FORTUNE RECOMMENDS

Snowball vs. avalanche: Which is the best way to pay off debt?

BY **IVANA PINO**

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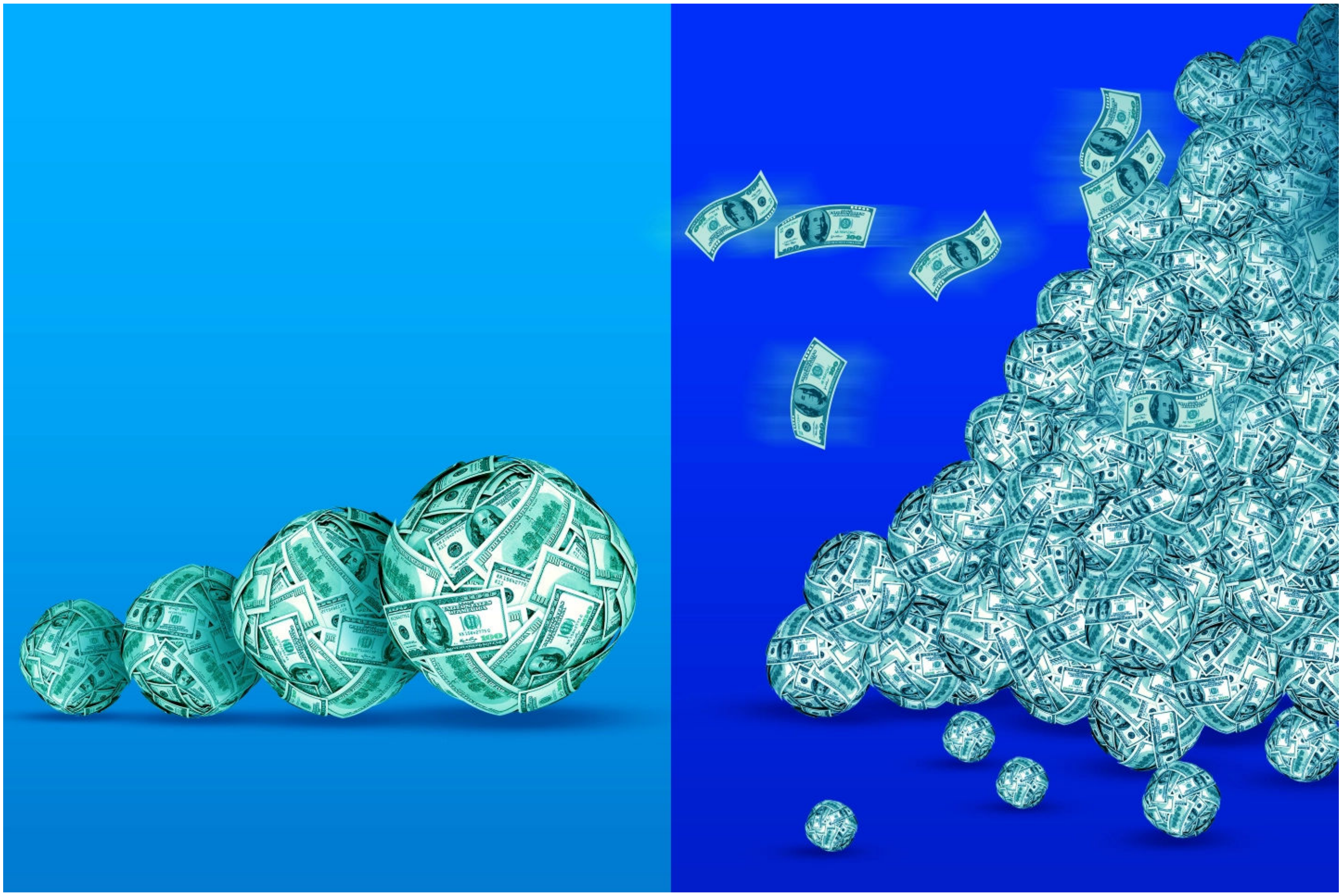

The debt snowball and avalanche are two commonly used debt repayment strategies.

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When you're faced with a massive debt balance, the journey ahead can seem daunting. But choosing the right repayment strategy is key to effectively chipping away at your debt over time. The right strategy will depend on a number of different factors like the kind of debt you have, the terms of your debt, and what makes the most sense for you and your budget long-term.

Two of the most common strategies are the snowball method and the avalanche method. We'll break it down for you.

What is the snowball method?

