

Ready to build a Spending Plan?
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**THE MECHANICS OF
CREDIT**

**FINANCIAL
EDUCATION**

5KEYS 
Financial Coaching
a division of
Freedom 5:one Ministries

What is Credit?

Credit is the ability to borrow money or access goods or services with the understanding that you'll pay later. Credit is a fundamental part of financial stability, and building a good credit score is crucial for long-term financial health. It enables individuals to access credit and loans, purchase a house or car, and even get a job. Good credit is a valuable asset that can help achieve financial goals and lead to a better quality of life.

Building credit takes time and effort, but it is well worth it. Here are some reasons why building credit is so important.

Access to Credit and Loans:

Credit allows individuals to borrow money from lenders, which is necessary for most people to achieve their financial goals. Without good credit, it can be challenging to access credit or loans, hindering the ability to buy a house, car, or start a business. Building credit over time can help qualify for better interest rates and more favorable terms on loans, making it easier to achieve financial goals.

Lower Interest Rates:

Having good credit can also help secure lower interest rates on loans and credit cards. Lenders use credit scores to measure financial responsibility, and the higher the score, the more likely to get a better interest rate. A lower interest rate can save thousands of dollars over the life of a loan, making it easier to pay off debt and achieve financial stability.

Renting a Home:

Building credit is just as important for renting a home as buying one. Many landlords check credit reports before renting out a property, and poor credit can make it challenging to find a place to live. Building credit can improve chances of getting approved for a rental property and even help negotiate lower rent.

Job Opportunities:

Credit scores can impact job opportunities. Some employers check credit reports during the hiring process, particularly for jobs that involve managing money or financial

responsibilities. A poor credit score can signal financial instability and may cause an employer to pass over a candidate. Building credit can help demonstrate financial responsibility and increase chances of getting hired.

By building credit, individuals are taking a critical step towards securing their financial future and achieving long-term financial goals.

Credit Danger

While building credit is essential for financial health, there are also potential dangers associated with it. It's important to understand the risks involved and who should avoid credit.

Debt:

One of the biggest dangers of building credit is falling into debt. Credit cards and loans provide easy access to money, but they also come with interest rates and fees that can add up quickly. High levels of debt can lead to financial instability and can even impact credit scores negatively. **Individuals who struggle with debt management should avoid building credit until they have their finances under control.**

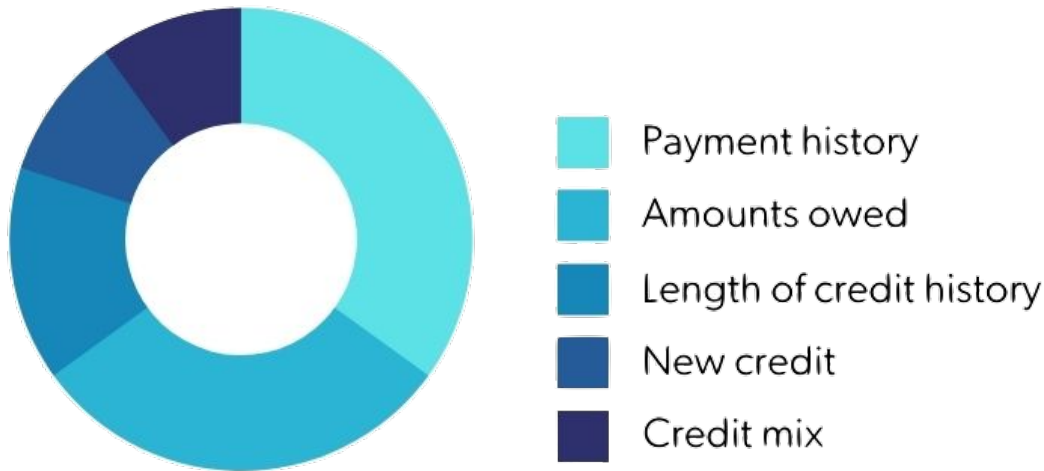
Impulse Purchases:

Having access to credit can lead to impulse purchases, which can quickly lead to debt. **It's essential to have self-discipline and budgeting skills to ensure that credit is used responsibly. Individuals who struggle with impulse purchases or have difficulty controlling spending should avoid building credit until they can develop better financial habits.**

