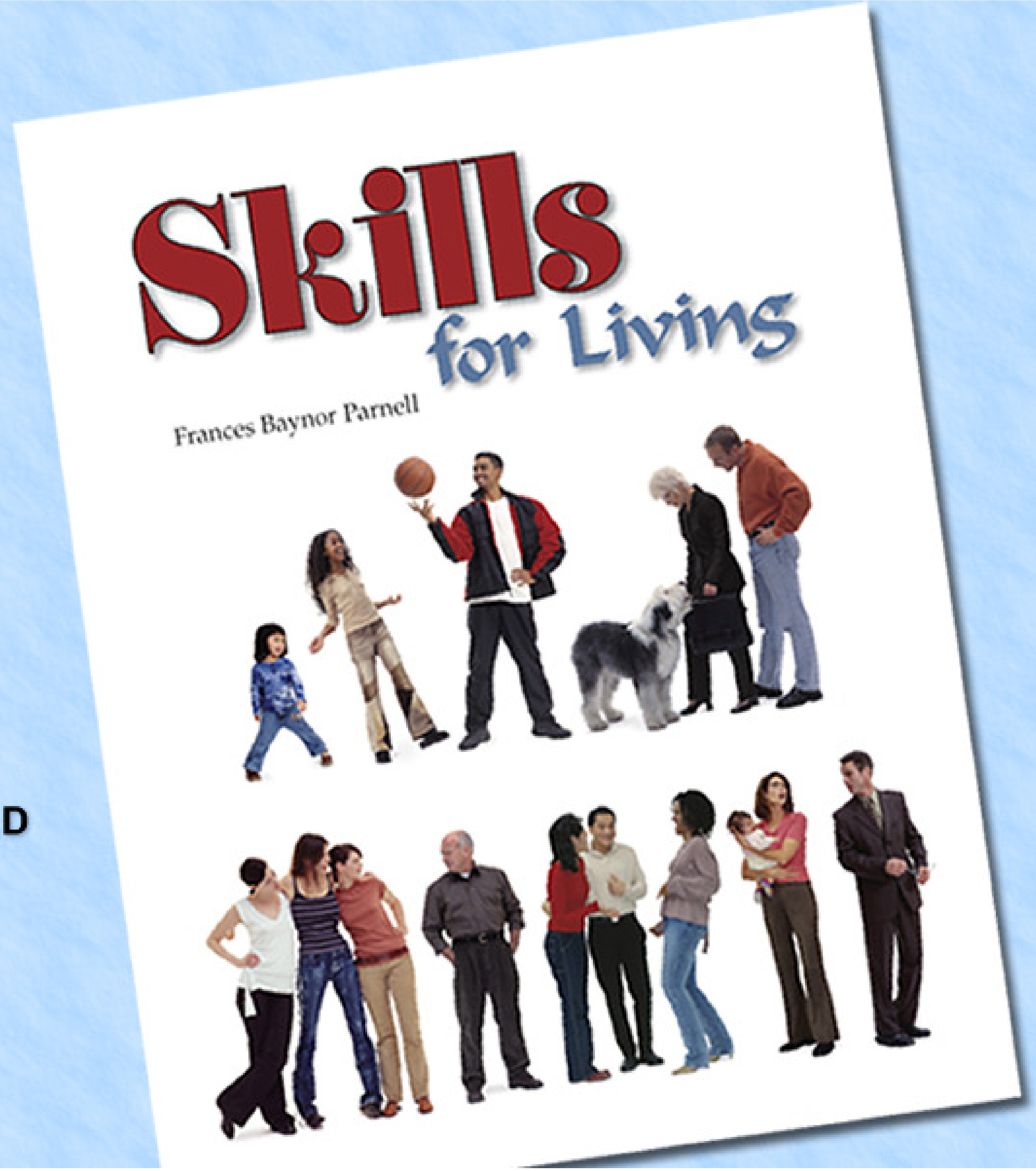

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Topic 19-4
Using Consumer Credit

- In this topic, you will study about using consumer credit, as well as
  - **Types of credit**
  - **The pros and cons of using credit**
  - **Applying for credit**
  - **Why credit costs**
  - **Shopping for credit**
  - **Credit contracts**
  - **Using credit wisely**

Using Consumer Credit

Objectives for Topic 19-4

After studying this topic, you will be able to

- identify different types of credit
- analyze the pros and cons of using credit
- describe how to establish a credit rating

Topic 19-4 Terms

- credit
- creditors
- collateral
- credit rating
- finance charges
- interest
- annual percentage rate (APR)
- credit contract

What Is Credit?

