

Comparing Credit Cards

Using credit cards isn't necessarily bad. However, you need to be cautious when using them. They can be a tool to help you manage your monthly expenses when used wisely—but can wreck your monthly budget and create financial problems for years to come when overused or abused. Understanding the basics of credit cards will help you make better choices about which card is best for you. The following information will help you make more informed decisions about credit cards.

Part 1. Credit Card Facts

- Credit cards are a type of revolving credit, which means your monthly payments depend on how much you charge on your card rather than being a set amount for a specific number of months.
- Household debt on credit cards is about \$1.4 trillion—making it about one-third of all debt owed by U.S. families.
- Students graduating from college have an average credit card debt of \$6,800 in addition to an average of \$33,000 in student loans.
- Over 83 percent of all adults in the US have at least one credit card; 90 percent of those with credit cards have more than one. The average number of credit cards accounts is 2.3 per family.
- Almost 50 percent of credit card holders pay the total amount charged every month and carry no balance forward. For those who carry a balance, the average amount owed is \$4,500 per person or \$8,700 per family.
- Households with lower incomes tend to have more credit card debt than households with higher incomes. As average income increases, average credit card debt decreases. However, the percent making minimum payments is about the same for all income levels.
- Making minimum payments or carrying a balance each month increases the total amount paid for the goods and services purchased with a credit card. For example: Suppose the interest rate is 17 percent and there is a \$10,000 balance on the account. The minimum payment would be about \$240 a month, and it would take 340 months (over 28 years!) to pay off the card—with no additional charges on it.) That's a total of \$13,607 in interest.

Part 2. Credit Card Basics

Understanding the basics of credit cards can help you make better choices when making credit decisions. Not all credit cards are alike. Here are some ways in which they differ.

- **The annual fee.** Some credit cards charge an annual fee, and some do not. The amount of the annual fee may vary from card to card. Most people who have a strong credit record can find cards that do not charge an annual fee.
- **Other fees.** Credit cards usually charge stated fees for late or missed payments, going over your credit limit, or making certain transactions such as cash advances.

- **The annual percentage rate (APR).** The APR can vary from card to card by several percentage points. Furthermore, some credit cards offer a low APR for the first few months and then increase it after three or six months. The APR on cash advances often differs from the APR for purchases.
- **The grace period.** Almost all credit cards have a grace period, which is the amount of time you have to pay the balance without paying interest. It generally starts the first day of the billing cycle and lasts for specified number of days. While grace periods vary from one card to another, they tend to be 21 to 25 days. The longer the grace period, the more interest-free days the cardholder has to pay the balance before incurring interest. (Note: Cash advances on a credit card may not have a grace period.)
- **The way interest is calculated.** The interest on credit cards is calculated using the average daily balance. By using this method, the APR is divided by 365 and then multiplied by the average of each day's balance for the billing cycle. While there are other ways to calculate interest, the average daily balance has become the standard for credit card companies.
- **The credit limit.** This is the maximum amount of money a cardholder can charge. A higher credit limit gives the cardholder flexibility but can also lead to credit card balances that are difficult to pay off.

Part 3. Other credit card features, services, and incentives

Credit cards also differ in the types of services and features offered, which may influence your decision when choosing a card. However, you should carefully compare the benefits of these incentives with the potential costs associated with the interest rates and other basics. Following are some of the additional features, services, and incentives offered by credit card companies.

- High or no credit limits.
- Rewards such as cash back, gifts, airline miles, discounts on gasoline or other purchases.
- The number of merchants who accept the card.
- Travel services such as covering the rental car insurance deductible, discounts on hotels, travel-life insurance, cash advances, or ATM privileges.

Part 4. Credit Card Comparison Chart

Follow the directions provided by your teacher to complete the chart below.

	Card #1	Card #2	Card #3
APR (annual percentage rate): Is it fixed or variable?			
Penalty APR and trigger events when it is charged			
Annual fee			
Late fee			
Over-the-limit fee			
Transaction fees (balance transfers, cash advances, etc.)			
Grace period			
Method of computing account balance			
Rewards for use			

Calculating Your Interest Rate

Using the information provided in **Slides 15.1–15.3**, calculate the following monthly interest rate.

