Te whai hua - kia ora!

sorted in Schools

US 28088 (version 3)

Credit and Debt

Describe credit and debt and their impacts on personal finances

LEVEL 1

CREDITS 3

THEMES

Debt

Managing my money

Contents

Nau mai haere mai!

Welcome to the Credit and Debt module.

This module supports you to develop your understanding of how credit and debt can impact on personal finances and factors that contribute to debt being manageable or unmanageable.

You will be assessed on how well you:

- Describe credit in relation to personal finances including:
  - types of credit
  - types of credit provider
- Describe debt in relation to personal finances including:
  - managable debt
  - unmanagable debt
- Describe factors that affect credit or debt in terms of their impact on personal finances. This must cover **at least four** of the following:
  - changes in circumstances
  - changes in income
  - interest rates
  - penalties
  - administration fees
  - credit rating

Evidence/Judgements for Achievement	Evidence/Judgements for Achievement with Merit	Evidence/Judgements for Achievement with Excellence
For **TWO** of the **five scenarios**, you need to describe: • the type of credit • the type of credit provider • if the debt is managable or unmanagable debt • the factors affecting credit and debt and their impacts on personal finances. (factors may include; changes in circumstances, changes in income, interest rates, penalties, administration fees or credit ratings.).	As well as meeting the requirements for Achievement, you need to: • describe **at least two examples** of how to minimise the impacts of credit and debt on personal finances.	As well as meeting the requirements for Merit, you need to: • explain the relationship and management of **credit and debt** on personal finances.

Potential links to NCEA Level 1 Achievement Standards

You may be able to use your knowledge, content, and modified work in this module and assessment task as evidence towards the following Achievement Standards:

- **AS 90981** Make a financial decision for an individual or group
- **AS 90988** Demonstrate understanding of the interdependence of sectors of the New Zealand economy.

Discuss with your teacher whether this is an option.

This module is about the reasons and ways that people borrow money and the ways that credit and debt can impact on people's financial situations.

Working through this module will help you to build the skills and knowledge you need when thinking about borrowing money, including understanding the rights, risks and responsibilities of borrowing.

In this module you will explore:

- **Topic One: Credit and debt** – the difference between credit and debt; types of credit; understanding your financial identity.
- **Topic Two: Types of credit providers** – family/whanau/iwi, banks, digital time payment options, credit unions, private lenders, finance companies and store cards.
- **Topic Three: Manageable and unmanageable debt** – the impacts of manageable and unmanageable debt.
- **Topic Four: Factors affecting credit and debt** – changes in circumstances; changes in income, interest rates; penalties; administration fees, credit ratings.
- **Topic Five: The impact of credit and debt on personal finances** – positive and negative financial impacts of credit and debt

Resources

There are lots of useful resources for exploring credit and debt.

Two Sorted in Schools resources that have particular relevance to this module are:

- Debt Sorted Booklet. You can find this booklet on the **student activities** page of the Sorted in Schools website by clicking on Theme and selecting Debt from the dropdown menu.
- Sorted in Schools tool **What shapes my financial identity.**

Be sure to watch the fun, informative video that accompanies this module

Credit and Debt video

Other useful tools and websites include:

- **Sorted.org.nz guide to tackling debt**
- **Sorted.org.nz debt calculator**
- **Responsible Lending Guideline**
- **MoneyTalks**

Topic One: Credit and debt

Learning Outcomes for Topic One

- ✓ Understand the difference between credit and debt
- ✓ Understand your financial identity
- ✓ Understand the difference between good debt and bad debt.

Success criteria

You should complete all activities in this topic. They will help you to meet the assessment requirement of describing types of credit.

Most people know what it is like to lend or borrow something, for example, clothes, a bicycle or an umbrella.

In this module the focus is on borrowing money, which involves using someone else's money to make a purchase, with the promise of paying that person or organisation back at a later stage. Borrowing can be informal, such as borrowing $5 from a friend to pay for a bus ticket, or formal, such as borrowing $5000 from the bank to buy a car.

The focus of this topic is on understanding key terms that are used throughout this module. This includes understanding the difference between:

- credit and debt
- good debt and bad debt
- manageable and unmanageable debt.

We'll also explore some of the reasons that people borrow money, with a focus on needs and wants.

The relationship between credit and debt

Credit

Credit means the creation of any form of deferred payment. It is a way to buy goods and services and then pay for them later. For example, when you use a credit card, you are spending money that you don't have. If you have a credit card, the bank lets you borrow money up to an agreed amount to pay for things. However, you have to pay the money back within a set amount of time. If you don't pay it back before the deadline, the bank will charge you interest.

It's important to remember that when you buy something on credit, you are taking on a debt.

Debt

Debt refers to an asset obligation owed by one person to another. It is money that you owe to someone else. For example, if you borrow money from a whānau member, a bank or a loan company, you have debt. In a similar way, if you use a credit card to buy something that costs $120, you have a debt of $120. Debt doesn't just come from purchases. If the bank charges you interest or fees for borrowing the money, the interest becomes part of your debt.

Loans

A loan is money you borrow to use and that you have to pay back within an agreed amount of time.

The main reason we borrow money is that we need or want something straight away that we don't have the money to pay for.

Understanding needs and wants

Needs are goods or services that you need to be able to function and live. These include your needs for food, clothing and shelter. Wants are goods or services that are not necessary but are desirable such as a new phone or a family holiday.

Wants can feel like a need, but if we pause to think about them, we can usually identify whether they are something we genuinely need or just want really badly. If something is a want rather than a need, and you don't have the money to pay for it, it's often a good idea to wait until you have the money before you purchase it.

