

Most People Get Burnt On Car Finance, Find Out The Tricks BEFORE You Buy Your Next Car



At Mike Mackenzie My Finance People we take care of all of your financial needs. When it comes to car finance we often feel like throwing on a cowboy hat, because car finance is still stuck in the wild wild west.

There are so many variables with car finance that unless you know what you're doing you can be caught out and burnt badly. Car dealers are excellent at sales and they know how to dazzle and confuse even the most savvy customers.

Before you even enter the store they have already started the process of selling to you with the numerous ads they put on tv, radio, online and the newspaper (I think these still exist). One of their favourite promotions is the 0% or 1.9% finance options.

Please don't ask me if I can beat 0% or 1.9% finance because it's the wrong question to ask. After I explain why in this very long blog post you will fully understand that it's cheaper to get an 8% interest loan from a broker than 0% or 1.9% from the dealership.

I regularly meet up with other brokers to exchange ideas and experience and I had a fascinating chat with Brent who use to work in a car dealership. He told me in the five years that he wrote finance exclusively for the dealership he did less than 50 loans at 1.9%. When you consider how much they are pushing these 1.9% loans in their ads and how many cars they are selling this is even smaller than their interest rate.

The low interest rate the dealers advertise has only one purpose, to get you into the store.

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Once you're in the store they can go into full sales mode and if you really want 0% finance you're going to find out all the little sub clauses which ends up making it more expensive than an 8% loan.

You will quickly find out it's not available on all models, only certain ones. Not always but usually these models are the one they are having trouble selling or they want to move on quickly because the new one is coming. There are two problems with this in being you might end up compromising on the car you want because you're chasing the 0% finance more than what you want and the other is the issues you will face when you go to sell it (more on this later).

Most of these 0% or 1.9% finance are over 36 or 48 month contracts. Now paying off a \$54,000 car in 48 months means your monthly repayments even at 0% and would be \$2,250 per month which is the same as a \$471,287 home loan at 4% over 30 years.

Most people can't afford this so they put in a ballon or residual amount for you to pay when the contract is up. This makes the monthly repayments more affordable but means at the end of 48 months you need to come up with \$27,000 to keep your car.

You now have two options to keep your car, you can sell it or refinance it. If you choose to refinance it then you're going to get a higher interest rate because its now a used car and we're looking at 8-10% when we start the finance process again.

If you decide to sell it remembering that it was only available on a red automatic SUV, you could possibly be 1 of 50 people trying to sell the exact same car at the exact same time because you all signed up for the special offer of 0% or 1.9% finance. Even though you bought a new car only two years ago, it was "plated" three ago and do you think you will get \$27,000 for a trade in? It will be touch and go especially considering the amount of similar vehicle trying to be sold at that same time.

The last problem you have is that the dealer will tell you that because you are getting an awesome deal on the finance they cant negotiate on the price, so you're forced to pay the recommended retail price. Depending on how good you are at haggling and how motivated the dealer is to sell you normally get to beat the price down a bit when purchasing. Of course the dealer added some extras on top at the start knowing this would happen, so the old game of cat and mouse continues.

For a \$54,000 car it would be fair to say you should be able to get him down to \$48,600 which is 10%. I have software that allows me to find cars for you and do the haggling on your behalf and it varies between 5-15% in discounts I have been able to get clients but I will go into that later.

If you were to purchase your car for \$48,600 with an interest rate of 8% and pay it off in two years like the above example, you're monthly repayment would be \$2,198 saving you \$52 a month or \$1248 over the total loan. Not many people will pay off a car in that time but I didn't want to make the maths too complicated and compare apples with apples.

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Normally I would take the \$48,600 loan over 5 years which is the most common option for car loans and it would be secured by the lowest possible interest rate being a brand new car. Getting the \$54,000 car at 0% over two years and then having to refinance it for another 3 years at a higher interest rate being a used car would mean that the option of haggling with dealer on price and getting Mortgage Broker In Perth to do the finance would be a much cheaper option.

