

PAYDAY LOANS

You have probably seen “stores” or TV commercials where you can borrow money without going to a bank or other financial institution. This type of short-term loan is often called a **payday loan** because the term is usually only until your next pay day. These are usually not a good idea as they charge very high rates of interest and it is compounded daily. Many people get into a lot of financial trouble thinking these loans can get actually get them out of trouble.

Example 1: Teresa’s car payment of \$450.00 is due in 3 days and she does not have enough money to pay it. She went to a payday loan store for a loan. She had to repay the store \$536.80 within 14 days.

- What is the daily interest rate for the loan?
- What is the annual interest rate of the loan?

Solution:

- Calculate the interest paid, and use the simple interest formula with time in days.

Teresa paid $\$536.80 - \$450.00 = \$86.80$ in interest

$$I = \$86.80 \quad P = \$450.00 \quad r = ? \quad t = 14 \text{ days}$$

$$r = I \div (P \times t) \times 100$$

$$r = 86.80 \div (450.00 \times 14) \times 100$$

$$r = 1.38\%$$

The daily interest rate is 1.38%

- To calculate the annual or yearly interest rate, multiply the daily interest rate by the number of days in a year – 365 days.

$$1.38\% \times 365 = 503.7\%$$

The yearly interest rate is 504%. WOW!!!

This is why payday loans are **not** a good idea.

Example 2: Chris borrowed \$125.00 from a payday loan store and agreed to repay it in 25 days at an interest rate of 1.20% per day. How much will Chris have to repay?

Solution: Use the simple interest formula using the interest rate as a daily rate and the term in days.

$$I = ? \quad P = \$125.00 \quad r = 1.20\% \div 100 = 0.012 \quad t = 25 \text{ days}$$

$$I = Prt$$

$$I = 125.00 \times 0.012 \times 25 = \$37.50$$

Now add the interest to the amount that Chris borrowed to get the total amount.

$$A = P + I$$

$$A = \$125.00 + \$37.50 = \$162.50$$

Chris will have to repay a total of \$162.50 to the loan store.

ASSIGNMENT 9 – PAYDAY LOANS

1) Haylie borrowed \$325.00 from a payday store, and 10 days later she paid back the loan and interest with a cheque for \$365.50.

a) What was Haylie's daily interest rate?

b) What was Haylie's annual interest rate?

2) Brad borrowed \$250.00 from a payday loan store. He paid back the loan and interest 9 days later. His annual rate of interest was 425%. How much interest did Brad pay?

3) Mike borrowed \$725.00 from a payday loan store and agreed to repay it in 15 days at a daily interest rate of 1.67%. How much in total did Mike repay the store?

4) Gurpreet agreed to pay \$527.50 to a payday company that gave him a loan of \$485.00 at 1.10% per day. How many days did he have the money?