Delayed gratification is the ability to resist the impulse to do or get something straight away in order to get something better in the future. In terms of wants, delayed gratification might involve saving up for something instead of borrowing money to buy it or deciding not to buy something so that you can save the money instead.

Watch this short TED talk **Don't Eat the Marshmallow** to learn about the concept of delayed gratification.

Discuss with a classmate how the concept of “not eating the marshmallow” might apply:

- within your own life
- to the concept of debt.

The emphasis in this module is not on someone else defining your wants and needs, but encouraging you to be aware of the difference. Understanding the difference between a need and a want is really important when it comes to borrowing money. Some needs are obvious, for example, the need for food, clothes and a safe place to sleep. Other needs are more personal, for example, for some people, regularly giving part of their income to a church is an important demonstration of faith.

Family and cultural obligations

Family and cultural obligations can blur the line between needs and wants because our money choices reflect and impact on our relationships with others. This is especially true when it comes to cultural activities, identities, values, and beliefs. For example, fa’alavelave is the Samoan cultural practice of gifting money for large occasions such as weddings, funerals and significant birthdays. In a Samoan aiga, giving a gift to someone who is turning 21 may be viewed as a need rather than a want.

Types of credit

In this module (and in your assessment) the focus is on four types of credit:

- **personal loans**
- **mortgages**
- **credit cards**
- **revolving credit**
- **buy now pay later options.**

When you use any of these types of credit to purchase or pay for something, then you are in debt.

Personal loans

A personal loan is money borrowed from a friend, family member, bank, or other money lender that you pay back in fixed payments called installments. Generally, you pay both fees and interest on the money you have borrowed, which will form part of your weekly, fortnightly or monthly payments. The amount of interest can vary a lot and can make a big difference to the amount you have to repay on top of the amount you borrowed.

Personal loans are available through banks, credit unions, peer-to-peer and payday lenders, and loan shops. People use personal loans to pay for all kinds of things – weddings, renovations, holidays or consolidating their debts. But borrowing from some lenders can cost you dearly, so you need to research the options and know what you're getting into.

Mortgages

Buying a house is often the biggest purchase of a person's life. A home loan, also called a mortgage, is a financial commitment that usually lasts for years. The interest rate on a home loan tends to be a lot lower than the interest rate on a credit card or on a loan for a car. However, because a mortgage can be hundreds of thousands of dollars, the interest that you pay for the loan can also be hundreds of thousands of dollars.

Use the **Sorted Mortgage calculator** to get a sense of how much interest people who have a mortgage need to pay. To use the calculator, you'll need to invent a loan amount, say $400,000. You can find a current interest rate by visiting the **borrowing rates** page showing all of the New Zealand banks. Choose a term of 25 years and find out what the weekly repayments would be and how much interest you would end up paying over the term of the loan.

The amount you can borrow will depend on how much money you can afford to repay each month (based on your income) and how much a lender will lend on a property. Lenders will want to be sure that you'll be able to keep up with your repayments and still have enough money to live on.

Credit cards

Credit cards allow you to borrow money up to a certain limit as long as you make regular minimum repayments. Most credit cards have an annual fee. Credit cards tend to have higher interest rates than other forms of credit, and the rate can vary depending on what features the card offers. Repayments can quickly get out of hand if you don't clear the balance each month.

People who have a credit card can use it to get cash. This is called a "cash advance". The interest rates on a cash advance are usually higher than that charged for personal loans.

Revolving Credit

Revolving credit is like a big overdraft. You need to be disciplined, as there are no set repayments and you can withdraw or deposit money up to your credit limit whenever you like.

Buy Now Pay Later

Buy now pay later is a purchasing scheme that allows consumers to obtain goods or services either instore or online without paying the full amount upfront. The consumer is able to take the item home on the day by making a small deposit. The remainder of the price is then paid off in scheduled payments over a fixed time period. For example, buying a television or a washing machine, you can take it home and use it while you're still paying it off. However, buying something using buy now pay later option can involve additional fees and interest payments, so it's important to know the true cost of the product before buying something this way. Generally, the things people buy using this option lose their value as soon as they're bought, which is something to consider.

Understanding your financial identity

One way to understand where the line lies between needs and wants in your own life is to explore your financial identity. Your financial identity is shaped by your values; what you believe and what is important to you and your whānau.

Your financial identity includes your beliefs, knowledge and behaviours related to money. It also includes knowledge from your whānau and community and the choices you make about saving and spending.

Good debt and bad debt

No one likes being in debt, whether it's financial debt or just owing someone a favour. But when it comes to money, a debt is considered good debt if you're using the money borrowed to buy a good or service that will increase in value over time. Examples of good debt can include paying for education or buying a house.

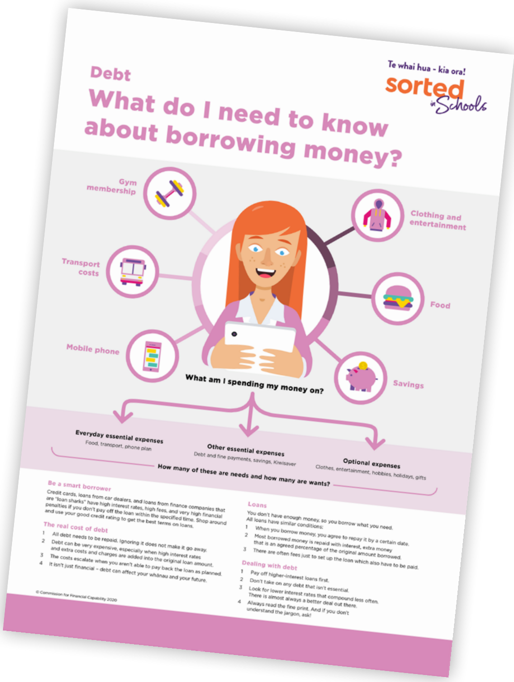
In contrast, bad debt is the result of borrowing money to pay for goods and services that lose their value after you've bought them, for example, a television, a game console or a holiday. These things aren't bad in themselves, but borrowing money to pay for them can create problems for your future self if it takes you a long time to pay the money back. The additional costs of interest and fees can stop you from being able to get ahead financially and can even lead to you rolling backwards.

