

Credit Builder Loans: Ideas for financial educators and financial institutions

Consumers have access to a variety of products and services to help them build credit. The Consumer Financial Protection Bureau's research on credit builder loans (CBLs) can help financial educators and financial institutions think through how well a CBL or another credit building product fits the financial situation and goals of the consumers they serve.

What are credit builder loans?

CBLs are designed to help consumers establish a credit score or improve an existing one, while at the same time giving them a chance to build savings. Terms vary by lender, but CBLs are typically in the range of \$300 to \$1,000 and share the same basic design. Unlike a secured credit card, CBL borrowers do not make an opening deposit. Instead, the lender moves its own funds—equal to the dollar value of the loan--into a locked savings account. The borrower is then responsible for making monthly payments. The lender releases the payment funds, minus any interest or fees, back to the borrower. Many CBL programs encourage borrowers to set aside the returned funds as savings. The lender reports the borrower's payment history to the three major credit reporting agencies as a standard installment loan, helping borrowers establish a credit history or add to an existing file.

Who benefits most from credit builder loans?

In our research, we found that consumers who have no existing debt tend to benefit more from CBLs than people with existing debt.

For borrowers without existing debt, the CBL significantly increased their likelihood of having a score and increased the score itself by up to 60 points, on average (relative to a starting score of 560).

Borrowers who had existing debt, on average, benefitted much less from CBLs. Nearly all already had a credit score, so the CBL had minimal effect on their likelihood of being scored. In addition, the CBL appeared to slightly lower their credit scores, on average, suggesting they struggled to add the CBL to their existing monthly bills.

There was some evidence the CBL helped people build savings. The estimated increase for all participants was about \$253.

About these ideas

The Consumer Financial Protection Bureau funded a contractor to evaluate the effects of a CBL. The participating midwestern credit union offered the CBL as a standalone product to customers and did not pair it with wraparound services, as some credit building programs do. A total of 1,531 people interested in building their credit participated in the study, each with a chance to open the CBL. The researchers tracked three primary outcomes: participants' likelihood of having a credit score, their actual credit scores, and their savings balances. Each CBL product and program is unique, so results will vary across programs. However, the evaluation raises important considerations for financial educators and financial institutions interested in helping consumers build their credit.

To read more about the evaluation, go to [Targeting Credit Builder Loans: Insights from a Credit Builder Loan Evaluation](#). To learn more about our work on credit, visit our [Expanding Access to Credit webpage](#). All of the CFPB's tools and resources about credit building and other topics are available on the Resources for Financial Educators webpage at www.consumerfinance.gov/adult-financial-education.

Ideas for Financial Educators and Financial Institutions

The Bureau's research on CBLs suggests that financial capability practitioners, financial institutions, and others can help consumers benefit from CBLs and other credit-building tools in the following ways:

- **Help borrowers stay current on their credit builder loans.** Our research found that about 40 percent of people who opened the CBL made at least one late payment on the CBL—this despite the fact that payments were immediately deposited into their accounts. This finding suggests that some borrowers may not have fully understood how the CBL worked, may have forgotten about a CBL payment due date, or struggled to align their cash flow with CBL payment due dates. **Financial educators** and **financial institutions** can play an important role in all of these areas: ensuring borrowers understand the terms of credit building products, have systems in place to remind themselves of upcoming payments, and time their bills around their income.
- **Help consumers stay current on other debt obligations.** Similarly, CBL borrowers with existing debt may fall behind on other loans, highlighting that **financial educators** and **financial institutions** must maintain a comprehensive view of a consumer's financial situation. A borrower may prioritize CBL payments

over other loan payments. In the Bureau's study, the CBL did appear to increase late payments on non-CBL loans for borrowers with existing debt. In helping consumers decide whether a CBL or another credit building product is a good fit for them, financial educators and financial institutions may help borrowers assess their existing debts and payment obligations, as listed in a credit report.

- **Encourage consumers to use CBLs as a savings tool.** The savings opportunity offered by CBLs appears promising but potentially underutilized. **Financial educators** and **financial institutions** may take extra steps to highlight the savings aspect of CBLs and related credit products. Goal setting and commitment exercises around savings in advance of the funds being released may increase savings activity for CBL borrowers. Financial educators and financial institutions may help borrowers consider the pros and cons of withdrawing versus saving the payments funds that are deposited into their accounts.
- **Connect CBL borrowers in need of more support to wraparound services.** **Financial educators** and **financial institutions** can partner to develop CBL programs that offer wraparound services such as one-on-one financial coaching or credit education to help consumers manage CBLs, especially if they have existing credit obligations. Wraparound services may be less necessary for consumers without existing loans.
- **Continue to assist consumers in finding the right loan or other product for their situation.** The Bureau's research showed that not all consumers interested in building their credit benefitted from a CBL. For **financial educators** and **financial institutions**, it is important to help consumers determine if a CBL is right for them. And specific loan terms vary, even among CBLs. Thus, financial educators and financial institutions must be careful to explain the structure and terms of the specific products clients are interested in. For example, some CBLs release payments back to borrowers immediately, while others release payments as a lump sum at the end of the program. One design may be a better fit for a particular consumer, so it is important to know the details of credit building opportunities presented to consumers.

Resources for financial educators and consumers

The CFPB has developed resources to help financial capability practitioners and consumers with credit education and credit building, including:

[**Want credit to work for you? Start with these steps.**](#) Colorful, compact booklet designed to help financial educators talk to consumers about how to order and review credit reports,

dispute any errors they identify, make a plan to establish or build credit, and respond to identity theft.

How to rebuild your credit. Brochure with steps that can help consumers recover from financial challenges that hurt their credit.

Building credit from scratch. Brochure with steps consumers can take to build and maintain good credit.

Check your credit report. Brochure that shows free ways to check a credit report and provides information about finding and fixing mistakes, updating information, and guarding against identity theft.

Understand your credit score. Brochure explaining that banks, credit card companies, and other businesses use credit scores to estimate how likely consumers are to pay back the money they borrow.

Where to find free access to a credit score. Brochure that provides information about obtaining free credit scores and lists companies that offer existing credit card customers free access to one of their credit scores.

You have a right to see specialty consumer reports. Brochure informing consumers about specialty consumer reporting companies and their right to get a free report from each one every 12 months.

Credit reports and scores. Website with resources to help consumers better understand credit reports and scores, learn how to correct errors, and improve their credit record over time.