Guest blog: How to build credit on a tight budget

by Tracy Becker

We need to clear something up: You do not need to be rich–or even middle-class–to have good credit.

Credit scores and income are not linked. People think income means everything, which isn't true. Income is only a factor when you're looking for a loan, like a mortgage or car loan. When it comes to building credit, everyone is on an even playing field.

Stay on track

Setting a budget is an excellent first step, it's staying on track with that budget that can become challenging for consumers. There are excellent interactive tools and apps offered online that can help consumers build, manage and stay accountable to their monthly budget. These platforms allow consumers to input bank account information and credit accounts, and set up a customized budget based on monthly obligations. Many platforms will send you automated updates, warnings, and reminders when bills are coming.

Here are a few more tips for building credit starting with the most important:

Always pay your bills on time.

Credit is a Catch-22. To build it, you need it (but not too much debt!), so that you can demonstrate that you can make payments on time. Hopefully you're paying the majority of your balance – or the full balance each month on your revolving lines and never missing a payment on installment loans. When building credit, you likely have limited credit history (which is a factor in your scores). You do not want to start off that history with bad debt or by getting yourself stuck in the cycle of revolving debt by paying only the minimum on your credit card each month.

If you have no credit, the first step is to open a credit card or secured credit card.

If you do not find a credit card that will approve you, based on limited or no history, then you can open a secured credit card. Here's the difference:

- Credit cards – These are revolving lines of credit (that don't require a deposit). They allow consumers to borrow funds–up to a certain limit–and pay them back by the monthly closing date. If entire balance is not paid back by the monthly closing date, interest is charged on the carried-over balance. Credit cards should be used responsibly since it is easy to overspend when using plastic.
- Secured credit cards – These cards require a deposit as collateral and are therefore a good option for high-risk applicants looking to build credit. Maintain a low balance and pay off your balance in full every month.

The second step is to become an authorized user.

This can help those who want to build higher scores once they have primary credit. This option is only for people who have someone in their life, such as a close relative or friend, who has substantial credit history and good payment habits. If that's the case, you can be added as an authorized user to most credit cards, and the primary holder's strong (preferably long) credit history will reflect on your limited credit. It's important to note that your limited credit will not impact the primary's credit and, even better, the authorized user doesn't need to have a card or even access to the account.

Just being authorized in addition to having cards of your own will help boost your scores. Make sure the account you are added to is much older than your primary credit accounts, the history of payments is good and the balance is not close to the limits. With these boxes checked, you should start seeing their credit reflect on yours within a few months.

The third step is to apply for another credit card

Once you have a primary card and the authorized user account shows up, check your FICO scores at MyFICO.com. Then you can apply for another card based on your new and improved credit score. There are many credit sites that offer credit cards based on varied score thresholds. These sites list they type of card, reviews, and ratings.

Remember – credit is money.

Credit cards have the power to help build your credit scores, but they should be carefully managed (especially if you're on a tight budget). It's important that you are not charging more than you can afford to pay off. If you do carry a balance, make sure it is no more than 7 percent to 10 percent of your credit limit, since high balances impact scores negatively.

By carrying a balance, you're also risking getting stuck in a "debt cycle." This is when you don't have enough income to pay off your credit card bill in total because you need that money to afford your living expenses.

A few more points:

- As a rule of thumb, credit scores are tabulated based on your credit history, balance-to-limit ratio, variety of credit, payment history and new credit inquiries. This formula can vary depending on the individual report.
- Ideally you should aim to have three to six credit accounts – a mix of cards and installment loans.
- If you plan on taking out a loan or mortgage in the future, be aware of the impact that inquiries can have on your credit. Avoid opening and closing accounts for a few years before you take out a loan.

No matter where your income stands, building credit and managing your finances takes time and strategy. Consumers need to educate themselves on credit management and reporting to fully understand the consequences of their actions. Strong credit will mean you're ready to get affordable financing when you need it. So it's important, if you don't already have credit, that you start building it now.

Author bio

Tracy Becker is the President and CEO of North Shore Advisory, Inc., a leading Credit Restoration, Education and Monitoring Company specializing in Credit Services. Tracy is a FICO Certified Professional a Certified

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