Managing credit: C1 – C7

This chapter aims to give the student knowledge and skills within the field of Managing credit and that they understand the consequences of having a loan, they gain knowledge of different types of loan, repayment periods, purchase objectives, interest rates and how to manage their debt.

What is credit:

an arrangement in which you receive money, goods, or services now in exchange for the promise to pay later

- **What are the different loan types?**
  - **Open-ended loan**

    An open-end loan is simply a loan that does not have a specific date for repayment. If you have a credit card or a line of credit with your financial institution, you actually have an open-end loan.

  - **Mortgage**

    The term “mortgage” refers to a loan used to purchase or maintain a home, land, or other types of real estate. The borrower agrees to pay the lender over time, typically in a series of regular payments that are divided into principal and interest. The property serves as collateral to secure the loan.

  - **Guaranteed loan**

    A type of loan in which a third party agrees to pay if the borrower should default

- **What is interest?**

  Interest is the price you pay to borrow money or the cost you charge to lend money. Interest is most often reflected as an annual percentage of the amount of a loan. This percentage is known as the interest rate on the loan.

  - **What is simple interest?**

    With simple interest, your interest rate payments added into your monthly payments, but the interest doesn’t compound. For example, a five-year loan of EUR1,000 with simple interest of 5 percent per year would require 1,250

EURO over the life of the loan (1,000 EURO principal and 250 EURO in interest). You'd calculate the interest by multiplying the principal, the APR and the length of the loan: 1,000 EURO x 0.05 x 5

- ### What is compounded interest

This is determined by continually calculating the interest on the principal plus the interest charged for the previous payment period. Compound interest is designed to generate higher returns, at times much higher than simple interest, by compounding the interest earned in the previous terms. If you take out the same loan above but it charges compound interest, you'd pay slightly over 1,332 EURO over the life of the loan (1,000 EURO principal and 332 EURO in interest).

- ## What is Principal

Loan principal is an amount that someone has borrowed. This applies to all forms of debt, whether it's a credit card balance, a car loan, or a mortgage

- ## What is APR

Annual percentage rate (APR) refers to the yearly interest generated by a sum that's charged to borrowers or paid to investors. APR is expressed as a percentage that represents the actual yearly cost of funds over the term of a loan or income earned on an investment. This includes any fees or additional costs associated with the transaction but does not take compounding into account. The APR provides consumers with a bottom-line number they can compare among lenders, credit cards, or investment products.

- ## What is risk?

- ### Collateral

The term collateral refers to an asset that a lender accepts as security for a loan. Collateral may take the form of real estate or other kinds of assets, depending on the purpose of the loan. The collateral acts as a form of protection for the lender. That is, if the borrower defaults on their loan payments, the lender can seize the collateral and sell it to recoup some or all of its losses.

- ### High risk

"High risk loans" are loans that pose more risk to a lender that choose to issue credit to someone with a low credit score—considered a "high-risk borrower." The borrower's low credit score is the result of a history of making late payments, keeping credit card balances close to their limits, having recently applied

- ### Low risk
  "Lenders are always on the lookout for low-risk borrowers – that is, consumers with good credit records that show they have be diligent about repaying previous debts; These loans do not require any security offer from the borrowers. And the loan amount can be put to any personal use, common amongst them are home improvements, buying a car, going to a holiday tour, for wedding or you can use the loan for debt consolidation.

- ### Passing on risk
  Goods being sold remain at the seller's risk until the property in the goods is transferred to the one who buys the goods known as the buyer. Once this property is passed, the goods are at the buyer's risk even if the delivery has not been made. This is what passing of risk means in the business world.

What is debt?

Debt means the amount of money which needs to be repaid back and financing means providing funds to be used in business activities.