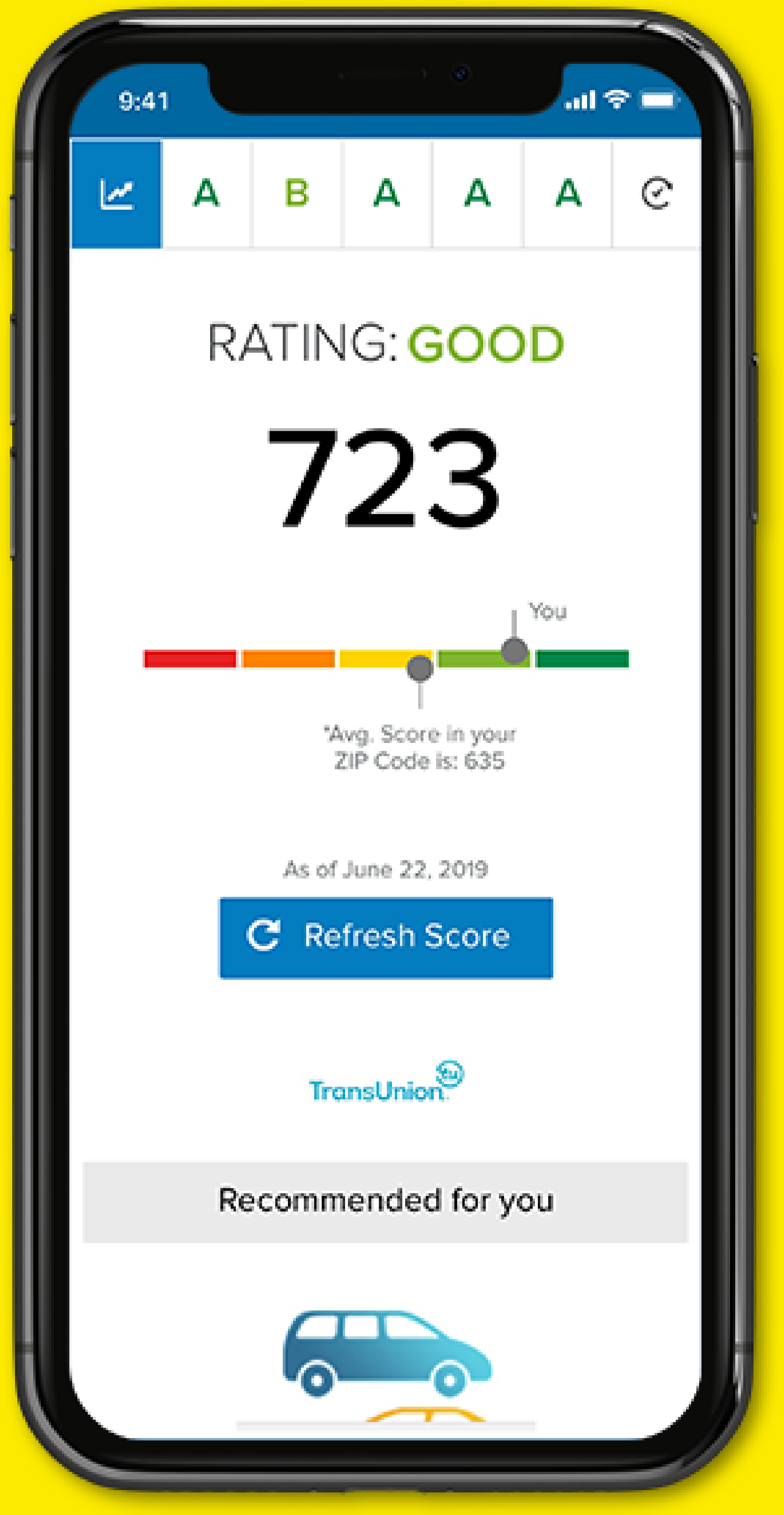
Credit

Hami Finance Club - 3/11/2021

What is Credit?



- Informally, "credit" can refer to the creditworthiness / reliability of a business or an individual
  - Saying someone "has great credit" means they have been financially reliable over an extended period of time
  - One good way to build credit after you turn 18: buy everything on credit and pay it back immediately
  - The better your credit, the more you're able to borrow
- However, today we'll discuss credit as a contract in which a borrower agrees to pay back a lender at a certain time
  - This allows people/businesses to make large purchases without paying in full (i.e. homes, cars, business supplies)
  - The borrower almost always pays ***interest***

How does Interest Work?

- Interest is essentially the price of borrowing money
  - When you use credit (borrow money) you are charged an additional percentage of the amount borrowed.
  - Interest rates are often measured as an Annual Percentage Rate (APR)
- Example: You borrow $100 with a 5% APR. You will need to pay back $105 after one year
- Interest rates can ***vary greatly*** based on your credit score, the type of borrowing you're doing, what your loan is for, and current economic conditions

Types of Interest

- Fixed-Rate Interest
  - An interest rate that stays the same throughout the loan period
  - Example: our $100 fixed-rate loan with a 5% APR required a $105 repayment
- Adjustable-Rate Interest
  - An interest rate that varies throughout the loan period depending on the state of the market and/or economy.
  - Example: 5 year ARM (Adjustable Rate Mortgage)
    - The Real Estate market is very competitive when you first take out a loan, and you're able to secure a 2% interest rate on your new home.
    - A few years later, the market slows and your interest rate increases to 8%. Suddenly, you're unable to afford the mortgage anymore.

Leveraging Credit

- Learning about interest might convince you that buying anything on credit is bad, but this is far from the case.
- Example: if you start a business that you think will be highly profitable in the long term but will require taking on debt at first, that is a risk that can be worth taking
- This is why many savvy investors use ***margin*** (a form of credit) to give themselves more buying power
- Using credit *should* be avoided, however, on anything that is non-essential or cannot potentially return a profit

Thank you for coming!

Feel free to ask any questions
Our next meeting will be on Thursday 3/25