Activities

1) Complete the **[What shapes my financial identity?]** booklet. As you do this, think about how your financial identity influences your definition of needs and wants in your own life.

2) Discuss how the following cultural concepts might blur the line between needs and wants:

- having a sense of duty to care for and serve others
- feeling responsible for meeting the needs of a community as well as the needs of yourself and your immediate family
- having cultural obligations or expectations about how money is used.



3) Explain the following terms in your own words:

- personal loan

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- mortgage

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- credit card

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- revolving credit

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- buy now pay later

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4) Download the Debt Sorted infographic from the **student activities section of the Sorted in Schools** website. You can find this by choosing "Infographic" from the drop-down menu under Media and then selecting "Debt" using the Theme menu.

According to the infographic, what are four ways to deal with debt?

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4. ....

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Before moving on to Topic Two, check that you understand:

- ☑ the relationship between credit and debt
- ☑ the following types of credit:
  - personal loans
  - mortgages
  - credit cards
  - revolving credit
  - buy now pay later.
- ☑ the difference between good debt and bad debt.

Topic Two: Types of credit providers

Learning Outcome for Topic Two

- [x] Understand different sources of credit.

Success criteria

You should complete all activities in this topic. They will help you to meet the assessment requirement of describing types of credit providers. The focus of this topic is on the different groups and organisations that provide credit.

Debt comes in many forms – credit cards, hire purchase, car loans, personal loans, mortgages and student loans.

There's no shortage of people out there wanting to lend us money! You have easier access to credit than any other generation. Phone plans, online shopping, in-app purchases; there are many ways to fall into debt.

This topic covers a wide range of sources of credit and contains a lot of information. You may like to work through it as a group, with each group member finding out about a different credit provider and then reporting back their findings to the rest of the group.

Assessment tip:

In your assessment, you need to refer to different types of credit providers:

- family/whanau/iwi
- a bank
- digital time payment options
- a credit union
- a private lender
- a finance company
- a store card.

Borrowing money can seem like a quick fix, but debt can end up being a serious drag on your finances.

Common costs associated with most loans are:

- interest rates – the amount of interest you need to pay on the loan
- administration fees – some money lenders charge a set-up fee when you set up a loan
- penalties – some loans have penalties if you miss a payment.

To find the best loan for your circumstances, you need to know what the fees and interest rates are. Before taking out a loan, it's important to add up the total costs and see how long it will take you to get out of debt. This handy **debt calculator** will do the maths for you!

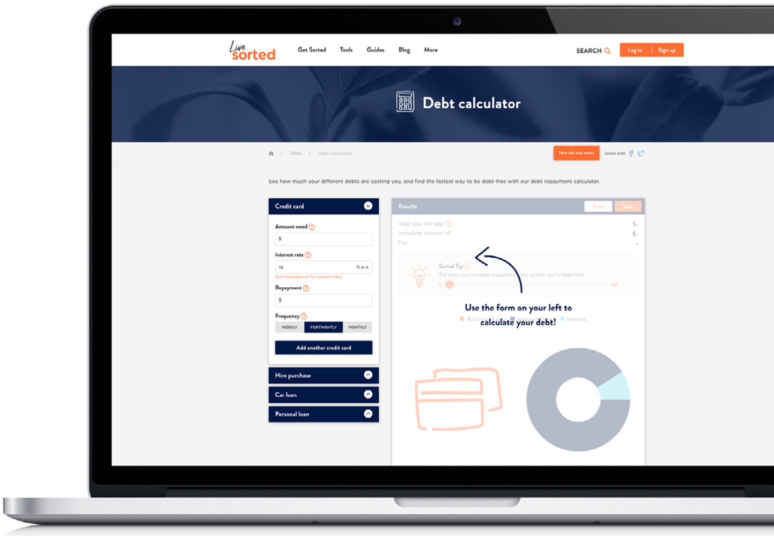
Many loans have administration fees that can be more than $100.

By law, lenders must provide a statement outlining:

- all the fees and charges
- what will happen if you can't make payments
- what interest rate will be charged
- how interest is calculated.

Assessment tip:

In your assessment, you will be asked to identify sources of credit for a range of different scenarios. As you'll see in this topic, there are lots of options. You may like to come back to this section when you're doing your assessment to look for some useful ideas.



Family/Whānau/Iwi

One option when you need money is to borrow it from friends or whānau. This is often the cheapest option and can be a good starting point, but it's also important to think about ways that borrowing money from people you care about can affect your relationships with them. Being clear about expectations and honouring agreed repayment timeframes is really important.

Banks

To get a loan from a bank, you need to be able to show that you are responsible with money and can pay back what you have borrowed, along with the interest and fees you will be charged.

