



# Using credit cards wisely

Crown Financial Ministries New Zealand



Spending on New Zealand issued credit cards was \$42.7 billion in the year to June 2021, with card spending increasing by 58% over the past ten years.

An encouraging aspect of the latest Reserve Bank credit card data is that interest bearing credit card advances outstanding have been declining in New Zealand since April 2019. There was a 7% decline in outstanding advances in the year to May 2021 and the total in May 2021 was 6% lower than in May 2011.

However, the debt owed on credit cards after the monthly payment is due, and the amount of interest paid on the outstanding debt is still significant. In May 2021 interest bearing advances on New Zealanders credit card were \$3.3 billion, while total advances outstanding on credit cards were \$5.9 billion.

The average interest rate on credit card balances was 10.1%, but this includes the interest free balances. The average interest rate on interest bearing advances was 17.7%. That suggests card holders paid around \$590 million in interest in the year to May 2021. In contrast, banks were paying just 0.82% interest on term deposits and even less on general saving accounts.

Credit limits on cards are also declining, reducing by 3.9% to \$22.2 billion in the year to May 2021.

Past research suggests that most people are unconcerned about the high interest rates on credit cards because they intend to pay them off that month. However, additional, and unplanned purchases leave many credit card holders permanently in debt on their card and repayment of outstanding balances is not achieved as planned.

### **Using credit cards**

The following suggestions will help you control the use of credit cards.

- Use only one credit card. Pick a card with an excellent rewards programme, but don't let the rewards influence you to spend more than you need.
- Cancel all other cards.
- Accept a credit limit that you can easily pay in full on your present income each month, and reject all credit limit increases.
- Create a register to keep track of credit card purchases or use internet banking regularly to keep up-to-date with what you are spending and will have to pay at the end of the month.
- Use credit cards only for budgeted purchases.
- Keep in mind that although you can afford to buy something does not mean you have to buy it. Ask yourself if you really need it.
- If you ever fail to pay off the balance, stop using the credit card until you do!

### **Paying the card off on time**

Credit card interest is a waste of money. Pay your credit card off every month during the grace period and you will never have to pay interest charges. You can set up a direct debit from your transactions or savings account each month to pay the full balance on your credit card, but you need to check you have enough money in your bank account to pay the full amount.

One option to consider is to transfer the amount from your transactions account on the same day that you made a charge on your credit card, putting the money into an account specifically for paying for your credit card purchases. You spent the money, so it is no longer money that is available to spend on other things. When the payment is due you will have enough money to pay the card off in full.

### **Can you manage without a credit card?**

It used to be difficult to pay for some goods and services, such as airfares or accommodation, without a credit card. However most businesses now offer alternative payment options on their websites. Now it is possible to pay for purchases directly from your bank account, or using a debit card. If you struggle to pay off your credit card in full you need to consider whether you can manage without a credit card.

### **Conclusion**

Credit cards are a useful financial tool if you can control your spending, but one that carries significant financial risk if spending on the card is not controlled. I use a credit card, but I never fail to pay off my balance at the end of the month, and I never pay late fees. For that, I take advantage of the convenience the card allows, earning airline dollars, and enjoy a period of interest-free money.

Interest accumulates quickly once a balance at the end of the month is not paid in full, so limit purchases to what you know you can fully pay off each month. It is much easier to manage if you have just one card. Credit card companies make money by charging high-interest rates and late fees. Many consumers get trapped in an endless cycle of debt by carrying balances.

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