Hands on Banking®
Money skills you need for life

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Credit – Lesson – What is Credit?

Instructor Instructions

Welcome to Wells Fargo's Hands on Banking® Program!

The Hands on Banking® program is an easy and enjoyable way to teach and learn the essentials of financial education. Whether it's opening a checking account, paying for college, buying a home, or starting a small business, the *Hands on Banking* program provides real-world skills and knowledge everyone can use.

Using the Instructor Guides

These instructor guides can be used to present financial education to your audience. Additional resources are available at https://handsonbanking.org. We encourage you to review these materials prior to presenting. Doing so will allow you to present the materials more effectively and confidently.

Each Instructor Guide Includes:

The lesson includes:

- Lesson Overview
- Learning Objectives
- Starting a discussion questions
- The basics
- Tips
- Activities (Instructor and Participant copies)
- Lesson Summary

Printing Instructions

Please print one copy of the Instructor information and multiple copies of the Participant information located at the end of this instructor guide.

How to Access the Online Program

The *Hands on Banking* program is available free of charge at https://handsonbanking.org in both English and Spanish.

Thank you for sharing these valuable financial education programs with students and adults in our communities. As an instructor, your training and guidance will provide others with the knowledge and skills they need for a brighter financial future. Please contact us via email with any comments or success stories at HOBinfo@wellsfargo.com.

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Lesson Overview

This lesson provides an easy-to-understand introduction to credit, how it can benefit participants and the risks they should watch out for. Participants will learn the differences between good and bad credit, how to build credit and the "five C's"—how lenders evaluate credit worthiness.

Learning Objectives

After completing this lesson, participants will be able to:

- Define credit
- Describe how credit can benefit them
- List risks to be aware of when dealing with credit
- Explain the differences between good and bad credit
- Explain how to build good credit
- Define the 5 C's—how lenders evaluate credit worthiness

Start the Discussion

To start a discussion with your participants, ask some open-ended questions. Here are some examples you could use:

- When did you receive your first credit card?
- Describe your first experience with credit.
- Did you understand the concept of credit at that point?
- Are there risks you take when you take out a loan or use your credit card? How can you minimize these risks?
- Do you know your "credit worthiness" as defined by your lenders?

The Basics

Credit is the ability to borrow money.

- There are lots of situations where people borrow money: car loans, credit cards, student loans, etc. In each case, you're borrowing money from a lender with a promise to pay it back.
- The money you owe is called debt.
- Earning the trust and confidence of banks and other businesses to lend you money is called establishing credit. By showing them you're trustworthy, you strengthen your ability to borrow again the next time. This is called having a good credit record or a good credit rating.
- When you borrow money, you need to make monthly loan payments and usually have other costs called interest and fees.

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Activity #1 – The Benefits and Risks of Credit (Instructor Copy)

Instructor Note

Divide the class into small groups. Ask each group to brainstorm the benefits and risks of using credit. When they're finished, discuss the key points as well as the benefits and risks listed in the chart below.

Instructions

Have your participants list the benefits and risks of using credit in the boxes.

Key Points:

- Having the ability to borrow money when you need it gives you flexibility.
- But borrowing too much money and being unable to pay it back is a serious problem in our country.
- It's important to use credit responsibly and avoid having too much debt.
- If you understand how credit works and use it wisely, it can help you to reach your goals.

Benefits and Risks of Credit

CREDIT BENEFITS	CREDIT RISKS
• The option of buying something today and paying the money back over time, rather than having to wait. • The flexibility to act on major purchases and life opportunities that may require more money than you have on hand right now, like buying a computer, or borrowing for college. • Easier to rent an apartment and to get service from local utility companies. Easier to buy what you want, when you want it.	• Overdoing it; borrowing more than you can afford to repay. • If you don't make your payments on time, you'll damage your credit record. • Losing money on late fees. • Having to pay additional interest. Difficulty getting loans or credit in the future.

TIP!
How much debt can you repay?

- General guideline #1: Never borrow more than 20% of your yearly net income.
- General guideline #2: Keep your credit card debt low enough so that your required payments are no more than 10% of your monthly income.