APR	19 percent
Beginning Monthly Balance	\$1,000
New purchase on the 10th	\$500
Days in billing cycle	30

Reading Your Credit Card Statement

Part 1. Define the following terms, using your own words.

- a. Summary of account activity

- b. Payment information

- c. Late payment warning

- d. Minimum payment warning

- e. Notice of changes to your interest rates

- f. Other changes to your account terms

- g. Transactions

- h. Fees and interest charges

- i. Year-to-date totals

- j. Interest charge calculation

Part 2. Use the following credit card statement to answer the questions on the following page.

CARD Statement

A Account Number 1234 1234 1234 1234
C Statement Closing Date 11/09/19
C Credit Line \$2,100.00
C Credit Limit \$1,576.80

B TERESA TORRES
D 123 ANY STREET
D CITY CA 12345

E **Account Summary**

Previous Balance	\$1,688.15
- Credits	\$0.00
- Payments	\$1,688.15
+ Purchases & Other Chgs	\$523.20
+ Cash Advances	\$0.00
+ FINANCE CHARGE	\$0.00
= New Balance	\$523.20

F **Payment Information**

New Balance	\$523.20
Scheduled Minimum Payment	\$35.00
Scheduled Payment Due Date	12/01/19

H

Late Payment Warning: If we do not receive your minimum payment by the date listed above, you may have to pay a late fee of up to \$35.00 and your APR's will be subject to increase to a maximum Penalty APR of 29.99%.

Minimum Payment Warning: If you make only the minimum payment each period, you will pay more in interest and it will take you longer to pay off your balance. For example:

If you make no additional charges using this card and each month pay...	You will payoff the balance shown on this statement in about...	And you will end up paying an estimated total of...
Only the minimum payment	1.5 years	\$627
\$49	1 year	\$596 (Savings=\$31)

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If you would like information about credit counseling services, call 1-800-555-5555.

Rate Information

YOU MAY PAY YOUR BALANCE IN FULL AT ANY TIME
 YOUR RATE MAY VARY ACCORDING TO THE TERMS OF YOUR AGREEMENT
 NOTICE: SEE REVERSE SIDE FOR IMPORTANT INFORMATION ABOUT YOUR ACCOUNT

Type of Balance	Corresponding ANNUAL PERCENTAGE RATE	Daily FINANCE CHARGE RATE	Average Daily Balance
PURCHASE(S)	19.80%	.05424%	\$.00
CASH ADVANCE(S)	21.80%	.05972%	\$.00

Composite ANNUAL PERCENTAGE RATE 21.80% **J** Days in Billing Cycle 25

Transactions **K**

Trans Post	Reference Number	Description	Credits	Charges
10/08 10/08	XXXXXXXXXXXXXXXXXXXX	MERCHANT NAME		523.20
10/08 10/09	XXXXXXXXXXXXXXXXXXXX	PAYMENTS	1,686.15	

Detach an mail with check so that your payment is received no later than the "Payment Due" date. See reverse for important additional information.

Account Number 1234 1234 1234 1234
 New Balance \$523.20
 Scheduled Minimum Payment \$35.00
 Scheduled Payment Due Date 12/01/19

L **Amount Enclosed** \$

12/01/19

PAYMENT ADDRESS
 123 ANY STREET
 LOS ANGELES, CA 90030-0086

TERESA TORRES
 123 ANY STREET
 CITY, CA 123456

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- a. How much did Teresa Torres charge on her credit card in October?
- b. What is the credit limit on this credit card?
- c. How much of that credit is available at the time of this statement?
- d. How does her previous balance compare to the new balance shown on this statement?
- e. Was she charged any interest on her purchases this month? If so, what was the amount? If not, why was there no interest added to her account?
- f. How much would she need to pay on this statement to avoid paying any interest?
- g. What is the annual percentage rate for purchases on this account? How does that differ from the annual percentage rate for cash advances?
- h. What would happen to the interest rate if she missed a payment or made a late payment on this account?
- i. Suppose Teresa decided to make only the minimum payments on her October purchase, with no other charges on this account. How long would it take her to pay it off? How much interest would she pay? How much would her purchase really cost?
- j. Looking at this statement, do you think Teresa is handling her credit card responsibly? Why or why not? What would you recommend?