

## PARENT TOPIC 4 MONEY COSTS - CREDIT AND DEBT

# How debt grows

*Partner A has borrowed on the joint credit card to buy a new laptop and the card debt is now at the limit of their card – it has reached \$3,000.*

### **1. What would happen to the amount they owe if they only paid off the monthly minimum payment each month?**

Your card provider sets you a minimum repayment each month on the credit card. This amount is generally only a fraction of your outstanding balance, often as low as 2.5% or \$25 for every \$1,000 owed.

If the couple don't add any more debts to their card. They have to pay

- minimum repayments of 2.5% or \$10 (whichever is the less).
- interest charged from the date of purchase (unless you pay it all off each month)
- interest at 16% per year.

Each month they would be paying 2.5% of the \$3000 they owe – which in the first month would be \$75.

The problem is that each month they would only be paying off a small amount (\$35) of the principal amount they owe, the rest (\$40) goes to pay off the interest on what they owe.

### **2. How long would it take to pay off this credit card debt?**

If they only pay the minimum repayment each month of \$75 and do not add any more purchases to the card, it will take them:

**4 years and 11 months** to repay the debt of \$3,000.

Over that time they will have paid back: the **\$3,000 loan PLUS** a total of **\$1,385.00 in interest**.

Ideally, a credit card account should be paid off in full each month. If that's not realistic, then pay **more** than the minimum repayment and stick to that amount. For example, you would clear the \$3,000 in 2 years by paying a regular \$150 per month.

**Use the credit card calculator on the *MakingCents* website [www.makingcents.com.au](http://www.makingcents.com.au) to work out payments for you.**