THE WALL STREET JOURNAL.

Why a Fed Rate Cut Might Not Offer Much Relief on Credit-Card Bills

By Angel Au-Yeung, Reporter

Credit-card interest rates are at their highest levels in at least 10 years. (Klaus Vedfelt/Getty Images)

Credit-card interest rates are at around their highest levels in at least a decade. So the Federal Reserve's expected rate cut should help lower bills, right?

Not necessarily.

The average annual percentage rate, or APR, on credit cards as of May was 21.5%, according to Fed data, up from around 15% in 2019.

The Fed's cut could bring moderate relief for cardholders, "but it's not going to be a windfall," said Charlie Wise, senior vice president of research and consulting at TransUnion, a credit-reporting agency.

The average credit-card balance in the second quarter was about $6,300, up from $5,270 two years earlier, according to a TransUnion report. If the Fed cuts its benchmark rate by a quarter to half a percentage point, that would amount to interest savings of around $2 to $4 monthly, said Wise.

There’s no guarantee a cardholder’s rate will come down at all, however. That’s because interest rates on cards consist of two factors.

The first is the prime rate, which is pegged to the federal-funds rate and is currently around 8.5%, Wise said. If the Fed cuts rates by a quarter-percentage point, the prime rate would go down to 8.25%.

But the second factor is the interest that card issuers charge on top of that.

That extra interest, known as the APR margin, reached 14.3% in 2023, the highest level in the past decade, according to a February report from the Consumer Financial Protection Bureau. The increases on APR margins have outpaced the prime rate’s changes, according to the agency.

The American Bankers Association has said higher margins reflect the growing number of subprime cardholders issuers have served. The industry group said that helps cover the risks of providing credit access to those consumers.

The truth is likely somewhere in the middle, said Jim McCarthy, former senior adviser to the CFPB and chairman of a consulting firm. “The cost of doing business is going up, and at the same time it’s becoming more lucrative and people are willing to pay for the service,” he said.

The Fed is expected to announce more rate cuts in coming months. But even so, an easing of people’s credit-card rates isn’t guaranteed, said McCarthy. The federal-funds rate is just one of many factors that card issuers take into account in setting rates.

“Gone are the days when we can draw a direct correlation,” he said.