You can get different types of loan through a bank, for example:

- **Personal loans** (usually for amounts above $2000 and up to about $80,000), which can be used to pay for life events such as overseas travel, purchases or as a way to consolidate debt. (Consolidating debt involves putting all your smaller debts together so that you only have one bill to manage and pay.)
- **Car loans.** Car loan rates vary depending on how much you want to borrow. If you're borrowing a small amount, the interest rates might be similar to a personal loan. If you borrow over a certain amount to buy a car, the bank might ask to use the vehicle as security for the loan (which means they can take the car if you aren't paying off your debt). A secured loan can mean that you are charged a lower rate of interest.

The bank will look at things like:

- your income
- whether you pay your bills on time
- whether you save any money
- whether your income is paid into your bank account
- whether you have any other debt
- your credit rating.

Digital time payment options

Pay-later options

In Aotearoa New Zealand, there are services that let you take an item for use straight away, but instead of paying all at once you can spread the payments out over six to eight weeks. Unlike hire purchase schemes, there are generally no fees or interest.

Four of these services are:

- Afterpay
- Laybuy
- Humm
- Partpay.

These services can help you to get something you want, but you can end up in money trouble if your circumstances mean that you can't make repayments.

Credit unions

A credit union is similar to a bank but unlike banks they don't make profit and they tend to operate at a smaller and more local level.

Bank and credit union interest rates are often lower than those offered by other lenders and they often charge fewer fees.

Private lenders

Private Lenders are businesses, and individuals looking for sound investments opportunities. Private Lenders tend to be more entrepreneurial and the outcomes they want from their investments often vary to those of traditional banks and this is good news!

Private Lenders who are seeking investment opportunities that are "outside the square" for the traditional Bank. These private lenders have a desire to understand your strategies and opportunities and they are prepared to assist.

Non bank private lenders often take a very different view on loan transactions than the Banks and depending on each transaction the private lender loan is often only very slightly more expensive than the traditional bank loan

Finance companies

A finance company is a company or organisation that makes loans to individuals or businesses. They make money by charging interest on the money they lend and by charging fees. Finance companies usually charge higher interest rates than banks. They will often lend money to people who can't get a bank loan.

Car dealers often offer car loans that are actually provided by a finance company. The dealer will sign you up for a car loan as part of the purchase process.

Finance companies often require lenders to secure their loans by agreeing that the finance company can take something they own if they don't make loan repayments. Not making repayments is called defaulting on your loan.

Interest rates on car loans can vary widely, so you need to shop around. If you take out a secured loan, you might be able to get a lower interest rate.

Find out more about repossession and **debt collection** on the Consumer website.

Loan shops

Loan shops are one type of finance company. If you're in urgent need of cash, a local loan shop can seem tempting. However, their interest rates can be very high.

Loan shop staff will often talk of repayment as a certain number of dollars a week, rather than focusing on the total amount you will pay back over time. However, they are required by law to tell you the total cost of the loan and have to clearly state the actual interest rate so that you have all the facts to compare.

It pays to avoid lenders that charge very high interest rates – especially if they're offering money door-to-door and don't have an office. These lenders can include "loan sharks" who may use heavy-handed techniques to make people pay up.

Loan shops often charge interest by the week on payday and people can easily end up paying many times what they borrowed. It's common for interest rates on these types of loans to be several hundred percent each year.

Store loans

A store card is a credit card that can only be used in a particular store or chain of stores. Store cards can charge for replacement or additional cards or to reprint a statement. You could also have to pay a fee to change the repayment terms and, if you don't pay on time, you may be charged a penalty fee.

Hire purchase

Stores that sell larger items such as washing machines and televisions often offer hire purchase. When you buy something on hire purchase, you can take it home and use it while you're paying it off. Hire purchase can seem like an easy way to pay when you don't have enough money to pay for something in full, especially if the deal is interest-free at first. However, it's important to find out the true cost of hire purchase before signing up.

Most hire purchase agreements come with a range of charges and fees. For example, you might have to pay a $100 set up or account fee even when you're on an interest-free deal. Some retailers insist that you buy repayment insurance as well. This insurance means that if you have a loss of income, for example, because you have a serious injury, the insurance company will continue paying your hire purchase payments.

Mobile truck shops

Mobile truck shops are often seen in communities in which people are struggling financially. The trucks sell household items such as electronic goods or clothing. People can borrow money to pay for things, often with low or no interest. However, the items mobile trucks sell are often far more expensive than the same items in shops and of lower quality.

Activities

1) Watch the video '**Credit and debt**'. Now that you know about loans and debt, what device would you give Connie?

2) Will is studying at the Southern Institute of Technology. He used a **finance company loan** to buy a $12,000 electric car. The loan has a term of five years, with an interest rate of 6.99% interest and a $10 per month account fee. After owning the car for a few months, Will has discovered that he couldn't keep up the car loan repayments.

   a. Go to the Sorted.org **debt-calculator** and work out how much Will's loan is costing him. Choose the 'personal loan' option. Note that 5 years is 60 months.

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   b. Why is Will's car loan an unmanageable debt?

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   c. If the loan is a secured loan, what might happen if Will continues to default on his loan repayments?

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3) Lissa used her **credit card** to pay for return flights to Australia. The airfares cost $691. The interest rate on her credit card is 12.9 %.

   a. Use the **Sorted.org.nz debt calculator** to find out how long it will take Lissa to pay off her credit card debt if she makes payments of $60 a month.

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   b. What will the total cost of the airfare be once she has paid it off in full?

