Managing Your Family's

Cooperative Extension Service
Michigan State University

Extension Bulletin 488
(Formerly Folder F-240)
Home and Family Series

BY LUCILE KETCHUM
Extension Specialist in Home Management

RUTH MASON SIGHS as she looks over the bills for the month, trying to think how they'll stretch the paycheck that Jim will bring home tonight. Groceries will take $150. Then there's the house payment, light bill, payment on the new washer, payment on the car, shoes for Johnnie, and the telephone bill.

Already it adds up to almost as much as Jim's paycheck will be.

And there's that bill for the things she charged at Jones'. A birthday gift to buy for Susan. Allowances for the children. And Jim really needs a new suit before his trip to New York at the end of the month. They've been planning to get it from month to month but there never seems to be enough cash to go around.

Ruth decides she'll talk with Jim about getting the suit on an installment plan. They never have bought clothes "on time," but she sees no other way to get the suit by the time he needs it.

And so it goes — another "easy" payment!

MORE DEBT: GOOD OR BAD?

Many other families are in the same boat as the Mason's — using more and more credit to buy the things they want.

Some folks say this is a bad situation. Others say it's good — that wide use of credit is one of the things that helps to give us such a high standard of living in America.

Good or bad, certainly many families and individuals *do* use credit in order to enjoy today — rather than waiting until they can save the purchase price — such things as automobiles, refrigerators, automatic washers, education, and even vacation trips. Others use credit in the form of a charge account simply as a convenience. Still others borrow money to meet emergencies, such as illness or being out of work. And some folks say that buying equipment and furnishings for the home on the installment plan is a way of saving — that they wouldn't be able to save the purchase price of such items without a contract to make them do it. Moreover, some will say, even though it costs more to buy "on time," it's worth the extra cost to have certain conveniences and comforts while the family is growing, rather than to wait until enough savings can be accumulated.

IT'S HOW YOU MANAGE CREDIT THAT COUNTS

Whatever your reasons, using credit in itself isn't necessarily good *or* bad. It's the way you use it that means either benefits or problems for you.

You have to manage credit. If you don't, your debts will manage you — keep you from doing and having many things you really want.

You may not have thought of it in this way, but actually your credit — the confidence others have in you which makes it possible for you to borrow money or to buy on time — is indeed a valuable personal asset.

The purpose of this leaflet is to bring together some ideas which may help you use credit to your advantage.

We're Talking About "Consumer" Credit

We are not talking about the mortgage on your home.

In the space of this leaflet we will concern ourselves only with **consumer credit.** By this, we mean the kind of credit that families use to buy consumer goods and services — cars, television sets, washing machines, vacation trips, college expenses — things that are "consumed" (used to provide the kind of living a family wants). Consumer credit is short-term credit — usually within the range of 1 to 36 months.

Its use has ballooned in recent years, and buying on credit rather than paying cash now seems to be the usual pattern of family money management. Moreover, retail dealers and lending agencies all compete with each other to get more and more of us "on the cuff."

It's Your Money

In general, extending credit widely has provided a useful service for families, **but it is not a free service.** It costs money to buy "on time" or get "instant cash" from a lender. So it will be worth your while to compare costs of credit from different sources — just as you compare costs of furniture or automobiles.

There's another hazard. Credit sales often are promoted in such a fashion that people may be tempted to buy more than they can afford. One more "small monthly payment" may seem hardly worth thinking about but when all the payments are put together they can add up to trouble. The very characteristic that makes installment credit a convenient means to provide a better living can result in a burden of debt that takes half a man's pay check — or more.

So — it pays to ask a few questions before you sign the contract.

ASK YOURSELF THESE QUESTIONS

There are three big questions you ought to ask yourself. They are:

1. Shall I use credit for this particular purchase?
2. Have I found the best credit "buy" that I could?
3. How is my credit rating?

Let's look at the questions one-by-one.

Question 1. — Shall I use credit for this purchase?

Before you answer this question, ask yourself and answer — several others:

(a) *How will the payments fit into my family's regular spending?* If you haven't been in the habit of budgeting (planning expenses before you spend), now is the time to start — before you take on installment payments. Will you have to go without necessities or other items that are more important to your family than this purchase? No one else can give you the answer. Sometimes it's learned the hard way, by living with installment payments that are too big for your income. Sitting down together as a family and figuring all your living expenses ahead of time isn't easy — but it might save a great deal of real trouble.

(b) *How much will credit cost us?* What's the difference between the cash price and the price you'll pay if you buy "on time"? Is it worth the cost to you to be able to make the purchase now on credit, and pay later? Or would it be better to use savings? Or to wait until you can save enough to pay cash?

(c) *Will whatever we are planning to buy outlast the time we'll be making the payments?* Give long service? (It's no fun to pay for "dead horses"!)

(d) *Is this something that we will want as much when we are making the payments as we do now?*

(e) *Will it mean better family living?* (Save time? Save energy? Give satisfaction to the family? Protect health? Make it possible for you to increase income?)

