

Credit cards are not evil,
but they can be dangerous

Advantages

- ① Convenience - whip out the card and pay. You don't have to carry large amounts of cash.
- ② Pay on time and it builds up your credit rating

③ Emergencies } If there is a costly repair you may need to use the full credit limit (Pay it back).

④ Rewards programs - points, car rental insurance, extended warranty, price guarantee.

⑤ Record of transactions.

⑥ Use the company's money:
You earn extra interest,
because the credit card company
paid for your item today, but
you don't pay the bill until
the due date.

Example You buy an item for \$2,000 on May 10, you receive your statement June 8 and have a payment due date of June 29. You earn 2% on your savings account. How much interest did you earn if it is simple interest
How much interest did you earn

if it is compounded daily?

Bought May 10, pay June 29
days to earn interest = 50 days

Simple

$$I = prt$$

$$= 2,000 (0.02) \left(\frac{50}{365}\right)$$

$$= \$5.48$$

Compounded

$$A = P \left(1 + \frac{r}{n} \right)^{nt}$$

$$A = 2,000 \left(1 + \frac{0.02}{365} \right)^{365.50}$$

$$A = 2,005.49$$

$$I = A - P$$

$$= 2,005.49 - 2,000.00$$

$$I = 5.49$$

Marlena purchases a dress on a credit card for \$300 on March 15. Her credit card statement arrives on April 15 and she pays the amount due on May 15. How much interest did Marlena earn between her purchase date and payment date if she earned 4.5% interest, compounded daily?

What is the interest earned if this was calculated using simple interest?

61 days

$$\textcircled{a} I = 300(.045) \left(\frac{61}{365} \right)$$

$$= 2.26$$

$$\textcircled{b} A = P \left(1 + \frac{r}{n} \right)^{nt} = 300 \left(1 + \frac{.045}{365} \right)^{\frac{365 \cdot 61}{365}}$$

$$A = 302.26 - 300$$

$$= 2.26$$

Marlena purchases a dress for \$650 on a credit card on May 20. Her credit card statement arrives on July 1 and she pays the amount due on July 31. How much interest did Marlena earn between her purchase date and payment date if she earned 7.5% interest, compounded daily?

What is the interest earned if this was calculated using simple interest?

72 days

$$I = 650(.075) \left(\frac{72}{365} \right)$$

$\$9.62$

$$A = 650 \left(1 + \frac{.075}{365} \right)^{\overset{nt}{\cancel{365} \cdot 72}}$$

$$= 659.69 - 650 = 9.69$$

Consumers should be aware of differences in fraud protection for credit cards and debit cards, Beverly Harzog, credit card expert with Credit.com, said. With credit cards, the maximum liability for fraudulent charges is \$50. If you report the loss or theft of your card before it's used, you're not liable for anything. In most cases, the \$50 is also waived

"The rules for debit cards are different," she said. Harzog said if your debit card is lost or stolen, you have to report this within two business days to limit your liability to \$50. If you don't report it within two days, you can be liable for \$500. But if you don't report an unauthorized transfer within 60 days of receiving the statement showing the fraudulent transfer of money, your losses can be unlimited.

Disadvantages

- ① Don't use as "free" money
- ② Extremely high interest rates if you don't pay on time.
- ③ Hurts credit score if you pay late.

Utilization Rate - it affects credit score.

It is the % of the balance used on each credit card as well as the total of all credit cards.

You have 2 credit cards:

#1 - balance owed is \$3,200
and total credit is \$10,000

Utilization rate = $\frac{\text{balance used}}{\text{credit limit}}$

$$\text{Card \#1} = \frac{3,200}{10,000} = 32\%$$

Card # 2 - used \$1,725
credit limit \$5,500

$$\text{Utilization rate} = \frac{1725}{5,500} = 31.4\%$$

Total

$$\begin{array}{r} \text{card \#1} \quad \text{card \#2} \\ 3,200 + 1,725 \\ \hline 10,000 + 5,500 \end{array} = \frac{4925}{15,500} = 31.8\%$$

Lenders want your utilization rate to be 20% for a positive impact on your credit score. 20% per card as well as total.

FICO Score factors in
order of importance

<u>Factor</u>	<u>weighted</u>
① Payment History	35%
② Utilization Rate (Credit used vs. Credit Limit)	30%
③ Length of credit history	15%
④ # of types of credit	10%
⑤ credit inquiries	10%

Articles:
Win at the credit scoring game
What your credit report says about you.