

Financial Literacy Understanding Credit

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Overview

Guidelines for communicating to students and families regarding the risks of credit and understanding debt:

- Americans, including most college students, carry debt and must understand the importance of building a solid credit history
- Students must assume responsibility for managing their spending
- Students must realize the negative impact identity theft could have on their credit rating, and manage their behavior accordingly

Overview

What to communicate to students and families regarding the risks of credit and understanding debt:

- During any pursuit of credit – home loan, auto loan, private education loan, etc – the applicant will be asked to authorize the lender to obtain a credit history
- This history can be calculated as a “score.”
- A lender uses this score to help answer the question,
 - “What is the likelihood that this borrower will pay us back on time?”
- And, most importantly, be sure students and families know to ask for help at any time in the process.

Key Message to Students

Build a Solid Credit History:

- Establish a budget and stick to it; buy only what is needed
- Be responsible; pay balances on time
- Pay more than the minimum monthly payment
- Use *one* credit card to establish credit; having multiple cards is harder to manage
- Watch your credit limits

Key Message to Students

How?

- Live within your financial means
- Set and realize financial goals
- Maintain good credit
- Determine how to get more for your money

Why?

- *A good money management philosophy will help you focus on class work, reduce stress and achieve more.*

Understanding Credit

Make the Most of Your Current Financial Resources



Student Credit Card Statistics*

UNDERGRAD Students with Credit Cards	1998	2000	2001	2004
Percentage who have credit cards	67%	78%	83%	76%
Average number of credit cards	3.5	3	4.25	4.09
Percentage who have 4 or more cards	27%	32%	47%	43%

UNDERGRAD Credit Card Balances	1998	2000	2001	2004
Average credit card debt per student	\$1,879	\$2,748	\$2,327	\$2,169
Median credit card debt per student	\$1,222	\$1,236	\$1,770	\$946
Percentage with balances from \$3,000-\$7,000	14%	13%	21%	16%
Percentage with balances exceeding \$7,000	10%	9%	6%	7%

* 2008 data will be available in November.

Student Credit Card Statistics*

GRAD Students With Credit Cards	1998	2000	2003	2006
Percentage who have credit cards	95%	95%	96%	86%
Average number of credit cards	6	4	6	5
Average credit card debt	\$4,925	\$4,776	\$7,831	\$8,322
Median credit card debt	\$2,834	\$3,068	\$3,730	\$3,476
Percentage with balances from \$6,000 - \$15,000	22%	20%	25%	22%
Percentage with balances exceeding \$15,000	6%	6%	15%	15%

* 2008 data will be available in November.

Good Debt vs. Bad Debt

- Good debt helps finance long-term benefits, such as home ownership and education.
- Bad debt provides short-term gratification, such as a vacation or a impulsive purchase that's forgotten long before you've paid for it.

Credit Cards: Pros

- Establish a positive credit history
- Reduces need to carry cash
- Provides security in emergencies
- Extends purchasing ability for larger purchases

Credit Cards: Cons

- Interest paid on unpaid balances
- Maxed-out credit cards cannot be used in a real emergency
- Unplanned (spontaneous) purchases disrupt budgeting and leave less for planned expenses
- Poor credit payment record stays on credit report for 7 years and may cause denial of additional credit (private student loan, auto loan, apartment rental, mortgage, etc.)
- Can create emotional stress

Warning Signs for Credit Trouble

- Paying a bill late
- Paying only the minimum due; or worse, paying less than the minimum
- Often exceeding the credit limit
- Using one credit card to pay off another
- Using a student loan to pay off a credit card
- Working overtime or a second job to keep up with bills

Credit Example – Is It Worth It?

Jim's Spring Break Trip to Mexico

- \$750 VISA charges for airfare, shared hotel, food, etc.
- 19% interest, repayment begins immediately
- Minimum payment is 2% of balance
- Payoff takes **93 months or 7.75 years**, assuming no further credit purchases



Amount Borrowed	Minimum Monthly Interest Payment	Total	Total Repaid
\$ 750	\$ 15	\$645	\$1,395 !!!

Source: www.bankrate.com Example is an estimate only. Assumes fixed \$15 monthly payments, although minimum required payment may be more.

Credit Reporting

Make the Most of Your Current Financial Resources



What is a Credit Report?

- Provides a history of credit use to current and prospective lenders.
 - Data provided to credit bureaus by all creditors with whom students already have a relationship
 - Data updated frequently, monthly or more
- Allows lenders to assess risk of extending credit or lending money to individual.
- Used for all forms of credit, including private student loans, apartment rental, credit cards, etc.

What is a FICO[®] Score?

- FICO scores are the credit scores most lenders use to determine credit risk. (FICO is the acronym of Fair Isaac & Company, developers of the software used by bureaus when performing a credit check.)
- Scores based solely on information in consumer credit reports maintained at the credit reporting agencies – Experian, TransUnion, and Equifax.

Equifax 800-685-1111 www.equifax.com

Experian 888-397-3742 www.experian.com

TransUnion 800-888-4213 www.transunion.com

A SCORE BY ANY OTHER NAME

The three credit bureaus each have their own name for a FICO score.