(f) *Is our income certain for the length of time that payments will run?* And do we have enough life insurance protection to cover the debt?

Question 2. — Have I found the best credit "buy"?

The main sources of consumer credit in Michigan are:

(a) Lending agencies
- Credit unions
- Personal loan departments of banks
- Small loan companies
- Sales finance companies (Companies that take over credit "paper" from dealers. Examples: Commercial Credit Corporation; Universal Credit Corporation; General Motors Acceptance Corporation; Associates Investment Corporation.)
- Pawnshops

(b) Retail sales establishments
- Department stores, specialty shops, appliance stores, auto sales, for example. Such companies as Sears, Penney's — even dime stores — now offer credit service.

The charges from these different sources vary a great deal. Take time to investigate. Find out what kind of service you can expect, what the cost and repayment terms will be. **Do this before you make a bargain, for once you sign a contract, you're committed to carry out your part.**

Find Out the Dollar Cost. You probably compare prices on shoes, dresses, coats, housewares. Why not on the cost of credit?

Credit costs vary widely among different lenders and among stores that sell on the installment plan. In fact, costs may differ considerably among the various "plans" available from a single store.

It will pay you to take time to get the facts. You need to know more than the down payment and monthly (or weekly) payments — so take time to check your contract. The contract should give you enough information so that you can figure how much a credit plan will cost you in total. You need to know:

(a) how much is to be financed;

(b) the amount of each installment payment; and

(c) the number of installments.

This is the way you figure cost: Multiply the amount of the monthly payment by the number of payments to be made. From this figure subtract the amount that is to be financed. The difference will be the dollar cost of credit.

EXAMPLE:[1] — A refrigerator costs \$300 and can be paid for by making a \$12 down payment and 12 monthly payments of \$25.92 each.

Multiply payment amount × number of months to be made (\$25.92 × 12)	\$311.04
Subtract the amount financed (Cash price minus down payment) \$300 — \$12)	\$288.00
Dollar Cost of Credit	\$ 23.04*
Total cost when bought on credit (\$300 cash price plus \$23.04 credit cost)	\$323.04

** Cost of credit equals \$8 per \$100 per year on unpaid balance of \$288. This is equivalent to a simple annual rate of 14.8%.* *See chart, page 4.*

Find Out the "True" Annual Interest Rate — If You Can. As the use of installment credit has increased, a great deal of confusion has developed over interest rates. As a result, it has become extremely difficult — sometimes impossible — for a consumer to compare the cost to him of credit from the bank, the credit union, the department store and other sources.

"Truth-in-lending" legislation was proposed in 1961 and there have been extensive hearings on the bill. Proponents say that the consumer "has the right to know." Opponents (some lenders and retail establishments) argue — among other things — that it is impossible to figure accurately what the true annual interest rate would be on installment

[1] *Table from "Consumer's Quick Credit Guide," United States Department of Agriculture publication, June 1964.*

payments as they are commonly set up. There is some truth in this claim, but the consumer could be given much more exact information about interest rates than he usually is given.

This Is What the Trouble Is All About. In commercial lending and in the early days of personal lending, most loans were single payment loans. Under this plan, it is customary to borrow a sum of money for a period of time — say six months or a year. At the end of the period the usual agreement is that the borrower will repay the amount of the loan plus interest figured at a stated rate per year. For example, if a person should borrow $500 at 6 per cent and repay it at the end of the year, the interest charge would be $30 ($500 × .06). However, if he should repay at the end of six months his interest payment would be $15 because he would be charged **only for the time** that he had the money. You could say that paying credit charges is like paying rent on a house — you pay for the **use** of money for a certain period of time.

Borrowers sometimes have trouble saving up enough cash to repay a single-payment loan when it falls due, so installment credit plans were invented as a convenience service — a convenience for both lenders and borrowers.

But lenders charge for this service in different ways. This is where the confusion begins when you try to compare costs of installment credit plans.

If you take the yearly rate as a measuring stick, the tables below show about how **rates** compare in the case of two commonly used ways of stating credit charges.

Be Careful with Retail Credit! Suppose you are buying a washer or a television — or whatever it may be — your interest in getting a "best buy" in merchandise can blind you to the possibility of a "best buy" in credit. So, when you buy on time, pay attention to finding out exactly what the total cost of the credit purchase will be — the total when you add the down payment and all of the monthly payments. Compare this total to the cash price of the item and to credit costs from other sources. Examine all parts of the contract **before you sign,** in order to be sure that you know what agreements you are making .

Find Out About Service. As you shop for credit consider other factors besides cost. What service will you get? Are payment arrangements convenient? Are the payments spread over a long enough time so that you can handle them along with your other expenses? At the same time, is the repayment schedule set up so that you will pay off the loan as quickly as possible to save financing costs? And by how much will you be able to reduce credit costs by paying ahead of schedule?

TYPICAL CHARGES FOR INSTALLMENT CREDIT*

Based on the beginning amount owed

If charges are based on the beginning amount owed and are included in the 12 equal monthly installments —

With a charge of:	Simple annual rate is:
$ 4 per $100 or 4% per year	7.4%
$ 6 per $100 or 6% per year	11.1%
$ 8 per $100 or 8% per year	14.8%
$10 per $100 or 10% per year	18.5%
1% per month	22.2%

(For a short cut, you could say that in this kind of plan the "true" annual interest rate is about double the figure stated.)

Stated at a monthly rate, on unpaid balance

Credit unions, small loan companies, and some other lending agencies use a **monthly rate** (instead of an annual rate). But they commonly charge interest only **on the unpaid balance** — rather than the original amount of the loan.

If charges are at a monthly rate, and are on the unpaid balance —

With a charge of:	Simple annual rate is:
¾ of 1% per month on unpaid balance	9%
⅚ of 1% per month on unpaid balance	10%
1% per month on unpaid balance	12%
1¼% per month on unpaid balance	15%
1½% per month on unpaid balance	18%
2½% per month on unpaid balance	30%

* *Tables from "Consumer's Quick Credit Guide," United States Department of Agriculture publication, June 1964.*

Will you receive pleasant, courteous treatment and privacy in doing business with the lender or the store? Will there be a penalty if you miss a payment? What does the contract say about repossession of goods? Does the lender or store have a good reputation for doing business in a sound and fair way — or at least does he **not** have a bad reputation?

Select the credit plan best suited to your needs — regular 30-day charge account,[3] 90-day account, revolving account, installment account, single payment loan, or installment loan. (There are variations of these, but these are the main choices you'll have.)

What do you promise to do? Be sure you know before you sign the contract, because when you sign, you agree to all the terms stated. And now the last — and a very important — question.

[3] *There are few regular 30-day accounts today. Most stores offer an "optional" account. As a customer, you may manage the optional account as a "regular" one by paying within a specified time limit. However, if you do not pay on time, the store will carry the account as a "revolving" or "budget" account — which means that they will add a carrying charge. This is usually 1 to 1½% per month (12 to 18% true annual interest).*

Question 3. — How Is My "Credit Rating"?

You often hear it said that it is an advantage to establish credit, but perhaps not as much is said about keeping your credit good. Once you establish credit, you are watched — not only your record of payments, but any reports about your activities from newspapers and other sources. Through the National Credit Exchange your credit rating follows you all over the country — and even to some foreign countries.

KEEP YOUR CREDIT GOOD!

Protect this valuable property — your credit:

Make payments promptly, at the agreed time.

If you are unable to meet a payment, call your creditor or visit him and tell him what you will be able to do.

Be especially careful to protect property until it is paid for.

FOR FURTHER READING

Black, Hillel, *Buy Now-Pay Later*. New York, William Morrow and Co., 1962.

Cobleigh, Ira U., *How and Where to Borrow Money*. New York, Avon Books (The Hearst Corp., 959 Eighth Ave., New York, N. Y. 10019).

Neal, Charles, *Sense With Dollars*. Garden City, N. Y., Dolphin Books (Doubleday and Company, Inc.), 1965.

Troelstrup, Arch W., *Consumer Problems and Personal Finance*. New York, McGraw-Hill, Third Edition, 1965.

Unger, Maurice A. and Harold A. Wolf, *Personal Finance*. Boston, Allyn and Bacon, 1964.

Michigan State University Publications

Business Facts for Families, Bulletin E-358.

Family Investments, Bulletin E-340.

Planning the Use of the Family Dollar, Bulletin E-256.

Record of Important Family Papers, Bulletin E-451.

MSU publications are available from your County Extension Office, and from the MSU Bulletin Office, P.O. Box 231, East Lansing, Mich. 48823.

MSU BULLETINS DEALING WITH OTHER HOME MANAGEMENT TOPICS

Management in Families	
What Is Home Management?	Extension Bulletin E-452
Decision Making	Extension Bulletin E-453
Managing Resources	Extension Bulletin E-454
Process of Managing	Extension Bulletin E-455
How Does a Young Wife Manage?	Extension Folder F-294
Values in Living	Extension Bulletin E-416
How Many Persons Is a Homemaker?	Extension Bulletin E-415
Choosing and Using	
Your Automatic Dishwasher	Extension Bulletin E-388
Your Automatic Clothes Dryer	Extension Bulletin E-389
Your Refrigerator	Extension Bulletin E-390
Your Food Freezer	Extension Bulletin E-391
Your Automatic Washer	Extension Bulletin E-392
Your Household Range	Extension Bulletin E-393
Your Cleaning Appliances	Extension Bulletin E-442

Electricity in the Home, Extension Miscellaneous Series CE-29

MSU publications are available from your County Extension Office and from the MSU Bulletin Office, P. O. Box 231, East Lansing, Michigan 48823.

Issued in furtherance of cooperative extension work in agriculture and home economics, acts of May 8, and June 30, 1914, in cooperation with the U.S. Department of Agriculture. George S. McIntyre, Director, Cooperative Extension Service, Michigan State University, East Lansing, Mich.

2P—30M—11:67—JH