Advantages and Disadvantages of Credit Cards

What are the advantages and disadvantages of using a credit card?

If you're out shopping, it may be more convenient to carry a credit card to pay for your purchases than it is to carry cash or your checkbook. But that convenience comes at a price. Before you charge out to say "charge it," consider the consequences of doing so.

Convenience versus the potential to overspend

Credit cards are accepted almost everywhere. You can use your card to pay for your groceries, fix your car, pay your tax bill, or handle the co-payment at the doctor's office. Merchants want you to use a credit card because they know they'll be paid by the issuer, and the issuers want you to use your cards because they collect interest on any unpaid balances you carry over from month to month.

Precisely because credit cards are so convenient, there's a risk you might pull them out too often. If you charge every purchase you make and don't pay off your total balance at the end of the month, you may soon discover yourself overwhelmed with debt. With interest charges adding to the burden, you could find it difficult to carry the load you've shouldered.

Low-cost loans versus high-cost fees

If your credit card offers a long grace period (the length of time prior to your minimum payment due date during which you may pay off your account without incurring any interest charges) and carries no annual fee, you can receive an interest-free loan every time you use the card. As long as you pay the entire balance each month before the minimum payment due date, you may be able to go as long as 50 days between charging a nice dinner out and paying for it. A long grace period can be especially helpful if you're sure you'll have the money to pay your balance before the due date.

But if you happen to miscalculate and find that you can't pay off your entire balance by the due date, then the costs associated with your card can suddenly escalate. Transaction fees (particularly for cash advances), late fees (if your payment posts to your account after the due date), and finance charges can make that nice dinner out an expensive mouthful to swallow.

Instant cash versus instant costs

Whether you need money for the down payment on a new car or to buy an antique roll top desk, you could take a cash advance on your credit card to obtain it. Many credit card issuers will allow you to take large cash advances, sometimes up to the amount of your available credit limit. You can usually get a cash advance from many financial institutions. In most cases, you can also get a cash advance from an automated teller machine (ATM), although you may be limited to a daily ATM maximum withdrawal amount, typically $200 to $300.

Instant cash means instant interest, however. Most credit card plans offer no grace period on the repayment of cash advances; the finance charge may be computed from the moment you get the money. In addition, the interest rate levied on cash advances is sometimes several percentage points higher than that charged on purchases, and there's usually an additional transaction fee that may range from a $5 minimum to three percent of the cash advance amount.

Building a positive credit record versus falling deeper in debt

If you have no credit history, using a credit card offers you a convenient opportunity to build one. By making at least your minimum required payments by their due dates, you'll show lenders that you can handle the monthly payment schedules.

Remember, however, that it's not how much you owe but rather how satisfactorily you make your payments that establishes your creditworthiness. New cardholders must be especially careful not to let balances increase beyond their ability to make payments against them. If you're late making payments and/or pay less than the minimum required, you'll undermine your attempts to establish a positive credit record.

Tracking expenses versus managing records

Your credit card issuer tracks your purchases, returns, and payment history. At the end of each (usually monthly) billing cycle, you'll receive a statement containing the relevant information for that cycle. You'll know exactly where you've spent your money, which may help you budget your money. At the end of the year, if you itemize your deductible expenses on your income tax return, these records can also help you locate items you can deduct.

On the other hand, you'll have to do a certain amount of record keeping of your own. You must be prepared to check your statements as they arrive, match your purchase receipts against the amounts listed on the statements, and notify the issuer if you discover errors. If you dispute an item, you'll need to keep track of the status of the dispute until it's resolved.

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