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4) Arlo needs to buy a new fridge for his flat. The fridge he wants costs $978 and the delivery fee is $89. Arlo doesn't have the money to pay for the fridge up front, so he is going to use **after pay.** He discovers that there is a $55 set up fee for the loan and a monthly service fee of $1.80 per month. The first 12 months of the hire purchase are interest-free. After that, the interest is 20.3% per year. Arlo agrees to pay the hire purchase off in 4 years (48 months).

a. Use the **Sorted.org.nz debt calculator** to find out the true cost of the fridge. To do this, you'll need to scroll down to select the Hire Purchase option on the left-hand side of the page.

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5) Choose an expensive item such as a new bicycle or cell phone.

a. Work out a realistic price for the item by finding an example online.

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b. Identify two providers that you could borrow the money from, including one bank and one credit union.

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c. Using one of the providers work out:

i. How much would you need to borrow?

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ii. What is the term (timeframe) of the loan?

....

iii. What will the interest rate be?

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Before moving on to Topic Three, check that you understand:

- ✓ common costs associated with loans
- ✓ the following sources of credit:
  - family/whanau/iwi
  - banks
  - digital time payment options
  - credit unions
  - private lenders
  - finance companies
  - store cards.

Topic Three: Manageable and Unmanageable debt

Learning Outcome for Topic Three

- [x] Describe manageable and unmanageable debt.

Success criteria

You should complete all activities in this topic. They will help you to meet the assessment requirement of describing manageable and unmanageable debt in relation to personal finances.

Manageable debt is debt that is planned and can be repaid within your budget.

Unmanageable debt is when your debt repayments cause your budget to be in deficit. In other words, when your living costs, expenses, and debt repayments are more than the amount you earn.

Manageable and unmanageable debt can impact on your finances in various ways.

Manageable debt

Here are some positive financial impacts of **manageable** debt:

- If your debts are manageable, you may have a surplus in your budget (left over money). You can use this money to build up an emergency fund so that if unexpected events happen, you can cover their costs without getting into further debt.
- Managing your debt well can give you a good credit rating. This can help you to get a loan in the future (for example, a mortgage) and can reduce the amount of interest you pay on a personal loan.

Unmanageable debt

Here are some negative financial impacts of **unmanageable** debt:

- If your debts are unmanageable, unexpected events can have a much larger and longer financial impact because you don't have a safety buffer and will struggle to create one. If an unexpected event results in a big cost, you may need to borrow money to pay for it. This can create a debt cycle that is hard to get out of.
- If you are not managing your debt well, you will get a poor credit rating. This may mean that you find it harder to get a loan in the future or, if you do get one, you may be charged higher interest.
- Finance companies are less strict about who they lend money to than banks are but usually charge a lot more money. If you can't get a loan from a bank because of your credit rating, and desperately need some cash, you may end up borrowing from a finance company instead.
- If you miss a debt payment because you can't afford to pay that month, you might get a penalty, which adds to your debt.
- If you have taken a secured loan, you might end up losing a valuable asset such as your car. If you need your car for work, this can have wider financial impacts.

- If you can only afford to pay the minimum payment on your monthly credit card bill, you will end up paying a lot of interest. It can be really hard to get out of this cycle, as it's not easy to pay off a big bill in one month if you're already struggling to cover all your costs.

Phew! As you can see, unmanageable debt can have a big impact on your finances. It can also be enormously stressful and can impact on your well-being and your relationships with others. Thankfully, if you're struggling with your finances, there are lots of places to get help. The Sorted.org website provides lots of tips, tools and resources that can help you to manage your money, as does the **FinCap website**. You can also get free online and face-to-face budgeting advice through **MoneyTalks**.

Talking to lenders can also help. For example, if you explain to a lender that you are in financial difficulty, they may be able to arrange a finance plan for you that allows you to pay off a debt in manageable chunks. You can also organise a larger loan at a lower rate of interest and use it to pay off a range of smaller loans.

Activities

1) Read this **blog about credit card debt**. Would you describe the writer's debt as manageable or unmanageable? Justify your answer.

2) Return to the **Stuff article about a loan that a couple used to buy a new car** that you read in Activity 3. How did unmanageable debt impact on the couple's finances?

3) Read this Sorted.org guide on **How to get out of debt fast**. Share one thing you have learned with a classmate or whānau member.

4) Download the Debt Sorted booklet from the **student activities page of the Sorted in Schools website**. You can find this by selecting "Booklet" from the Media drop-down menu, and then selecting Debt from the Theme drop-down menu. Read the scenario described on page 6 of the Debt Sorted booklet. Write down three things that Jo did to make his debts more manageable.

1.

2.

3.

Before moving on to Topic Four, check that you understand:

- manageable and unmanageable debt in relation to personal finances.

Topic Four: Factors affecting credit and debt

Learning Outcome for Topic Three

- [x] Describe factors that can affect credit and debt.

Success criteria

You should complete all activities in this topic. They will help you to meet the assessment requirement of describing factors that can affect credit and debt, including explaining their impact on personal finances.

Remember that debt can be a helpful tool to help you move ahead with your life, but debt can also create big problems for your future self to deal with.

In this topic we'll be exploring some of the factors that can affect credit and debt.

As you saw in the previous topic, the main costs when you borrow money are interest and fees. These can be affected by various factors: the current finance rate, by your credit rating, and by whether your loan is secured or unsecured.

