

The logo for KIVA U features a green stylized leaf icon to the left of the text "KIVA U". The "K" is formed by two leaves, and the "U" is a solid green block letter.

KIVA U Understanding Loans & Credit

Managing money well is critical to stability, success, and achieving your goals. Using budgets to plan for your income and expenses will help you make informed choices about how to responsibly spend, save, and share your money. This will allow you to build good credit and when/if you ever need a loan or need to apply for a credit card, your good credit history will help make sure you get the best arrangements possible. This will also help you to achieve whatever goals you have set for yourself- to buy a car, go to college, travel the world, or start your own business. We've put together this introduction to loans and credit to help you start your financial history off well.

How Credit Works

An important factor in your financial planning and health is building good credit. **Credit history** encompasses the life of your financial management using banks and other borrowing and lending companies. It allows credit card companies, banks, and landlords, to assess whether you are a good candidate for credit. This will determine if they believe you are a qualified person to lend or rent to and what your interest rate should be.

What is Interest?

Interest is the cost of using someone else's money. If you borrow money from a bank or credit card company, it is likely that they will charge you a percentage of the amount of money you owe them as a fee. If you lend money, you could charge interest to the borrower to earn a profit. Banks often pay their customers interest for keeping money with their institution.

You can begin building good credit upon opening your first bank account. Managing that account well will help establish a good base for your **credit score** (also known as your FICO score). When you have a good credit score, you are more likely to be approved to rent your own apartment, get a loan from the bank for a car or home, or open a credit card account with a low interest rate.

How Do Loans Work?

So what do you do if there is something you need to pay for today, that you lack the funds to purchase immediately? People run into this problem all the time when they

want to buy their first car or are figuring out how to pay for college. One option is to take out a loan, which is a type of credit.

Just like the borrowers on Kiva.org, when a person needs money to purchase something now but needs the flexibility to pay it back over time, they can apply for a loan. When applying for a loan from the bank, think carefully about the amount of money you want to borrow and how long it will realistically take for you to pay it back. Banks usually charge interest on loans that they give, so finding an option with a reasonable rate and fewer fees is key.

A bank will review your application, mainly assessing your current income and your credit history. They want to be sure you have enough money coming in that you will be able to make repayments on the loan, and your credit history gives them a sense of whether you are good at managing your money and paying off debts on time.

If you do not have a high enough income or strong credit history, you can have someone who has already built strong credit (a cosigner) sign for the loan with you, so that the bank knows someone else will pay your debt if you cannot. Sometimes, banks will also allow you to secure the loan with collateral. Collateral is something of value that the bank can take and sell if you are unable to repay your loan. Once approved for a loan, starting on a particular date, you will begin making monthly payments to go toward both paying off the loan and paying additional interest on the account until the loan is repaid in full.

Further Reading

- 1) Citibank Financial Education Curriculum (goo.gl/3FrhLX)
- 2) MSN Money: Your Credit Rating (goo.gl/43i34K)

Review & Discussion Questions

- 1) What are some of your personal savings goals?
- 2) How does someone build good credit?
- 3) What are some ways one could damage their credit?
- 4) Would you lend money to someone who had a bad credit history?
Why or why not?