

Shopping for an Auto Loan

LESSON DESCRIPTION AND BACKGROUND

Wise consumers shop for credit just as they might shop for a car or a computer. In this lesson, to begin learning the skills needed in shopping for credit, the students fill out a credit-comparison chart for a hypothetical auto loan. Then, using the same techniques, they shop online for a loan. Finally, they compare the cost of the same loan at various local lending institutions. In the course of these inquiries, they also take account of costs of automobile ownership over and above the purchase price and credit cost.

Lesson 17 correlates with national standards for economics and personal finance as shown in Tables 1-2 in the introductory section of the publication.

ECONOMIC AND PERSONAL FINANCE CONCEPTS

- Annual percentage rate (APR)
- Auto loan
- Credit

OBJECTIVES

At the end of this lesson, the student will be able to:

- Compare costs of different loans and choose the loan with the lowest cost.
- Demonstrate how to shop for a loan online.
- Explain the factors that reduce the cost of a loan.

TIME REQUIRED

Two 45-minute class periods

MATERIALS

- A copy for each student of **Exercise 17.1, 17.2, 17.3, and 17.4** in the *Student Workbook*

ADDITIONAL RESOURCES



To download visuals, find related lessons, correlations to state standards, interactives, and more visit <http://fffl.councilforeconed.org/9-12/lesson17>.

PROCEDURE

1. Introduce the lesson's focus on shopping for automobile loans. Explain briefly that shopping for the best deal on a loan is just as important as shopping for the best deal on shoes or vacation travel or anything else. Money is money. The lowest-cost loan is usually the best choice for a borrower.
2. To shop for a loan, a borrower must first decide on the type of loan, the amount to be borrowed (principal of the loan), and the number of years to repay the loan. Then the borrower should shop for the loan with the lowest annual percentage rate (APR) of interest. The lowest APR should have the lowest finance charge (cost of the loan). If it does not, the borrower has probably been given incorrect or misleading information.
3. Discuss some of the mistakes people make in shopping for a loan.

Mistake 1: Looking for the lowest monthly payment. The monthly payment can be lowered by lengthening the repayment period. But, the longer the repayment period, the higher the finance charge over the life of the loan. Don't focus solely on the monthly payments.

Mistake 2: Not asking for the identical principal and repayment schedule in comparing loans offered by different lenders. Always compare the cost of the same loan. Don't try to compare apples and oranges.

Mistake 3: Not asking for both the APR and the finance charge. By asking for both, you will be sure the information given is correct.

4. Give each student a copy of **Exercise 17.1** from the *Student Workbook*. Ask the students to read the exercise, complete the chart, and answer the accompanying questions. When they have finished, discuss the completed chart and the answers to the questions.

Answers to Exercise 17.1:

- a. Which loan is the best deal? (**Online Lending Site.**)
- b. Which loan is the worst deal? (**Friendly Finance Company.**)
- c. Jill took the best loan. How much extra did she pay because she financed her car instead of buying it for cash? (**\$1,416.47**)
- d. How much money did Jill save by taking the best deal rather than the worst deal? (**\$2,485.38**)

5. Give each student a copy of **Exercise 17.2** from the *Student Workbook*. Because this exercise requires Internet access, it should be conducted in a computer lab or distributed as a homework assignment. When the students have completed the activity, discuss their answers with the class.

- a. Which loan has the lowest APR? (**Answers will vary.**)
- b. How do the APRs on new-auto loans compare to APRs for used-auto loans? (**Answers will vary; the students should be able to describe how these APRs appear to differ.**)
- c. Are the loan rates the same in all areas? (**No. There is variation from one region to another.**)

d. Are the loans quoted only in terms of their interest rates, or are there other costs involved? (**Some lenders require fees such as application fees or document-preparation fees.**)

6. While this lesson focuses primarily on the cost of automobile loans, it also provides an opportunity to identify other costs of owning and operating a vehicle. Ask: What are some of these other costs? (**Insurance, maintenance, repairs, fuel, parking, permits, accessories, taxes, and licensing.**)

7. Also point out that a hidden cost of buying a car is depreciation. *Consumer Reports* estimates that cars lose 45 percent of their value over the first three years of ownership. Not all cars depreciate at the same rate. *Consumer Reports*, *Kelley Blue Book*, www.CarSoup.com and other websites have information that enables consumers to learn how well different cars hold their value.

