



Credit Cards & Rewards

Credit cards are nearly always in high supply. Many companies are happy to create their own credit card and reward system. Consumers are excited to show off credit cards, limits, and brag about rewards.

Is it important to have a credit card(s)? Do rewards really matter that much?

Here's my perspective on Credit Cards and their respective rewards.



Purposes:

1) Build Credit

Credit cards help build your credit over time in various ways. See June Newsletter on building credit.

2) Financial flexibility

Monthly expenses differ month to month. Credit cards allow you to cover a majority of expenses throughout the month without needing to pay for those expenses with your income/savings for 30-60 days.

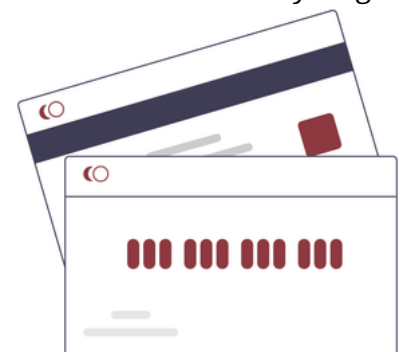
Essentially, you can afford to purchase items now while paying for them later without incurring interest as long as you pay before the end of the grace period.

3) Large Purchases & Short-Term Loans

0% interest credit cards for 12, 15, or even 18 months. If there's an item you need to purchase such as adoption expenses, flights, Christmas, and/or other items then you can purchase it now on the credit card and pay for it a year later without any interest.

4) Rewards:

Most credit cards offer rewards: 1-3%, sometimes 5% or more. Cards also give you 'bonus points' for spending thousands of dollars within a few months. Rewards can lead to hundreds of dollars you get back (normally tax free).



Negatives:

1) Behaviorally

Credit cards give you ease to spend more than you would normally. Credit cards are meant to get people to focus on the short-term buying mentality. You rationalize purchases without even realizing it.

2) Minimum payments

It's easy to make the minimum payment and ignore the interest accruing. Small minimum payments make it easy to forget and ignore the chunk of debt on the credit card. Again, behaviorally credit cards entice you to spend more, make minimum payments, and forget about all the interest accruing that you will have to pay back.

3) Complex reward systems

The reward systems can be complex and lead to spending more money than you normally would. Instead of getting cash back rewards you are enticed to use your rewards for airline tickets, gift cards, or other items. The idea is to get you to spend more money, but feel good doing it because you are using reward points instead of your own credit card balance/savings.

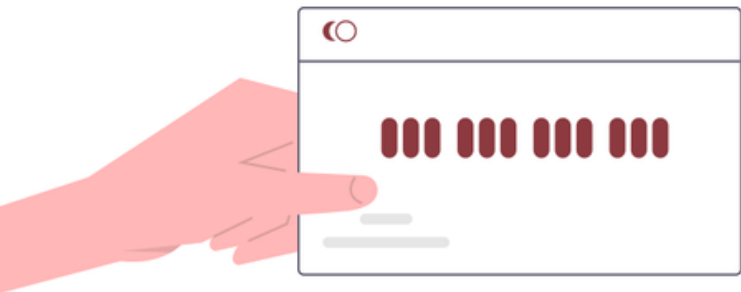
One example is traveling. You see that prices are lower with a different airline or hotel, but because you have a credit card that provides better rewards with a specific airline or hotel, then you are more likely to choose that hotel/airline, even when others are cheaper. This happens often even when the net difference is still more expensive with the airline. Consumers often like the idea of rewards better than a cheaper alternative.

4) Too easy to qualify:

Credit card companies are smart. They send out mail and advertisements to you over and over and over. They qualify you with little to no information. They only require a small minimum payment so you don't have to think about the debt. They give you large lines of credit from \$5k to \$15k to \$20k+.



I recommend setting up an account at NerdWallet to get an idea of your credit score, current credit cards, and the best way to compare credit cards.



Conclusion:

Credit cards can be used responsibly and efficiently to receive rewards. However, even if you never pay interest you may actually be spending more than you should because of what credit cards do to us behaviorally. Rewards create this same type of spending behavior. Taking rewards as cash back may be best for you. Alternatively, if you enjoy the gamification of rewards and like to research and find the best ways to use your rewards then know that you may end up spending more than you normally would. Sometimes that's okay, and sometimes it's not.

Full disclosure:

I have many credit cards and use them for different purposes at different times. I use travel, 0% interest, and other types of credit cards. However, I usually only use one or two credit cards at a time. I do not enjoy keeping track of which one gets me the best rewards at restaurants or gas or online shopping, etc. I almost always use my rewards for cash back. Sometimes I use travel rewards for airline tickets, but rarely do I find it's the best option.

For example, CapitalOne has their own portal to find flights, but often these are a tad more expensive than other sites so the reward redemption does not save me that much and oftentimes is more expensive. I am not an expert on rewards redemption, but I do know I am not interested in spending so much time finding the best rewards.

Attached you'll find the monthly investment article.

Blake Jones, CFP®, EA
Mobile: 385.985.4434
PomegranateFinancial.com
PomegranateFinancial@gmail.com



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