding debts including those with other creditors

YFN: Outside of debt consolidation, are there any other debt relief options? For example, loan refinancing?

Deverson Warner: Loan refinancing means taking a new loan to pay out an existing loan. This is an option for some individuals but again one has to look at the specifics of each situation. A client may have taken a loan a year ago for \$15,000 and now has a balance on the loan of \$11,000, but finding him or herself in a cash strapped situation approaches the bank to refinance the existing loan with a new loan for \$15,000 in order to pay off the balance of the current loan and provide him or her with \$4,000 in cash.

The key is to find out exactly what the client intends to do with the funds. It would not make sense to try to assist the client in getting out

of one unmanageable debt situation by providing him or her with an option that would essentially place him or her in an even more unmanageable debt situation. That would be akin to trying to get someone out of a hole by digging a bigger hole. And, many times when the loan officer investigates further, it becomes obvious that the client wants to use the funds to finance a want and not a need. So refinancing would not be in the best interest of the client in such situations.

YFN: Are there circumstance that warrant your advising a client to sell an asset to improve his or her finances?

Deverson Warner: Many times. Take for example a small business experiencing cash flow problems. A loan may not be the solution. What the business may need is an infusion of cash without increasing its debt obligations. The solution therefore may lie in liquidating an asset such as a fixed deposit or reducing the price of the business's products or services in an attempt to increase the cash flow.

When it comes to the sale of real estate however, a quick sale to increase cash flow is a little more difficult, especially in these times of economic downturn... No one is buying, the market is quite bearish.

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YFN: Are repayment holidays also included in the list of debt relief options? Let's suppose an individual's debt management difficulties have been brought on by an unexpected crisis e.g. unforeseen medical expenses or legal expenses incurred as a result of a child who has gotten in trouble with the law. Can the individual approach his or her bank and request a payment holiday on an existing loan, let's say for three to six months?

Deverson Warner: Again, it is not as simple as that. The bank would have to look at the individual's present financial situation. Because while the principal can be waived for a short term period, the interest has to be paid. So if that individual is just one year into a fifteen year mortgage, the interest would be the most substantial part of the payment hence a waiver of the principal payment, which would be relatively small in comparison to the interest payments may not put the individual in a better financial situation.

Even if this is not the case, one has to consider that the amount waived has to be tacked on to future payments to bring the payment schedule back in line with the contracted end date so the key questions is - **How is the**

individual going to make up for those missed payments? Because the intention is not to refinance the loan.....Granted refinancing can be an option. Another option is for the individual to apply for a second loan to cover the medical or legal fees instead of exhausting all the available cash resources....

Certainly there are extenuating circumstances whereby a moratorium on the interest and principal may be applied. But such circumstances are usually rare. Let us say, for example, that a country's tourism infrastructure has been almost totally devastated by a hurricane and hence hotel workers have all been laid off for six months and guarantees have been given that the tourism sector will be up and running at the end of the six month period. In this case, it is not an isolated or individual circumstance. A bank may therefore consider a moratorium on interest and principal for those employees until the hotel sector resumes operations.

YFN: What are your views on payday loans?

Deverson Warner: It puts you more in debt because if you are asking for an early payment of your salary because you are out of cash half way into the month, then it means that getting a payday loan will only serve to cause you to get

deeper and deeper in debt. Not only would you have fees and interest to pay on the payday loan but by the middle of the next month you are once again strapped for cash. So you will always be having to seek out loans to get you to the next paycheck and the next.

YFN: What advice would you give to individuals in relation to effective debt management?

Deverson Warner: Before getting into any debt obligations look at your net income and any other existing commitments including rent, if applicable. You have to base your debt wants on your level of income.

Ask yourself, how much do I have at my disposal to be able to comfortably repay that loan? Now a person's notion of what is comfortable might vary widely. I know of persons whose debt service to income is about 80% and they are still persistent in arguing that they can comfortably repay another loan. However, the accepted benchmark is that a person's debt servicing should not exceed 40% of net income.



Debt is the worst poverty

Thomas Fuller



NEWSFLASH.....