- ***Credit*** is an arrangement that allows the consumer to buy goods or services now and pay for them later

Types of Credit

- ***Cash credit*** is money offered as a loan
- ***Noninstallment*** credit is credit to be repaid in full at the end of the month
- ***Installment credit*** is repaid in a series of regular, equal payments made at regular intervals

Sales Credit

- ***Regular charge accounts***
  - Account must be paid off by the end of the billing period
  - No finance charges
  - Open end credit
- ***Installment charge accounts***
  - Closed-end credit
  - Used for major purchases
- ***Revolving charge accounts***
  - Credit limit
  - Finance charge added if bill is not paid in full

Credit Cards

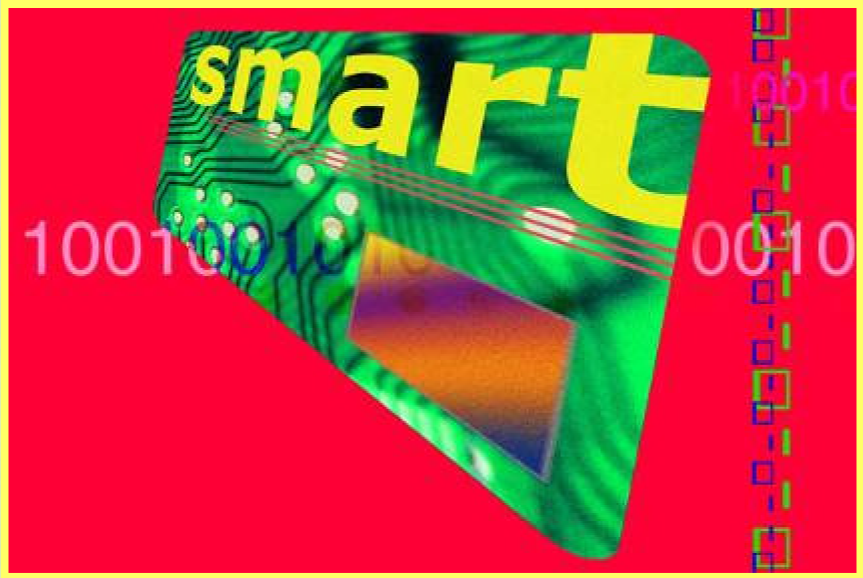
- A type of revolving charge account
- If your card is lost or stolen,
  - you are responsible for no more than $50 worth of charges made by someone else
  - you are responsible for the charges you made
  - report the loss immediately

Loans

- A loan is a financial transaction in which the lender agrees to give the borrower a certain amount of money

The Pros and Cons of Using Credit

- ***Creditors*** are people who give credit and to whom debts are owed
- ***Collateral*** is something of value that you own and that you pledge to a creditor as security for a loan



The Pros and Cons of Using Credit

- Pros
  - convenient
  - provides temporary help in emergencies
  - allows purchase of expensive items
- Cons
  - makes spending too easy
  - encourages impulse spending
  - is expensive
  - if payments are not made, you may lose the item
  - misuse can lead to long-term effects

Applying for Credit

- Are you a good credit risk?
- Can you handle the responsibility of credit?
- What will creditors use to evaluate you?

Establishing a Credit Rating

- A ***credit rating*** is the creditor's evaluation of your ability to repay debts
- To establish a credit rating,
  - open bank accounts
  - buy something on a layaway plan
  - be prepared to make a big down payment
  - apply to a local department store for a charge account with a low limit
  - ask a relative to cosign a loan for you

Establishing a Credit Rating

- Check your credit rating by visiting
  - www.ftc.gov/credit
  - www.annualcreditreport.com
- Report any errors in your report immediately

The Three Cs of Credit

- ***Character***
  - Your personal attributes, including honesty and reliability
- ***Capital***
  - Your income; your occupation and length of employment; other financial resources
- ***Capacity***
  - Your ability to repay in relation to other debts and living expenses

Why Credit Costs

- What do businesses spend in order to provide credit for customers?
  - Interest on money borrowed to cover operating costs
  - Cost of paying credit department employees
  - Cost of additional help to collect bad debts
  - Compensation for losses on unpaid bills

Shopping for Credit

- Comparison shop for the
  - total cost of using credit
  - terms of credit agreements
- ***Finance charges*** are the total amount a borrower must pay the creditor for the use of credit
  - interest
  - service charges
  - any other fees

The Cost of Credit

- The cost of credit is determined by
  - the amount of credit used, which determines the ***interest*** —the price you pay the creditor for the use of money over a period of time
  - the ***annual percentage rate (APR)***—the actual percentage rate of interest paid per year
  - the repayment time—longer repayment time means a larger amount of interest

Credit Contracts

- ***Credit contracts*** are legally binding agreements between creditor and borrower that detail the terms of repayment
- ***Cosigners*** on a contract agree to pay the debt if the debtor fails to pay

Using Credit Wisely

- Determine how much credit you can afford
- Evaluate whether or not to use credit when making a purchase
- Shop for the best terms to meet your needs

Handling Credit Problems

- Notify your creditor immediately if job loss, illness, or accidents occur
- ***Debt consolidation*** involves borrowing money to pay back debts, then making manageable payments on the loan
- Credit counseling helps you
  - work out a reasonable budget
  - learn money management skills

Handling Credit Problems

- Court protection includes
  - the ***Wage Earner Plan***, a legal arrangement by the court that schedules debt repayment
    - All assets are protected while the debtor pays
  - ***bankruptcy***, which occurs when the court declares that a person is unable to pay debts
    - The debtor's possessions are sold and the cash is distributed to the creditors

Summary for Topic 19-4

- Deciding whether or not to use credit is an important consumer decision
- Shopping for the best credit terms helps consumers compare finance charges and get the best deal
- Misusing credit can lead to serious financial problems
- Consumers who cannot handle serious credit problems should seek help from credit counselors