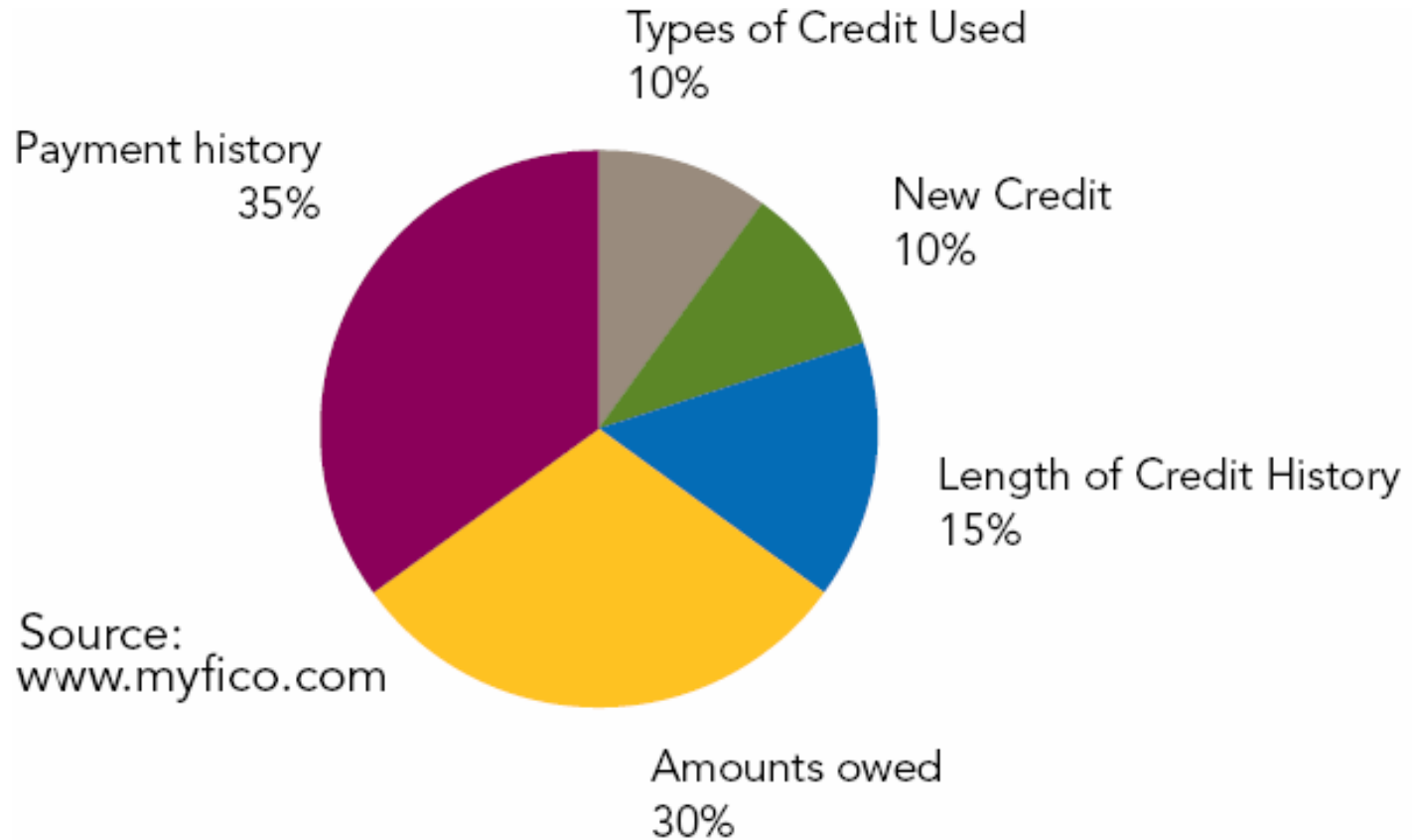
You may hear of:

- BEACON[®] score (from Equifax)
- PLUSSM score (from Experian)
- EMPIRICA[®] score (from TransUnion)

What is a FICO[®] Score?

- As credit information changes, scores tend to change as well. The 3 FICO scores affect both how much and what loan terms (interest rate, etc.) lenders will offer
- **www.annualcreditreport.com** publishes a free annual credit report, site is sponsored by Equifax, Experian and TransUnion and *consumers may receive 1 free copy annually*

What Makes Up a FICO Score?



Source:
www.myfico.com

- | | |
|------------|--|
| 35% | Past payment history: late payments, delinquencies, bankruptcies |
| 30% | Outstanding debt: amounts you owe |
| 15% | Length of credit history: time since current accounts opened |
| 10% | Types of credit: loans, mortgage, credit cards, lines of credit, etc. |
| 10% | Applications for credit: every application affects your score |

Where to Go for Credit Help

- Avoid credit “repair” services that charge a fee and guarantee “fixing” a poor credit record.
- Call 888-5OPTOUT (888-567-8688) to be removed from direct mailing lists.

American Consumer Credit Counseling

www.consumercredit.com

800-769-3571

Myvesta

www.myvesta.org

800-698-3782

National Foundation for Credit Counseling

www.nfcc.org

800-388-2227

Questions