1



The **Governor of the Eastern Caribbean Central Bank, Sir K. Dwight Venner** will be making a public presentation of the 2008/2009 annual report on Monday, 29 June 2009. Tune in to your local radio station and learn about the role and operations of the Bank, and its relevance to the everyday lives of the people of the ECCB region.

The Annual Report will also be available on the ECCB's website at www.eccb-centralbank.org

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Financial Literacy Month, celebrated in October of each year throughout the ECCU has been renamed **Financial Information Month.**

The month may have a new name but it has the same unwavering focus to increase understanding of financial matters among the people of the Eastern Caribbean Currency Union and catalyse the development of enduring financial education programmes targeting the public.

IN
THE
HEADLINES

What's going on?

3

Look out for the following upcoming issues on the Regional Government Securities Market (RGSM) for June 2009.

- 5th June 2009, Government of St Vincent and the Grenadines 91 day treasury bill of \$20 million.
- 18th June 2009, Government of Antigua and Barbuda 91 day treasury bill of \$17 million.

Government securities (*treasury bills, notes and bonds*) issued on the RGSM are sold via the Eastern Caribbean Securities Exchange (ECSE).

Treasury Bills are sold through a single price auction where the yield of the security is determined by competitive bidding by investors. Each investor must submit a bid specifying a yield for a specified quantity of securities not less than \$5,000 and in increments of \$1,000 thereafter. Those bids that fall within the yield accepted by the auction will be awarded the security. Each successful investor receives the same yield for his/her securities.

Treasury Notes and Bonds are usually sold on a fixed price subscription basis where the price is determined by the government before issuing the securities and the investor submits an application for an amount not less than \$5,000 and in increments of \$1,000 thereafter. For more information on government securities visit www.ecseonline.com



Understanding the Prospectus and the RGSM

A prospectus is a disclosure document issued by companies and governments intending to sell securities. The prospectus contains key information relevant to the offering including the planned use of the money, and other historical financial and economic data.

In the case of governments in the ECCU, the securities sold are usually treasury bills and bonds. Treasury bills are short-term debt instruments (maturities up to a year), commonly referred to as T-bills. Bonds are long term with maturities over one year.

Any person who purchases any of these debt instruments is essentially making a loan to government at an agreed upon price which usually includes an interest rate to compensate the lender for the funds provided.

In order for a prospective purchaser to evaluate the potential risk and return of a particular government security, he would need to assess the level of risks that would be incurred in lending funds to government and the government's ability to repay the loan at the specified time in the future. Such information can be determined by analysing the prospectus issued by the particular government for the sale of securities.

So what should you as a potential investor be assessing? You will need to assess the fiscal performance of the particular government. Your assessment should include, but not be limited to an analysis of the major sources of income and expenditure, and the size and components of the government's debt. This should allow you to determine if the particular government would have adequate income to honour its current as well as the future debt obligations that would be incurred by this new debt. You will also have to determine the buoyancy of the income sources to determine whether such sources will continue to adequately generate the funds required to meet the obligations of the government.

Another area that should be assessed is the country's economic performance factors, such as the rate of growth of gross domestic product (GDP), the consumer price index, wages and salaries in the main sectors and balance of payment statistics. By evaluating the aforementioned data, you would be able to determine the direction of the economy, that is whether the economy is growing or contracting.

Why is this important? In a country where the economy is growing, employment opportunities are being created, the business sector is expanding and demand for goods and services are increasing. Given that most of government's

revenue is derived from taxation, a strong economy provides a favourable tax collection environment. There is also less strain on government's expenditure. When the economy contracts, the earnings of citizens and corporations decline and hence impact adversely on governments' tax revenue sources. Additionally, in an environment of economic contraction, the government is less likely to attract foreign investments required to catalyse new industries and provide for additional revenue generating sources within the country.

You should also assess the government's track record in honouring its debt obligations. This must be disclosed in the prospectus along with other material events, such as the impact of a recent hurricane, and any event, which could affect the assessment of the security being issued.

So now that you know what to look for, why not find out more about the Regional Government Securities Market (RGSM)? For further information, visit the Eastern Caribbean Central Bank website at www.eccb-centralbank.org or the Eastern Caribbean Securities Exchange website at www.ecseonline.com *SLW*

Try to learn something about everything and everything about something. *Thomas Huxley*