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Good Credit vs Bad (Instructor Copy)

Instructor Note

Ask the class:

- What does having "good credit" mean?
- What does having "bad credit" mean?

After discussing the answers to those questions, ask the class to supply good and bad credit signs and the result of each.

- Good credit means that you make your payments in full and on time.
- Bad credit is just the opposite.

Signs of Good and Bad Credit

Good Credit Signs	**Bad Credit Signs**
• Paying at least the minimum required payment • Paying on time • Never missing a payment • Staying within your credit limit Result • Easier to borrow money • No additional penalty fees • More money you'll keep in your pocket	• Paying too little • Paying too late • Missing payments • Going over your credit limit • Having too much debt Result • Difficult to borrow money • You lose money on late fees • More money spent on finance charges

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Activity #2 – How to Establish Credit (Instructor Copy)

Instructor Note

Tell your participants to read each statement and decide whether it is a good way to establish good credit. After they are finished, discuss each statement, then open the floor to discuss other tips and techniques they may have come up with.

Instructions

Have your participants read each statement and decide whether or not it is a good idea for establishing good credit. Have them write "True" or "False" in the left column.

Establishing Good Credit

HOW TO ESTABLISH GOOD CREDIT	TRUE OR FALSE?
Avoid getting a credit card until you are a homeowner.	False
Open a savings account or checking account and manage it well.	True
Never spend more than you have in the account. This reflects on your ability to repay loans.	True
Get multiple credit cards at top quality stores and skip making payments on occasion.	False
Get one or two gasoline or department store credit cards and pay your bill on time, every month.	True
Only borrow money from family and friends.	False
Use cash advances from one credit card to pay of balances due on others.	False
Take out a small loan for an appliance or a computer, and repay it monthly—in full and on time.	True
Get a secured credit card by opening a savings account with a balance equal to the card's limit.	True
Overdraw your checking account for the same amount each month. This demonstrates a consistent need.	False
Put your apartment and utilities in your own name and always pay your bills on time.	True

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Activity #3 – The 'Five C's' of Credit (Instructor Copy)

Instructor Note

Instruct your participants to match each of the 5 C's with its correct description. After they are finished, walk through each "C." How do lenders decide whether or not to loan you money? The 5 C's of course—character, capacity, capital, collateral and conditions. Some lenders develop their own loan decision"scorecards" using aspects of the 5 C's and other factors.

Instructor Note

Have your participants read the descriptions in the right hand column of the table. Then, instruct them to write in the right "C" for each description—character, capacity, capital, collateral or conditions.

"Five C's" of Credit

WHICH "C"?	DESCRIPTION
CHARACTER	• When lenders evaluate this "C," they look at stability—for example, how long you've lived at your current address, how long you've been in your current job, and whether you have a good record of paying your bills on time and in full. • If you want a loan for your business, the lender may consider your experience and track record in your business and industry to evaluate how trustworthy you are to repay.
CAPACITY	• Your other debts and expenses could impact your ability to repay the loan. • Creditors therefore evaluate your debt-to-income ratio, that is, how much you owe compared to how much you earn. • The lower your ratio, the more confident creditors will be in your ability to repay the money you borrow.
CAPITAL	• This term refers to your net worth—the value of your assets minus your liabilities. • In simple terms, how much you own (for example, car, real estate, cash, and investments) minus how much you owe.
COLLATERAL	• This term refers to any asset of a borrower (for example, a home) that a lender has a right to take ownership of and use to pay the debt if the borrower is unable to make the loan payments as agreed. • Some lenders may require a guarantee in addition to this. • A guarantee means that another person signs a document promising to repay the loan if you can't.
CONDITIONS	• Lenders might consider a number of outside circumstances that may affect the borrower's financial situation and ability to repay, for exam- ple what's happening in the local economy. • If the borrower is a business, the lender may evaluate the financial health of the borrower's industry, their local market, and competition.

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Lesson Summary

Instructor Note

Summarize this lesson by reviewing these key points with your participants.

