FGB FINANCIAL FOUNDATIONS

• *Financial Education for Everyone* •

CREDIT

WHAT IS CREDIT?

Credit is the ability to borrow money or access goods/services with the understanding that you'll pay later. Your credit is your reputation as a borrower, it determines how likely you are to repay your debt.

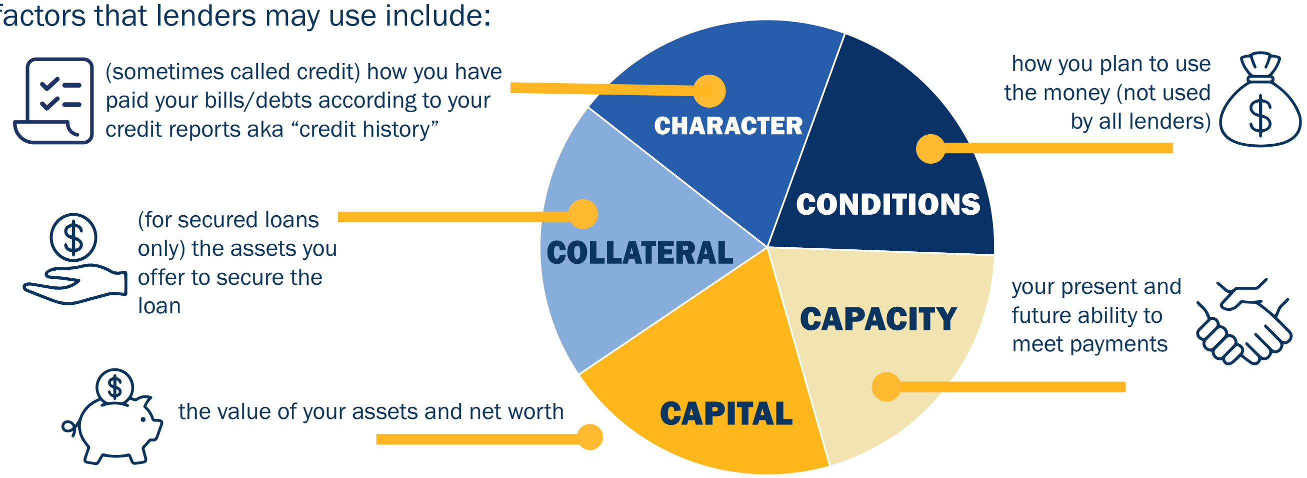
Lenders, banks, merchants, and service providers (aka creditors) grant credit based on their confidence you can be trusted to pay back what you borrowed.

WHY IS CREDIT IMPORTANT?

Good credit is necessary and important if you plan to borrow money for major purchases, such as a car or a home. You'll need to prove to lenders that you can handle your financial obligations.

THE FIVE C'S OF CREDIT

It's important to remember that methods and factors may vary by lender, but typically, a lender will determine whether you're a good credit risk (aka how likely you are to pay the loan back, as agreed) A few key factors that lenders may use include:



Tip: According to Investopedia, some consider the criteria that lenders use as the four Cs. Conditions are sometimes excluded to emphasize the criteria most in control by the borrower.

Notes:

THE IMPACT OF CREDIT

Credit Can Affect Your Lifestyle

While you may not currently be in the market for a house, your credit score and history is still important. Landlords use your credit to decide whether to rent to you. After all, property rental is a loan, and owners want to be sure they will be paid back.

Before you can buy a house, mortgage lenders want to know that you won't default (not pay) on your mortgage. If you do not have good credit, the lender will consider it risky to offer you a mortgage loan.

If you're approved for a mortgage, your credit affects your interest rate and interest rates directly impact your monthly mortgage payment. Companies may use your credit scores as a factor in determining your home insurance rates.

Bad Credit = Higher Interest Rates = Higher Payments

Utilities

While unexpected, utility companies may check your credit **before opening an account or borrowing equipment.** Electric companies technically state that you're borrowing one month of electric service. Before turning on your electricity, the company will check to see if you have good credit. Most utility services conduct credit checks, including cable, telephone, water, even cell phone service providers.