8. Tell the students that there are several organizations (and websites) that provide information for car buyers. *Consumer Reports* (online or in libraries), www.consumerreports.org, *Kelley Blue Book* (www.kbb.com), American Auto Dealers Association (www.nada.org), and carsoup.com are all sources that tend to provide neutral, unbiased information. Edmunds (www.edmunds.com) has a calculator that estimates the "True Cost to Own" a car. The calculator enables users to compare the following costs over a five-year period: depreciation, fuel, taxes, maintenance, repairs and insurance. Using tools like these can help consumers make decisions that meet their preferences and their budgets.

Completed chart for Exercise 17.1

Lender	APR	Finance Charge	Total Cost	Monthly Payment
Last National Bank	6.65%	\$1,799.00	\$18,799.00	\$522.19
Online Lending Site	5.27%	\$1,416.47	\$18,416.47	\$511.57
Car Dealer	7.24%	\$1,964.01	\$18,964.01	\$526.78
Friendly Finance Company	13.95%	\$3,901.85	\$20,901.85	\$580.61

CLOSURE

Conclude the lesson by reminding the students what they have found. Rates for auto loans can differ for many reasons, and it usually pays to shop for the best rate. The Internet has made it fairly easy to compare interest rates across a wide range of potential lenders. Doing your homework to find the best deal can save you a lot of money when you are purchasing a car. Remind the students that the same approach used in identifying rates for auto loans can easily be applied to comparing rates for auto insurance—and a lot of money can be saved by doing a little research.

ASSESSMENT

Give each student a copy of **Exercise 17.3** from the *Student Workbook*. Tell the students that their homework assignment is to explore the cost of owning and operating a new and used vehicle of their choice. For simplicity, students should pick one model of vehicle and use it to compare new- and used-car costs. The students should read the instructions to **Exercise 17.3** and go to www.edmunds.com to collect the information they will need to complete the activity. When everyone has completed the activity, have the students report and discuss their findings with one another.

You may wish to identify the new car and used car which had the highest cost and the one that had the lowest cost of ownership over the five years.

Answers to Exercise 17.3:

- What are the two biggest expenses in owning a new car during the first five years? (**Probably depreciation and fuel.**)
- What are the two biggest expenses in owning a used car in the first year? (**Probably depreciation and fuel; as the car gets older, maintenance becomes more important.**)
- What is the total cost of owning the new car for five years? (**Answers will vary.**)
- What is the total cost of owning the used car for five years? (**Answers will vary.**)

- What is the difference in cost between purchasing a new car as compared to purchasing a two-year-old car? (**Answers will vary.**)

EXTENSION

Give each student a copy of **Exercise 17.4** from the *Student Workbook*. Assign the students to work on this activity individually or in groups.

Have the students make a list of some of the banks, savings and loan associations, credit unions, and finance companies in your area; then ask them to contact four of these lending institutions and ask the loan officer at each institution what the APR is for a \$15,000 new-car loan.

The students should also ask if there are any additional fees that might add to the cost of the loan. Make sure the students ask whether customers with a checking or savings account might qualify for a lower rate.

Have the students fill in the chart for **Exercise 17.4** and compare their results to those found in **Exercise 17.2**. When they have finished, they should answer the questions at the end of **Exercise 17.4**. Discuss these answers with the class.

Possible answers to Question f. from **Exercise 17.4**:

- **Advantages:** *Local institutions may offer more assistance and personal attention than online shopping.*
- **Disadvantages:** *The Internet provides a wider range of choice for auto loans. The Internet is available 24 hours a day; local institutions are not.*