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Financial Literacy for the Roma



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# 3

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## WHAT IS THE CONTENT OF THE MODULE 3: SENSIBLE BORROWING?

**TOPIC 1. DEBT MANAGEMENT: HANDLE BORROWING  
WITH CARE**

**TOPIC 2. THE COST OF BORROWING**

**TOPIC 3. CHOOSING A LENDER AND A TYPE OF LOAN**

**TOPIC 4. CONTROLLING DEBT**





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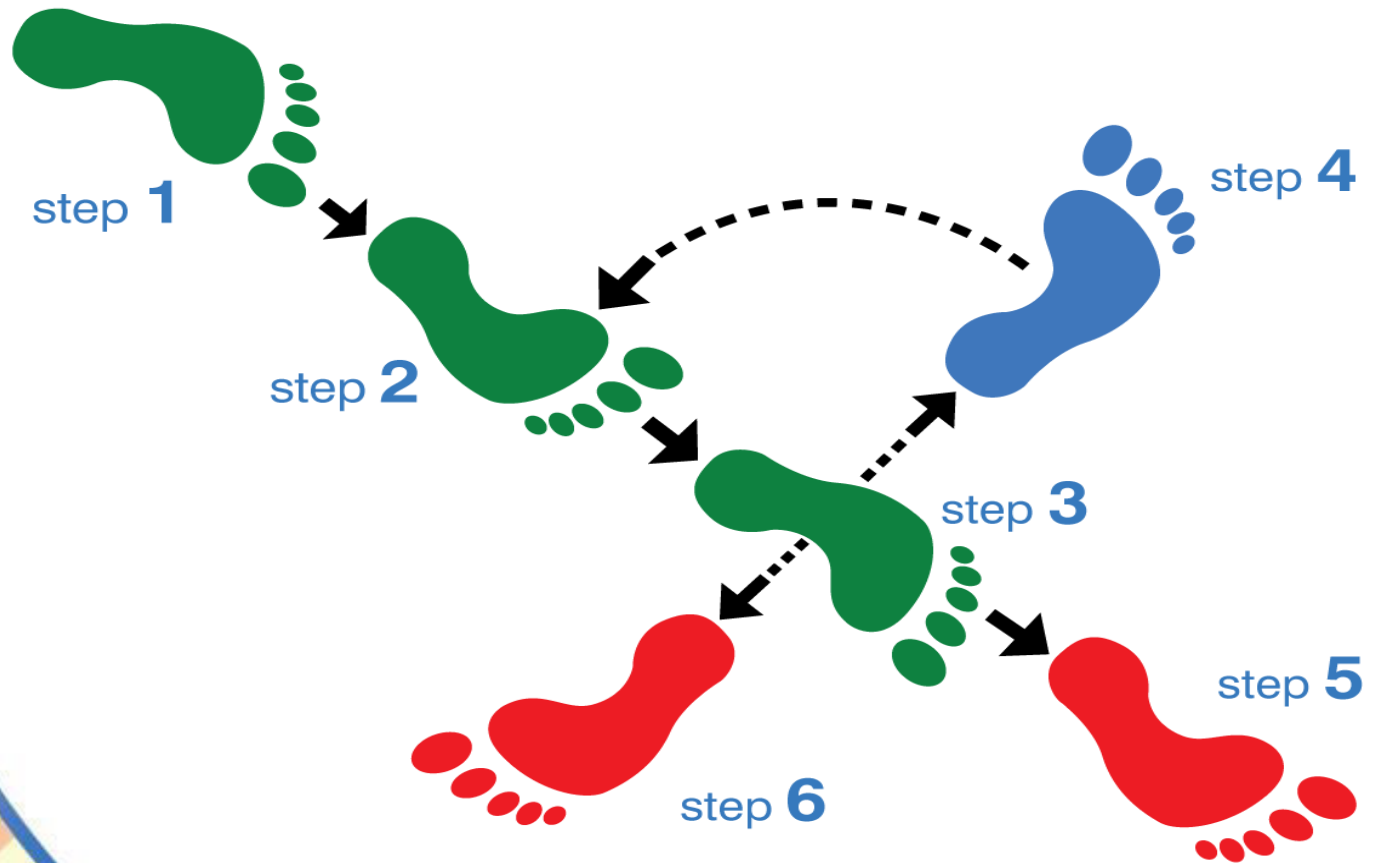


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## 3+3 steps Clever Path





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## 3+3 steps Clever Path



- ✓ How can I borrow money?
- ✓ Where can I get it from?
  - ✓ At what cost?