The exception to the rule of refinancing a car over 5 years or less is when you're looking to buy or refinance your home to another bank. Servicing is key in this scenario, so I would recommend 7 year loan term. Unfortunately last year I had a few young couples that bought their car before the house and this significantly delayed their plans in purchasing a home. Especially with Keystart because if over 10% of your income goes to servicing other debt, you won't get a loan with them.

The main difference between car loan and home loans.

In home loans the bank pays you a commission for processing the loan and the rate is pretty standardised across the industry. I can write home loan with 42 different banks and were talking the difference from the highest to the lowest being 0.5%-0.7%

In the car finance world you can choose up to 4% or \$2,500 for your origination fee, meaning if the customer is only interested in a low interest rate you keep the interest rate low and jack up the origination fee. Then on top of that you have the fees for set up of the loan and ongoing monthly fees.

To make sure you're getting a good deal on car finance you need to talk about the monthly repayment.

This is the total cost of the loan which includes the interest rate, origination fee, set up costs and monthly ongoing fees divided by the length of the loan in months.

My sister in law went to a car dealer and she came back to me saying the interest rate is 4.79% and the monthly repayment was \$705. I was able to find her a loan for 8.5% which would cost her \$704 per month. Obviously I got her lower interest rate than 8.5% but I wanted to see how high I could push the interest rate and still beat the low 4.79% the dealer offered her. Also if you do get your hands on the initial contract you will find it hard to find all of these numbers, it had more pages than a home loan refinance I did the week before and this was for a car under \$40,000.

Why Balloon/Residual payments are the devil

Just when you thought it was safe to go back into the water (car dealerships) because you now know about interest rates, origination fees, set up costs and monthly ongoing charges I now throw in balloon payments which changes everything up.

Balloon or residual payments are the secret herbs and spices car dealerships use to turn line ball potential customers into happy clients. Many customers have tried to out think the dealership and said look I really want that car but I just cant afford \$1,100 per month can you please lower the price.

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Obviously the dealer can't sell the car for less because he wants to make a profit but if he doesn't get the customer to buy he is stuck with an unsold car. Hence the balloon payment was created.

Forgetting about the 0% finance over 48 month option if you were to buy a car from a dealer over 5 years for a \$54,000 car this might cost you \$1,100 per month and at the end of five years you would own the car outright.

If you can't afford the monthly repayment the dealer can put in a 30% balloon meaning your monthly costs drop to \$766 which is more affordable. The catch is at the end of 5 years instead of owning your car outright you have to give the dealer \$16,200 to pay off the balloon.

You may end up with no car and a small personal loan depending on the size of your final balloon payout.

Yes, you may be able to refinance depending on the age of the vehicle but the lenders willing to offer finance are fewer in number, which can result in higher interest rates due to less choices.

Balloon payments can be handy for commercial clients but personally I would never recommend them to a client buying a personal vehicle. If you can't afford paying the car at the full payment then you will probably find yourself in trouble when the loan expires.

What Interest rates can you get me?

Now if you have read to this point, you will understand that they are not the most important thing when buying a car but due to the amount of misinformation on the internet I feel like I need to briefly recap interest rates.

I mention 8% as the interest rate I can get for car loan and the truth is I usually get lower. I have access to 31 different lenders for personal/car loans and they all have a different appetite for risk.

The banks offer a lower interest rate to people that have a mortgage compared to people renting or living at home.

The banks offer a lower interest rate to people with a high credit score that haven't had any defaults recorded against their name.

The banks offer a lower interest rate to people who buy a car from a dealership because they assume there is less risk they are selling a lemon.

The banks offer a lower interest rate to a brand new car compared to second hand.

These four points are all pretty straightforward and why the interest rate I can get you will vary by quite a bit. Normally it's closer to 7% than 8% but it doesn't usually go above 10% unless you have multiple defaults and then it sky rockets to 28%.

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For some clients especially commercial clients speed and ease is more important than interest rate. With bank A I can get them a loan at 8% but its going to take 1-2 weeks and they need to supply full financial information including BAS statements, tax portal, profit and loss statements. With bank B they might get 9% but it takes 48 hours and they just have to supply a letter from the accountant.