Employment

Prospective employers may use information found in credit reports to make a hiring decision. Your credit report can even be used to verify your identity, and for other purposes defined by federal law. Many employers conduct credit checks as part of the hiring process.

Employers can check credit reports, not credit scores. Employers and landlords typically cannot access your credit report without your written permission.

Personal/Business Loans

If you're dreaming of starting your own business, or need a personal loan, you'll need to have good credit in order to qualify for either type of loan.

Notes:

CREDIT BUREAUS

Credit bureaus are the companies that collect and maintain consumer credit information from lenders for credit cards, mortgages, and other types of loans. Lenders regularly report whether you're paying your bills on time, whether you've ever defaulted on your loans, and how much debt you owe to them. The credit bureaus also pull relevant public records, like tax liens or bankruptcy information, from state and local courts. This information is included in your credit report.

There are 3 Major Credit Reporting Agencies: **Equifax · Experian · TransUnion**

WHAT IS A FICO SCORE?

A FICO Score is a three-digit number based on the information in your credit reports. It helps lenders determine how likely you are to repay a loan. Typically, FICO scores range from 300-850 and can be classified as follows:

- Exceptional (800-850)
- Very Good (740-799)
- Good (670-739)
- Fair (580-669)
- Poor (300-579)

The higher your credit score, the more likely you are to qualify for credit, rental housing, insurance, etc. Basically, your credit score determines IF you'll be able to borrow money and how much it will cost you in interest.

LATE PAYMENTS

- To avoid late payments, set up automatic payments and due date alerts

- There are **30,60, and 90-day** late payments

- Lenders may not report late payments until 30 days past due, but some may send your account to a collection agency if you are 60+ days past due

- Late payments will stay on your credit report for 7 years

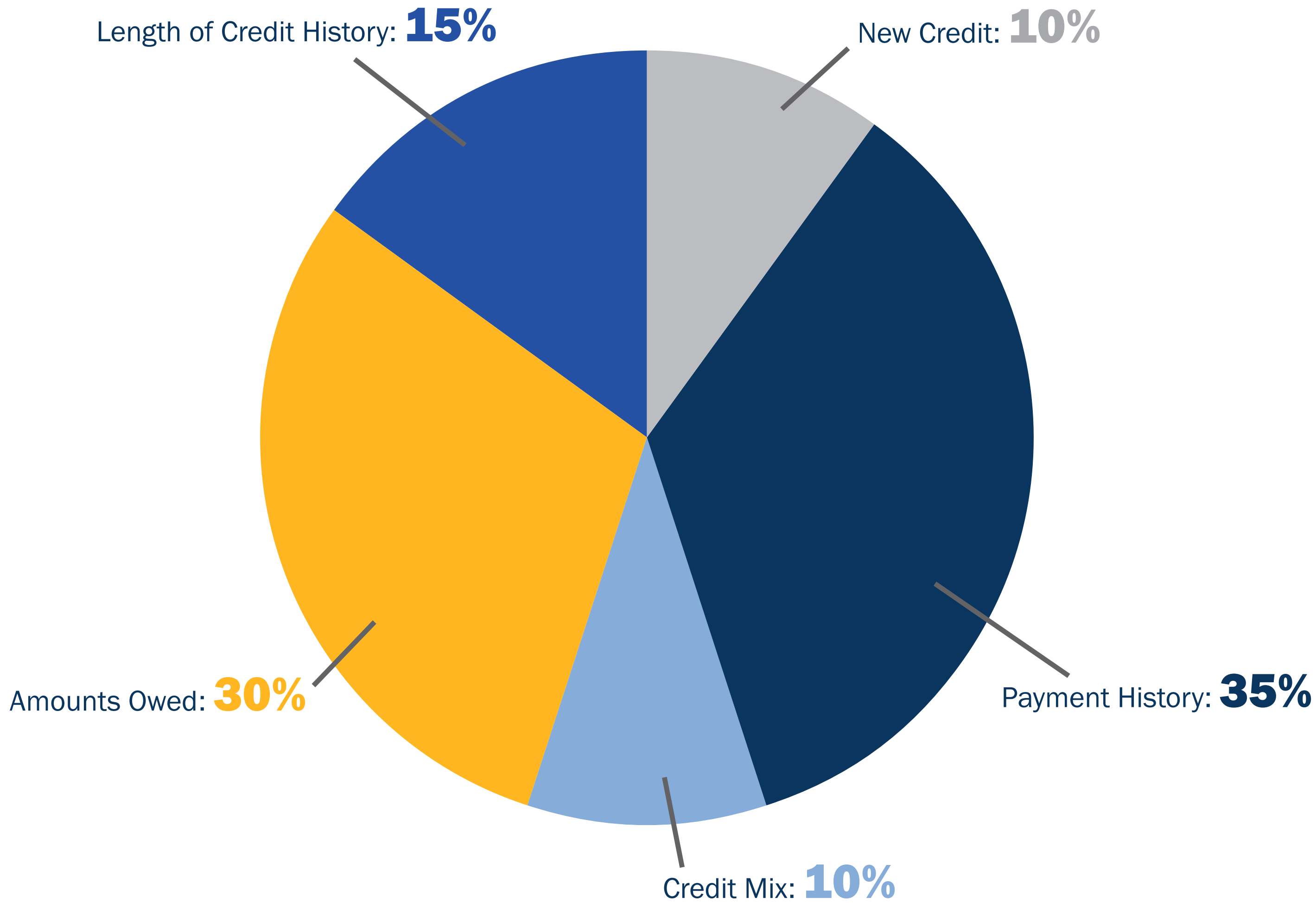
- If you're past due your due date but pay it before the 30-day period, you should not be affected; however, late fees may apply

- If you are struggling with late payments, consider changing your due date

Avoid late payments!

Notes:

THE FIVE THINGS THAT MAKE UP YOUR CREDIT SCORE



1. **Payment History:** Helps a lender determine the risk it will take when extending credit and the MOST important factor in a FICO score.

2. **Amounts Owed:** Owing money doesn't necessarily mean that you're a high-risk borrower, but if you're using a lot (or most of) your available credit banks could interpret this to mean that you are at a higher risk of defaulting.

3. **Length of Credit History:** This includes how long your credit accounts have been established, the age of your oldest account, age of your newest account, etc.

4. **Credit Mix:** Includes the different types of accounts you have (example: credit cards, retail accounts, installment loans, mortgage loan, etc.)

5. **New Credit:** Typically, opening several credit accounts in a short amount of time represents a greater risk.

WHAT DOES APR MEAN?

Annual Percentage Rate (APR) is the cost of your loan as a yearly rate. The APR helps you compare loans and other credit card rates.

Fixed vs Variable APRs

There are two main types of APR, fixed and variable. If you prefer predictability, a fixed APR may be for you because the interest rate is set at the beginning of the loan and does not change.

In the case of a variable APR, the interest rate is benchmarked to the prime rate, which can change over time. As the interest rate changes, whether up or down, the APR fluctuates.

Prime Rate

According to Investopedia, prime rate is the most commonly used benchmark used by banks and lenders when setting interest rates for loans and credit cards.

Most credit cards have a variable APR that stays above the prime rate and is based on the cardholder's personal credit history. Generally, the higher a cardholder's credit score, the lower the interest rate they'll receive.

FIVE THINGS TO KNOW BEFORE GETTING A CREDIT CARD

Adapted from AskMoney[1]

Credit cards can seem simple, but minor decisions can have a big impact on your credit profile. Set yourself up for success by knowing these five things BEFORE getting a credit card.

1. Check rates and fees in advance
2. Avoid fees, interest, and late payments, if possible
3. Avoid using your full credit limit
4. Pay more than the minimum balance each month
5. Know how to navigate credit card fraud

[1]McDonald, Tamila. Ask Money. 2022. www.askmoney.com/credit-cards/tips-before-credit-card. Accessed 1. May. 2023.

Notes: