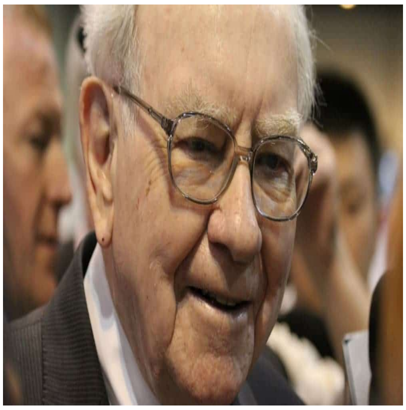

Should You Listen to Warren Buffett's Tip on Credit Cards?

Description

Warren Buffett quotes have become almost as profuse and culturally popular as Bible verses. In fact, when you read words such as, "Risk comes from not knowing what you are doing," and, "Price is what you pay, value is what you get," you almost feel as if you're listening to the wise King Solomon himself, scribing the Proverbs with a knack for practical wisdom.

So, when it comes to credit cards, you might expect Buffett to have a wise turn of phrase or two. In truth, he has said very little. The Oracle of Omaha has only one quote attached to his name, and it was spoken almost two decades ago during a speech to high school students in Omaha.

"Avoid credit cards," he said, "just forget about them."

Should you listen to Warren Buffett's advice on credit cards?

First off, let's clear the air. The great Oracle himself has admitted to owning a credit card, an American Express card in fact. In fact, as the years have passed, it seems Buffett left off an important word in his credit card statement. "Avoid," he should have said, "credit card *debt.*"

In this regard, Buffett is indisputably right. Credit card debt is one of the most ferocious kinds of debt out there. With APRs that range from 15% to 30%, credit card interest can easily become a ball and chain, forcing you to pay more toward interest, distracting you from paying off the principal.

As Buffett himself has pointed out, unpaid credit card balances work like an investment in reverse. In the same way that investments grow by compound interest, credit debt is compounded by APR. On day one, you accrue interest on your unpaid balance. On day two, you accrue interest on your unpaid balance *plus* the interest you accrued the day before. This interest accumulation continues until you finally pay the balance in full.

So, are credit cards bad?

If you're the kind of person who regularly carries a balance on your card, meaning you don't pay your statement balance before its due date, listen to the Oracle. Avoid credit cards. For those who can pay off their charges, a credit card won't throw you in a pit of debt. In fact, they can be an effective tool that gives your budget an extra bit of muscle.

Many credit cards — even the most basic ones — come with a slew of coverages and insurances: fraud protection, rental car insurance, travel insurance, medical coverage, price protection, and extended warranties. To be clear, these are built into the credit card. When you purchase items with your credit card, say, a new sofa from IKEA, you'll automatically get an extended warranty, if your card has that feature.

Additionally, rewards credit cards and cashback cards give you the opportunity to earn money while you spend. If you use these cards like a debit card, meaning you spend only what you have — you can amass rewards without going into debt.

Canadians with bad credit need not fear credit cards, either. If you want to rebuild your credit score, you can benefit from a secured credit card. A secured credit card works like a normal credit card, except you put up an initial deposit to use it. As long as you use the secured credit card responsibly, you may slowly but surely improve your score.

At the very least, you could go with a "plan B" card, the balance transfer credit card. If you amass too much credit card debt, these cards offer low intro APR periods to help you get back on track.

The Oracle may not have said very much on credit cards. But truthfully he doesn't need to. If you know how a credit card works, as well as how to use one to your advantage, you can avoid the pitfalls and benefit directly from a credit card's perks and rewards.

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