How to understand special promotional financing offers on credit cards

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CREDIT CARD TERMS

How do you tell the difference between a zero interest and deferred, or "no" interest credit card offer?

Look for the "if." Zero interest offers use language like "0% intro APR on purchases for 12 months."

Deferred interest offers use language like "No interest if paid in full within 12 months." The "if" means you could end up paying more than you expected.

Many retailers offer special promotional financing for big purchases through deferred interest offers. These offers promise people that they won't be charged interest during a promotional period, if they pay their promotional balance in full by the end of the period. Consumers may find the costs of deferred interest less transparent.

Recently, a major U.S. retailer announced it will no longer offer deferred-interest promotions on its store credit card. Instead, it will offer a promotional period with zero percent interest.

With this zero-interest approach, you don't accrue interest charges during the promotional period even if you don't pay off your balance by the end of the promotional period.

Though deferred interest and zero interest may seem similar, the differences can have big effects on your wallet.

Here's how these promotions work, and the key differences between them.

The difference between zero interest and deferred interest promotions

A zero percent interest promotion will not add interest based on the balance of your promotional purchase during the promotional period. Even if you still have an unpaid balance when the promotional period is over, you will start to pay interest on **that remaining balance only** from **the date the promotional period ends**. This promotion may also require you to meet other terms as well, such as making your minimum monthly payments on time. You may see a phrase like, "0% intro APR for 12 months," to describe this type of promotion.

In contrast, you might have seen retailers offering credit cards with advertisements like, "No interest if paid in full in 12 months." Watch out for the "if." That means the promotion is a deferred interest offer. Deferred interest means that if you do not pay off the **entire balance** of the promotional purchase you've made on your card, then interest going back to **the date of the purchase** will be added on top of the remaining balance. This promotion may also require you to meet other terms as well, such as making your minimum monthly payments on time.

Let's break this down. This chart shows you the difference between the two types of credit card offers.

Here's an example based on buying a $400 TV with a card that has one of these two promotions. In this example you make your payments on time but don't pay off the whole balance during the promotional period.

Please note the following calculation is just an example. An actual billing statement might be slightly different.

Promotional offer

ZERO PERCENT INTEREST PROMOTION
0% for 12 months

DEFERRED INTEREST PROMOTION
No interest if paid in full in 12 months

Purchase amount

ZERO PERCENT INTEREST PROMOTION
$400

DEFERRED INTEREST PROMOTION
$400

What you pay off during the promotional period (assume payment of $25 per month)

ZERO PERCENT INTEREST PROMOTION
$300

DEFERRED INTEREST PROMOTION
$300

Remaining principal balance after promo ends

ZERO PERCENT INTEREST PROMOTION
$100

DEFERRED INTEREST PROMOTION
$100

Interest rate during the promotional period

ZERO PERCENT INTEREST PROMOTION
0%

DEFERRED INTEREST PROMOTION
25%

Accrued interest during the first 12 months

ZERO PERCENT INTEREST PROMOTION
$0

DEFERRED INTEREST PROMOTION
$65

Interest rate starting after the promotional period

ZERO PERCENT INTEREST PROMOTION
25%

DEFERRED INTEREST PROMOTION
25%

Amount you owe at the end of the promotional period

ZERO PERCENT INTEREST PROMOTION
$100

DEFERRED INTEREST PROMOTION
$165

At the end of the promotional period, you've only paid $300 of the $400 purchase price for the TV. That means that after 12 months you still owe $100 to finish paying for the TV itself.

If you bought the TV using a card with the zero interest promotion, you will owe $100 after the promotional period ends. You will start paying interest only on what you still owe, and pay at the annual interest rate in your contract.

If you bought the TV using a card with the deferred interest promotion, you will owe $165 after the promotional period ends - $100 on the TV itself and another $65 in interest charges. This is because your interest was only deferred. Since you didn't pay off the balance by the end of the promotional period, the credit card company will charge you the $65 interest that had been accruing during the promotional period. You will also start paying interest on what you still owe including the $65 interest charge at the annual interest rate in your contract.

How deferred interest is calculated

To get to the $65 interest charge in the example above, the credit card company will add up the interest charges from the previous 12 months. Here is how we did the math in our example:

1. In the first month, after you purchase the TV, you paid for $25 of the TV.
2. The credit card lender subtracts your payment from the $400 total borrowed and records the interest charge, roughly $8. But, this interest is not charged yet.
3. The next month, you pay another $25 towards the balance on the TV.
4. This next payment is subtracted from the total and the interest that is being deferred is recorded again, this time roughly $7. Again, this interest is not charged yet.
5. You continue to pay the $25 towards the purchase each billing cycle, each month.
6. After the 12-month promotional period ends, you still haven't paid off the original price of the TV, which was $400. So all the charges that were recorded and not yet charged are now added together to get the interest you owe for the promotional period. That interest charge is added to the amount you still owe on your purchase.

What to consider when getting a card with a zero interest or deferred interest promotion

A zero interest promotion doesn't add interest retroactively if the entire promotional purchase balance isn't paid off. But, there are still some important things to consider for both zero interest promotions and deferred interest promotions:

- **You are still borrowing money:** Remember, even if the interest rate is zero or deferred and you get the deferral, you are still borrowing money that you have to repay.
- **The length of the promotional period:** Make sure you understand how long the promotional period lasts. Some credit card companies vary the length of time of these periods based on the amount of your purchase.
- **You will have a higher interest rate after the promotional period:** Know what the interest rate will be after the promotional period ends. A promotional rate is usually lower than the usual rate on the card. Store credit cards normally carry a much higher rate than a typical bank credit card.
- **The terms and conditions:** Read the credit card agreement terms and conditions. For example, some zero interest offers only apply to purchases above a certain amount. Understanding these terms and conditions keeps you in control of how much you will actually pay when you use the card.
- **What you'll have to pay each month to pay off your purchase during the promotional period:** If you're using the card to avoid paying interest on a purchase, figure out how much you will need to pay each month to pay off the promotional balance before the promotional period ends. *The minimum payment due is usually not enough to pay off the balance by the end of the period*.
- **How other purchases on your card may affect the promotion:** If you have other balances on the card that do not have deferred interest, any amount above your minimum payment will usually be applied to the balance with the higher interest rate. If you want your extra payments to go toward your promotional balance so that you can pay it off within the promotional time period, you can ask your credit card company to apply anything you pay above the minimum monthly payment amount to your deferred interest balance.

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