What the Fed raising rates would mean for your credit cards and bank accounts

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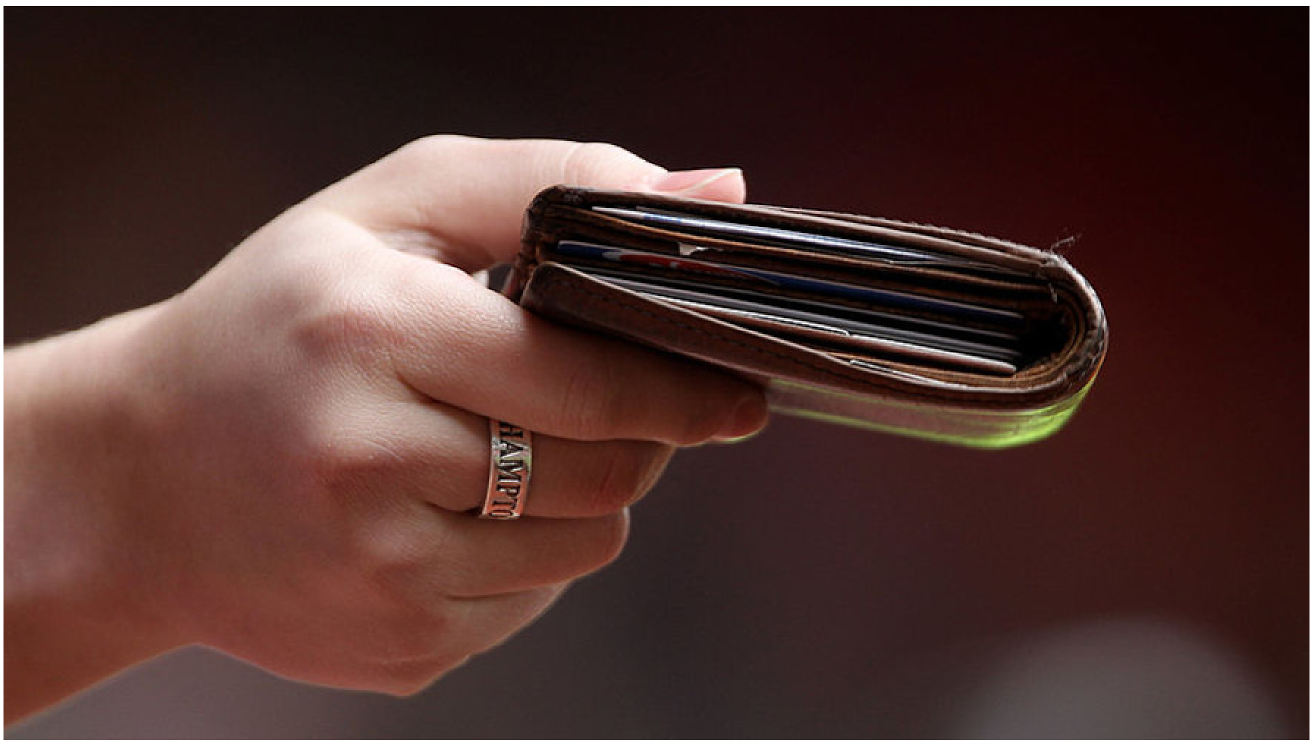
By

MariaLaMagna

Reporter



Phil Cole/Getty Images
The Fed is expected to announce a rate hike on Wednesday.

A major decision by the Federal Reserve this week could impact your wallet very soon.

The Fed began a two-day policy meeting Tuesday and is expected on Wednesday to announce an increase in the target range for its federal funds rate to between 0.5% and 0.75%. (In other words, the Fed is expected to announce an increase in how much banks will be charged to borrow money from Federal Reserve banks. The Fed raises and lowers interest rates in an attempt to control inflation.)

For everyday consumers, a rise in the federal funds rate has numerous effects; experts are expecting the dollar to strengthen, for example, as a result.

“Any money that is saved is going to be more valuable, and any debt outstanding will be more expensive,” said Sean McQuay, a personal finance and credit cards expert at the personal finance company NerdWallet.

Here’s how a rise in rates will affect your credit cards and savings account.

Credit cards

Because a rise in the federal funds rate means banks will likely pay more to borrow from the Federal Reserve, they may pass that cost on to consumers.

Credit card interest rates are variable (banks and credit card companies should state that their rates are variable in the literature customers receive to learn about their cards), and they are tied to the prime rate, an index a few percentage points above the federal funds rate. It is a benchmark that banks use to set home equity lines of credit and credit card rates; as federal funds rates rise, the prime rate does, too.

As a result, credit card holders are likely to see their interest rates rise, and that will happen soon, said Greg McBride, the chief financial analyst at the personal finance company Bankrate.

When the Fed raised the rate in 2015 — the first rate hike since 2006 — it only took about a month or two for the majority of banks that the personal finance website NerdWallet works with to change the variable APRs on their credit cards, McQuay said. They included both major banks and lesser-known ones.

What’s more: Banks are under no obligation to let their customers know they are raising their credit card rates when the Fed announces an interest-rate increase, so consumers should check on their own to find out if their rates are rising, McQuay said.

The average household now pays a total of $1,292 in credit card interest per year, according to NerdWallet’s research. If the Federal Reserve does increase its rates as analysts have expected it will do, the total will rise to $1,309, NerdWallet found. Although that amount won’t “break the bank,” McQuay said, consumers who have debt should expect this trend of rising interest rates to continue.

People who currently have credit card debt should consider trying to refinance or consolidate it now, or find a lower-interest rate card they can transfer their existing balances to, said Rachel Podnos, an attorney and financial planner based in Washington, D.C.

Many balance transfer cards have 0% introductory interest rates, McQuay said. Banks and credit card companies will likely keep those rates at 0% rather than raise them to slightly over 0%, because offering that 0% introductory rate is helpful for marketing. However, because the banks will be paying more to borrow, they may eventually shorten the introductory period if they are unable to afford that 0% for the long periods of time they offer now. As a result, securing one of these cards sooner rather than later would be a good idea.

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Bank accounts

For savers, a rise in Federal Reserve interest rates is good news, Podnos said.

Savings account rates will likely increase slightly, which should help consumers, especially since interest rates on savings accounts are at historic lows. (Although consumers shouldn't expect those rates to rise much, McBride said; banks will likely have to collect extra income from borrowers before being able to pass those funds onto the savers, he said.)

Still, this is a good time for people who keep their liquid savings in a savings account to make sure they are getting the maximum savings rate available to them, he said.

Bankrate and NerdWallet compile lists of the highest-yielding savings accounts.

On NerdWallet's list, the best savings rates were 1.1% at Salem Five Direct, an online division of Salem Five Bank, based in Salem, Mass., 1.05% at Synchrony Bank, based in Stamford, Conn., and 1% at an online savings account at Ally Bank, based in New York. None of these had a required minimum deposit.

Bankrate's list also includes money market accounts.

Podnos said consumers should make sure they are putting their money in bank accounts that are federally insured.

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