Students and Credit Cards

Credit cards can be a major source of financial hardship for students.

Unlike student loans, credit card payments are not deferred until after graduation – you are responsible for repaying your debt as soon as it is charged. Since most students have modest income, your only source of money to pay credit card bills may be student loans, other credit cards, or you may even be forced to skip payments and take a blow to your credit score.

So if credit cards are so bad, why not just use cash for everything? To a certain extent, using cash – especially for everyday expenses – is an option you may want to consider. Studies have shown that people spend less overall when using cash as opposed to credit. But at other times, you may not have the cash you need for an emergency situation or you may need to buy an airline ticket or rent a car – each of which is more convenient with a credit card as opposed to a debit card.

Like anything, credit cards can be used for sound and unsound reasons. Using credit for a financial emergency like a car repair far away from home would be a responsible use of credit. But using credit cards for dinners out, gadgets, and entertainment can be risky. As a general rule, if you can eat, drink or wear an item, it's usually not a good use of credit.

Minimum Payment Trap

One of the most common problems people have with credit cards is that they fall into the minimum payment trap – confusing their ability to make the minimum monthly payment with actually repaying their debt. Making just the minimum payment means you may end up paying 3 times more than the amount you originally charged!

Imagine you've charged a total of $2,000 and then stop making new charges. If your card has an interest rate of 19% and a typical minimum repayment policy of 2% of your balance per month, it will take you more than 22 years to pay off the card.

How is that possible? Even though you pay off 2% per month, the amount you owe grows each and every day because of interest – your 2% just pays the interest and a tiny fraction of the principal. By the time you pay off the card making just the minimum payment, the interest charged will be nearly $5,000, making the original $2,000 actually cost you $7,000!

Coupled with much higher interest rates than education loans and the risk to your credit score from even occasional missed payments, and it's easy to see how credit cards could become a serious problem.

Since abusing credit cards can lead to serious financial trouble, should you avoid? Not exactly. There are some benefits associated with credit cards:

- Emergencies. None of us can predict the future, and unanticipated bills are a part of life.
- Consumer protection. Credit cards offer fraud protection that some debit cards may not.
- Convenience. Car rentals and hotel stays are more convenient with a credit card since a "hold" is not placed on funds in your bank account. Some banks also have daily spending limits on debit cards that could be a problem, especially if travelling overseas.

One important point to remember is that *you* are the only one qualified to set your *personal* credit limit, which may be very different than the credit limit on your card. Credit card companies raise the credit limits of those who pay their bill on time, leading some to feel that they can obviously handle more debt because their credit card company says so. Not so fast. Just because you can make the payments does not mean that you're making the best financial decision.

The best level of credit card debt is zero. As a financially responsible adult, you are the one who must say "no thanks" to credit card debt.

College Foundation of North Carolina

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