



## **Lesson Eight**

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# Cars and Loans



# the costs of owning and operating a car

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## Ownership (fixed) costs:

- Purchase price
- Sales tax
- Registration fee, title, and license
- Financing costs
- Insurance

## Operating (flexible) costs:

- Gasoline
- Oil and other fluids
- Tires
- Maintenance and repairs
- Parking and tolls





# decisions, decisions...

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## **Quality**

What level of quality do I want?

What level of quality do I need?

## **Cost**

How much do I want to spend?

## **Car Model**

Should I choose a car with a well-known name even if it costs more?

## **Research**

What do consumer magazines say about the kind of car I want?

## **Recommendation**

Do I know anyone who owns the kind of car I want?

## **Timing**

Should I wait until there's a sale on the kind of car I want?

## **New or Used**

Should I buy a new or a used car?

## **Where to Buy**

If I buy a used car, should I buy it from a dealer or a private party?



# shopping for a new car

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## Before you shop, ask yourself:

- Which car model and options do I want?
- What is the invoice price? What is the true cost to the dealer?
- How much am I willing to pay the dealer above the invoice price?
- What is the value of my present car that I will be trading in?

## Before you buy, be sure you:

- take the car for a test drive.
- make your offer to as many dealers as possible.
- compare final sales prices and buying services.
- compare financing costs from various sources.
- try to sell your old car yourself (dealers usually give better deals without a trade-in).
- decide whether you need an optional service contract.



# shopping for a used car

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**Before you shop, ask yourself:**

- **How much can I afford to spend?**
- **Which car models and options interest me?**
- **What is the cost of car maintenance?**
- **Where is the nearest shop that services the kind of car I want?**
- **Are parts readily available for the kind of car I want?**
- **What price can I expect to pay? (Check recent prices in used-car “blue books,” on the Internet, in newspaper ads, consumer magazines, etc.)**
- **What kind of financing is available?**
- **What are the costs of a loan?**
- **Do I know how to read a “Buyer’s Guide” sticker?**

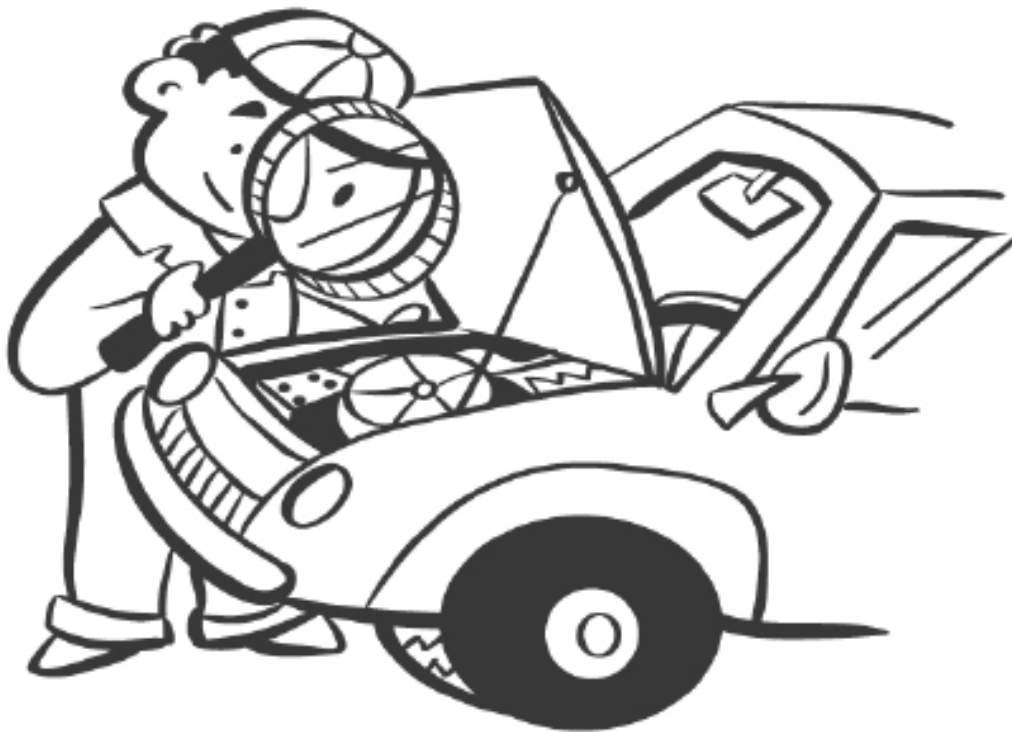


## shopping for a used car

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**Before you buy, be sure you:**

- **know the reputation of the dealer.**
- **know what type of warranty comes with the car.**
- **know what type of service contract comes with the car.**
- **ask about the maintenance history.**
- **take the car for a test drive.**
- **have the car inspected by an independent service maintenance person.**





## sources of used cars

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### New-car dealers:

- provide quality used vehicles.
- have a service department available.
- ask higher prices than other sources.



### Used car dealers:

- specialize in previously owned vehicles.
- offer only limited warranty (if any).
- may sell vehicles in poor condition.

### Private parties:

- can offer a good buy if the vehicle was well maintained.
- offer little consumer protection.

### Other sources:

- sell vehicles that have been driven many miles.
- examples: auctions or sales by government agencies, auto rental companies, the Internet



# how many prices are there?

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**List Price/Retail Price/Sticker Price:**

The price the dealership is asking for a new car.

**Invoice Price/Dealer Invoice Price:**

The price the dealer has paid the manufacturer for the car.

**Base Price:**

The price of the car before any options are added.

**Book Value:**

The value of a used car listed through resources like Kelley Blue Book at [kbb.com](http://kbb.com).

