

Name _____

Credit vs. Savings The Reality of Making Minimum Payments

Let's explore a very important credit concept. Buying items on credit is not bad in and of itself. Credit used wisely can increase your credit score. The danger comes from making minimum monthly payments. Just how long does it take to payoff a credit card bill making minimum monthly payments?

Create a spreadsheet to explore the following scenario:

Suppose you decide to buy a \$2000 laptop on a credit card that charges 21% annual interest. You plan to payoff the laptop by making the minimum monthly payment of \$40 each month.

Your friend decides to save the money first and deposits \$40 a month into a savings account with 0.125% monthly interest.

The top of your spreadsheet should look like this:

Credit vs. Savings: How fast can you pay off a credit card bill VS saving the money first?									
Amount charged/ left to pay	Annual Interest Rate	Payment	Interest Paid	Principal Paid	How much is left to pay off	VS	Amount Deposited	Interest Rate	Total In Account
\$2,000.00	21%	\$40.00	\$35.00	\$5.00	\$1,995.00		\$40.00	0.125%	\$40.05
\$1,995.00	21%	\$40.00	\$34.91	\$5.09	\$1,989.91		\$40.00	0.125%	\$80.15
\$1,989.91	21%	\$40.00	\$34.82	\$5.18	\$1,984.74		\$40.00	0.125%	\$120.30
\$1,984.74	21%	\$40.00	\$34.73	\$5.27	\$1,979.47		\$40.00	0.125%	\$160.50
\$1,979.47	21%	\$40.00	\$34.64	\$5.36	\$1,974.11		\$40.00	0.125%	\$200.75

Once you have completed your spreadsheet, use it to answer the questions on the back of this sheet.

1. What is the balance on your credit card after the first year? How much of the original \$2000 have you paid?
2. How much did your friend save in the first year?
3. How long will it take you to payoff the first \$1000 from your credit card?
4. How long will it take your friend to save the first \$1000?
5. Extend your spreadsheet for 10 years – so 120 payments. Have you paid off your credit card balance? Explain. How much has your friend saved in 10 years?
6. What if you double your monthly credit card payment? How long will it take you to payoff the balance now? How does this compare to your friend's \$40-a-month savings plan?
7. Is there a way you could compromise? Develop a plan that would combine savings & credit in such a way that would give you the best of both worlds.