Will debt consolidation hurt or help my credit rating?

Answer:

Debt consolidation can lead to an improvement in your credit rating by making your debt easier to manage. Sometimes, debt consolidation means taking a loan at a lower interest rate to pay off several smaller loans at higher interest rates. Making one payment instead of many may help you keep your debt under better control, make it easier for you to make timely payments, and thus improve your credit rating.

Although managing your debt will improve your credit record in the long run, consolidation can have a more immediate impact. For example, if you have 10 accounts in default on your credit report, your lenders will consider you a bad credit risk. But if you can pay off those accounts with a consolidation loan, you have eliminated the problem. Your new credit report will now show that you cured the defaults and retired the debts. And you have only one open account--your consolidation loan. As long as you stay current on the consolidation loan payments, your credit rating will be viewed more favorably than before.

Remember, your goal is to manage your debt by making your payments more affordable. You can do this by lowering your interest rate or increasing the number of months you have to pay off the debt. There is no point in consolidating if you don't achieve one or both of these goals--you'll want to be sure you can afford the consolidation loan and make the payments. Otherwise, you'll end up back where you started.

Although debt consolidation has its advantages, you must recognize that by extending the time to pay off your debt, you will ultimately be paying more in interest charges. Also, once you get a consolidation loan, you should consider closing some of your credit card accounts so that you can't simply run up your bills again.