**BA 355: ICE 4 (15 points)**

In Cases 2.1 and 2.2, we used simulated (fake) credit score and loan default data to determine how those two factors might be related. Real data is preferable to fake data, and the following source might give us some insight into how interest rates for automobile loans depend on credit scores.

<https://www.businessinsider.com/personal-finance/average-auto-loan-interest-rate>

|  |  |
| --- | --- |
| CS | APR |
| 400 | 14.59% |
| 550 | 11.03% |
| 630 | 6.61% |
| 720 | 3.48% |
| 815 | 2.34% |

1) Read the article, paying particular attention to the information in the tables.

2) Using the data from the *first* table in the article, create a list of paired data points with credit score in the first column and average loan APR for a new car in the second column. Since the credit score data comes from a range of values, average the two (like we did in Case 2) to get a single number – for example, for “non-prime” scores from 601 to 660, use 630 as the value. This should yield five data points.

3) Draw a scatter diagram of the points (shocking!) and fit a straight line through them. Fix the x-axis to start at 300 on the graph. Determine the equation of the line and r2. Format the trendline label to be to Percentage with 3 decimal places of accuracy. What are the equation of the line and r2?

4) One way to interpret r2 is: The x-variable explains/determines r2% of the y-variable. Interpret r2 this way. According to real data, what is your conclusion about the relationship between credit scores and interest rates on new automobile loans?

Credit score determines almost all, 96.6%, of what your interest rate will be on an auto loan.

5) Starting at 350 on the left and increasing by 100 credit score points each step, interpret the y-intercept (at 350) and the slope (per 100 units) of the line. In other words, what does the line tell us about the worst interest rates (at credit score 350) and how the rates change (per every 100 units)?

Interest rates can be upwards of 16% (16.3%) for really bad credit scores like 350 but the interest rate drops on average by 3.2% for every credit score increase of 100 points.

6) Assume your credit score is 700; what kind of rate are you likely looking at? What if you had a perfect credit score of 850?

700 is about 5.2%, 850 is about 0.4%.

7) By how many points must your credit score increase to decrease your interest rate by a percentage point (1%)?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| CS | Loan | APR |  |  |
| 824 | $427 | 1% |  |  |
| 733 | $460 | 4% |  |  |
| 642 | $495 | 7% |  |  |
| 550 | $531 | 10% |  |  |
| 459 | $569 | 13% |  |  |
| 368 | $608 | 16% |  |  |
|  |  |  |  |  |
|  |  | Just picked some interest rates |

About 31 or 32 points. (31.43)

8) Google “auto loan calculator” and use the one that pops up online assuming a $25,000 loan for 5 years. Using the equation from part 3) and the auto loan calculator, develop a relationship between monthly payment and credit score. How much would you need to increase your credit score to decrease your monthly payment by, say, $25? Explain your steps on this part.

Relationship: Starting at $613 for the worst credit score of 350, loan payment drops by about $0.40 for every one-point increase in credit score (or $40 per 100-point increase). You would need to increase your credit score by about 63 points to see a $25 decrease in monthly loan payments.