Key points from the "What is Credit?" lesson:

- Credit is the ability to borrow money.
- There are lots of situations where people borrow money: car loans, credit cards, student loans, etc. In each case, you're borrowing money from a lender with a promise to pay it back.
- The money you owe is called debt.
- Earning the trust and confidence of banks and other businesses to lend you money is called establishing credit. By showing them you're trustworthy, you strengthen your ability to borrow again the next time. This is called having a good credit record or a good credit rating.
- When you borrow money, you need to make monthly loan payments and usually have other costs called interest and fees.

Instructor Note

At this point in the class, consider using these recommended Topics like Credit Cards, Your Credit Report and Your Credit Score as a discussion resource or a takeaway for your participants. You can find them and other Topics on https://handsonbanking.org.

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PARTICIPANT HANDOUT

Activity #1 – Benefits and Risks of Credit

Instructions

List the benefits and risks of using credit in the boxes below.

Benefits and Risks of Credit

CREDIT BENEFITS	CREDIT RISKS

TIP!

How much debt can you repay?

- General guideline #1: Never borrow more than 20% of your yearly net income.
- General guideline #2: Keep your credit card debt low enough so that your required payments are no more than 10% of your monthly income.

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PARTICIPANT HANDOUT

Activity #2 – How to Establish Credit

Instructions

Test your knowledge of how to establish credit. Only some of these tips are correct. Read each and decide whether or not it is a good idea for establishing good credit. Write "True" or "False" in the left column.

Establishing Good Credit

HOW TO ESTABLISH GOOD CREDIT	TRUE OR FALSE?
Avoid getting a credit card until you are a homeowner.	
Open a savings account or checking account and manage it well.	
Never spend more than you have in the account. This reflects on your ability to repay loans.	
Get multiple credit cards at top quality stores and skip making payments on occasion.	
Get one or two gasoline or department store credit cards and pay your bill on time, every month.	
Only borrow money from family and friends.	
Use cash advances from one credit card to pay of balances due on others.	
Take out a small loan for an appliance or a computer, and repay it monthly—in full and on time.	
Get a secured credit card by opening a savings account with a balance equal to the card's limit.	
Overdraw your checking account for the same amount each month. This demonstrates a consistent need.	
Put your apartment and utilities in your own name and always pay your bills on time.	

TIP!
Good credit management over time is key to building your credit and determining whether you can obtain credit for large future purchases, such as a car, a home, or college education.

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PARTICIPANT HANDOUT

Activity #3 – The “Five C’s” of Credit

How do lenders decide whether or not to loan you money? The 5 C’s of course—character, capacity, capital, collateral and conditions. Some lenders develop their own loan decision “scorecards” using aspects of the 5 C’s and other factors.

Instructions

Read the descriptions in the right hand column of the table. Then, write in the right “C” for each description—character, capacity, capital, collateral or conditions.

“Five C’s” of Credit

WHICH “C”?	DESCRIPTION
	• When lenders evaluate this “C,” they look at stability—for example, how long you’ve lived at your current address, how long you’ve been in your current job, and whether you have a good record of paying your bills on time and in full. • If you want a loan for your business, the lender may consider your experience and track record in your business and industry to evaluate how trustworthy you are to repay.
	• Your other debts and expenses could impact your ability to repay the loan. • Creditors therefore evaluate your debt-to-income ratio, that is, how much you owe compared to how much you earn. • The lower your ratio, the more confident creditors will be in your ability to repay the money you borrow.
	• This term refers to your net worth—the value of your assets minus your liabilities. • In simple terms, how much you own (for example, car, real estate, cash, and investments) minus how much you owe.
	• This term refers to any asset of a borrower (for example, a home) that a lender has a right to take ownership of and use to pay the debt if the borrower is unable to make the loan payments as agreed. • Some lenders may require a guarantee in addition to this. • A guarantee means that another person signs a document promising to repay the loan if you can’t.
	• Lenders might consider a number of outside circumstances that may affect the borrower’s financial situation and ability to repay, for exam- ple what’s happening in the local economy. • If the borrower is a business, the lender may evaluate the financial health of the borrower’s industry, their local market, and competition.

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