The 7 important bits of information you need to compare offers on car finance

1. Price of car
2. Interest rate
3. Set up costs and ongoing fees
4. Origination fees (broker fee)
5. Ballon payment
6. Length of loan
7. Monthly repayment

To compare apples with apples you need all 7 pieces of the puzzle and if they don't give you that freely (you shouldn't have to ask, they should be straightforward and explain the process like I'm doing here), then they are sharks circling in the water. Mentioning 0% finance will only send them into a feeding frenzy, it's the bait they use to lure you in. They should be forced to play the Jaws theme music when mentioning 0% finance in all of the car ads, to give the customer fair warning.

Below is a potential conversation between a customer who saw the 0% finance ad and who hasn't read this blog talking with a trained professional sales person from a car dealership.

"Do you like this car? It's only at \$54,000 until the end of the month or \$1,194 for 60 payments."

"Wow! That's amazing but I'm not sure if I can afford that?"

"How much can you afford?"

"\$700 per month is my max."

"I will be right back, let me talk with the manager quickly... Good news we can do it for \$700 per month."

The sales person only spoke about 1 of the 7 important things you need to know about when purchasing a car to know if you got a good deal on the finance.

We have the price of the vehicle at \$54,000 and the interest rate would be 8% to get 60 monthly payments of \$1,194. To reduce the payment from \$1,194 to \$700 which is a reduction of \$494 per month the sales person could have done a few different things.

If we assume that they didn't lower the price or the interest rate because they want to make a profit it only leaves 2 things to change to decrease the monthly repayment. Increase the amount of months or add a balloon payment to the loan.

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Changing it to a 7 year loan term or 84 months would only reduce it to \$841 per month so they would have to add a ballon payment of \$7,000 to the end of the loan term. If they wanted to keep it at a 5 year loan term they would need a ballon of \$19,500.

If this client is at his max and can't afford to go any higher, what do you think will happen in 5 or 7 years when he finds out he has a ballon payment to pay for as well. I'm fairly confident he wont have a spare \$7,000 laying around.

Most lenders don't lend for car finance when the car will be over 12 years at the end of the finance term. For \$54,000 the customer may have bought a second hand luxury car that was already 5 years old and by the time we add 7 years of finance from the dealer the option they have to refinance will be severely limited, which means it will be a much higher interest rate.

Is there a hassle free option?

Recently I have gotten access to some exceptional software which I alluded to earlier in the blog. A bank that specialises in car finance and is in partnership with most of the dealers around Australia and has an exclusive quoting tool. This quoting tool is only available to a select few brokers in WA and Mike Mackenzie is one of them.

On your behalf I fill in the form asking what car you're looking for and the software searches which car yard has the best price for you. This software is searching the best price the dealer has not the lowest price advertised because as we know the dealer adds extra money to that total knowing they will be bartered down.

The dealer is bartering with other dealers to win your business, instead of you trying to barter the dealer down. This way you can't be intimidated or fall for their high pressure selling tactics. It takes all of the stress and hassle out of buying a car. Once you know you have the best price possible, the Mortgage Broker In Perth will get you a fantastic deal on your finance and you'll more than likely would have saved thousands off you next car purchase.

This service is complimentary, you won't be charged for it so you have nothing to lose and everything to gain. Please go to a car yard and get the best possible price on the vehicle and let me show you how much I can beat it by.

Car dealerships make their money off the car and the finance of the car. By using this revolutionary service you can save on the car and the finance. Luckily for the car dealership not many brokers have access to this amazing software.

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Mike Mackenzie looks after all of your financial needs, so we take a holistic approach to finance. We will ask you about your goals and dreams to make sure we get you a loan that will assist you in the future. The last thing you want is getting a nice car now but being told that you cant buy a home for 5 years unless you sell your new car. I look forward to finding the car of your dreams and saving you more than you thought was possible.

Sincerely,

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