

Activity 8: Beware of Car Title Loans

Instructions

- Read the scenario carefully.
- Write down some things that Michael could have done differently.
- Be prepared to explain your answers.

Scenario

Michael had \$500 in unexpected medical expenses and needed a loan. He saw a television commercial that declared, "If you have a car, you can get a loan." Michael had a car worth about \$2,500, so he decided to apply for the loan. The finance company Michael saw in the commercial loaned him \$500 at 20 percent interest per month. Note that the finance company did not advertise the APR. The finance company took his car title as collateral and Michael kept the car. With a 20 percent monthly interest rate on the \$500 loan, Michael owed \$600 at the end of the month -- the \$500 loan plus \$100 in interest. Michael could not repay the \$600 at the end of the month. The lender could have repossessed the car. However, the lender gave Michael the option of just paying the \$100 interest and gave him until the next month to pay the loan. At the end of the next month, Michael still owed \$600 (\$500 loan + another \$100 in interest) and still could not repay. By the end of one year, Michael had paid \$1,200 in interest for his \$500 loan – \$100 every month = \$1,200! This equates to a loan with a 240 percent APR. Finally, Michael received a bonus from work and was able to pay off the \$600.

This is an expensive way to borrow money! What could Michael have done differently?
