

Credit Card Interest: How it Works

Credit card interest is the fee for borrowing money when a balance remains unpaid on your account. However, if you pay your statement balance in full by the due date each month, you can typically avoid interest charges all together.

Understanding how credit card interest is calculated can help you make informed financial decisions and potentially reduce the amount of interest you pay over time.

What is Credit Card Interest?

Any unpaid balance carried from one billing cycle to the next will be charged a percentage. Interest is based on the card's Annual Percentage Rate (APR), which is usually calculated daily and compounded over time. As a result, interest may accrue not only on your original balance but also on previously charged interest.

Interest Rates vs. APR

For credit cards, the interest rate and APR are generally the same and represent the annual cost of carrying a balance. However, on other types of loans, the APR may also include additional fees and costs.

- **Interest rate:** The percentage charged on an outstanding credit card balance. Most cardholders can avoid interest on purchases by paying their balance in full each month by the due date.
- **APR:** A broader measure of borrowing costs that may include fees on certain loan products. For credit cards, the APR typically reflects only the interest charged on the balance.

Because APR can include additional costs on some financial products, it may be higher than the stated interest rate.



Types of Credit Card Interest

Credit cards often feature variable interest rates and may apply different APRs depending on the transaction type.

- **Variable-rate APRs:** Variable APRs can fluctuate over time based on changes to an index or benchmark rate, such as the prime rate, that lenders use to set rates. The cardholder agreement outlines how and when these changes may occur.
- **Fixed-rate APRs:** Although less common, fixed APRs may still change under certain circumstances. Card issuers are generally required to provide advance notice before making changes.
- **Penalty APRs:** A penalty APR may be applied after repeated late or missed payments. Federal law requires issuers to provide 45 days' notice before imposing a penalty rate.

- **Introductory APRs:** Many credit cards offer promotional introductory APRs for new purchases, balance transfers, or both. These rates often remain in effect for a specified period, providing the account remains in good standing.
- **Cash advance APRs:** Cash advances typically carry a higher APR than standard purchases, and interest often begins accruing immediately.
- **Balance transfer APRs:** A balance transfer APR applies to balances moved from one credit card to another. Some cards offer low or no-interest rates for balance transfers, though fees may apply.

When is Interest Charged?

Interest is generally charged when a balance is carried from one billing cycle to the next. Even if you pay the balance in full later, you may still owe interest that accrued before the payment was received.

Reducing your outstanding balance and paying it off by the due date can help minimize interest charges.

How Credit Card Interest is Calculated

While calculation methods vary slightly by issuer, most credit card companies use the average daily balance method.

To determine interest charges:

1. Divide the APR by 365 to calculate the daily interest rate.
2. Multiply the daily interest rate by your average daily balance.
3. Multiply that amount by the number of days in the billing cycle.

The formula is:

Average Daily Balance x Daily Interest Rate x
Number of Days in the Billing Cycle

How to Avoid Paying Credit Card Interest

Pay Your Balance in Full Each Month

Paying your statement balance in full by the due date is the most effective way to avoid interest charges.

If paying the full balance is not possible, make the largest payment you can. Try to at least meet the minimum payment required.

Make Payments Early or More Frequently

You do not need to wait until the due date to make a payment. Paying earlier or making multiple payments throughout the month can help reduce the average daily balance used to calculate interest.

Setting up automatic payments can also help ensure payments are made on time.

Consider a 0% Introductory APR Card

If you need to open a new credit card to make a large purchase or consolidate debt, consider a credit card with a 0% introductory rate.

This will help reduce interest costs during that promotional period. It is important to understand when the introductory rates expire and what the rate will be afterwards.

Take Advantage of the Grace Period

Most credit cards offer a grace period between the end of your billing cycle and your payment due date. Paying your statement balance in full during this period can help you avoid interest charges on purchases.

APCI Federal Credit Union & You

APCI Federal Credit Union offers members our **Mastercard® Plus card** at a great rate, with no annual, balance transfer, cash advance, or late fees. Cardholders earn points for cash back, gift cards, merchandise and travel awards with CURewards®. A **secured credit card** option is also available.