## TOPIC 1. HANDLE BORROWING WITH CARE

What are your usual reasons for extra costs?  
Have you ever borrowed money ?  
Who borrowed you the money ?  
How difficult was it for you to return the  
money?





## Borrowing experiences (Exercise 3a)

<b>Source of money to borrow</b>					
Family members, relatives and friends					
“Loan sharks”					
Developing/humanitarian organization					
Credit cooperatives					
Banks					
...					



## Borrowing experiences (Discussion)



*What are legal sources of money to borrow?*

*What must be accompanied by an applicant for a loan?*

*Is it possible to get a loan for poor people ?*

*What is collateral ?*

### **General borrowing tips:**

- ✓ *Do not borrow more money that you really need.*
- ✓ *Spend borrowed money wisely, and stick to your plans.*



## TOPIC 2. THE COST OF BORROWING

*What is a loan agreement ?*

*What are the costs of borrowed money?*

*What are interest payments?*

*What is a loan calculator?*

*What is an informal loan?*







## TOPIC 2. THE COST OF BORROWING

### LOAN AGREEMENT

- ✓ formal agreement signed between a lender and a borrower

### BORROWED MONEY COST

- ✓ compensation for a person (institution) who borrowed money

### INTEREST PAYMENTS

- ✓ money you should repay to the lender in addition to the principal amount

### LOAN CALCULATOR

- ✓ a system that allows the borrower to project how much and how long will it take to repay the borrowed amount

### INFORMAL LOAN

- ✓ a loan between parties that have no legal license to give a loan





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## Loan calculator (Exercise 3b - part 1)



- ✓ Click to the link <http://www.calculator.net/loan-calculator.html>
- ✓ The calculator has different active cells in which you must enter values.
- ✓ Commonly, you will decide upon the loan amount, term of loan, and possibly the way you are supposed to secure the loan repayment with depositing some money to the bank.





## Loan calculator (Exercise 3b - part 2)

Entering data in the right cells. The calculator itself gives results which are usually given in a form of a total amount of money they should repay at the end of the loan period, or the amount of annuity. The result is sensitive to any change in data entered in active cells. It is highly recommended to proceed with this exercise in a case study manner, with parameters to change (provisory or taken by real bank offers). For example, an introductory example may be done with the following values:

- The LOAN amount: 1,000
- Interest rate (if applicable): 3%, 5%, 7%
- Loan term (in years): 1, 3, 5
- Total monthly (annual) payment (variable to be discussed)





## How to calculate interest payments without the help of a loan calculator (Exercise 3c)

$$\text{LOAN} \times \left[ 1 + \text{INTEREST RATE} \right] =$$



**ANNUAL  
REPAYMENT**





## Effective interest rate I.

- ✓ the higher nominal interest rates the higher the effective interest rates, other things being equal
- ✓ the more frequent repayment the higher the costs of borrowing, since after each repayment you effectively use a smaller amount of money
- ✓ different currencies have different interest rates
- ✓ bank charges higher interest rates when it lends currency that may lose its value against the other currencies





## Effective interest rate II.

- ✓ What looks cheaper at the first glance, may eventually turn into an expensive alternative, it would be wrong for an average bank customer to try guessing what will be cheaper at the end.
- ✓ Banks are better in doing business with different currencies, so that probably all foreseeable changes in relative value of one currency to others are already built in interest rates.
- ✓ The best way is to borrow the currency in which you will probably need to pay your expenses, that way, you will avoid paying extra money when converting one currency into another.