**Asking Price:**

The amount a seller wants for his/her used car. You may be able to buy the car for a slightly lower price than this.





# shopping for a car loan

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## These factors may vary between loans...

- Annual Percentage Rate (APR)
- Length of the loan
- Monthly payments
- Total finance charge

## and so does the amount you'll repay!

### Borrowing \$8,000 at different rates:

APR	Length of loan	Total monthly payment	Total finance charge	To be repaid
10.00%	36 months	\$258.14	\$1,293.04	\$9,293.04
	60 months	\$169.98	\$2,198.80	\$10,198.80
12.25%	36 months	\$266.67	\$1,600.12	\$9,600.12
	60 months	\$178.97	\$2,738.20	\$10,738.20
13.00%	36 months	\$269.55	\$1,703.80	\$9,703.80
	60 months	\$182.02	\$2,921.20	\$10,921.20



# calculating the total cost of a loan

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## To estimate the total cost of a loan:

amount of the loan x APR x number of years\*

Example:

amount of the loan: **\$10,000**

APR: **10%**

number of years: **5**

**$\$10,000 \times 0.10 \times 5 = \$5,000$  interest**

**$\$5,000$  (interest) +  $\$10,000$  (amount of loan) =  $\$15,000$  total cost**

## To estimate the amount of monthly payments:

total to be paid divided by number of months of the loan\*

Example:

total to be paid: **\$15,000**

number of months: **60 (5 years)**

**$\$15,000 \div 60 = \$250$  per month**

\* These formulas produce estimates that are slightly higher than your actual costs and payments. They do not account for smaller interest payments as you repay the loan.



# how much can you afford to borrow?

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## How much can you afford to borrow? (the 20-10 rule)

**20:**

**Never borrow more than 20% of your yearly net income.**

Example:

You earn \$400 a month after taxes.

Your yearly net income is:  $\$400 \times 12 \text{ months} = \$4,800$

20% of your yearly net income is:  $\$4,800 \times 20\% = \$960$

**You should have less than \$960 of debt!**

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**10:**

**Your monthly payments should be less than 10% of your monthly net income.**

Example:

You earn \$400 a month after taxes.

10% of your monthly net income is:  $\$400 \times 10\% = \$40$

**You should pay less than \$40 per month for all debts!**



# types of car insurance coverage

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## **General Liability (40-50% of premium)**

Pays for bodily injury.

Pays for property damage (e.g. to another person's car).

## **Collision (up to 30% of premium)**

Pays for the physical damage to your car.

Includes a deductible (paid by the customer).

## **Comprehensive (about 12% of premium)**

Pays for damage caused by vandalism, fire, floods, theft, etc.

## **Medical**

Covers medical payments for injured driver and passengers.

## **Uninsured motorist**

Pays for bodily injury in accidents caused by uninsured drivers.



# how insurance rates are set

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## **Personal characteristics**

Age

Sex

Marital status

Personal habits

Type and frequency of vehicle use

## **Geographic location**

“Rural” usually lowers rates, “urban” usually raises rates

## **Driving record**

Accident with death, bodily injury, or property damage

Number and kind of moving violations

## **Vehicle characteristics**

Damage, repair, and theft record of type and model of car

Value and age of car



## scenario 1

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Manuel wants to buy a car. He wants to know exactly how much he can afford to spend each month to own, operate, and maintain a car.

Manuel's net monthly income is \$1,280.

His fixed expenses are:

- \$350 for rent

His flexible monthly expenses are:

- \$75 for savings
- \$25 for utilities
- \$185 for food
- \$35 for transportation (bus fare)
- \$150 for tuition and books
- \$40 for entertainment
- \$20 for personal items
- \$29 for household items



If Manuel gets a car, he expects to spend about \$40 a month on gas and oil, and about \$20 on parking and tolls.

Manuel needs to have car insurance. He has shopped around and expects that a car insurance premium will cost about \$225 a month.

**1. How much can Manuel afford for a monthly car payment?**

**2. If he took a 60-month loan on a \$6,000 car at 10%, how far would he be over budget?**



## scenario 1

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Manuel needs to have car insurance. He has shopped around and expects that a car insurance premium will cost about \$225 a month.

**1. How much can Manuel afford for a monthly car payment?**

*\$86*

**2. If he took a 60-month loan on a \$6,000 car at 10%, how far would he be over budget?**

*\$41.48*



## scenario 2

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Rose is thinking about buying a car. She has \$1,000 saved for a down payment. She wants to know how much she can afford to spend each month on a car.

Rose brings home \$926 each month from her first job. She brings home \$974 from her second job.

Her fixed expenses include:

- \$250 for rent
- \$34 for a credit payment on furniture

Her flexible monthly expenses include:

- \$100 for savings
- \$20 for telephone
- \$175 for food
- \$45 for transportation (bus fare)
- \$70 for tuition
- \$20 for school supplies
- \$40 for clothing
- \$40 for entertainment
- \$20 for household supplies
- \$29 for personal items



If Rose gets a car, she expects to spend about \$60 a month on gas and oil, and about \$30 on parking and tolls.

If Rose gets a car, she will need car insurance. She expects her car insurance premium to be about \$175 a month.

**1. How much can Rose afford for a monthly car payment?**

**2. If he took a 60-month loan on a \$6,000 car at 10%, how far would she be under budget?**





## scenario 2

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If Rose gets a car, she expects to spend about \$60 a month on gas and oil, and about \$30 on parking and tolls.

If Rose gets a car, she will need car insurance. She expects her car insurance premium to be about \$175 a month.

**1. How much can Rose afford for a monthly car payment?**

*\$156*

**2. If he took a 60-month loan on a \$6,000 car at 10%, how far would she be under budget?**

*\$28.87*