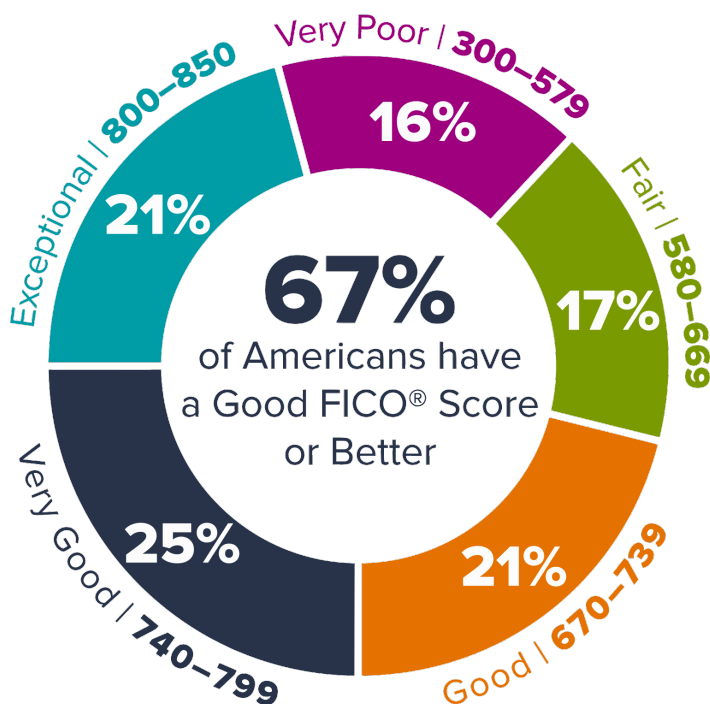
Worth repeating:

Individuals who struggle with debt management, impulse purchases, or have a history of missed payments should avoid building credit until they can improve their financial habits.

The 5 Factors that Make Up Your Fico Credit Score



There are many different types of credit scores, but the FICO® score is the most common credit scoring model today and the one that is used by most lenders.



FICO scores range from 300 to 850 points. Typically, a score more than 650 is considered "fair," a score more than 700 is considered "good" and a score more than 750 is considered "excellent."

The primary factors that affect your credit score include payment history, the amount of debt you owe, how long you've been using credit, new or recent credit, and types of credit used. Each factor is weighted differently in your score.

Let's take a closer look at the factors that make up your FICO credit score and the importance of each in how the model calculates your score.

1. Payment History **Weight: 35%**

Payment history defines how consistently you've made your payments on time. This is the most important contributor to your credit score.

2. Amounts You Owe **Weight: 30%**

Credit utilization, or how much of your credit limits you are using, is weighted almost as heavily as paying on time. It's good to use less than 30% of your credit limits — lower is better. You can take several steps to **lower your credit utilization**. Scores respond fairly quickly to this factor.

3. Length of Your Credit History **Weight: 15%**

Your credit history is based on the length of time you've had credit accounts open in your name. A longer credit history can help your credit score. If you've had a credit card open for a long time, it makes good sense to continue using that card responsibly to maintain a good score.

4. New Credit You Apply For **Weight: 10%**

Also known as *credit inquiries*, the pursuit of new credit negatively affects your score. Every time you apply for credit, your score goes down. There is one exception: when you're shopping for a mortgage, student or auto loan, credit scoring models only count one inquiry if your comparison shopping with multiple lenders is done within a 14- to 45-day period.

For example, if you're shopping for a car and apply for financing at three different car dealerships, your score will not decrease three times; it will only decrease once during the shopping window. That could vary depending on the type of loan you're seeking and the credit scoring model used.

Note that inquiries will affect your credit even if you're denied or ultimately decide against the loan or credit card. Each inquiry affects most people's score by less than 5 points and can stay on your report for up to 24 months.

5. Types of Credit You Use **Weight: 10%**

Your score can increase if you responsibly use different types of credit, such as installment and revolving debt. Even so, it's not necessary to have many different types of credit in order to have a good score.