## TOPIC 3. CHOOSING A LENDER AND A TYPE OF LOAN

*Which bank lends me the money under the best conditions ?  
What questions should I ask in the bank?  
How long does it take until I get a loan ?*





## *In the bank office – understanding loan application procedure (Exercise 3d – part 1)*

Step 1: The client introduces himself to the bank officer. Let the client be 30 years old, male, full time employed with regular monthly income. He is supposedly married, with 3 children (2 at school), with the unemployed spouse.

Step 2: The bank officer asks him to explain the reasons for applying.

Step 3: The client may respond that he needs to take a loan for renovation of the premises where he lives with his family. The client has calculated that he would need 5000 for the renovation. He has seen a TV ad of a promotional bank offer, and he has heard from friends and colleagues that they offer good conditions compared to other banks.





## *In the bank office – understanding loan application procedure (Exercise 3d – part 2)*

Step 3: The client presents basic facts and documents about his financial standing. For instance, the client may respond that his regular monthly income is 850 euros (or what is appropriate for each country), and additional income in the family comes from children allowances (105 euro per a month).

Step 4: The bank officer presents a bank offer for a loan. The officer has to present the offer of his bank to the client (based on a real bank offer) and explain the advantages of the product, borrowers' obligations and the requirements he has to meet to be an eligible client.

Step 5: The client goes through the bank offer, and asks questions about the offer.

Step 6: If the terms are acceptable, the client will start a formal application, and wait for an approval.





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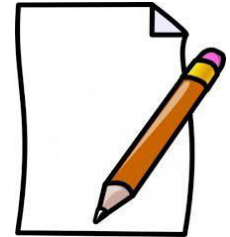
*Which alternative is best for borrowing money?  
Can I get a loan even though I am not employed ?  
How long will the process of granting a loan take ?  
What is the protection of borrower rights ?  
What does refinancing a loan mean?*





## Choosing between different borrowing sources (Exercise 3e)

Source of money to borrow	Type of loan	Cost of borrowing	Requirements to get the money	Duration of procedure	Protection of borrower rights
Family members, relatives and friends					
“Loan sharks”					
Developing/humanitarian organization					
Credit cooperative					
Bank A	Consumer loans				
Bank A	Debit card with overdraft				
Banks A	Credit cards				
Bank B	Consumer loans				
Bank B	Debit card with overdraft privilege				
Banks B	Credit cards				
....					



## What do you know about loans? (Exercise 3f)

### Meeting with brothers Horvath

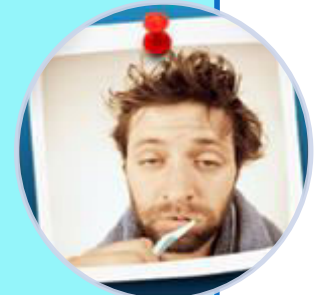
- Waiter
- Monthly income 700 euro + 100 euro tips

Peter (30 years)



- Unemployed
- Monthly income 200 euro from the state support

Jan (28 years)





## Brothers Horvath informed us about loans



### Credit card "loan in your pocket,,

- it is a payment card due to it you can withdraw money or to pay by money which are not yours.
- certain period of time is this "pocket loan" for free, but then you have to pay some money back as an interest despite of borrowed money.



### Interest rate "money produces money,,

- "borrowed money to the bank"
- the interest rate on the market depends on the amount of interest the central bank
  - for deposits is the price paid by the bank to the client
  - for loans is that the amount paid by the client to the bank





### ***Credit card***

- ✓ regularly used for bank customers to borrow money
- ✓ kind of product available only to best borrowers
- ✓ if you do not have regular income, or permanent employment, or you have already taken excessive amount of debt, your application for credit card may be easily turned down

### ***Debet card***

- ✓ filled with your own money, the money that you already put in a bank (deposited at a bank)
- ✓ used by a customer to borrow money
- ✓ excessively high costs



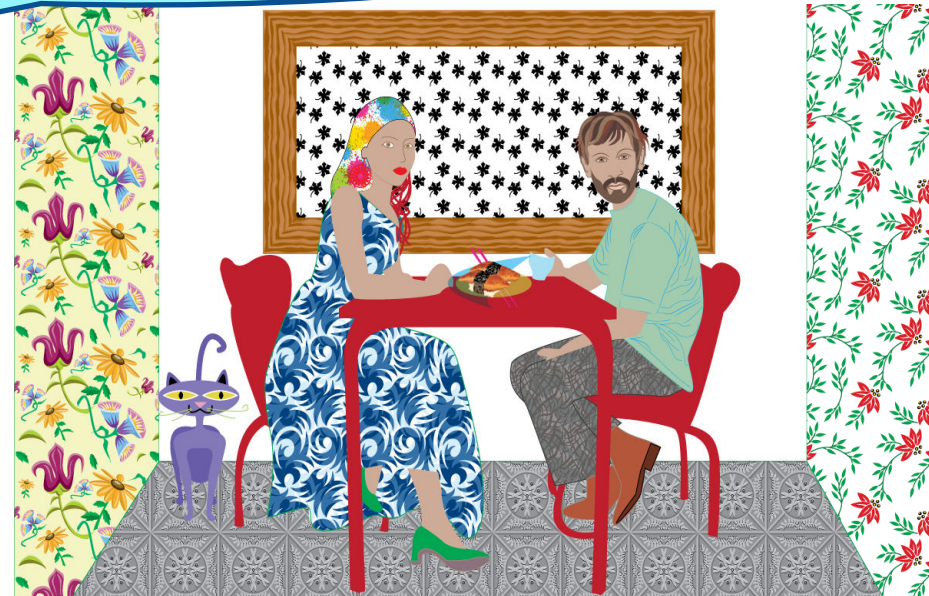
## Bank card tips

- ✓ read carefully and find right figures in the bank loan offer or loan contract before get it signed.
- ✓ avoid over-drafting your debit card/checking account.
- ✓ if you need cash, take it from your debit card. Bank charge extra cost if you take some money from your credit card (e.g. using bank teller machines).
- ✓ if you need cash, take it from teller machines that belong to your bank. Bank charge extra cost if you take the money from bank teller machine that does not belong to your bank.



## TOPIC 4. CONTROLLING DEBT

*What happens if I pay the loan late?  
How do I know when and how many I have to pay ?  
What should I do, so I had the money for the payments?*







## Planning your family budget with money flows related to the loan (Exercise 3g - part 1 )

*You have two groups of cards. The first group is your income- money. The second group are your expenditures.*

*Divide the income and expenditures for the regular and unexpected.*

*Assign to the cards with expenditures cards with money. Think about the allocation of the reserve for unforeseen expenses.*





## Planning your family budget with money flows related to the loan (Exercise 3g - part 2 )

*You have the loan.*

*Suggest how to adjust your income and expenses so that you remain out of your income to installment loan.*





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## Planning your family budget with money flows related to the loan (Exercise 3g - part 3 )

An exercises on **borrowing money from relatives with no interest** – teacher gives datas for calculations:

- Your car broke down.
- To rearranhge a bathroom.



## The most important rights granted to the borrower

- ✓ right to be fully informed,
- ✓ right to terminate contract in case that your bank change something in it,
- ✓ right to start complaining procedure in case of bank misconduct





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## Other rights granted to the borrower

- ✓ to be fully informed about the terms of contract
- ✓ right to give up of the contract without any explanation, some time after it has been signed
- ✓ to be informed by your bank that the terms will be changed right





### QUESTIONS FOR ASSESSING THE COMPREHENSION OF MODULE 3:

1. Explain the difference between *legal* and *illegal* sources of money to borrow.
2. What are the basic features of “usury”, and why do you think this practice may be ethically unacceptable?
3. What will a bank ask you to present as a proof that you are eligible loan customer? Give some examples.
4. Do you need to have some assets in possession in order to be able to borrow? Why?
5. Many things that a bank may charge when granting a loan actually increase your costs of borrowing. Give some examples?
6. Explain the importance of an effective interest rate.
7. How does amount of interest payable depend on interest rate, loan amount and term of loan? Explain.
8. Name and explain some borrower’s rights.
9. When you borrow money from a bank you must think about your regular income. Please give some examples of your regular income.