

What Is Credit? Why Is It Important?

What is Credit?

- An arrangement that allows you to make purchases now with the understanding that you will repay the amount later
- The amount you repay may often come with interest
- A way to build financial power by establishing *creditworthiness* – your ability to pay what you have borrowed

Types of Credit

- **Revolving Credit** – A line of credit issued as a credit card with a set spending limit. One may use as much or as little available. Payments can be made in full or in part each month. Amounts that carry over into the following month may be charged interest
- **Installment Credit** – A line of credit issued as a loan for a specific purchase which may be paid back in steady increments over time. For instance, student loans, a car loan and house mortgages are considered installment credit
- **Service Credit** – A line of credit outlined in a contract established between you and a service provider. The service provider offers services under terms you agree to pay them. Examples include electric bill and cell phone plan

Ways That Credit Gets Used

- **Personal Loans** – lenders may determine whether to approve a loan and if so, set a spending limit, interest rate and fees associated with the loan
- **Student Loans** – if requesting a loan from a private lender, they will check your credit history to determine how much to lend you, interest rates, etc.
- **New Job** – depending on the role, an employer may review your credit report before offering you the position
- **Apartment** – landlords may request a credit report to determine whether they will allow you to rent their apartment
- **Homeownership** – banks and lending institutions may request a credit report to determine the size of the loan, interest rate and mortgage payments
- **Car** – banks and car companies will use your credit history to determine whether to grant you a car loan and for how much
- **Insurance** – insurance companies will review your credit history when applying for many types of insurance such as, car and homeowners' insurance

Important Note: Information presented is gathered through a combination of public resources and not put together by an official financial/insurance advisor. Information provided are meant to serve as nothing more than suggestions and left to the reader's discretion.

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The Following Can Cause a Negative Impact On Your Credit

- Not making regular payments on time or the inability to fully pay the minimum payment amount can lead to ***Bad Credit***
- Bad Credit can be reflected on your credit report which outlines your financial history and used by lenders to determine loan approvals
- Late ***payments, foreclosures and collections*** will stay on your credit report for **7 years** while ***bankruptcies*** will stay on your credit report for **10 years**

How To Get Started with Building & Maintaining Good Credit

- ❖ If you don't have credit (or no loans) consider,
 - Becoming an ***authorized user*** on an account of a family member
 - Opening a student credit card account, check out NerdWallet's [*Best College Student Credit Cards of January 2023*](#)
 - Applying for a ***secured card*** which requires that one pay a deposit and after you've established history of paying on time, you can look into upgrading to an unsecured card
 - Applying for a ***credit-builder loan*** also known as, a ***reverse loan*** where you make payments for a designated amount that gets placed in a savings account and the funds become available to you at the end of the loan period
- ❖ If you have credit (a loan or service under your name) consider,
 - Start and/or continue to make payments on time
 - Pay ***at least the minimum amount*** given to avoid a late fee plus a penalty on your credit report
 - It's recommended that credit card usage remains below 30% of your credit limit
 - Designate a card to keep open over time even if it's no longer used as often. Credit history takes into account your average account age
 - Be mindful of how many credit lines you open; lenders may choose not to loan you money if you have too many credit lines open
 - **If you have multiple accounts open**, prioritize paying off the account with the highest interest rate first by paying a little more than the minimum amount each month

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Credit History & Reports

- A record of how someone manages money and debt which outlines one's loans and credit card accounts
- Lenders report details about your account activity to the three major companies also known as **credit bureaus** who track of credit history: Equifax®, Experian® and TransUnion®
- The reports are used to calculate one's credit score which are used by lenders to evaluate a loan or credit applicant's creditworthiness

Credit Score Ranges

- General credit score range can be from 300 – 850 but some credit-scoring companies may do 250 – 900
- Scores are calculated based on
 - **Payment History** – Covers 35% of your score. Tracks record of payments made to credit cards and loans
 - **Credit Utilization** – Around 30% of your score. Considers how unused money is available on open credit lines
 - **Length of Credit History** – Around 15% of your score. Refers to the length of time credit accounts have been open, and the recent activity made on an account
 - **Credit Mix** – About 10% of your score. Refers to different types of credit accounts (ex. car loan, credit cards, etc.)
 - **New Credit** – About 10% of your score. Tracks the most recent account you opened. Opening multiple accounts or taking out new loans in a short period of time is considered a red flag

FICO & VantageScore are two commonly used credit scoring models by credit bureaus. Score ranges are listed below.

FICO:

- Poor: 300-579
- Fair: 580-669
- Good: 670-739
- Very good: 740-799
- Excellent: 800-850

VantageScore:

- Very poor: 300-499
- Poor: 500-600
- Fair: 601-660
- Good: 661-780
- Excellent: 781-850

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Resources

- **Free Credit Reports** – You are entitled one free credit report every 12 months from each of the three credit bureaus (Experian, Equifax and TransUnion). That's 3 FREE REPORTS!
Note: The report lists your financial history and rarely includes credit scores. Go to <https://www.annualcreditreport.com/index.action>
- **Credit Karma** – To get free credit scores from Equifax and TransUnion, also keeps track of credit account activity and offers resources and information to managing debt. Can be downloadable by phone
- **Your Bank** – Many financial institutions may post your credit score on your monthly bank account statement and/or via the banking app
- [NerdWallet's Best College Student Credit Cards of January 2023](#) – Lists pros & cons of student credit cards and additional details to consider
- [Credit Karma's 5 best credit-builder loans of 2023](#) – Provides additional information on what credit-builder loans are, what to watch out for and loans to consider

QR Codes to Links & Articles

Free Credit Reports



Credit Karma



Best Credit Cards 2023



Best Credit-Builder 2023



Credit & Why
You Need It



5 Tips for Lower
Credit Utilization



What is a
FICO Score



How To Improve
My Credit Scores



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