



AW Financial Management LLP

Financial Planning
Independent Financial Advice
Investment & Wealth Management

River House, 1 Maidstone Road, Sidcup, Kent, DA14 5RH
Tel: 01322 669 059 www.awfm.co.uk

“Cars”

The cost of motoring is probably one of the most significant factors in family finances, second only to mortgage and rental costs. Whilst we fully accept that cars are not all about the money, money is a huge element of motoring, especially with rising fuel and insurance prices. Here we briefly examine the different ways of *financing* a car but first how about considering ...

Do you *need* a new car?

This acquisition, however made (purchased or rented) is going to be costly in terms of finance. We recommend that you take 5 to consider the following:

- Have we been too readily seduced by car adverts? Have we bought into the advertising spin that unless we have the latest car model, our lives will be somehow incomplete and unbalanced? Do you believe all of that?
- Consider the environmental impact of the decision you are making. Do you really buy the potential myth that you need to keep replacing your car every 3 to 5 years or is there a better way both for your pocket and for the environment?
- Consider some of the benefits of owning an older car. Are you less precious about it? Will you lend it to others if they have a greater need than you? Will it be cheaper to insure for all drivers (over a certain age)?
- What else could you do with the money (either a capital sum or a monthly payment)? Are there better things to spend your money on?

The cost of depreciation

I once heard a very wise person say the cheapest car for you to own and drive is the car you already own. Yes, there is the point at which a car becomes too unreliable and the repairs are too costly to be economical but most people reach that decision point way too quickly. The issue here of course is depreciation. An older car depreciates in value at a far lower rate than a newer car. And don't be fooled into thinking that the way you purchase the car helps you to avoid the cost of depreciation, it simply doesn't.

On the What Car? website www.whatcar.com (at the time of writing) is a very helpful depreciation calculator. I put in two cars, a Mercedes C200 CDI Estate and a Citroen C5 1.6 Estate. I have only picked on these two cars at random but have sought a mid range and higher value alternative.

These are the results:

	List price	Val yr 1	Val yr 2	Val yr 3	Val yr 4
Mercedes C200 Estate	£27,995	£19,250	£15,925	£13,075	£10,600
Loss between periods £		-£8,745	-£3,325	-£2,850	-£2,475
Loss in % terms		-31%	-17%	-18%	-19%
Citroen C5 Estate 1.6 HDi	£20,995	£9,800	£7,976	£6,225	£5,024
Loss between periods £		-£11,195	-£1,824	-£1,751	-£1,201
Loss in % terms		-53%	-18%	-22%	-19%

What I glean from these figures is that the PR & Marketing guys have pulled off an absolute miracle in getting most of us to consider changing our cars every few years. So before you go any further, why not consider the questions and issues raised under the “Do you need a new car?” section, in the light of this data.

However, this is a Fact-File and so we are going to look at the four main ways of owning/borrowing a car:

Leasing/Contract Hire

With leasing you can change your car regularly – typically every three years – and perhaps avoid the repair and maintenance costs that come with driving an older vehicle. But you will never own the car and you will always make monthly payments while your agreement is in place.





How leasing works:

If a car is worth £20,000 when new, and worth £13,000 when two years old, you will pay the £7,000 difference – plus interest charges and other depreciation mark-ups. You then give the car back.

The only money that is required up front is your first payment (usually equal to three monthly payments). Lease payments are cheaper than a loan purchase because the charges are based on different values.

With a lease the car's final value – what it is worth for re-sale at the end of the agreement – will be taken into account. You will never actually own the vehicle – the lease company will – which means that if you default on payments you will lose the car, whatever other financial penalties may be imposed.

In effect you hire the vehicle for an agreed period of time and pay a fixed sum for the privilege. The fixed sum will take into account the average mileage you are likely to do. The higher the mileage, the higher the payment, because the more miles on the clock the less the car will be worth when the lease company comes to sell it. And of course if you exceed the agreed mileage, you will face further charges.

The lease can be just for the car, or can include servicing, but again at an increased cost.

Terms usually range from 18 months to five years, and when the lease ends you simply return the car, settle the contract and walk away. Crucially, if you want to end the contract early (because you have insufficient income to cover the payments perhaps) there will almost certainly be penalty costs to pay.

Hire Purchase

Hire Purchase is the traditional way to finance a car purchase. You pay off the entire price of the vehicle through a series of monthly payments. At the end of the contract period the vehicle becomes your property.

The monthly payment is determined by the amount of deposit paid, the period of the contract and the sale price of the vehicle.

HP is very similar to borrowing a sum of money from a bank and paying it back over a fixed period of time, with interest. Hire purchase is a type of secured loan which are often preferred over alternative (unsecured) loans because they allow a greater borrowing limit. The term "secured loan" means exactly that, a loan that the lender can secure against an asset (in this case, a car).

Purchase

This is split into two main sections:

Buying a car without a loan

As we continually promote debt free living, we would continue to promote this option as a very serious contender as being the best way to purchase and own a car. You can clearly decide how much you are willing to spend on the car based on your available budget and the car is then yours and you owe nothing to anyone. Many car showrooms do try to push some form of finance deal but this is because they will make more money on the deal with you. We find this distasteful but it is a fact of commercial life and so you do need to look at all of the options carefully.

Buying a car with a loan

With this option you will have to make a significant down-payment (like a deposit for a house) at the outset, and then you pay monthly loan payments which comprise of both capital and interest for a fixed term, until you have paid off the loan and the car is yours. You would normally expect car loans to be over 3 to 5 years. If you have a flexible mortgage, you may find it better to use your mortgage funds to borrow the money

Summary

Whichever way you cut it, motoring is for most people, a very expensive necessity especially when you take into account the cost of Insurance particularly for younger drivers and the environmental impact of new car production is immense. All things worth considering.

If you have any questions or need an independent review of your financial planning arrangements, please contact us to discuss your situation further. AW Financial Management LLP is an Independent Financial Adviser regulated by the Financial Conduct Authority.

Information given in this document should not be taken as advice as it is intended for guidance only. If you wish to have an assessment of your own situation, you should contact the office for advice.