The snowball method is a strategy where you start off slow and pay off your smallest debt balances first. Over time, as you knock out your smaller loans one by one, you begin to tackle bigger balances afterward. Say you have five student loans that range from $1,000 to $10,000. Using the snowball method, you would start your repayment journey by paying off that $1,000 balance first and then moving on to your next smallest balance until you only have that one large $10,000 loan left to pay off.

The key here is to start building momentum and slowly work debt repayment into your budget. This is also an effective strategy for borrowers who anticipate that their income will grow over time. By the time you're working on paying down your biggest debt, you may have more income available than you did when you first started paying down debt.

So, why does this work? Because small amounts of progress can help motivate borrowers to stay the course. "The snowball method involves making the minimum payments on all debts and using any excess funds to pay your smallest debt as fast as possible. Once that loan is paid off, apply any excess after the minimum payments to the next largest debt," says Jill Fopiano, the CEO and president of O'Brien Wealth Partners in Boston.

"While this may not be the most efficient way to pay off debt, it is a series of small wins which can be motivating and confidence-boosting to the borrower."

How about the avalanche method?

If you're the kind of borrower who prefers to tackle their biggest challenge first, meet the avalanche method. This strategy involves paying down balances with the highest interest rates first. While this method could mean a higher payment from the start, prioritizing debts with higher interest means that your payments will likely decrease over time as you liquidate those balances. It also means that you'll pay less in interest over the life of your loans and could even trim your repayment timeline significantly.

To implement this strategy, you'll need to list out your debts from highest to lowest interest rate. Each month, after you've made the minimum payment on each loan to remain in good standing with your lender, you'll allocate any extra funds to your debt with the highest interest rate. This method involves a lot of discipline and it may take some time before you begin to see those higher balances get smaller, but it's also likely to save you more money long-term.

Pros and cons of each strategy

When you're settling on a plan of attack for your debt, knowing the potential benefits and drawbacks of each strategy is key. If you're thinking of using the snowball method, a few of the major pros and cons include:

Pro: The snowball method can help you score quick wins. Tackling your smallest balance first means that it likely won't take you long before you're able to eliminate a loan. This could be the motivation you need to continue on your debt repayment journey.

Pro: If your income isn't where you want it to be yet, the snowball method can help you get the ball rolling on debt repayment. If you haven't reached your full earning potential, implementing the snowball method could make it easier to tackle your debt as you work to boost your income over time. By the time you're left with your biggest balances, you might be in a better financial position to pay them down.

Con: The snowball method increases your payments over time. If your goal is to have more income available for other money goals down the line, increasing your payments over time could make it more difficult to hit those costlier milestones like buying a home or starting a family.

Con: You will likely pay more in interest over the life of your loan. Setting your bigger balances aside could end up costing you more over time. "The debt snowball method can be valuable for maintaining energy and dedication while paying off debt," says Daniel R. Hill, CFP and president of Hill Wealth Strategies in Richmond, Virginia. "However, the snowball method can obviously lead to a balance being held on an account with a high interest rate for a longer period of time because it's not the main focus."

The avalanche method comes with its own unique pros and cons, including:

Pro: Your payments will decrease over time. The goal of the avalanche method is to start with your highest interest debt. While this could mean a bigger payment at the start of your repayment period, chipping away at these larger balances first means that your payment will likely decrease over time.

Pro: You'll pay less in interest over time. Rather than letting your high-interest loans sit and accumulate interest, you'll save money by paying off those debts first.

Con: It may take longer to pay off your first loan. If you're looking for a quick win, this strategy may not be the best fit. "A disadvantage is that it may take longer to get balances down to zero and paid off because only the minimum payments are being made on the smaller accounts," says Hill.

Con: Starting off with higher payments could be difficult for lower earners. Depending on what your financial situation looks like at the start of repayment, starting off with bigger payments could feel like a stretch for your budget.

Pros	Cons
PAYMENTS DECREASE OVER TIME	CAN TAKE A WHILE TO SEE A REWARD
YOU'LL PAY LESS IN INTEREST OVER TIME	HIGHER PAYMENTS CAN BE STRESSFUL FOR BORROWERS WHO ARE AT THE START OF THEIR CAREERS

The takeaway

The best debt repayment strategy for you will ultimately depend on the strategy you think you can stick to and the one that works best for your loan type, interest rates, cash flow situation, and long-term goals.

"If you have debt that has a wide spread in interest rates, the avalanche method will be even more powerful," says Fopiano. "If, on the other hand, you have numerous smaller debts at similar interest rates, the snowball method may help you manage the repayment process with more discipline."