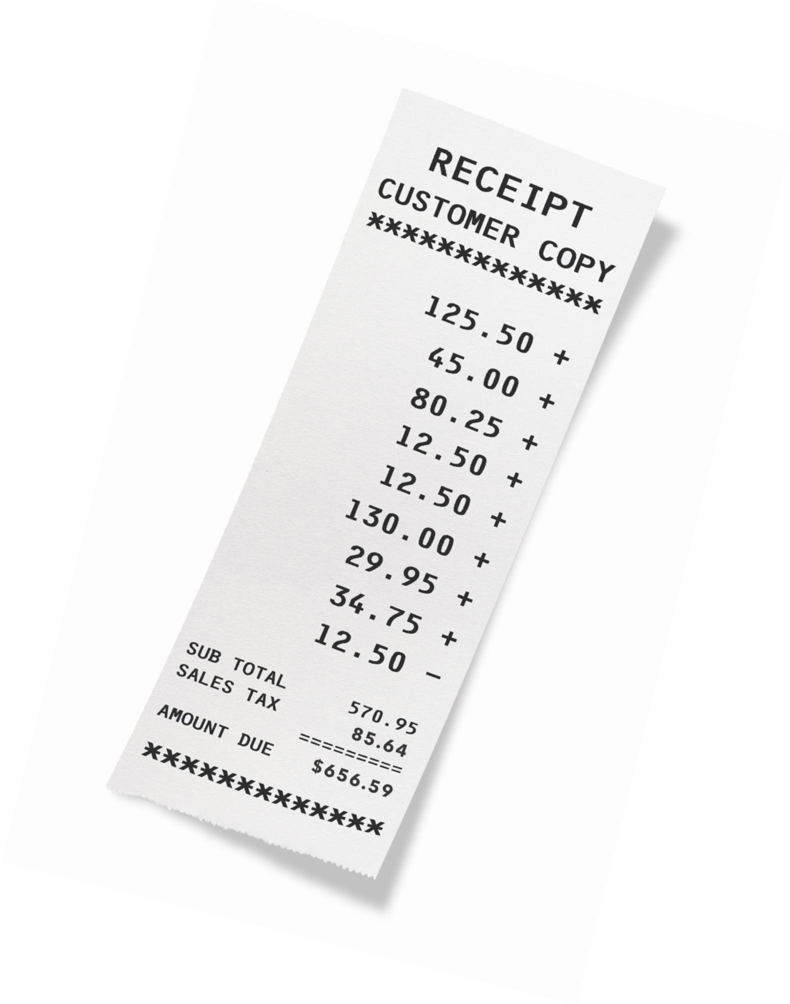
Assessment tip:

In your assessment, you need to write about **four specific factors** that can affect credit and debt.

These factors include:

- changes in circumstances
- changes in income
- interest rates
- penalties
- administration fees
- credit rating.

These factors can either affect your ability to manage debt or affect the amount of debt you have.



Factor One: Changes in circumstances

Life is full of unexpected events, and not all of them are nice. Unexpected events such as a relationship break-up, a broken tooth, or your cat getting hit by a car can affect us mentally, emotionally and sometimes physically. Unfortunately, many unexpected events also carry a financial cost that we may or may not be able to manage. These unexpected events can have a long-term impact.

But it's not all bad news – some changes in circumstances can help you to stay out of debt or get out of debt faster.

Here are some examples of changes in circumstances that can have a major impact on your finances and your level of debt.

Relationships

Being in a relationship can reduce your living costs because they are shared with your partner. If both people are working, it might be possible to live off one income and use the other income to both save and pay off debt. Paying off debt quickly can save tens of thousands of dollars in interest.

Raising children requires a significant investment of time, energy and money. Despite all the special things that come with having children, financially it can be a challenging time.

The ways people spend, save, and share money can vary a lot. Being in a relationship with someone who has different spending patterns and priorities can be challenging.

Relationship break-ups such as a separation can be very expensive, especially if lawyers are involved. If two people own a house together, they may need to sell it at a time when market prices aren't good.

Covering costs on your own can sometimes be harder than when you are part of a couple.

Changes in income

If you're a student and are living off a student loan or allowance, you can lose your eligibility for these if you fail more than half of your course. Students often struggle to get by financially, so losing sources of income may mean the end of their study.

People who are self-employed, freelancers or gig workers often have unpredictable sources of income. For example, they might get paid a large amount of money for a three-month contract but then have no work for the next few months. This means that they need to have money set aside to cover their expenses when they don't have money coming in.

Having a permanent job can create financial stability, but people's work circumstances can still change in ways they can't control. For example, sometimes people get made redundant from their jobs. If a person has taken on a lot of debt, thinking that they can manage it because they have a steady income, losing their job can quickly turn manageable debt into unmanageable debt.

In a similar way, if you have a serious accident you might not be able to work for an extended period of time. In Aotearoa New Zealand, the Accident Compensation Corporation (ACC) will cover most of your lost income but not all of it.

Your level of income can affect your ability to get credit. For example, when you apply for a mortgage, the bank will need to see evidence of your income. Getting a mortgage when you don't have a permanent job can be challenging.

Income changes can have a positive impact as well. If your pay increases, you can choose to pay off your loan more quickly, reducing the amount of interest and fees you need to pay.

These are just a few examples of ways that changing circumstances can impact on your credit and debt.

Factor Two: Changes in interest rates

Interest rates can go down as well as up, but the biggest risk for a borrower is when interest rates increase. When you borrow money, your contract may allow your lender to change the terms of your loan without your agreement, including the interest rate.

A lender does need to communicate these changes, usually within five working days, but they don't have to tell you personally. They might just put a notice on their website or on their physical premises. Checking your loan statement and your loan payments can help you to be aware of this, but there might not be anything you can do about it.

