

What Is A Credit Builder Loan and How Does It Work?

"We are sorry to inform you that your loan application has been declined due to a low credit rating. You can re-apply once your credit improves."

Have you received this message when the bank turned down your loan? Do you feel like you are being charged a higher interest rate due to your low credit score? Do you know that even novice borrowers are often denied loans and mortgages citing the lack of credit history?

[Credit builder](#) loans are an excellent way to improve your credit score and overcome a rocky credit history. These loans also offer you a chance to establish a strong credit rating before you start applying for mortgages or loans from banks.

Are you excited to learn more about them? Read on!

What Is A Credit Builder Loan?

When we talk about loans, high interest rates and persistent outstanding debts come to mind. You probably haven't heard anyone say that getting a loan to build your credit score is a good idea. But a credit builder loan is quite different from a regular loan.

Credit builder loans are a blessing for anyone struggling to improve their credit rating or to establish a credit history. As opposed to the standard borrowing procedure, you pay back the sum of the credit builder loan over time before you can use the loan amount.

These timely payments ascertain that you are a reliable borrower and improve your personal credit profile. The lender reports these payments to credit agencies, who will take them

into account while calculating your credit score.

How Does It Work?

The credit builder loan works in much the same way as an instalment loan – all you have to do is make regular payments towards the loan. But you do not get access to the money that you've borrowed. Rather, this money is safely tucked away in a savings account.

Once you've paid the loan off on time, the lenders give you the initial money that you borrowed. The act of making timely payments towards the credit card loan will be counted as responsible financial behaviour on your credit history.

So essentially, a credit builder loan will improve your credit score. The good news is that this will assure lenders that you'll pay them back, so you stand to get loans with low interest rates in the future.

Many banks or loan disbursement companies do not charge any interest on credit builder loans. However, they may ask for a fixed membership fee, even if you choose to not take the loan.

Benefits Of Getting A Credit Builder Loan

Considering that you can't even touch the borrowed cash, it is only fair to question the need for availing a credit builder loan. However, as you will see in this section, the benefits of the loan truly outweigh any cost associated with it.

Easy To Repay

Since there is no interest on many credit builder loans, you only have to pay a small amount per month in addition to any monthly membership fees. Meeting a minimal target is not

considered very difficult for most people, making a credit builder loan the easiest way to improve your credit rating.

Reports To Multiple Agencies

While it all depends on your financial aid organisation, more often than not your loan repayments are reported to Experian, Equifax and Transunion. These three are undoubtedly the most premier and trustworthy credit reporting agencies.

Every major finance unit consults these agencies when enquiring about the credit rating of a loan applicant. Therefore, you can be assured that every step you take will have a positive impact on your rating.

Build Your Credit For A Major Purchase

If you are planning a major purchase in the future, then it is paramount that you maintain a healthy credit rating. Not only will it make it easier for you to get financing for your purchase, but it would also ensure that you get the best interest rates.

The monthly membership amount is small enough that everyone can afford it. And making these monthly payments alone has a positive impact on your credit rating. Repay the credit builder loan promptly, and you have a winning formula for improving your credit score.

Establish A Credit History

What if you have no credit history? Finance agencies have no way of judging the kind of borrower you will turn out to be. Therefore, they may refrain from granting you the loan or charge a higher interest.

However, if you use a credit builder loan to establish a good credit history, then it would be easier for you to get financing at the best rate in the future.

Short-term Loans

The maximum duration of a credit builder loan is six months. It is much easier to plan your repayments for this duration when compared to a loan that lasts for years. Since the loans are short term, you can take two loans in a year.

Taking multiple loans and repaying them on time has a very positive impact on your credit rating. It demonstrates that you have a history of being consistent with your repayments.

Learn To Manage Your Finances

Taking a credit builder loan can be considered as training in managing your finances. Since the repayment amount and monthly fees are small, you can consider this to be a crash course on dealing with loans. The lessons you learn with a credit builder loan will help you when you have to take a bigger loan in the future.

Improve Your Credit Score Today!

These are all the benefits of a credit builder loan, the most important of which is boosting your credit scores. You should definitely consider taking a credit builder [loan UK](#) – especially if you feel that your poor or non-existent credit rating is holding you back from getting the required financing at the lowest interest rate.

Ensure that you understand all the terms and conditions related to the loan, and there are no hidden charges that added at the end. Ask your lender exactly how much you have to pay monthly while deciding the credit builder loan amount.