

4-1

INTRODUCTION TO CONSUMER CREDIT

OBJECTIVES

Become familiar with the basic vocabulary of credit terms.

Become familiar with types of lending institutions.

Compute finance charges for installment purchases.

What do you need to know before using credit?

- Why does credit compel people to overspend?
- Have you ever seen an advertisement about obtaining your credit score on TV, on radio, or in print media?
- How is your credit score like a credit “report card?”

Key Terms

- **credit** – when you purchase something that you do not pay for immediately
- **debtor** – people who use credit
- **creditor** – organizations or people who extend credit to consumers

- **credit rating** – this is your credit “report card”

Every time you use credit, the creditor reports how well you met your financial obligations to a credit reporting agency.

- **credit reporting agency** – a company that compiles records on all users of credit to be used by creditors before they issue credit to a consumer.

Key Terms

- **FICO score** – named for its creator, Fair, Isaac and Company the score, which range from 300 to about 850, summarizes the probability debtors will repay their debts. The higher the score the better.
- **installment plan** – when stores offer creditworthy customers the convenience of paying for merchandise or services over a period of time.

Example 1

Heather wants to purchase an electric guitar. The price of the guitar with tax is \$2,240. If she can save \$90 per month, how long will it take her to save up for the guitar?

Example 2

Heather, from Example 1, speaks to the salesperson at the music store who suggests that she buy the guitar on the installment plan. It requires a 15% down payment. The remainder, plus an additional finance charge, is paid back on a monthly basis for the next two years. The monthly payment is \$88.75. What is the finance charge?

EXAMPLE 3

0% financing or
Same as cash

Carpet King is trying to increase sales, and it has instituted a new promotion. All purchases can be paid on the installment plan with no interest, as long as the total is paid in full within six months. There is a \$20 minimum monthly payment required. If the Schuster family buys carpeting for \$2,134 and makes only the minimum payment for five months, how much will they have to pay in the sixth month?

CHECK YOUR UNDERSTANDING

Janet had a credit score of 660. She then missed three monthly payments on her credit cards, would this cause her score to go up, down or stay the same? State your reasoning.