Changing interest rates can have a big impact on people who have large debts such as a mortgage. Interest rates going up can cost people with mortgages tens of thousands of additional dollars.

Factor Three: Penalties

If you are late with a repayment or do not pay back any money at all, you are breaking a contract. If this happens, a fee will be added to the amount you owe and you will have to pay extra. Penalties have to be outlined in any lending contract you sign, so it's important to read the fine print.

When you have debt, it's good to try to pay back all or part of your loan early. This can save you a lot of money on interest. If you pay a loan off early, you might have to pay an additional fee, called a break free. Lenders charge this fee to make up for the interest they would have received from you if you hadn't paid the loan back early. However, there is usually some flexibility in loans and if you're in a position to pay a loan back early, it's worth checking what your options are with the lender.

Factor Four: Administration Fees

The costs we pay for financial services. These can be fixed (a set amount per month or for setup) or a percentage (based on the amount of funds being managed). It's important to factor these fees in when we're gauging whether a decision is worth making.

Factor Five: Credit ratings

A credit rating is an assessment or judgment of how likely you are to pay money back if you borrow it. A credit report contains information about your credit rating.

Once you start paying bills and/or borrowing, you'll start building up a credit file that can show how much you've borrowed and whether you make regular payments on time, for example, on your credit card, hire purchases, car finance or your mortgage. Your internet and power payments can be recorded as well.

A credit report is a record of any bill or loan payments you haven't paid for more than 30 days and whether a lender has had to take steps to get you to make a payment. When you miss a bill or mortgage payment, you can get a negative score, which can stay on your credit record for five years. This can affect your ability to borrow money or get credit.

Lenders usually check your credit history when you apply for credit, whether it's a personal loan, a car loan, a mortgage or a new credit card. Phone and power companies might also check your credit rating. Potential landlords can also check it.

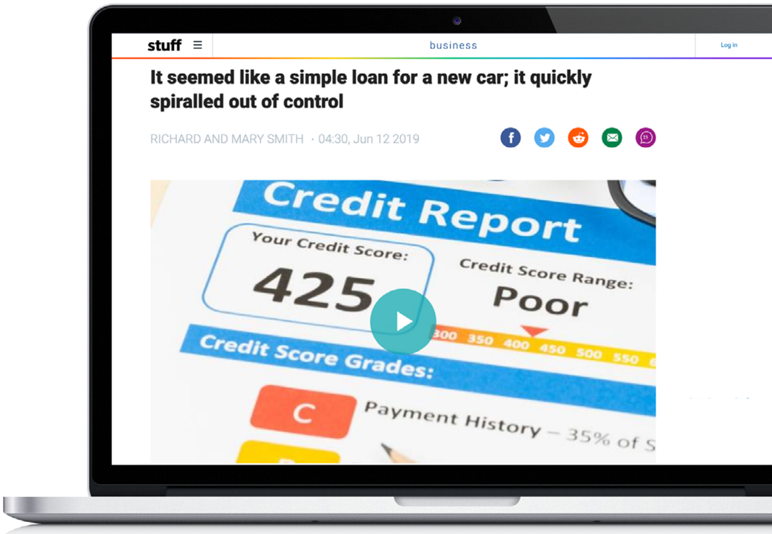
This can have some significant consequences. For example, a bank might decide not to lend you money that you need or they may charge you higher interest to cover the risk that you won't be a good borrower. Finance companies often charge different rates of interest based on a borrower's credit rating.

Activities

1) Read this **Stuff article about a loan that a couple used to buy a new car**.

Which of the following factors can you find evidence of in the article?

- ☐ changes in circumstances
- ☐ interest rates
- ☐ penalties
- ☐ credit rating.



2) Read this **Stuff article on Credit Scores**.

a. How can people find out their credit score?

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b. Can defaulting on a student loan affect your credit rating?

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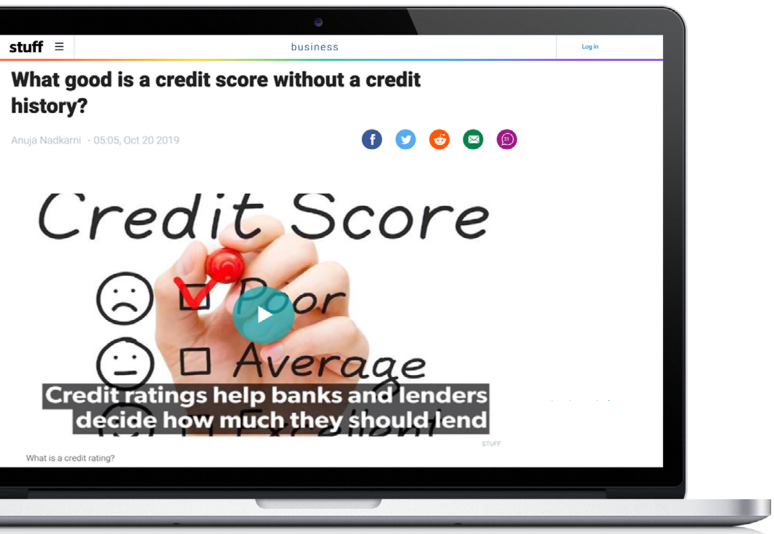


Before moving on to Topic Four, check that you understand:

✔ ways that the following factors that affect credit and debt can impact on personal finances:

- changes in circumstances
- changes in income
- interest rates
- penalties
- administration fees
- credit ratings.

Topic Five: The impact of credit and debt on personal finances

Learning Outcome for Topic Four

- [x] explain the impact of credit and debt on personal finances.