If you need help with building your budget or accountability to follow one, reach out to TR@5keysFinancial.com or visit us at [5keysFinancial.com](https://www.5keysfinancial.com)

How to build credit

Building credit is essential for financial health and can open doors to various opportunities, such as lower interest rates on loans and better rental options. Here are ten effective ways to build credit:

1. Open a Credit Card Account:

- Apply for a secured credit card if you're just starting out or have poor credit. Make small purchases and pay off the balance each month.

2. Become an Authorized User:

- Ask a family member or friend with good credit to add you as an authorized user on their credit card. Their good payment history can help boost your credit score.

3. Pay Bills on Time:

- Consistently paying bills, such as utilities and rent, on time can positively impact your credit score, as some services report payment history to credit bureaus.

4. Keep Credit Card Balances Low:

- Maintain a low credit utilization rate by keeping your credit card balances below 30% of your credit limit.

5. Diversify Your Credit Mix:

- A mix of credit types, such as credit cards, installment loans, and retail accounts, can positively affect your credit score.

6. Limit Credit Inquiries:

- Avoid applying for multiple credit accounts in a short period, as each application can result in a hard inquiry, temporarily lowering your credit score.

7. Use a Credit Builder Loan:

- **Some banks and credit unions offer credit builder loans, where the borrowed money is held in a savings account until the loan is paid off, helping you build credit through timely payments.**

8. Monitor Your Credit Report: See Steps below

- **Regularly check your credit report for errors or discrepancies and dispute any inaccuracies with the credit bureaus.**

9. Keep Old Accounts Open:

- **The length of your credit history is a factor in your credit score. Keeping older accounts open, even if they are not frequently used, can help maintain a longer credit history.**

10. Increase Your Credit Limit:

- **Request a credit limit increase from your credit card issuer. This can reduce your credit utilization rate, provided you don't increase your spending.**

Steps to Monitor Your Credit Report:

1. Obtain Free Credit Reports:

- By law, you're entitled to one free credit report from each of the three major credit bureaus (Equifax, Experian, and TransUnion) every 12 months. Visit [AnnualCreditReport.com](https://www.annualcreditreport.com) to request your free reports.

2. Stagger Your Requests:

- Instead of requesting all three reports at once, stagger them throughout the year (e.g., one every four months) to monitor your credit more frequently.

3. Review Personal Information:

- Ensure that your personal information (name, address, Social Security number) is accurate on each report.

4. Check Account Information:

- Verify that all accounts listed are yours and that the details (balance, payment history, credit limit) are correct.

5. Look for Errors and Discrepancies:

- Common errors include accounts that aren't yours, incorrect balances, and inaccurate payment histories. Check for duplicate accounts and ensure closed accounts are reported correctly.

6. Identify Unauthorized Activity:

- Watch for unfamiliar accounts or inquiries, which could indicate identity theft.

Steps to Dispute Errors:

1. Gather Evidence:

- **Collect documentation to support your dispute, such as payment records or statements showing correct information.**

2. Contact the Credit Bureau:

- **Each credit bureau has an online dispute process. You can also submit disputes by mail. Provide a clear explanation of the error and include copies of your evidence.**

3. Contact the Creditor:

- **Notify the creditor (e.g., bank, credit card company) of the error and provide the same documentation.**

4. Follow Up:

- **Track your disputes and follow up if you don't receive a response within 30 days. The credit bureau is required to investigate and respond within this timeframe.**

5. Review the Results:

- **Once the investigation is complete, the credit bureau will provide the results. If the dispute is resolved in your favor, ensure the corrected information is reflected in your report.**

Additional Tips for Monitoring Your Credit:

1. Use Credit Monitoring Services:

- **Consider subscribing to a credit monitoring service that provides regular updates and alerts for changes in your credit report. Some services are free, while others offer premium features for a fee.**

2. Sign Up for Fraud Alerts:

- **Place a fraud alert on your credit report if you suspect your information has been compromised. This makes it harder for identity thieves to open accounts in your name.**

3. Utilize Free Tools:

- **Many financial institutions and credit card issuers offer free credit score tracking and monitoring tools to their customers.**

4. Set Up Alerts:

- **Enable notifications from your bank or credit card issuer for large transactions or changes in account status to catch suspicious activity early.**