

Borrowing – Using Your Credit Card

There are many advantages and benefits to using your credit card and there are some things you can do to help you manage your card well and get the most out of your credit card.

Choose the right card

Start by choosing the right card for you and your lifestyle. Make sure the annual fee, interest rate and rewards and benefits work with how you intend to use your credit card. Making sure you have the right card for you will start you off on the right foot.

Once you have chosen the right card, keep the fact that credit costs money at the top of your mind when you make decisions about how to use your credit card.

Don't Spend Money You Don't Have

Don't spend more money than you have. It can be tempting to think of a credit card as free money or an unending supply of borrowed money. However, credit cards are far from free and using that credit comes with a cost. Your credit limit is the maximum amount you can borrow on your card, but even if you stay within your credit limit, you still have to pay back everything you spent as well as the interest it accrues if you carry a balance on your card. You may even have to pay extra fees if you miss a payment. Because of the high interest rates on credit cards, paying interest on your purchases will add up quickly and eat up the benefit you get from any rewards.

To give you an example, if you make a purchase on your credit card for \$2000 and you make the minimum payment each month, how long will it take you to pay it off with an Annual Interest Rate of 19.99%? Making just the minimum payment, it would take you 15 years and 3 months to pay it off. Your original balance would be \$2,000 and you would pay \$2,238.13 in interest over the 15 years and 3 months, and the total cost of your \$2000 purchase would be \$4,238.13... more than double the price of the item! If you paid the minimum payment each month plus an extra \$10 each month, it would take you 7 years and 6 months to pay off your \$2000 purchase. It would cost you \$1275.14 in interest for a total of \$3,275.14. That extra \$10/month would save you \$962.99 and you would pay it off 7 years and 9 months earlier! If you paid a fixed amount of \$100 each month rather than just paying the minimum payment, you would pay off your \$2000 purchase in 2 years and 1 month. You would pay \$452.92 in interest for a total cost of \$2,452.92, saving \$1785.21 compared to if you only paid the minimum payment each month. You would also pay it off 13 years and 2 months faster. If you want to see how these payment scenarios work out with one of your own purchases you can use the free Credit Card Payment Calculator on the Government of Canada website at <https://itools-ioutils.fcac-acfc.gc.ca/CCPC-CPCC/CCPCCalc-CPCCCalc-eng.aspx>

Pay Off Your Balance in Full Every Month

Try to pay off your balance in full every month. It is best to spend only what you can afford so that you can pay off your credit card balance in full every time and avoid late payment fees and interest charges. And, as we saw from the example, even if you can't pay off your credit card balance in full each month, even small increases over the minimum payment amount will work out to significant savings in cost and time. And, this is just looking at a single payment. If you are continuing to put purchases on your credit card, you may never be able to get yourself out of the hole of debt you'll create.

If you find yourself with growing credit card debt, talk to someone at your financial institution as soon as possible. They'll be able to sit down with you and look at your debt and help you come up with a plan for reducing your debt as quickly and affordably as possible. The sooner you seek help, the more likely that your financial institution will be able to help you reduce your debt effectively.

Make Payments On Time

Always make your payments on time. If you miss a payment, you may be charged a late payment fee and will begin to accrue interest charges on the balance you're carrying on your card which can make your credit card costs snowball quickly. Whether you make your credit card payments on time every month affects your credit score which can affect you in significant ways if you ever need to borrow money or even in other situations such as trying to rent a home or sign up for a cell phone contract. If you don't make your payments on time, that will cause you to have a lower credit score. Potential lenders will see that you aren't reliable at paying back your debt and will be hesitant to lend to you or may lend to you at a much higher interest rate than they would if you had a better credit score. Even landlords, cellphone and other service providers will look at your credit history to see if they can trust you to pay your bills on time. Most credit card issuers will determine a minimum payment for your credit card. This does not usually cover all your spending on your card but is the minimum amount you must pay in order for your credit card account to stay in good standing and to avoid late fees. It is best to pay off your full balance every month so you avoid any interest charges but if you can't do that, be sure to pay at least the minimum amount on your card and pay it on time.

Watch Your Credit Utilization Rate

Pay attention to your Credit Utilization Rate. This is the amount of credit you use compared to the amount of credit available to you. For example, if you have a \$5,000 limit on your credit card and spend about \$1500 on your card each month, then your credit utilization rate is about 30%. It is recommended that you try not to let your credit utilization rate exceed 30% of your available credit. This is also a factor that goes into determining your credit score. Just because you have credit available to you, doesn't mean you should use it. It's also good to leave some room on your credit card available for an emergency or if something unexpected comes up.

Credit cards can be a fantastic financial tool if you use them carefully and manage them well. Following the best practices we've outlined here will help you to manage your card well so you can enjoy all the benefits and advantages of having a credit card.