Success criteria

You should complete all activities in this topic. They will help you to meet the assessment requirement of explaining the impact(s) of credit and debt on personal finances.

In this final topic, we'll look at the impact of credit and debt on personal finances.

Assessment tip:

To get an Excellence grade in your assessment, you need to be able to explain the relationship and management of credit and debt on personal finances.

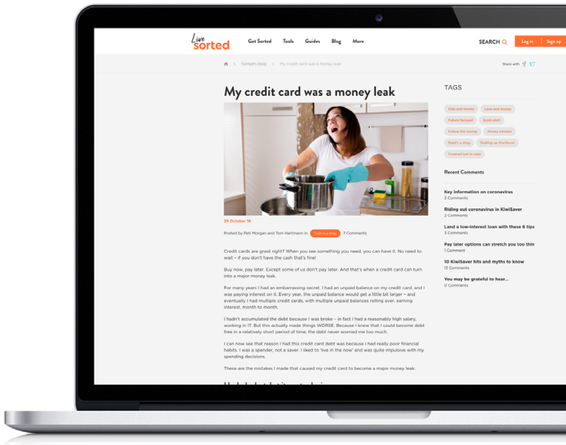
Here are some positive financial impacts of credit and debt:

- It may have a surplus in your budget (left over money). You can use this money to build up an emergency fund so that if unexpected events happen, you can cover their costs without getting into further debt.
- Managing your debt well can give you a good credit rating. This can help you to get a loan in the future (for example, a mortgage) and can reduce the amount of interest you pay on a personal loan.

Here are some negative financial impacts of credit and debt:

- unexpected events can have a much larger and longer financial impact because you don't have a safety buffer and will struggle to create one. If an unexpected event results in a big cost, you may need to borrow money to pay for it. This can create a debt cycle that is hard to get out of.
- you will get a poor credit rating. This may mean that you find it harder to get a loan in the future or, if you do get one, you may be charged higher interest.

Activities



1) Read this blog about credit card debt. Would you describe the writer's debt as manageable or unmanageable? Justify your answer.

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2) Return to the Stuff article about a loan that a couple used to buy a new car that you read in Activity 3.

   How did unmanageable debt impact on the couple's finances?

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3) Read this Sorted.org.nz guide on How to get out of debt fast. Share one thing you have learned with a classmate or whānau member.

4) Download the Debt Sorted booklet from the student activities page of the Sorted in Schools website. You can find this by selecting "Booklet" from the Media drop-down menu, and then selecting Debt from the Theme drop-down menu.

   a. Read the scenario described on page 6 of the Debt Sorted booklet.

   b. Write down three things that Jo did to make his debts more manageable.

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Before moving on to your assessment, check that you understand:

- [x] the positive and negative financial impacts on credit and debt.

Ka pai!

You've completed the Credit and Debt module. Use the checklist below to make sure that you are ready for your assessment.

Checklist for:
US 28088 Demonstrate understanding of credit and debt on personal finances

I can:

- ✓ explain what credit and debt are
- ✓ explain the difference between good debt and bad debt
- ✓ explain the following sources of credit:
  - a bank
  - a credit union
  - a private lender
  - a finance company
  - a store card (for example, hire purchase).
- ✓ explain how the following factors can impact on credit and/or debt:
  - changes in circumstances
  - interest rates
  - penalties
  - credit ratings.
- ✓ explain the impact of manageable and unmanageable debt.

Reference list

Student activities	sortedinschools.org.nz/students/activities/
Glossary	sortedinschools.org.nz/api/v1.0/download?filename=credit-and-debit-glossary&files=2451
Credit and debt module video	vimeo.com/425275556/88bd203516
What shapes my financial identity	sortedinschools.org.nz/students/activities/?category=activity-docs&tag=debt&start=0&limit=6
Tackling Debt	sorted.org.nz/guides/tackling-debt/
Debt calculator	sorted.org.nz/tools/debt-calculator
TED talk - Don't eat the marshmallows	ted.com/talks/joachim_de_posada_don_t_eat_the_marshmallow?language=en#t-317912
Mortgage calculator	sorted.org.nz/tools/mortgage-calculator
Debt sorted infographic	sortedinschools.org.nz/students/activities/?category=infographic&tag=debt&start=0&limit=6
Repossession / Debt collection	consumer.org.nz/articles/repossession
Pay Later options	
Afterpay	afterpay.com/en-NZ/how-it-works
Laybuy	laybuy.com/nz/how-it-works
Oxipay	oxipay.co.nz/
Partpay	zip.co/nz/how-it-works/
Article - a loan that a couple used to buy a new car	stuff.co.nz/business/opinion-analysis/113350799/it-seemed-like-a-simple-loan-for-a-new-car-it-quickly-spiralled-out-of-control
Article - Credit scores	stuff.co.nz/business/116461730/credit-simple-told-me-i-had-a-good-score-but-it-had-no-information-about-me
FinCap website	fincap.org.nz/
Money Talks website	moneytalks.co.nz/
Blog - credit card debt	sorted.org.nz/must-reads/my-credit-card-was-a-money-leak/
Get out of debt fast	sorted.org.nz/guides/tackling-debt/get-out-of-debt-fast/
Booklet - Debt sorted	sortedinschools.org.nz/students/activities/?category=booklets&tag=debt&start=0&limit=6

Te whai hua - kia ora!

NCEA Level: 1 (version 2)

QAAM Number: #3176

Unit Standard: #28088

Unit Standard Title:

Demonstrate understanding of
credit and debt on personal finances

Notes: