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THE LURE OF BUYING ON CREDIT

You and I - as consumers - owe banks, finance companies and retailers more than $220 billion, or about 20 percent of our annual disposable personal incomes. And these figures do not include our home mortgage loans. Personal bankruptcies resulting from inabilities to pay some of these debts are at an extremely high level. In this Newsletter we will look at some of the pitfalls to be avoided in buying on short-term consumer credit.

The charge account is one of the oldest forms of personal credit - in effect lending the customer money for a short period of time. Under the ordinary arrangement, items are "charged" on "open" account in the merchant's books and paid for by the buyer at his convenience during the subsequent month. There may be an application for credit with some answers on the form checked out, but there is usually no formal instrument executed on each sale such as a promissory note or contract. Usually there is no interest charge if paid promptly although general prices in the store may be somewhat higher to help defray the dealer's added costs.

The amount of credit the individual is able to obtain in this way depends largely upon the store's policy about extending credit and the individual's general reputation as to ability and willingness to meet his or her obligations.

These are known as "convenience" accounts because they are often times used by people who are able to pay cash. Sometimes they represent "prestige." The store owner often considers it as a way to increase his sales and profits without having to increase prices. Unfortunately, this is one of the easiest kinds of credit to abuse or misuse.

Large debts can be piled up with little restraint.

Today, about 80 percent of short-term credit is "installment credit"; nearly half of which is held by banks either through direct loans to the consumer or by buying the consumer's promissory note from the retailer.

Under any of the possible arrangements, there are some features that are much different than the charge accounts noted above. Nearly all are based on formal applications with signed documents attesting to the transactions and methods of repayment. Most carry an interest and other charges and are usually "conditional sales" contracts.

Under the charge account, title to the property purchased passes directly to the buyer at the time of the transaction. Under a conditional sales contract, title to the goods remains with the seller (or whoever buys the contract). Installment loans from banks or other financial institutions usually require some type of collateral or security, either by title to the item purchased or some other asset owned by the borrower.

Where title to the goods remains with the seller (or lender) until final settlement, failure to make prompt payments can result in repossession of the goods purchased or listed on the contract. Under open-end or revolving type of arrangements, all items purchased over an extended period of time and added to the original contract may legally be repossessed since title for none of them passes until all have been paid in full. Buyers should be particularly wary of this type of contract.
Under installment plans, there is usually a down payment with regular payments adjusted to the buyer's pay days. They cover both the principle and interest and any other charges.

Most retailers and lenders are honest and are required by the truth-in-lending law to tell the customers the annual percentage rate of interest (APR) they are charging. This can be used to make direct comparisons along with comparing total costs. However, retailers also extend this type of credit primarily to increase their sales. In this effort, some go to great lengths to encourage buying "NOW on these favorable terms..." Some few high-pressure sellers are not legitimate retailers and use many ploys to take advantage of unsuspecting consumers. Following are some additional pointers to watch out for before signing any contract:

- Do you really need or want it badly enough to tie up future earnings?
- Is everything to be delivered or work to be done completed? Is everything in writing?
- Can you meet the payments without undue stress with all your other regular bills and payments?
- Have you checked the annual percentage rate of interest (APR) and total costs with those available from other sources?
- Could you make a larger down payment and save dollars?
- What have you given as security? What would you lose in case of default?
- Does the contract give rights to some of your other property?
- Who will you be paying? Are there any grace periods? How will faulty work or merchandise be handled? - if someone else buys the contract?
- Is there an acceleration clause? - default in one makes all due and payable?
- Can you take the merchandise out of the county or the state?
- Do you have to carry insurance on the goods or your life? Can you pick your own insurance company?
- Are there any balloon clauses - very large final payments that you may not be able to make in one month and thus have to refinance?
- How much of your pay check will be tied up in payments?

There is not much of a problem in obtaining retail credit or borrowing. The main problem of credit is to resist it and be able to make the payments on time. The family should be aware of how much it is costing them in terms of the price of the item, plus the interest and other charges, to have the item today to be repaid from future earnings.

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