



22% of Canadians Switched to a No-Fee Credit Card: Smart Move or Big Mistake?

Description

Wanna pay an annual fee to use a credit card? According to a survey by J.D. Power, around one in five Canadians (22%) are saying, “no thanks.”

According to J.D.’s 2021 Canada Credit Card Satisfaction Study, 22% of Canadians switched from a card with annual fees to a no-fee credit card in the last year and a half — and they’re feeling pretty good about it. Credit cardholders gave their credit card providers a collective 766 satisfaction score (out of 1,000), a whole two points higher than last year’s score (764).

Of course, this makes sense. After all, the pandemic caused many to tighten up their budgets and cut discretionary spending, including credit cards with annual fees.

But now that the country is opening up, many Canadians may want to switch back to those annual fee credit cards. It may seem counterintuitive, but, in some cases, a card with *no* fee can actually cost Canadians more than a card with fees. And it all comes down to one thing: credit card rewards.

When paying an annual fee is worth it

The number one reason to pay an annual fee for a credit card is to maximize your rewards. Many cards with annual fees come with higher earn rates: more cash back, travel miles, and rewards points per dollar spent. If you spend enough, the rewards that you earn will outweigh the annual fee.

But that’s the trick. You have to earn more than the annual fee itself.

For instance, let’s say you get a credit card with an annual fee, let’s call it Card A. This card offers 5% cash back on all grocery purchases with an annual fee of \$120. In order for Card A to be worth its cost, you’d have to spend at least \$2,400. At \$2,400, you earn \$120 in cash back, and you’ll break even.

But don't stop there. In order to see if the card is *truly* worth it, you must compare it with a card that doesn't offer an annual fee.

So, let's say, in addition to Card A, you're also looking at Card B. Card B has no annual fee and an earn rate of 2%. If you spend \$2,400 on Card B, you'll earn \$48. Because you don't pay an annual fee, you can consider that \$48 a profit.

At what point does Card A become more profitable than the no-fee Card B? The answer here is \$4,000. At \$4,000, you'll earn \$80 in cash back on Card B. On Card A, with the higher earn rate of 5%, you'll earn \$200. If we factor in the \$120 annual fee, then you'll pocket \$80 on Card A, making it equal with its no-fee counterpart.

So, if you know you'll spend more than \$4,000, then, in this situation, Card A is worth it.

Another reason to get a card with an annual fee is to secure a lucrative welcome bonus. Many cards with annual fees come with hefty bonuses that will more than pay for the fee itself. If the bonus pays for the fee, and you know you can meet the requirements to get that bonus, by all means — get the card. You'll more than likely have a higher earn rate, and you can “test drive” the card for the first year.

When an annual fee is a bad idea

For one, if you're on a budget, I would stick to a card with no fee. A card with an annual fee might tempt you to spend more than you can afford, especially if you're trying to make the card worth the cost.

Secondly, I'd avoid cards with annual fees if you regularly carry a balance on a credit card. When you carry a balance on your card, meaning you don't pay your balance in full and on time for a billing cycle, you'll incur interest. Since the interest rates on credit cards can be extremely high (from 19.99% to 30%), you could easily find yourself accumulating more interest charges than any rewards program could ever help you earn.

Finally, if you're happy with your no-fee card, then maybe a card with an annual fee isn't worth it. Of course, I would do the math just to be sure. If a card with an annual fee helps you earn more rewards, it might be worth biting the bullet and paying the fee.

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