5.3 Suggested Responses: Economist as Life Coach (Thinking About Credit Like an Economist)

Economist as Life Coach

What recommendations would an economist offer? Explain your answer using at least one of the principles of economic thinking.

1. Yara got into her dream school. Scholarships and grants will cover tuition and books, but not housing or meals. She's considering a $7,000 federal student loan to live on campus and avoid a long commute.

Cost-benefit principle: *An economist might recommend Yara take the loan if the benefits of living on campus outweigh the costs. Living closer could save her time and stress, and possibly help her focus more on academics. She should consider not just the financial cost of the loan but also the potential benefits, like better grades, stronger friendships, and more time for studying or campus jobs.*

2. Camila sees a new gaming laptop on sale for $900. She has $300 saved but considers putting the rest on a credit card. She doesn't have a job yet, but says she'll "figure it out."

Opportunity cost principle: *An economist would probably caution Camila against using a credit card without a plan to repay. She may have to give up future opportunities to pay off the $600 balance plus interest. The true cost isn't just the $600 borrowing along with interest payments, but also what else she could've done with the future income she'll use to pay for the laptop.*

3. Arjun has built good credit. He now qualifies for an unsecured rewards card. The credit card offers 2% cash back but comes with a $95 annual fee.

Cost-benefit principle and interdependence principle: *An economist might say Arjun should weigh the benefits of the 2% cash back against the $95 annual fee. If he expects to spend more than $4,750 over the year and pay the balance off each month, then the benefits of the cash back (2% of $4,750 = $95) would cover the cost of the fee, so any additional spending earns him net rewards. If he expects to spend less than $4,750 or he can't always pay the balance in full, the benefits might not outweigh the cost.*

4. Bassey is offered a private student loan with a lower interest rate than a federal loan. But the private loan doesn't offer flexible repayment or forgiveness options.

Opportunity cost principle: *An economist may warn Bassey to consider not just the interest rate, but also what he gives up with the private loan, like repayment flexibility and forgiveness options. The lower rate looks cheaper, but the true cost may be higher if he loses access to safety nets federal loans offer.*
Interdependence principle: *An economist would also point out that Bassey's expectations about his future employment and future interest rates will likely influence his decision. If Bassey expects that it will be easy to find a job that allows him to make his loan payments monthly, then the flexible repayment options will be less important in his decision making*

5. Chen has paid the minimum on his credit card for the past year. He wants to buy a concert ticket for $250, but still has a credit card balance of $400. He plans to pay it off "sometime next year."

Marginal Principal: *An economist would likely advise Chen to avoid adding more debt before paying off the balance on his credit card. Charging "just one more thing" may seem small, but over time, each extra purchase adds up and becomes harder to pay off as interest compounds.*
*I**nterdependence Principle**: An economist might say Chen ought to purchase the ticket if he expects to receive a raise in the very near future. But he should keep in mind that things may happen in the future that would prevent him from paying off his balance on his intended timeline (like an emergency or unexpected expense). If he doesn't expect a raise, he shouldn't add more debt until he pays off his current balance.*